

The Price of Leverage:
What LTV Constraints Tell about Job Search and Wages
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Summary

- Question: how does household leverage affect labor market outcomes?
- Setting:
 - Introduction of a LTV ceiling (85%) in Norway exogenously reduces household leverage
 - Treated group: households with predicted LTV (from ML models) above the ceiling
 - Focus on the sample of unemployed workers from mass layoffs
- Finding: lower household leverage leads to higher reemployment wages, longer unemployment durations, and broader job search (in terms of industries and occupations)
- Contributes to the growing literature on the labor market effects of household debt and macroprudential policies (e.g., Dobbie and Song, 2020; Bernstein, 2021; He and le Maire, 2022; Di Maggio, Kalda, and Yao, 2022, ...)

Comment 1: Effect of LTV Restriction

- Restricting LTV can have three effects:
 1. Discourage or delay homeownership (authors show that this is not the case)
 2. Use the same down payment to buy cheaper houses
 - Leverage goes up
 - Changes in type of housing and location. Can this have a separate effect on labor market outcomes?
 3. Buy the same house, but with higher down payment
 - Leverage goes up
 - Liquid assets go down - could have a separate negative effect on labor market outcomes
- Is the control group's liquidity constraint also affected by the reform?
 - Yes if the LTV ceiling also applies to home equity loans/cash out refinancing

Comment 2: Sample Selection

- The reform started in 2012, and sample ends in 2013
- Includes workers who buy homes up to 12 months before their displacement
- Average worker experiences an unemployment spell of 133 days, and LTV restriction increases unemployment spell by 79 days
- The full unemployment duration and reemployment wage for some workers are outside of the sample frame
- Suggestions:
 - Use hazard model to estimate effect on unemployment durations
 - Show robustness dropping workers laid off in the later part of the sample
 - Extend the sample period to later years

Comment 3: Mechanism

- Proposed mechanism: lower debt payments relaxes households' liquidity constraints (note: the restriction does not affect net wealth)
- The magnitudes are really large: reducing DTI by about 100% leads to a increase in unemployment durations by 79 days and a relative wage gain of 3.3pp
 - A 10% increase in UI replacement rate typically increases unemployment duration by 3.5 to 7 days and have zero or small positive effect ($<1\%$) on wages (Nakajima, 2012; Nekoei and Weber, 2017)
 - Dobbie and Song (2020): short-term payment reductions have no effect on wages
 - He and le Maire (2022): access to liquidity up to 20k USD increases unemployment duration by 4 days and reemployment wages by 1%
- What else could be going on?

Comment 3: Mechanism

- Financial distress
 - Individuals with high ETV (>85%) before the reform are likely to have negative or close to negative housing equity, which leads to costly default or lower labor supply/housing lock (Bernsten, 2021; Brown and Matsa, 2020)
 - Compare households with negative and positive housing equity (e.g., variation in housing price changes) and cross tabulate with liquidity constraints
- Behavioral explanations
 - Higher debt levels increase the level of anxiety and stress and lead to a “scarcity” of cognitive resources (Mullainathan and Shafir, 2013; Kaur et al., 2021)
 - Data on job search effort? Prescription drugs and mental health?
- Retraining programs: debt overhang reduces human capital investment
- Entrepreneurship: more housing equity as collateral

Conclusion

- Very interesting paper at the intersection of household finance, macro, and labor
- Suggestions:
 - Discuss other confounding effects of LTV restrictions
 - Address sample selection
 - Dig deeper into the mechanisms