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Effectiveness of macroprudential policies under borrower heterogeneity[☆]

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Abstract

We study the impact of macroprudential policies using a novel model which takes into account households' ability to borrow under different loan-to-value ratios which are tied to their collateral values. Such model generates a larger amplification in real and financial variables, compared to standard models that assume homogeneity in the leveraging and deleveraging process.

Conditional on this model, we consider the implications of macroprudential policies that aim to lean against an excessive credit cycle. In particular, we allow macroprudential authorities to tighten excessive lending to higher leveraged households, whose riskiness had been evaluated too optimistically. We find that a policy that targets only the group of households that most strongly deleveraged after an adverse idiosyncratic housing investment risk shock, is welfare-improving at social and individual levels, relative to a macroprudential policy which targets all households in the economy.

Keywords: Endogenous Loan-to-Value ratio, Heterogeneity, Macroprudential Policy
JEL-Codes: E23, E32, E44

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