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Commentary

Asset securitization in general—and mortgage securitization in particular—have grown dramatically during the past two decades. Has this growth influenced the effectiveness of monetary policy? Does a change in the federal funds rate have the same impact on output today that it did before the advent of securitization? If so, is that due to the effect of the federal funds rate on mortgage- and asset-backed security rates, or to non-interest-rate effects?

Arturo Estrella's paper uses two equations to explore such questions: the first determines whether the extent of securitization has affected the sensitivity of output to changes in the federal funds rate; the second tests if such a change is due to Federal Reserve control over mortgage rates or to changes in liquidity and/or credit channels. My comments focus on whether the paper's findings for mortgage-backed securities are likely to hold for asset-backed markets more generally.

A number of important differences between the two markets prevent us from drawing the same conclusions about them. First, other asset-backed markets have a shorter history than mortgage-based markets. Mortgage-based securitization began in the 1970s, while other assets were not securitized until the mid-1980s. Second, the two markets have different growth rates. Mortgage-based securities grew approximately 10 percent annually between 1995 and 2000, while overall asset-backed securities grew 30 percent over the same period.

Another important difference between the markets is that issuers of nonmortgage asset-backed securities are not federally sponsored. Many are not regulated financial institutions, and therefore may not have the same motivations as Fannie Mae and Freddie Mac. Stulz and Johnson (1985) suggest that secured debt may help firms alleviate agency problems associated with risky debt—a motivation clearly more important for non-government-sponsored firms than government-sponsored ones. The issuance and pricing of the nonmortgage securities will also be affected by credit conditions and perceived credit risk for firms that do not have an implied government guarantee. Credit spreads in the nonmortgage asset-backed market, for example, increased significantly in 1998 as a result of financial distress experienced by some high-risk automobile issuers and commercial real estate issuers. Finally, there is anecdotal evidence of a reverse relation between output and the extent of securitization for nonmortgage asset-backed security markets. James (1988) and Stanton (1998), for example, find that securitization by commercial banks increases during recessions and increases still more for weak banks.

Given such differences, it would be interesting to perform similar tests using data (available beginning in 1985) from other asset-backed markets. While the time series is not as long as that for mortgage data, we may still be able to make inferences about the effects of securitization in these markets on monetary policy—or at least to highlight differences between the impact of securitizaton on the nonmortgage and mortgage markets.

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Although we may be unable to draw conclusions from this paper about the asset-backed market in general, Estrella's work adds significantly to our knowledge of the effect of mortgage securitization on monetary policy. The different tests performed using single- and multi-family mortgage securitization ratios, for example, provide strong evidence that output is less sensitive to changes in the real federal funds rate as the extent of mortgage securitization rises. The paper also suggests that this change results not from loss of control over mortgage rates but from non-interest-rate effects such as liquidity and/or credit channels. Regarding methodology, it might be necessary to test the causality in the multi-family tests, since the securitization ratio in that case is cyclical.

References

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