

Accepted Manuscript

Title: Mortgage Default, Lending Conditions and
Macroprudential Policy: Loan-Level Evidence from UK
Buy-to-Lets

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PII: S1572-3089(18)30180-3
DOI: <https://doi.org/doi:10.1016/j.jfs.2018.03.008>
Reference: JFS 618

To appear in: *Journal of Financial Stability*



Please cite this article as: Robert Kelly, Conor O'Toole, Mortgage Default, Lending Conditions and Macroprudential Policy: Loan-Level Evidence from UK Buy-to-Lets, *Journal of Financial Stability* (2018), <https://doi.org/10.1016/j.jfs.2018.03.008>

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Mortgage Default, Lending Conditions and Macroprudential Policy: Loan-Level Evidence from UK Buy-to-Lets

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January 4, 2018

Abstract

Using a unique sample of mortgage loans for the UK buy-to-let market, we estimate a “double trigger” default model which links originating debt service and loan-to-value ratios to ex post default. We investigate whether the relationship between these ratios and default can be informative in the calibration of macro-prudential limits. We find default increasing with originating loan-to-value and falling in the origination debt service ratio. A non-linear cubic spline model is used to identify threshold effects and we identify clear turning points in these relationships. This analysis could provide one input into supervisory considerations when setting limits in a macro prudential context. In addition, we investigate how multiple loan portfolios interact with these thresholds with strong evidence to support tighter macroprudential restrictions on loans for second and subsequent properties.

Keywords: Macroprudential, Credit Risk, Mortgages, UK.

JEL Classification: E32, E51, F30, G21, G28

*Corresponding author: robert.kelly@centralbank.ie; conor.otoole@esri.ie. We thank seminar participants at the European Economic Association conference, IFABS conference 2016 and the Central Bank of Ireland seminar series for helpful comments and suggestions. We would also like to thank conference participants at the Czech National Bank, IES Conference on “Challenges for Financial Stability in Europe”, October 2016. Particular thanks go to Roman Horvath, Gabriel Fagan, Niamh Hallisey, Fergal McCann and Gerard O'Reilly. The views presented in this paper are those of the authors alone and do not represent the official views of the Economic and Social Research Institute, the Central Bank of Ireland or the ESCB. Any remaining errors are our own.

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