

# **DETERMINANTS AND EFFECTS OF MORTGAGE EQUITY WITHDRAWAL IN THE UNITED KINGDOM**

**Philomena M. BACON**

**School of Economics  
University of East Anglia  
Norwich NR4 7TJ  
United Kingdom  
email: p.bacon@uea.ac.uk**

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## **ABSTRACT**

During the noughties in the UK, we have seen a massive explosion in unsecured personal debt mirrored to a lesser extent by an exponential rise in secured debt. Much of the secured debt is attributed to an increase in Mortgage Equity Withdrawal (MEW), that is, borrowing secured on the housing stock but not invested in it. In this paper, two broad questions are posed: Is the rise in property prices underpinned by the rise in MEW? Do MEW borrowers represent a greater risk to lenders than other borrower types? Both questions are answered using data from the Council of Mortgage Lenders (CML) over the period 1979-2006 covering over a million secured loan approvals. CML data takes the form of annual cross sections of approvals, from which a monthly time series dataset has been extracted for use in this research. Our analysis focuses on differentiating between three borrower types: MEW, First time buyers, and Trade up/down borrowers, in terms of: interest rate charged; loan term; age, income of applicants; and other characteristics used to justify the size of loans approved. Applying Granger-causality tests to the time series data, we find that the rise in advance size has caused house prices to rise. After applying co-integration tests, an Error Correction Model is estimated that explains the endogenous dependency of property prices on MEW. Discrete choice models applied to the cross section data are used to identify reasons for the extraordinary phenomenon.

**Key Words:** *Mortgage Equity Withdrawal; Discrete Choice Models; Granger Causality; Cointegration; Error Correction Models; Vector Error Correction Models.*