At the heart of the transmission mechanism of the global financial cycle to the domestic economy is the ability of financial intermediaries, whether banks or shadow banks to leverage up quickly to very high levels when financing conditions are favourable. Credit is excessively sensitive to the financing costs. It is possible, in addition to or instead of monitoring the cyclical properties of credit growth to use financial regulation to cut the ability of financial intermediaries to be excessively procyclical. Policy levers to do so are the leverage ratio or additional capital requirements.

Importantly, we should not forget that, usually, there are a number of important domestic distortions that interact with capital flows and credit growth. In practice, for political reasons, we see subsidies to investment in real estate and to debt in many countries. These subsidies are instrumental to creating the initial froth in real estate prices and investment. By all means, the first thing to do should be to remove these distortions. It is also important to remember that excessive borrowing by a country often means that someone else is lending excessively: macroprudential policies apply to lending countries just as well as they apply to borrowing countries

Finally, for any of this to work, macroprudential authorities should be independent. In return for their independence, macroprudential authorities should be accountable to elected bodies. Their mandate on financial stability should be as transparent as possible and well explained to the parliament and general public. This involves pointing out to the citizens, the very large costs of financial crises. Unfortunately, we have many very concrete examples of these huge costs all over the world: economic costs, social and political costs and even direct threats to the social fabric of our countries. Avoiding financial crises is a difficult task for which one is rarely thanked as in best cases nothing dramatic happens. It should nevertheless be a policy priority.