Comments on Ono, Uchida, Udell, and Uesugi’s “A Close Look at Loan-To-Value Ratios in Japan: Evidence from Real Estate Registries”

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Paper Summary

✓ Analyzes the loan-to-value (LTV) ratios for business loans by Japanese banks from 1975 to 2009
  ➢ Examines the cyclicality, their determinants, and the ex post performance of the borrowers with high vs. low LTV ratios

✓ Uses a unique micro dataset compiled from the official real estate registries in Japan
Findings

✓ **LTV ratio** (for business loans) exhibits counter-cyclicality
  - Average LTV ratios are the lowest during the bubble period in the late 1980s and early 1990s
    - Increase in loan volumes is less than the increase in land values during booms (vice versa)
  - Counter-cyclicality of LTV ratios is robust to controlling various determinants

✓ **Ex post performance** of the borrowers with high-LTV loans was no worse than those with low-LTV loans
  - Their performances were even better during the bubble period
Loans Land Value

Excess Risk-Taking

LTV=1

LTV>1

Loans

Land Value

Loans

Land Value
Counter-cyclical Story

LTV < 1

LTV = 1

Excess Risk-Taking

Loans

Land Value

Loans

Land Value

Bubble
Contributions

✓ This paper finds some new results and suggests some policy implications for the cap on the LTV ratio
  ➢ Previous research: residential loans
  ➢ Challenging results against conventional wisdom
    ■ Banks’ excess risk-taking with lax lending standards during the bubble period

✓ Next, my comments/questions
Why are the LTV ratios **lowest** during the **bubble** period?

- The land values were *exceptionally* increasing during the bubble period…
- The land prices in *Tokyo* and *Osaka* were much more increased than the average land price in Japan
  - Consistent with Figure 11
  - How about looking the LTV ratios by dropping these areas?

- How about the effects of new entry of *city banks* for SMEs during the bubble period?
  - More *conservative* than regional banks?=> If yes, the LTV ratio should be getting low?
Change of Commercial Land Price

- Tokyo
- Osaka
- All average
LTV ratio is really counter-cyclical?
- If we ignore the bubble period, it looks like that the LTV ratio seems to be pro-cyclical
  - E.g., Figure 4 especially after the bubble period
- How about the possibility of twin peaks among borrowers depending on the purpose of loans?
  - E.g., working funds (Low LTV ratio?) vs. real estate investment (High LTV ratio?)
  - Many latter cases might have already dropped in this paper...
  - Want to see the detailed descriptive statistics of LTV ratios year by year...
Comment #3

- Cannot ignore the **survival biases** to understand the low LTV ratios during the bubble period (although already pointed out in the paper….)
  - Firms are still **registered in 2008** and afterwards…
- **Many risky firms** might have already went bankrupt during the 1990s….
  - If the **LTV ratios** of these firms had been **high** during the bubble period, the results might look different…
  - Significant effects on the results of **ex post performance**?
Comment #4

✓ How about the effects of rescheduled loans and/or debt forgiveness on the LTV ratios?
  ➢ New registry or not? If yes, the LTV ratio should be getting low…
    ■ But the LTV ratios are increasing in the 1990s

✓ Implicit assumption that high LTV ratio indicates risk-taking by banks (vice versa)
  ➢ Can we detect banks’ risk-taking only by looking the LTV ratio? (pp.5 again…)
  ➢ Consistent with the results of ex post performance?
    ■ High risk/High return
  ➢ Ability to repay loans is the most important factor for banks when they decide to extend loans or not
    ➢ First priority vs. Second priority
Excess Risk-Taking and LTV ratio

LTV=1

LTV<1

can be consistent

Land Value

Loans

Bubble

Loans

Land Value
Other comments

✓ Can compare the LTV ratios **across years**?
  - Uses the **hedonic model**
  - Can compare land values **across firms**

✓ Excess risk-taking might be true **only for a part of all loans**
THANK YOU!