

The political economy of household debt, disposable income and consumption

IPR Report

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Executive Summary

- Household debt has risen sharply as a % of GDP since the 1990s across OECD countries as a whole, although there are some exceptions, and it has broadly plateaued since the financial crisis.
- In the same period, there has been a secular decline in the labour share on average across the OECD. This poses the question of whether the fall in the labour share is related to the rise in household debt.
- Most new debt is acquired through housing rather than in short-term loans, which are declining as a share of total loans in the OECD as a whole and the UK specifically.
- In this period, house prices have increased at a rapid rate and past econometric analysis shows it is the change in house prices that best predicts changes in household debt. However, house prices could have been both a driver and an outcome of the increasing acquisition of new debt.
- The fact the dynamics of debt vary across countries, and to some extent this can be mapped onto growth regimes or credit regimes, i.e., the demand-side, institutional and political drivers of growth and debt.
- The UK case strongly suggests that equity release played an important role in increasing consumption prior to the financial crisis, but the net reduction in equity release since then may help to explain part of the stagnation of the last 15 years.
- Anglophone countries are not a homogenous group of countries but there is some indication that yearly declines in household income are related to the acquisition of new household debt and vice versa.
- The report emphasises the role the housing market plays in the dynamics of household debt and consumption, particularly in countries with permissive credit regimes such as the UK and the US.
- Is there a way to break the dependence on household debt as a stimulator of consumption? The report ends by speculating on the role of universal cash benefits to stimulate aggregate demand.

1. Introduction

Financial markets have become a ubiquitous part of our social and economic lives. Individuals and households borrow through student loans, home mortgages, personal loans, credit cards, payday loans. Neo-classical economic theory points to the role of saving and borrowing in smoothing consumption across the life course. The theory is that if one can estimate lifetime income, and lenders are also able to identify that lifetime earnings potential, households can borrow when their current income is lower than their expected average lifetime income and save when it is higher, thus smoothing their consumption. This lifecycle model can also be applied to more short-term shocks in income or costs, with borrowing (or lending) smoothing the changes over a longer period. More broadly, lending and borrowing can facilitate the deployment of capital to the most productive ends, meaning that financial 'deepening' can make economies more efficient.

However, the dangers of debt – taken on by households and governments or corporations – became a subject of intense public debate and academic scrutiny after the financial crisis of 2007-08. While some in the media pointed at individual cases of profligate lending and risk-taking of bankers, many identified that the root causes of such a global financial crisis were primarily structural. The conditions facilitated by central banks and regulators allowed bubbles in assets to occur and required governments to bail them out when they became too big to fail, facilitated by the macro-level dynamics of debt rather than individual cases of reckless borrowing¹. Many argued that the rapid accumulation of *household* debt drove investment in real estate rather than new capital investment, which made it especially vulnerable to a financial crash (Turner, 2016).

Figure 1 shows that household debt increased on average as a percentage of GDP in 16 OECD countries for which there was full data, dramatically so in the run up to the financial crisis at which point there was something of a plateau as the effects of the crisis rippled through the economy and financial sector. However, this dynamic occurred somewhat differently depending on the country, with some countries experiencing very limited growth in household debt in the pre-crisis period. The 2010s have seen considerable deleveraging of household debt in some countries, while others continued to see debt rise.

¹ Hyman Minsky's financial instability hypothesis that such dynamics are fundamental to the nature of capitalist economies was also widely cited – stability can only breed future instability.

Household debt in OECD countries

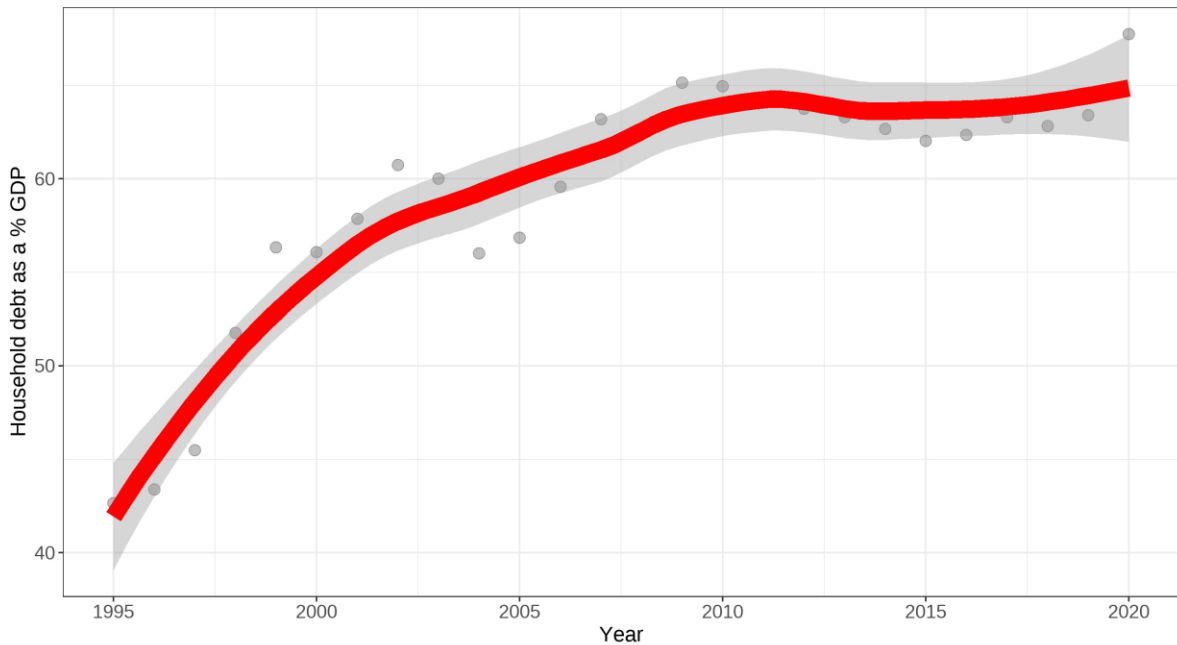


Figure 1: Unweighted mean of household debt in 16 OECD countries as a % of GDP [Source: OECD]

In the UK, the rise in household debt was a lot steeper than the OECD average prior to the financial crisis, going from just over 50% of GDP in the mid-90s and reaching nearly 100% of GDP in 2008. But equally there was more deleveraging of debt in the post-financial crisis period and only plateauing in the mid-2010s.

Household debt in the UK

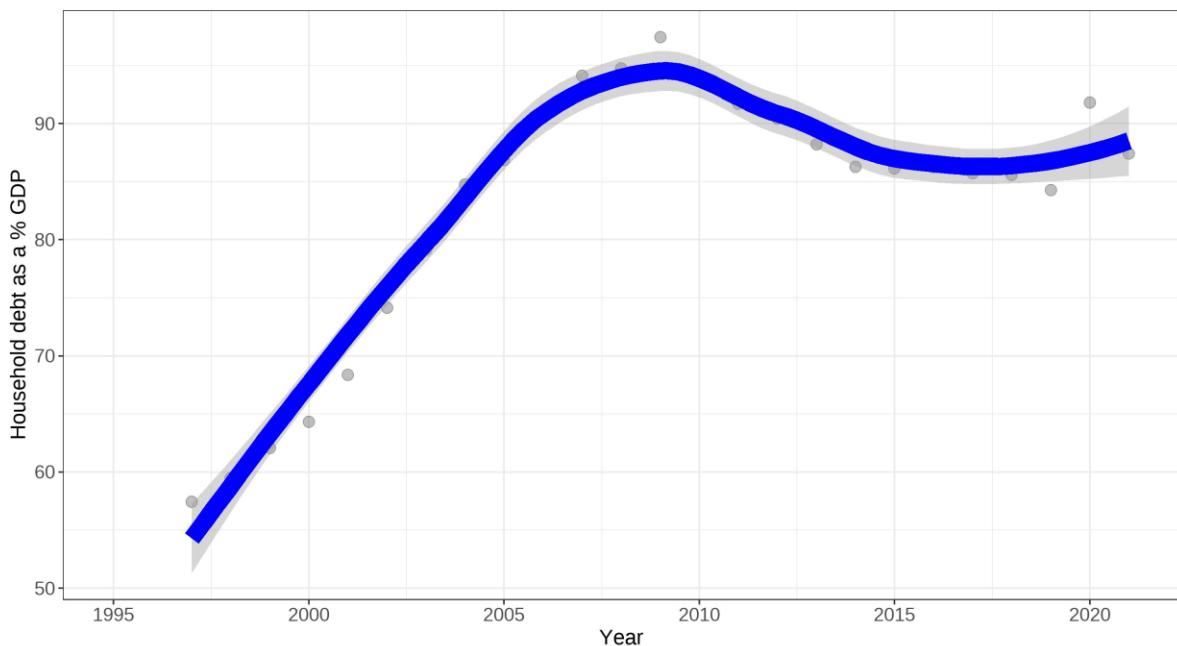


Figure 2: Household debt in the UK as a % of GDP [Source: OECD]

Figure 3 shows just how heterogeneous trajectories in household debt have been across five major economies. The US represents the most straightforward accumulation and deleveraging story with household debt peaking at the point of the financial crisis and then nearly returning to the levels seen in 1995 by 2020. Australia saw a steeper increase in household debt prior to the financial crisis. But from 2008 onwards, the growth of debt merely slowed rather than household debt falling as a share of GDP. Germany, on the other hand, saw falling household debt in the run up to the financial crisis and after. It has moved from the country with the highest ratio of household debt to GDP of the five to the lowest with household debt only at 50% of GDP. Sweden and France are more similar in that their increase in household debt has been relatively steady from the early 2000s onwards, albeit Sweden's rate has been greater.

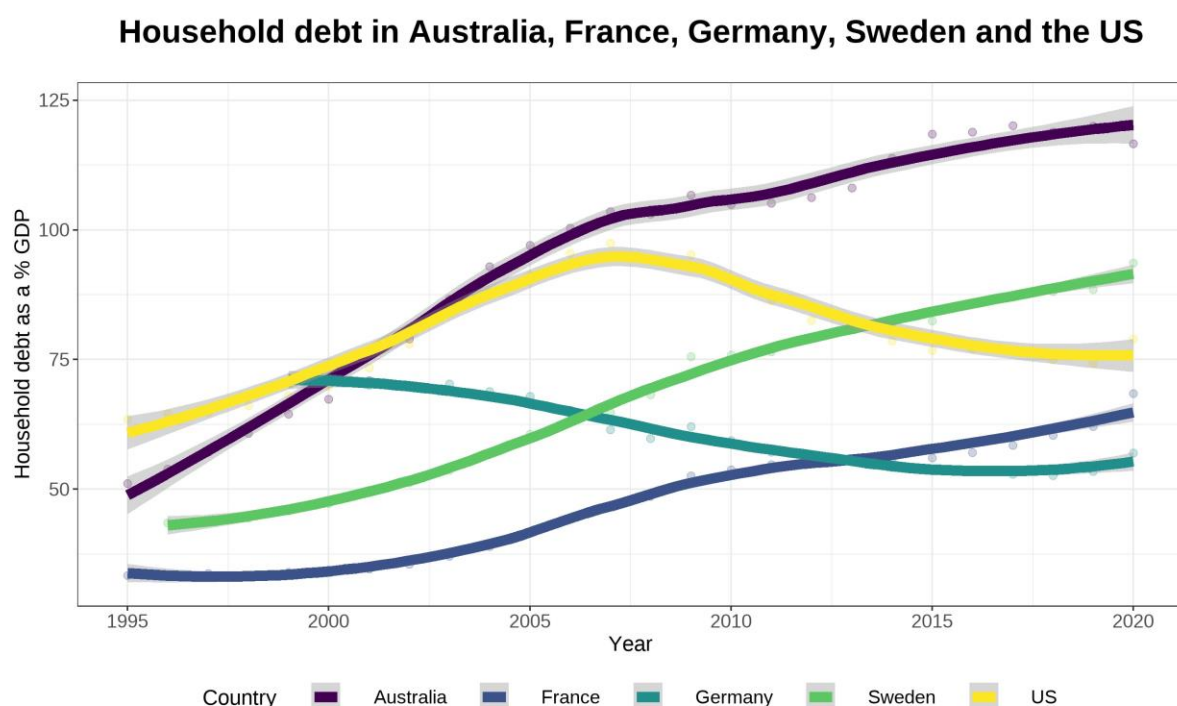


Figure 3: Household debt in Australia, France, Germany, Sweden and the US as a % of GDP [Source: OECD]

What explains this surge in household debt overall in the OECD and what explains the differences in trajectories across countries? Potential drivers of household debt are often grouped into supply-side and demand-side factors. Put simply, these are the characteristics and dynamics of *lenders* and *lending conditions* (supply) on the one hand and the characteristics and dynamics of households as *borrowers* (demand) on the other. Specific supply-side and institutional variables include factors such as the length of time required to resolve insolvencies, the quality of bankruptcy laws and the legal origins of a country (Coletta et al., 2018: 1213). The base rate set by the central bank can also be seen as a supply-side factor. Demand-side variables at the macro-level include the wage share, levels of inequality or demographics as well as factors that affect the risk-aversion of consumers.

Of course, both drivers of household debt are likely to interact (Johnston et al., 2021) and some country-level dynamics such as the level of self-employment or informal employment may be cast as both demand-side (insecurity reduces the confidence of borrowers) and supply-side (banks are unwilling to lend to those outside formal employment contracts). Changes in house prices increase the willingness of banks to supply more debt as loan-to-value ratios decline as well as encourage households to borrow more.

Importantly, supply-side factors driven by government policies that regulate lending do not occur in a vacuum. If it is the case that supply-side factors in general are the most significant determinant in explaining the levels of household debt in a country at a given time, this does not imply that these are necessarily the fundamental or root cause of household debt. For example, loosening credit conditions are not only a driver of household debt but also house prices, which in turn increase the wealth of households and their ability to leverage debt. But more crucially, government policies and institutions that lead to house price increases and/or the loosening of credit constraints may be driven by other structural factors in the economy or stagnation that governments seek to respond to.

One such structural factor that looms large over advanced major economies is the secular decline in the labour share. Figure 4 shows an unweighted average of OECD countries over the last 50 years indicating a fall of roughly 10% in the share of gross value added received by workers.

Aggregate labour share

Average of OECD countries (1970-2019)

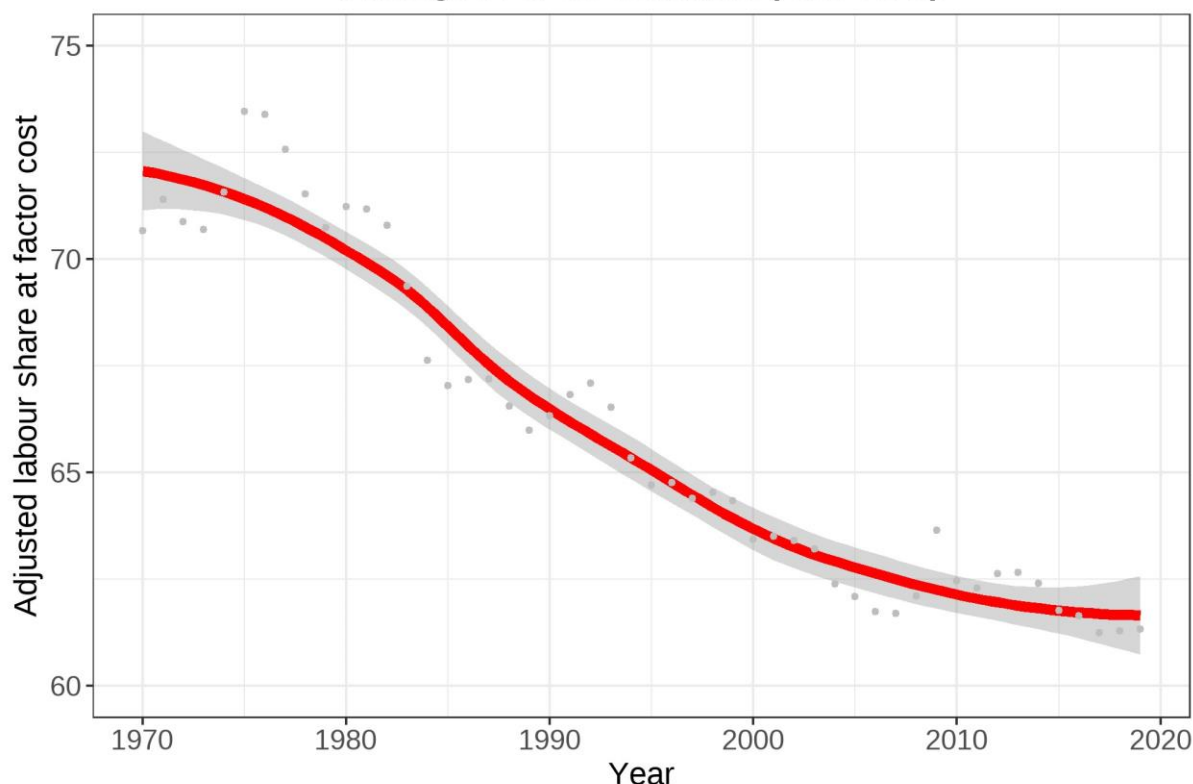


Figure 4: Unweighted mean of the adjusted labour share at factor cost in 16 OECD countries [Source: AMECO]

There are many explanations for the declining labour share, including globalisation, deindustrialisation, Superstar firms and workers bargaining power and demography. We summarise this literature in another IPR report (Chrisp et al. 2022) that examines the argument that technological change is an important contributing factor. While we find that certain technological factors do appear to be related to the decline in the labour share, here we are not primarily concerned with the causes of this decline but with the consequences.

The decline of wages as a share of GDP is seen as problematic for economies that rely on household incomes to stimulate consumption and growth. As wages fall so does spending power and thus household consumption and aggregate demand, which some argue is the key cause of the stagnation of advanced economies and the low growth that has beset them (Baccaro et al. 2022). Heterodox economists, among others, have argued that it is this stagnation that forced the hands of governments to find new stimuli of aggregate demand, which for many economies resulted in the loosening of credit conditions and other supply-side measures that facilitated the expansion of household debt. Thus, the supply-side policy changes may have been the proximate cause of an expansion of household debt, and indeed their withdrawal and tightening after the financial crisis may be the explanation for the subsequent plateauing of household debt, but these policy changes and other related supply-side factors may themselves be driven by broader macroeconomics.

These macroeconomic factors also interact with the broader institutional context and a country's 'growth regime' (Hassel and Palier, 2020). The financialisation of an economy, and thus the permissiveness of its credit conditions for households to borrow, is tied into a broader set of institutions related to education, social security, ICT and labour markets that in turn determine the composition of aggregate demand and crucially whether an economy is export-oriented or domestic consumption-oriented. However, there is not always a perfect alignment between 'credit regimes' (Wiedemann, 2021) and the typologies created by the Varieties of Capitalism literature (Hall and Soskice 2001), World of Welfare Capitalism (Esping-Andersen, 1990) or indeed the more recent growth regime literature (Hassel and Palier, 2020). We explore these factors more in the next section.

The type of household debt also matters. Across OECD countries, including the UK, most household debt is secured using residential housing, as opposed to unsecured lending that is explicitly for consumption, whether short-term or long-term. In fact, over the period in question, a growing share of household debt was tied to residential housing in OECD countries. Figure 5 shows this increase from the late 1990s to 2020 when nearly four-fifths of all household debt was secured with residential housing.

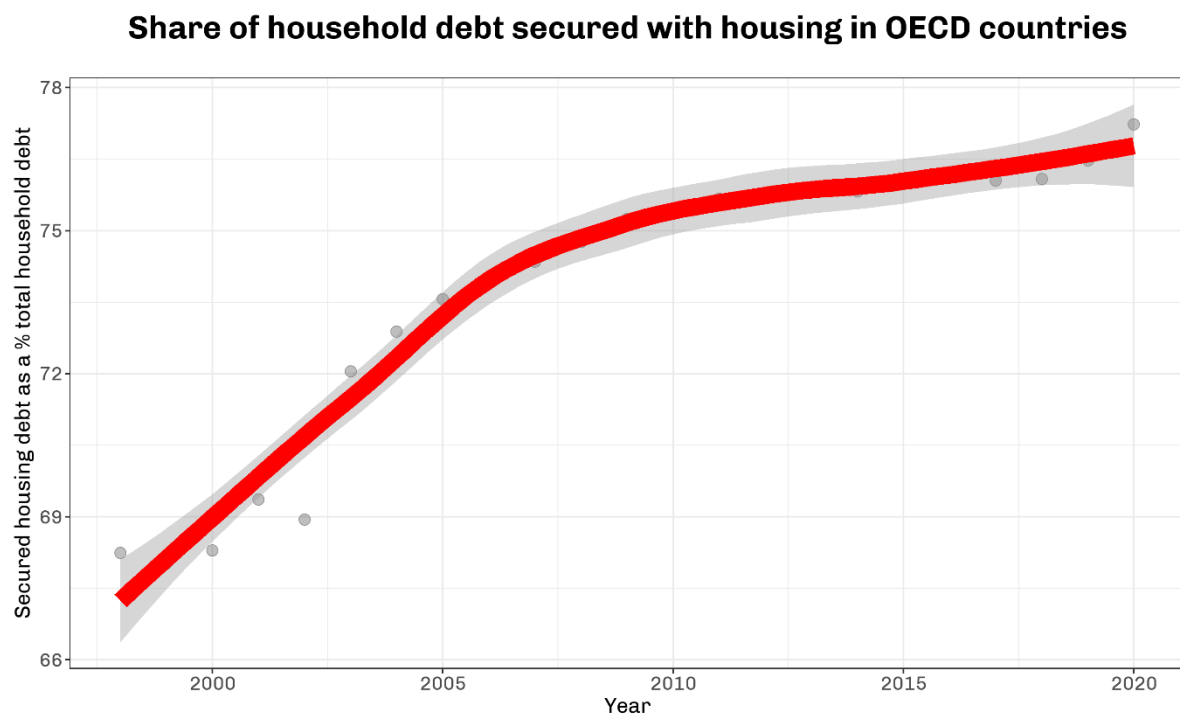


Figure 5: Unweighted mean of the share of household debt tied to housing or dwellings in 10 OECD countries for which full secured housing debt data was available [Source: OECD]

In the specific case of the UK the trend has been more variable, with the distribution of debt appearing to go in waves. Figure 6 shows that during the large expansion of household debt until the financial crisis, there were periods when housing was a key contributor, such as the early 90s and late 2000s but also when other forms of debt were expanding at a faster rate, such as the early 2000s.

Share of household debt secured with housing in the UK

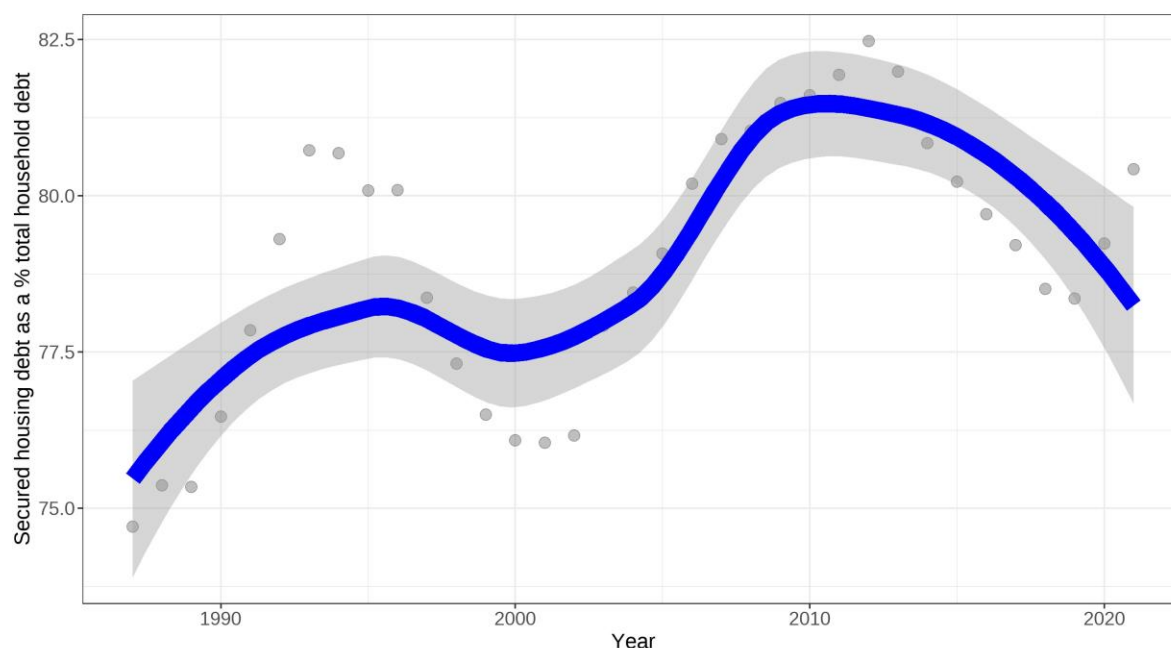


Figure 6: The share of household debt tied to housing or dwellings in the UK [Source: ONS]

Meanwhile, short-term loans appear to provide the mirror image for OECD countries as a whole, as short-term debt has declined as a share of all household debt, falling from 11% in the late 90s to less than 7% in 2020 (see Figure 7). Of course, this did not necessarily mean that short-term debt was also not rising in real terms or as a share of household incomes. Figure 8 shows that short-term debt also rose as a percentage of household disposable income prior to the financial crisis but then saw considerable deleveraging after the financial crisis. Similarly, although the overall trend in the UK is downwards (Figure 9), there were brief periods in which short-term loans were expanding as a share of total household debt at the turn of the millennium. Nevertheless, the link between housing and household debt is undeniably a crucial part of the story of the last 30 years of financialisation.

Short-term debt as a % of total household debt in OECD countries

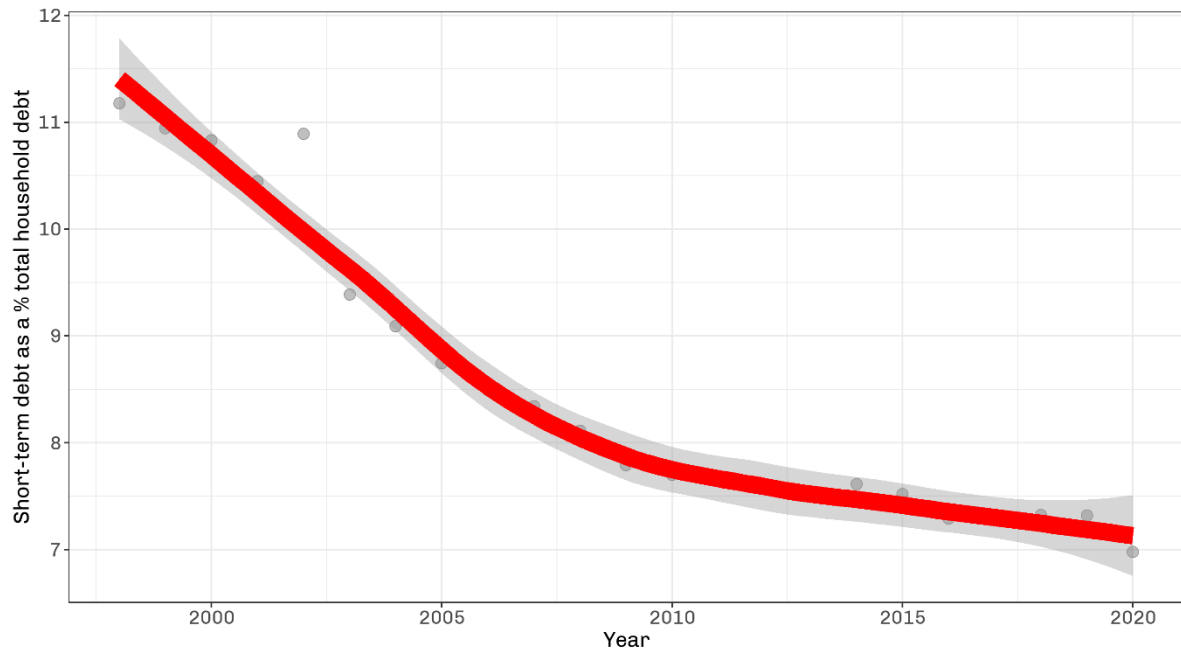


Figure 7: Unweighted mean of the share of household debt held as short-term loans in 17 OECD countries for which full short-term loan data was available [Source: OECD]

Short-term debt as a % of disposable income in OECD countries

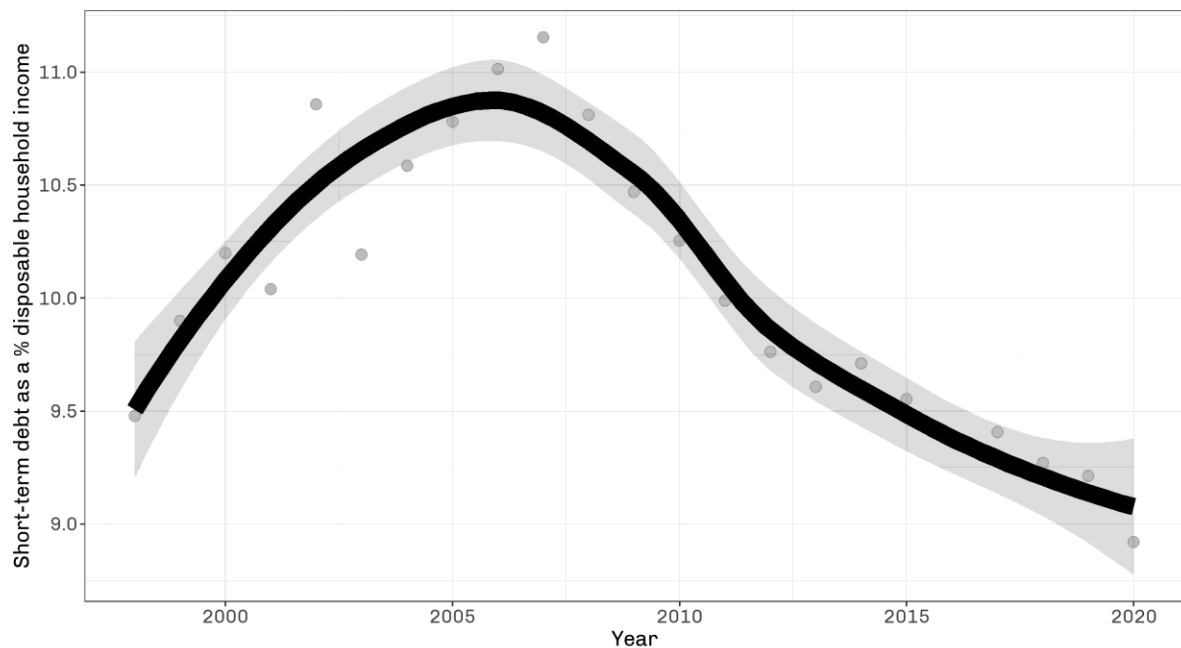


Figure 8: Short-term debt as a % of disposable income in 17 OECD countries for which data was available [Source: OECD]

Share of household debt that is unsecured short-term loans in the UK

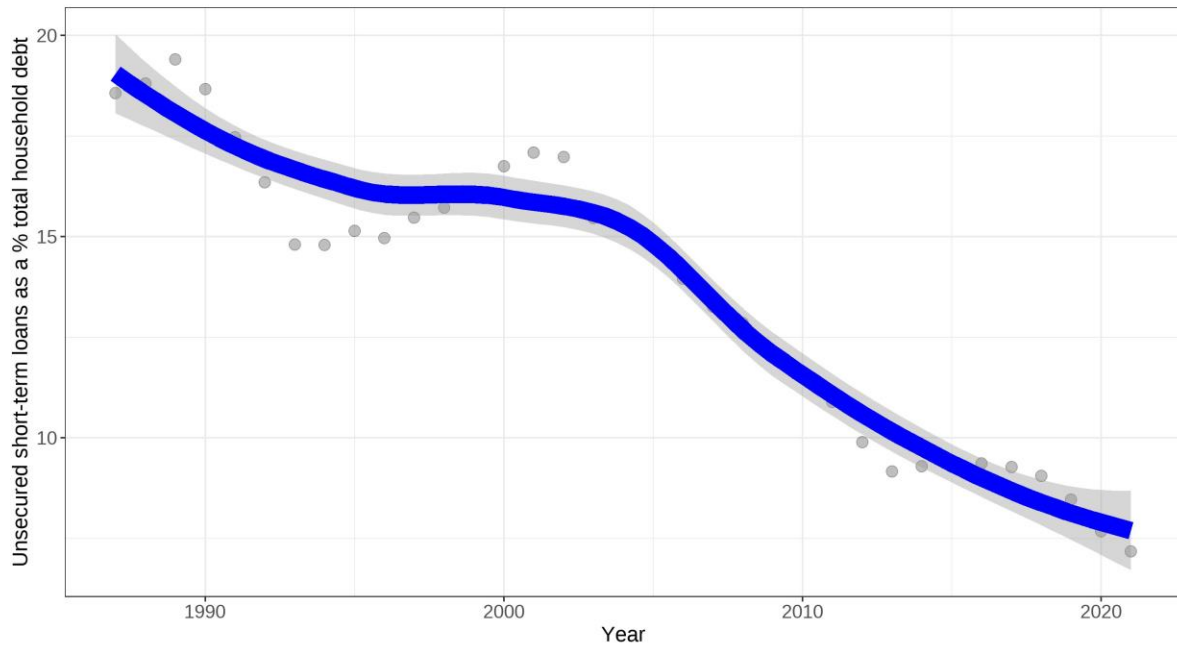


Figure 9: Short-term debt as a % of disposable income in the UK [Source: ONS]

The fact that secured debt is increasing as a share of total household debt at the expense of short-term loans would ostensibly appear to complicate the assumed mechanism by which household debt feeds into consumer spending. However, the fact that debt is secured by residential housing stock does not necessarily mean that there is no relationship between that debt and household consumption. While it is true that much of the new household debt will be used to buy housing, in certain contexts, loans will be made against a house already owned through equity withdrawals. These equity withdrawals have a clear direct link to household consumption and we explore this dynamic more in the section on the UK case. Even in the case of loans directly funding home purchases, the *sale* of the property may provide a huge cash injection to households through inheritance or downsizing. This kind of privatised Keynesianism has no doubt had its stimulating effects on many economies, but if it is solely achieved through the accrual of household debt there are obvious limits to its sustainability.

In this research note, we provide a summary of the theoretical and empirical perspectives that examine and explain the dynamics of household debt over the last 30 or more years. In particular, we zoom in on the UK case, providing a descriptive and explorative overview of the political economy of debt and consumption in the British economy. Finally, we then explore the extent to which these dynamics can be understood as a wider Anglophone liberal market economy phenomenon.

2. Growth regimes, credit regimes and household debt

One starting point for identifying the drivers of household debt is an econometric analysis of the factors that relate to its growth and decline. Stockhammer and Moore (2018) identify seven explanations of the macroeconomic determinants of household debt. These include:

- (1) Residential house prices (Ryoo, 2016; Godley and Lavoie, 2007)
- (2) Upward movements in the prices of assets demanded by households (Cooper and Dynan, 2016)
- (3) The income share of the top 1% (Frank et al., 2014)
- (4) Falling wages (Barba and Pivetti, 2009; Stockhammer, 2012)
- (5) Rolling back of the welfare state (Lapavistsas, 2013)
- (6) The age structure of the population (Modigliani and Brumberg, 1954)
- (7) Short-term interest rates (Taylor, 2009)

They test these for a panel of 13 OECD countries over the period 1993 – 2011, examining both the short-run and long-run. They find that the most robust macroeconomic determinant of household debt is real residential house prices in both the short- and long-run, and some evidence for the theory that an ageing population has an effect in the long-run. However, they find no evidence of the other explanations as determinants of household debt.

Descriptively, we can see there is a similar, though not identical, trend to levels of household debt as a % of GDP. Figures 10-12 show changes in real house prices from 1995 onwards for the OECD average, the UK and the same five major economies examined in the introduction section (Australia, France, Germany, Sweden and the US). For all countries that saw increases in household debt as a share of GDP, including the OECD as a whole, there were steep rises in the real house prices up until the financial crisis. The only country that did not see increases in house prices was Germany, which simultaneously did not increase household debt in that period.

Real house prices OECD average

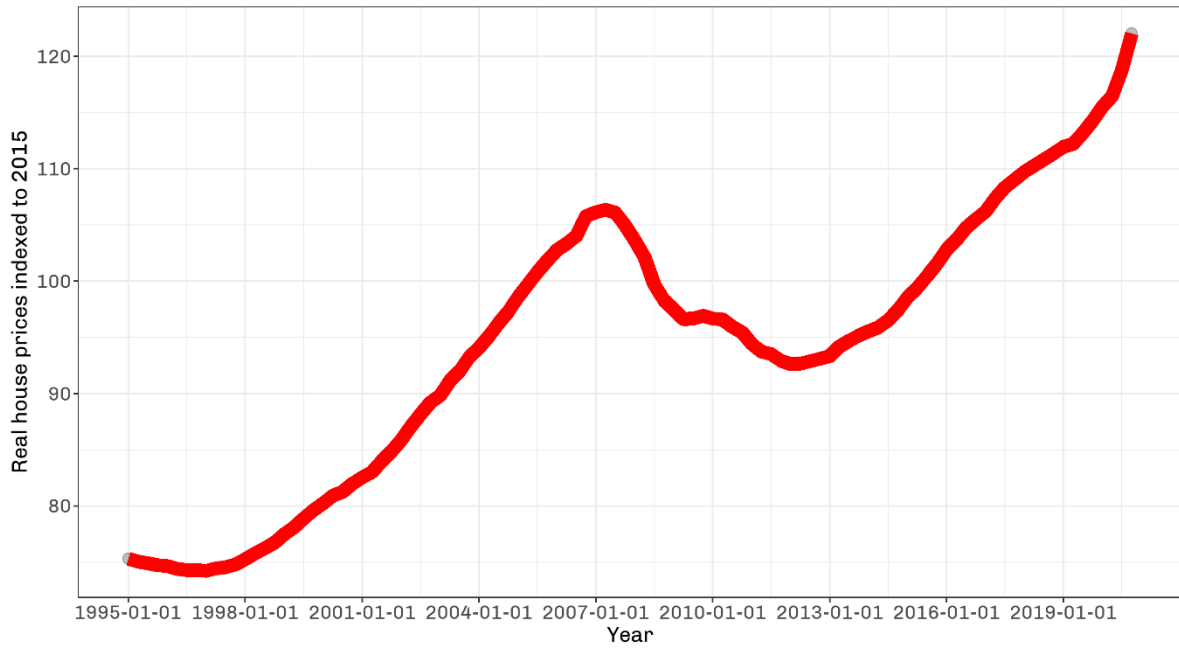


Figure 10: Unweighted mean of real house prices indexed to 2015 levels as 100 [Source: OECD]

Real house prices UK

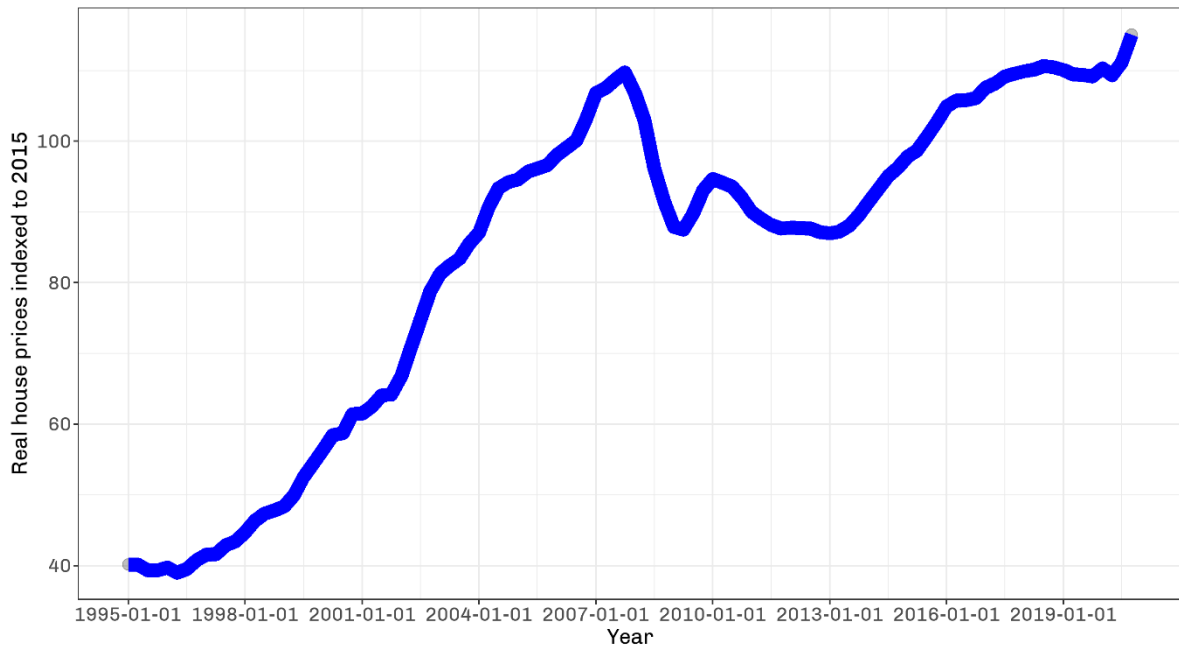


Figure 11: Real house prices in the UK indexed to 2015 levels as 100 [Source: OECD]

House prices in Australia, France, Germany, Sweden and the US

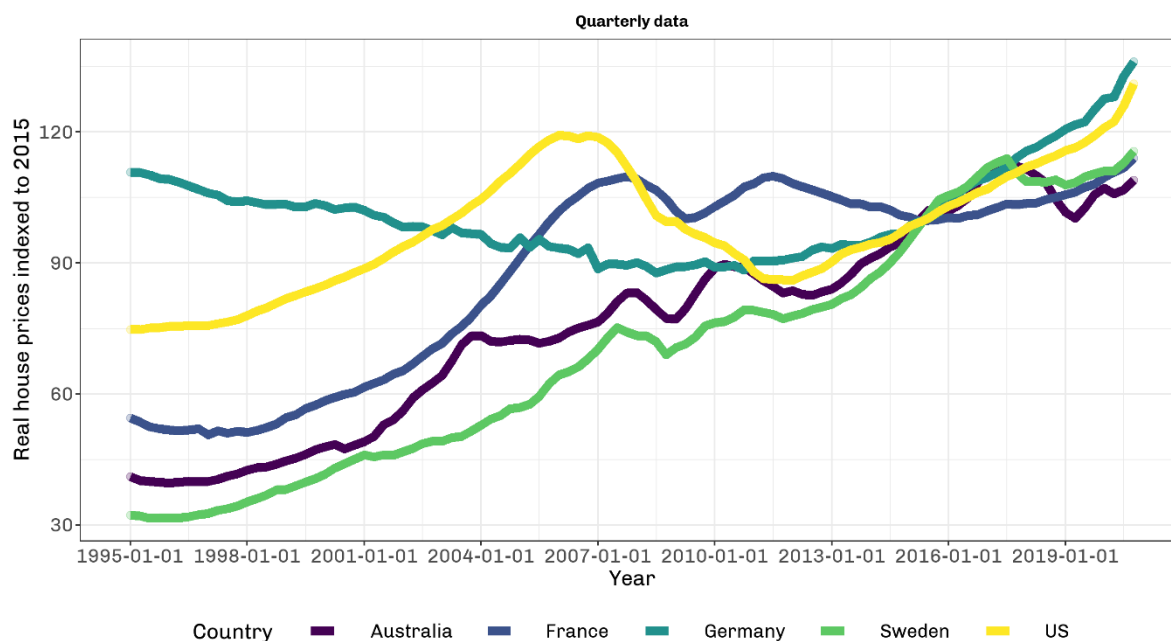


Figure 12: Real house prices in Australia, France, Germany, Sweden and the US indexed to 2015 levels as 100 [Source: OECD]

However, the robust empirical link between house prices and household debt does not settle the question, as alluded to in the previous section with respect to supply-side factors affecting the levels of household debt. Firstly, there is an obviously endogenous relationship between the two: while rising house prices will enable greater borrowing given the increased wealth and equity of homeowners, equally greater capacity to borrow and the acquisition of debt drives up the price of housing. Secondly, the increase in house prices is itself facilitated by government policies, not least the interest rate and rules around credit.

This concern about wider endogeneity motivates emulating the holistic approach taken by the growth regime literature (Baccaro and Pontusson, 2016; Hassel and Palier, 2021), which in turn builds on the comparative political economy that understands the interlinking significance of multiple institutions, policies, and outcomes (Esping-Andersen, 1990; Hall and Soskice, 2001; Beramendi et al., 2015). This more recent literature on growth regimes moves beyond a supply-side analysis of institutions to a neo-Kaleckian demand-side approach that argues that macroeconomic output and employment are primarily determined by aggregate demand. Typically, neo-Kaleckian macroeconomists have distinguished between wage-led and profit-led growth. However, Baccaro and Pontusson (2016) argue that the process of deindustrialisation and deunionisation has led to a period of stagnation in real wage growth and productivity gains that have necessitated alternative growth strategies. The two main strategies they outline contrast the role of household consumption and net exports as drivers of growth. Consumption-led growth may be fuelled by real wage growth but increasingly the absence of real wage growth has meant relying on growing household

indebtedness. Export-led growth can be identified when the export sector is sufficiently large and exports are price elastic, meaning wage restraint boosts competitiveness but depresses consumption².

The demand-side accounts of growth regimes are not independent of the supply-side institutions of firms, labour markets and financial markets and thus a growth regime can be said to comprise mutually interacting and complementary constellations of political economic institutions and macroeconomic drivers of growth. These include systems of wage-bargaining and wage-setting, the regulation of the labour market and the financial system, households' access to credit, the inclusiveness of the education system, the generosity of the social protection, the development of ICT industries and the demand for skills in the labour market, as well as the sector that drives economic growth, that is, exports or domestic demand (Hassel and Palier, 2021).

In their work on the growth models of the US and the UK, Reisenbichler and Wiedemann (2022) argue that there are two main mechanisms by which debt-financed consumption serves to drive growth: the housing channel and the income-maintenance channel. The former relates to the inter-related dynamics of growing house prices and both household borrowing and spending. Growing housing wealth increases households' propensity to borrow and consume as it can substitute for savings (Fuller, 2019) and facilitates greater borrowing access due to increased leverage. The income-maintenance channel is cast as a form of consumption smoothing in the absence of adequate social insurance as found in liberal welfare states. Credit is seen to be a last resort to compensate for stagnating wages and economic insecurity and to fund necessary life-cycle costs not provided by the state such as childcare.

This model is also fundamentally reliant on permissive credit regimes including 'deep financial markets, capital markets for mortgages and pension assets and the allocation of capital and credit disproportionately towards the household sector' (Reisenbichler and Wiedemann, 2022, p. 215). Governments can also assist with tax relief on mortgages or consumer loans as well as other policies to reduce borrowing costs for households or provide guarantees. Rising house prices also incidentally provide additional pressure for governments to assist more with potential buyers that take on increasing amounts of debt to be able to become homeowners.

However, the connection between growth regimes and household debt is not simply conceived of as due to financialisation or housing, but also to the welfare state more broadly. To some extent, household debt may, then, as Lapavistas (2013) and others argue a replacement for the welfare state. There are two distinct primary mechanisms by which household debt, serving in its consumption smoothing function, may serve as a replacement for aspects of the welfare state. The first is by acting as a substitute for insurance against shocks to income, such as unemployment or sickness. Rather than drawing on benefits during income shocks, households may take out short-term loans or other forms of debt to maintain their income as much as possible to cover their needs. The drawbacks of this approach for those on the receiving end of income shocks are obvious, but the empirical question is whether retrenchment of the social security system encourages or indeed necessitates the taking of loans to cover income

² Growth could be driven by both consumption and exports if exports are relatively price inelastic.

shocks. The second mechanism is alluded to above: debt can facilitate the acquisition of assets, specifically housing, which in turn provide security and welfare, particularly in older age. Thus, we may assume that the weakening of entitlement to generous public pensions may be one driver of the acquisition of debt to purchase housing.

Of course, the assumption is that if debt does act as a substitute for the insurance provided by welfare state policies, then one possible solution for reducing household debt, if an excessive amount is perceived as a threat to financial stability and a driver of crises, would be to expand welfare provisions, certain important services such as childcare and/or resources to households. A basic income provided to all households could act as a stimulus equal to the amount of household debt created to cushion households from shocks to their income (Crocker, 2020).

However, there is an alternative expected relationship between social protection and household debt. It is also argued that the extra security and insurance guarantees that welfare state institutions provide facilitate the accumulation of household debt, on both the demand- and supply-side. In this proposition, household debt is not a substitute but a complement to generous welfare state provisions. This is more likely to be a dynamic in the case of working-age insurance benefits, as there is a less clear mechanism linking the accumulation of debt in buying a home to the protection that more generous pension entitlements provide.

Another perspective is provided by Comelli (2021) who argues that the directionality of welfare spending with respect to *different age groups* is what matters. If the welfare state is strongly orientated to 'social consumption'-based policies supporting earnings-related benefits for labour market insiders and old age pensioners at the expense of 'social investment'-based policies, younger people will be more risk averse and less likely to take on debt.

There are also distinct macro- and micro-level dynamics that complicate the narrative. For example, at the micro-level it may be the case that increased wages fuels the acquisition of debt as it becomes possible to borrow more. In other words, it is higher income individuals and households that take on more debt and explain a greater share of the dynamics of debt accumulation. However, at the macro-level, we may argue that debt sustains consumption and economic growth in the context of a *fall* in the aggregate wage share. Similarly, individuals that see reduced pension entitlements may not be more likely to be able to purchase housing with a mortgage, but the retrenchment of pensions may be accompanied by the loosening of financial regulations to facilitate home-buying *in general* as policymakers seek to provide an alternative way of delivering security in old age.

Wiedemann's (2021) recent work on 'credit regimes' and the relationship with welfare and income is extremely useful here. He identifies three dimensions that affect the levels and distribution of debt in the economy:

- (1) The depth and breadth of financial markets, i.e. how much capital can be used to lend to households and business, which in turn is influenced by the distribution of households' financial assets, firms' funding needs and securitisation practices

- (2) The allocation of capital between households and business, driven by the extent to which there are strong long-term relationships between banks and firms, which in turn weakens mortgage markets and pension assets
- (3) Regulatory and fiscal policies, most notably loan-to-value ratios, rules about securitisation practices, tax incentives for mortgages and state-funded companies that assist with extending homeownership through borrowing

There are clear links to the wider growth regime and Variety of Capitalism framework but Wiedemann argues that the credit regime can operate independently of that and the precise interaction of welfare state institutions and credit regimes is important. For example, he finds that household debt only acts as a replacement for unemployment insurance in credit permissive regimes. Unemployment insurance generosity has no impact on the levels of household debt either way if credit is restricted within an economy as it is in many Continental European countries. In the next section, we turn to a highly permissive credit regime in the UK.

3. Debt and consumption in the UK

The UK is a commonly examined case study of the role of household debt and its assumed relationship with consumption as a liberal market economy that relies on strong household expenditure to drive aggregate demand. The financial sector has always played an important role in the British economy and the strength of its institutions in facilitating credit are commonly cited as one of the important factors in its imperial expansion, the industrial revolution and transition to capitalism. Yet, while the financial sector and the City of London as an engine of growth (and inequality) is an indispensable part of the picture, here we focus primarily on the effect and dynamics of financialisation with respect to households borrowing and consumption behaviour.

Starting from the long-term perspective, Figure 13 shows changes in new net household debt in the UK over the last 150 years alongside gross disposable income, consumption and the labour share, using data compiled by the Bank of England.

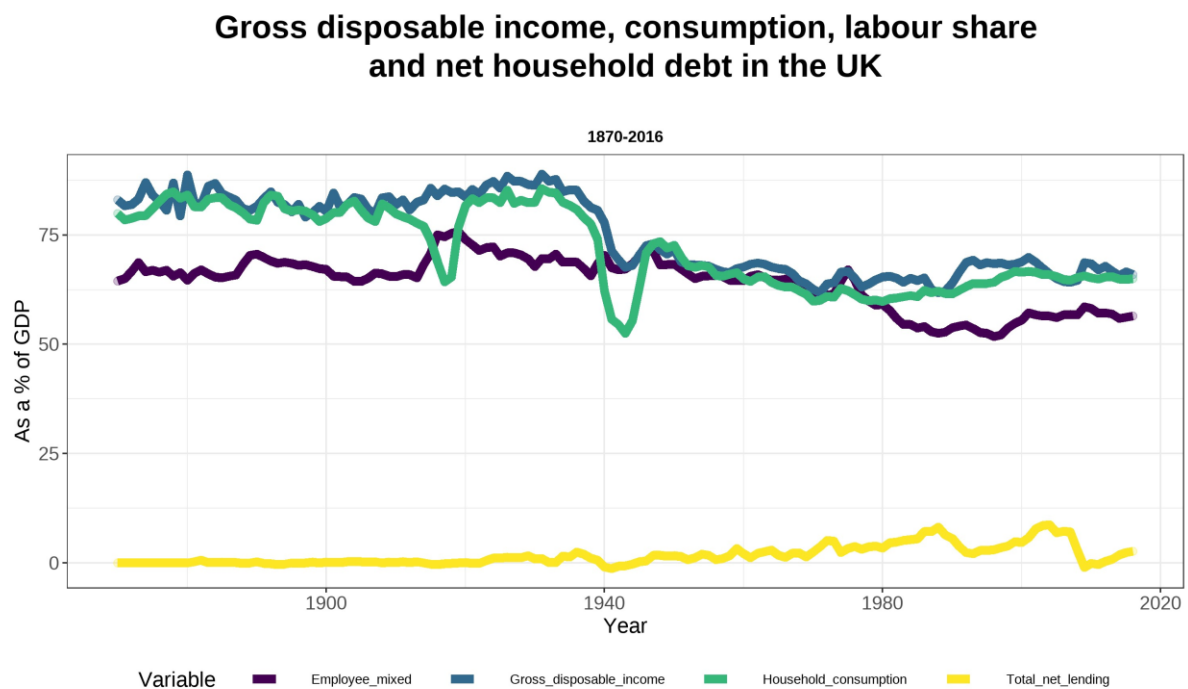


Figure 13: Long-term historical changes in gross disposable income, the addition of employee compensation and mixed income, household consumption and total new net lending in a given year [Source: Bank of England Millennium of Data Spreadsheet]

Zooming in on the last 30 years, one of the most interesting elements to the UK story is that the expansion of household debt occurred during a period up until the financial crisis in which the labour share increased as a % of GDP or GVA. However, the trends in gross disposable household income do seem to track changes in net household debt. When there was a decline in gross disposable income, new net household debt was at

its highest in the UK suggesting that it may have been compensating for the shortfall. On the other hand, this relationship appears to falter somewhat after the financial crisis when consumption falls as a share of GDP, household income increases but debt stays relatively constant.

Gross disposable income, consumption, labour share and net household debt in the UK

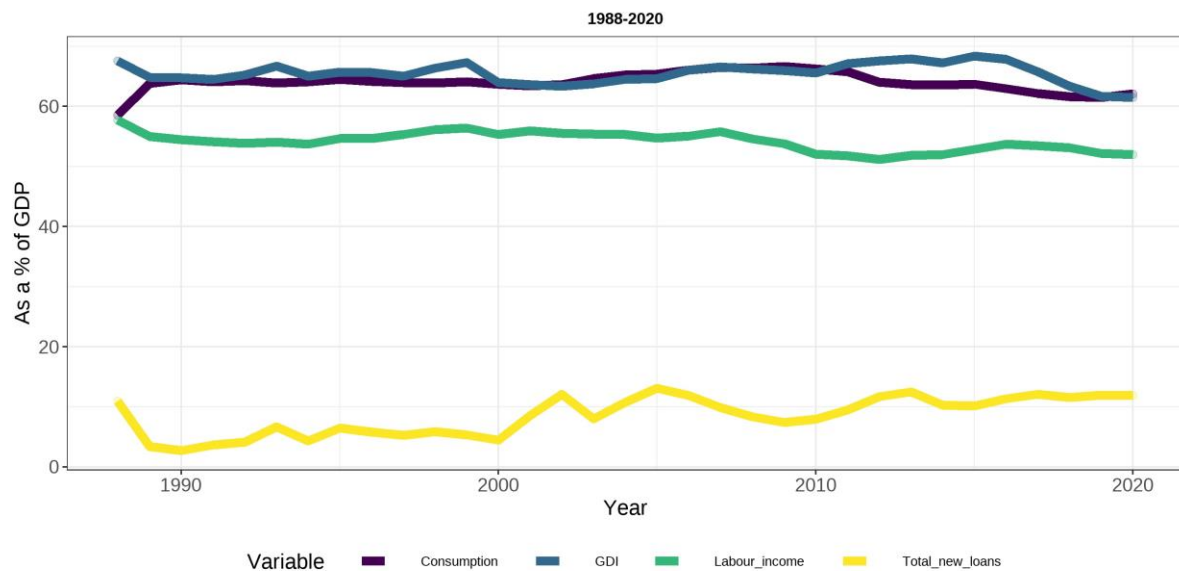


Figure 14: More recent relationship between household income, consumption, labour income and new household debt [Source: ONS]

The fact that increasing debt occurred at its peak by close to 10% of GDP per year may seem almost unbelievable and indeed given the low levels of new housebuilding it cannot have served to stimulate investment in new housing but rather driving up the price of existing stock or with equity withdrawals. Briefly with respect to the accuracy of the statistics, these numbers are broadly replicated across ONS Blue Accounts data and the Bank of England’s own quarterly datasets, as seen in Figure 15.

However, the Bank of England also provides data on equity withdrawals, which allow us to see directly the mechanism from housing debt to boosting household incomes and expenditure. Figure 16 shows the net equity withdrawals in quarterly terms alongside the gap between household income and consumption. We can see that equity withdrawals were particularly prominent in the period prior to the financial crisis and have been negative after the financial crisis. This helps to explain perhaps why the link between household debt and household income appears to decline after 2010. And it also is no doubt linked to the poor economic performance of the UK since then, starved of its stimulus of aggregate demand and growth in equity withdrawal-fuelled consumption.

If we plot the gap between household income and consumption against equity withdrawals in the period, we see a clear correlation between consuming a greater share of gross disposable income and equity withdrawals.

Yearly/quarterly new household debt in UK



Figure 15: Comparing statistics on new net household debt across two sources: Bank of England and ONS

Household income, consumption and housing equity withdrawals in the UK

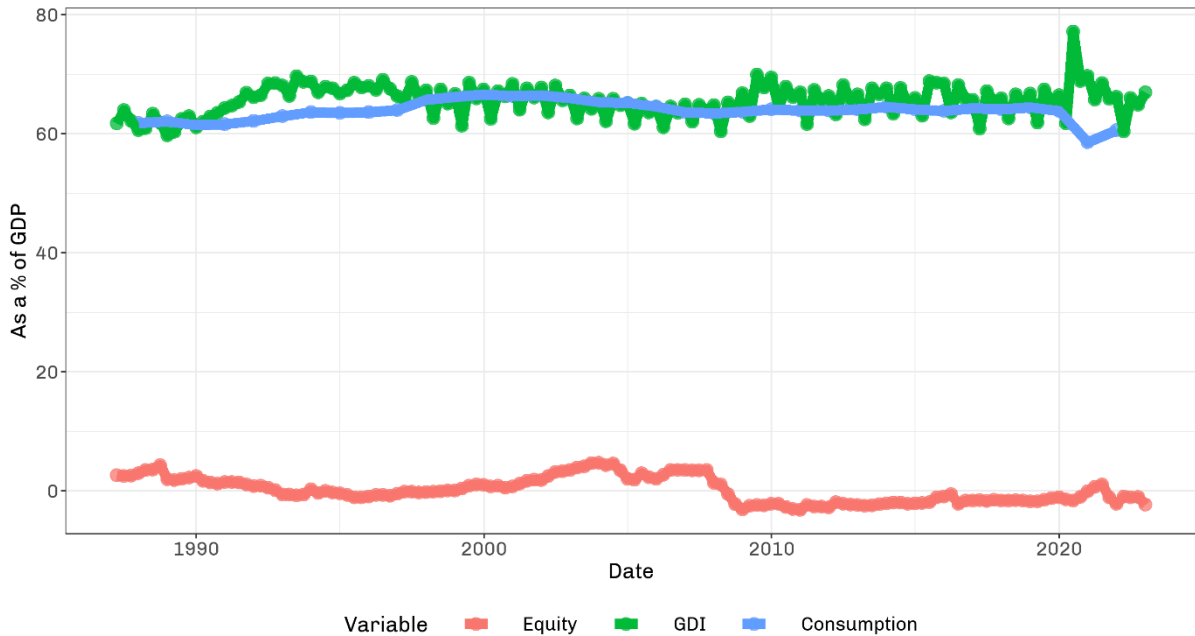


Figure 16: Household income, consumption and housing equity withdrawals in the UK [Source: ONS and Bank of England data]

**Correlation between equity withdrawals
and the difference between GDI and consumption**

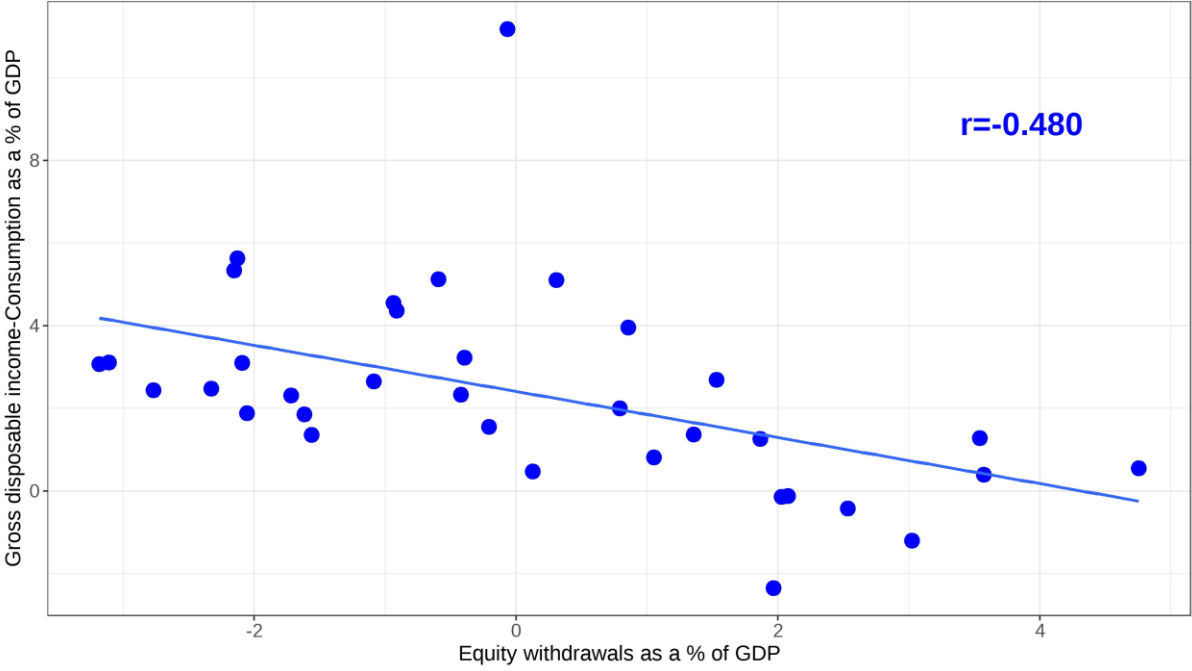


Figure 17: Correlation between equity withdrawals and the difference between gross disposable income and household consumption in the UK between 1987-2023 [Source: ONS and Bank of England data]

4. Anglophone liberal growth regime

In this section, we examine the case of the Anglophone liberal growth regimes. The US and UK typically serve as archetypal examples of the liberal growth regime or variety of capitalism. However, we extend our analysis to three other Anglophone countries, Australia, New Zealand and Canada. Ireland shares many but not all of these institutions but is excluded primarily on the basis that it is explicitly classified as belonging to an FDI-driven growth regime by other authors (Hassel and Palier, 2021; Bohle and Regan, 2022). There are also related concerns about the reliability of GDP figures that make comparative analysis difficult, particularly when such analysis uses GDP as an anchor to compare trends across time and countries as we do here.

There are many political and economic institutions that Anglophone countries share – highly liberalised labour markets, high net migration, liberalised and embedded financial institutions, social security systems that rely on means-testing, tuition fees for university, majoritarian electoral systems (not including New Zealand since 1994) and common law among others. It is the combination and interaction of these various institutions that provide the basis of any discussion of a liberal Anglophone growth regime.

While there are still important differences across Anglophone countries that will be discussed in more detail below, the broad trends related to the subject of this paper are relatively similar. Firstly, household debt is higher as a % of GDP in all Anglophone countries than the OECD average, albeit only recently so in New Zealand. Figure 18 shows the extent of household debt in Anglophone countries, with Australia maintaining nearly twice as much debt as a % of GDP as the OECD average at over 120% of GDP.

Household debt in Anglophone countries vs. other OECD countries

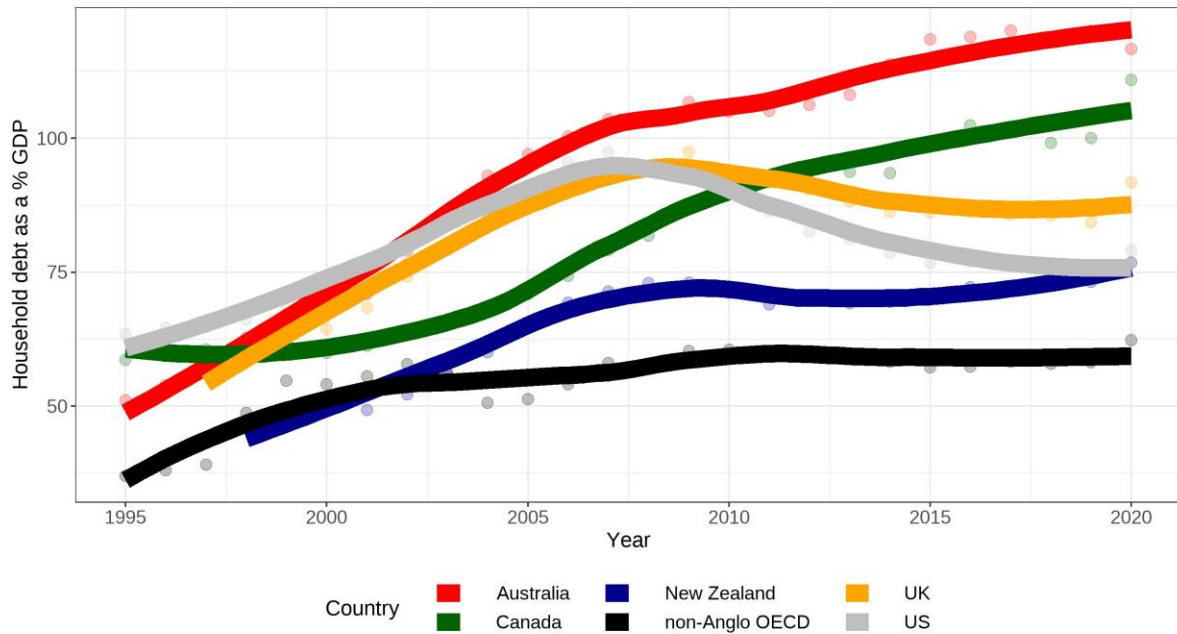


Figure 18: Household debt in Anglophone countries compared to other OECD countries [Source: OECD]

Similarly, all five Anglophone countries have higher than average levels of household consumption as a % of GDP, with the US exhibiting particularly high household consumption (Figure 19).

Levels of household consumption in Anglophone countries vs. other OECD countries

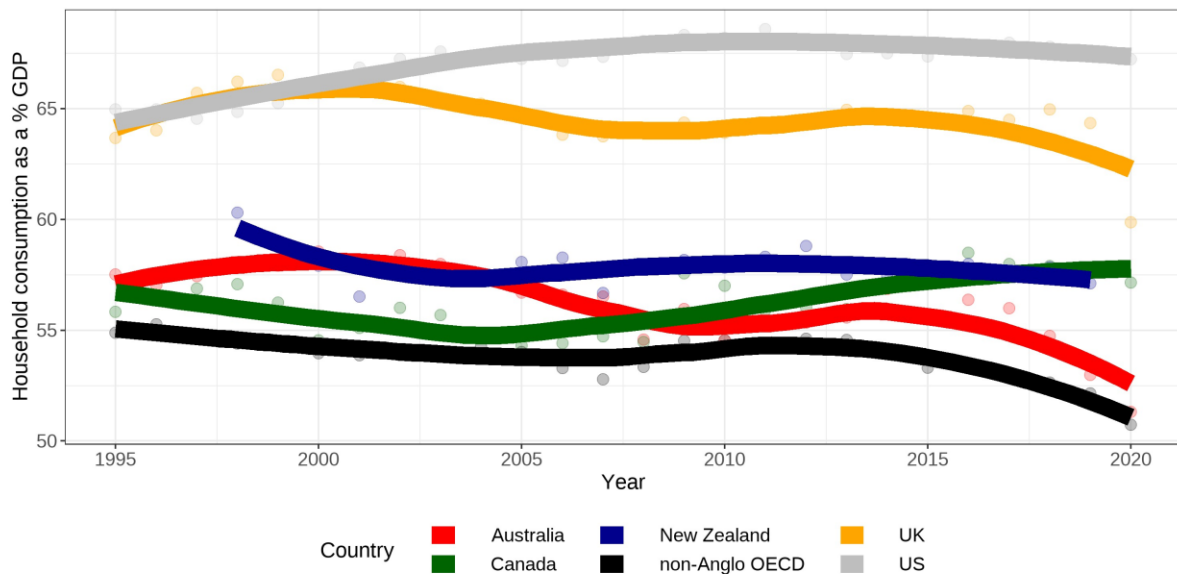


Figure 19: Household consumption in Anglophone countries compared to other OECD countries [Source: OECD]

The contribution of the real estate sector and financial services sector to gross value added is higher in all five countries than the OECD average. Figure 20 shows the trends in value added in real estate, while Figure 21 shows it for financial services. New Zealand has only recently gone above the OECD average in financial services but has a very high percentage of real estate value added.

Value added in real estate in Anglophone countries vs. other OECD countries

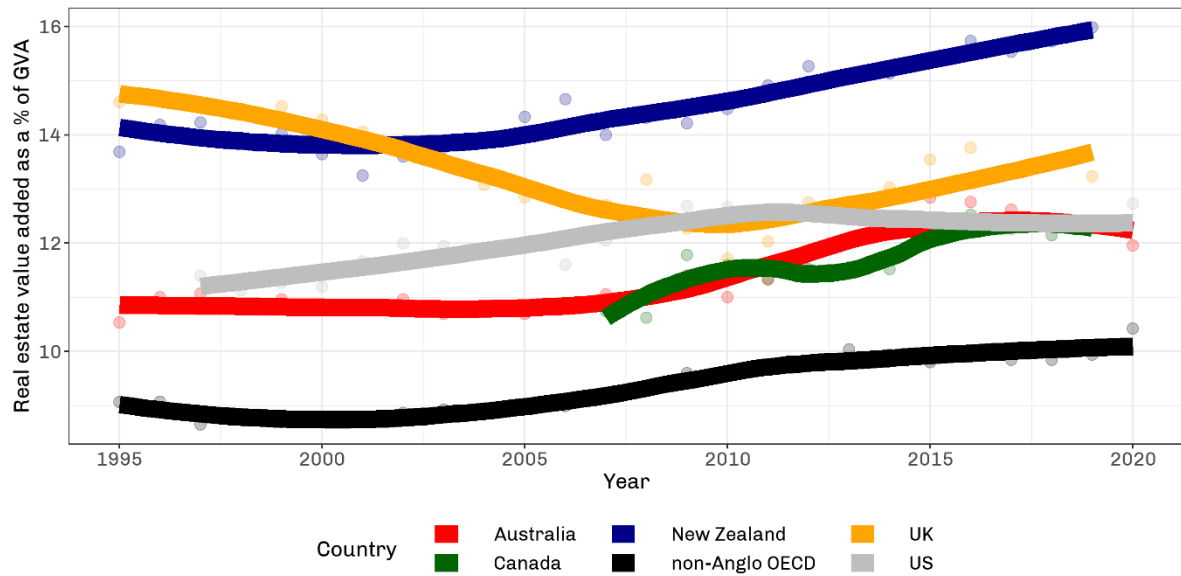


Figure 20: Real estate sector value added in Anglophone countries compared to other OECD countries [Source: OECD]

Value added in financial services and insurance in Anglophone countries vs. other OECD countries

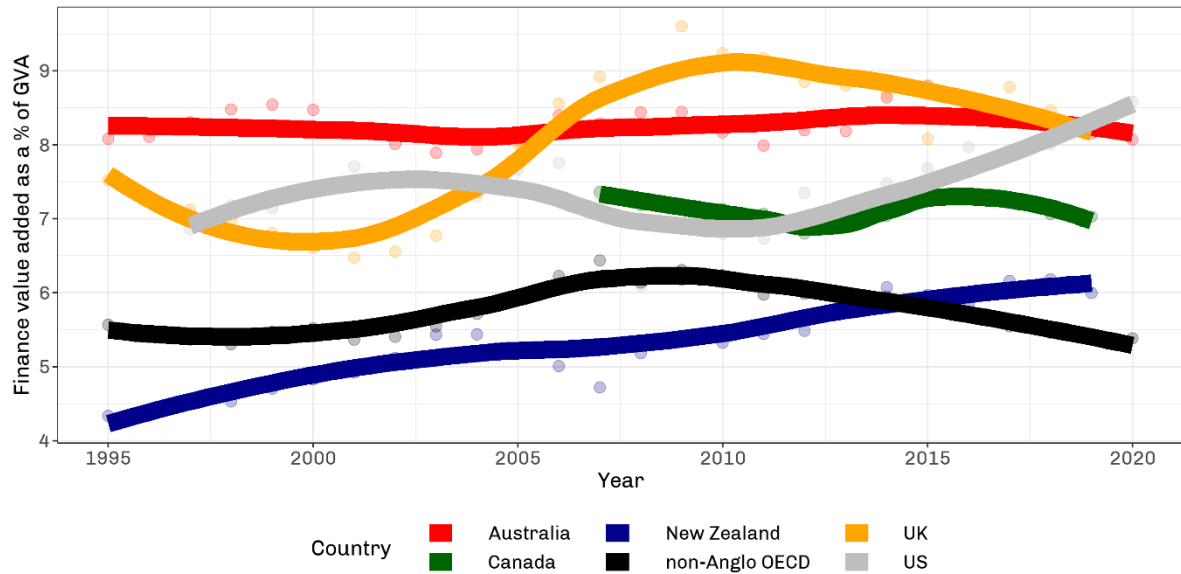


Figure 21: Financial services and insurance value added in Anglophone countries compared to other OECD countries [Source: OECD]

Finally, contrary to the idea that it is only household debt that is driving domestic demand, all Anglophone countries have higher labour shares as % of GDP than the average of other OECD countries, with the highest labour share in the US (Figure 22). It is important to state though that this is not the same as the labour share as a % of GVA or the adjusted labour share.

Labour share in Anglophone countries vs. other OECD countries

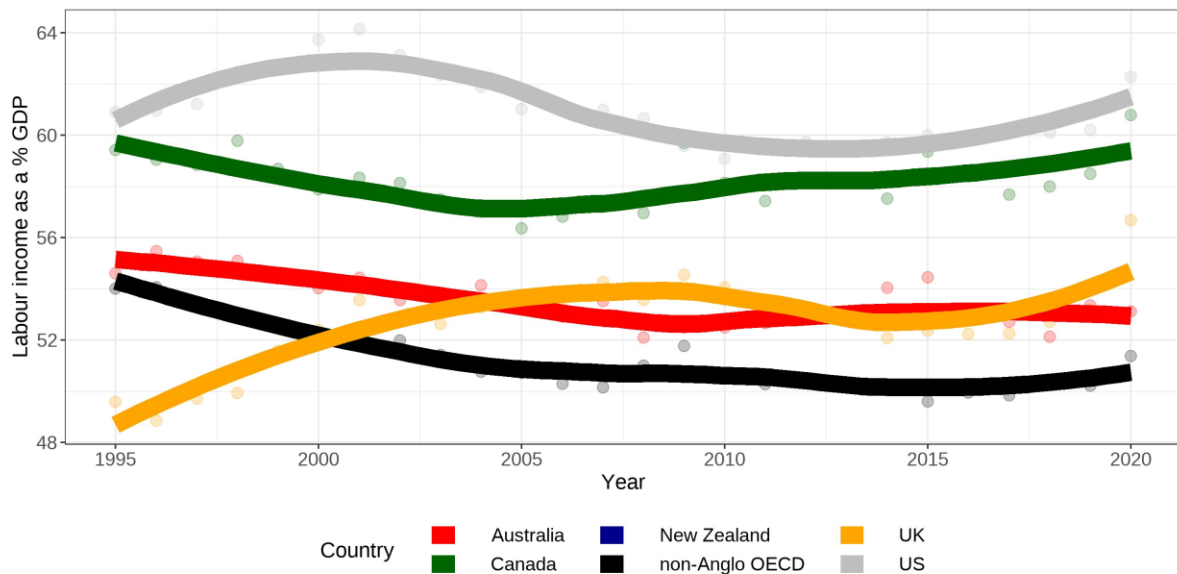


Figure 22: Labour share as a % of GDP in Anglophone countries compared to other OECD countries [Source: OECD]

However, one immediately noticeable difference between Anglophone countries, besides the fact that overall levels of household debt and consumption are relatively dispersed, is trends over time. Household debt in Australia has continued to rise even after the financial crisis, albeit at a slower rate. Canada has also seen continually increasing levels of household debt, despite taking off at a much later stage to the other countries. On the other hand, the US has seen dramatic deleveraging since 2007 to the point where in 2020, household debt was nearly at the OECD average. The UK is relatively similar to the US but has not seen the same level of deleveraging. New Zealand’s household debt was slowly rising until the crisis and has plateaued at a relatively low level close to the OECD average.

Household consumption has been falling as a % of GDP since 1999 in the UK and has also been falling in Australia, while the US saw consumption increasing until 2010 at which point it has plateaued at a high share of GDP. Canada saw a decline in the share of household consumption until the financial crisis before it began to rise again. New Zealand has seen relatively flat household consumption for the time there is data. The labour share also was not falling at all in the period of household debt accumulation in the UK and Canada.

The gross savings rate for households also points to the lack of distinctiveness in the liberal Anglophone countries, where it is not that dramatically different from the OECD average in all but New Zealand. The fact it is the latter that has such low gross savings rates is interesting given it has the lower rates of household debt. The low level of gross disposable income for households in New Zealand explains that and apart from the US implies that the demand-side explanation for accumulation of household debt may be related to strained household income rather than wages per se. Figure 23

indicates the gross savings rates while Figure 24 shows gross disposable income for households.

Gross savings rate in Anglophone countries vs. other OECD countries

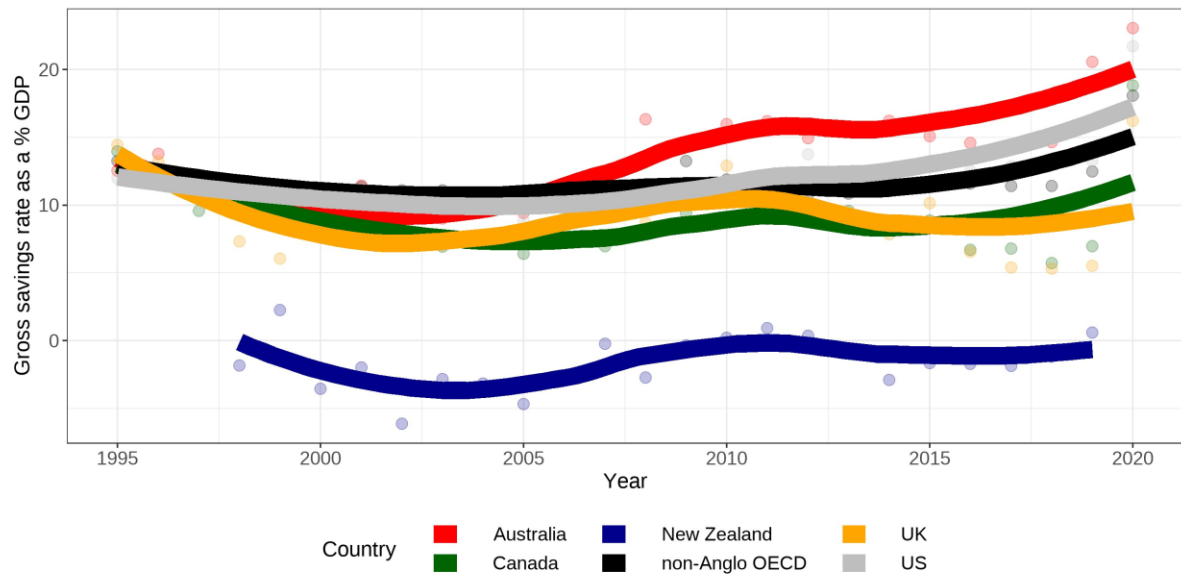


Figure 23: Gross household savings rate in Anglophone countries compared to other OECD countries [Source: OECD]

Gross disposable income (household) in Anglophone countries vs. other OECD countries

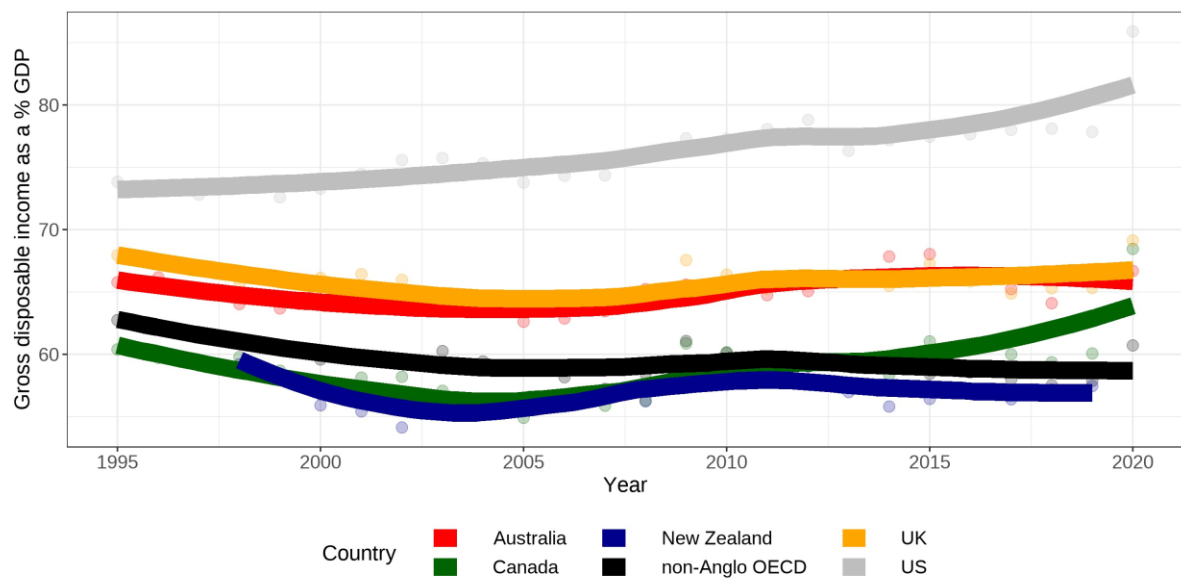


Figure 24: Gross disposable income in Anglophone countries compared to OECD countries [Source: OECD]

Looking at the dynamics of gross disposable income, consumption and new net household debt in each country, within-country variation does point to the connection between declining gross disposable income and higher net acquired debt in that year. If we assume that a variety of country-specific factors, including supply-side credit constraints. Figure 25 shows the negative relationship between changes in gross disposable income and newly acquired debt for all countries bar Australia.

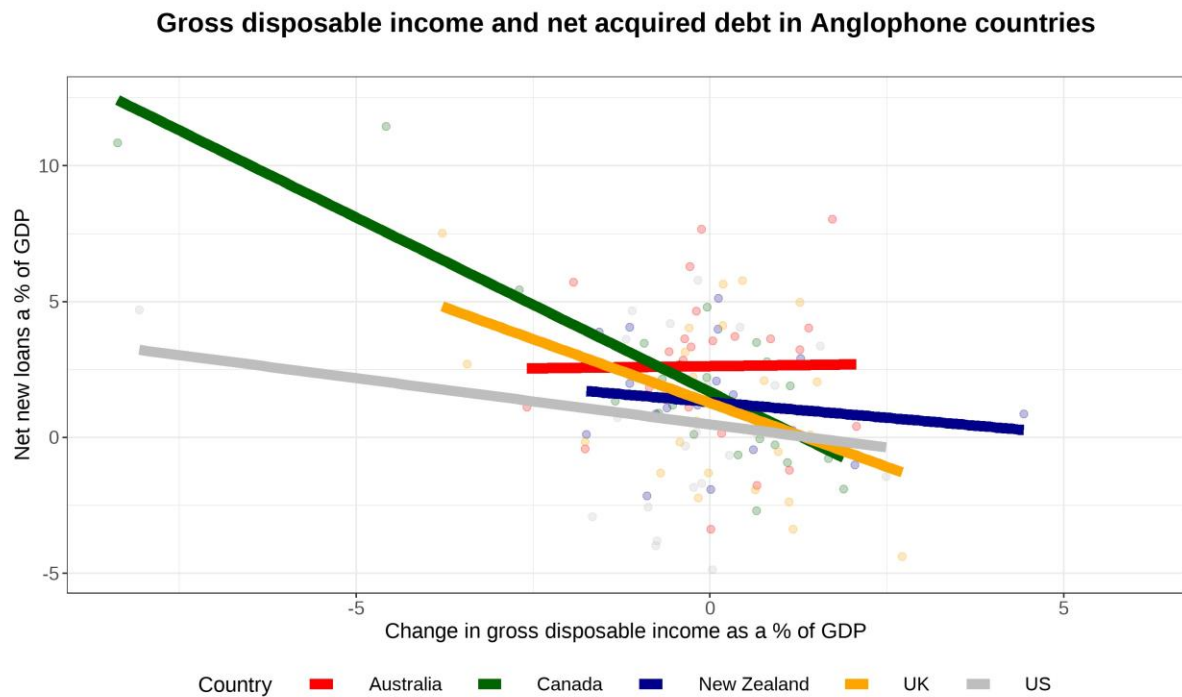


Figure 25: Relationship between change in gross disposable income as a % of GDP and net new loans as a % of GDP.

Finally, we look under the hood of gross disposable income to understand the extent to which different trends are occurring there and driving the inadequacy of household income, given that the wage share does not appear to be consistent across countries.

Figure 26 shows that in the UK, it is interestingly property income that appears to have declined as well as household profit from self-employed earnings and dwellings.

Distribution of gross disposable income in the UK

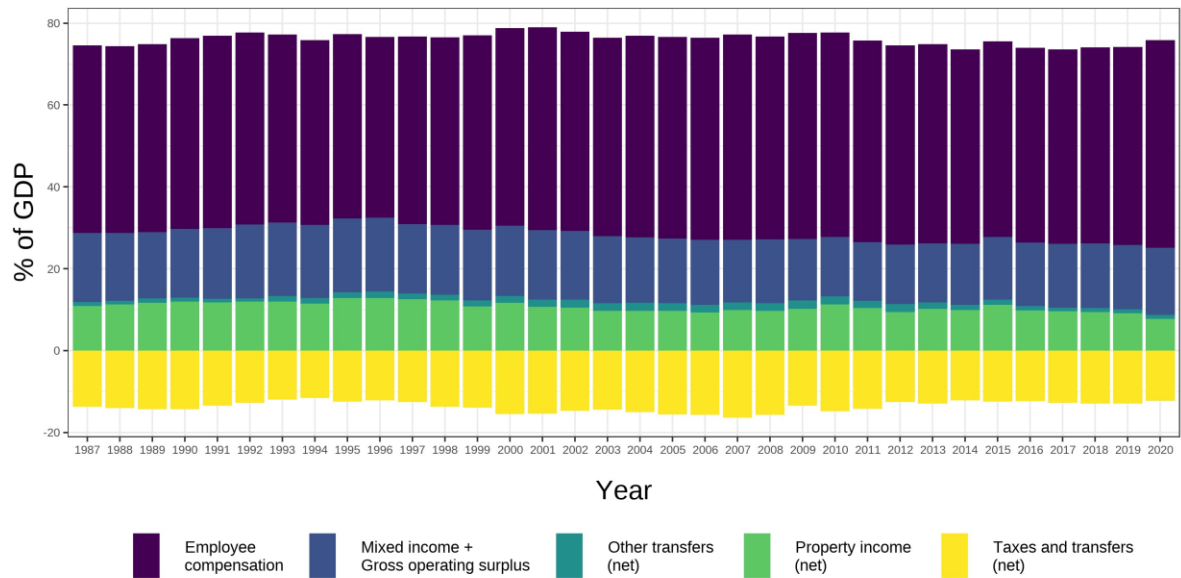


Figure 26: Distribution of gross disposable income in the UK [Source: ONS]

Whereas Figure 27 shows that in the US increases in government transfers relative to taxes and returning post-crisis property income are responsible for the increase in gross disposable income despite static or falling employee compensation.

Distribution of gross disposable income in the US

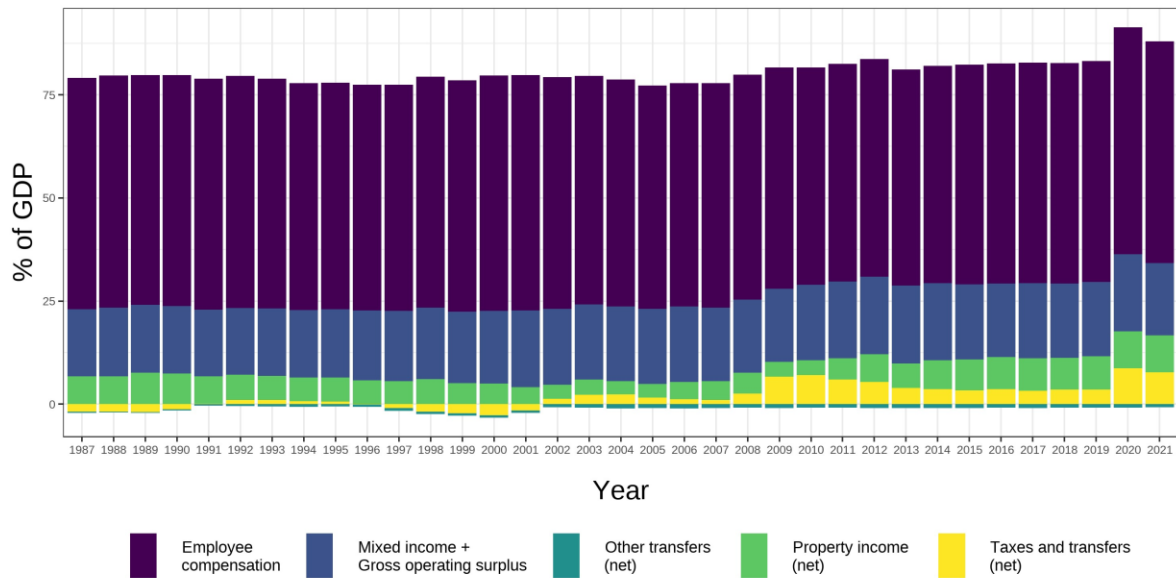


Figure 27: Distribution of gross disposable income in the US [Source: OECD]

Australia has seen a decline in employee compensation over the long-run while taxes and benefits and property income have fluctuated and household profits and earnings from self-employment have been relatively flat over time (see Figure 28).

Distribution of gross disposable income in Australia

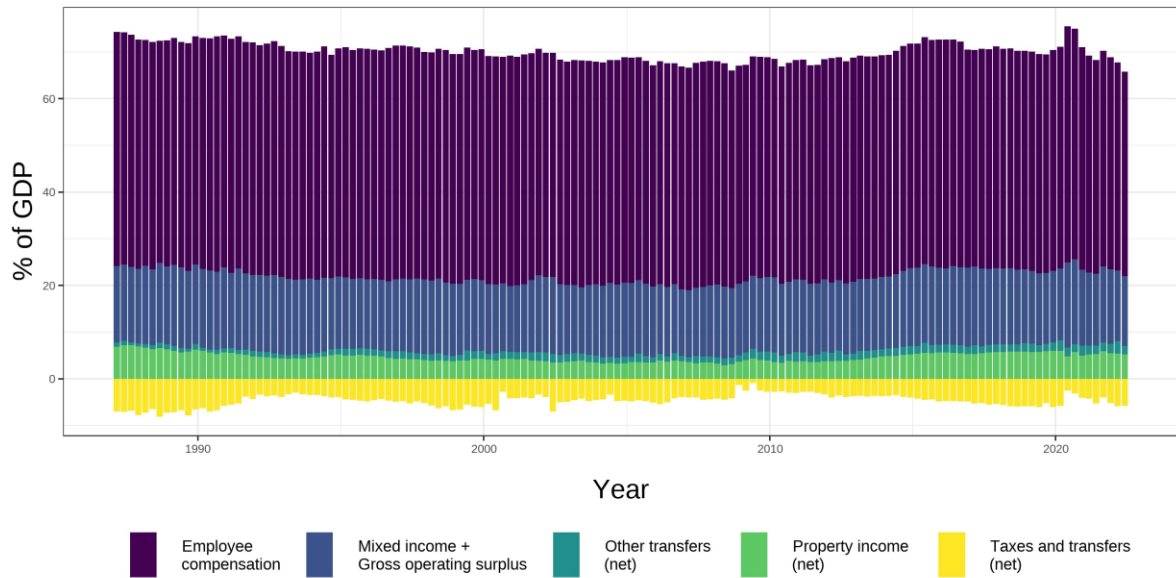


Figure 28: Distribution of gross disposable income in Australia [Source: ABS]

Finally, Figure 29 shows that New Zealand has seen a considerable fall in employee compensation in the long-run partly countered by reduced taxation and household profits.

Distribution of gross disposable income in New Zealand

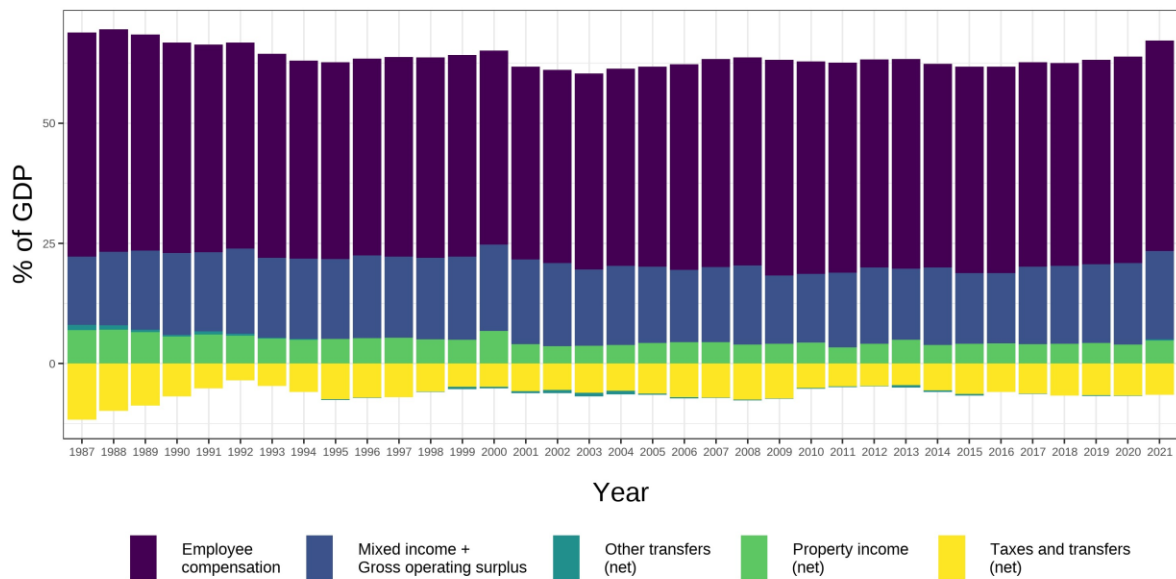


Figure 29: Distribution of gross disposable income in New Zealand [Source: StatsNZ]

Thus, while there appears to be some link between the accrual of household debt and declines in gross disposable income, the big picture is heterogeneity rather than consistent and dependable patterns, which goes some way to explaining why many of the assumed factors in the growth regime literature do not appear significant in the econometric analysis (Stockhammer and Moore, 2018) and why Wiedemann (2021) cites the distinctiveness of credit regimes.

Growth regimes are perhaps far more porous or less rigid than argued by some. In other words, there is more potential for a varied constellations of macroeconomic outcomes and political economic institutions even if there may be some clustering, path dependence and mutual interdependencies between educational, labour market and financial institutions.

5. Conclusion

This research note has provided an analysis of trends in household income, debt and consumption and summarised literature that seeks to understand what drives these trends, using a political economy framework. The interaction between household income, debt and consumption is an important factor in the functioning of advanced economies and particularly in Anglophone countries and the UK. As many other economists have argued, the exclusive focus on government debt in media and political debates obscures a central driver of instability in our economies: household debt.

The analysis suggests that aggregate dynamics in household debt at the country level are inextricably linked to housing in most advanced economies. The scale of debt used to purchase homes is such that it is the overwhelming driver of the dramatic changes we have seen in most countries. However, this does not mean that debt and consumption patterns are not linked. The UK case in particular shows that households were not borrowing solely to purchase housing in the lead up to the financial crisis, as net equity withdrawals were roughly half of the total amount of new net debt. Even when debt is used to purchase housing, this can stimulate consumption and growth through the development of the real estate sector and the money received by households selling appreciated assets.

If this expansion of household debt was a critical factor in sustaining household consumption in many economies in the period leading up to the financial crisis, then this suggests that stagnation subsequently may be linked to the flattening of new household debt. The US serves as a reminder that the expansion of debt is not the only driver of consumption and economic activity, as it has seen substantial economic growth during a period of debt deleveraging, but for many other economies such as the UK, the inability to expand household debt to sustain consumption has no doubt been a key factor.

In the absence of wage-led and (household) debt-fuelled growth, is there an alternative way to stimulate household consumption? One obvious solution would be for government to provide more income to households through transfers, either through government spending or as some have suggested through central bank financing (Turner 2016, Crocker 2020). This could be done through a universal basic income transferred to all households or targeted at low-income households. Of course, this may be more difficult to sell in an era of high inflation with supply constraints suggesting that additional stimulus may accelerate inflationary pressures. But in the longer term, consumption-led economies such as the UK must consider how to provide households with sufficient income without resorting to the further accumulation of household debt that drives instability and crisis.

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