

Comments on “Household credit in Asia-Pacific”

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Introduction

Mounting household (HH) debt raises concerns about financial vulnerability. In recent years, HH credit in Asia has grown fast, posing challenges to policymakers. This is also because the resulting “excessive” HH debt could adversely affect consumption or output after it reaches a tipping point. To stabilise high HH debt economies, policymakers would need to move ahead of the curve and introduce a good mix of monetary and macroprudential policies.

Against this backdrop, the paper by Moritz Schularick and Ilhyock Shim timely examines differential impacts of monetary policy and macroprudential policy on credit growth in 12 Asian economies – extending the database for macroprudential measures by Shim et al (2013). With sharp methodological ingredients, the paper estimates those policy impacts using instrumentals for domestic interest rate changes and an inverse-probability-weighted (IPW) estimator as well as a local projection approach.

The paper sheds light on the regional terrain of HH credit growth and policy options for macro-financial stability. The paper provides the following two points associated with the deployment of macroprudential policy and its harmonisation with the conduct of monetary policy. First, it shows evidence that general bank credit tightening is more effective than housing credit tightening in curbing household credit growth. Second, it provides a case for policy complementarity. Macroprudential policy has a significant effect on credit growth but no discernible one on output and inflation. In contrast, monetary policy has a significant effect on both the financial and real fronts. These findings could have important implications for a policy mix, which I will discuss later in my remarks.

General comments

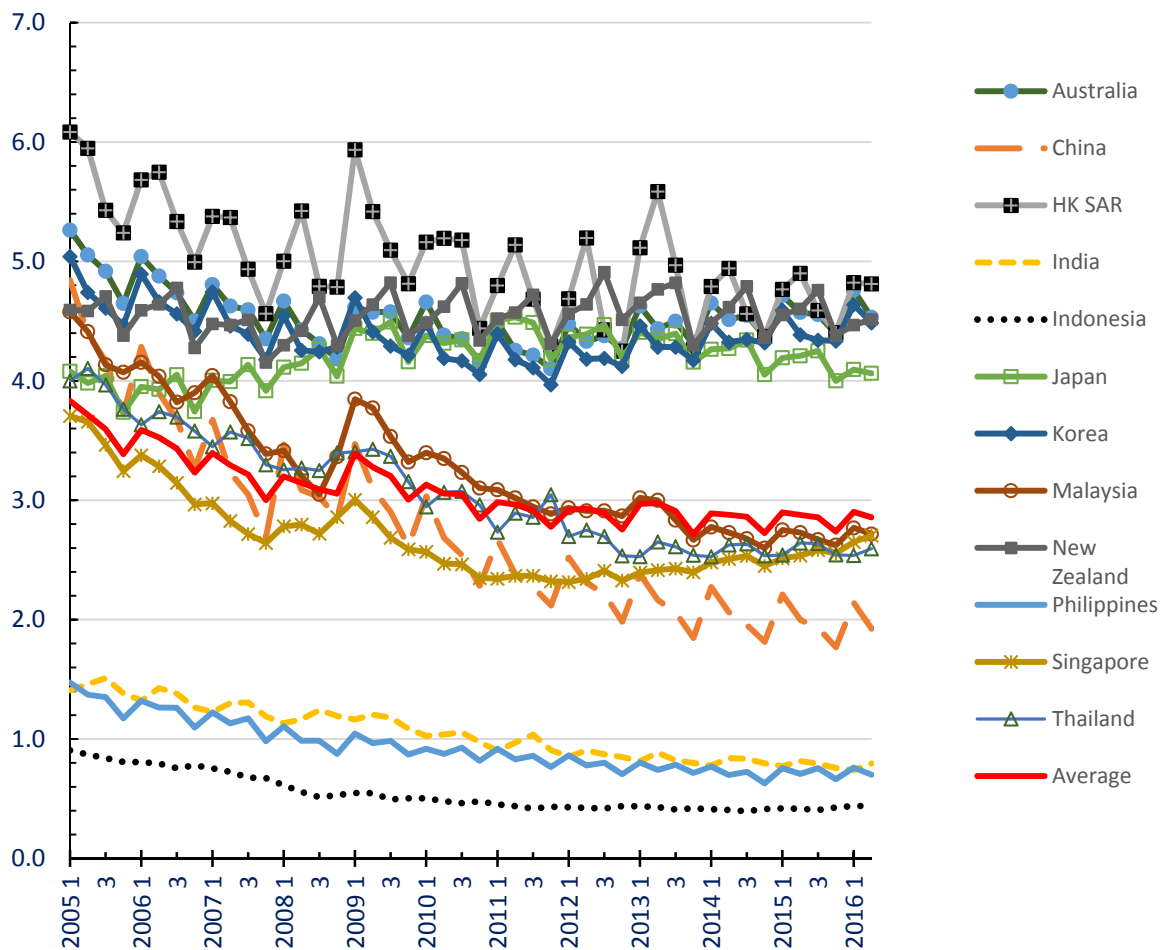
Let me first make general comments and pose some questions as follows. The private credit-to-GDP ratio is a well known metric of financial imbalance. Are there concerns about financial imbalances in the private sector of Asian economies? How are credit expansions translated into mounting HH debt? How can prudential measures be deployed to temper HH credit growth? Does aiming at a narrow target on “bank” credit call for a balloon effect? Does cumulative credit growth matter for consumption and income? If there is complementarity between monetary policy and macroprudential policy, how can the two policies be reconciled in the era of low inflation and low growth?

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The data on credit to the private sector in 12 Asian countries show that the private credit-to-GDP ratio has on average stabilised in recent years but still remains higher than the pre-Global Financial Crisis (GFC) level in some countries (Figure 1). Noting that a higher ratio reflects financial deepening and/or credit excess (after a tipping point), Hong Kong SAR, Australia, New Zealand, Korea and Japan are above the group average (orange line); Malaysia, Thailand, China, and Singapore are around the average; and India, the Philippines and Indonesia are below the ratio of 1.0. Figure 2 shows changes in the private credit-to-GDP ratio (as a fraction) after the GFC. Many countries saw an increase in the ratio during the GFC (red dots in chart) and then pulled it down below the pre-crisis level (blue ticks), but Australia (0.22), Korea (0.23), and New Zealand (0.17) remain above the pre-GFC level.

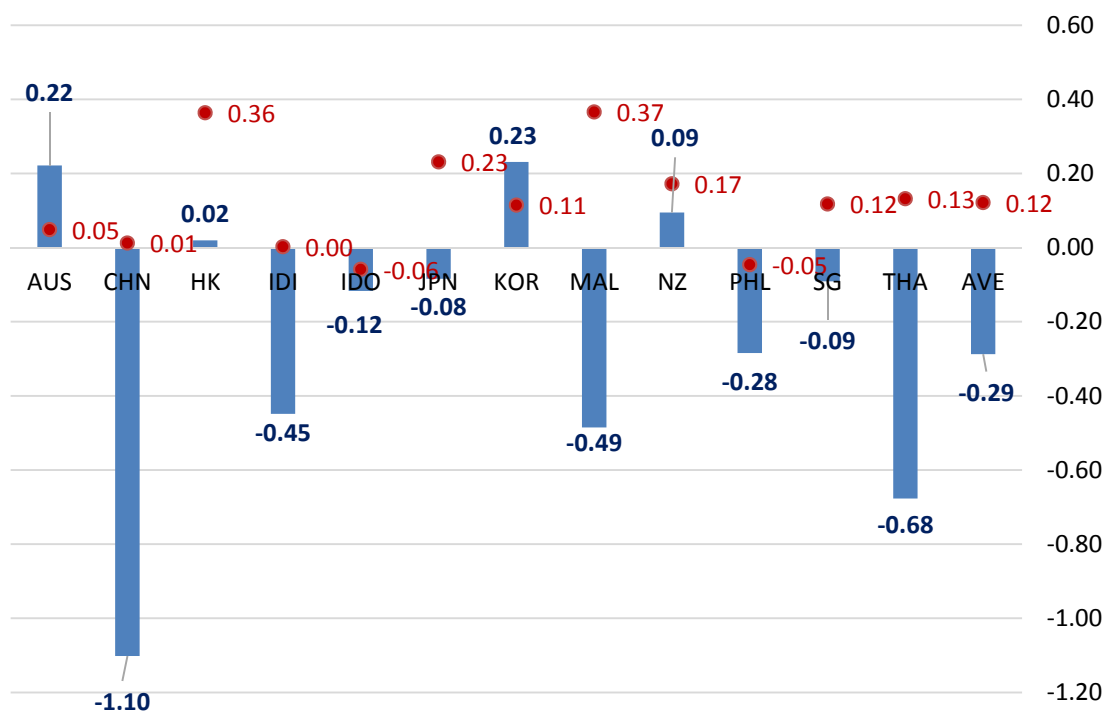
Credit to the private sector (12 Asian economies)

Figure 1



Note: Quarterly data for 2005Q1–2016Q2 are not seasonally adjusted.

Source: Haver Analytics.



Note: Red dots represent changes in the one-year average of the private credit-to-GDP ratio (in fraction) before (2007Q4–2008Q3) and after the GFC (2008Q4–2009Q3).

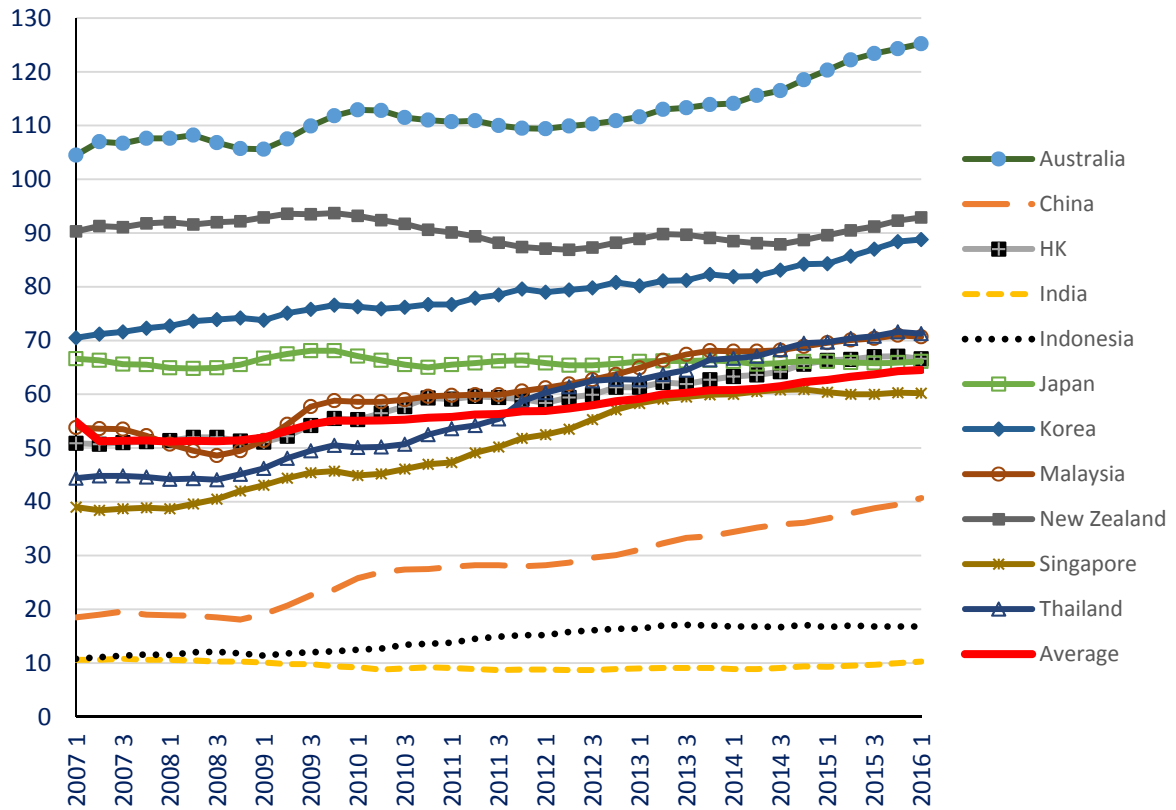
In contrast to stabilising private credit relative to GDP in Asia, HH credit relative to GDP in Asia overall has been rising, as shown by the paper's Figure 1. As a result, HH debts (relative to GDP) have grown rapidly in many countries (Figure 3). This contrast poses a question associated with the drivers or sources of private credit evolutions. Specifically, I wonder if the private credit share has shifted from firms to HHs. Understanding their evolution will help address how much, and how to, deploy prudential measures (Figure 4).

As regards the coverage of credit management, the paper finds that "general bank" credit tightening is more effective than "housing" credit tightening, supporting a broader coverage in targeting credit. A balloon effect suggests needs for the comprehensive management of credit: in the case of Korea (Figure 5A), tightening bank loans to HHs may call for a balloon effect on HH credit through non-bank depository or other financial corporations, not subject to (bank-based) macroprudential measures. This may lead to the unintended consequence of shifting credit risk to shadow banking. I also would like to note that the credit terrain paints different pictures for different countries. The balloon effect may depend on institutional structure: in the case of Thailand (Figure 5B), loans to HH show different dynamics across lender types and have been stabilised in recent years.

There could be non-linearity in the effects of HH debt on consumption and income. Previous studies (eg Cecchetti, Mohanty, and Zampolli (2011)) suggest that excessive debt has adverse effects on the real front through increased future debt-service burdens. It is also notable that a tipping point beyond which HH debt constrains consumption or income differs between country groups (high- vs low-income countries or advanced vs EM economies).

Household debt as percent of GDP

Figure 3

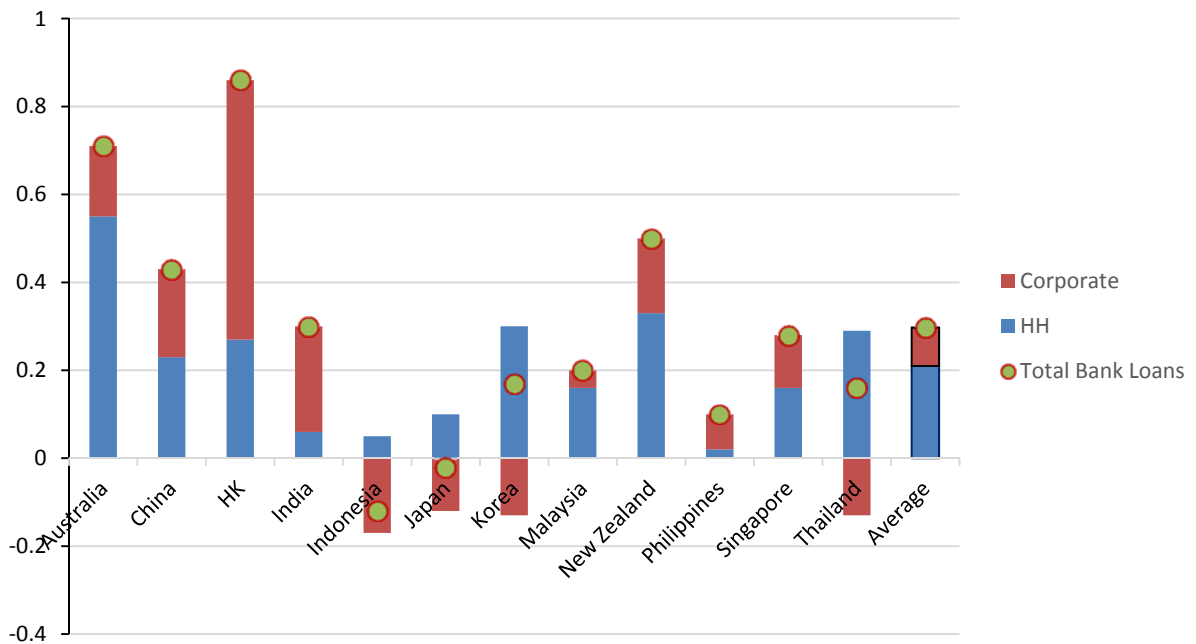


Notes: This figure on the household debt to GDP ratio comprises 11 Asian Countries (2007Q1–2016Q1). The Philippines is not included owing to data availability.

Source: FRED.

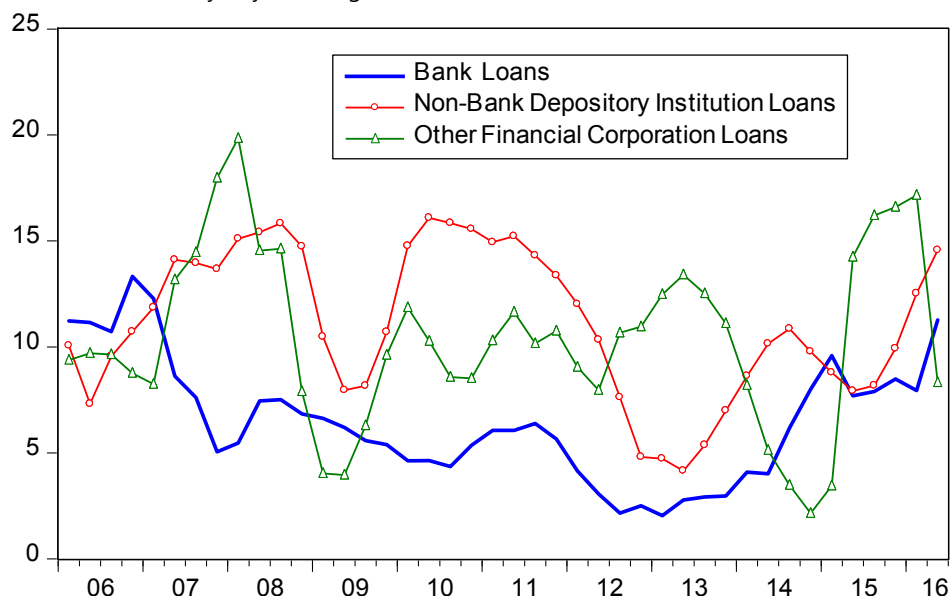
Drivers of private credit: changes in the ratio of bank lending to GDP

Figure 4

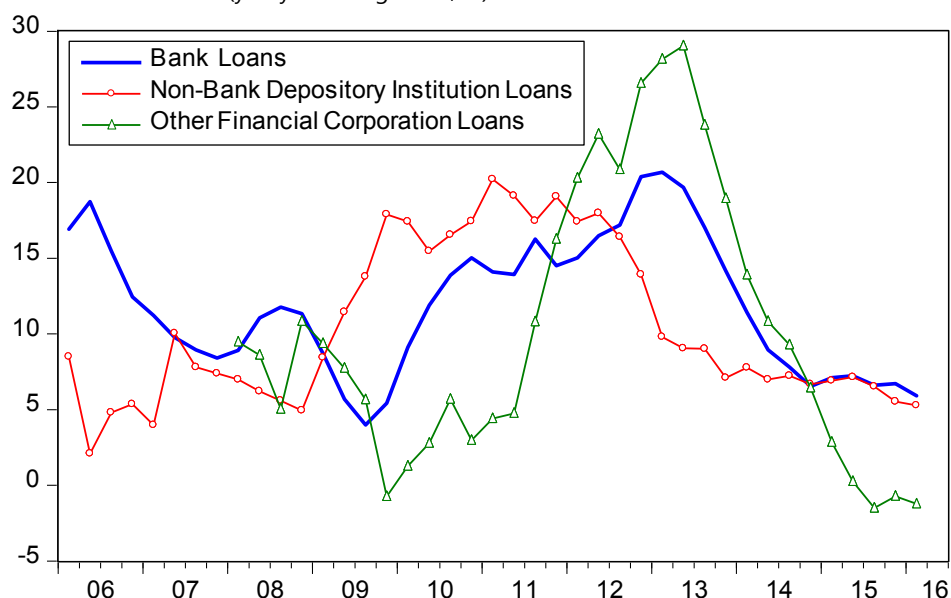


Source: Schularick and Shim (2016) Table 2.

A. Korea: loans to households (y-o-y annual growth, %)



B. Thailand: loans to households (y-o-y annual growth, %)



Note: In panel A, other financial corporations comprise insurance, pension, specialised credit financial companies, public financial institutions, and other financial intermediaries.

Source: Haver Analytics.

The paper’s findings shed light on the complementarity of monetary policy and macroprudential policy for macro-financial stability. Macroprudential policy has an effect on HH credit but no pronounced one on output and inflation – suggesting its use primarily for financial stability. Considering policy complementarity, do the two policies move in the same or opposite direction in terms of the policy stance? Clearly, given high inflation pressures, monetary tightening could accompany macroprudential tightening. Conversely, against disinflationary pressures and

mounting HH debt, could there be a mix of monetary loosening and macroprudential tightening?

A related recent study by Choi and Cook (2016) examines a mix of monetary and macroprudential policy mix for inflation targeting economies. This study finds that macroprudential tightening is more likely to temper inflation or slow credit growth when the economy is booming and more likely to occur to check credit expansions when inflation is below target while monetary policy space is limited. It also suggests increasing needs for the mix of accommodative monetary policy and tighter macroprudential policy at low inflation and low growth.

Specific comments

Let me now give my specific/technical comments on the paper. First, in measuring policy actions, the authors could consider including policy rate target changes in monetary actions and loan-to-deposit ratio changes in prudential actions. Second, instruments for domestic policy rates to control for foreign policy (p 25) could include unconventional monetary policy measures undertaken by the Fed, ECB, and BoJ (or global liquidity) – in addition to the US policy rate – as they could also have affected domestic policy rates. Third, it could be checked if the cumulative effects of monetary policy on output and inflation that widen over the projection horizon (Figure 11) could reconcile the stability of the system. Fourth, to consistently estimate policy effects on inflation, regressions could control for imported inflation or structural factors because, for example, macroprudential tightening may coincidentally concentrate on the era of oil and commodity price falls.

My last comment is that the paper could benefit from taking into account the recent debate on macroeconomic trilemma or dilemma in using instrumental variables for estimation. Following Jordà, Schularick, and Taylor (2015), the paper isolates fluctuations in domestic interest rates driven by the base country, exogenous to the domestic economy, to deal with the macroeconomic trilemma (p 14). The paper introduced the term, z_{it} , to account for a direct link between domestic and global interest rates for peg countries with open capital accounts. Even for floats, however, it is hard to isolate domestic interest rate policy from global interest rates under capital mobility by keeping expected appreciation aligned with the (desired) interest rate differential. So, exchange rate regimes may not matter, as in the argument for dilemma (Rey (2015)). In this light, the paper could introduce another control for floats with capital mobility.

Summary

To summarise, Schularick and Shim's paper covers very important issues emerging in the region: HH credit and policy options for macrofinancial stability. It nicely contributes to the literature on monetary and macroprudential policies with comprehensive data and empirical rigour. The paper offers very useful findings for policymakers who need to harmonise proactively the two policies with constrained policy space in the face of low inflation/growth and financial imbalances.

References

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