



# Real Estate Booms and Busts: Implications for Monetary and Macroprudential Policy in Europe

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# Summary

- Great paper
- Main messages:
  - Complex role of real estate in MP transmission
  - Our understanding has improved, but much more is needed
  - Local institutions/culture/contract-structure matter
  - Leaning against the wind? Difficult. Especially in multi-country setting
  - Central role for macroprudential policies



# Seven elements of MP transmission



1. MP stance → Lending (mortgage) rates
2. → Real estate prices
3. → Residential investment
4. → Consumer spending
5. → Mortgage debt
6. → Non-price credit conditions
7. → Inflation (rents)

# Seven elements of MP transmission



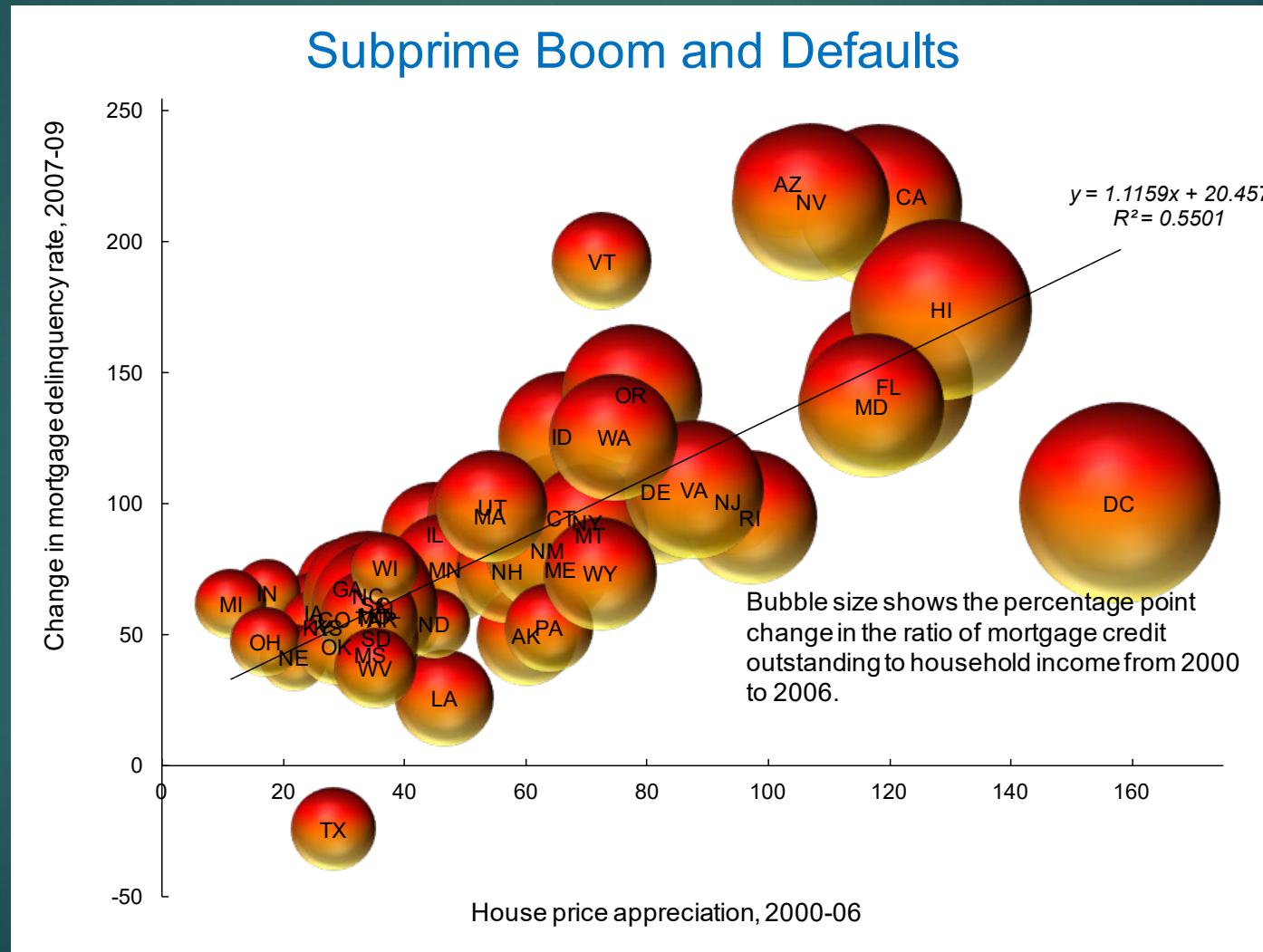
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# House prices and financial stability

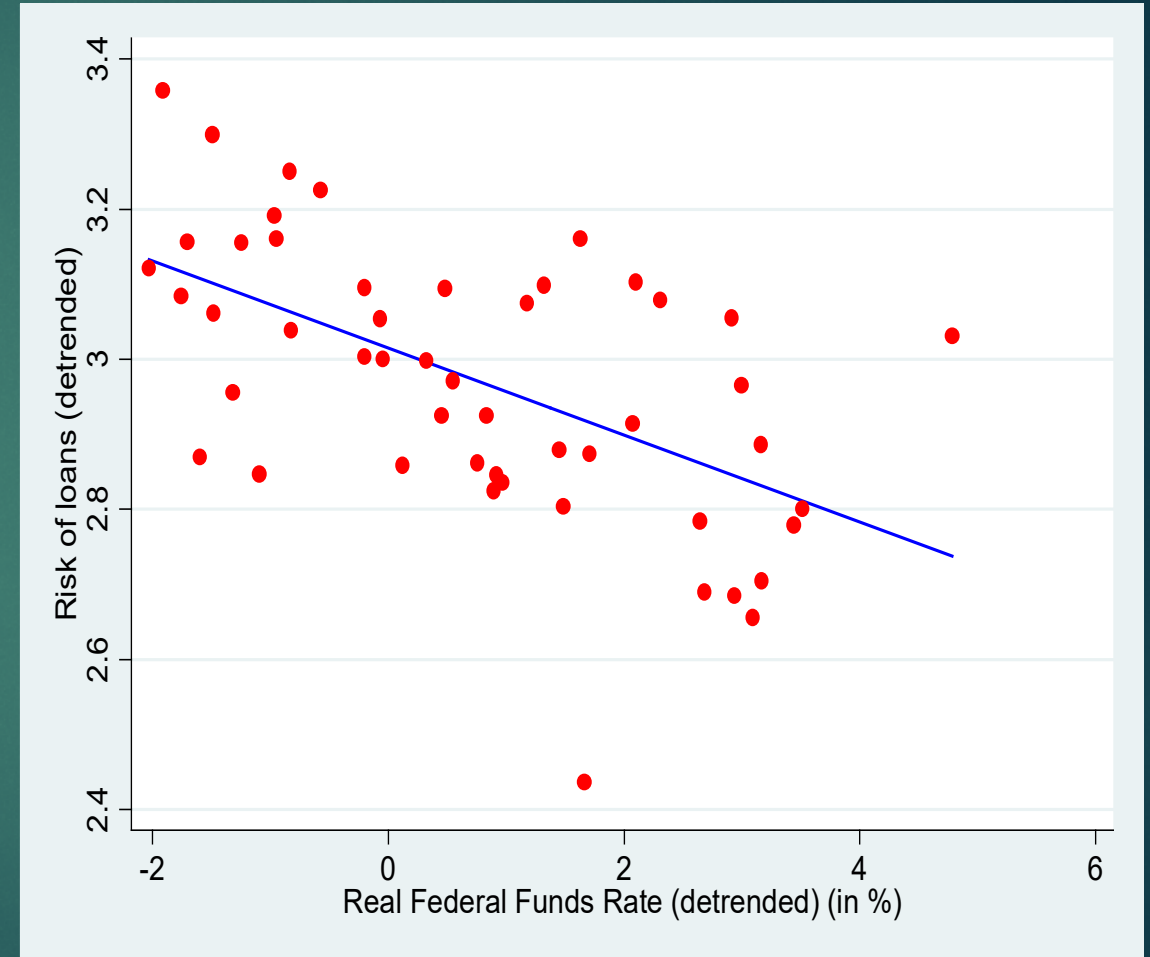
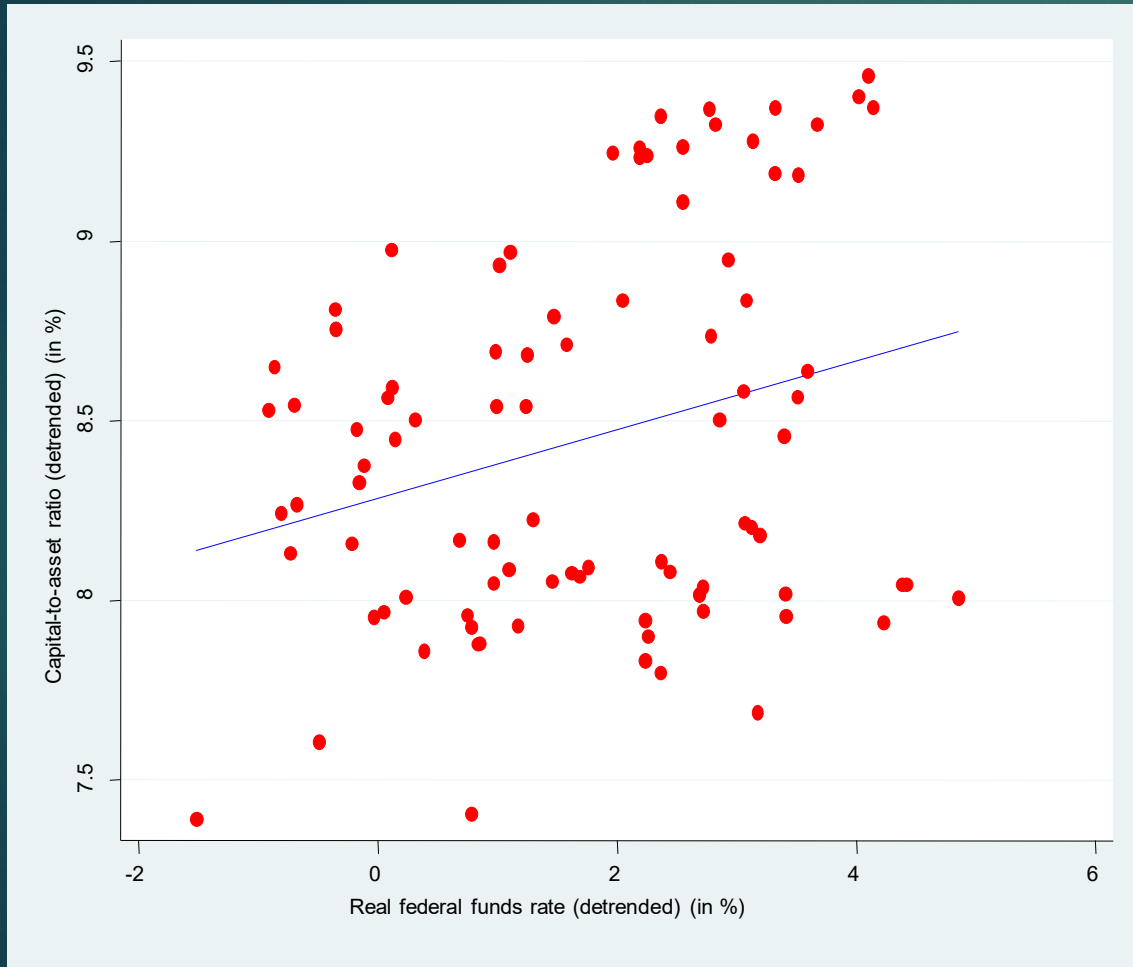


- House-price booms/busts often associated with financial crises
- But leverage and credit quality are what really matters
  - Household debt (Mian/Sufi/Verner 2017), (Cerutti et al. 2017)
  - Lending standards Jimenez et al. (2014), (Dell’Ariccia/Laeven/Suarez, 2017)
- Special role for construction sector (Dell’Ariccia/Ebrahimy/Igan/Puy 2020)
- Policy implications:
  - MP: LAW?
  - Macroprudential tools

# GFC: Crisis severity in line with magnitude of credit booms

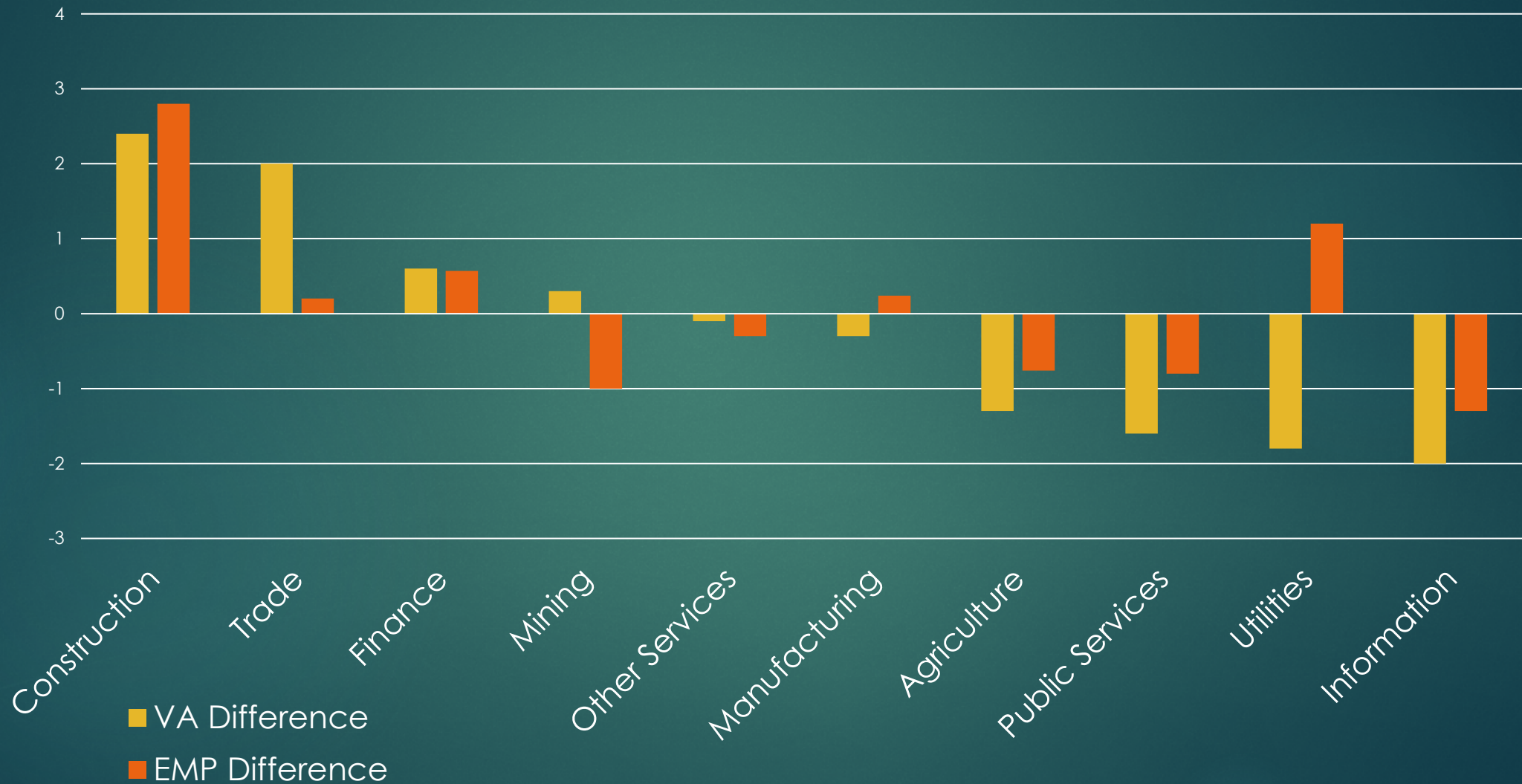


# Policy rate and risk taking, evidence from the US



Source: Dell'Ariccia, Laeven, Suarez, JF 2017

# Difference in VA and Employment between "Good" and "Bad" Credit booms





# Local institutions matter for transmission mechanism and financial stability

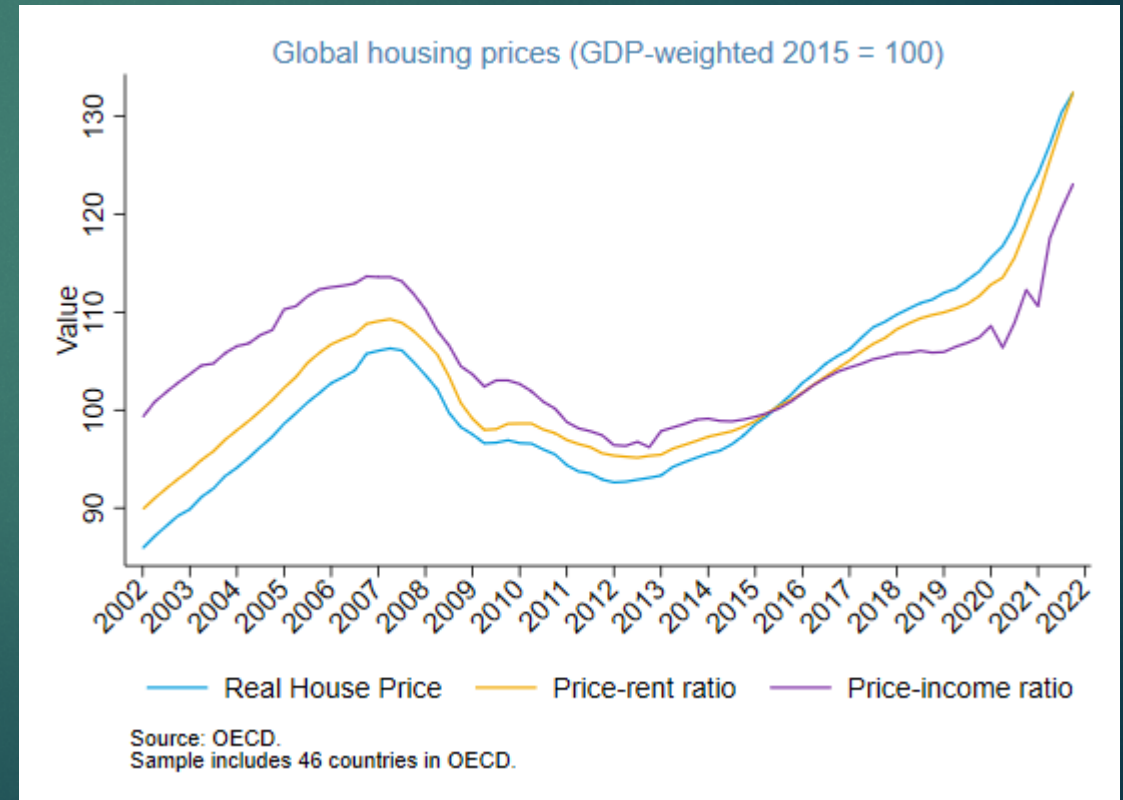
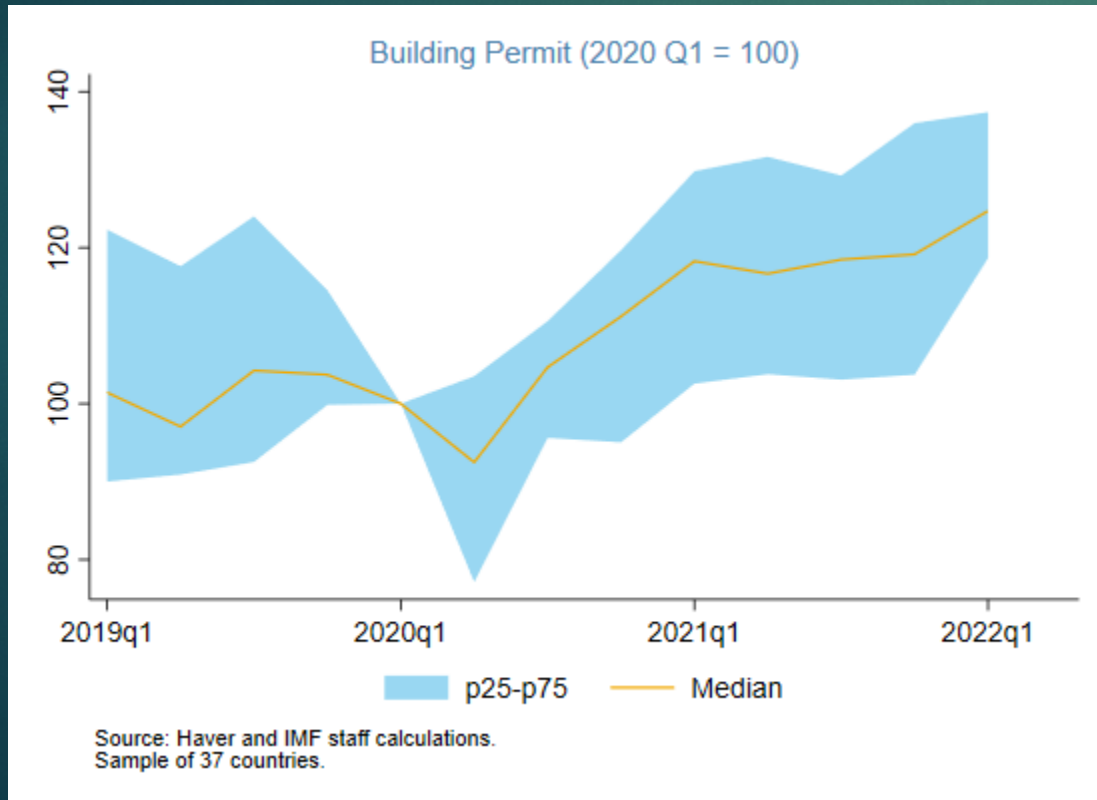


- Mortgage leverage ratios / Household indebtedness
- Contractual details
  - Fixed vs variable rates
  - Portability
- Bank capitalization / NPLs / Securitization
- Land scarcity / Building regulations
- Path dependency: Credit/Construction/House-price booms

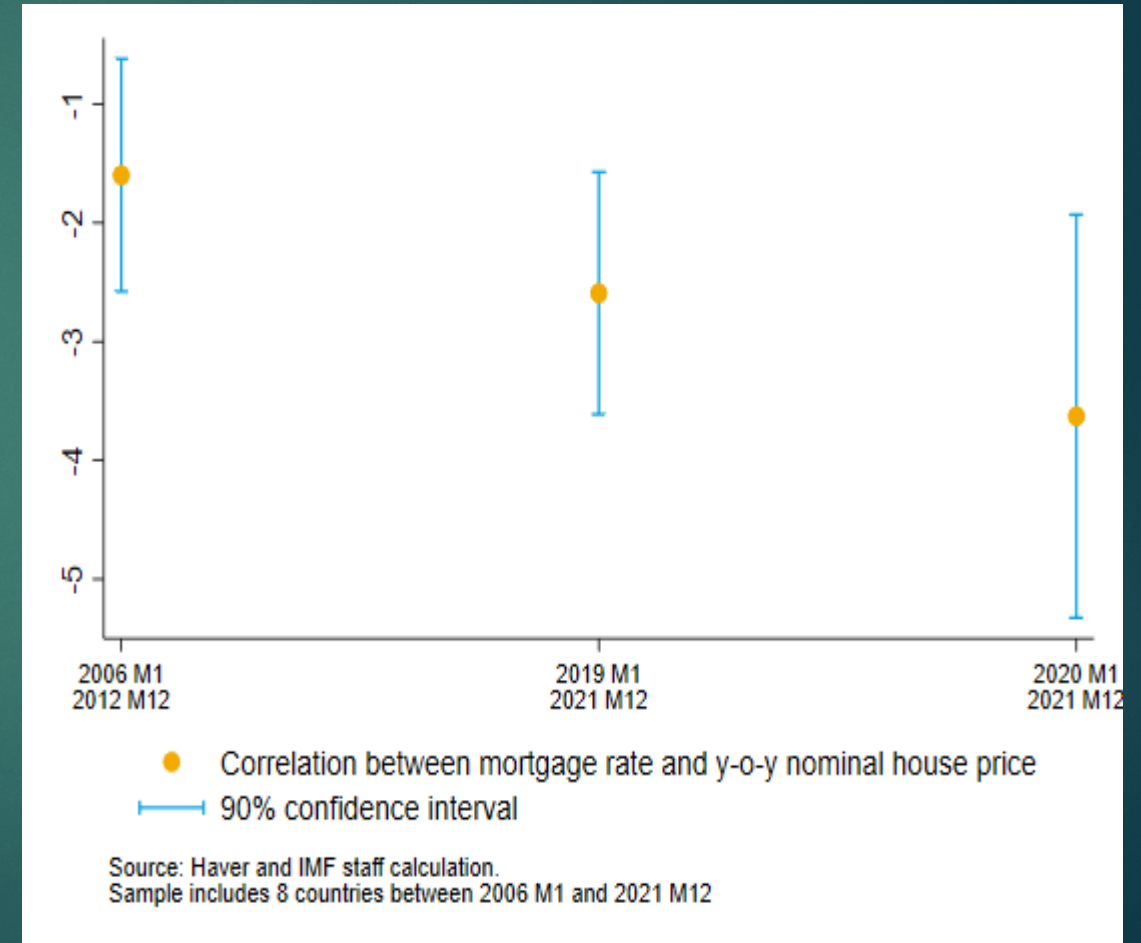
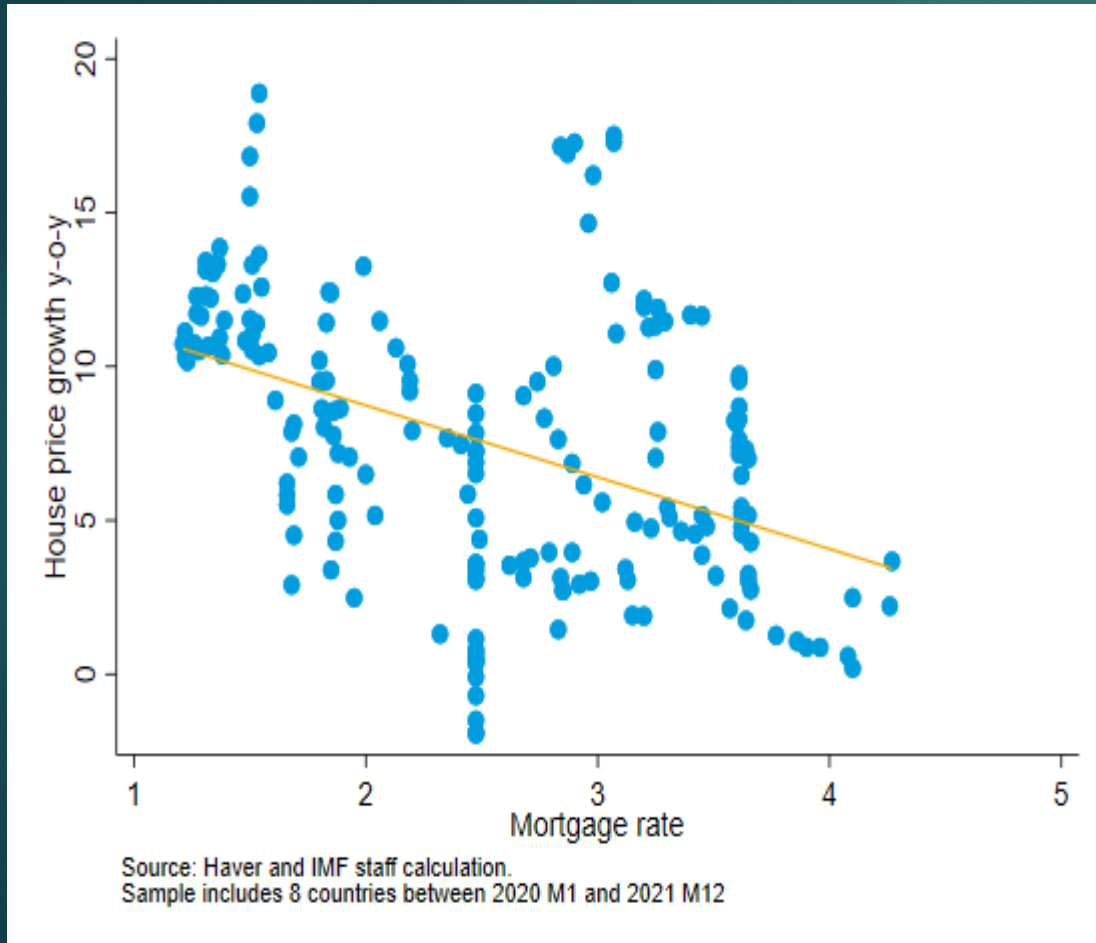
# Residential real estate markets have been trending up

- Building activity increased after lockdown period

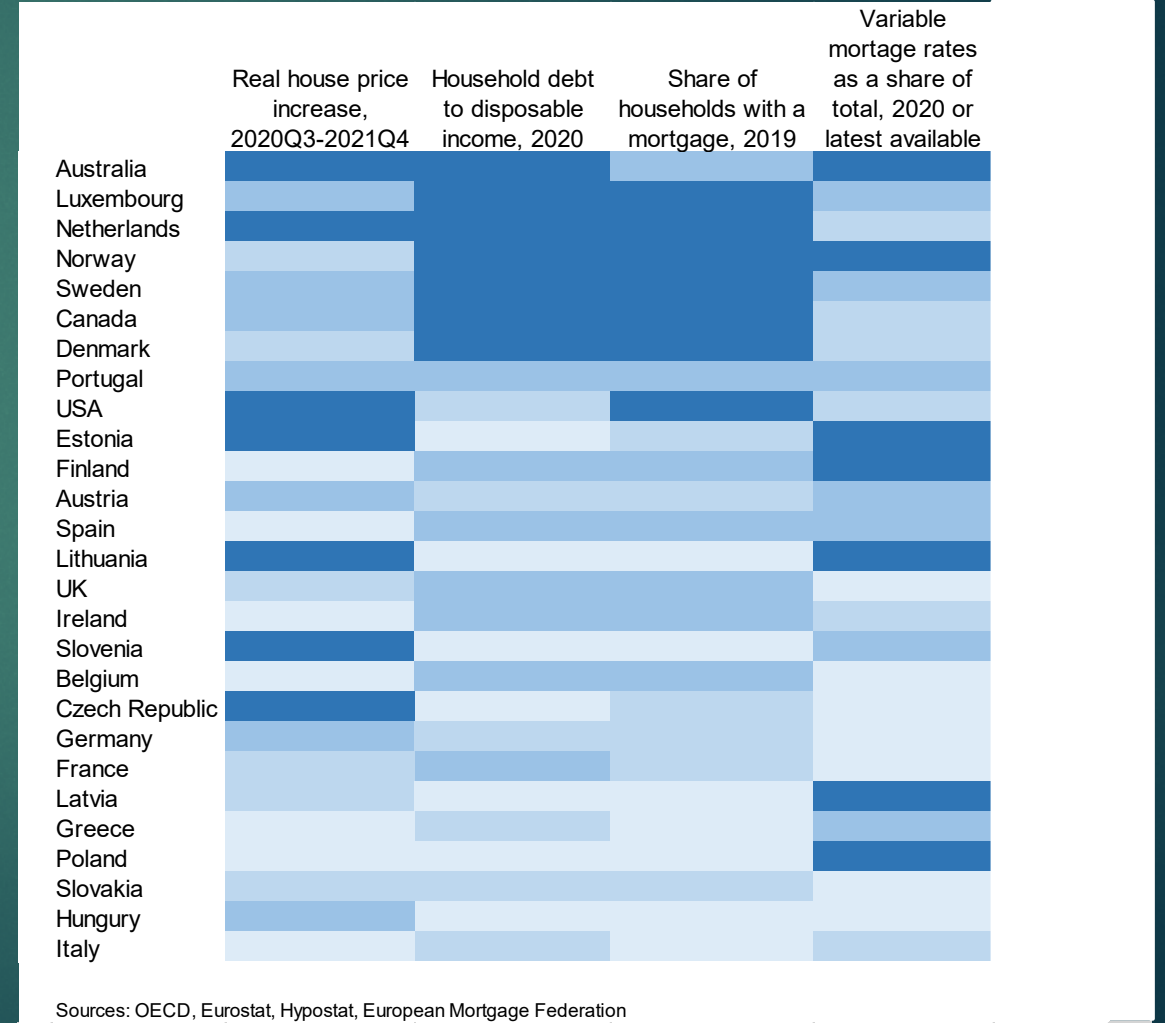
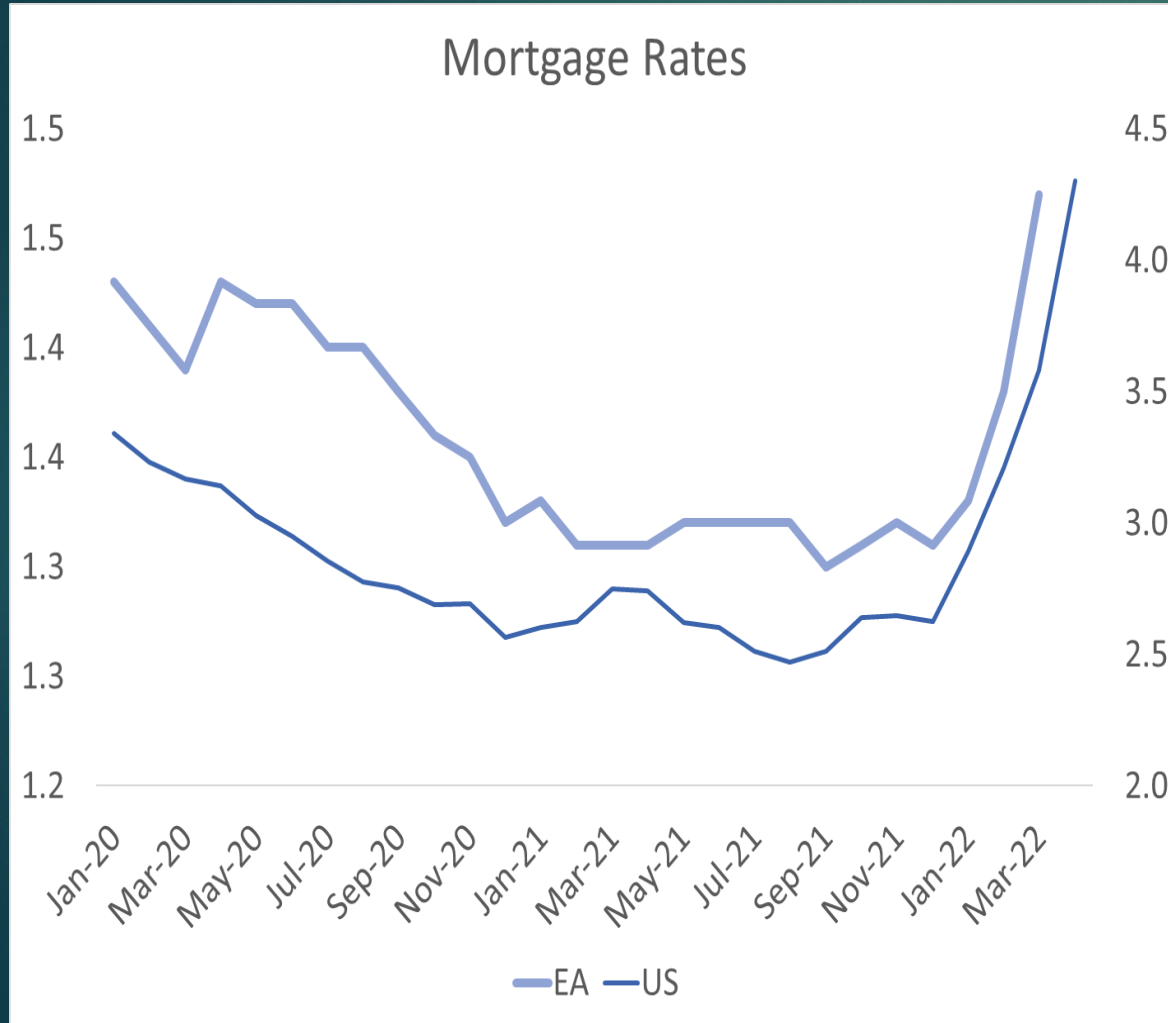
- Rapid increase in prices outpaced rents



# Mortgage rates an important factor in recent price increases



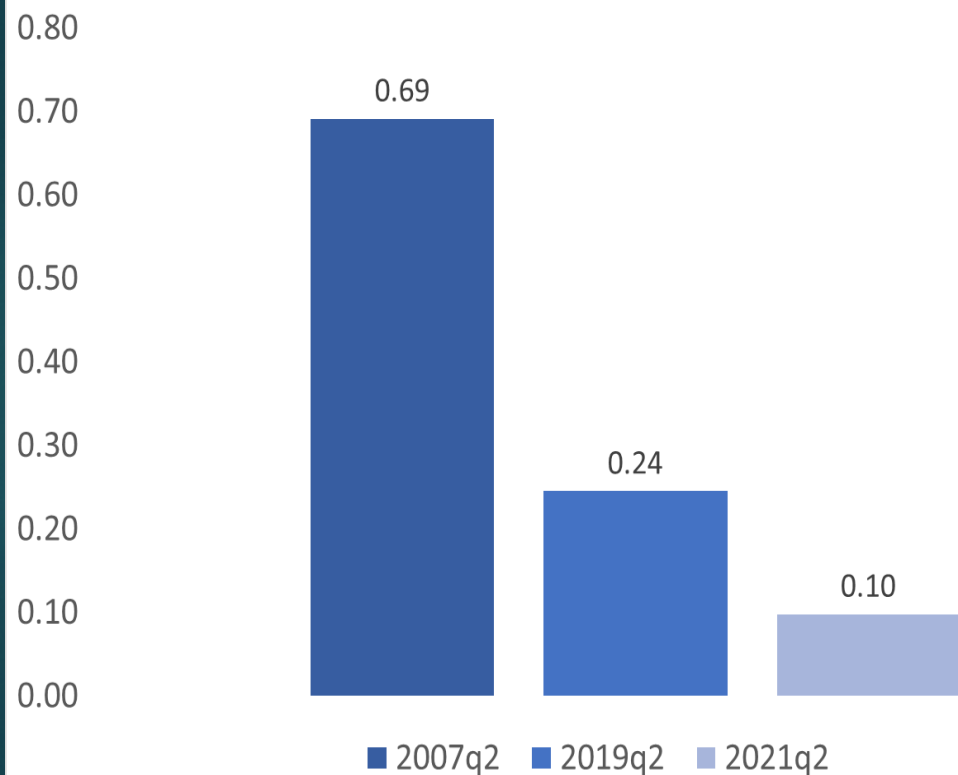
# Factors contributing to sensitivity of house prices to policy rates



# Twin boom in credit and house prices?

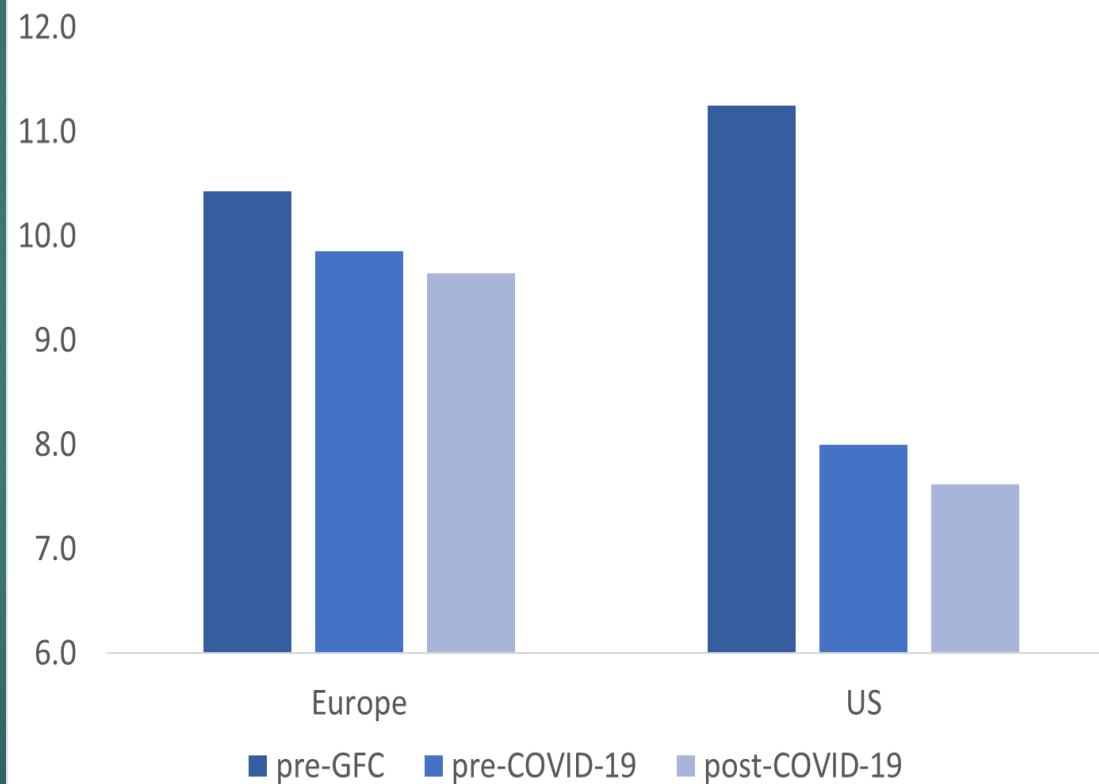


Correlation: Real house price growth and HH debt to GDP growth over time



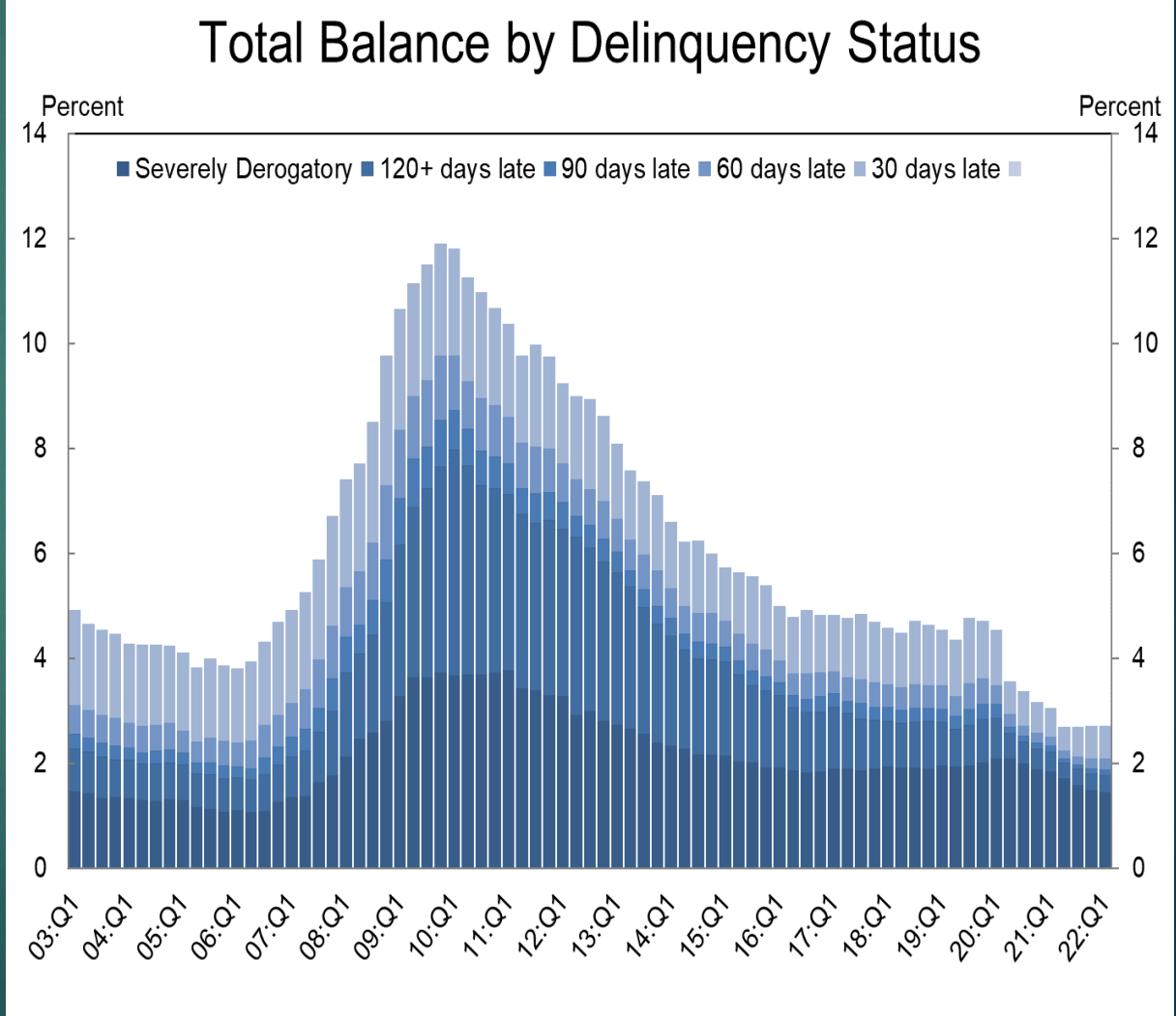
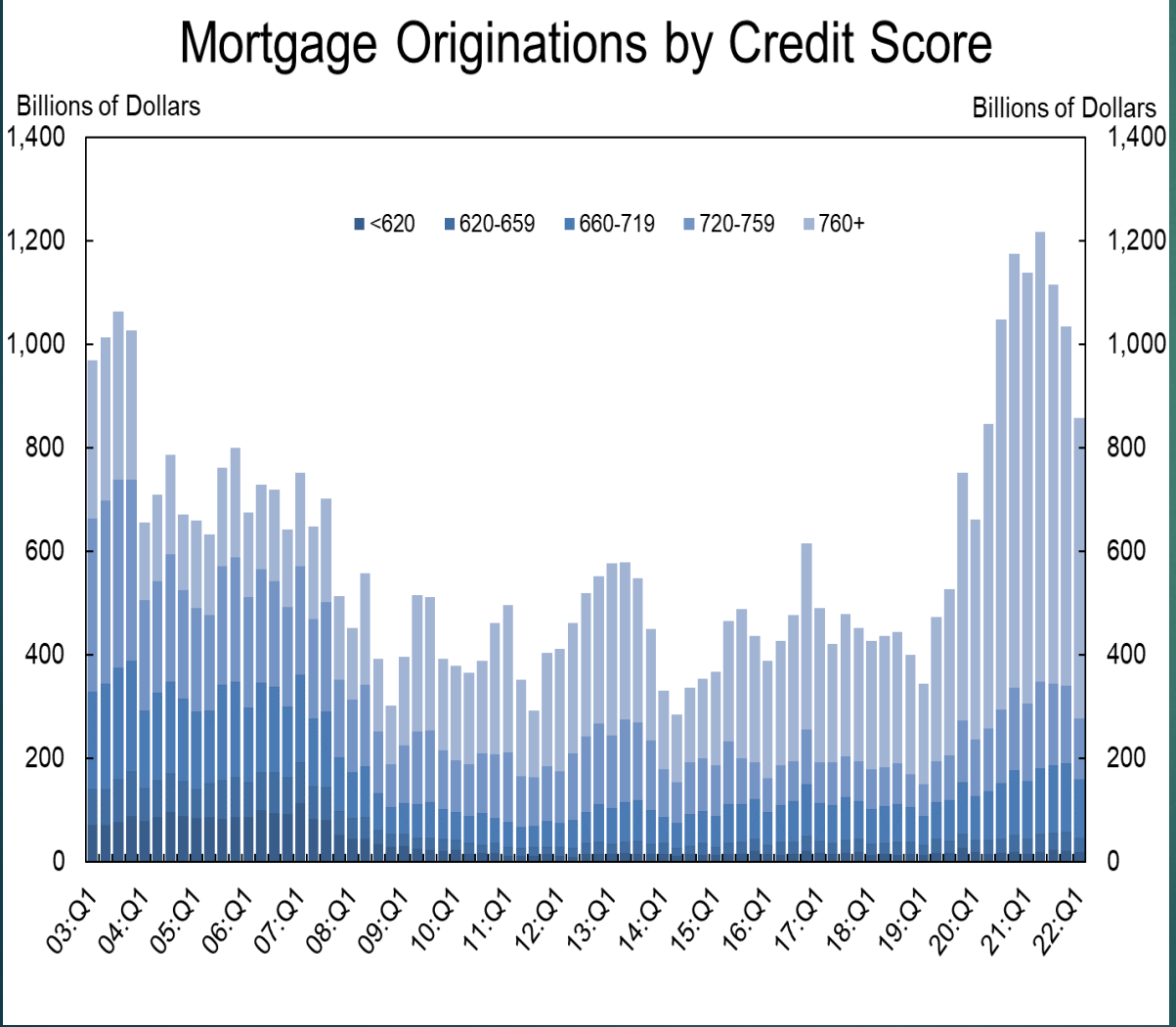
Sources: BIS, staff calculations.  
In a sample of 40 countries.

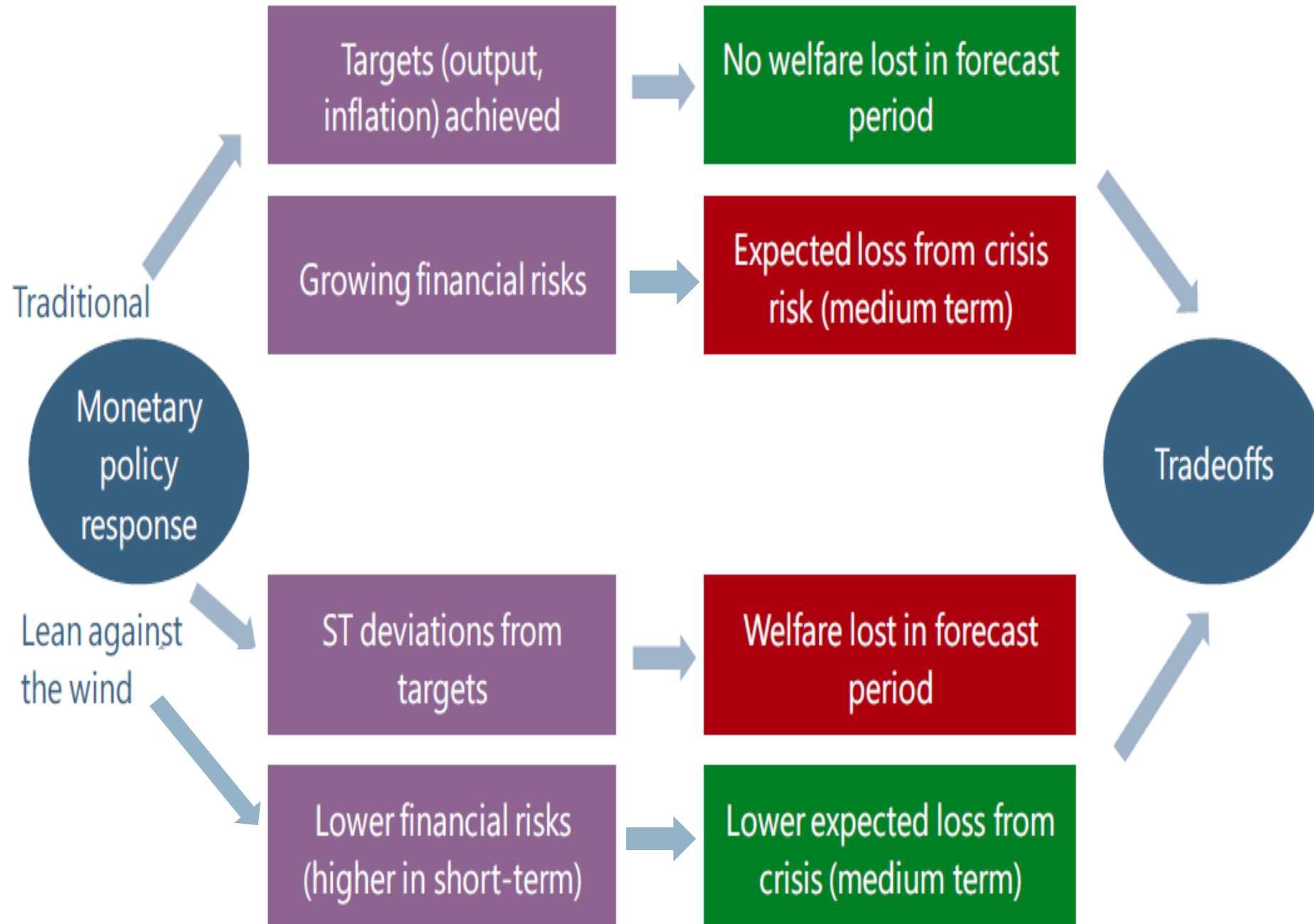
Household Debt Service (percent of income)



Sources: BIS, staff calculations.

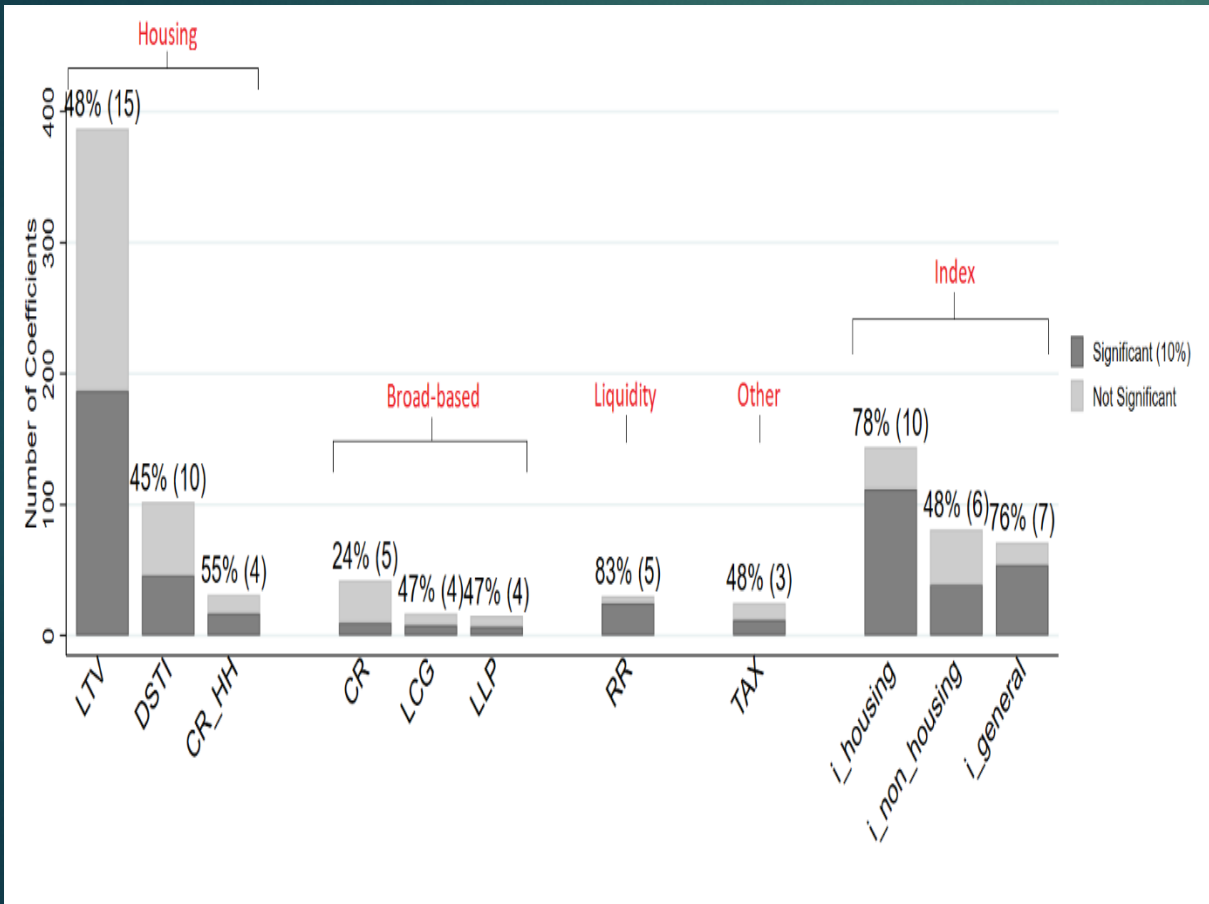
# Borrowing pool different from pre-GFC



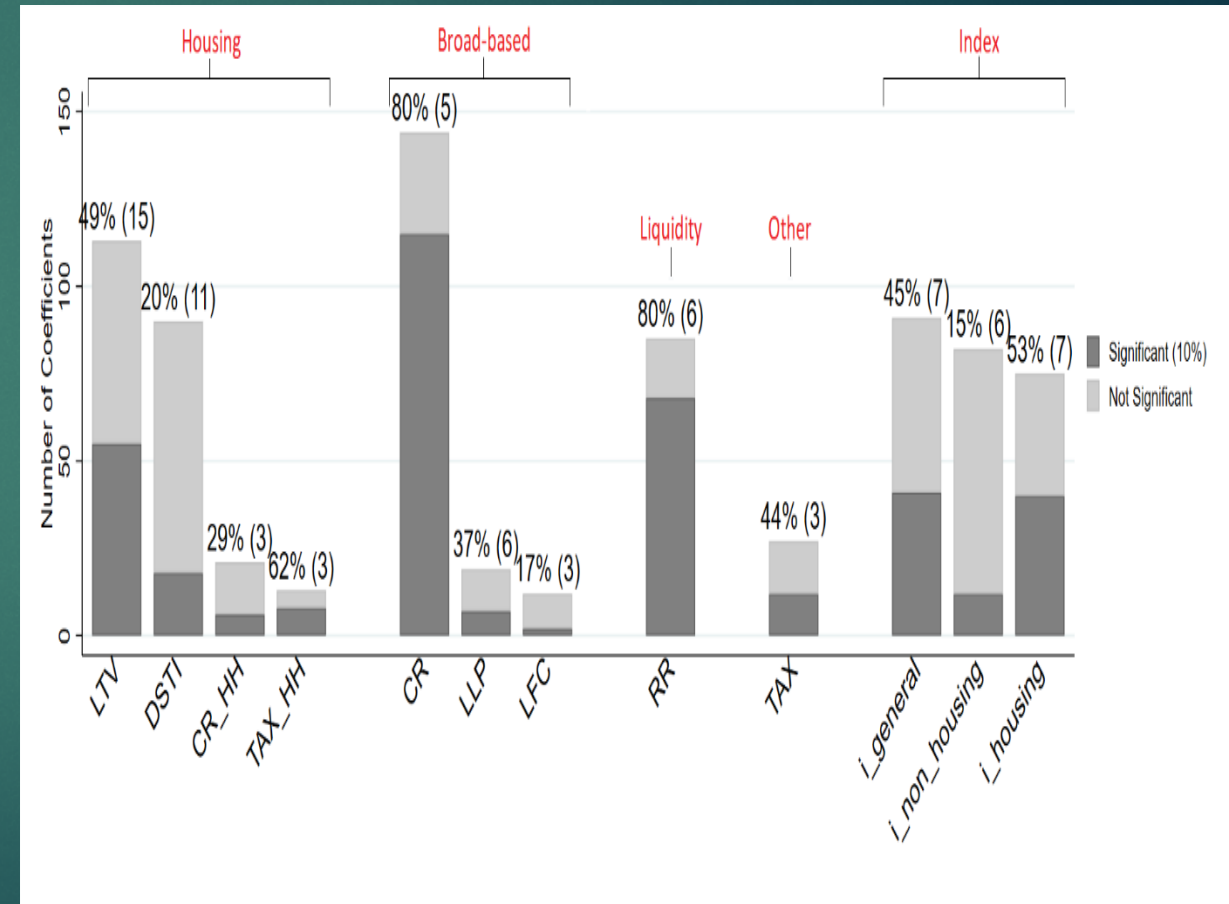


# Does macroprudential policy work?

## Effects on Household Credit



## Effects on Real Estate prices





# Effectiveness of macroprudential policies



- Short-term relatively effective
- Some evidence of leakages: Need for cross-border cooperation
- Leakage appears to increase over time (as for CFMs)
- More effective when stance aligned with monetary policy
- Biljanovska et. Al, 2022, Araujo et al., 2020

# Takeaways



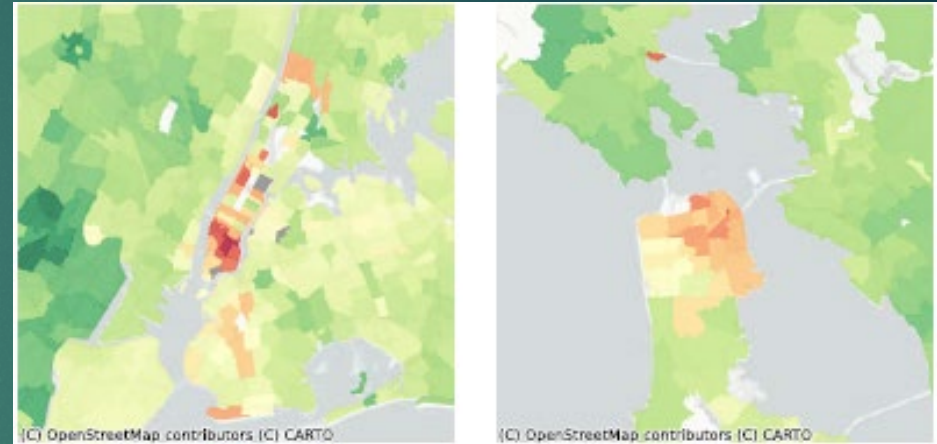
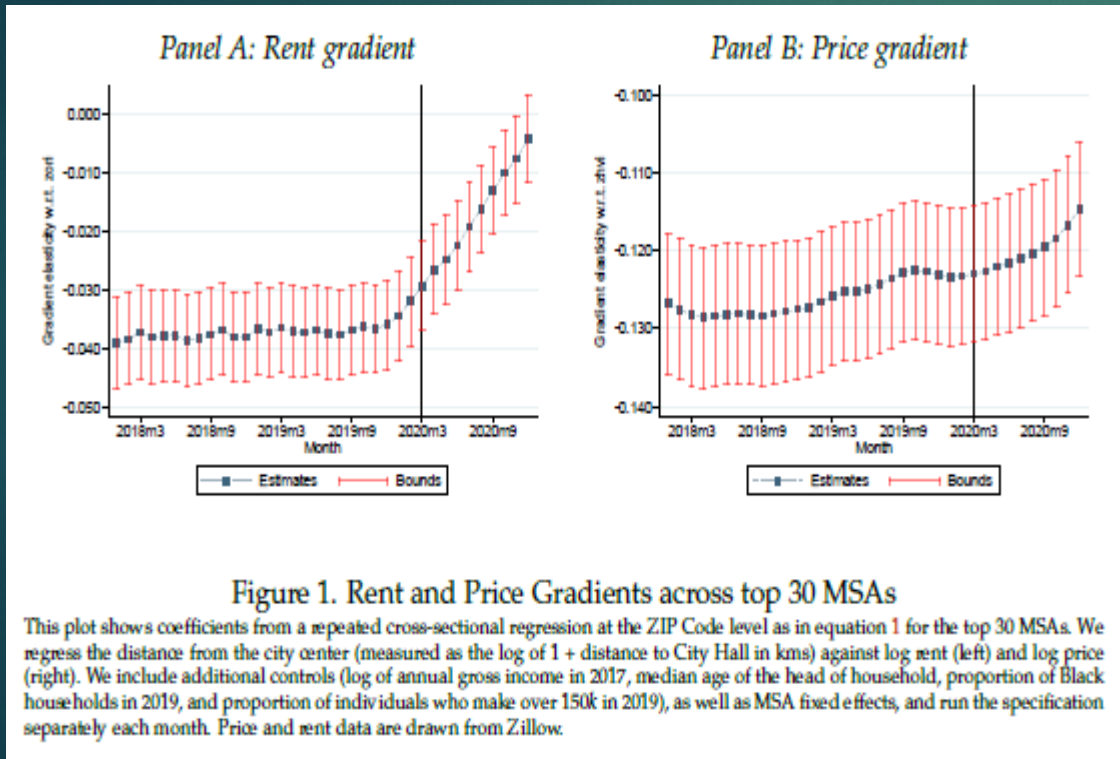
- Great paper
- Detailed review of current state of understanding of links between monetary policy and housing sector dynamics
- Critical, albeit positive, assessment of progress since GFC
- Policy implications:
  - Monetary policy needs to take into account transmission through real estate
    - Especially, in markets with high leverage
  - Central role for macroprudential policy
  - Debate on LAW remains open:
    - More difficult in heterogeneous monetary jurisdictions
    - If macroprudential policies prove insufficient



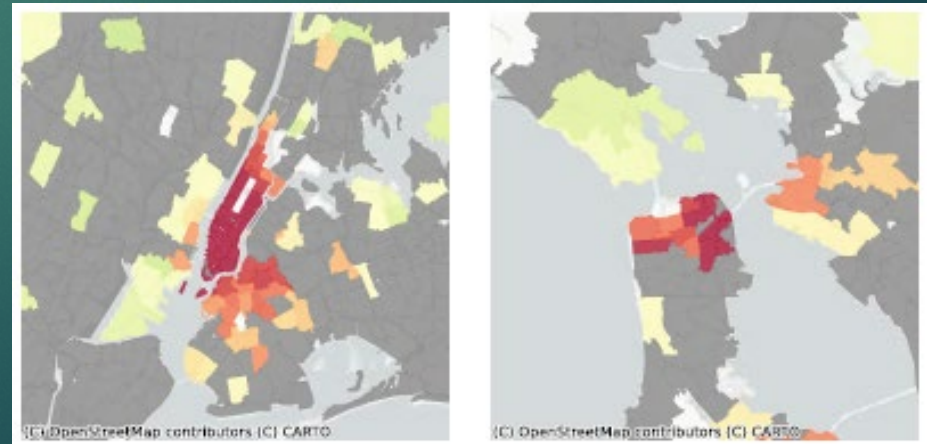
# Structural effects from the pandemic?

Weakening link between distance to city center and rents/prices

- ▶ House prices declined in formerly bubbly cities such as NYC and SF

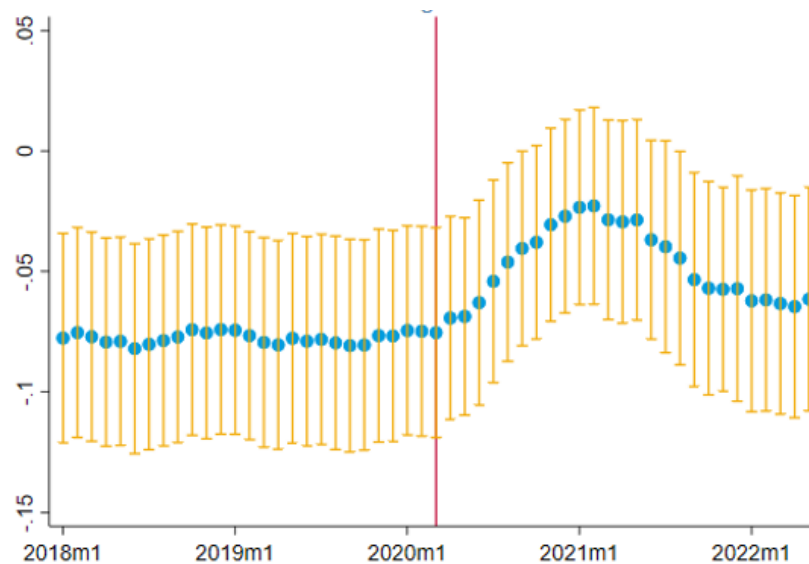


- ▶ Rents declined even more

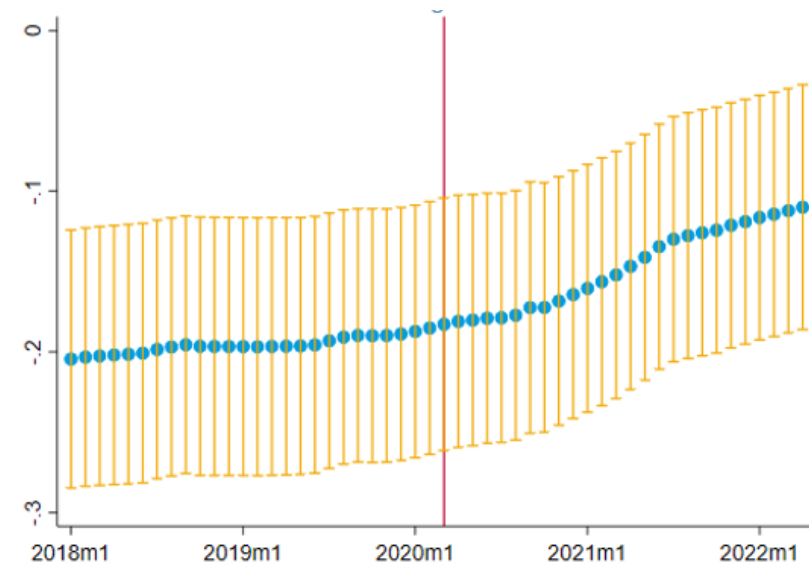


# Structural effects from the pandemic?

## Rent Gradient



## Price Gradient



The plots show coefficients from a repeated cross-section regression at a ZIP code level for top 7 metro areas as shown below.  $distance_i$  denotes the distance of the are from a centroid zip location, measured in miles.  $X_i$  includes ZIP-level controls for log median household income and proportion of black households in 2019 ACS. MSA fixed effect are also included. Both rent (**left panel**) and house price (**right panel**) data are obtained from Zillow.

$$\ln(price_i) = \alpha + \beta_1 \ln(1 + distance_i) + X_i\beta + MSA_i + \epsilon_i$$