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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?

Household Indebtedness

- 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**

Household Indebtedness

- 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 enterprise credit markets?

Household Indebtedness

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?

Household Indebtedness

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

Household Indebtedness

- 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

Household Indebtedness

- 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

Household Indebtedness

- Part II: Determinants of arrears on HH credit in EU countries
 - Data are from HH survey. Fraction of HHs in 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

Household Indebtedness

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....