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

Yukihiro Yasuda
Tokyo Keizai University

November 30, 2012
HIT-TDB-RIETI International Workshop on the Economics of Interfirm Networks

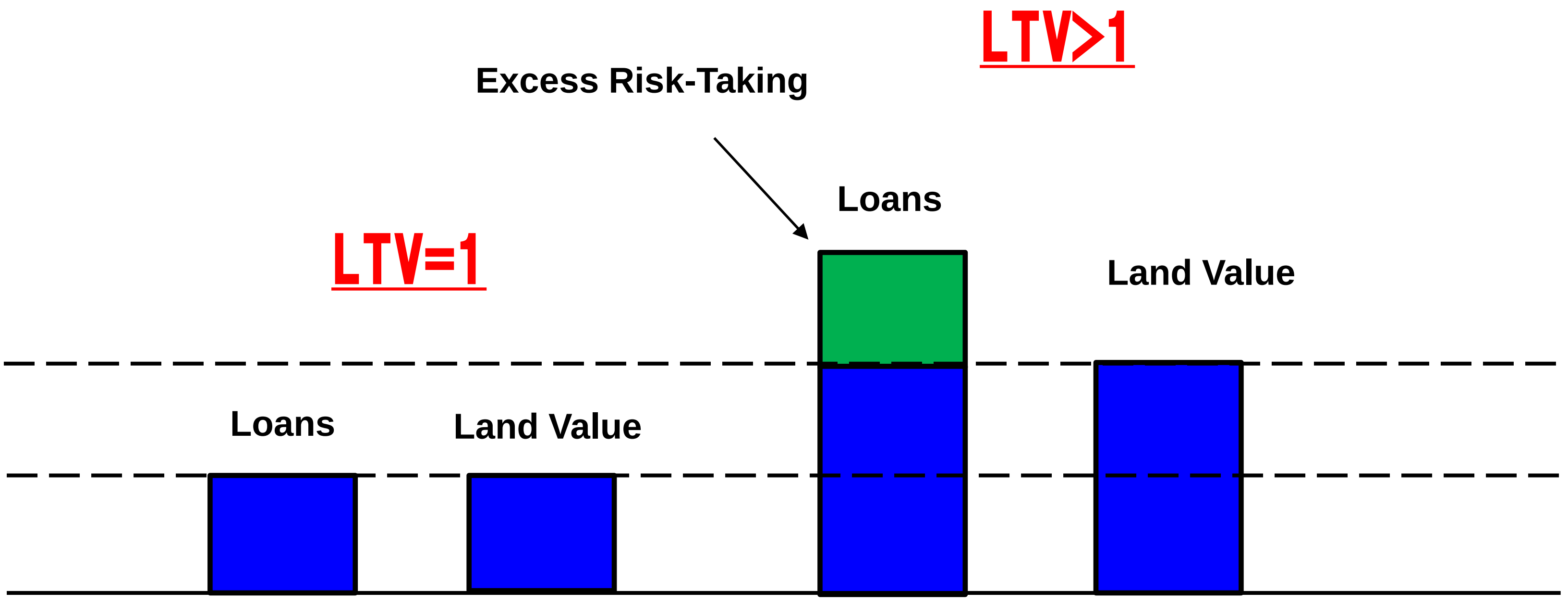
Paper Summary

- ✓ 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 complied from the official real estate registries in Japan

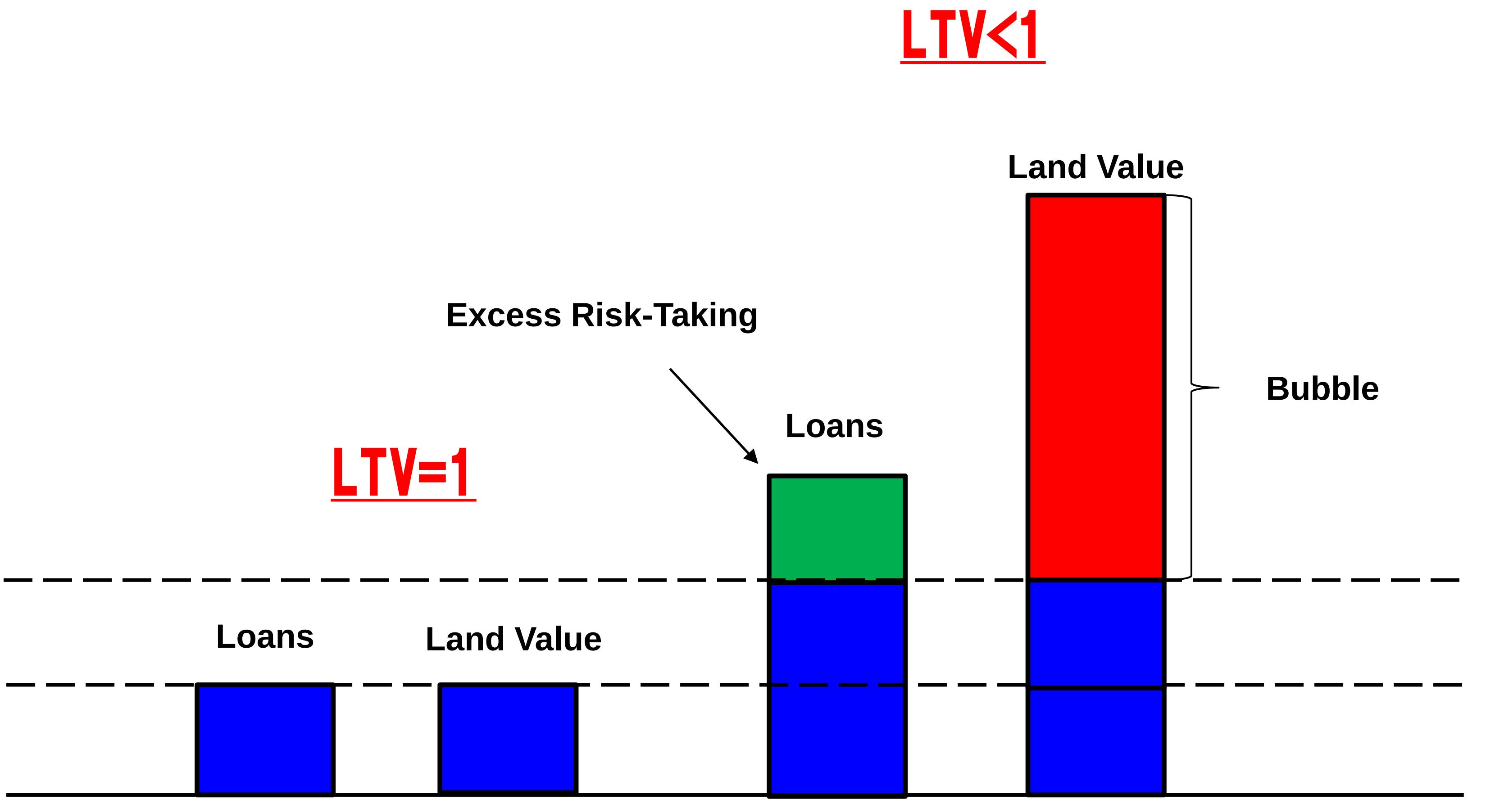
Findings

- ✓ 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

Pro-cyclicality Story



Counter-cyclical Story



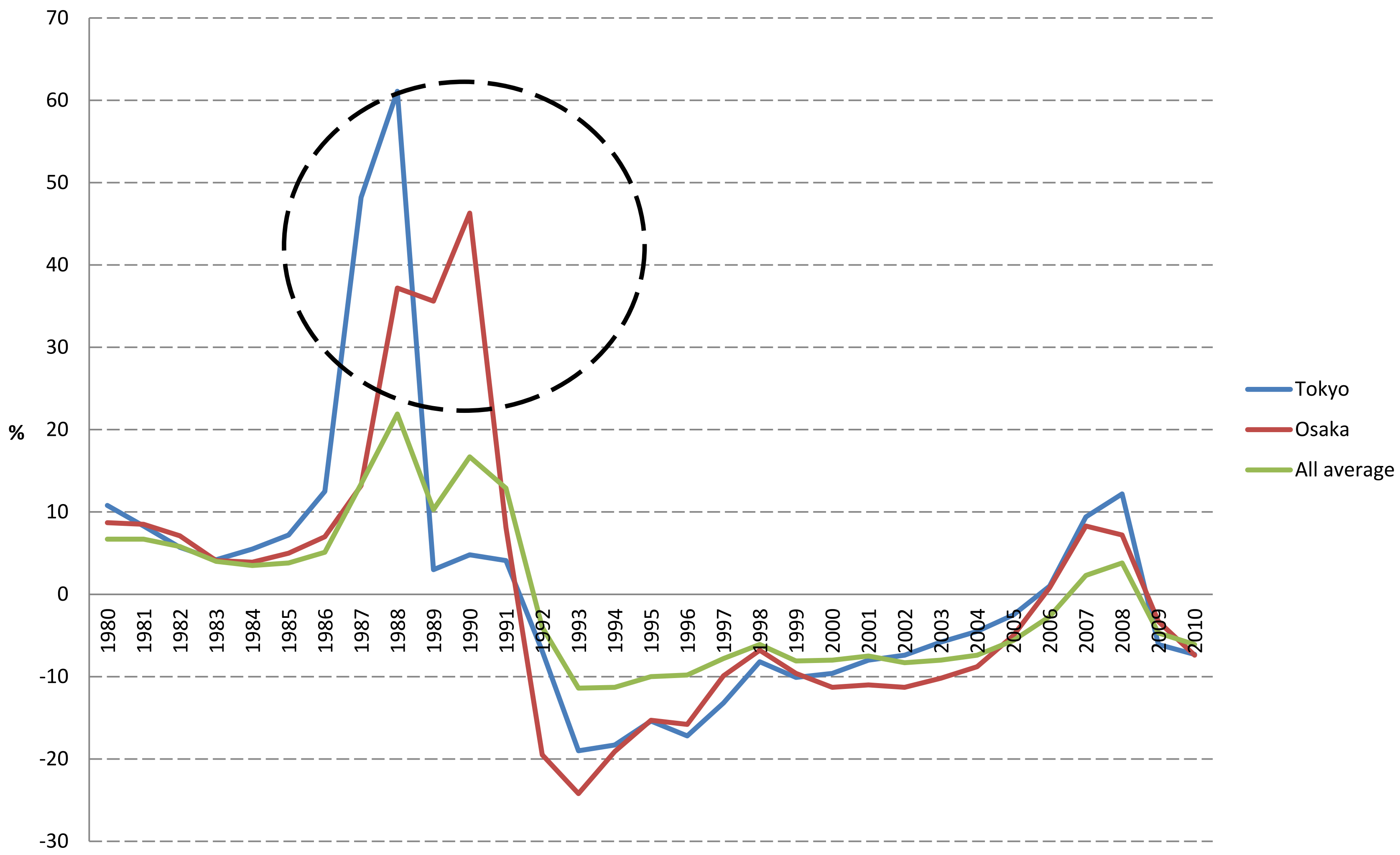
Contributions

- ✓ 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

Comment #1

- ✓ 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



Comment #2

- ✓ 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…

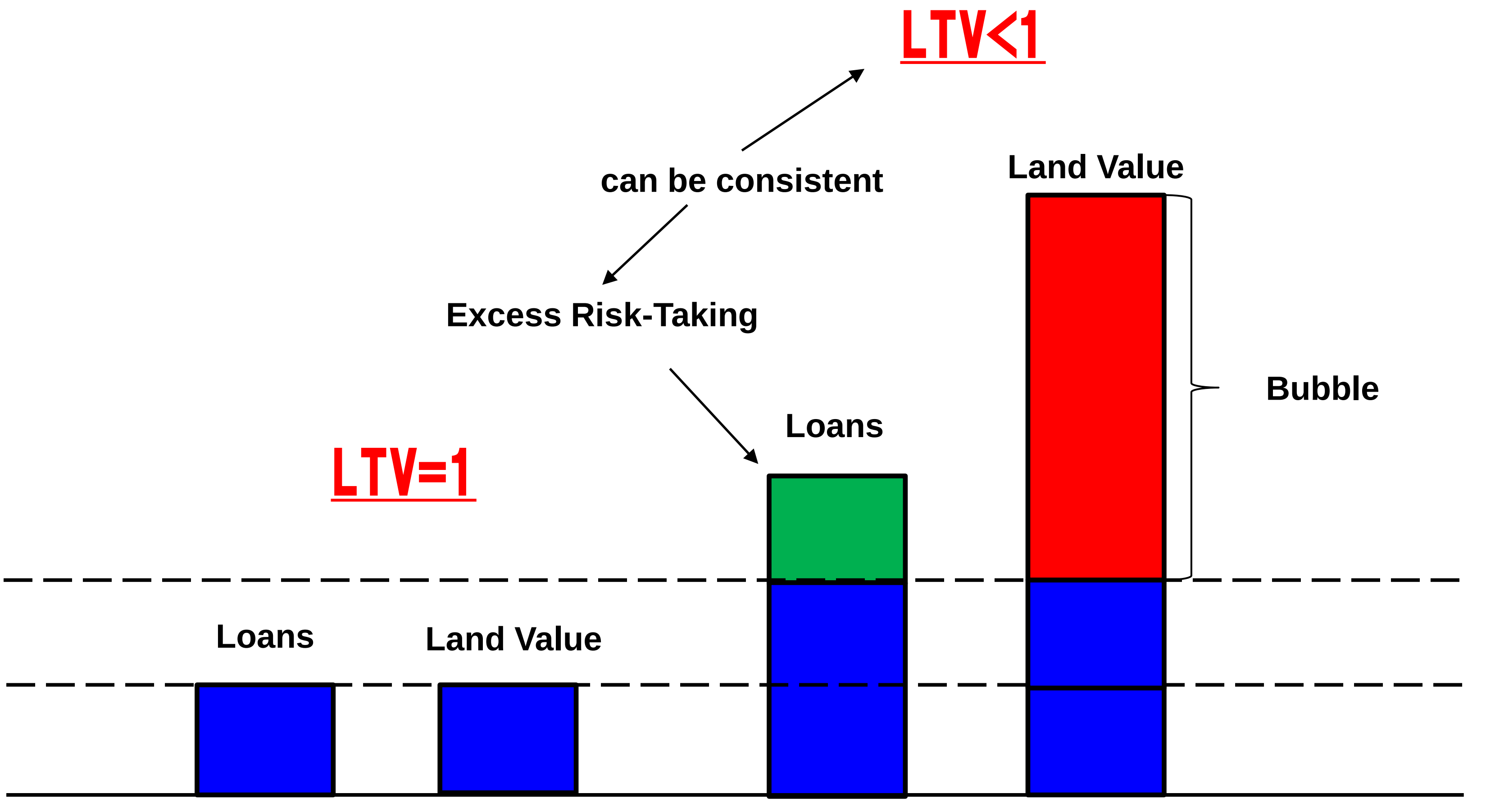
Comment #3

- ✓ 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



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!