Comments on the Use and Effectiveness of Macroprudential Policies

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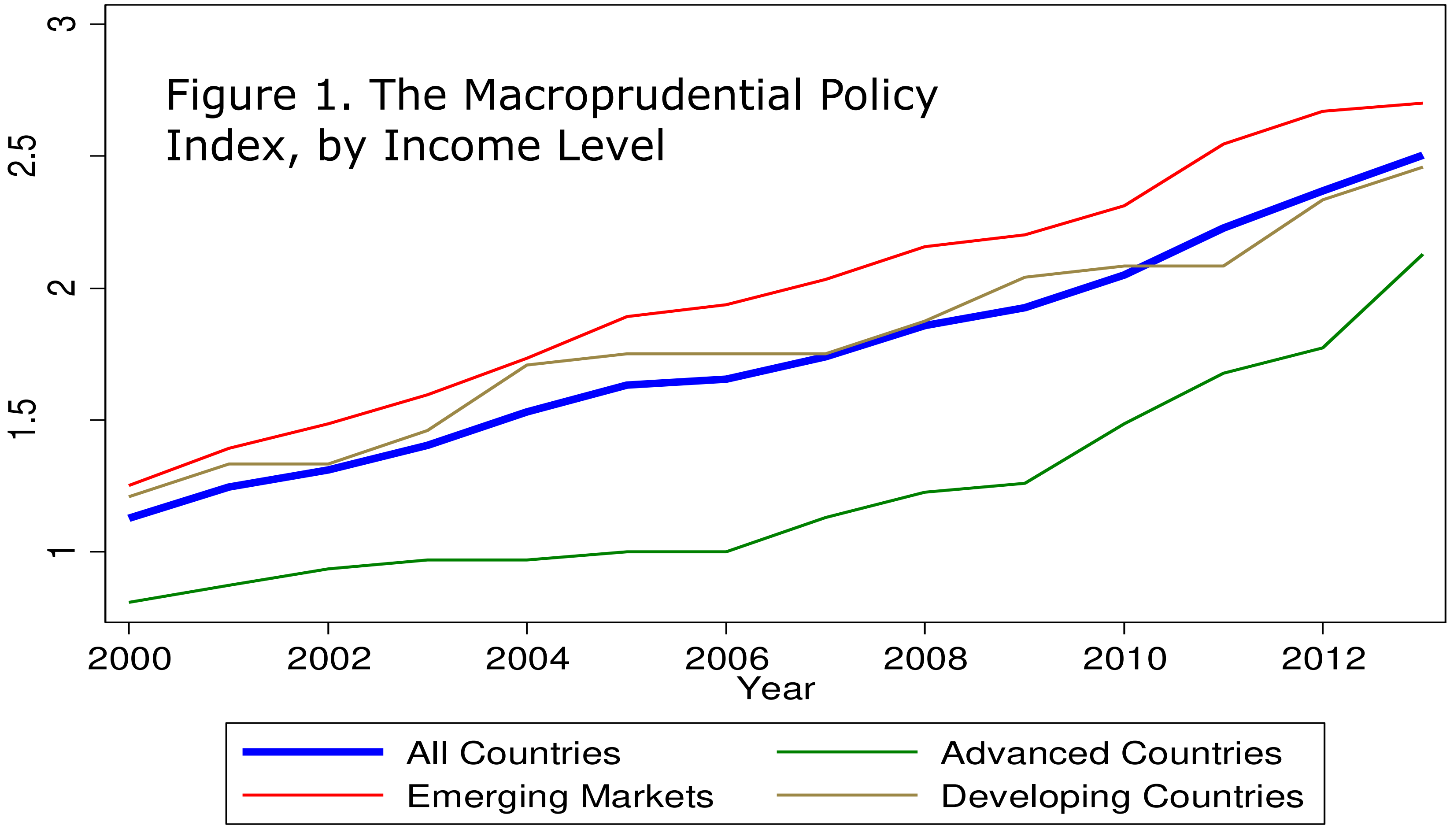
Governance issues: An inaction bias?

- Outsourcing monetary policy to independent CBs was “easy”
  - A clear and measurable objective: low and stable inflation (sometimes with some attention to short-term output)
  - A clearly understood (almost mono-dimensional tool): the policy rate
  - Accountability led to properly designed incentives for central bankers

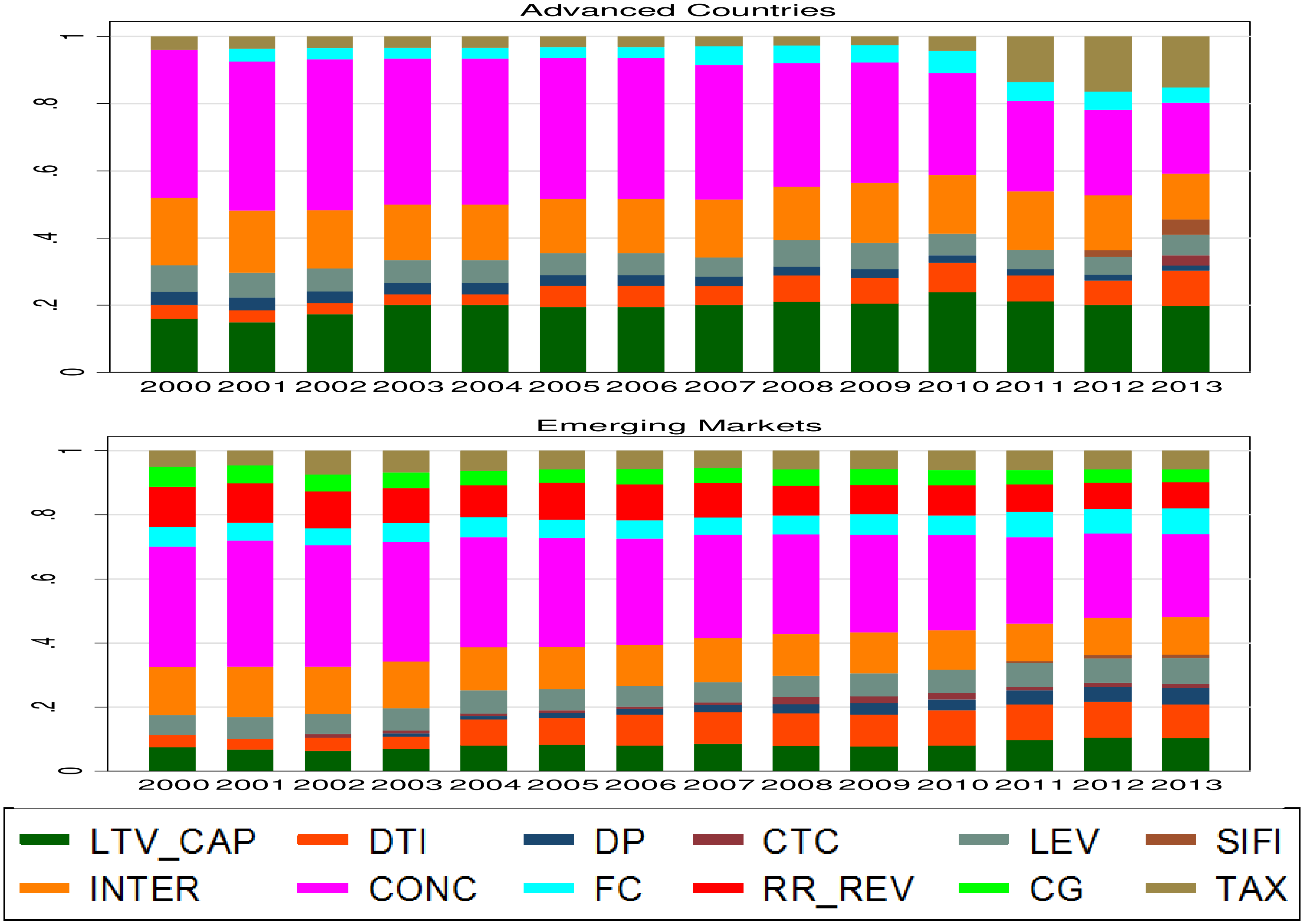
- But financial stability much more complicated
  - Is there as a too stable banking system?
  - Multiple objectives, difficult to measure
  - Nobody sees the crises that do not happen
  - Accountability complicated, potential for poor incentives
  - Systemic nature makes problem worse than for MiP (no yardstick)

Increasing use of MAPs

(% of country-year observations using any instrument)

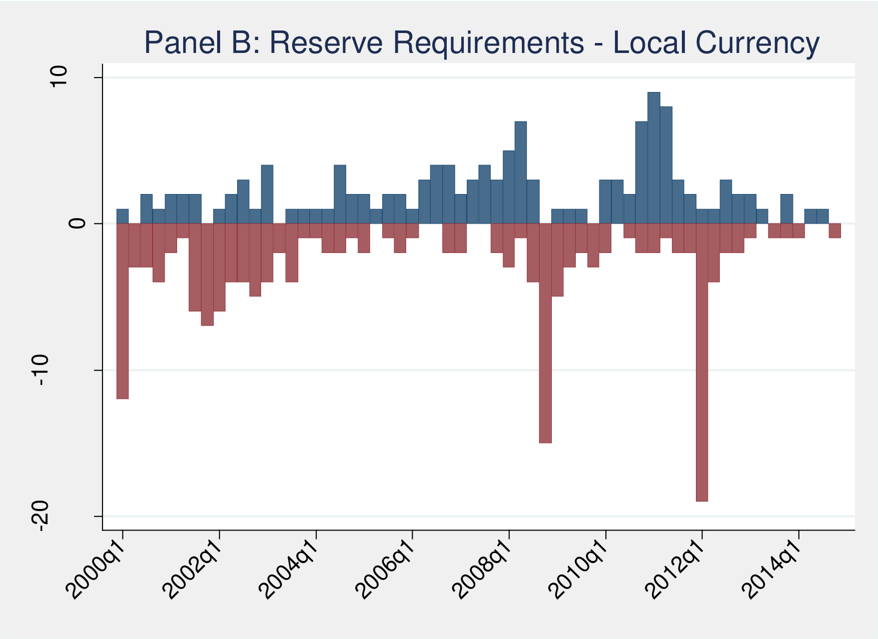


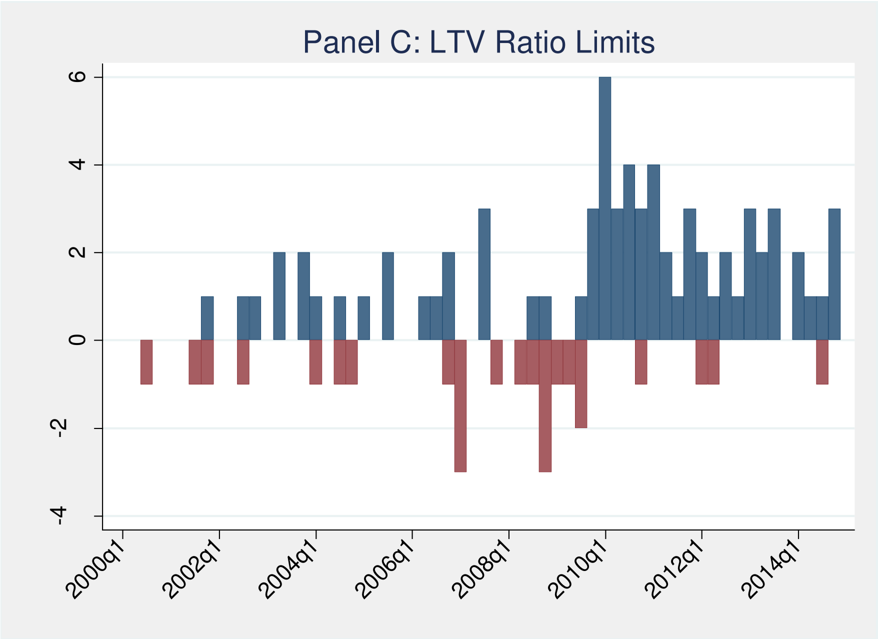
ACs Use More Borrower-based
EMs Use Broad Set of MAPs



Cyclical Use of Policies

- RR loosening coincided with GFC and the European sovereign debt crisis
- LTV tightened often after GFC (counter acting loose monetary policies in several countries)

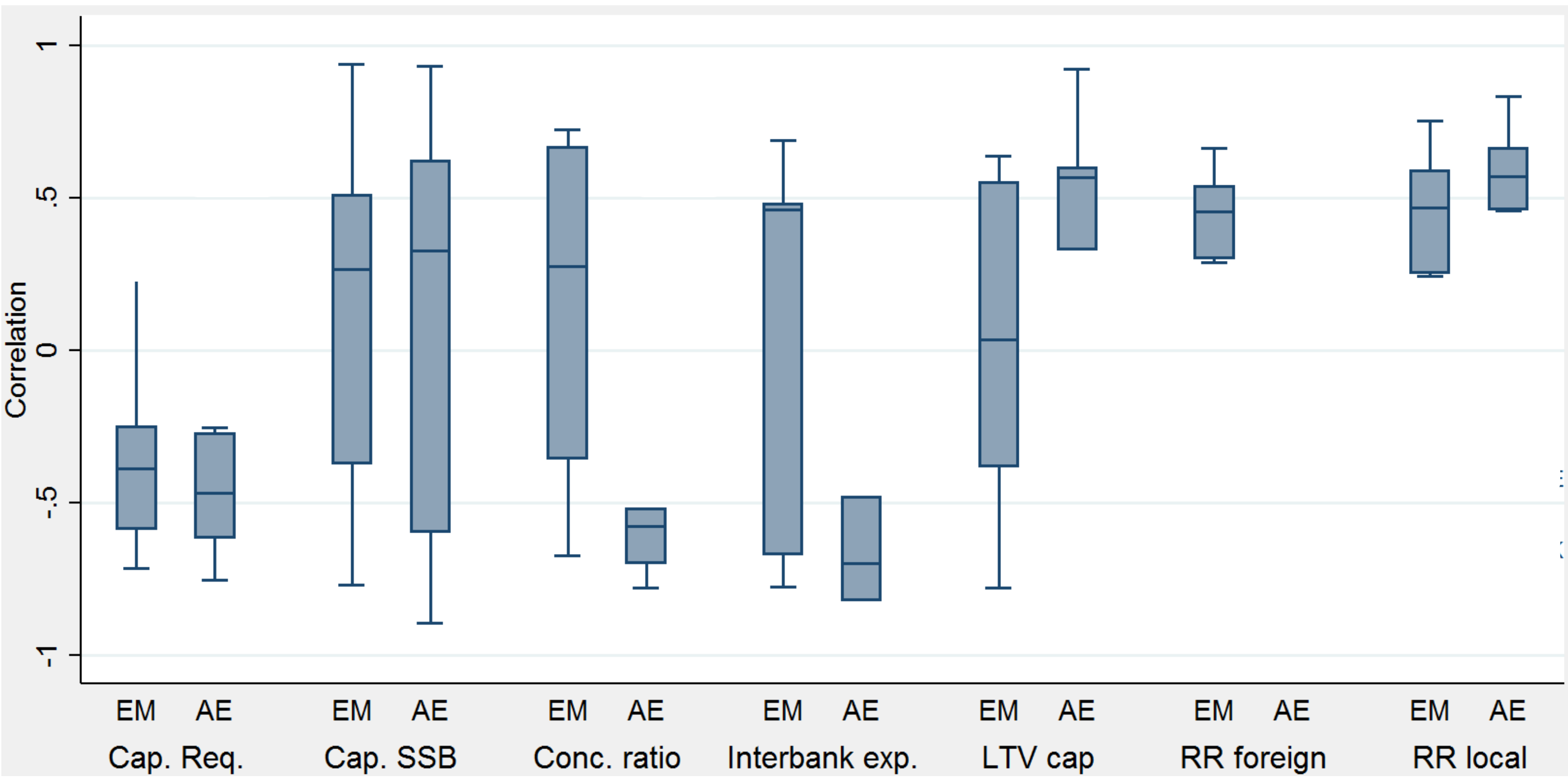




Source: Cerutti, Correa, Fiorentino, and Segalla (2017)

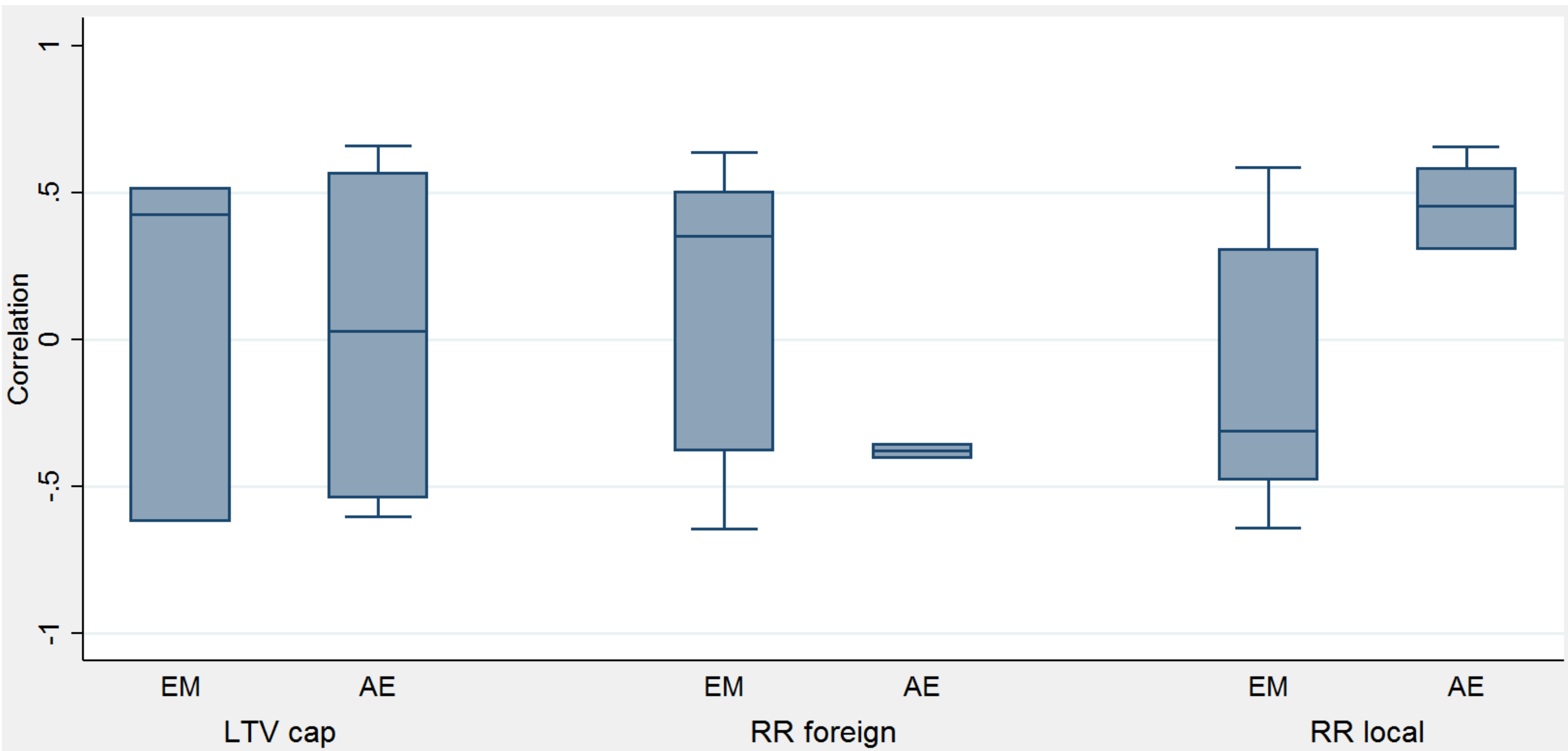
Usage relative to credit growth ?

- Cap. SSB, CONC, INTER: not many statistically significant correlations and broadly distributed
- LTV and RR show more counter-cyclical usage



Use relative to monetary policy?

- LTV used with higher policy rates in some AEs, but also to tighten while lowering policy rates (e.g., Canada, Hong Kong)
- RR (Local) used more to (partially) offset policy rate changes, but there is general heterogeneity



Challenges when looking at effectiveness

- Limited use of Macroprudential measures
  - Recourse to indexes, but…
- Heterogeneity within and across countries
- Endogeneity
  - Negative bias on effectiveness coefficients
- Simultaneous use of multiple policy tools
  - Need GE approach
  - But calibration remains a challenge

Economic effects are meaningful, but vary in magnitude

- Based on existing literature:
  - Cross-country/cross-measure heterogeneity
  - Macroprudential can slow credit growth down
  - But more effective in building buffers
  - Less clear effects on real estate prices (but perhaps less important)

- Effects over time?
  - Circumvention likely to increase
  - Cat-and-mouse game
  - Compare to capital flow measures

Conclusions

- Evidence of increase use of macroprudential policies
  - At times in sync at others opposite to MP
- Evidence of effectiveness
  - Especially on credit (overall and HH credit)
  - But differentiate by country and individual MAPs
  - Need to be pragmatic, a times discretionary within frameworks, targeted at specific markets/objectives
  - Ensuring resilience can reinforce avoiding booms/busts
- But overall, MAP still at early stage
  - Interactions with other policies. Adaptations. Costs. Political economy concerns. Rules vs. discretion.

  $\Rightarrow$ More data, research on effects, risks, calibrations, etc.

Data for this presentation

- Country coverage: (31 AEs, 64 EMs, and 24 LICs)/2000-2013 (annual data)
- Binary measures:

  -Loan-to-Value Cap (LTV)
  -Debt-to-Income Ratio (DTI)
  -Time-Varying/Dynamic Loan-Loss Provisioning (DP)
  -Counter-Cyclical Requirements (CTC)
  -Leverage Ratio (LEV)
  -Capital Surcharges on SIFIs (SIFI)
  -Limits on Interbank Exposures (INTER)
  -Concentration Limits (CONC)
  -Limits on Foreign Lending (FC)
  -Reserve Requirements (RR)
  -Credit Growth Caps (CG)
  -Levy/Tax on Financial institutions (TAX)

- Sources: Cerutti, Claessens, Laeven (JFS 2015); Source: Cerutti, Correa, Fiorentino, and Segalla (2017); Rabanal (2017)