
## 1. IMF'S LATEST HOUSING MARKET ASSESSMENTS

- **Belgium (Selected Issues): A new IMF paper, "analyses the risks of a rapid house price adjustment in Belgium and the potential repercussions for the Belgian economy."** Specifically, "the paper argues that current house prices are closer to their equilibrium than simple historical ratios would suggest and that given the moderate overvaluation, a gradual and limited adjustment seems a plausible scenario."

- **Iceland (Selected Issues): "House prices do not appear to be overvalued or misaligned from fundamentals, based on various approaches."** The paper says that "a time series analysis, cross-country comparison, and parametric estimation all suggest there is no overvaluation in the housing market. The demand-side factors may lead to further increases in house prices, and should be closely monitored to maintain macroeconomic and financial stability."

- **Ireland (Article IV): "Property markets are bouncing back rapidly."** The report notes that "(…) house prices rose 16.3 percent y/y, as fast as the increases during the boom period, though they are still 38 percent below peak."

- **Malaysia (Article IV): "Although there are signs of cooling in the housing market and personal lending growth has been curtailed, financial vulnerabilities remain due to high household debt and elevated house prices," according to the new IMF report.** The report says: "House prices have risen steadily (...) outpacing incomes and rents. Although population growth is strong this cannot fully explain the increase in house prices compared with other countries. However, there are tentative signs of cooling in the housing market in Kuala Lumpur. Residential supply is increasing (…) and is particularly strong in Johor and has recently recovered in KL."

- **Malta (Article IV): Core domestic banks are exposed to the housing market, says the latest IMF report on Malta.** The report notes that "After a period of downward correction in 2008-09, Malta's housing market seems to have stabilized." However, "One of the main risks facing core domestic banks relates to their exposure to the real estate sector. Around two thirds of loans extended by banks are secured with real estate collateral, and mortgages are one of the few segments of bank loans which have been increasing recently (…). This risk can be exacerbated by the weak performance of the EU countries, generating negative spill-over effects on the Maltese economy and its financial sector."

## 2. An interview with Lars E.O. Svensson

Professor Lars E.O. Svensson is a Resident Scholar in the IMF's Research Department during 2015. He is a Visiting Professor at the Stockholm School of Economics since 2013 and an Affiliated Professor at Stockholm University. Previously, he was Deputy Governor of Sveriges Riksbank from 2007 to 2013. Prior to his appointment, he advised the Riksbank for over 15 years while teaching at Stockholm University and later at Princeton University. He has been a member of the Monetary Policy Advisory Board and the Economic Advisory Panel of the Federal Reserve Bank of New York. He has published extensively in scholarly journals on monetary economics and monetary policy, exchange-rate theory and policy, and general international macroeconomics. In the interview below, Professor Svensson presents his views on role of monetary policy and household debt in the housing market.

- **Hites Ahir:** *The need to keep monetary policy rates low to support an ailing economy, but at the same time, manage a boom in the housing market—that's the scenario in which many policymakers around the world find themselves in. How should policymakers approach this type of scenario?*

  **Lars E.O. Svensson:** First, one must identify what problems one needs to solve while keeping in mind the available policies and policy tools, the objectives of these policies, and what the policies can achieve.

  Let me start with monetary policy. With flexible inflation targeting, the objective of monetary policy is to stabilize inflation around the inflation target and resource utilization around a long-run sustainable rate. The main policy instruments are the policy rate and communication, including forward guidance. When the policy rate is constrained by its effective lower bound (which is not zero but negative and not hard but soft), unconventional policies such as large-scale asset purchases (quantitative easing) and exchange-rate policies (foreign-exchange interventions and currency floors) can also be used.

  It is important to remember the limitations of monetary policy. Monetary policy cannot achieve financial stability. For that, you need financial-stability policy, that is, macro- and microprudential policy and corresponding supervision and regulation. Monetary policy cannot solve structural problems. For that, you need the appropriate structural policy or policies.

  If the forecasts for inflation and resource utilization in an economy are below the inflation target and a long-run sustainable rate, respectively, expansionary monetary policy is called for, in the form of a real policy rate below the neutral real interest rate or, if that is prevented by the effective lower bound, unconventional policy instruments.

  Suppose that the economy is also experiencing a housing boom, in the form of rising housing prices. Whether that calls for additional policy action depends on whether the boom is a problem or not. Rising housing prices need not be a problem. If the general level of interest rates falls because the neutral real interest rate falls, equilibrium housing prices will rise, everything else equal, since equilibrium housing prices reflect the present value of future housing services. In this context, it is important to remember that the neutral real interest rate is not determined by monetary policy but by underlying structural factors, such as a "saving glut", demography, and potential-growth prospects. Monetary policy can only make the actual real policy rate deviate above or below the neutral real rate for a few years, but it does not determine the neutral real rate.

Thus, whether rising housing prices is a problem or not requires thorough analysis. Are the rising prices the natural response to rising disposable income, falling equilibrium mortgage rates, or reduced effective housing taxes? Are they the consequence of an urbanization process from rural regions with low and stagnant housing prices to congested urban regions with increasing prices due to high demand and limited space for new housing? Is construction limited because of regulation and zoning restrictions? Or are the rising prices the consequence of falling mortgage lending standards or increasing loan-to-value ratios? Are they due to increasing buy-to-live or buy-to-let? Are the housing costs for owner-occupied housing, including mortgage debt service, raising rapidly above rents and are they becoming unsustainably high relative to disposable incomes? Are the rising housing prices due to unrealistic expectations of future housing prices or mortgage rates? Are the new higher housing prices sustainable or not? Are the rising housing prices resulting in mortgage equity withdrawals that finance excessive consumption, revealed by unsustainably low or even negative household saving?

How are household balance sheets evolving? Are loan-to-value and net-wealth-to-total-assets ratios reasonable? Are borrowers' repayment capacity and resilience to shocks such as increasing mortgage rates, housing price falls, and income losses due to unemployment satisfactory?

Thus, only after analyzing the situation and answering questions such as those above can it be determined whether the rising housing prices are a problem and, if so, what the nature of the problem is. And only after the nature of the problem has been clarified can it be determined what the appropriate policy is to handle the problem. Depending on the nature of the problem, the appropriate policy may be housing, macroprudential, or fiscal policy, or a combination of those.

- **Hites Ahir:** *Can monetary policy be used to manage problems associated with a housing boom?*

**Lars E.O. Svensson:** It has been suggested that monetary policy should be leaning against the wind of rising housing prices and household debt. Here, "leaning against the wind" means tighter policy than justified by stabilizing inflation around the inflation target and resource utilization around a long-run sustainable rate. It means accepting average inflation somewhat below target.

If the inflation target is credible, so inflation expectations are anchored at the target, it means that average inflation will fall below inflation expectations. Then there will be costs in the form of higher average unemployment that exceeds the long-run sustainable rate.

If inflation expectations instead adjust downwards, meaning that the credibility of the inflation target is lost, there may be less costs in the form of higher unemployment, but the loss in credibility may make it more difficult to achieve the inflation target in the future. Furthermore, the combination of low inflation and low inflation expectations makes the economy more vulnerable to negative shocks and increases the risk that the economy gets stuck in a liquidity trap with a binding effective lower bound for the policy rate.
Thus, leaning against the wind has a substantial cost in terms of a worse macro outcome during the next few years and an increased risk of being trapped with a binding effective lower bound for the policy rate. What are the potential benefits? A possible benefit is that somewhat higher policy rates and thereby mortgage rates may dampen the growth of housing prices and thereby that of household debt. Furthermore, less household debt might reduce the probability of a future crisis and/or the depth of a crisis in case it would occur. Thus, the potential benefit is a better expected future macroeconomic outcome. If the benefit exceeds the cost, leaning against the wind is arguably justified. But this requires a *quantitative* assessment of the cost and benefit. A gut feeling is not enough.

In assessing the policy-rate impact on household debt, one has to take into account that nominal household debt displays considerable inertia, because the average length of mortgages is several years (about seven years in Sweden), so only a fraction of mortgages turn over each year. Furthermore, tighter monetary policy dampens the growth of both the price level and nominal disposable income. Thus, tighter policy slows down both the numerator and the denominator of both real debt and the debt-to-income ratio. Thus, the net effect of higher policy rates on real debt and debt-to-income is likely to be quite small. According to estimates published by the Riksbank the effect in Sweden is indeed very small and not statistically significant from zero. Higher policy rates may even increase the real debt, if the policy rate has a faster and bigger impact on the price level and disposable income than on nominal debt, as I have argued in a paper. Using also estimates of the how the probability of a crisis depends on real debt (Schularick and Taylor 2012) and how the depth of crisis depends on initial household debt (Flodén 2014), it then possible to estimate the benefit of leaning against the wind. Using estimates of the impact of the policy rate on unemployment (for instance, Riksbank estimates in its *Monetary Policy Report*), it is possible to estimate the cost in terms of unemployment of leaning against the wind. A comparison of the cost and benefit in the Swedish case shows that the benefit is about 0.4 percent of the cost. That is, according to this calculation, using Riksbank and other estimates, the cost is about 250 times the benefit. (Svensson 2015). According to these calculations, leaning against the wind is clearly not justified.

Furthermore, leaning against the wind has an additional cost when the inflation target is credible and household inflation expectations are anchored at the target. Inflation below household inflation expectations imply that the real debt burden becomes higher than anticipated and planned for. In the Swedish case, during the last three years, households have expected inflation to be around 2 percent of the inflation target. But the price level has instead been approximately constant during the last three years. This means that the real value of a fixed nominal debt has increased by 6 percent during the last three years compared to if inflation had equaled the target (Svensson 2015). This is a substantial increase in real debt burden of households and if anything increases any risks associated with household debt.

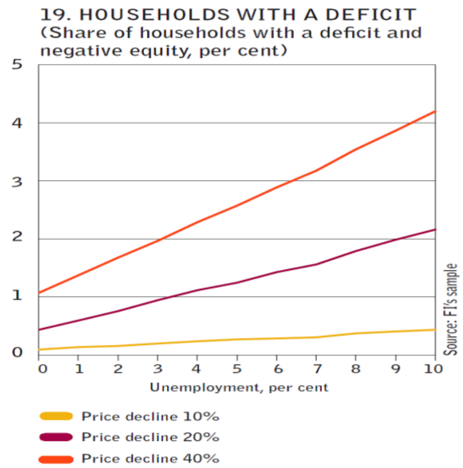
The conclusion is that monetary policy is not suitable to handle problems with rising housing prices and household debt. Leaning against the wind indeed seems inherently flawed as a policy to manage such problems. So, there is no choice but to use other policies, such as macroprudential policy, housing policy, or fiscal policy.

- **Hites Ahir:** *How can policymakers assess whether household debt poses a problem?*

  **Lars E.O. Svensson:** For assessments of whether household debt is a problem or not, the annual *Mortgage Market Report* of Finansinspektionen, the Swedish Financial Supervisory Authority, provides a good model. In this annual report, Finansinspektionen uses individual data on new borrowers collected from the banks to assess the banks' lending standards and the borrowers' repayment capacity. Furthermore, stress tests on the individual data are used to assess the borrowers' resilience to shocks in the form of mortgage-rate increases, housing-price falls, and income falls due to unemployment. After detailed and thorough analysis, the assessment of Finansinspektionen in its reports of the last few years is that the banks' lending standards are high, that the new borrowers' repayment capacity and resilience to the shocks mentioned are good. In my mind, this report is the single best source of information about any risks associated with the Swedish housing and mortgage market.

  As an example, in one of the stress tests in the report, the new borrowers are subject to both a fall in housing prices and an income fall due to an increase in the unemployment rate. The question is what fraction of the new borrowers would after such a shock face the difficult situation of having both a deficit in a so-called left-to-live-on analysis and negative equity in their housing (that is, a loan-to-value ratio above 100 percent). In a left-to-live-on analysis, the household's discretionary income, the household's disposable income after paying housing costs and standardized costs of obtaining a reasonable consumption standard, is calculated. A deficit in such an analysis means that the household has to obtain a temporary relief from its debt service, reduce its consumption, use up its savings, or sell its property. If the household chooses to sell its property, negative equity means that the household has to realize a loss.

  Figure 19 from the *Mortgage Market Report* 2014 (p. 17) presents the result of this stress test. The figure shows that a 10 percentage increase in the unemployment rate and a fall in housing prices of 20 percent would put only about 2 percent of the new borrowers in the above difficult situation. This small fraction indicates substantial resilience of the new borrowers. The report further notes that the loans of such households only account for just below 2 per cent of the total lending volume to new borrowers. Furthermore, the old borrowers are on average more resilient than new borrowers, since old borrowers have on average benefitted from previous increases in housing prices and disposable income and have lower loan-to-value and debt-service-to-income ratios.




- **Hites Ahir:** *So, if monetary policy is not suitable, how can any problems with household debt be handled?*

  **Lars E.O. Svensson:** As I said, it is important to first clarify and analyze what the potential problem is, and the appropriate policies depend on the precise problem found. As an example, in the Swedish case, the household debt-to-income ratio was growing rapidly before 2010, although real and financial assets were also growing at least as fast as debt. The household savings ratio was increasing to historically high levels. Nevertheless, as a precaution, in October 2010 Finansinspektionen introduced a loan-to-value cap of 85 percent for new mortgages.

  Since then, the debt-to-income ratio has been approximately flat. The loan-to-value ratio for new mortgages has stabilized around 70 percent, meaning that the average down payment and equity for new borrowers is 30 percent, a sizeable buffer against any fall in housing prices. Finansinspektionen has also increased banks' risk weights on mortgages to 25 percent and increased capital requirements on systemically important banks to a high 16 percent for the Basel III Tier 1 Capital Ratio. It has also proposed that banks' shall propose individual amortization plans for borrowers. It has refined its annual *Mortgage Market Report* to provide even better monitoring of banks' lending standards and borrowers' repayment capacity and resilience to shocks.

  Finansinspektionen is currently working on a proposal of compulsory amortization –a proposal I personally think is unnecessary, since borrowers' repayment capacity and resilience to shocks is good, households' saving ratio is historically high, and substantial voluntary amortization is already taking place.

  Thus, Sweden and Finansinspektionen provides an example of active and arguably good macroprudential policy. But each country's macroprudential and other policy actions need to be tailored to the particular problems and issues in that country. The situation varies a lot from country to country. There is no one size that fits all.

## 3. THE RISE OF A GLOBAL MARKET IN HOUSING: AN UPDATE

- **"When price-to-income or price-to-rent ratios get out of whack, it's often a sign of a housing bubble. But the story in Vancouver is more interesting. Almost by chance, the city has found itself at the heart of one of the biggest trends of the past two decades—the rise of a truly global market in real estate,"** James Surowiecki reported in a *New Yorker* article of May 2014. Recently, there have been a lot of stories on how the housing market continues to become more globalized.
  - ✓ *What are the latest stories?* "Buying upscale homes in the U.K. through trust funds and overseas-based companies is popular among the rich as a way to minimize taxes and protect privacy," Bloomberg reports. Similarly, in an extensive series of articles, the *New York Times* "examined the influx of global cash fueling the city's high-end real estate boom." Moreover, "(…) Government Pension Fund of Norway, the world's largest sovereign-wealth fund, last year purchased $7.6 billion worth of property globally, more than any other sovereign fund, (…)" according to the *Wall Street Journal*. Similarly, "Asian investors shelled out US$40 billion (…) on property around the world in 2014, up 23 per cent over 2013," notes the *Strait Times*. And "By a wide margin, the U.S. was voted the most stable and secure country for investment, outstripping both second-place Germany by 55 percentage points, and third-place U.K. by 60 percentage points (…) Two-thirds of survey respondents expect China to become the largest source of capital into the U.S. in 2016 and beyond; ten percent expect that could happen as early as 2015. Seventy-two percent of survey respondents said they expected this investment to be a long-term, permanent inflow," according to the latest survey from the *Association of Foreign Investors in Real Estate* (AFIRE).

  - ✓ *What has been the latest reaction to these developments?* Using data from the Metropolitan Police investigations and Land registry record of corporate holdings of property in England and Wales, *Transparency International UK* finds that "(…) property in the UK can be acquired anonymously through companies registered in secrecy jurisdictions and anti-money laundering checks can be bypassed with relative ease (…) Transparency International's key recommendation is that transparency should be established over who owns the companies that in turn own so much property in the UK." Moreover, The Australian government announced plans to charge fees to foreign buyers who invest in the housing market. Specifically, the government will charge "foreign home-buyers A$5,000 for properties valued under A$1 million and an additional A$10,000 for every additional A$1 million" (*Reuters*). The *New York Times* reported that "17 nonprofit organizations (…) urged the Treasury Department to require that the real estate industry verify the identities of buyers and screen them for potential money-laundering risk."

  - ✓ *Other views from a recent conference—Global Real Estate: Where Does Smart Capital Flow?* Two themes emerged from the conference. First, the speakers at the conference are optimistic about the outlook for capital flows into real estate. Second, when investing in real estate in emerging markets, due diligence remains important, and even more important and critical is to have a good local partner. The conference was organized by the Center for Real Estate and Urban Analysis of George Washington University.

## 4. THE CORDON: OTHER VIEWS AND ANALYSIS ON HOUSING MARKETS

- **Cross country:** The Use and Effectiveness of Macroprudential Policies: New Evidence (IMF Working Paper) | Resolving Residential Mortgage Distress: Time to Modify (iMFdirect) | Global House Price Index - Q4 2014 (Knight Frank) | Q4 2014: The global property markets: slowdown in Asia, US, Dubai and the Pacific, but Europe's boom accelerates (Global Property Guide) | How to ensure the lowest paid aren't forced out of cities (Financial Times) | The Emerging Markets Housing Bubble (Huffington Post) | A Tale Of 2 Bubbles (Seeking Alpha) | Asia's housing bubbles look a lot like the U.S. housing bubble did (Washington Post) | Deciphering the fall and rise in the net capital share (Brookings, Economist) | Mortgaging the Future? (Federal Reserve Bank of San Francisco) | How Long Can Central Bankers Ignore Bubbles? (Wall Street Journal) |

- **New Book:** When the Bubble Bursts: Surviving the Canadian Real Estate Crash by Hilliard MacBeth (Amazon, Mortgage Broker news) |

- **Argentina:** Investors Getting Ready For Argentina's Real Estate Resurrection (Forbes) |

- **Australia:** Strengthening Australia's Foreign Investment Framework (Treasury) | Australia's property market joins closed-door club (Reuters) | Why Sydney's property market is running so hot (Business Spectator) | 'We are driving very fast without seat belts': Experts warn of new asset bubble (Sydney Morning Herald) |

- **Canada:** Canada's Financial Sector: How to Enhance its Resilience (iMFdirect) | The full Hilliard MacBeth interview (Mortgage Broker news) | Oil price plunge pulling Calgary's housing market down with it (Reuters) | 'Corrections In Progress' In Most Canadian Housing Markets: Teranet (Huffington Post) | Canadian Housing Market Scorecard (BMO) |

- **China:** China's Real Property Problem (Bloomberg) | Chinese Rushing to Buy Property for Portugal Visa Get Burned (Bloomberg) | Do Bank Loans and Local Amenities Explain Chinese Urban House Prices? (SSRN) | Bubble or Riddle? An Asset-Pricing Approach Evaluation on China's Housing Market (Nanyang Technological University) | In China, a Building Frenzy's Fault Lines (New York Times) | China's house price crisis is creating a perverse bailout bubble for property companies (Business Insider) | The Chinese government thinks it has found the answer to the country's property-market crisis (Business Insider) | Intercity Information Diffusion and Price Discovery in Housing Markets: Evidence from Google Searches (SSRN) | China's developers face more price pain (Financial Times) |

- **Denmark:** Denmark Ready to Intervene in House Market in Euro-Peg Fight (Bloomberg) |

- **Germany:** Germany caps rents to tackle rise in housing costs (Financial Times) | German Resurgence - Which Asset? Stocks, Bunds Or Real Estate? (Seeking Alpha) | Germany's Weidmann Warns of Overvalued Urban Housing (Wall Street Journal) |

- **Hong Kong:** Hong Kong steps up efforts to cool red-hot property market (Reuters) |

- **Indonesia:** Why Jakarta's property boom isn't a bubble (CNBC) | New Roads, Other Infrastructure Driving Indonesia's Housing Market (Wall Street Journal) |

- **India:** Housing Price Indices in India (SSRN) | Union Budget 2015: The nuts and bolts of property tax (Times of India) | India's property hangover: Discounts, gold to cure multi-billion dollar backlog (Reuters) | Modi's money laundering crusade looms over India property bubble (Chicago Tribune) |

- **Ireland:** Irish Home Prices Fall Most Since 2012 Amid New Borrowing Rules (Bloomberg) |

- **Italy:** Fitch: Italy Mortgage Guarantee Scheme Unlikely to Spur Lending (Reuters) |

- **Korea:** Capital Inflow Shocks and House Prices: Aggregate and Regional Evidence from Korea (SSRN) |

- **New Zealand:** Bernard Hickey: Blame it all on Basel (New Zealand Herald) | New Zealand Government Working To Boost Housing Supply, Says Finance Minister (International Business Times) |

- **Norway:** Norway tightens mortgage rules to cool housing market (Reuters) | Norway on Bubble Watch as Anxiety Over Oil Plunge Recedes (Bloomberg) | Norway's central bank is worried about a housing bubble (Business Insider) |

- **Poland:** The Impact of Swiss Franc Loans on Polish Households (CEIC) | The effect of road traffic noise on the prices of residential property – A case study of the polish city of Olsztyn (Elsevier) |

- **Singapore:** Singapore: The Next Global Domino To Fall In Real Estate (Seeking Alpha) | Singaporeans top real-estate buyers among Asians (Strait Times) | How Singapore Fixed Its Affordable Housing Problem (Citylab) |

- **Spain:** Vivienda y su contexto (El Pais) | Un sector menos especulativo (El Mundo) | El precio de la vivienda en España ha tocado suelo, según Fitch (El Pais) |

- **United Arab Emirates:** Dubai property price slide deepens (Financial Times) |

- **United Kingdom:** UK housing inequality grows as generation gap in ownership widens (Financial Times) | Buy-to-Let Booms as BOE Awaits Powers to Curb Mortgages (Bloomberg) | What the latest statistics tell us about housing – in six charts (Guardian) | Property crowdfunding is a good idea — in theory (Financial Times) | Weak foundations (Economist) | Subsidy cuts hit affordable housebuilding (Financial Times) | How do you fix a housing crisis in a time of austerity? (Guardian) | Stamp duty reforms fail to dent record revenues (Financial Times) | Mortgage market hopes for post-election pick-up (Financial Times) | London Super-Luxe Is Cooling. BOE Will Be Watching (Wall Street Journal) |

- **United States:** February Market Reports: Slower and Steadier (Zillow) | Housing and Mortgage Market Review (Arch MI) | Is the government greasing the skids for another housing slump? (American Enterprise Institute) | Credit supply and the housing boom (VOX) | Capitalization of Charter Schools into Residential Property Values (NBER) | Mortgage Rates, Household Balance Sheets, and the Real Economy (NBER) | Prepared Remarks of Melvin L. Watt Director FHFA at the Goldman Sachs Housing Finance Conference (FHFA) | Information Losses in Home Purchase Appraisals (Federal Reserve Bank of Philadelphia) | The "Recovery" in U.S. Housing Prices (EconoMonitor) | The Importance of the Federal Housing Administration in the Housing Market (Center for American Progress) | A legacy of the housing bubble that won't go away: home bidding wars (Washington Post) | A Quantitative Analysis of the U.S. Housing and Mortgage Markets and the Foreclosure Crisis (Federal Reserve Bank of Philadelphia) | Is Timing Everything? Race, Homeownership, and Net Worth in the Tumultuous 2000s (SSRN) | An Extrapolative Model of House Price Dynamics (NBER) | | Supreme Court to rule on underwater loans (Financial Times) | Computational Forecasting with FRED: An Application to State-Level House Prices (SSRN) |

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