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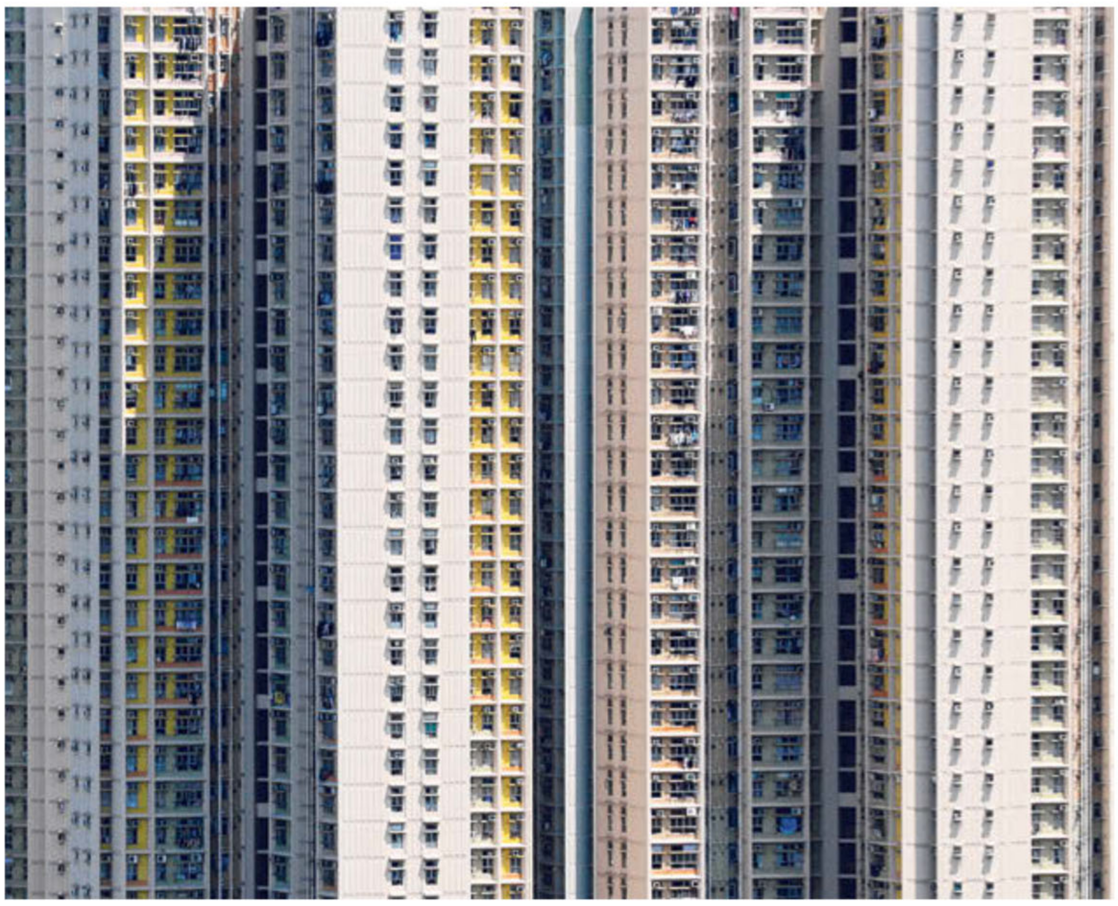

Policy makers are concerned about housing affordability and possible disruptions to financial and macroeconomic stability when property prices are volatile.
PHOTO: REUTERS

List best practices for use of macro-prudential policies in housing market

This seems called for now, so Asian regulators can be guided in their implementation, with flexibility built in to account for differences in the region's markets. BY RAMKISHEN S RAJAN AND RUIJIE CHENG

ASIA has faced at least three major crises in the last two decades – Asian Financial Crisis (AFC) of 1997-98; Global Financial Crisis (GFC) of 2008-09; and the ongoing Covid-19 crisis of 2020. In between these crises was the Nasdaq bubble collapse of 2001, the "taper tantrum" period in 2013 and multiple other negative shocks. Throughout all these, with a few exceptions, most of the economies in Asia continued to embrace global capital flows.

Apart from concerns about sharp booms and busts in capital flows, such financial openness has rendered the region highly sensitive to global financial cycles, a term coined by Hélène Rey of the London Business School to refer to a high degree of synchronisation of financial asset prices, capital flows and credit growth across countries with open capital accounts.

GLOBAL FINANCIAL CYCLE AND HOUSING

While much of the focus of the global financial cycle has been on financial assets (equities and bonds), somewhat less attention has been paid to the property market. While cross-border commercial real-estate investment has been growing rapidly in Asia, residential real estate remains of particular interest to policymakers as it is usually the single largest asset in the typical household portfolio, and banks are directly or indirectly heavily exposed to the real-estate sector.

As a result, significant developments in housing markets can impact household wealth, which in turn affects domestic consumption and the overall macro-economy. Property market stability is also closely related to the soundness of financial institutions and financial stability at large.

The conventional belief has been that property is much less liquid, requires much greater capital outlay and therefore should be far less impacted by the global financial cycle. However, over the years, there has been a surge in interest in global real estate as an alternative asset by high net worth investors (HNWIs), Sovereign Wealth Funds (SWFs), and other institutional investors.

For instance, the Government of Singapore Investment Corporation (GIC) has long been a major global investor in real estate and has built an impressive global real-estate portfolio which includes residential investments.

In addition, the creation and widespread popularity of real estate investment trusts (Reits) have led to the rapid financialisation of real estate. This, in turn, has made the role of international capital flows and the global financial cycle highly relevant to the property market globally. The International Monetary Fund's Global Financial Stability Report in April 2018 showed that housing price synchronisation across countries has been increasing over the years, as many countries have been exposed to the generally loose global financial conditions since the GFC.

The rapid rise in residential property prices since the GFC has led to concerns among policy makers – both about housing affordability, especially in global cities like Hong Kong, Singapore and Seoul, and about possible disruptions to financial and macroeconomic stability in the event of sudden reversal in property prices.

Moreover, the heighted synchronicity across housing markets may also transmit or amplify financial and macro-economic shocks in local property markets.

MACROPRUDENTIAL POLICIES IN ASIA

Since the GFC, macroprudential policies have become a part of the toolkit of policy makers worldwide, though many Asian countries have used them since the mid-1990s. Even in Asia, their use has intensified since 2009 following the aggressive quantitative easing in major advanced economies.

Among the most frequently used property-related macroprudential policies are those that target borrowers, including loan-to-value (LTV) and debt-to-income (DTI) ratios, which limit the amount of mortgage loans and overall credit flows to the property market.

In addition, macro-economic prudential policies have usually been accompanied by fiscal measures on property transactions, such as seller stamp duties levied on housing units sold within certain holding periods, as well as differentiated or additional buyer stamp duties targeting international buyers or domestic buyers of multiple properties.

There is a growing body of empirical evidence to suggest that macroprudential policies can help decouple domestic house prices from global ones and moderate house price appreciation.

Indeed, the relative stability and resilience of housing markets in Asia in the face of the Covid-19 shock can be partly attributed to the macroprudential policies in place that have helped to ensure a degree of moderation in property price rises pre Covid-19. The prevailing low interest rate environment has no doubt been an important factor as well in propping up regional house prices.

However, the real test will come with the rollback of the various government measures to protect jobs and incomes, and of the central bank measures to provide financial relief to SMEs and individuals facing temporary cashflow difficulties.

As concerns shift from one of liquidity to outright solvency and in the event the property market starts declining sharply, there may be scope to relax some of the property-related macroprudential measures in place. Hong Kong took a pre-emptive step in August by raising the loan-to-value ratio from 40 to 50 percent in the case of non-residential properties. Thus far housing-related macroprudential policies have largely remained unchanged in most regional economies.

Despite the frequent use of macroprudential policies by regional central banks, of concern is that there is no clear set of best practices or principles that guide Asian regulators in their implementation or adjustments. Countries in Asia and elsewhere would benefit from regional rules of good conduct regarding the use of macroprudential policies, while still ensuring sufficient flexibility is given to differing country contexts.

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