Linkages Running between the Business Cycle, Lending and Movements in Housing Prices

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There have been lively discussions on the interconnectedness of the real economy and finance since the global financial crisis. These discussions are based on the recognition that the strengthening of the real economic and financial nexus over a long period of time lay at the root of the financial crisis. In this study, GDP, loans and housing prices, which are major variables of the real economic and financial sectors, are examined to understand the stylized facts of the interconnectedness in terms of the business cycle, and through historical decomposition the factors causing changes in these variables are measured dynamically to grasp their mutual impacts.

The results of the analysis in this paper can be summed up as follows: first, although the linkages running between housing prices and both GDP and lending have been strengthened since the financial crisis, the extent of their interrelation is lower than that in major countries. This seems partly attributable to the effects of the government real estate policies that have been constantly implemented in response to changes in the real estate market. These government policies have limited not only the extent of changes in housing prices but also their linkages with GDP and loans, helping the upward trends of both GDP and loans continue on a more stable path. Secondly, the interlinkages among these variables have intensified at times of monetary contraction rather than expansion. During periods of expansion, meanwhile, domestic variables are found to have fluctuated in line with overseas variables. Thirdly, there has been a clear relationship in which GDP and housing prices affect loans unidirectionally, and other interlinkages have not been strong. Since 2000, however, as loans have responded to housing prices more sensitively than in the past due mainly to real estate price hikes and increases in

households' mortgage loans, the power of GDP to influence lending appears to show a weakening pattern.

Based on these results, the following implications can be drawn: first, since housing prices have a growing influence on the domestic real economy and loan extension and the overseas sector also has substantial influence, we need to be vigilant against shocks from these sectors and monitor them constantly. Second, given that policy measures for stabilizing the real estate market, such as LTV and DTI regulations, contribute to reducing the possibility of systemic risks arising triggered by these sectors and, furthermore, that the economy is entering a recovery phase, we need to point out the positive roles that these regulations play in terms of financial stability.

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