Debt, Real Estate, and the Rise of Inequality in the UK and Western Europe from 1970

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abstract

Tells two interlocking stories: money and housing. Before 1970, credit was rationed by governments through central banks. Its deregulation was facilitated by the end of fixed exchange rates. The quantity of credit was assumed to be self-regulating, and controllable by interest rates and central bank operations. The authorities (as recently admitted by Mervyn King) were flying blind, assuming a quantity theory of money, versus the reality of endogenous money. In the space of thirty years bank balance sheets grew tenfold in relation to GDP. In housing and retail premises, banks found an ideal collateral: both a subsistence and status good, income elasticity greater than one (no diminishing returns), built-in collateral, the largest consumer expenditure, lightly taxed, tapping directly into labour income. Household debt grew faster than income, but housing equity rose much faster than debt. For both lenders and borrowers this became a property windfall. About two-thirds of the population were invested in home-ownership, and this became a bi-partisan political settlement that challenged the welfare state. But loose credit pushed housing increasingly beyond the reach of new entrants and polarized society. Debt service transferred resources from consumers to hoarders, and siphoned demand out of the economy, eventually leading to financial crisis, and to enduring stagnation. The windfall economy is ripe for another crash.