FINANCE theory GROUP

Incentive issues in finance:

Household Finance and Consumer Credit Markets

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Consumer credit markets are of first-order importance for households, financial institutions and the broader economy. The recent Great Recession associated with significant decline in consumer spending and millions of foreclosures revived the debate regarding the appropriate structure of consumer credit markets and their implications for the broader economy. Part of this debate is also about the appropriate scope of public policy interventions during economic downturns. Focusing on major imperfections including asymmetric information, costly liquidation, and limited enforcement we will analyze the design of consumer credit contracts and their equilibrium consequences. We will pay close attention to housing and residential mortgages that account for a largest share of household assets and liabilities. In doing so we will also discuss the implications of lessons from the recent crisis for mortgage market design, monetary policy pass-through, and macro-prudential and housing policy interventions. We will conclude by discussing the recent developments in consumer credit markets, including the significant rise of fintech and shadow banking, and their implications for credit market equilibrium.

Outline

1) Overview of household finance and consumer credit markets
2) Consumer contract design and incentives in partial equilibrium
3) Consumer contract design and incentives in general equilibrium
4) Lessons from the Great Recession and post-crisis developments
5) Directions for future work

References

*The main papers are in bold font. It may be useful to start with three survey-style papers, which are marked with ** and are underlined, as an introduction to the topic. After that, it can be useful to read papers marked with *.*

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