



**Housing, Stability and
the Macroeconomy:
International Perspectives**

Federal Reserve Bank of Dallas

Journal of Money, Credit and Banking

International Monetary Fund

**Housing Stability, Systemic Risk
and Securitization**

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This paper was presented at **Housing, Stability and the Macroeconomy: International Perspectives** conference, November 14-15 2013. The conference was sponsored by the Federal Reserve Bank of Dallas, the International Monetary Fund, and the *Journal of Money, Credit and Banking*. The conference was held at Federal Reserve Bank of Dallas (<http://dallasfed.org>).

Federal Reserve Bank of Dallas
Journal of Money, Credit, and Banking (JMCB)
International Monetary Fund
November 14, 2013

HOUSING, STABILITY AND THE MACROECONOMY:
INTERNATIONAL PERSPECTIVES

*HOUSING STABILITY, SYSTEMIC
RISK AND SECURITIZATION*

Susan M. Wachter

*Richard B. Worley Professor of Financial Management
Professor of Real Estate and Finance*



Housing Stability, Systemic Risk and Securitization

- **International House Price Boom-Bust of 2003-2008**
- **Good or Bad Securitization**
- **Implication of the Banking/Financial System**
 - **Real Estate Booms and Banking Busts**
 - **Fundamental Problem of Incomplete Markets and Mispriced Risk**
 - **Banks as Secret Keepers v. Transparency**
- **Securitization as a Solution?**

House Price Boom and Bust in the US



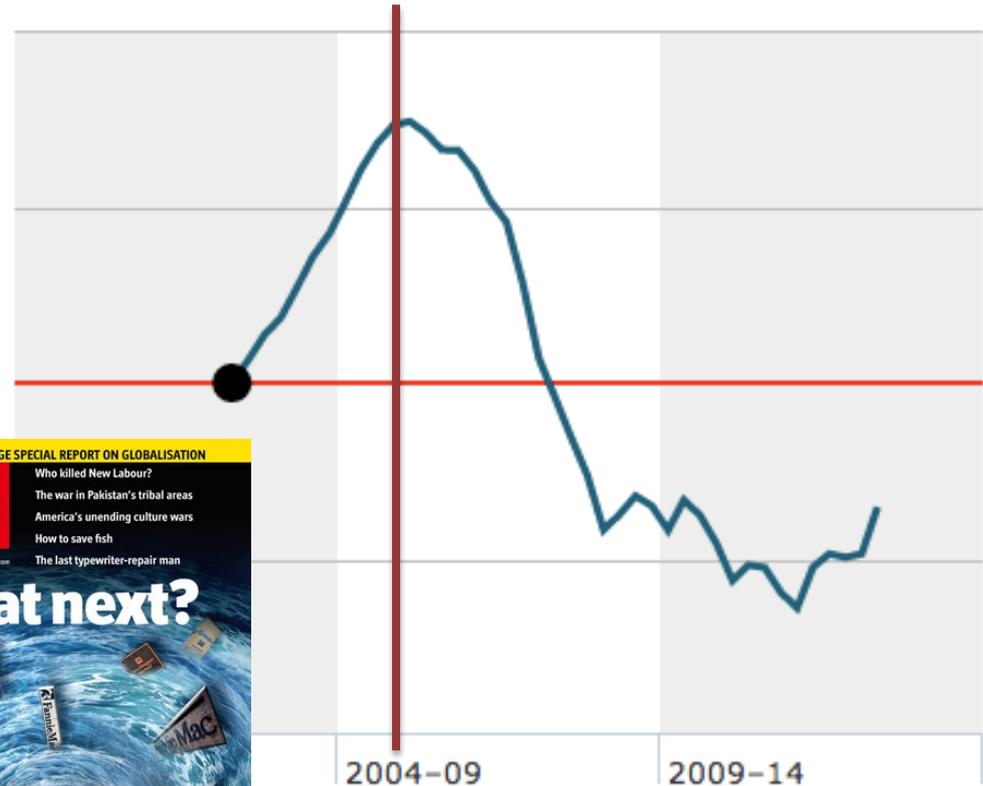
March, 2007



January, 2008



September, 2008



International Headlines 2007-2009

October 10, 2008

September 18, 2007

Darling steps in to halt bank run



UK and Iceland clash on crisis



March 30, 2009

December 22, 2008

Ireland Props Up Three Banks and Takes Control of One
New York Times (1923-Current file); Dec 22, 2008;
 ProQuest Historical Newspapers: The New York Times (1851-2009)
 pg. B3

Ireland Props Up Three Banks and Takes Control of One

By Hansberg News

Ireland will pump 5.5 billion euros (\$7.7 billion) into its three largest banks and take control of the Anglo Irish Bank Corporation to protect the nation's financial services industry from collapse. The government will inject 1.5 billion euros into Anglo Irish Bank in return for preferred shares with 75 percent of its voting rights, the government said on Sunday. The other two banks, Allied Irish Banks and Bank of Ireland, will each receive 2 billion



record pace, home prices have fallen 10 percent in the last year and the economy may shrink as much as 4 percent next year, according to the government. Ireland's financial regulator said on Oct. 14 that the six lenders covered by the government guarantee had about 39 billion euros in speculative property loans. The finance ministry has said that although it has a "substantial pool" of additional capital available it "encourages" the

El Banco de España interviene por fin la CCM tras dos meses de dudas

La decisión de la autoridad monetaria llega tras el rechazo de Unicaja al plan de fusión

El Gobierno garantiza los depósitos con un aval de hasta 9.000 millones

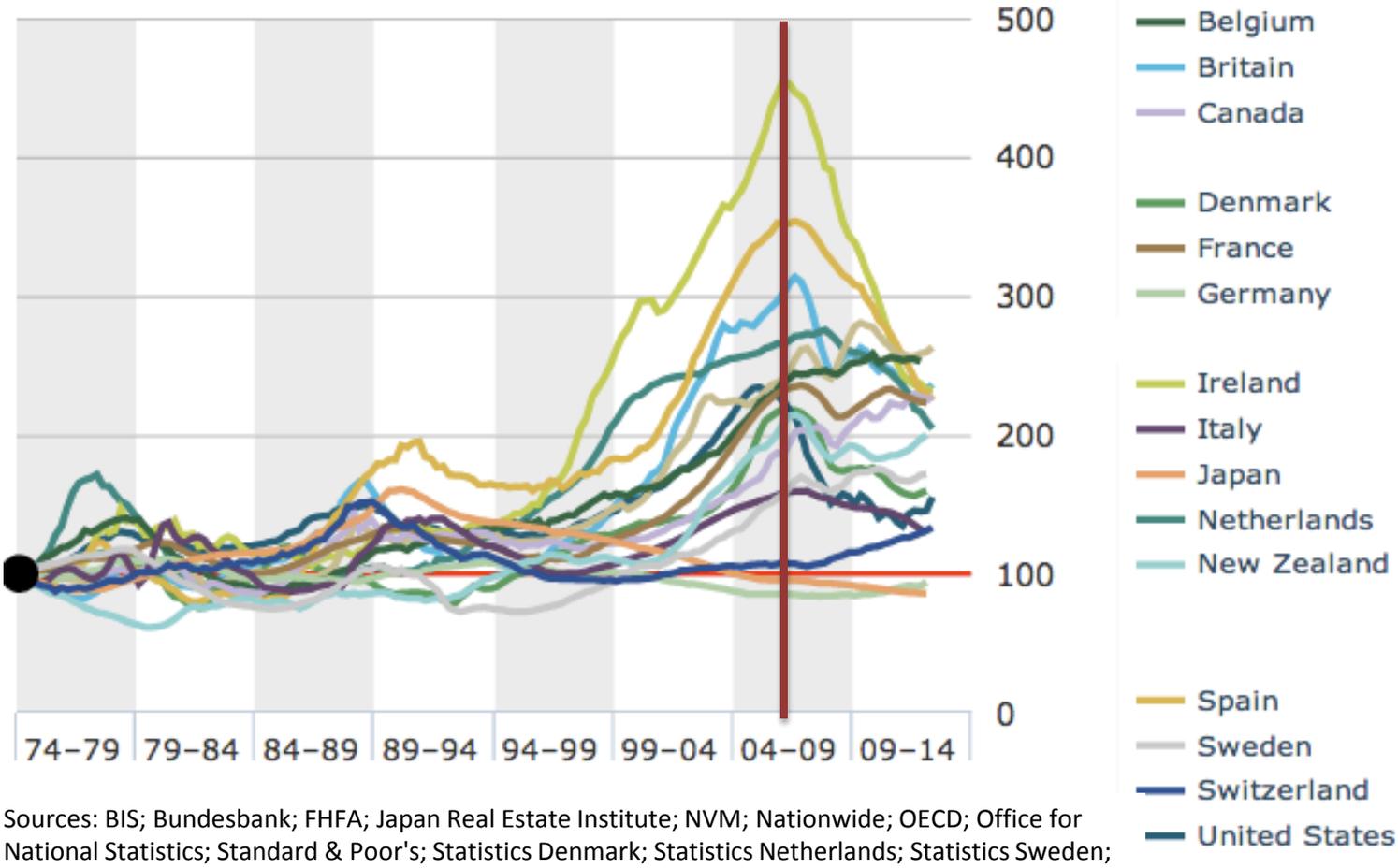
El regulador actúa nada más nombrar subgobernador al ex jefe de Supervisión, Javier Ariztegui

«Ante la crisis del sistema financiero». Tercera de Lorenzo Bernaldo de Quirós; «¿Iráme a los cipos, por Ignacio Camacho»; «El Banco de España empieza a actuar», por Carmelo Tajadura; y «En la Caja de Madrid a la Caja de Pensiones», por José Antonio Neves. Editorial y páginas: 32 a 35



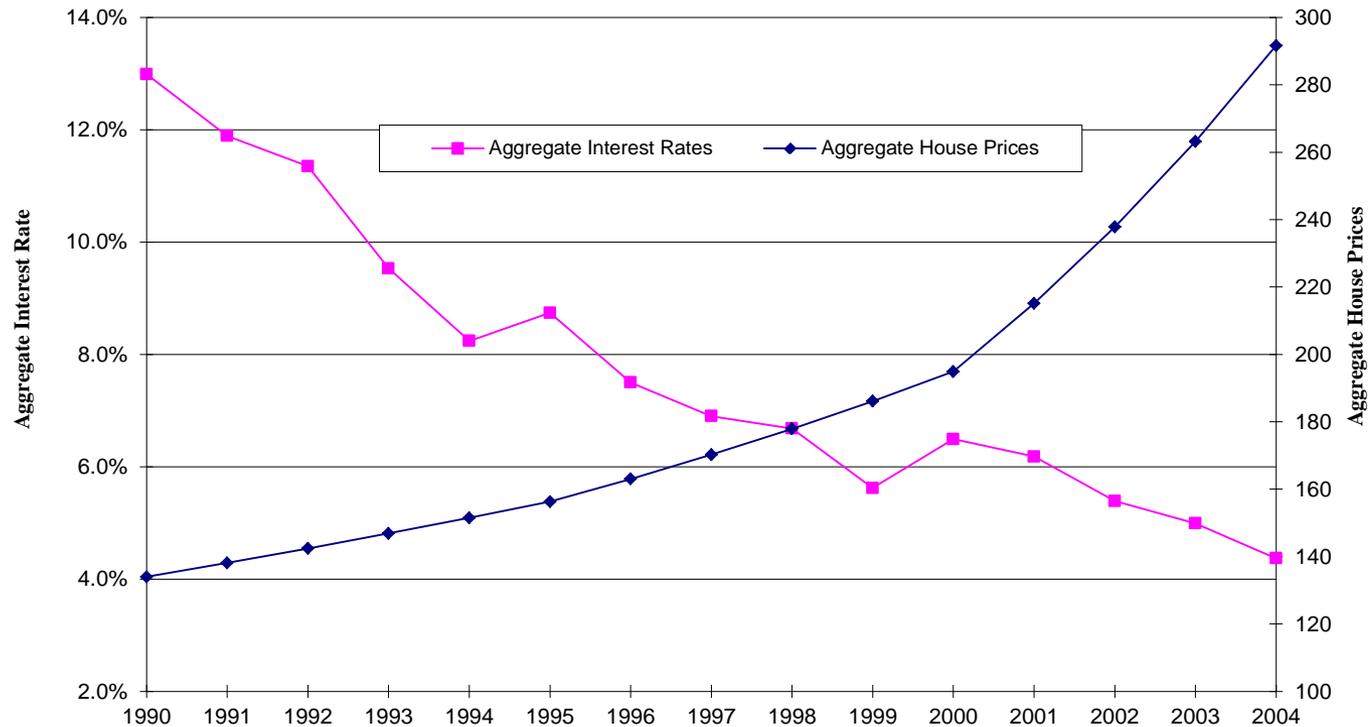
Global Housing Prices Peak in 2007

Q1 1975=100



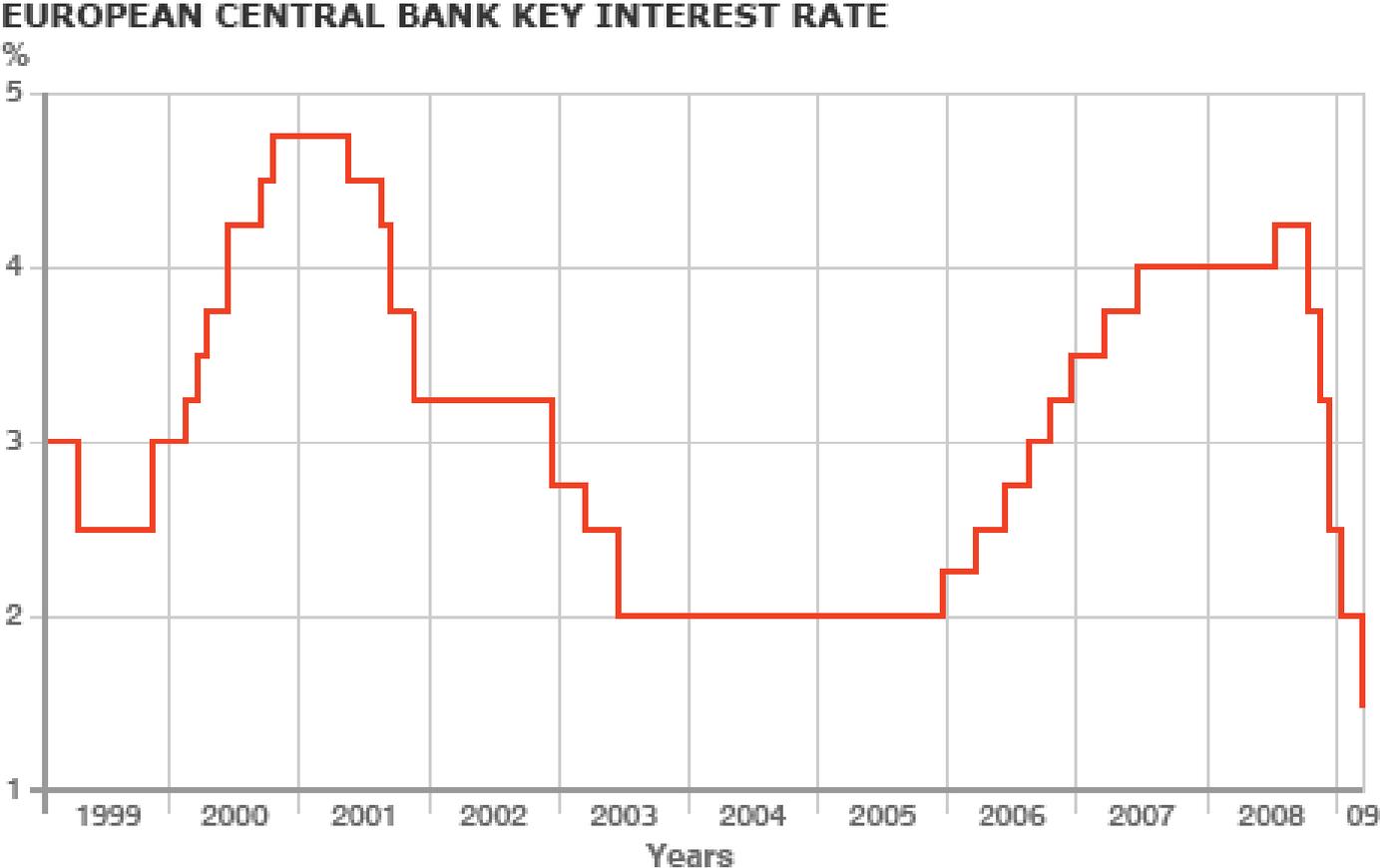
Sources: BIS; Bundesbank; FHFA; Japan Real Estate Institute; NVM; Nationwide; OECD; Office for National Statistics; Standard & Poor's; Statistics Denmark; Statistics Netherlands; Statistics Sweden; Thomson Reuters; vdpResearch

Prices Rise as Interest Rates Decline from 1990-2004



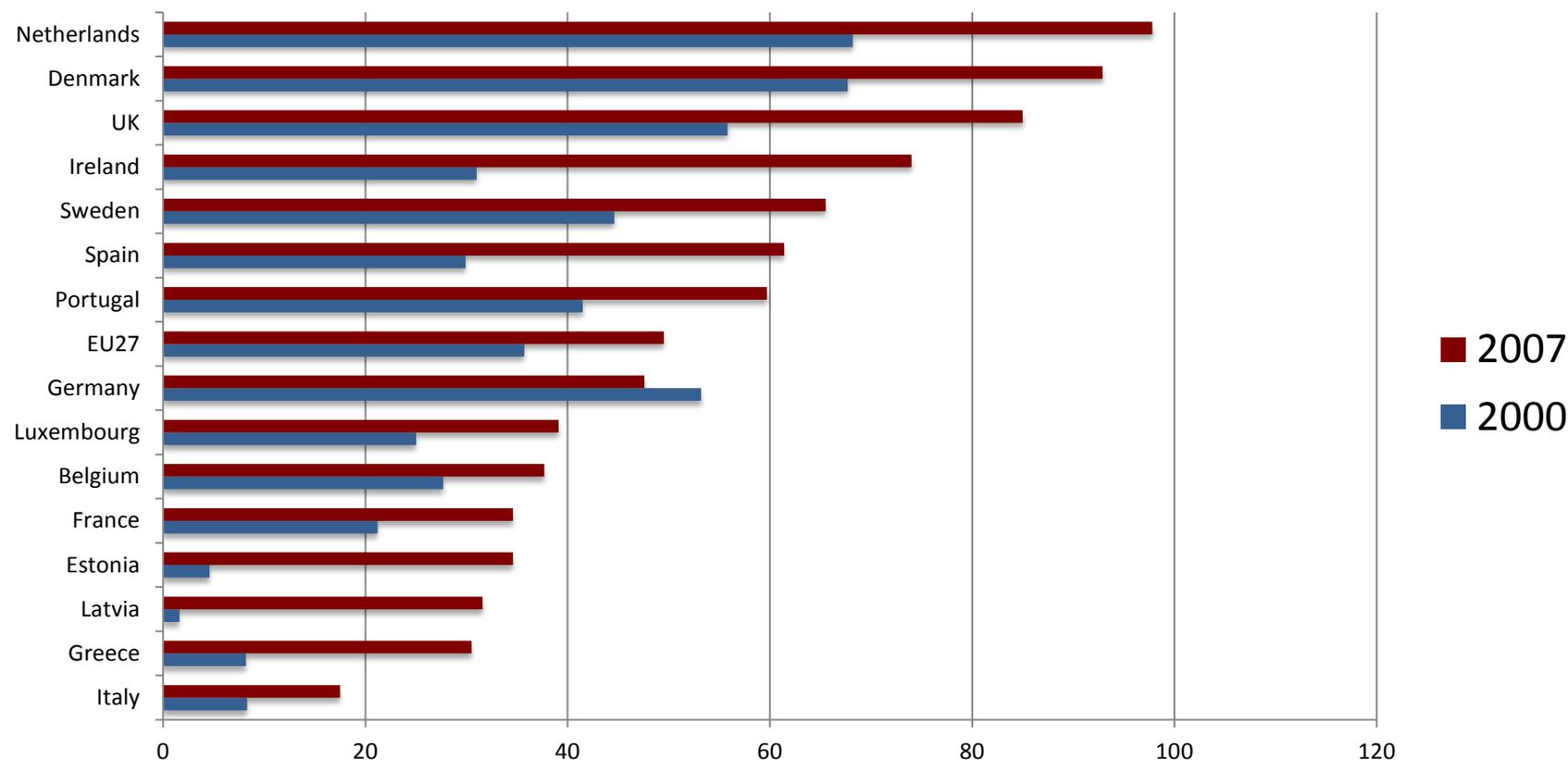
Aggregate values include data from: Spain, Ireland, U.K., Netherlands, Belgium, U.S., Japan, France, Canada, Italy, Australia, Sweden, Germany

Interest Rates Bottom in 2003



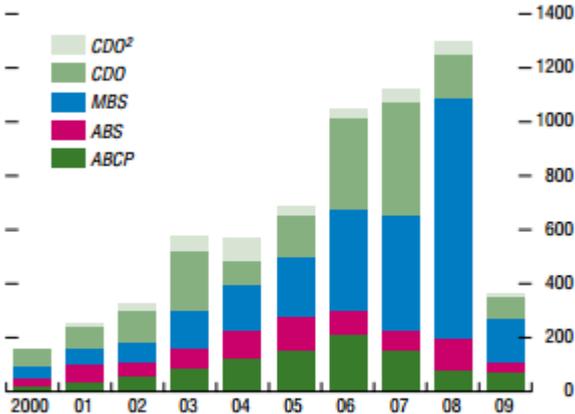
Mortgage Debt to GDP Ratio Grows at 4.8% per Year from 2000-7 and at 4.6% from 2004-7 for the EU27

Residential Mortgage Debt to GDP Ratio, %



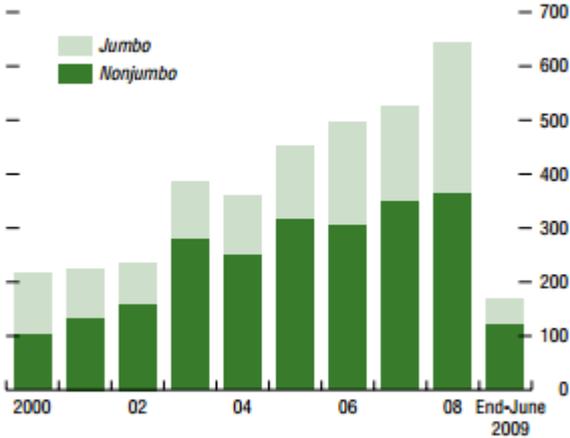
Securitization Takes Off 2003-2008

Figure 2.4. European Private-Label Securitization Issuance by Type
(In billions of U.S. dollars)



Sources: IMF staff estimates based on data from European Securitization Forum; JPMorgan Chase & Co.; and Moody's.
 Note: ABCP = asset-backed commercial paper; ABS = asset-backed security; CDO = collateralized debt obligation; CDO² = CDOs backed by CDO, ABS, and MBS; MBS = mortgage-backed security. Data for 2009 through end-June. For ABCP, 2009 data through end-May. ABCP data represent period-end outstandings.

Figure 2.9. Global Covered Bond Issuance
(In billions of euros)



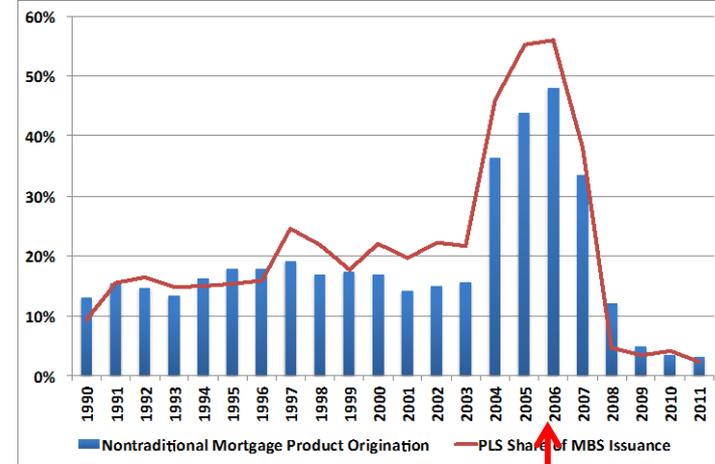
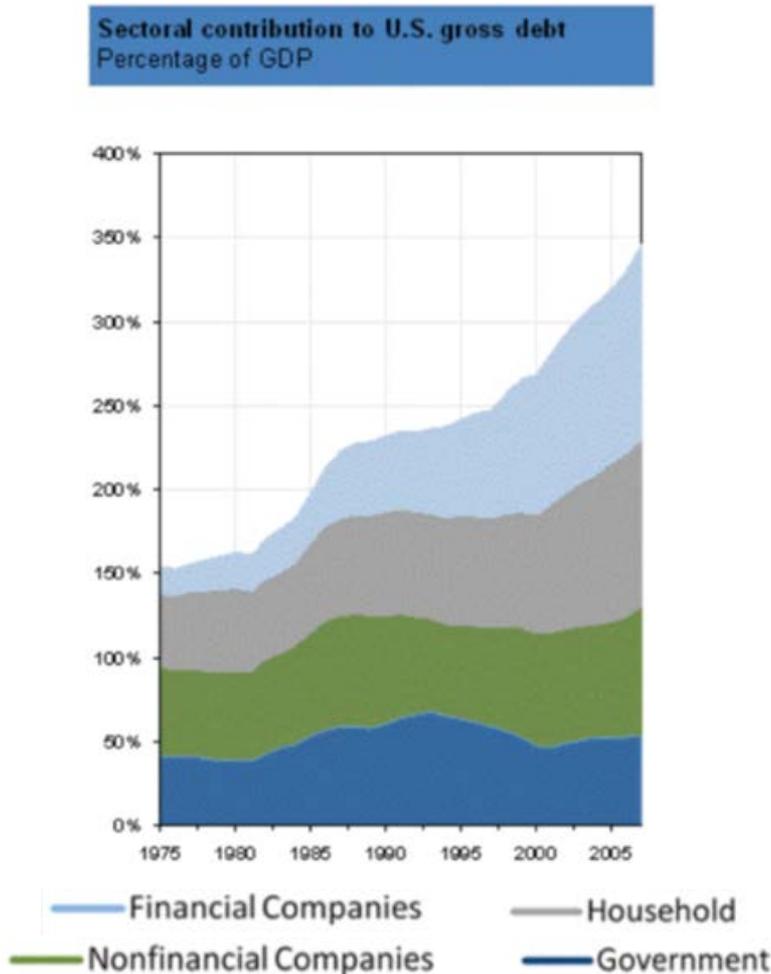
Sources: European Covered Bond Council; European Securitization Forum; Barclays Capital; Société Générale; and Dealogic.

World Economic and Financial Surveys October 2009
 “Global Financial Stability Report: Navigating the Financial Challenges Ahead”
 ©2009 International Monetary Fund



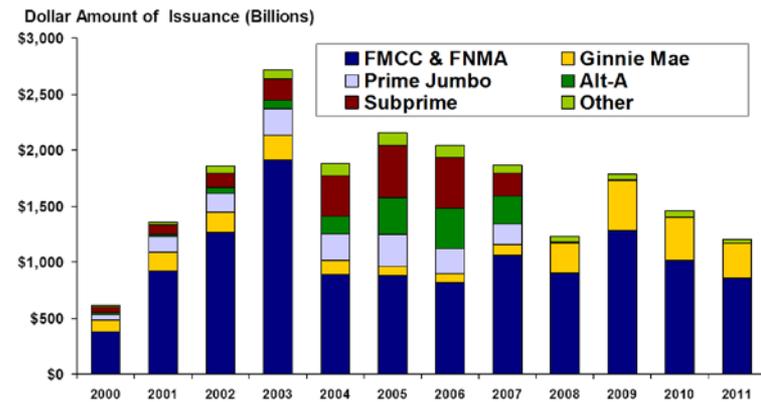
Mortgage debt to GDP rise results in systemic risk

Market Share of Nontraditional Mortgage Products and Private Label Securitization



Source: Inside Mortgage Finance 2012 Mortgage Market Statistical Annual. Nontraditional mortgage products are subprime, Alt-A and home equity loans.

MBS Issuance: Subprime and alt-A at 0 by 2008

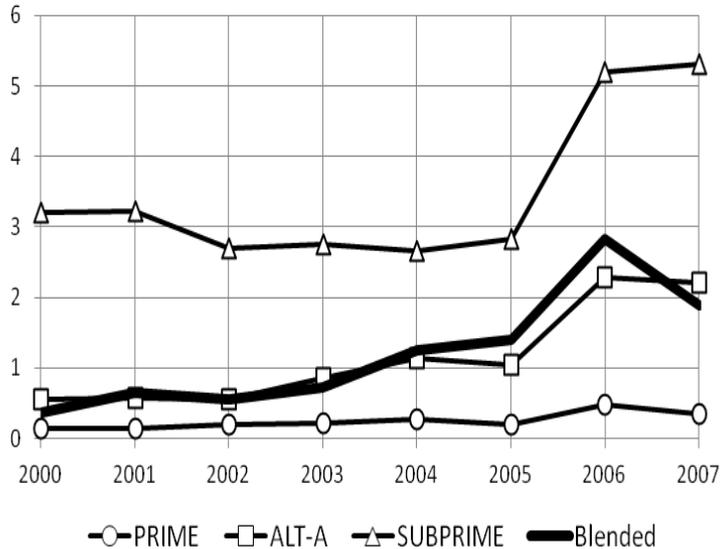


Sources: Inside MBS & ABS (The 2011 Mortgage Market Statistical Annual - Volume I), Inside MBS & ABS (February 3, 2012 issue).

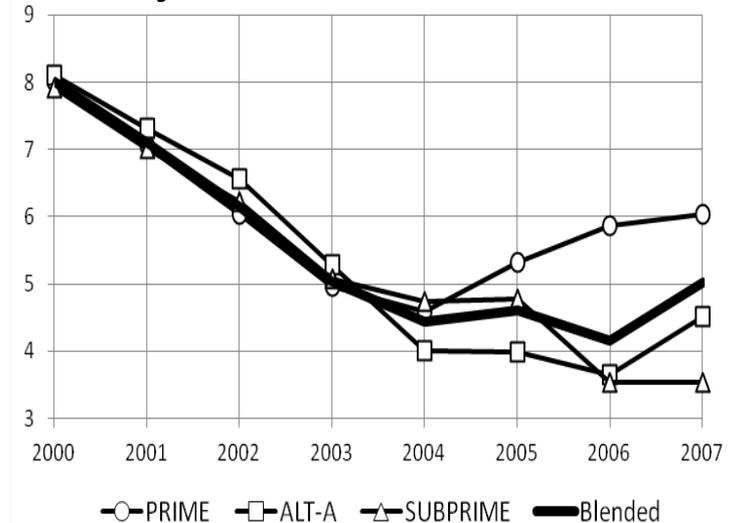
NTM: Defined here as Subprime and alt-A

Rates Out of Line with Projected Losses

Expected Annualized Loss



Loss-adjusted Rate

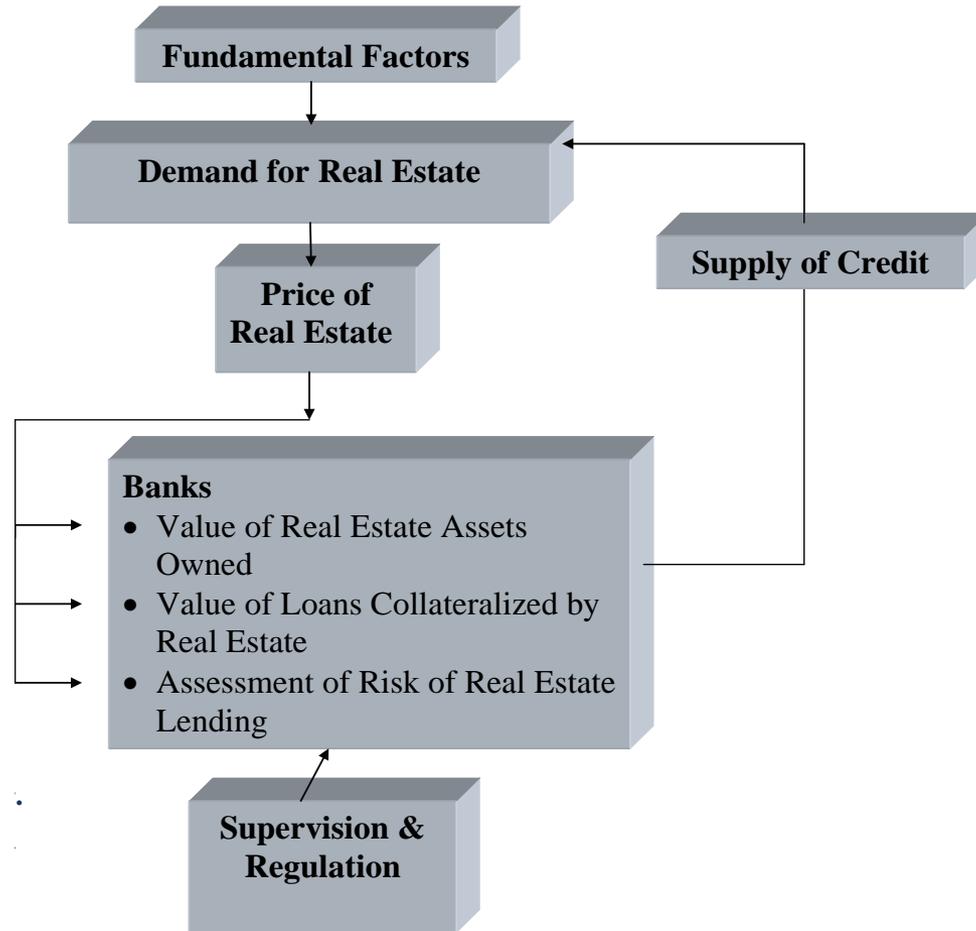


- Expected annual loss for subprime and alt-A jumps in 2005
- But not the required rate of return, using data available at the time
- Despite unpriced increased risk, mortgage flows increase in 2006
- Prices rise 24% from 2004 to 2006, 8% from 2005 to 2006
- Price volatility resulting from excessive mortgage supply/NTMs

Fundamental Problem: Real Estate Booms Put Financial Intermediaries at Risk

- **With heterogeneous beliefs and lack of short selling, optimists set prices.**
- **Lending at collateral's market price set by optimists implicates banking/ financial system.**
- **Banks may reduce lending standards in feedback loop.**
- **Price expectation formation, misaligned incentives, moral hazard issues**

5 Drives Real Estate Prices



Calls for Transparency in Securitization Markets

- **Securitization, the major innovation did not prevent market collapses, e.g. Spain.**
- **Information infrastructure, enhanced capital requirements**
- **Securitization markets for price discovery with full information and risk pricing**

Transparency in Securitization Markets: Not a Panacea

- **Securitization with full transparency with herding behavior, contagion effects, and imperfect information is reintroduces instability.**
- **Liquidity, risk pooling issues: Opacity maintains the pool.**
- **Price Revelation Securitization: Derivative markets with for price discovery with full information and risk pricing can provide signal risk, raise cost of capital, and complete markets.**

Thank you

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