

Household Debt in OECD Countries: Stylised Facts and Policy Issues

KDI International Conference
Household Debt from an International Perspective:
Issues and Policy Directions

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Outline of the presentation

Household debt in OECD countries

- Levels and growth of indebtedness
- Debt burden on households
- Distribution of debt and assets across households
- Delinquencies and foreclosures

Determinants of household debt

- Debt-Housing prices: a two-way causality
- Drivers of housing prices

Household debt and financial and macroeconomic stability

- Credit, funding and macroeconomic risks

Policy responses

- Micro-prudential
- Macro-prudential
- Monetary
- Housing

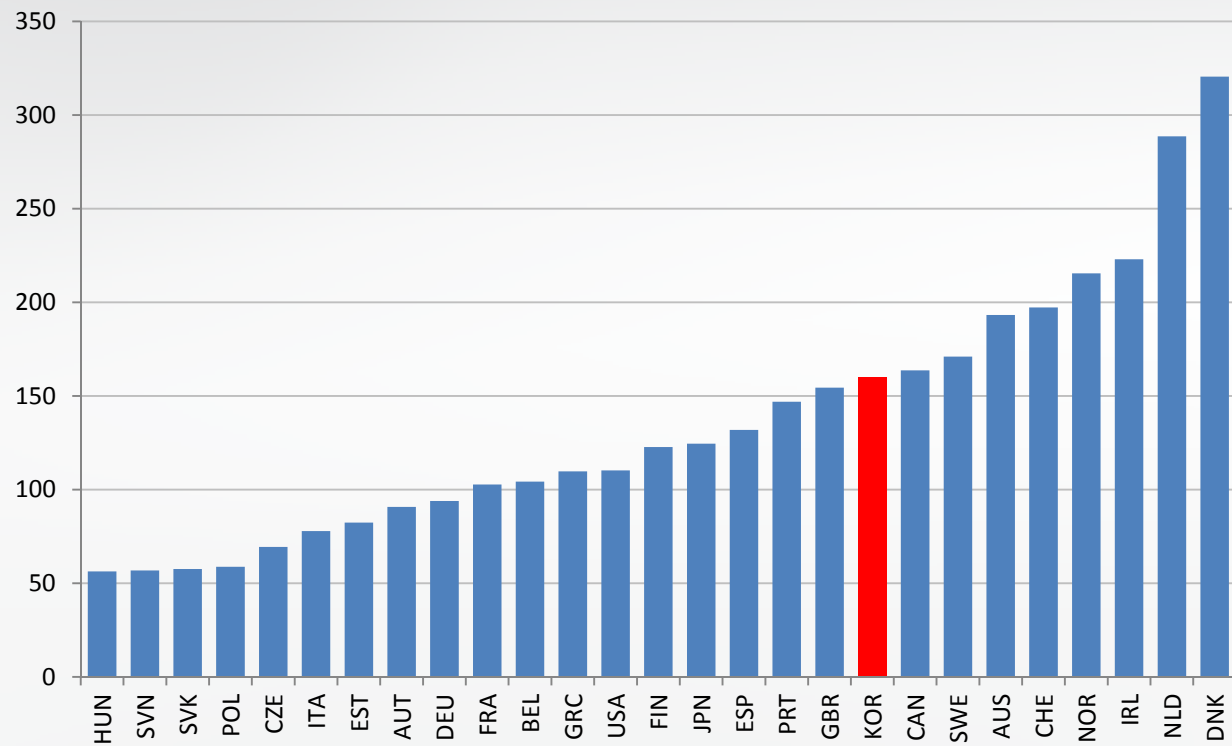
Conclusions

Household debt in OECD countries



Household debt in OECD countries

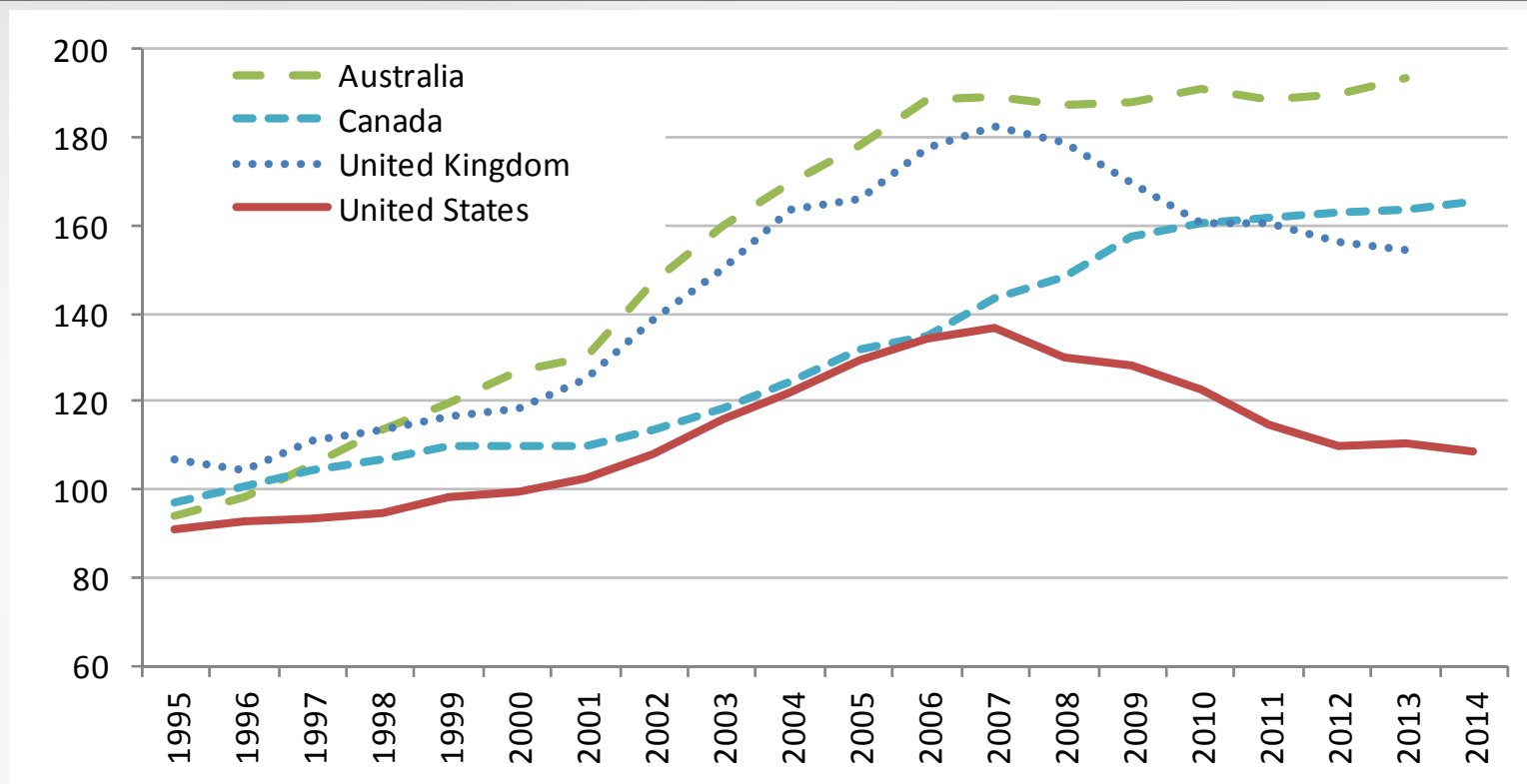
Per cent of net disposable income



Source: OECD National Accounts database.

Household debt in Anglo-Saxon countries

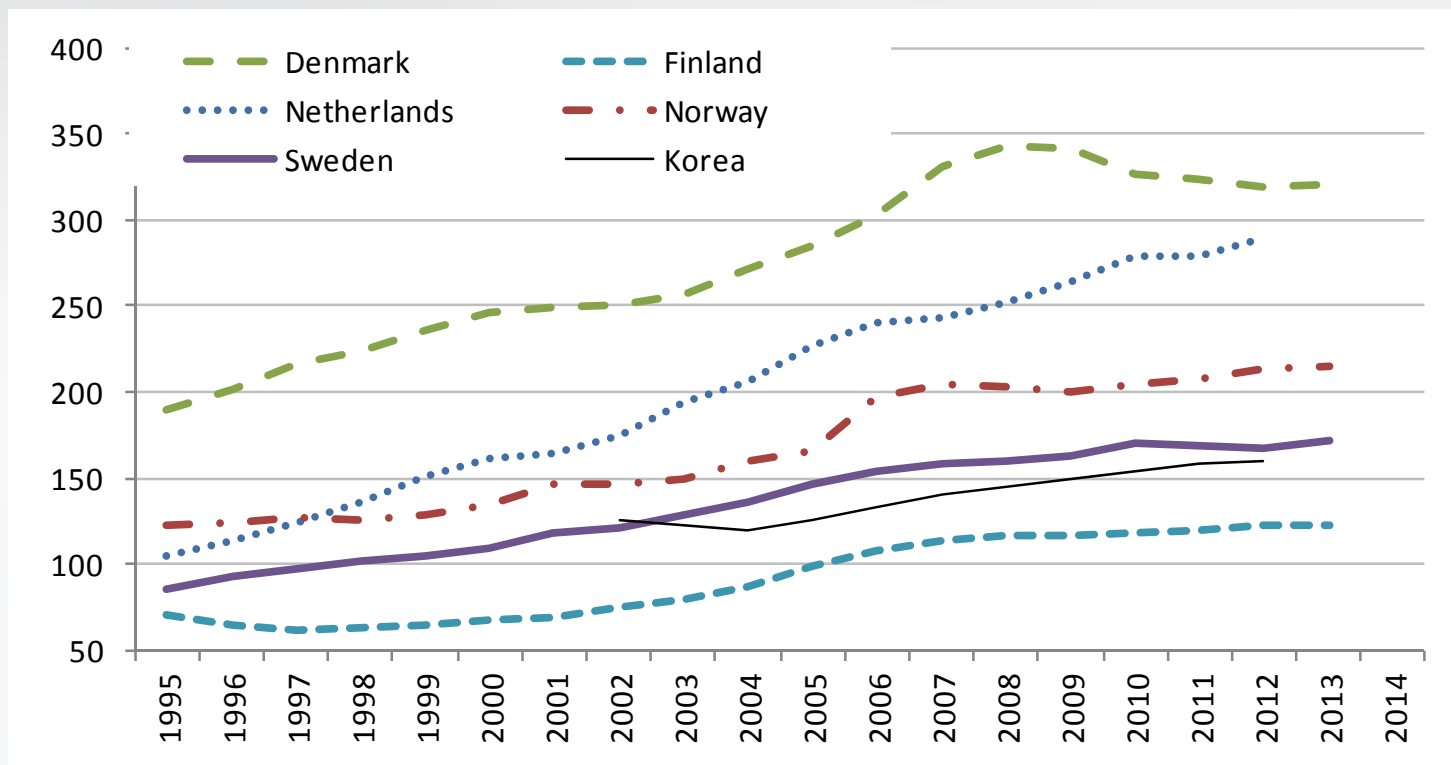
Per cent of net disposable income



Source: OECD National Accounts database.

Household debt in “Northern” countries

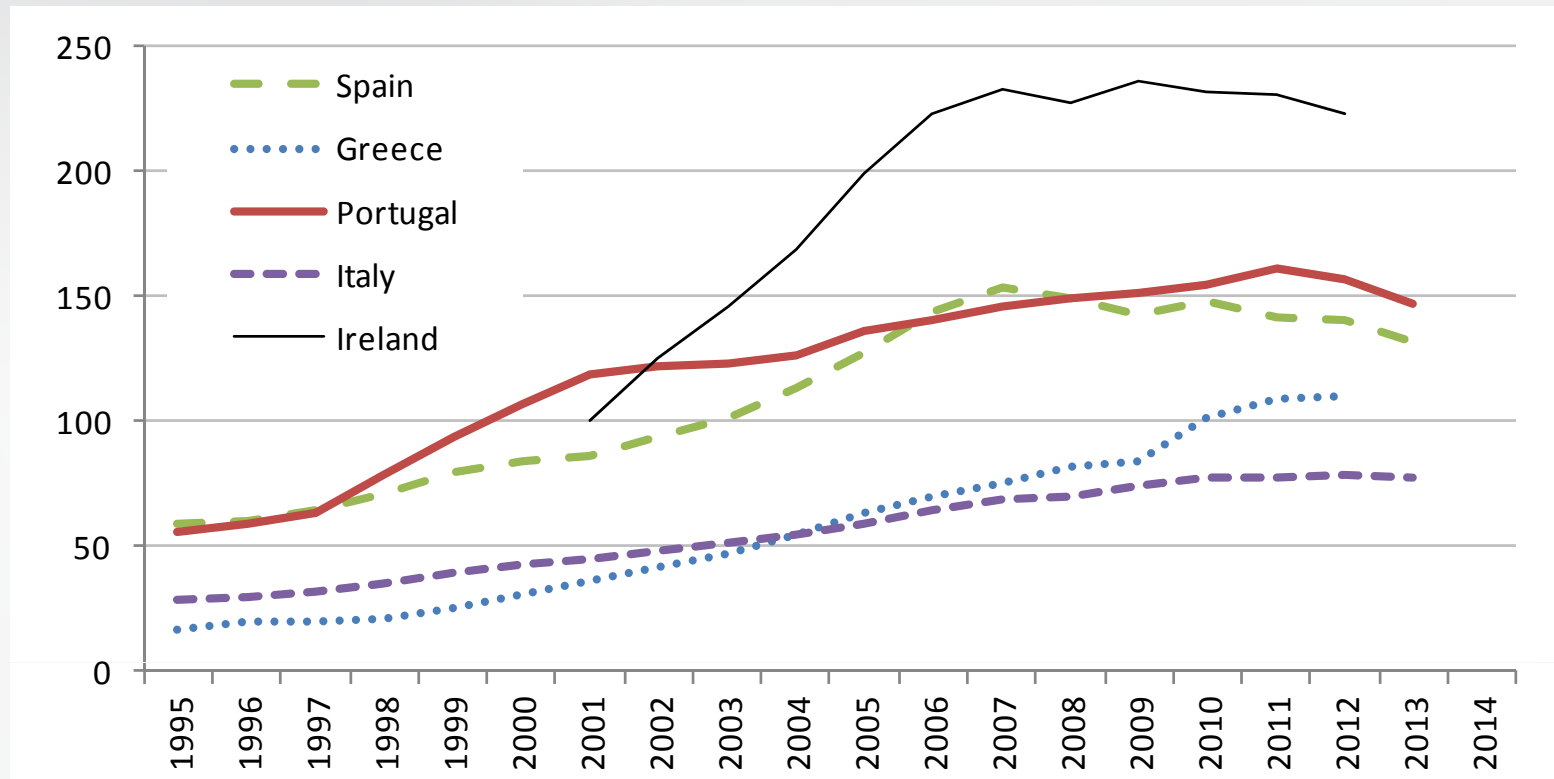
Per cent of net disposable income



Source: OECD National Accounts database.

Household debt in the euro area periphery

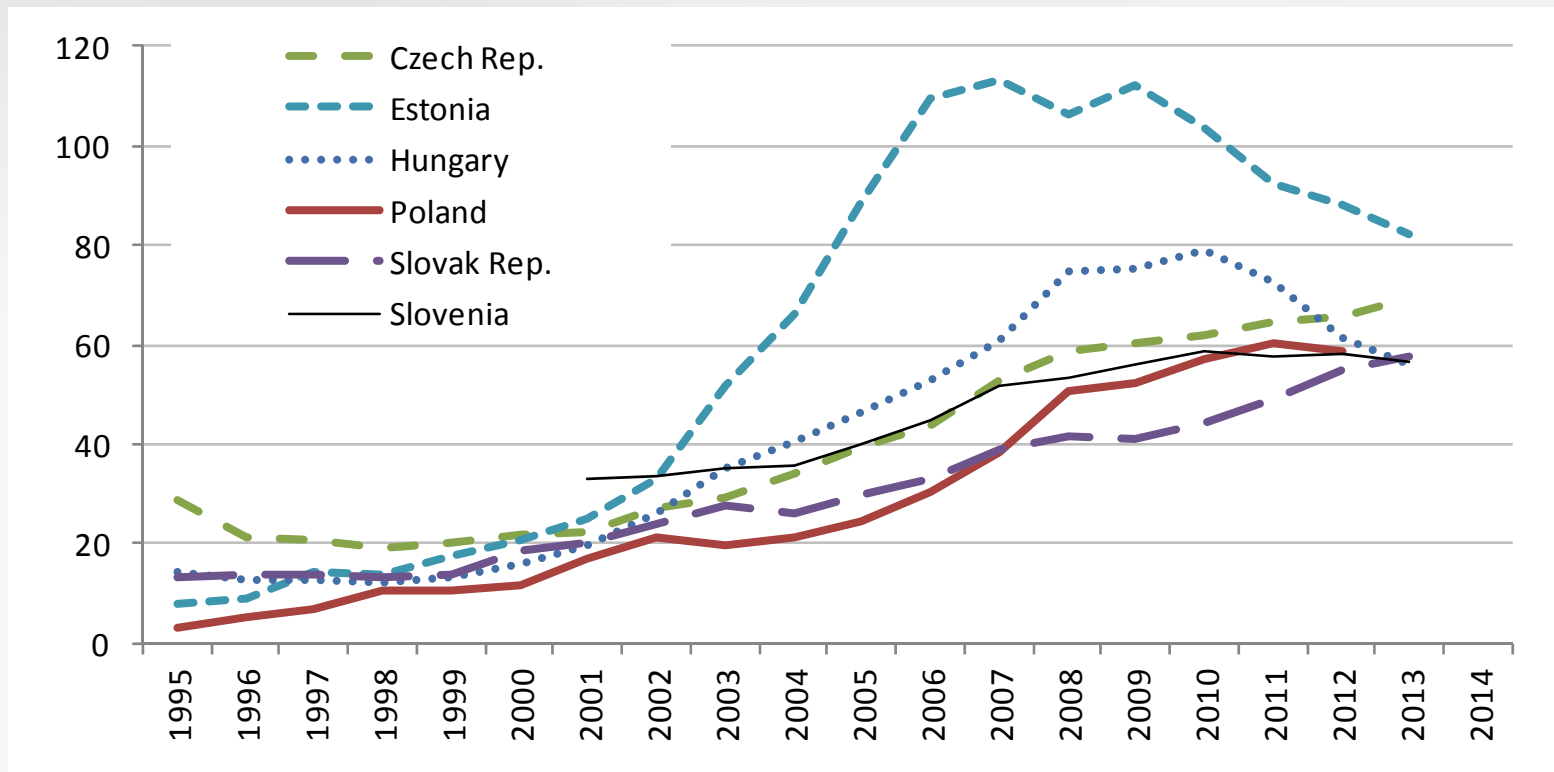
Per cent of net disposable income



Source: OECD National Accounts database.

Household debt in Central and Eastern Europe

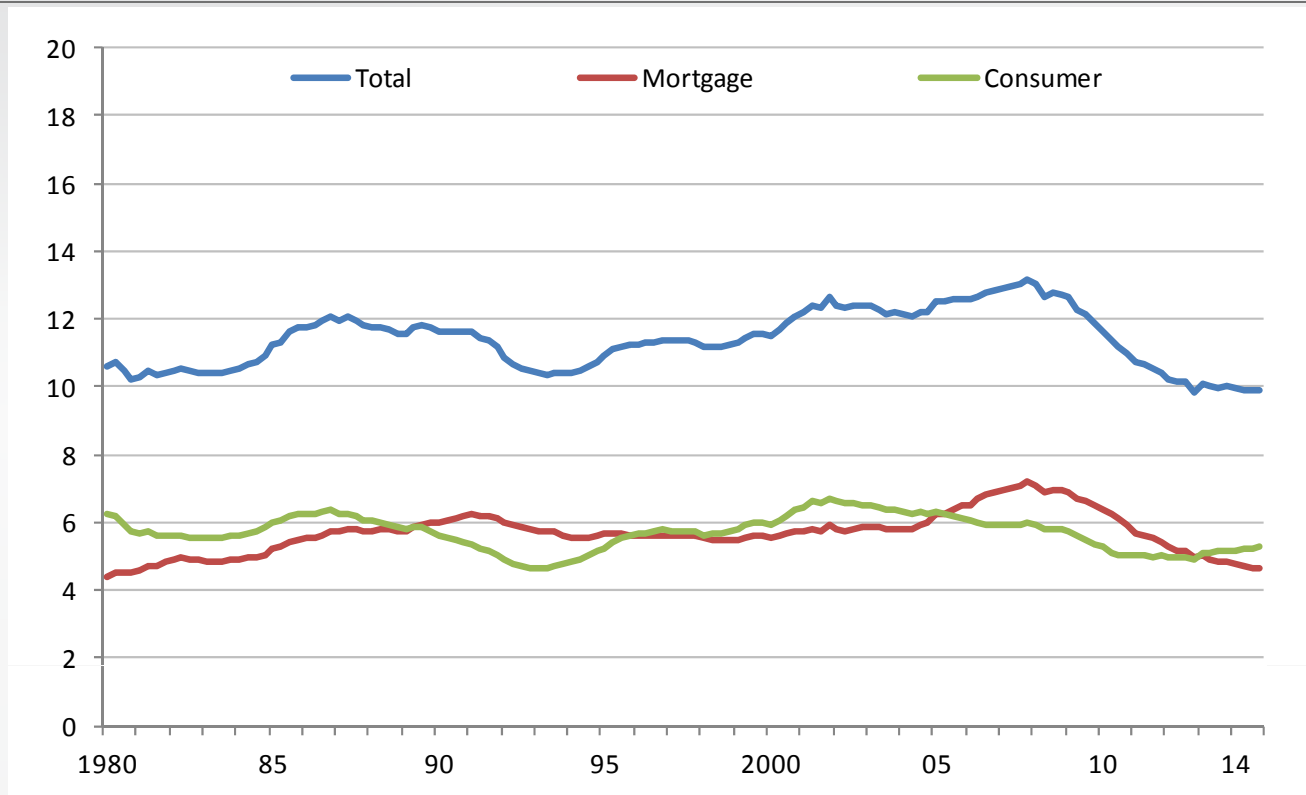
Per cent of net disposable income



Source: OECD National Accounts database.

Household debt service payments in the United States

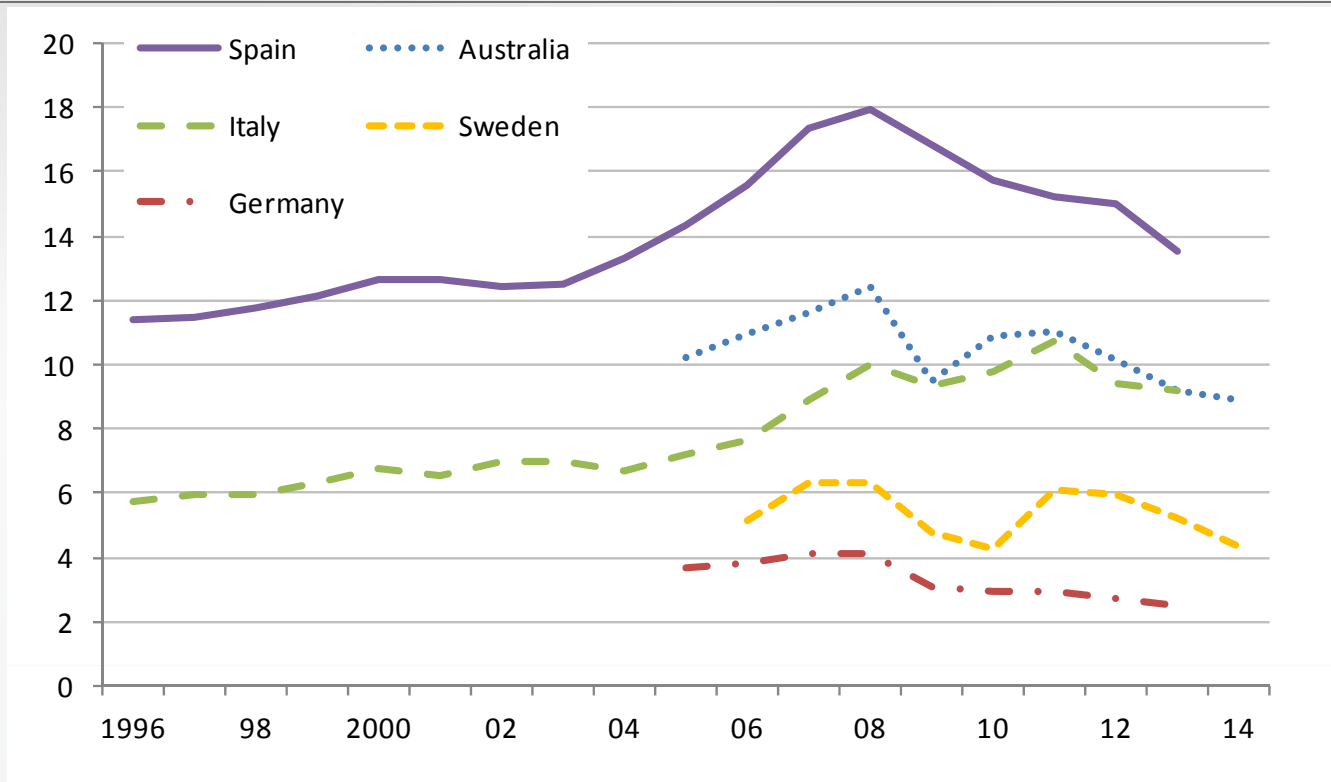
Interest and principal, per cent of disposable income



Source: US Federal Reserve.

Household debt service payments in selected OECD countries

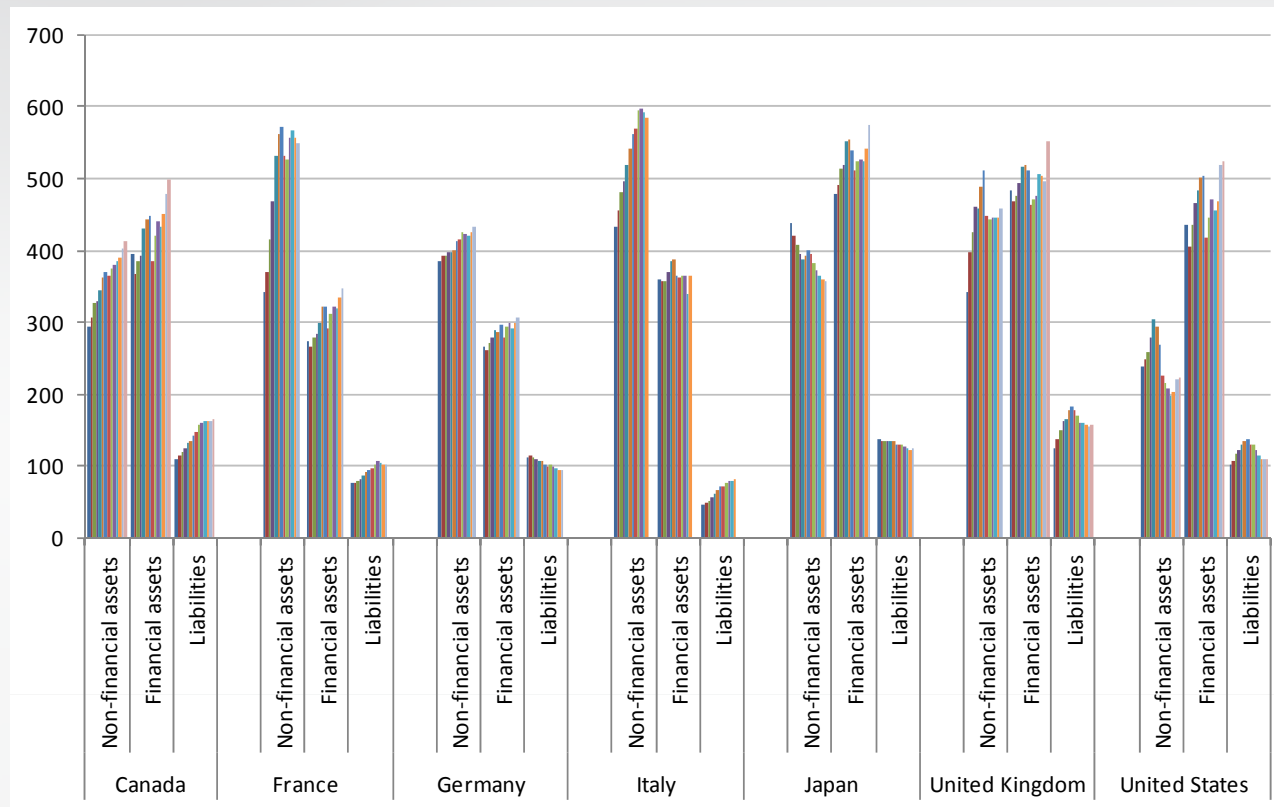
Interest and principal, per cent of disposable income



Source: IMF and author's calculations.

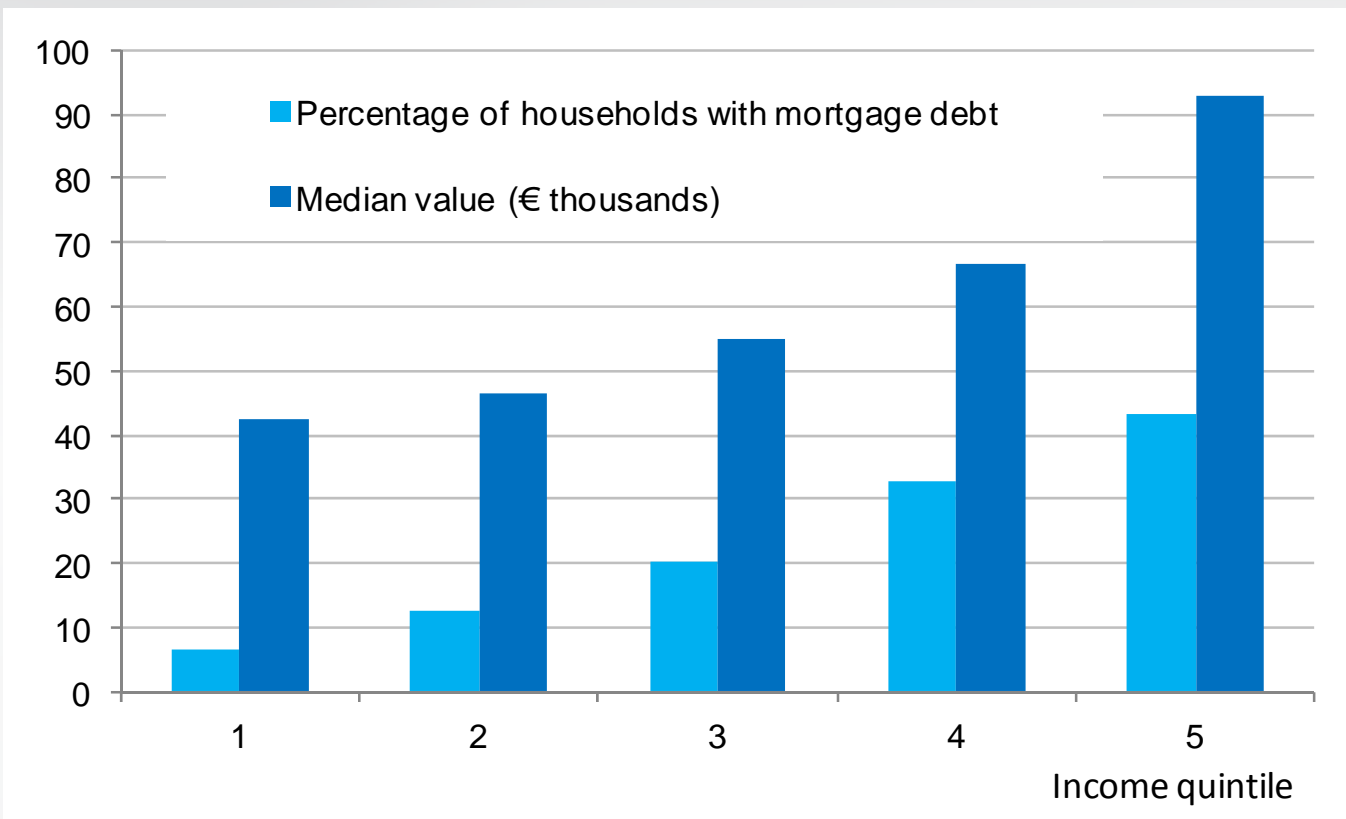
Household assets and liabilities in G7 countries

Per cent of net disposable income, 2001-2014 (or latest)



Source: OECD National Accounts Statistics.

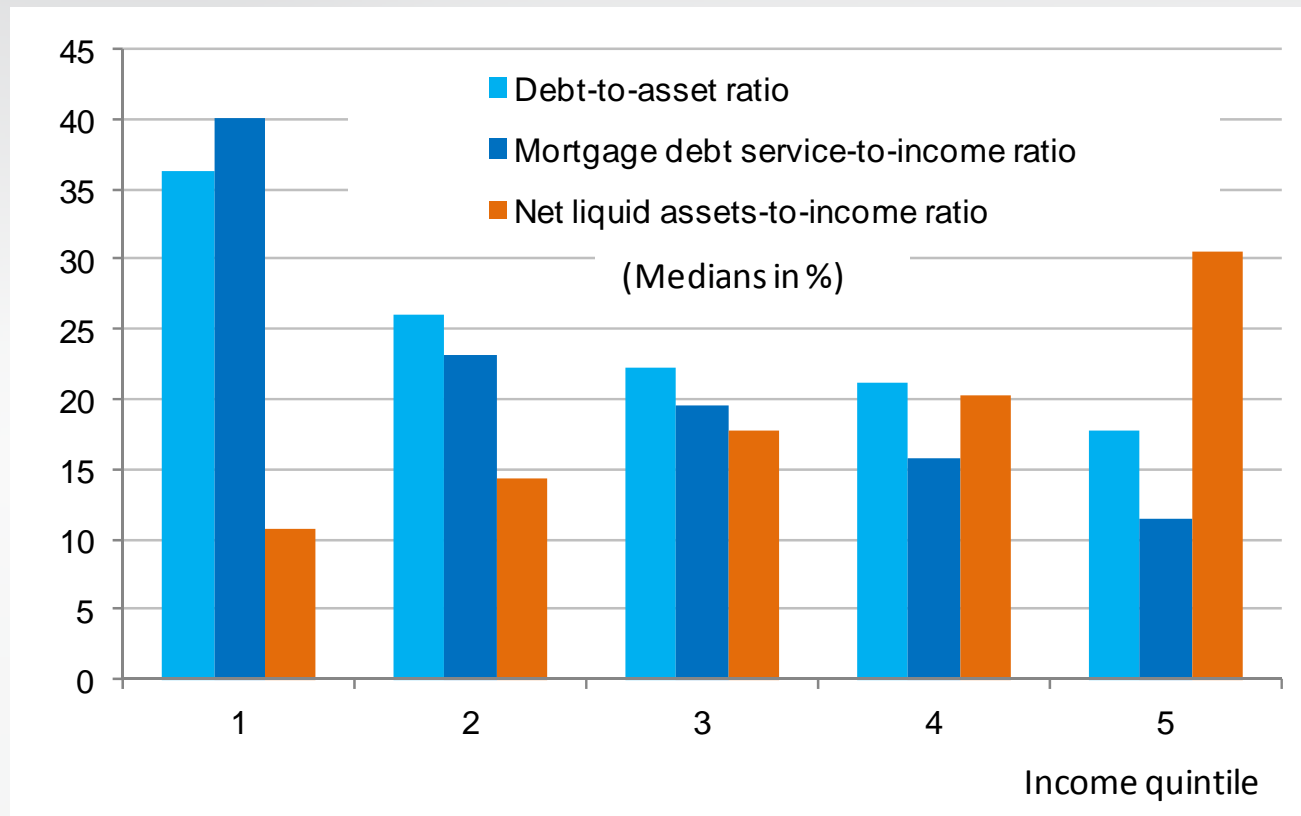
Distribution of mortgage debt in the euro area 2010



Source: Eurosystem Household Finance and Consumption Survey.

Distribution of mortgage debt in the euro area (cont.)

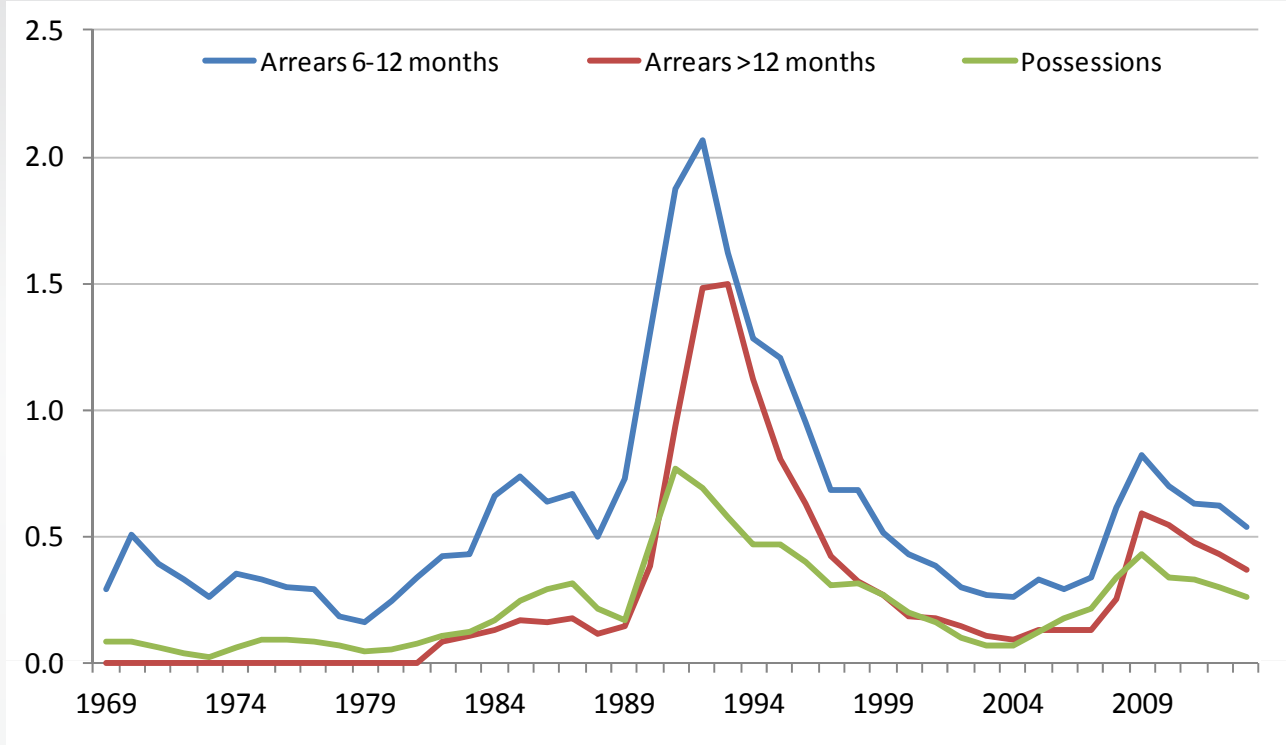
2010



Source: Eurosystem Household Finance and Consumption Survey.

Arrears and possessions in the United Kingdom

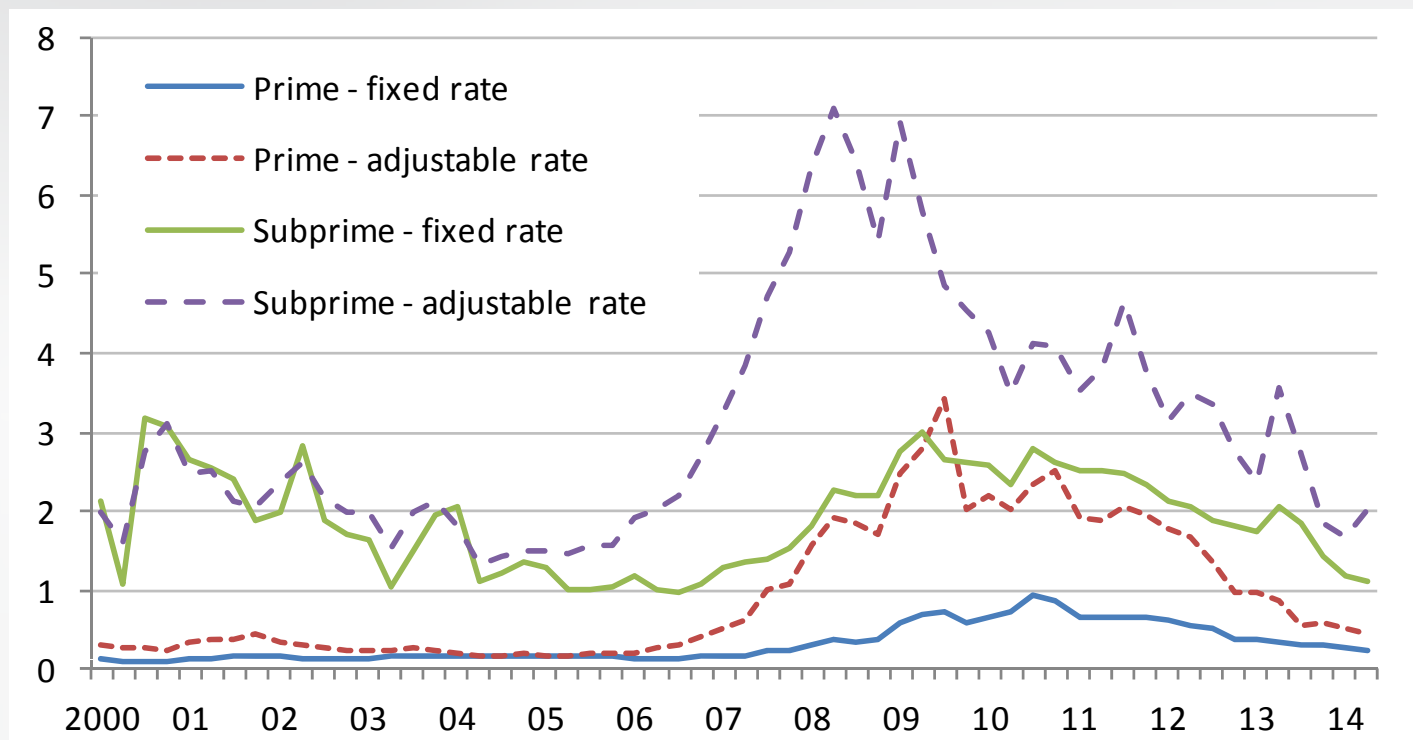
Per cent of outstanding mortgages



Source: Council of Mortgage Lenders.

Foreclosures in the US prime and subprime markets

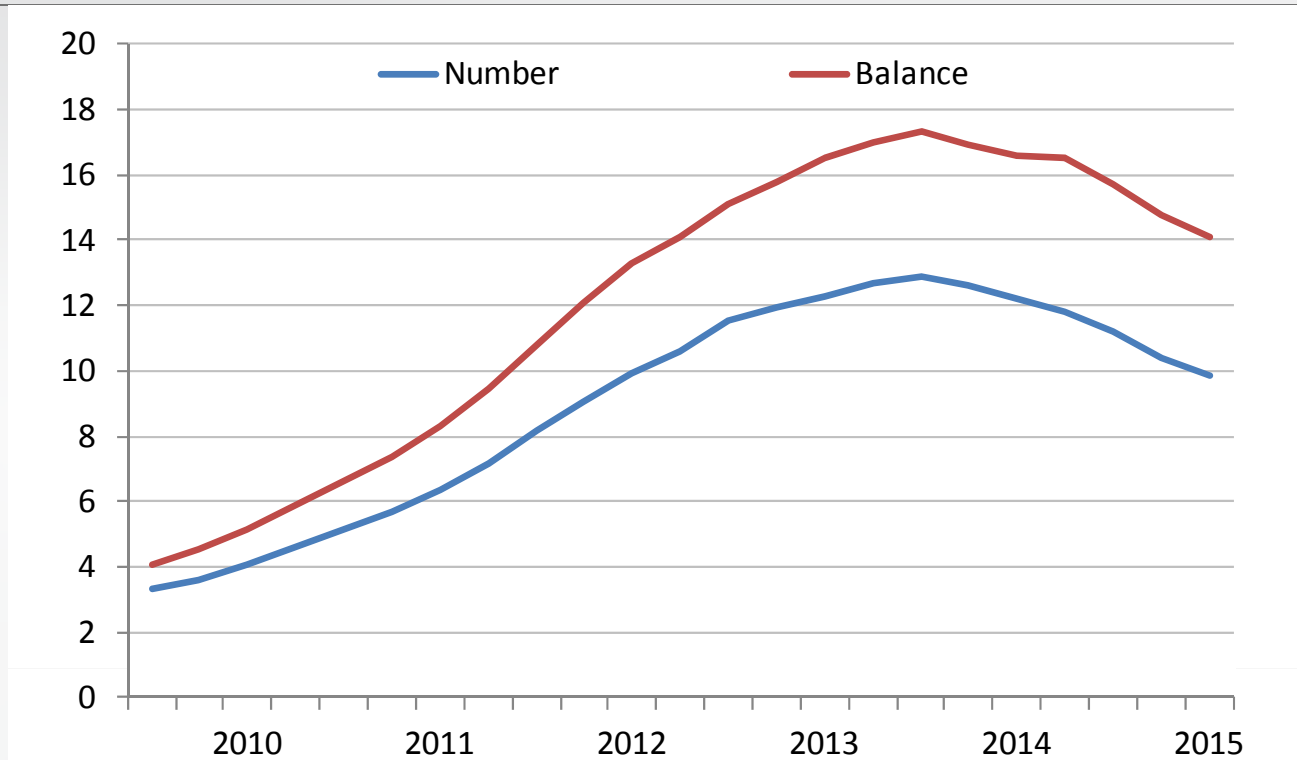
Percentage of foreclosures started per quarter



Source: Datastream.

Arrears in Ireland

Percentage of loans in arrears for more than 90 days



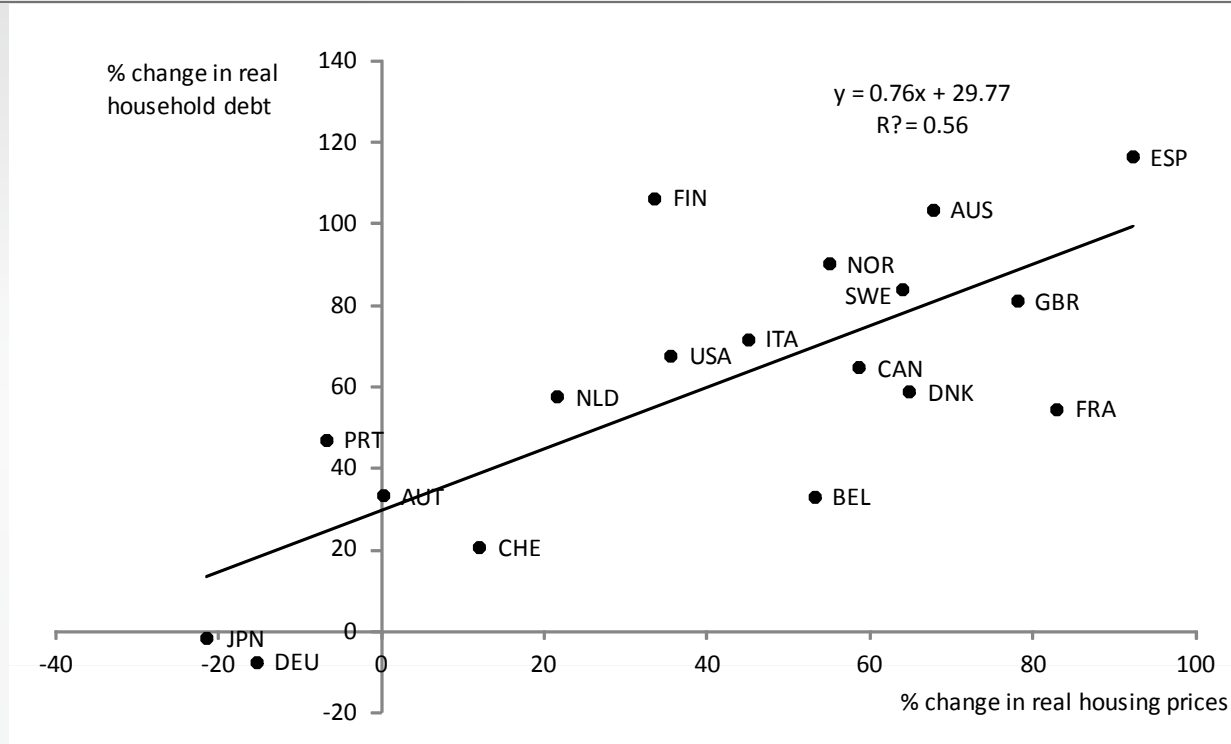
Source: Central Bank of Ireland.

Determinants of household debt



Growth in household debt and housing prices

2000-2007



Source: OECD Economic Outlook database and national sources.

Main determinants of housing prices

Demand

- Mortgage rates, lending standards and mortgage products
- Household real disposable income
- Unemployment
- Demographics
- Taxation
- Housing price expectations
- Foreign demand

Supply

- Profitability of construction
- Housing and land price expectations
- Planning and zoning regulations
- Infrastructure

Household debt and financial and macroeconomic stability

What are the risks associated with high/growing household debt

Credit risk

- Generally moderate
- But some cases of high risk lending (e.g. US, Hungary, Iceland)
- Defaults resulting from a sharp deterioration in macroeconomic conditions (e.g. euro area periphery)

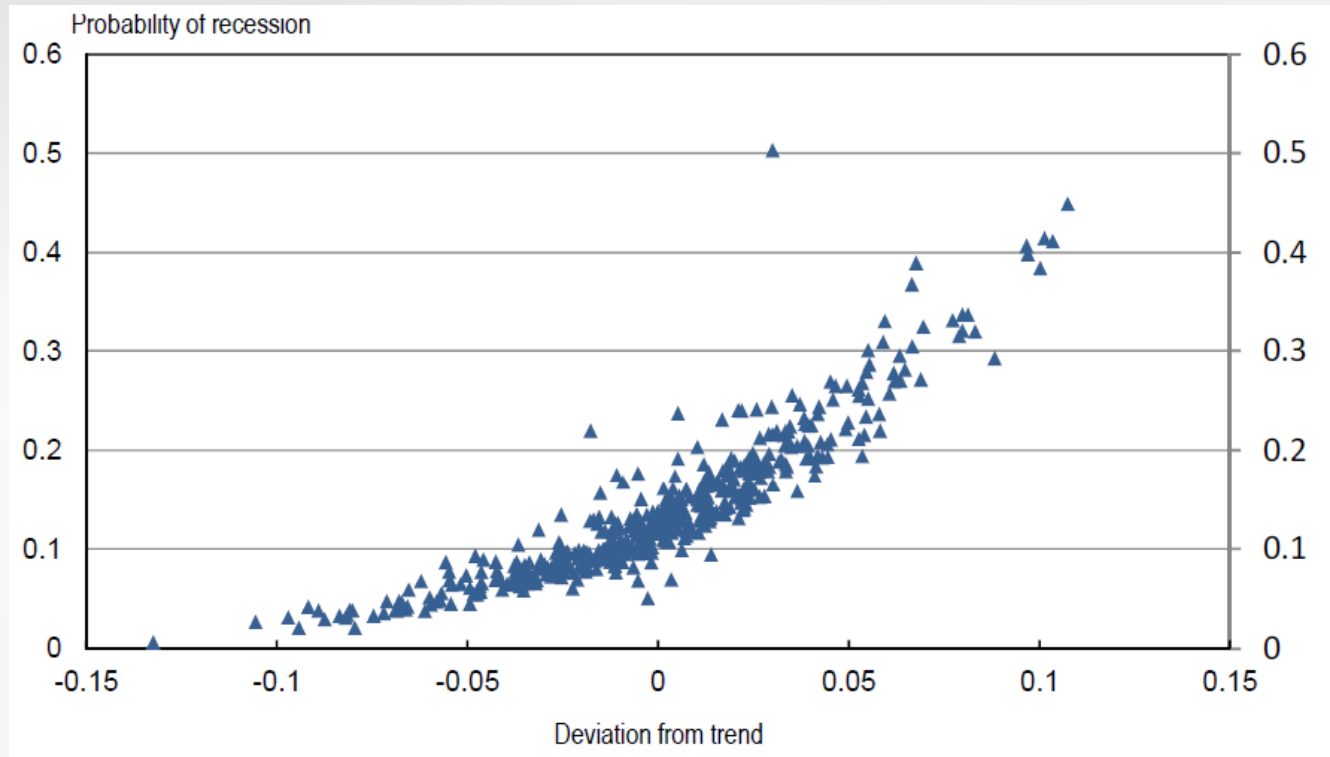
Funding risk

- Maturity mismatch (e.g. UK, Netherlands)
- Currency mismatch (e.g. Iceland, some Central and Eastern Europe countries)

Macroeconomic risk

- Fall in consumption (e.g. US, UK, Denmark)
- Reduction in residential investment
- Second round impact on the economy and the financial sector

Predicted probability of recession when household debt relative to trend rises



Source: Sutherland and Hoeller (2012), OECD Economics Department Working Paper No. 1006.

Characteristics of the cycle when debt is high and low

Earliest available year to 2010

	Number of recessions	GDP		Previous expansion	
		Average size	Average length	Average size	Average length
Total economy debt					
High	45	-4	4	26	29
Low	25	-2	4	16	20
Household debt					
High	42	-4	4	28	31
Low	32	-2	3	15	18
Government debt					
High	27	-2	3	18	23
Low	48	-4	4	25	27
Financial sector debt					
High	41	-5	4	27	30
Low	33	-2	4	16	19
Non-financial sector debt					
High	46	-4	4	25	28
Low	21	-3	4	19	23

Note: The cycle is the classical business cycle. The size is the cumulative percentage change in the level and the length is the number of quarters of the contraction or expansion phases.

High (low) debt = 50% of business cycles with highest (lowest) de-trended debt-to-GDP ratios.

Source: Sutherland and Hoeller (2012), OECD Economics Department Working Paper No. 1006.

Policy responses

How to avoid credit bubbles and excessive debt?

Sutherland et al. (2012) [OECD Economics Department Working Paper No. 1003]

- First line of defence: micro-prudential regulation
- Second line of defence: macro-prudential policy
- Third line of defence: monetary policy

The propagation of financial shocks depends on housing market features

-> A holistic approach to housing is needed

- Supply responsiveness
- Taxation of housing
- Rental market regulations, affordable housing...

First line of defence: micro-prudential

Return to the “basics”

- Sound underwriting: ability to repay and documentation (income, assets...)
- Appropriate incentives and transparency
- High loan-to-value ratio loans: more capital or mortgage insurance
- Non-amortising loans should be granted with great caution
- Adequate capital buffers for lenders and insurers

Areas requiring close monitoring

- Loans to developers and construction companies
- Loans for commercial property
- Lenders' funding model: maturity (and currency) mismatch

Second line of defence: macro-prudential

Instruments

- Caps on loan-to-value ratios, loan-to-income or debt-to-income ratios
- Risk weights on residential mortgages
- Countercyclical buffers
- Dynamic provisioning
- Liquidity requirements
- Measures targeted at foreign-currency lending
- ...

Implementation issues

- Trigger
- Responsibility
- Risk of circumvention

Third line of defence: monetary policy

Identification of a bubble

- Not all large upswings in housing prices are bubbles
- Relevant indicators: credit growth, liquidity, property prices... (e.g. BIS, ECB)
- Other information (e.g. underwriting practices, funding structures...)

Effectiveness of interest rate hikes

- Large hikes may be needed to stop a housing boom, with a big impact on output, employment and inflation
- Potential conflict with price and output stabilisation

Rationale for action

- Cost of “high debt” crises
- Systemic risk
- Other instruments may fail

Conclusions

- Household debt has risen in most OECD countries over the past two decades
- Household debt may entail risks for households, the financial system and the wider economy. Hence, it needs to be watched closely
- Micro-data on debt and assets need to become more widely available to allow better risk assessments
- Micro-prudential: monitor the quality of underwriting
- Macro-prudential: key to dealing with the credit/housing cycle, but work-in-progress
- Monetary policy: last line of defence
- A holistic approach to housing markets is needed

Thank you!