

Housing Bubbles and Support for Incumbents

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For many individuals, their most important economic asset is their home. The value of housing is thus a core element of an individual's permanent income. As a consequence, we would expect individuals to be attuned to how government policy affects the price of housing, and to vote accordingly. At the same time, extracting credible signals about the effects of government policy is difficult. Voters are thus faced with the challenge of making accurate inferences about government policy. In this paper we suggest that one way they do so is by taking cues from changes in housing prices in their local area.

The theoretical underpinning of this prediction comes from the theory of economic voting, which suggests that people use economic shocks to make inferences about the priorities and characteristics of governing politicians. In particular, voters may hold government accountable for changes in local house prices because they infer from these changes that the economic policy of the government is favorable to themselves (an egotropic motive), their local community (a geotropic motive) or to the economy as a whole (a sociotropic motive).

As empirical context, we focus on one country, Denmark, where government monetary and tax policies contributed to creating unusually high volatility in housing prices over the past decade, both by historical and cross-national standards. The burst of Denmark's housing bubble thus constitutes a well-suited case for examining the impact of policy-induced housing bubbles.

We ask if local differences in this partly policy-driven expansion and contraction of real estate prices shaped support for governing parties. Specifically, we test whether voters responded to short-term changes in local housing price by rewarding and punishing politicians when prices increase or decrease. We do so using two complementary empirical approaches. First, we link detailed registry data on local housing prices to election results at the precinct level across five national elections, allowing us to study whether *within-district* differences in housing prices are related to differences in voter support for the incumbent.

Second, to test the hypothesized causal mechanism, that voters are able to make inferences about government based on the state of their local housing market, we zoom in on individual voters' local contexts. Specifically, we link survey data from 2002 to 2016 (cross-sectional and panel) to uniquely detailed data from the Danish administrative registries, which allow for precise measures of how individuals' neighborhoods--measured at very low levels of aggregation--were affected by the housing bubble. This enables us to examine if neighborhood housing price changes are related to perceptions of national economic conditions (and support for incumbents).

The paper advances the empirical study of the political effects of local economic shocks in several ways. First, as one of the first studies, we highlight and theorize the relevance of housing price changes to political behavior. Second, unlike previous studies, we measure local economic conditions (in the shape of housing prices) at a very disaggregate geographical level. Third, whereas previous studies have tended to rely on sample-based measures of local economic conditions, we rely on population-based measures, i.e. measures based on all housing sales in the economy. Fourth, using panel data on both voters and precincts, we are--unlike the majority of studies in the extant literature--able to take stable differences between individuals and local contexts into account, and thus increase causal leverage.

Preliminary results suggest that voters do in fact factor in local housing price changes when deciding whether to vote for the incumbent government. These findings shed new light on how voters react to economic shocks in the local context, and in turn the incentives reelection-minded politicians face when dealing with housing bubbles. Since voters appear to react to changes in the local economy, the findings suggest that reelection-minded politicians should design policies with a view not just to the economy as a whole, but also to the geographic distribution of economic grievances.