Macroprudential policy in Lithuania: what have we learned so far?

Gediminas Šimkus
Chairman, Bank of Lithuania
Bratislava, September 21st 2023
Macroprudential policy is an outside tool providing stability to the financial system

"Stability leads to instability. The more stable things become and the longer things are stable, the more unstable they will be when the crisis hits."

- Hyman Minsky
Bank of Lithuania is responsible for macroprudential policy implementation

Full set of measures – acting in line with risks:

- **Borrower-based measures**
  - Introduced in 2011 (LTV, DSTI, duration limit, interest rate test)
  - Activity-based approach since 2017

- **Capital buffers**
  - 2nd in EU to introduce positive neutral CCyB in 2017 (after the pandemic, many more EU countries have also chosen this path)
  - 1st in EU to implement sectoral SyRB for mortgage portfolios

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<th>Source</th>
<th>Bank of Lithuania.</th>
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<td>* The exception applies to borrowers whose balance of each previous loan is less than 50% of the value of the dwelling purchased with the corresponding loan.</td>
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<td>* The maximum monthly installment of the loan must not exceed 50% of sustainable income using 5% interest rate for calculation</td>
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5 lessons learned for the effective macroprudential policy

1. Leaning early in the cycle and having strategic patience
2. Ensuring a balance between European set-up and national implementation
3. Data is the king
4. Responsibility and ownership of macroprudential policies
5. Prevention of policy leakages
First lesson:

1. Leaning early in the cycle and having strategic patience

- The costs of macroprudential tightening are visible immediately, while benefits – only in long term
- The need for strategic patience

2. Ensuring a balance between European set-up and national implementation

3. Data is the king

4. Responsibility and ownership of macroprudential policies

5. Prevention of policy leakages
Second lesson:

1. Leaning early in the cycle and having strategic patience

2. Ensuring a balance between European set-up and national implementation
   - Agility of the EU-based toolkit
   - Flexibility in terms of national implementation

3. Data is the king

4. Responsibility and ownership of macroprudential policies

5. Prevention of policy leakages
Third lesson:

1. Leaning early in the cycle and having strategic patience

2. Ensuring a balance between European set-up and national implementation

3. Data is the king
   - When concentrated in the hands of the policymaker

4. Responsibility and ownership of macroprudential policies

5. Prevention of policy leakages
Fourth lesson:

1. Leaning early in the cycle and having strategic patience

2. Ensuring a balance between European set-up and national implementation

3. Data is the king

4. Responsibility and ownership of macroprudential policies
   - Policy needs to have clear goals in order to be effective
   - Responsible owner is also a clear communicator

5. Prevention of policy leakages
Fifth lesson:

1. Leaning early in the cycle and having strategic patience
2. Ensuring a balance between European set-up and national implementation
3. Data is the king
4. Responsibility and ownership of macroprudential policies

5. Prevention of policy leakages
   • Importance of a holistic approach
Future challenges for the macroprudential policy

- Macroprudential policy has little experience in high interest rates and inflation environment
- There are more acute challenges of digital runs that pose liquidity risks and alter the maturity transformation behavior of financial intermediaries
- New geopolitical environment increases cyber security risks
- There is an increasing footprint of climate change on real activity and the uncertainty of the transmission to the financial sector
Despite future challenges, core principles of macroprudential policy will continue to have importance.

What happens in economics over and over again is that there are two sets of effects. The immediately visible effects. And the widespread invisible effects. **The widespread invisible effects are often much more important than the visible ones.**

- Milton Friedman
Thank you