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**MODELLING HOUSHOLDS' SAVINGS AND DWELLINGS INVESTMENT
– A PORTFOLIO CHOICE APPROACH**

Abstract

One important characteristic of dwellings is that housing can be regarded as an investment or asset. Our paper focuses on this function of dwellings and develops a stochastic portfolio choice model for the housing market, which is easy to incorporate into medium and large-scale macro models. Theoretical results suggest that house prices move in line with households' income, although house prices have a higher variance than income does. Another important implication of the model is that the portfolio share of housing investment depends on the excess return, defined as the difference between return on housing and financial investment and the variance of excess return describing the riskiness of an asset. Our intention is to test these theoretical implications of the model on several countries, however we test on UK data, due to the data availability. In this case, empirical results strengthen the model framework. To indicate the estimation difficulties in accession countries we display some results on the Hungarian housing market.

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