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News release

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Bank of England Quarterly Bulletin - Spring 2004

The Spring issue of the Bank of England Quarterly Bulletin is published today. Among the articles it contains are:

Asset pricing and the housing market

House prices have risen rapidly in recent years. There is little doubt that such rates of increase are unsustainable. But there is uncertainty about the sustainability of the current level of house prices, or the likelihood of price falls. This article applies asset-pricing theory to the housing market to gain additional insights into some of the factors accounting for the rise in house prices.

It shows that estimates of the ratio of house prices to net rentals are currently well above their long-term average, a scenario that in the past has often been followed by periods in which real house prices have fallen. Lower real interest rates account for part of the increase in the ratio, but to account fully for this increase the housing risk premium would need to have fallen too. Comparing the housing risk premium with that in the late 1980s suggests that house prices are closer to sustainable levels now than was the case in the late 1980s. However, because of data and model limitations no firm conclusions can be drawn.

Durable spending, relative prices and consumption

In real terms, the growth of durable spending has substantially outpaced that of spending on other goods and services since the mid-1990s. Nominal spending on durables and on non-durables has grown at similar rates during that period so the gap largely reflects the effects of falling relative prices. The article uses a simple framework to assess the behaviour of the real and nominal ratio of durable to non-durable spending in the long run. It also considers the current position of the ratios in more detail and provides some assessment of how we might expect them to have evolved given prevailing cyclical factors. The analysis shows that the nominal ratio of durable to non-durable spending is close to its estimated long-run path, which suggests that, unlike in previous cycles, there is currently little imbalance in durable spending. This may be surprising, as we might have expected durable spending to have reacted more to the fall in interest rates and rising housing equity over the past two to three years. The article also considers a number of other explanations as to why the nominal ratio has not risen more.

Measuring total factor productivity for the United Kingdom

A good understanding of past and current productivity growth is important for understanding aggregate supply capacity, and so for the conduct of monetary policy. To understand the sources of supply capacity it is important to measure output and factor inputs correctly. This article summarises recent and ongoing research at the Bank of England on improved measures of factor inputs, which are shown to have a potentially material impact on the estimates of total factor productivity growth.

The net effect of these measurement improvements is complex and varies over time. While the overall picture before and after these corrections remains broadly similar, the point estimates are often different. It appears that, when all these improvements are made, the decline in the growth rate of aggregate total factor productivity in the late 1990s, relative to the first half of that decade, is reduced but not eliminated. In addition, the correlation of total factor productivity growth with GDP growth is reduced.

Also in the Spring 2004 Bulletin:

- a regular commentary on 'Markets and operations';
- articles on 'The relationship between the overnight interbank unsecured loan market and the CHAPS Sterling system' and 'How much does bank capital matter?'; and
- summaries of recent Bank of England working papers and speeches from the Bank.

Note to Editors

Copies of the Quarterly Bulletin are available from the Publications Group, Bank of England, Threadneedle Street, EC2R 8AH (Tel: 020 7601 4030; fax 020 7601 3298) or from the Bank's Quarterly Bulletin pages.