

The Anatomy of the Transmission of Macroprudential Policies

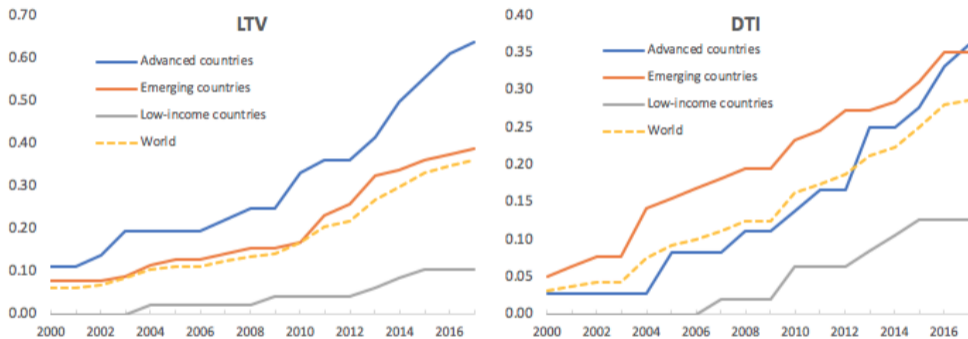
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Discussion by

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Context: Use of “Macroprudential” Policies is Rising Across Countries



Source: Cerutti et al. (2018)

Evidence on the efficacy of these policies is limited

What This Paper Does

Question: How did the introduction of LTV/LTI limits in Ireland in 2015 affect

- **Credit allocation?**
 - Aggregate mortgage issuance unchanged
 - Reallocation from low-income → high-income borrowers
 - Reallocation from high-LTV/LTI counties → low-LTV/LTI counties
- **House prices?**
 - House price growth slows most in most affected counties
- **Bank portfolios?**
 - More affected banks tilt portfolios toward higher-yield securities
 - More affected banks increase lending to risky firms

What this Paper Contributes

Micro-level empirical evidence on transmission channels and efficacy of macropru

- Theoretical benefits and tradeoffs are clear
[e.g. Dávila & Korinek (2017), Korinek & Simsek (2016), Farhi & Werning (2016)]
- Cross-country empirical evidence is mixed and hard to interpret
[e.g. Cerutti et al. (2015)]
- Micro-level evidence exists, but there is much still to be learned
[e.g. DeFusco et al. (2019), Van Bakkum et al. (2019)]
- This paper's results fill an important gap!

Main Focus of My Comments

Question: How did the introduction of LTV/LTI limits in Ireland in 2015 affect

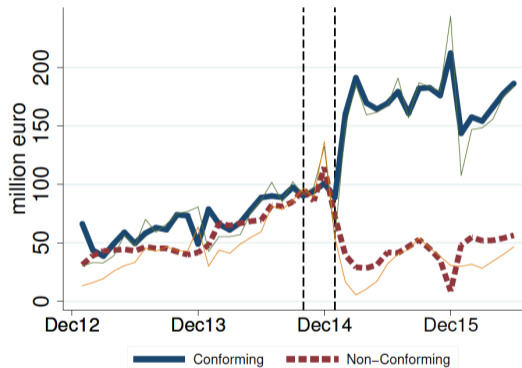
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Aggregate Mortgage Issuance Largely Unaffected by the Policy

Total Mortgage Issuance

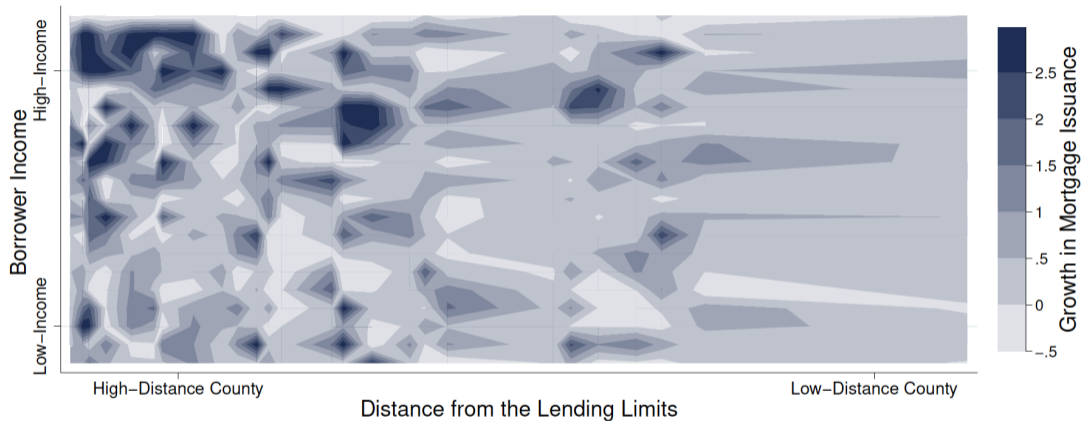


Conforming/Non-Conforming Issuance



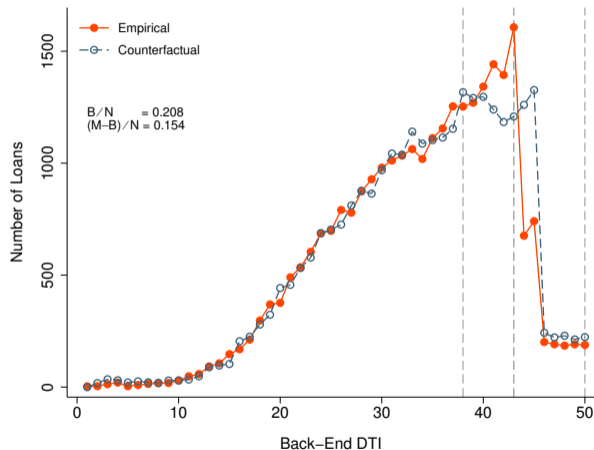
“[T]he increase in ‘conforming’ issuance offsets the collapse in the issuance of those mortgages that exceed the newly imposed limits, leaving aggregate issuance barely affected.”

Instead, Lenders Simply Reallocated Credit From Poor to Rich



“Mortgage credit is reallocated from low- to high-income borrowers and from counties where borrowers are close to the lending limits to counties where borrowers are more distant...”

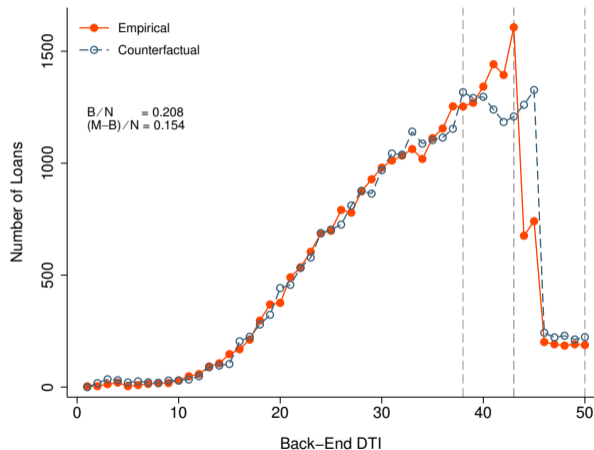
Very Different From How Lenders Responded to a Similar U.S. Policy...



Source: DeFusco et al. (2019)

- We study Dodd-Frank 43% DTI limit
- More than 1/3 of change in lending volume was on the *extensive* margin

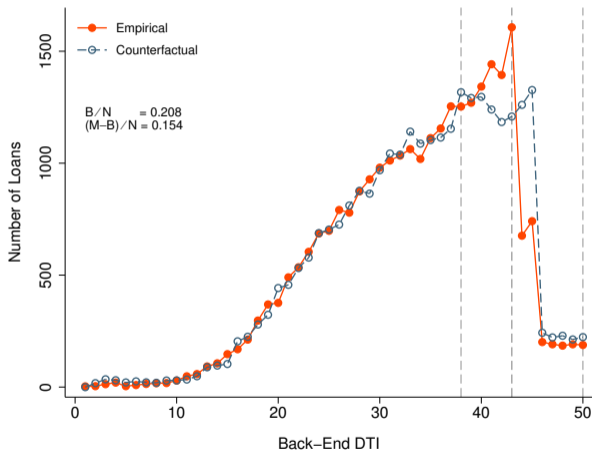
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- Why are results so different and what does this say about external validity?

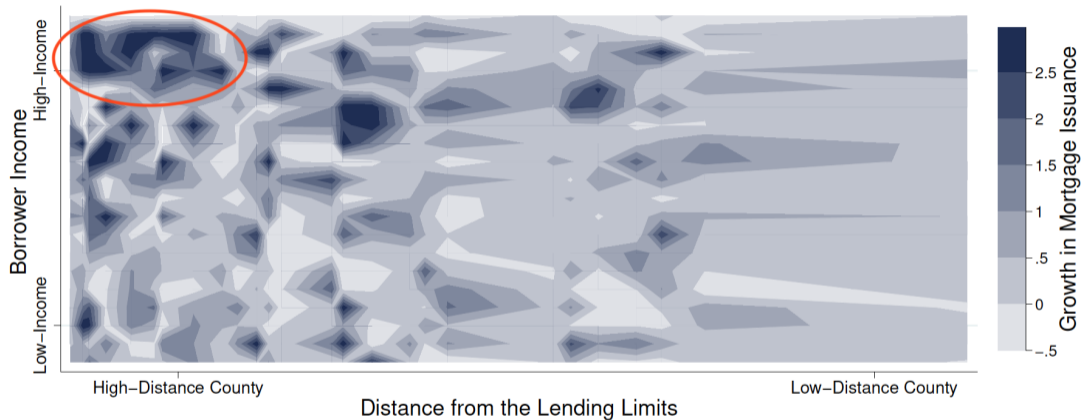
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- We study Dodd-Frank 43% DTI limit
- More than 1/3 of change in lending volume was on the *extensive* margin
- Why are results so different and what does this say about external validity?
- I think the answer lies in the specifics of Irish mortgage market institutions...

Instead, Lenders Simply Reallocated Credit From Poor to Rich



To make sense of the reallocation result, we need to understand why so many rich borrowers were NOT getting mortgages prior to the policy change

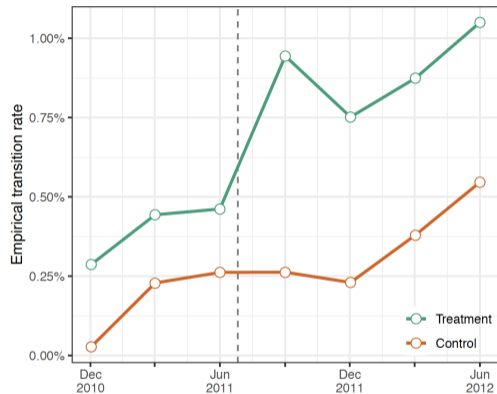
One Possible Explanation

“[B]anks suffered large losses exactly from high-income borrowers during the 2008-10 bust and therefore might have been reluctant to increase credit to these borrowers when the housing market started to pick up again.”

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- Consistent with O'Malley's finding of widespread strategic default in Ireland
- Strategic defaulters more financially sophisticated/higher-income on average

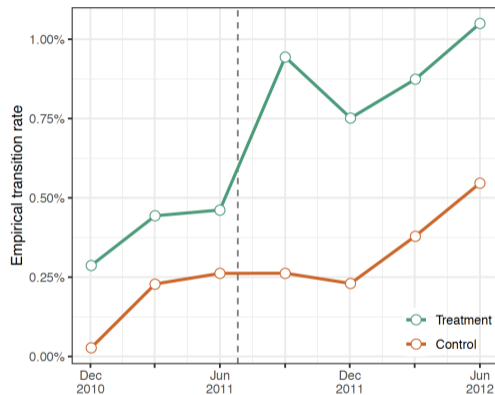


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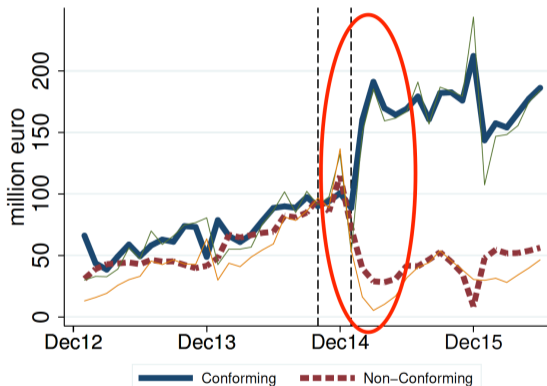
- Consistent with O'Malley's finding of widespread strategic default in Ireland
- Strategic defaulters more financially sophisticated/higher-income on average
- But strategic default much less common outside of Ireland (Ganong & Noel, 2019)



Source: O'Malley (2019)

This Can't Be the Entire Story Though

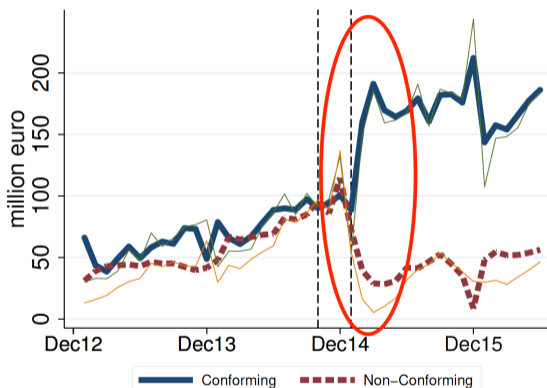
- If rich borrowers unprofitable on 2/7/15, then they're also unprofitable on 2/8/15
- What stopped banks from making these (slightly less) profitable loans before?



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- If rich borrowers unprofitable on 2/7/15, then they're also unprofitable on 2/8/15
- What stopped banks from making these (slightly less) profitable loans before?
- I think the culprit lies in footnote 8

“Almost all mortgages in Ireland are held on banks’ balance sheets. No active securitization market exists”
- Not the case in other contexts



Bottom Line

- It is not clear how far the reallocation results generalize outside of Ireland in 2015
 - Lack of secondary market → bank funding is constrained
 - Strategic default in Ireland → high-income borrowers less safe than elsewhere
 - Market structure: > 90% of lending by 5 banks (didn't mention, but likely important)
- This is not a problem, we still learn a ton about this policy!
- **Recommendation:** embrace these issues, turn “weakness” into strength
 - Move from
“The Anatomy of the Transmission of Macroprudential Policies”
 - Toward
“Market Friction X and the Transmission of Macroprudential Policy: Evidence from Ireland”
- More great empirical work like this on macroprudential policy is needed