

Discussion: Elenev, Landvoigt, Van Nieuwerburgh: Phasing-out the GSEs

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 - ▶ Is the economy better off without GSEs?
 - ▶ Answer yes, but not trivially true in incomplete markets
 - ▶ Quantify the effects of GSEs in a rich GE incomplete markets economy with heterogenous agents
- ▶ Discussion
 - ▶ Paper is forthcoming (Journal of Monetary Economics)
 - ▶ Model & mechanism
 - ▶ Causes of high leverage
 - ▶ When could adding GSEs be useful?

Model in a nutshell

- ▶ Two-good endowment economy i.e. non-housing (non-tradable) & housing Lucas tree
- ▶ Two shocks: non-housing fruit & house value
- ▶ Incomplete markets: four assets: housing, short-term bond, mortgage, mortgage insurance

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- ▶ Three agents:
 - ▶ risk-averse & patient
=Depositors/Savers
 - ▶ not so risk-averse & patient
=Intermediaries
 - ▶ risk-averse & impatient
=Borrowers

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- ▶ Government
 - ▶ income from endowment tax net of mortgage deduction, guarantee fee γ
 - ▶ supplies guarantees at fee γ
 - ▶ bails out deposits of defaulting banks

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 - ▶ insurance more costly → banks increase supply of non-mortgage bonds
 - ▶ reduction in guaranteed portfolio share increases incentives to internalize risk
 - ▶ lowers leverage, reduces mortgage portfolio and risk → financial sector fragility
 - ▶ fewer bailouts necessary
 - ▶ stable mortgage supply

GSEs bad because of moral hazard & inefficient allocation of risk

- ▶ GSE are bad because savers, i.e. risk-averse depositors foot the bill during crisis
- ▶ Induces fluctuations in consumption of risk-averse agent
- ▶ While intermediaries and borrowers benefit

Is high leverage caused by mortgage guarantees?

	2001-2003	2004-2005	2006-2014
Mortgages / RWA			
High E/A	62.07	65.24	67.56
Low E/A	61.74	65.83	68.25
Difference	0.33	-0.59	-0.69
t-statistic	(0.24)	(-0.37)	(-0.86)
Government-Backed MBS / RWA			
High E/A	24.12	24.00	21.45
Low E/A	8.85	6.99	9.29
Difference	15.28	17.01	12.15
t-statistic	(9.76)	(9.81)	(16.49)
Government-Backed MBS / MBS			
High E/A	95.74	95.39	96.96
Low E/A	95.96	94.69	94.30
Difference	-0.22	0.70	2.66
t-statistic	(-0.28)	(0.66)	(5.18)

Table: Begenau & Stafford 2016

What are the forces in the model that prevent GSEs from being beneficial?

- ▶ Other words: Under what circumstances would adding insurance be a good idea (i.e. better than market)
 - ▶ Here: too much risk-taking by banks and borrowers due to gov. MBS distortion
 - ▶ Also here: Private market able to provide stable and healthy mortgage supply even in bad times if γ high enough
- ▶ Value of home ownership?

Conclusion

- ▶ Great paper
 - ▶ complex model captures important features of the data
 - ▶ quantitative results suggests that abolishing GSEs is on net a good idea
 - ▶ with transition dynamics: costs in the short run
 - ▶ intuition of bad risk allocation neat and extendable beyond GSEs
- ▶ Causes for excessive leverage GSE alone?
- ▶ When would adding GSEs make sense?