



Cheap Credit, Expensive Houses? by Claire Labonne and Cécile Welter-Nicol

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Overview

- Housing and macro-prudential policy objectives can be misaligned.



- At the centre of this tension: **the Interest-Free Loans (IFL) policy** in France.



- They use this subsidized loans (**max amount IFL loans**) as an **instrument** both for:
 - **Credit Supply** : Credit → Housing Prices.
 - **LTV**: Credit conditions → Homeownership Accession.

General comments

- A small Introduction on the **French environment** maybe helpful:
 - Housing market resilient during crisis (D>S),
 - Low DTI but high LTV ratios,
 - “The increase in borrowing capacity can explain about 60% of the rise in existing home prices through 2011” (CAS, 2011).
- **Comparison with similar policies** in other countries is missing:
 - Mortgage Interest Relief at Source, MIRAS (UK),
 - Preferential loan program for low-income households by municipalities (DE)
- What are the **Interactions with other existing real estate incentives?**
 - Tax incentives such as the Scellier regime (no local but time variation),
 - temporary creation of the French Financing Corporation (SFEF) to support banks’ funding.
 - Common shocks?

Identification strategy

- The IFL is a good instrument under two conditions:

1. Is correlated with credit supply

Policy variation:

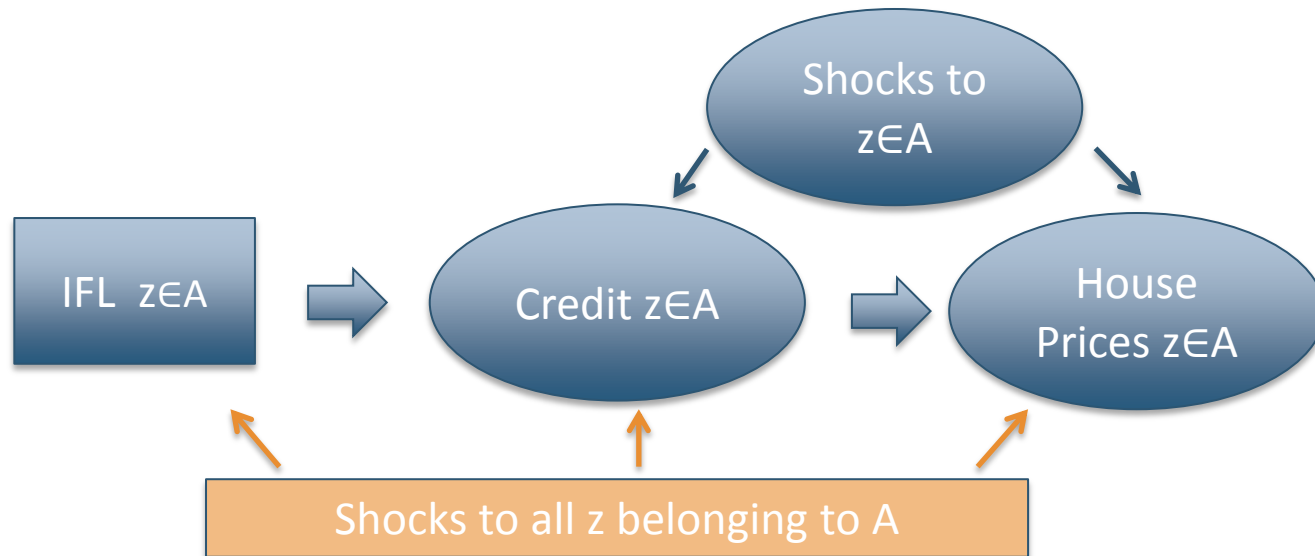
- local (4 areas)
- time (3 reforms 2010-2011)...

2. It is exogenous to price shocks

Endogenous to local housing market conditions

- ... France has about **36000 municipalities**
- IFL differentiated in **4 housing policy areas** (according to local housing conditions)
- Data on **6000 Zip-code**
- They Sample only Zip-code sitting on either side of housing policy zones
- **Imprecise classification for bordering ZIP codes** is at the basis of the **exogeneity of IFL** policy variation to house prices shocks within the sample.

IFL Exogeneity



- Bordering ZIP code have similar market conditions but different subsidy levels
- For those ZIP code IFL policy affects house prices only through Credit Supply
- What about **common shocks**?
- IFL endogeneity is not completely eliminated using bordering ZIP codes.

IFL and house prices

$$M_{z,t} = \beta^{(1)} IFL_{amount,z,t} + \gamma^{(1)} X_{z,t} + \mu_z + \varepsilon_{z,t}$$

$$P_{z,t} = \beta^{(2)} M_{z,t} + \gamma^{(2)} X_{z,t} + \mu'_z + \varepsilon'_{z,t}$$

- Average Housing Loans $M_{z,t}$ are instrumented by average max IFL amount $IFL_{z,t}$ and other borrower characteristics $X_{z,t}$ for Zip code “z” at time “t”.
- Variation in **Equilibrium Credit** $M_{z,t}$ can be due to:
 - Variation in **Credit Supply**
 - Variation in **Credit Demand**
- **↑Equilibrium Credit = ↑Credit supply** if households are credit constrained.
- Pro Credit Supply story.. the policy is aimed at areas with greater housing tensions and to low income borrowers (more likely to be credit-constrained).
- $P_{z,t}$, $M_{z,t}$ and $X_{z,t}$ (average across **all borrowers**) while $IFL_{z,t}$ (average across **eligible borrowers**)... elaborate more which are the possible effects.

Policy implications

“We show an exogenous credit supply expansion spurs both housing prices and homeownership accession”

- Relevant concerns about the effect of such policies on financial stability (do you observe increased delinquencies rates?)
- The paper would benefit from a discussion on the channel through which such policies could affect house prices..
- Is it because banks are willing to lend more? (credit supply shock)
 - IFL Policy works as a down payment
 - Lower capital ratios for the guaranteed part? 0% instead of the 35% risk weight for residential mortgages, Article 125 (1) CRR?.
- Effects of similar future Policies on homeownership accession should be evaluated in the context of current LTV regulation (35% favourable risk weight up to 80% LTV Article 125 (2) (d) CRR)

Minor Comments

- Paper would benefit from a more detailed discussion on representativeness of the sample for the whole France.
- How many municipalities in the sample used for estimation?
- Multicollinearity issues?
 - average income all individual (+) vs average income borrower (-);
 - max IFL is also function of average income observed borrowers.
- Justify more high elasticities (0.5-0.7) credit-house prices comparing to literature (measurement error).
- Title is a bit misleading... Cheap Credit, Expensive houses?

2010h1-2010h2-2011h1

PTZ characteristics			2008	2009 - 2010h1	2010 h2	2011	2012-2014	
Eligibility conditions	Income condition:	A	43 750 €			No condition	60 900 €	
		B1	31 588 €				42 700 €	
		B2						
		C					37 100 €	
Household size		The bigger is the household, the less restrictive the eligibility conditions based on income.						
Housing type		Both new and existing housing are covered.					New housing (existing only social	
Financial characteristics for the borrower	Subsidy rate	Maximum share of operation cost	20% 30 % for tax-free zones and sensitive urban areas	Existing: 20% - New: 30% In tax-free zones and sensitive urban areas : Existing: 30% - New: 40%		Existing: 20% New: between 25 and 40% according to ABC zones Lowered if energetic conditions not met	New: between 24 and 38% according to ABC zones Lowered if energetic conditions not met on new housing	
		Max. share of amount of other loans	50%	50% for existing housing 100% for new housing		100%		
	Max. amount (E = existing, N = new)	A	E	101 250€	101 250€	101 250€	174 000€	
			N	112 500€	150 000€	112 500€	218 000€	
		B1	E	66 000€			130 000€	
			N	82 500€	126 500€	82 500€	164 000€	
		B2	E	66 000€			120 000€	
			N	82 500€	126 500€	82 500€		
		C	E	61 875€			111 000€	
			N	82 500€	103 000€	82 500€		
Repayment schemes		The repayment scheme allows a deferred payment for a fraction of the loan that is decreasing in the household's income	The repayment scheme allows a deferred payment for a fraction of the loan that is decreasing in the household's income but increases with the ABC zone and is higher for new than for existing housing.					
Financial characteristics for the bank			Fiscal deductions compensate for the loss of earnings and its opportunity cost using a rate indexed on the French government bond rate.					