Financial Landscapes and Household Choices:
A Comparative Study of Wealth Effects on Consumption in the EU

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BACKGROUND #1

❑ Understanding the **relationship between wealth changes and household consumption** is essential for predicting consumer behaviour, informing monetary policy, and fostering economic stability (Singh, 2022; Badarinza et al., 2019).

❑ This study aims to shed light on the **response of non-durable consumption to changes in wealth**, within the diverse setting of the European Union, with its mix of developed and emerging economies.

MAIN RESULTS #3

❑ **Housing Wealth** has no significant impact on NC across the full period in EMEs but a negative effect in AEs.

❑ **Stock wealth** significantly boosts NC across the full period for both EMEs and AEs.

❑ **Money wealth** has a similar positive effect, but more pronounced in EMEs.

❑ Decreases in **short-term interest rates** lead to an increase in NC in both economies, with the impact being more pronounced in EMEs.

❑ In EMEs, none of the W components and IR were significantly related to NC during the **crisis** period, suggesting a higher impact of other factors overriding wealth effects.

Why **negative wealth effects ?**

- Inverse wealth effect
- Substitution effect
- Deleveraging
- Differences in sensitivity to changes in W

ECONOMIC POLICY IMPLICATIONS

Wealth Stability: policies for real estate and stock markets stabilization, to ensure household consumption smoothing, especially in times of economic uncertainty.

Interest Rate Adjustment: Monetary policy adjustments made cautiously, considering the impact of short-term IR changes on household NC in both samples.

Financial Resilience: Policies encouraging financial resilience and savings so that households in EMEs buffer against fluctuations in wealth and income. For AEs, such measures can further enhance stability in consumption patterns.

METHOD #5

- We first assess the form of the empirical model through a non-parametric approach, **categorical regression splines – CRS**:

$$C_{it} = f(I_{it}, HW_{it}, SW_{it}, MW_{it}, IR_{it}, Controls) + \sigma(I_{it}, HW_{it}, FW_{it}, MW_{it}, IR_{it}, Controls)\omega_{it} ,$$
$$f(.) \text{ and } \sigma(.) \text{ Unknown}$$

- Then, we employ the **Pooled Mean Group (PMG)** estimator and validate our results using Fieller's theorem to estimate confidence intervals. The estimated parametric specification is:

$$C_{i,t} = \alpha_i + \beta_{i,1}I_{i,t} + \beta_{i,2}HW_{i,t} + \beta_{i,3}SW_{i,t} + \beta_{i,4}MW_{i,t} + \beta_{i,5}IR_{i,t} + Controls + \varepsilon_{i,t}$$

Note: All variables, except IR, are expressed in log terms.

References:
Singh, B. (2022). Housing and stock market wealth effects in developing economies. International Economics and Economic Policy, 19(1), 29-49.
Badarinza, C., Balasubramaniam, V., & Ramadorai, T. (2019). The household finance landscape in emerging economies. Annual Review of Financial Economics, 11, 109-129.

QUESTIONS #2

🔍 How do **changes in wealth** (W) influence **non-durable consumption** (NC) patterns in **developed** (AEs) and **emerging** (EMEs) economies within the EU?

🔍 What **implications** does this relationship have for individual economic decision-making, market dynamics, and **policy formulation**?"

Evolution of non-durable consumption
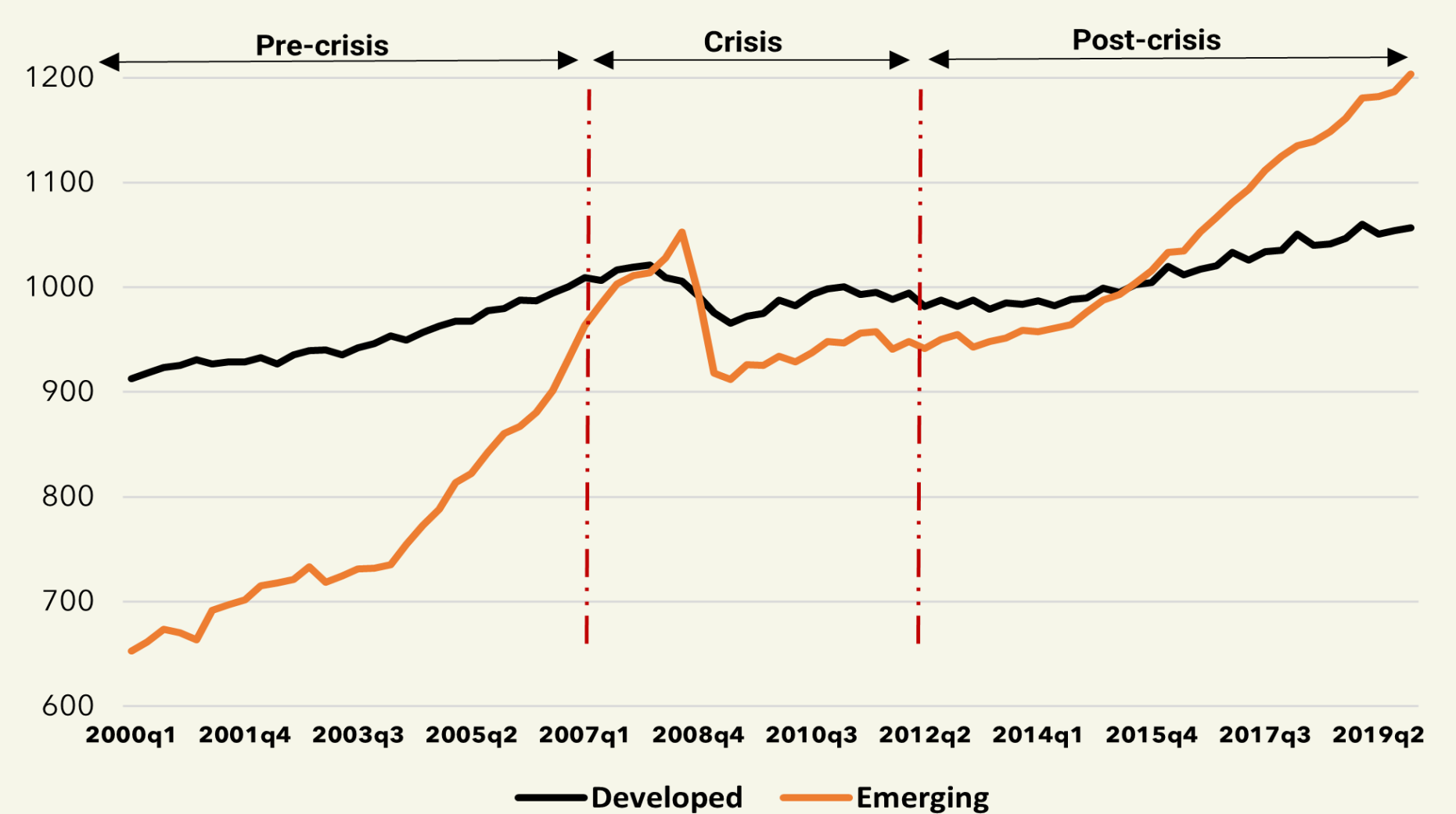
Note: The graph presents the evolution of average non-durable consumption expenditure in the two samples.

DEVELOPED ECONOMIES	FULL PERIOD	PRE-CRISIS	CRISIS	POST-CRISIS
HW effect	YES (-0.015)	NO	YES (0.099)	YES (-0.073)
SW effect	YES (0.026)	NO	NO	NO
MW effect	NO	YES (-0.011)	NO	NO
IR effect	YES (-0.010)	NO	YES (-0.005)	NO

EMERGING ECONOMIES	FULL PERIOD	PRE-CRISIS	CRISIS	POST-CRISIS
HW effect	NO	NO	NO	YES (0.078)
SW effect	YES (0.055)	NO	NO	NO
MW effect	YES (0.187)	NO	NO	YES (0.143)
IR effect	YES (-0.004)	YES (-0.011)	NO	YES (-0.007)

Note: The values displayed in parentheses represent elasticities to consume out of wealth or the elasticity of non-durable consumption to changes in short-term interest rate.

DATA #4

- **Outcome:** Households expenditure on semi-durable, non-durable goods and services (**NC**)
- **Data:** compensation of employees (proxy for income - **I**), house price index (housing wealth – **HW**), stock price index (stock wealth – **SW**), broad money (money wealth – **MW**), short-term interest rate (**IR**)
- **Controls:** Unemployment rate, ESI, GINI Index
- **Two subsamples:** 11 EMEs, 12 AEs
- **Period covered:** 2000 Q1 – 2019 Q4 (COVID-19 pandemic excluded)
- **Three sub-periods:** Pre-crisis (2000-2007), Crisis(2008-2012), Post-crisis (2013-2019)

CONCLUSIONS #6

❑ **Economic Linkages:** The study showcases the complex dynamics of income, wealth, and interest rates in shaping household consumption patterns across developed and emerging EU economies.

❑ **Policy Relevance:** Findings carry significant implications for monetary and fiscal policy design and the necessity of differentiated approaches for emerging and developed economies.