Discussion of

"Credit booms and macrofinancial stability" and "Rethinking financial deepening: Stability and growth in Emerging Markets"

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Bottom line

- Sustainable economic growth and financial stability are not necessarily conflicting
- What matters and needs to be balanced is:
  - Size
  - Pace, speed, duration
  - Prudent risk management
- How to achieve a balance requires information and answer several questions
  - “Dress me slowly, I am in a hurry”

Policymakers' questions

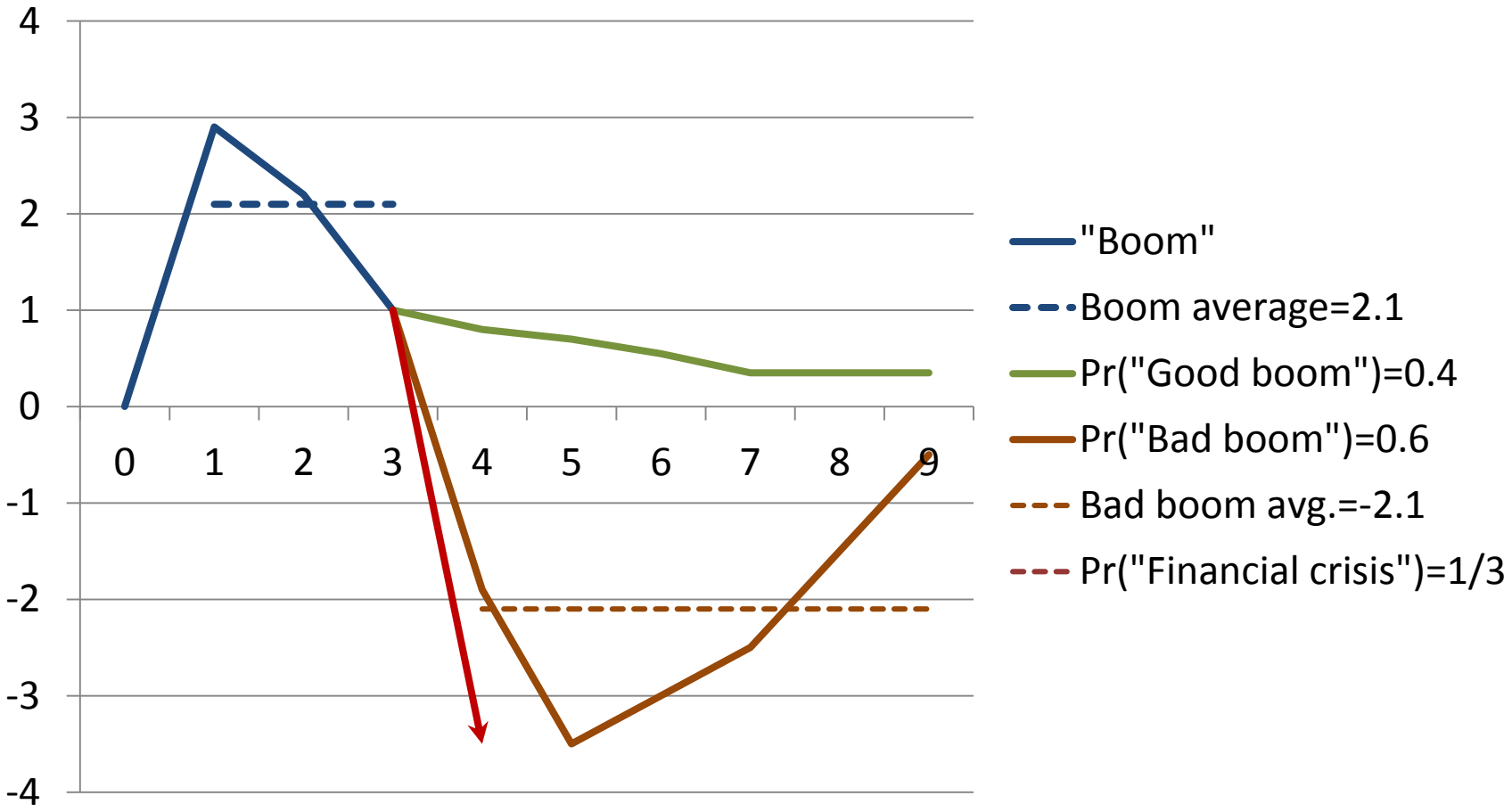
- Are there limits to financial development for growth and stability?
- When do credit booms occur?
- When is it necessary to intervene?
- When do they end up in busts?
- What are the implications for prudential policies?

Dell'Ariccia et al.

- Focus: financial cycle, i.e. credit booms, and its macrofinancial consequences
- Information: new, large cross-country dataset
  - 170 countries
  - 1970 to 2010
  - 176 credit booms
  - 110 economic underperformance after the boom
  - 57 financial crises after the boom

A stylized credit boom

(Real GDP growth – average percentage points relative to non-boom years)



Helping policymakers

- Can we predict credit booms in real time?
  - "Overall, it is difficult to predict credit booms."
  - Be more careful if GDP growth and financial reform
- Can we tell bad from good booms in real time?
  - Even more difficult
  - Useful characterization of bad booms: Larger, last longer, and start at higher level of financial depth
- Which may be a policy recommendation?
  - More booms happen in relatively undeveloped financial systems and they can play a role in deepening
  - No evidence that booms in emerging markets are more likely to end up badly

Helping policymakers (cont.)

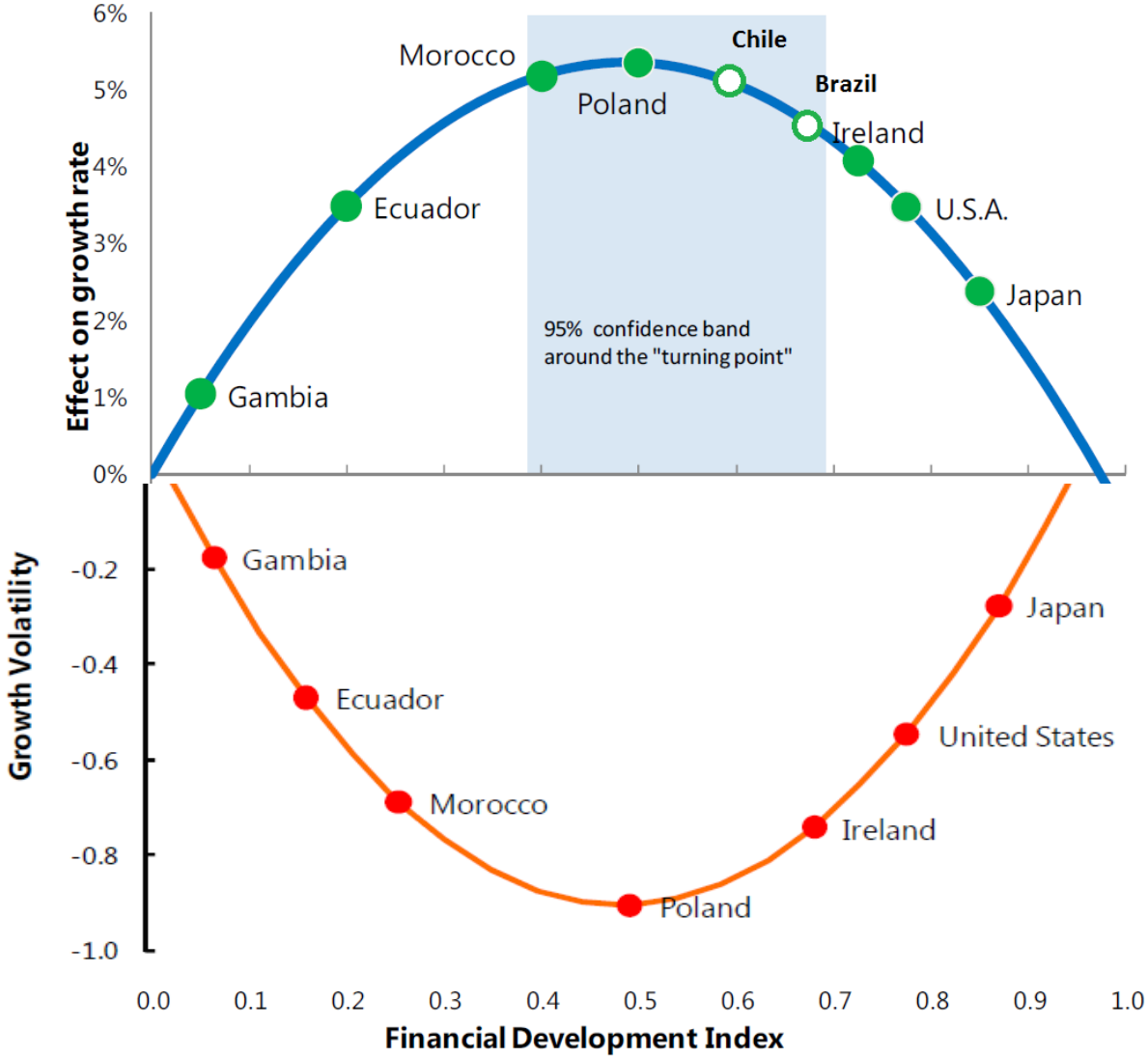
- Macroprudential policy should come into play in coordination with macroeconomic policy
  - Promising evidence of targeted macroprudential tools and limited effectiveness of monetary and fiscal policy in directly dealing with credit booms
- Practical implementation?
  - Policy intervention become increasingly justified as booms become larger and more persistent
- Is there a rationale for institutional arrangements? If yes, which ones? For more rule-based regulation? What about the discretion proposed in Basel III's countercyclical capital buffer?

Čihák et al.

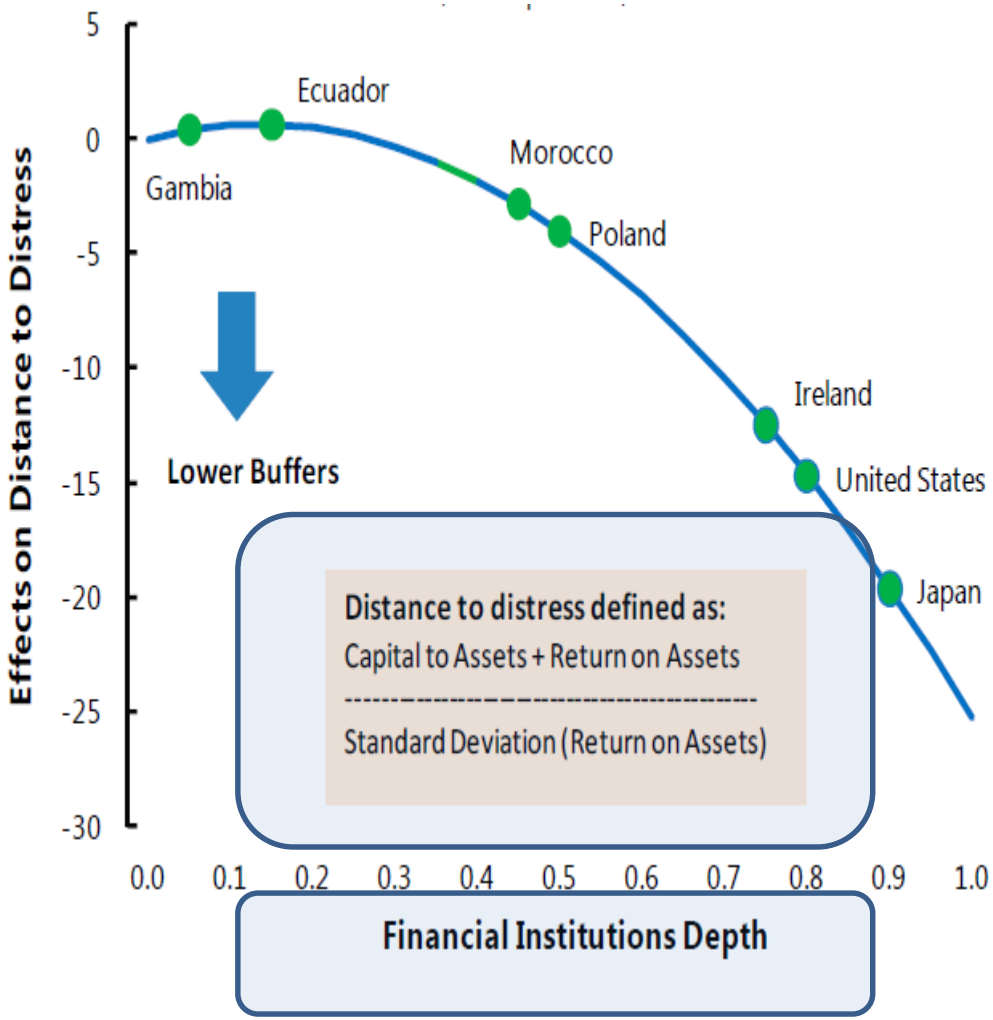
- Information: new, broad index for financial development:
  - 176 countries
  - 1980 to 2013
  - Financial markets and institutions
  - Depth, access and efficiency

- Access: financial services on the phone, internet, fintech?

Financial development and growth



Fin. development and stability



- Risks increase with depth and pace
- Why from the start?
  - Growth volatility is lower and hedging possibilities larger
- Other proxies for financial stability?
- Other index of fin. development?

Helping policymakers

- Balance size and speed according to initial financial deepening
- Improve institutional environment and the quality of the regulatory framework
- A set of regulatory principles are relevant for financial development and stability
- Could empirical evidence be provided on the relative relevance of institutions and principles at different levels of financial development?

Thank you!