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Home renovation and search frictions in the housing market

Yeonjoo Son¹¹University of California, Riverside, USA

ABSTRACT

This paper develops a search and matching model of the housing market with search frictions and home renovation to examine the impact of renovation on market outcomes. The model shows that increased home renovation is positively correlated with prices, vacancies, and sales, but negatively correlated with time-to-sell. To capture these market dynamics, I construct a search and matching model with key features such as renovation channels, heterogeneous houses, match-specific utility, and free entry. A key aspect of renovation is that it increases the intrinsic value of a house. To reflect this characteristic, I introduce two renovation channels: customization, which enhances homeowners' utility, and resale, which raises the sale price. The model matches stylized facts both quantitatively and qualitatively through numerical exercises. The results highlight that while renovation strengthens market competitiveness by shortening time-to-sell and increasing sales, its effect on price is relatively weak. These findings offer insights into market dynamics and the role of renovation in market tightness and volatility.

KEYWORDS Housing market; Search and Matching; Renovation

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