



# The Impact of Housing Prices on the Upgrading of Consumption

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**Abstract.** This paper examines the relationship between urban residents' consumption behavior and rising housing prices in China, focusing on how changes in housing prices affect consumption upgrading through the wealth effect and crowding-out effect. By synthesizing historical data and literature, this study reveals the impact of housing price fluctuations on residents' purchasing power and wealth perception, and their changes in consumption patterns. Results indicate that in cities with higher incomes, rising housing prices may promote consumption upgrading through the wealth effect; however, in cities with lower incomes, high housing prices primarily suppress residents' consumption capacity through the crowding-out effect, especially concerning non-essential goods and quality-of-life services. The paper also explores the housing price-to-income ratio in China compared to developed countries and offers policy recommendations based on the current real estate market conditions. This research provides valuable data support for policymakers and points out new directions for future studies on housing prices and consumption behavior.

**Keywords:** Consumption Behavior, Consumption Upgrading, Wealth Effect, Crowding-out Effect.

## 1 Introduction

In the context of globalization, the development and changes in the real estate market affect the stable growth of national economies and also alter residents' consumption behaviors and lifestyles. Since the latter half of the 20th century, the real estate markets in major global economies have undergone phases of robust development, cyclical bubbles, and market adjustments. Particularly during periods of global economic downturns, fluctuations in housing prices have significantly impacted residents' consumption capacity and choices. Since the economic reforms of 1978, China's real estate market has gradually developed. The abolition of the housing distribution system in 1998 marked the beginning of rapid increases in housing prices, accelerating urbanization, with housing prices witnessing nearly a threefold increase from 1998 to 2017. This growth not only propelled the process of urbanization but also greatly altered residents' consumption patterns. While rising housing prices have enhanced wealth perception and increased consumption capacity for homeowners, they have

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also limited the consumption potential of non-homeowners, especially those in the lower-income groups, through the crowding-out effect. This paper will explore the underlying wealth and crowding-out effects of rising housing prices, revealing the specific impacts of these increases on residents' consumption upgrading, and provide a deeper understanding of how changes in housing prices affect consumption choices, especially against the backdrop of improving living standards.

## **2 Literature Review**

Existing literature reveals the complex impact of housing price fluctuations on resident consumption behavior. Through an integrated analysis of related studies, the paper can gain a deeper understanding of the specific mechanisms through which housing prices affect consumption upgrading.

### **2.1 Theories of Consumption Upgrading**

Consumption upgrading is a social and economic phenomenon involving many aspects, which refers to the process of consumers' consumption changing from satisfying basic needs to higher and more diversified consumption levels under the background of economic growth and income improvement.

In the study on "Theoretical Analysis of Coexistence of Consumption Upgrading and Consumption Downgrading", Li suggests that China's consumption upgrading has gone through several stages, from survival necessities to the popularization of non-essentials, and then to service-based consumption. At the same time, the study emphasized that consumption downgrading and consumption upgrading coexist in some areas [1].

Huang analyzes consumption upgrading from multiple latitudes, including content upgrading and quality upgrading, in *The Theoretical and Practical Study of Residents' Consumption Upgrading*. The research pointed out that although theoretically consumption should be transformed from survival to development to enjoyment, in practice, factors such as uneven income distribution constrain the transformation of consumption from survival to enjoyment [2].

In the context of the current economic development, consumption upgrading has become an important factor in promoting sustainable social and economic growth. Through in-depth analysis and review of related literature, the study understands the dynamic process of consumption upgrading and its influencing factors from multiple perspectives.

### **2.2 House Prices and Consumer Behavior**

According to Dai's study, "Empirical Analysis of the Impact of Housing Price Changes on Residents' Consumption Behavior", shows that although rising housing prices theoretically produce a wealth effect and thus stimulate consumption behavior,

the inhibitory effect is more significant in practice, especially the negative impact on the consumption of durable goods [3].

Based on Wang's study "Analysis of the Impact of Housing Price Fluctuations on Chinese Residents' Consumption Behavior", the research points out that in the context of the continuous rise in housing prices, China's housing price fluctuations have a significant impact on residents' consumption behavior. High housing prices increase residents' financial burden of homeownership, leading to a decrease in consumption capacity. Although home ownership brings some wealth effect, high house prices are more often manifested as a crowding-out effect, i.e., high house prices inhibit the ability to spend on other types of consumption [4].

These studies show that the relationship between house prices and residents' consumption is complex, and that high house prices tend to inhibit consumption by increasing the economic burden on residents, especially in terms of durable goods and non-basic living needs

### **2.3 Existing Studies on House Prices and Consumption Upgrading**

According to Luo's study, "The Impact of House Prices on Urban Residents' Consumption Upgrading," it is found that rising house prices significantly inhibit urban residents' developmental and enjoyment consumption, especially in cities with high income levels, and the inhibitory effect of rising house prices on consumption upgrading is even more significant [5].

Ye pointed out in "the impact of house prices on consumption upgrading" that in cities with high consumption level, the rise in house prices promotes consumption upgrading through the wealth effect, while in cities with low consumption level, the crowding out effect brought about by the rise in house prices hinders consumption upgrading [6].

Through the above research, it is not difficult to see that house prices have a double effect on consumption upgrading: under certain conditions, rising house prices can promote consumption upgrading through the wealth effect; however, a more segmented study found that in low- and middle-income cities, high house prices mainly inhibit residents' consumption upgrading through the crowding out effect. Therefore, when formulating real estate policies, it is necessary to comprehensively consider the multiple effects of house prices on residents' consumption behavior in order to achieve balanced economic development and overall social prosperity.

## **3 Descriptive Analysis and Discussion**

### **3.1 The Wealth Effect of Rising Housing Prices**

Housing expenditure occupies a large proportion of China's residents' consumption expenditure, due to the fact that China's residents are affected by the traditional housing ideology

As the residents are deeply influenced by the traditional housing ideology, residents care a lot about housing ownership, and most of them prefer to own housing

assets. Real estate is an important part of the residents' assets, with the changes in housing prices, the residents' real wealth level changes, which in turn affects the residents' consumption behavior. The wealth effect of housing means that rising house prices will increase the value of residents' housing assets, thus promoting residents' consumption. The wealth effect theory reveals that rising house prices increase the value of residents' housing assets, thereby stimulating consumption. This effect is closely related to residents' expected incomes, interest rates and other consumption decision-making factors. Fluctuations in the real estate market affect consumption through several channels, including the direct wealth effect of house price changes on housing asset holders, the liquidity constraint effect, and the budget constraint effect on renters. In addition, the maturity and transactional activity of the real estate market significantly affect the extent to which the wealth effect is realized. The relationship between house prices and consumer behavior, as well as the wealth effect of the real estate market, is an important topic in current macroeconomic research. According to related research, rising house prices have a significant positive wealth effect on residents' consumption. Through the study, it is shown that there is a causal relationship between real estate prices and residents' consumption, and that changes in housing prices have a wealth effect on residents' consumption, whether analyzed in the long or short term. The research on real estate wealth effect also shows different results due to different measurement methods used, different selection of sample data and other factors. Some studies show that the real estate wealth effect plays a role in boosting consumption, while others show that the effect is weak.

In summary, the relationship between house prices and consumer behavior is complex and variable, and the wealth effect of the real estate market will be different in different environments and conditions [7].

### **3.2 Psychological Factors Affecting Consumption**

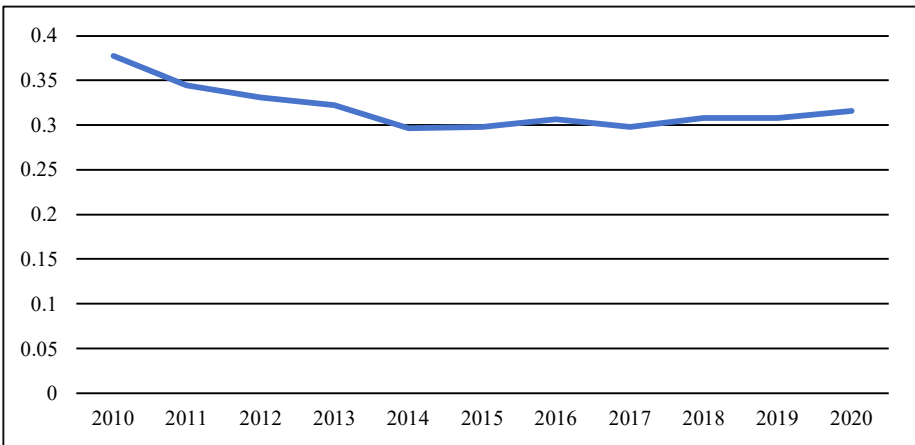
The increase in housing expenditures also affects the psychology of consumer spending. Residents' uncertain expectations of future income, as well as the high cost of loans and routine maintenance that they must bear to keep their existing homes, have reduced consumers' desire and ability to consume. This phenomenon is particularly prominent among young consumers, who are often the main force behind consumption upgrades but have to postpone or give up the pursuit of a higher quality of life due to mortgage pressures.

Psychological factors affecting consumers: Consumers' choices are limited by market prices and consumers' ability to pay, and the limitations on consumers' ability to pay for various commodities at a given price are manifested as a budget constraint. When housing prices rise, homeowners feel that they have become rich, and thus become psychologically happy, and optimism about future prospects makes them increase current consumption, for them rising housing prices bring a positive wealth effect; for renters who have not purchased a home, due to the rise in housing prices pushed up the price of rent, so that their ability to pay a decline in the future they expect that they will have to use more savings in order to meet the rising rent, so can only reduce other commodities, so they can only reduce the price of other goods.

They expect to have to use more savings in the future to meet the rent increase, so they can only reduce the consumption of other goods to "forced savings" to meet their consumption capacity. At this time, the wealth effect of rising house prices is negative for them.

### 3.3 China's House Price to Income Ratio and Its International Comparison

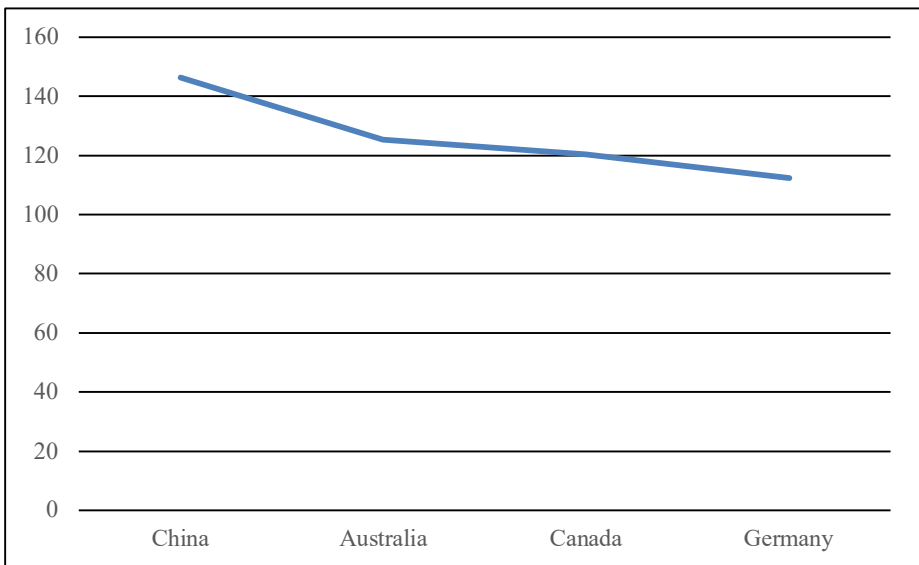
This paper analyzes the trend of China's house price-to-income ratio between 2010 and 2020, which reflects the changes in the housing market and its impact on residents' consumption. As seen in Figure 1, between 2010 and 2020, China's house price-to-income ratio underwent significant changes, falling from 0.38 in 2010 to a low of 0.29 in 2017, and then rising steadily thereafter to 0.32 in 2020. This trend suggests that, although certain adjustments to housing policies led to a decline in the house price-to-income ratio in the early years, in the last few years, the house price-to-income ratio has risen in recent years, suggesting a decline in housing affordability.



**Fig. 1.** Ratio of housing prices to residents' income (Data source: National Bureau of Statistics of China).

As seen in Figure 2, China's house price-to-income ratio is much higher than that of most developed countries when compared with international data. According to a report by the Organization for Economic Cooperation and Development (OECD), using the 2015 house price-to-income ratio as a benchmark, the house price-to-income ratios for Germany, Canada and Australia in 2020 will be 112.5, 120.4 and 125.3, respectively. China's house price-to-income ratio is 146.5, which is still higher than that of most developed countries in comparison, reflecting the particular challenges of the housing market in China's urbanization process. High house price-to-income ratios have a profound impact on consumption patterns. When housing costs take up a larger proportion of household income, residents have less disposable income to spend on other consumption, which may inhibit consumption upgrading, especially on non-essential goods and services. This is particularly evident in China's

first-tier cities, where consumption upgrading among young consumers is particularly affected. High house prices not only limit spending power, but may also change consumer psychology and behavior, thus affecting the structure and dynamics of the overall consumer market. The analysis in this paper shows that the house price-to-income ratio is an important indicator for understanding changes in the housing market and assessing their impact on consumption behavior. China's international comparison reveals the uniqueness of China's housing market and its possible impact on residents' consumption behavior, especially in terms of consumption upgrading. Policymakers should take these factors into account in order to formulate effective housing and economic policies to promote residents' consumption upgrading and healthy economic development.



**Fig. 2.** Ratio of housing prices to resident income in China, Australia, Canada, and Germany in 2020 (Data source: NBS data, OECD).

### 3.4 Manifestation of Consumption Upgrading and Its Influence

Consumption upgrading is particularly evident in China. As residents' incomes grow and living standards improve, more consumers are willing to pay extra for better consumption experiences, higher product quality and more personalized services. Specifically, consumption upgrading is mainly manifested in the following aspects: first, the shift from traditional basic consumption such as food and clothing to non-basic consumption such as electronic products, health products, education and entertainment; second, the shift from focusing on price to focusing on branding and quality; and third, the upgrading from satisfying basic needs to pursuing quality of life and aesthetic experience [8].

However, the significant rise in housing expenditure has had a significant impact on consumption upgrading. High housing prices, especially in China's first-tier cities, have become a major part of residents' expenditures, greatly squeezing the space for other types of consumption. The high real estate market has resulted in residents investing large sums of money for home purchases, limiting their ability to spend in areas such as education, leisure, and health. Studies have shown that high housing expenditures not only reduce residents' disposable income, but also increase the debt burden of households, thus inhibiting consumer spending on non-essential goods and slowing down the process of consumption upgrading [9].

### **3.5 The Crowding-out Effect of Rising Housing Prices**

The crowding-out effect occurs when housing expenditures take up a larger proportion of household income, thereby reducing available funds for other types of expenditures. This effect is particularly pronounced in housing markets where the rapid rise in house prices exceeds income growth. As housing consumption takes up a larger share of the budget, the share of disposable expenditures, especially on enjoyable goods, declines. This suggests that rising housing prices dampen residents' consumption upgrading, yet the effect is different for different types of households.

Against the backdrop of rising housing prices, the dampening effect on consumption upgrading is greatest for households without a home. When housing prices rise, these households expect higher housing costs in the future, and thus will either increase their savings to cope with future demand for a home or purchase a home through debt, which will reduce their consumption expenditure, with everyday necessities becoming their main consumer goods. For households that own a home, rising house prices have a slightly lower dampening effect on their consumption than for households that do not own a home. However, some households cope with the possible increase in housing loan payments, they will also reduce their non-essential consumption, and also daily necessities take up most of their consumption share. For multi-housing households, the effect of rising housing prices on their consumption upgrading is not significant; these households have a stronger financial income capacity and will not be affected by fluctuations in the price of a single housing unit, so their consumption structure will not change much [10].

## **4 Policy Recommendations**

### **4.1 Policy Measures for Stabilizing Housing Market**

The continued rise in housing prices, resulting in people not being able to afford housing, will have a direct impact on the improvement of residents' housing conditions. Many

In order to make up the down payment for housing and to cope with the high mortgage payments they will face afterwards, many residents will reduce their daily consumption expenditure and increase their savings balances.

In order to make the down payment and cope with the high mortgage, many residents will reduce their daily consumption expenditure and increase their savings balance. According to the current situation of China's real estate market, housing prices cannot be fully regulated by the market.

In order to maintain the sustained and stable development of the real estate industry, housing prices should be stabilized in a range compatible with the level of residents' wealth.

In order to maintain the sustained and stable development of the real estate industry, and to control housing prices to stabilize them within the range compatible with the level of residents' wealth, it is necessary for the government to play its due regulatory role. Maintaining stable and reasonable

Housing prices are also an important means of increasing residents' willingness to consume and expanding domestic demand. At the same time, the factors affecting housing price fluctuations in China are many and complex.

Housing price fluctuations in China are many and complex factors, should use a variety of means to curb the rise in housing prices, to be targeted to be resolved in a targeted manner.

#### **4.2 Encouragement of Consumption Upgrading**

Increase the disposable income of residents through tax cuts, raising the minimum wage and optimizing the social welfare system. At the same time, the government can implement measures such as consumption vouchers or direct subsidies to incentivize residents to increase spending in non-basic consumption areas such as education, leisure, culture and entertainment.

## **5 Conclusion**

This paper comprehensively analyzes the impact of rising house prices on residents' consumption upgrading, and explores the different performances of the wealth effect and crowding out effect in different cities and different income levels in China. It is found that although rising house prices can theoretically increase residents' consumption level through the wealth effect, in practice, rising housing prices significantly inhibit residents' development and enjoyment consumption, especially for low- and middle-income cities and homeless families, the inhibiting effect is more significant. Higher housing prices have more of a crowding-out effect, with rising housing prices reducing household spending on non-essential and enjoyable consumer goods and limiting residents' spending power. There are obvious differences in the responses of different types of households to housing price increases. Households without a home experience the greatest disincentive when housing prices rise, followed by households with one home, while households with multiple homes are virtually unaffected by housing price fluctuations due to their greater financial capacity.

Although this study provides insights into how rising house prices affect consumption behavior, there are a number of limitations. First, this study relies heavily on



historical data and existing literature and fails to include new developments in the Chinese real estate market in recent years. Second, the analysis in this paper focuses on urban residents and fails to adequately consider the situation in rural areas or small towns, where house price dynamics and consumption behavior may differ from those in large cities.

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