

# **The Macroeconomic Effects of Macroprudential Policy**

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## **Summary**

Central banks have increased their use of macroprudential measures to manage the financial cycle, but the effects of such measures on the core objectives of monetary policy to stabilize output and inflation are largely unknown. In this paper, we measure the effects of changes in maximum loan-to-value (LTV) ratios on output and inflation. We rely on a narrative identification approach based on detailed reading of policy-makers' objectives when implementing the measures. While the literature mostly relies on dummy variables to measure the effectiveness of macroprudential measures, we also consider the size and scope of changes in regulatory LTV ratios to capture the intensity of policy changes.

We find that a 10 percentage point decrease in the maximum LTV ratio leads to a 1.1% reduction in output over the next four years. As a rule of thumb, the impact of a 10 percentage point LTV tightening can be viewed as roughly comparable to that of a 25 basis

point increase in the policy rate. However, the effects are imprecisely estimated and the effect is only present in emerging market economies. We also find that tightening LTV limits has larger economic effects than loosening them.

At the same time, we show that changes in maximum LTV ratios have substantial effects on credit and house price growth. Since LTV actions are likely to target these variables, we use inverse propensity weights to reduce the endogeneity problem. We find that these effects are likely causal.