

Box 6

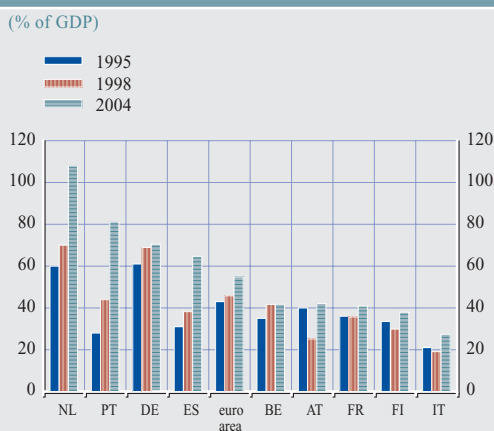
HOUSEHOLD DEBT RATIOS IN THE EURO AREA FROM AN INTERNATIONAL PERSPECTIVE

Household borrowing has increased considerably in a number of regions of the world over the past decade, bringing debt ratios to unprecedented heights. This has not only raised some questions about sustainability, but has also highlighted differences in the level and the evolution of debt ratios across countries. This Box examines the level of household debt ratios within the euro area and in comparison with a selection of mature economies.

In the fourth quarter of 2004, estimates of the euro area household debt-to-GDP ratio further increased to 55%. However, this figure masks substantial differences between euro area countries, with ratios ranging between 108% (the Netherlands) and around 27% (Italy) (see Chart B6.1). Outside the euro area, there are also considerable differences and, on average, even though they have been rising, household debt ratios in the euro area are among the lowest in the mature economies. Denmark, the UK, Australia, the US and Sweden all have debt ratios that exceed the euro area average (see Chart B6.2).<sup>1</sup> Aggregate numbers may not, however, always be meaningful for assessing sustainability, as the proportion of households carrying debt differs between countries. For instance, in the US, the Netherlands and Spain, the proportion of indebted households is around 65%, whereas in Australia and Germany around 40-50% of households have taken on debt, compared with only 19% in Italy.<sup>2</sup> An additional consideration for some of these countries is that the high level of net wealth (financial and housing) should be taken into account when assessing the sustainability of debt.

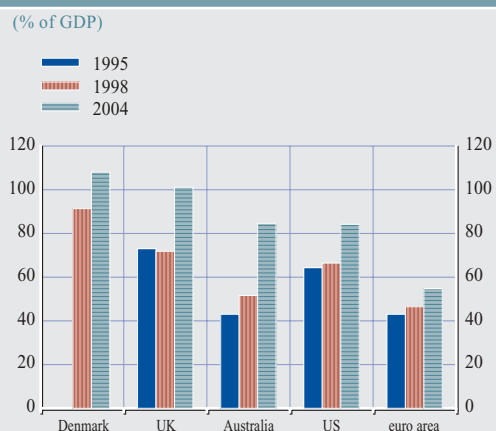
Rising household debt ratios over the past decade are often explained by the strength of house prices together with low interest rate levels. For example, the December 2004 FSR highlighted

Chart B6.1: Debt ratios within the euro area



Source: ECB calculations based on national financial accounts data.  
Note: The ratio for Finland refers to 2003.

Chart B6.2: Debt ratios for the euro area and outside the euro area



Sources: ECB, Australian Bureau of Statistics, Reserve Bank of Australia (RBA), Bureau of Economic Analysis, Federal Reserve, Bank of England and Danmarks Nationalbank.

1 It is important to note that definitions of debt can differ across countries.  
2 See J. Crook (2003), "The Demand and Supply for Household Debt: A Cross-country Comparison", mimeo, University of Edinburgh.

the close relationship between increases in house prices and loans for house purchase in euro area countries between 1998 and 2003.

There are several reasons why debt ratios may differ across countries. The incurrence of debt depends critically on the availability, cost and flexibility of debt financing. The underlying factors are to be found on both the demand side and the supply side, with the latter closely related to developments in capital markets and funding practices (see Box 14 in the December 2004 FSR). Moreover, the number of housing transactions is clearly different between EU15 countries. For instance, in relation to the size of the population, the number of transactions is highest in Ireland and the UK, and comparatively high in Denmark, Greece and Sweden, the latter twice as high as in Germany.

Different housing finance markets also have some specific features that may affect the level of housing-related debt. For example, the possibility to borrow more for the same collateral, re-mortgaging and the taking out of second mortgages – benefiting from low refinancing costs and increased house values – are common in the US, the UK, Australia and a few euro area countries (such as the Netherlands and, to a lesser extent, Ireland). Furthermore, a buy-to-let market, where households invest in properties for renting, may also lie behind higher debt ratios in specific countries. This is particularly the case in the UK and Australia, although this trend represents a small part of the stock. The rate and amount of first-time buyers, as well as the rate of owner-occupation, may also be factors contributing to debt ratios and may help to explain why they differ between different countries. For example, countries such as Australia, the US and the UK have reasonably high rates of owner-occupation (around 70%), which potentially explains the higher household debt levels in these countries. However, other factors appear to play a role, since other countries where households are highly indebted, such as Denmark and the Netherlands, have fairly low owner-occupation rates of below 55%.

To sum up, household debt ratios differ rather widely between regions and countries, with a variety of factors that could explain these differences. From a financial stability perspective, the scale of household sector indebtedness matters only to the extent that it affects the ability of households to service outstanding debt.