

Macroprudential policy:

From theory to practice

Prof. dr. Paul Hilbers

Director Financial Stability

DeNederlandscheBank

EUROSYSTEEM

Seminar NBR/IMF Macroprudential Policy at Work
October 22-24, 2015

Disclaimer: The views and opinions expressed in this presentation do not necessarily reflect the official policy or position of De Nederlandsche Bank. This document is strictly confidential. Please do not distribute further.

Agenda

Theory

- **Why is macroprudential policy necessary?**

Toolkit

- What are the new instruments?

Governance

- How is macroprudential policy conducted in NL?

Past
experience

- Which countries have been proactive so far?

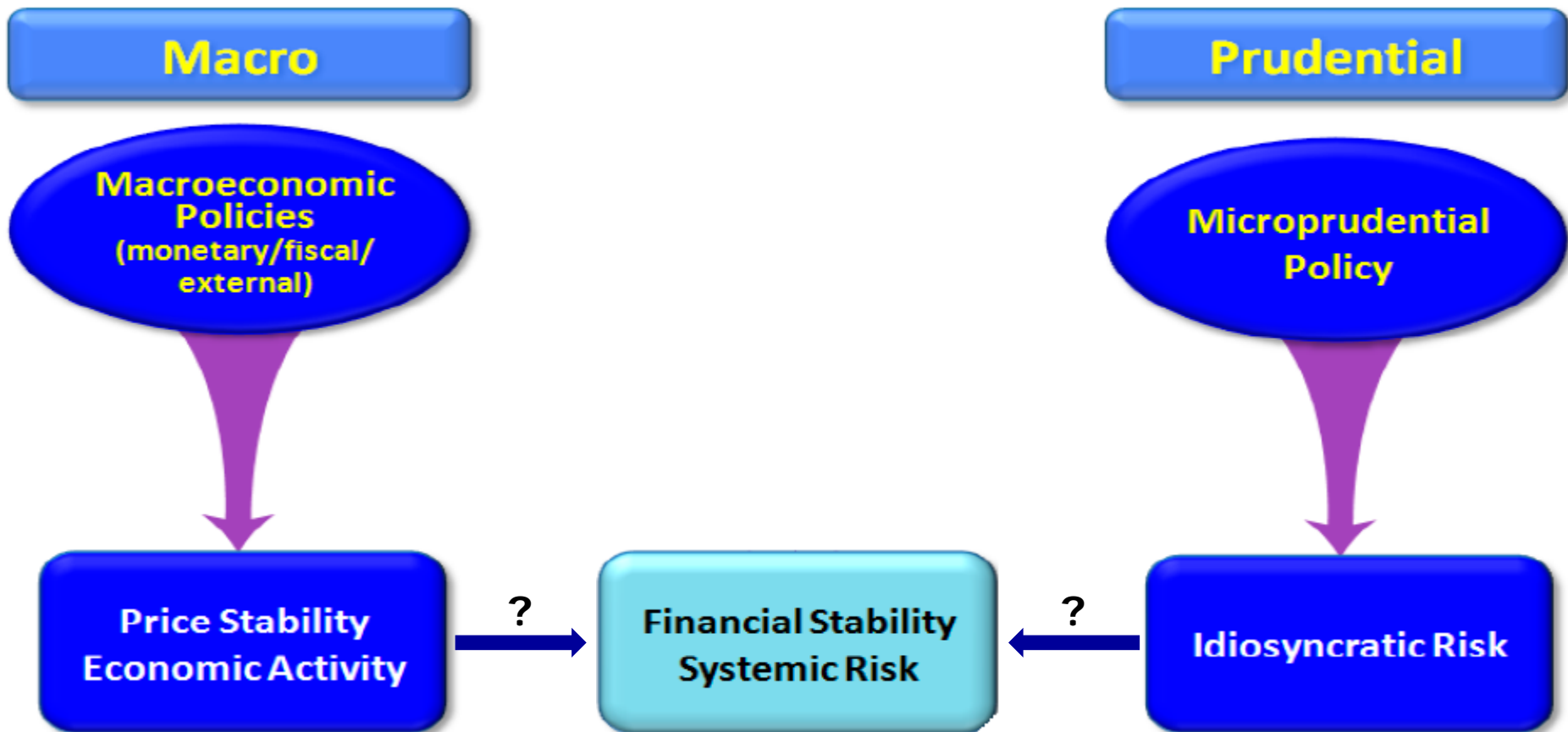
DNB's role

- When did DNB adopt/recommend a measure?

Future
challenges

- Concluding remarks

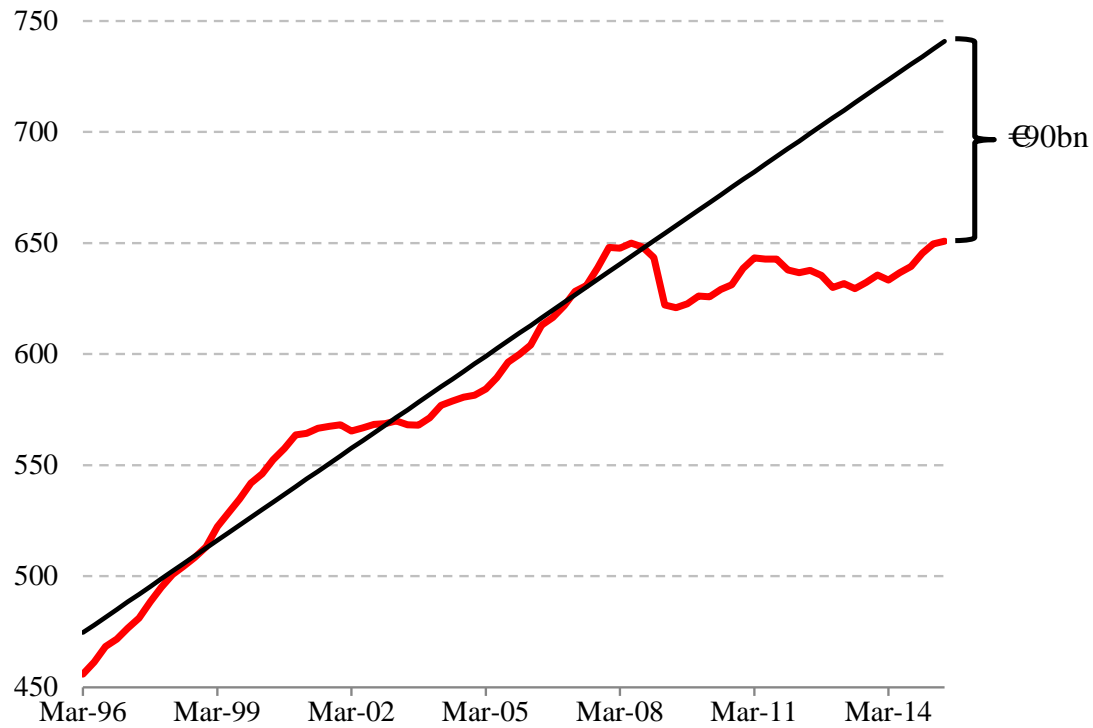
Economic policymaking before the crisis



The implications of the previous model

Real GDP

Netherlands, EUR bn, estimated trend is for the period 1996-2007



Source: CBS

International reform agenda

More resilient financial sector

- More and higher quality capital
- More liquidity, available when needed

More forward-looking supervision

- Sustainable business models and strategies
- Supervision of governance and compensation

Novel approach to supervision

- Timely and targeted intervention
- Independent, but accountable
- International cooperation

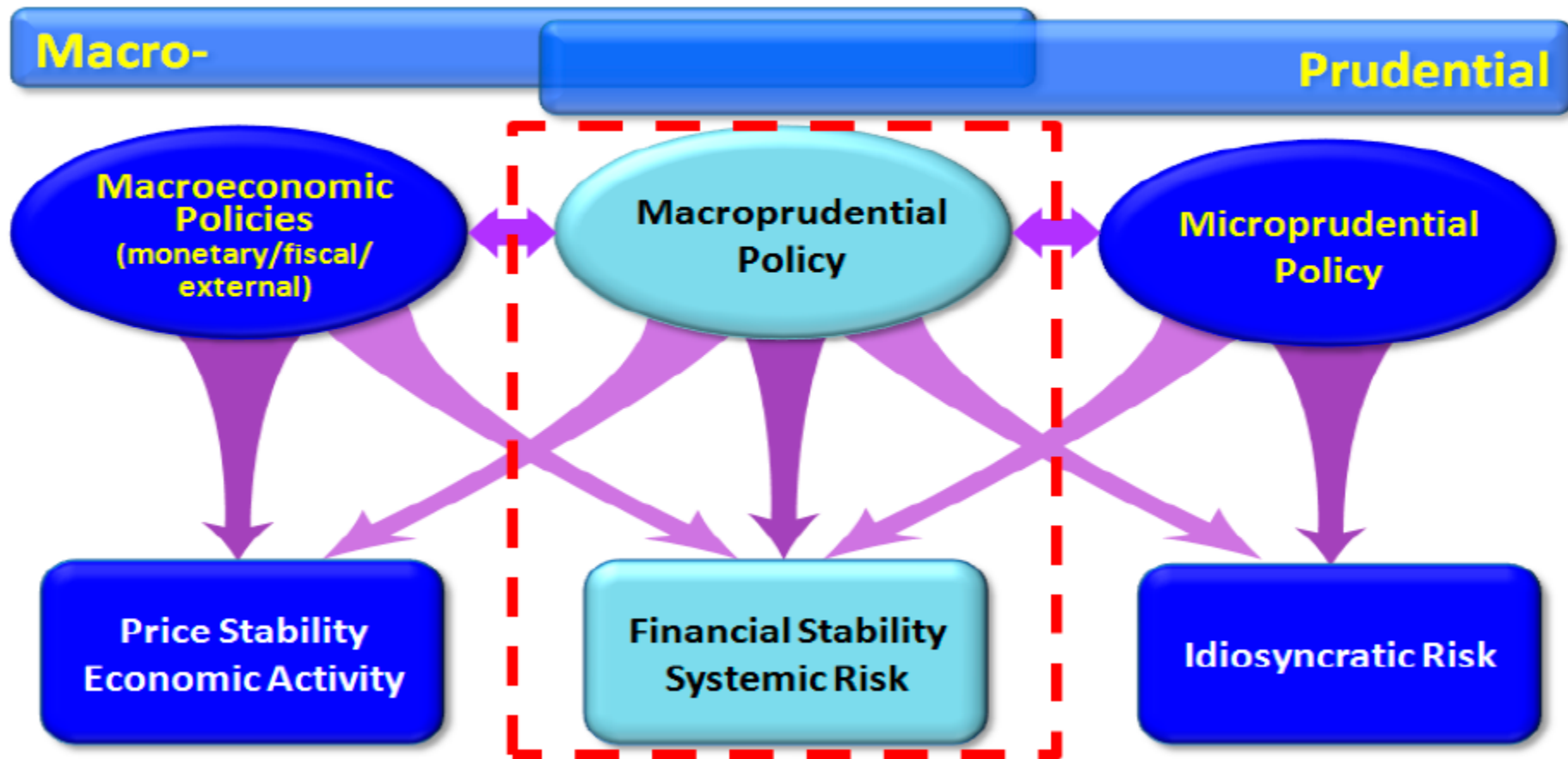
Enhancing macro-prudential oversight

- Focusing on the macro-prudential dimension

Effective crisis management

- A broad set of crisis management tools

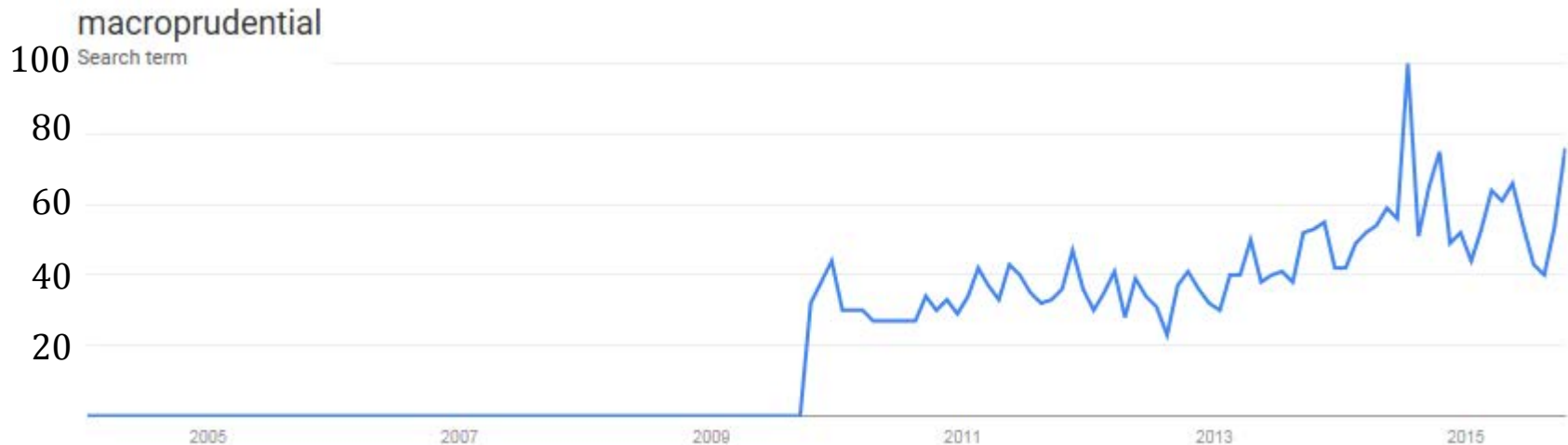
Economic policymaking after the crisis



The need for macroprudential policy was clear before the crisis

- The term 'macroprudential' first appeared in 1979, at a meeting of the Cooke Committee (the forerunner of the present BCBS) – Clement (2010).
- In 2000, the notion of a macroprudential approach to regulation received new impetus thanks to an influential speech by Andrew Crockett, at the time General Manager of the BIS.
- It was not until November 2009 in Seoul, the G20 Leaders *“called on the FSB, IMF and BIS to do further work on macroprudential policy frameworks...”*

Google trend



Agenda

Theory

- Why is macroprudential policy necessary?

Toolkit

- **What are the new instruments?**

Governance

- How is macroprudential policy conducted in NL?

Past experience

- Which countries have been proactive so far?

DNB's role

- When did DNB adopt/recommend a measure?

Future challenges

- Concluding remarks

Countercyclical
capital buffer

LTV/LTI caps

**Leverage
ratio**



Risk weights
for property
market loans

*Loan
amortisation*

Systemic buffers

Liquidity requirements
(**LCR/NSFR**)

*Macro stress
tests + regular
reports (OFS)*

Agenda

Theory

- Why is macroprudential policy necessary?

Toolkit

- What are the new instruments?

Governance

- **How is macroprudential policy conducted in NL?**

Past
experience

- Which countries have been proactive so far?

DNB's role

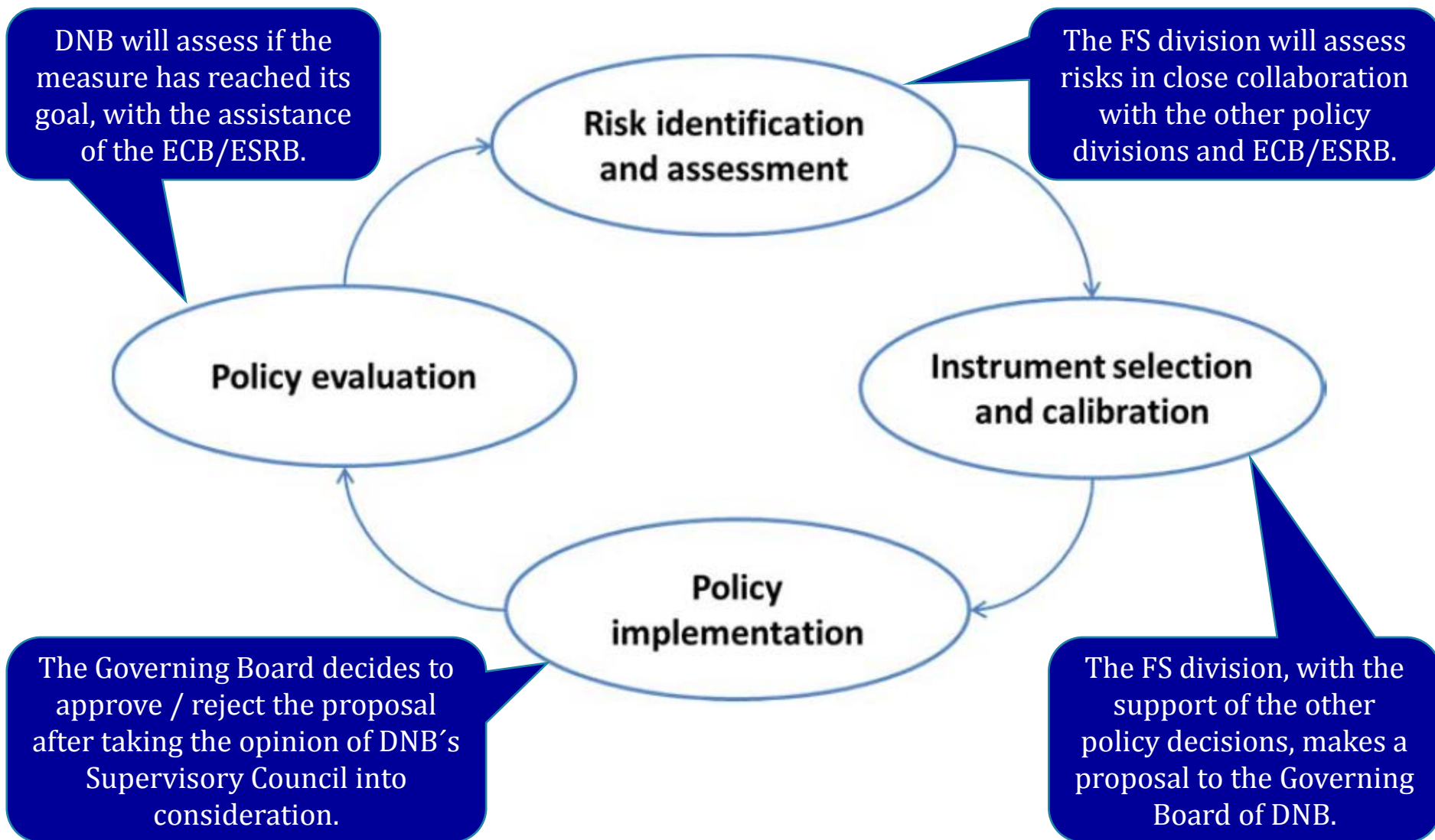
- When did DNB adopt/recommend a measure?

Future
challenges

- Concluding remarks

Macroprudential policy cycle

DNB's governance



Agenda

Theory

- Why is macroprudential policy necessary?

Toolkit

- What are the new instruments?

Governance

- How is macroprudential policy conducted in NL?

Past
experience

- **Which countries have been proactive so far?**

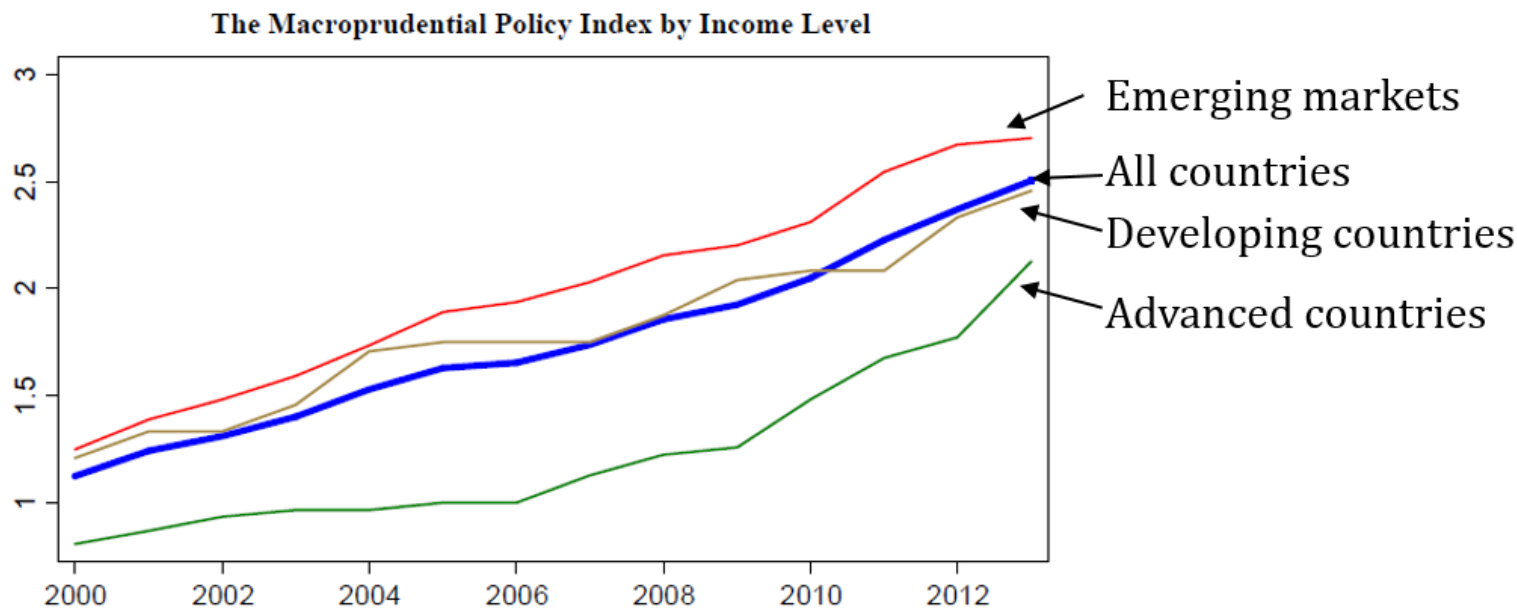
DNB's role

- When did DNB adopt/recommend a measure?

Future
challenges

- Concluding remarks

More countries are carrying out macroprudential policy



Macroprudential measure	Legal article	European countries that have announced or implemented the measure
CCB	130 CRD	Sweden and Norway
Higher risk weights for property market	124 & 458 CRR, 104 CRD	Belgium, Ireland, Romania, Norway, Sweden and United Kingdom
Higher LGD floor for mortgages	164 CRR	Norway
O-SII buffer	131 CRD	Austria, Finland, Netherlands and Norway
SRB	133 CRD	Austria, Bulgaria, Croatia, Czech Rep., Denmark, Estonia, Netherlands, Norway, Slovakia and Sweden
Leverage ratio	National law	Netherlands and the United Kingdom
Loan amortisation	National law	Netherlands, Slovakia and Sweden
DSTI limit	National law	Cyprus, Estonia, Lithuania and Romania
LTI limit	National law	Ireland and United Kingdom
LTV limit	National law	Cyprus, Czech Rep., Estonia, Finland, Ireland, Latvia, Lithuania, Malta, Norway, Netherlands, Poland, Romania, Slovakia, Sweden

How effective have some of these measures been?

- **Empirical evidence on the effects of macroprudential instruments is still scarce and preliminary.**

- **Cerutti, Claessens, and Laeven (2015) look at 12 macroprudential policies in 119 countries over the 2000-13 period. Three important conclusions are:**
 - Borrower-based policies (e.g. LTV/DTI limits) are used relatively more in advanced countries.

 - Borrower-based and financial institutions-based policies (e.g. limits on leverage and dynamic provisioning) appear to be effective in reducing credit and house price growth.

 - Policies work better in the boom than in the bust phase of a financial cycle.

 - Policies are (i) relatively less effective in developed and more financially open economies ('waterbed' effects).

Agenda

Theory

- Why is macroprudential policy necessary?

Toolkit

- What are the new instruments?

Governance

- How is macroprudential policy conducted in NL?

Past experience

- Which countries have been proactive so far?

DNB's role

- **When did DNB adopt/recommend a measure?**

Future challenges

- Concluding remarks

Dutch Macroprudential measures

The systemic buffers and the leverage ratio

Systemic buffers

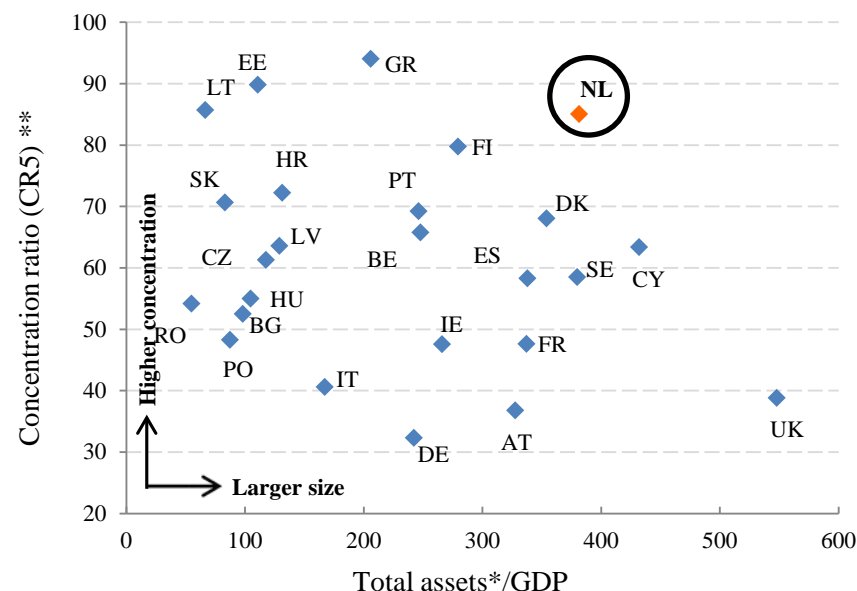
- In 2011, DNB and Ministry of Finance announced that the systemically relevant banks would need to raise their buffers between 1% and 3%.
- On 29 April 2014, DNB introduced 1-3% systemic buffers for the four major banks.
- Gradual phase-in between 2016 and 2019.

Leverage ratio (LR):

- ☐ The major banks were asked in Dec. 2014 to provide capital migration plans that show how they plan to reach the 4% LR by 2018 (as requested by the Dutch Cabinet).

Size and competition in the banking sector

EU countries, 2014



Source: ECB

* In measuring size of banking sector, total assets includes foreign branches and subsidiaries.

** The Concentration Ratio (CR5) is the balance sheet aggregate of the five largest banks over the total aggregate.

Note: The outliers Malta (653% of GDP) and Luxembourg (1618% of GDP) are excluded.

Dutch Macroprudential measures

Housing market

➤ **In 2011 (self-regulation):**

- ❑ Maximum of 50% interest-only per mortgage.
- ❑ Stricter enforcement of LTI-criteria by banks.

➤ **In 2013:**

- ❑ Tax deduction of interest payments apply to fully amortising loans (*new mortgages*).
- ❑ Lowering of tax deductibility rate from 51% to 38% in 2041 (*all mortgages*).
- ❑ LTV cap: from 106% in 2012 to 100% in 2018 (*new mortgages*).

➤ **In 2015:**

- ❑ Recommendation of the Dutch FSC for further lowering of the LTV to 90% by 2028 (the Finance Ministry has power over this instrument).

Agenda

Theory

- Why is macroprudential policy necessary?

Toolkit

- What are the new instruments?

Governance

- How is macroprudential policy conducted in NL?

Past experience

- Which countries have been proactive so far?

DNB's role

- When did DNB adopt/recommend a measure?

Future challenges

- **Concluding remarks**

Concluding remarks

- The crisis made it clear that macroprudential policy is a necessary complement to macroeconomic and microprudential policy.
- Designated authorities must not hesitate to act in a timely manner.
- EU countries have already implemented many macroprudential instruments.
- Going forward, we should form a better understanding as to how we must...
 - ❖ *...counter inaction bias in 'boom times'?*
 - ❖ *...implement policy during the bust?*
 - ❖ *...coordinate with the other authorities?*
 - ❖ *...prevent waterbed effects?*



Thank you!