FISCAL STIMULUS IN ECONOMIC UNIONS: WHAT ROLE FOR STATES?

The Great Recession and the subsequent passage of the American Recovery and Reinvestment Act returned fiscal policy, and particularly the importance of state and local governments, to the center stage of macroeconomic policymaking. This paper addresses three questions for the design of intergovernmental macroeconomic fiscal policies. First, are such policies necessary? An analysis of U.S. state fiscal policies shows state deficits (in particular from tax cuts) can stimulate state economies in the short run but that there are significant job spillovers to neighboring states. Central government fiscal policies can best internalize these spillovers. Second, what central government fiscal policies are most effective for stimulating income and job growth? A structural vector autoregression analysis for the U.S. aggregate economy from 1960 to 2010 shows that federal tax cuts and transfers to households and firms and intergovernmental transfers to states for lower income assistance are both effective, with one- and two-year multipliers greater than 2.0. Third, how are states, as politically independent agents, motivated to provide increased transfers to lower-income households? The answer is matching (price subsidy) assistance for such spending. The intergovernmental aid is spent immediately by the states and supports assistance to those most likely to spend new transfers.


OUT OF SIGHT, OUT OF MIND: CONSUMER REACTION TO NEWS ON DATA BREACHES AND IDENTITY THEFT

The authors use the 2012 South Carolina Department of Revenue data breach to study how data breaches and news coverage about them affect consumers’ take-up of fraud protections. In this instance, the authors find that a remarkably large share of consumers who were directly affected by the breach acquired fraud protection services immediately after the breach. In contrast, the response of consumers who were not directly exposed to the breach, but who were exposed to news about it, was negligible. Even among consumers directly exposed to the data breach, the incremental effect of additional news about the breach was small. The authors conclude that, in this instance, consumers primarily responded to clear and direct evidence of their own exposure to a breach. In the absence of a clear indication of their direct exposure, consumers did not appear to revise their beliefs about future expected losses associated with data breaches.


THE ECONOMICS OF DEBT COLLECTION: ENFORCEMENT OF CONSUMER CREDIT CONTRACTS

In the U.S., creditors often outsource the task of obtaining repayment from defaulting borrowers to third-party debt collection agencies. This paper argues that an important incentive for this is creditors’ concerns about their reputations. Using a model along the lines of the common agency framework, the authors show that, under certain conditions, debt collection agencies use harsher debt collection practices than original creditors would use on their own. This appears to be consistent with empirical evidence. The model also fits several other empirical facts about the structure of the debt collection industry and its evolution over time. The authors show that the existence of third-party debt collectors may improve consumer welfare if credit markets contain a sufficiently large share of opportunist borrowers who would not repay their debts unless faced with “harsh” debt collection practices. In other cases, the presence of third-party debt collectors can result in lower consumer welfare. The model provides insight into
which policy interventions may improve the functioning of the collections market.


ON THE USE OF MARKET-BASED PROBABILITIES FOR POLICY DECISIONS

This paper seeks to delimit the conditions so that market-based probabilities provide all the information required by the policymaker to arrive at the best decision possible. While there are several practical considerations regarding how to derive market-based probabilities from financial prices, the discussion here is confined to a theoretical analysis that assumes no impediment to obtaining the market-based probabilities.


OWNER OCCUPANCY FRAUD AND MORTGAGE PERFORMANCE

The authors use a matched credit bureau and mortgage data set to identify occupancy fraud in residential mortgage originations, that is, borrowers who misrepresented their occupancy status as owner occupants rather than residential real estate investors. In contrast to previous studies, the authors' data set allows them to show that such fraud was broad based, appearing in the government-sponsored enterprise market and in loans held on bank portfolios as well. Mortgage borrowers who misrepresented their occupancy status performed worse than otherwise similar owner-occupants and declared investors, defaulting at nearly twice the rate. In addition, these defaults are significantly more likely to be “strategic” in the sense that their bank card performance is better and utilization is lower.


NATURAL AMENITIES, NEIGHBORHOOD DYNAMICS, AND PERSISTENCE IN THE SPATIAL DISTRIBUTION OF INCOME

The authors present theory and evidence highlighting the role of natural amenities in neighborhood dynamics, suburbanization, and variation across cities in the persistence of the spatial distribution of income. The authors’ model generates three predictions that they confirm using a novel database of consistent-boundary neighborhoods in U.S. metropolitan areas, 1880–2010, and spatial data for natural features such as coastlines and hills. First, persistent natural amenities anchor neighborhoods to high incomes over time. Second, naturally heterogeneous cities exhibit persistent spatial distributions of income. Third, downtown neighborhoods in coastal cities were less susceptible to the widespread decentralization of income in the mid-20th century and increased in income more quickly after 1980.


FINANCIAL CONTRACTING WITH ENFORCEMENT EXTERNALITIES

Contract enforceability in financial markets often depends on the aggregate actions of agents. For example, high default rates in credit markets can delay legal enforcement or reduce the value of collateral, incentivizing even more defaults and potentially affecting credit supply. The authors develop a theory of credit provision in which enforceability of individual contracts is linked to aggregate behavior. The central element behind this link is enforcement capacity, which is endogenously determined by investments in enforcement infrastructure. This paper sheds new light on the emergence of credit crunches and the relationship between enforcement infrastructure, economic growth, and political economy distortions.


THE DYNAMICS OF SUBPRIME ADJUSTABLE-RATE MORTGAGE DEFAULT: A STRUCTURAL ESTIMATION

The authors present a dynamic structural model of subprime adjustable-rate mortgage (ARM) borrowers making payment decisions, taking into account possible consequences of different degrees of delinquency from their lenders. The authors empirically implement the model using unique data sets that contain information on borrowers' mortgage payment history, their broad balance sheets, and lender responses. The authors’ investigation of the factors that drive borrowers’ decisions reveals that subprime ARMs are not all alike. For loans originated in 2004 and 2005, the interest rate resets associated with ARMs as well as the housing and labor market conditions were not as important in borrowers’ delinquency decisions as in their decisions to pay off their loans. For loans originated in 2006, interest rate resets, housing price declines, and worsening labor market conditions all contributed importantly to their high delinquency rates. Counterfactual policy simulations reveal
that even if the London Interbank Offered Rate (LIBOR) could be lowered to zero by aggressive traditional monetary policies, it would have a limited effect on reducing the delinquency rates. The authors find that automatic modification mortgages with cushions, under which the monthly payment or principal balance reductions are triggered only when housing price declines exceed a certain percentage, may result in a Pareto improvement, in that borrowers and lenders are both made better off than under the baseline, with lower delinquency and foreclosure rates. The authors’ counterfactual analysis also suggests that limited commitment power on the part of the lenders regarding loan modification policies may be an important reason for the relatively low rate of modifications observed during the housing crisis.


WORKER FLOWS AND JOB FLOWS: A QUANTITATIVE INVESTIGATION

This paper studies quantitative properties of a multiple-worker firm search/matching model and investigates how worker transition rates and job flow rates are interrelated. The authors show that allowing for job-to-job transitions in the model is essential to simultaneously account for the cyclical features of worker transition rates and job flow rates. Important to this result are the distinctions between the job creation rate and the hiring rate and between the job destruction rate and the layoff rate. In the model without job-to-job transitions, these distinctions essentially disappear, thus making it impossible to simultaneously replicate the cyclical features of both labor market flows.