Soft Lending Standards, Hard Consequences: How Housing Booms Undermine Productive Investment*

Sangyup Choi†, Youngju Kim‡, and Youngjin Yun§

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Abstract

Housing booms expand banks' lending opportunities by raising collateral values but can also distort credit allocation toward real estate. Using two decades of Korean data that combine bank-level loan officer surveys, bank–firm matched credit records, and firm and bank balance sheets, we identify the causal effects of housing price shocks with a granular instrumental variable based on regional house price growth across 176 districts. Rising house prices lead banks to loosen mortgage standards while tightening business credit, especially to small and medium-sized enterprises (SMEs). These shifts translate into slower SME loan growth and stronger mortgage expansion. At the firm level, SMEs cut tangible investment sharply, whereas large firms remain unaffected. The evidence reveals a systematic reallocation of credit from productive to collateral-backed lending during housing booms, highlighting how financial cycles can weaken investment and long-run growth even without crises.

JEL classification codes: E22, E44, E51, G21, R31

Keywords: Housing booms; Credit reallocation; Firm investment; Bank lending survey; Granular instrumental variable

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†Yonsei University. Email: sangyupchoi@yonsei.ac.kr.

‡Bank of Korea. Email: econoky@bok.or.kr.

§Hanyang University. Corresponding author: youngjin.yun@outlook.com.