Household Indebtedness and Financial Fragility

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Household Indebtedness and Financial Fragility

by Tullio Jappelli, Marco Pagano, and Marco di Maggio

Discussion by Enrica Detragiache
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Household Indebtedness

• Most research on financial sector and macro does not distinguish between household credit and enterprise credit
• Do we need to draw this distinction?
• Why?
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• Financial development and growth:
  – Not clear why more credit should foster long-run growth if it goes to finance consumption. Mortgage lending may foster growth in the real estate sector, maybe...
  – In addition, more HH credit may lower aggregate savings, which may reduce growth if international capital markets are segmented
  – If international capital markets are segmented, more HH credit may crowd out enterprise credit. This may reduce growth
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- Determinants of financial development:
  - Macroeconomic conditions
  - Basic institutions
  - Contractual institutions
  - Financial sector policies

- Do these factors play different roles in the development of HH credit markets than entreprise credit markets?
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Financial fragility:

• Is credit to HHs a particular source of stability or instability?
• Ex. Credit booms can be associated with sharp downturns and bursting bubbles. Are booms involving lending to HHs more likely to end in tears?
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This paper

– Part I: Determinants of HH credit
– Part II: Determinants of arrears on HH credit in EU
– Part III: Determinants of HH insolvencies in UK, US, Germany
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- Part I: Determinants of HH credit
- Cross-section of 45 countries—2005
- Main findings:
  - HH credit is larger in countries with
    » High GDP per capita
    » Efficient judiciary
    » Well-developed credit registries/bureaus
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• Suggestions:
  – Discuss magnitudes:
    » Example: if Italy’s judicial efficiency was at the sample mean, HH credit-to-GDP would increase by about 10 percentage points. This is large!
  – Compare results with literature on private credit: are the determinants different?
  – Try to get data on creditor rights in personal bankruptcy (LLSV data are on corporate bankruptcy)
  – Control for inflation
  – Control for property rights institutions
  – Control for foreign bank presence
  – Forget the Gini coefficient
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• Part II: Determinants of arrears on HH credit in EU countries
  – Data are from HH survey. Fraction of HHs is arrears relative to HHs in survey:
    » Could the increase of the % in arrears simply reflect an increase in the number of HHs with outstanding debt?
    » Can this be corrected by using survey information?
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• Determinants of arrears on HH credit in EU countries

  – Findings (after controlling for country fixed effects):

  » More HHs are in arrears when unemployment is high and when the aggregate stock of HH debt is high
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• Comments:
  – Hard to draw policy conclusions, as in all papers on loosening lending standards:
    • Do more arrears mean that there should have been less lending in the first place?
    • Any expansion in the market is likely to entail lending to more “marginal” customers. Where should the line be drawn?
    • To get at financial fragility we may have to look at the effects on the lenders....
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Part III: Determinants of HH insolvencies in UK, US, Germany

Findings:
- A larger stock of HH debt is associated with more insolvencies
- Reforms that make it less costly for borrowers to discharge debt in bankruptcy lead to more insolvencies
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Comment: To evaluate the effects of bankruptcy reforms:

a) need to allow for a sufficient lag so that lending policies can adjust

b) need to consider the effect on lending volume as well as insolvency rates: if pro-debtor reforms are followed by an increase in lending, hard to argue they are bad....