UCLA Ziman Center for Real Estate

Real Estate and Urban Economics Seminar

The Cost of Consumer Collateral: Evidence from Bunching

Thursday, May 5, 2022
10:30 a.m. - 11:45 a.m.
Via Zoom Meeting Only

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Abstract

We show that borrowers are highly sensitive to the requirement of posting their homes as collateral. Using administrative loan application and performance data from the U.S. Federal Disaster Loan Program, we exploit a loan amount threshold above which households must post their residence as collateral. One-third of all borrowers select the maximum uncollateralized loan amount, and our bunching estimates suggest that the median borrower is willing to give up 40% of their loan amount to avoid collateral. Exploiting time variation in the loan amount threshold, we find that collateral causally reduces default rates by 35%. Our results help to explain high perceived default costs in the mortgage market, and uniquely quantify the extent to which collateral reduces moral hazard in consumer credit markets.

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