Business Cycle Implications of Mortgage Spreads

by Karl Walentin

Discussion by Dave Backus
NYU PhD Alumni Conference | May 31, 2013
Questions

- Are mortgages different?
- What does an SVAR add to a CCF?
- What mechanism connects asset prices and business cycles?
- How do international linkages work?
Are mortgages different?

- Baa–Aaa spread
- Term spread
- Mortgage spread (long)
- Mortgage spread (short)

Dave Backus (NYU) Walentin discussion June 1, 2013
Are mortgages different?

- Asset prices and business cycles: my summary
  - Asset price information complements quantities
  - Risk spreads roughly contemporaneous
  - Returns mostly lead
  - Approximately a one-factor world

- Questions about mortgages
  - What’s the risk?
  - Are they different?
What does an SVAR add?

- VARs and SVARs
  - More complex data summary
  - No factor structure
  - IRFs not weighted by importance

- Causality
  - Are spreads cause or effect?
  - Where do they come from?
  - What delivers identification here?
What’s the mechanism?

- Start with $E(mr) = 1$
  - Is the action in $m$, $r$, or both?
  - How does it get there?

- Risk and the price of risk
  - Risk seems to be countercyclical
  - Why?
  - Ditto the price of risk
  - Why?
International linkages?

- Fact: asset prices more highly correlated than GDP growth
- So...
  - Where do Swedish mortgage spreads come from?
  - Is this how business cycles are transmitted?
  - Another clue about causality?