Household Debt and Credit
2015 in Review
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The views presented here are those of the authors and do not necessarily reflect those of the Federal Reserve Bank of New York, or the Federal Reserve System.
Total Debt Balance and its Composition

Trillions of Dollars

Source: FRBNY Consumer Credit Panel/Equifax
Auto and Student Debt Growth has Outstripped Mortgage and CC

Housing
Auto
CC
Student
Total Balance by Delinquency Status

Source: FRBNY Consumer Credit Panel/Equifax
Transition into delinquency for current mortgages

Source: FRBNY Consumer Credit Panel/Equifax
Number of Consumers with New Foreclosures and Bankruptcies

Source: FRBNY Consumer Credit Panel/Equifax
Notable in 2015

- Delinquencies continued to decline
  - At year end 5.4% of debt was delinquent, lowest since early 2007
  - New foreclosures are at the lowest level we’ve seen
    - Data begin in 1999
  - Bankruptcies also trending down
  - Student loan delinquency remains high

- Total household debt rose $289 billion, or 2.4%
  - Auto debt led the way, growing $109 billion (over 11%)
    - Outstanding auto debt crossed the $1 trillion mark in Q2
  - Other non-housing debt also grew strongly (4.7% - 6.5%)
  - Housing debt growth has been sluggish since end of deleveraging, and continued in 2015
WHITHER MORTGAGES?
Why has mortgage debt been so sluggish?

- In spite of rising house prices, mortgage credit hasn’t expanded much
- House prices up more than 1/3 since early 2012
- But mortgage debt hasn’t grown (up less than 1%)
- A stark contrast to last expansion
  - Both prices and debt roughly doubled 2000-2006
- Why is this time different?
House Prices and Mortgage Debt

Index (Jan 2000 = 100)

CoreLogic HPI (Left Axis)

Mortgage Debt Outstanding (Right Axis)

Source: FRBNY Consumer Credit Panel/Equifax and CoreLogic
Fact 1: Foreclosures’ influence is fading

- Foreclosures eventually result in debt being “charged off”: disappearing from borrower’s credit report, reducing balances
  - Charge offs were minor (< $50 billion per year) until 2007
  - Then grew sharply to > $250 billion in 2009-13
  - Now declining ($130 billion in 2015)

- So foreclosures are still reducing balances, but influence fading

- Can’t explain sluggish growth since 2012
Fact 1: Foreclosures’ influence is fading

Source: FRBNY Consumer Credit Panel/Equifax
Fact 2: Purchases not adding much

- Housing transactions typically add to outstanding debt
  - Some new construction purchased with (net) new mortgages
    - Housing starts still well below boom levels
  - Sellers’ (paid off) mortgages are smaller than buyers’ (opened)
    - Sellers have paid down debt
    - Especially true when prices are rising, buyer must borrow more

- In 2006 and 2007, transactions added $800B - $1T annually
- $200B in 2009-11, now back to $350B
- Much lower contribution to mortgage debt than during the boom
Fact 2: Purchases not adding much

$ Billion

Source: FRBNY Consumer Credit Panel/Equifax
Fact 3: Much less cash out than in boom

- Borrowers can take cash out of properties without moving
  - With a cash-out refinance
  - With a junior lien (e.g., Home Equity Loans or Lines of Credit)
- Very important during the boom
  - $300-$400 billion in cash withdrawn per year in 2003-2007
- Declined sharply during the bust
- $10-$40 billion annual rate since 2012
- Much lower contribution to mortgage debt than during the boom
Fact 3: Much less cash out than during the boom

Source: FRBNY Consumer Credit Panel/Equifax
Fact 4: First-lien principal pay-down has grown a lot

- 2015Q4 outstanding mortgage debt is $8.25T
- We’ve seen this level 3 times now (all Q4)
  - 2006: $170 billion in annual pay-down (2.1%)
  - 2011: $234 billion in annual pay-down (2.8%)
  - 2015: $288 billion in annual pay-down (3.5%)
    - $118 billion or 70% increase since 2006 on same base
Fact 4: First-lien principal pay-down has grown a lot

Amortization has increased by $90 billion per year since 2009
Why is pay-down share increasing?

- Three factors determine pay-down share
  - Interest rate
    - Loans with low rates have higher principal pay-down per dollar of payment
  - Loan age
    - Older loans have higher principal pay-down per dollar of payment
  - Term of loan
    - Loans with shorter terms have higher principal pay-down per payment

- All of these factors are currently pushing principal share up
Interest rate, term and age determine principal share

Source: Authors’ calculations
Savings from refinancing a $200,000 mortgage

30-yr @ 6.8%, pmt 78
Assumes borrower income of $75,000 finances all payments

Payment $1,303
Principal $ 263 (4.2% of income)

15-yr @ 2.7%, pmt 1

Payment $1,352 (+3.7%)
Principal $ 902 (14.4% of income)

Source: Authors' calculations
Stock of outstanding debt has aged since 2003

Mean loan age rises from 23 to 50 months

Source: New York Fed Consumer Credit Panel / Equifax
Mortgage rates much lower, especially for 15-year

7/06: 6.8%

12/12: 2.7%
Credit Score at Origination: Mortgages*

Tight lending standards mean lower interest rates for average borrower

Source: FRBNY Consumer Credit Panel/Equifax

* Credit Score is Equifax Riskscore 3.0; mortgages include first-liens only.
Effective rate on outstanding mortgages has fallen

Down over 50% (380 bps) since 2000

Source: Bureau of Economic Analysis
Mortgage payments and their composition

2008-2015: Total payment falls 8%, principal paydown rises 41%

Source: New York Fed Consumer Credit Panel / Equifax
Summary

- Between 2000-2006, house prices and mortgage debt both doubled
- Since 2012 house prices have risen 34%, mortgage debt < 1%
- Foreclosures’ effect on reducing debt is fading
- Equity withdrawal and transactions adding only modestly to balances
  - $400 billion vs $1.4 trillion annual
  - Stable since 2012
- A big change: increased principal paydown from aging stock of continuing debt and refinesances into lower rate, shorter term debt
  - $300 billion in paydown annually
  - A major increase in savings for these households
Explanations, implications and outlook

- Some of this is easy to understand
  - When borrower doesn’t move or refinance, debt gets older and principal payment goes up
  - Lower rates and shorter terms refinances largely due to . . .
    - . . . decline in overall rates
    - . . . especially low 15-yr r
  - Tighter standards mean average borrower gets a lower rate

- Some of it is less clear
  - Are less equity withdrawal and transactions due to . . .
    - . . . borrower caution
    - or
    - . . . tighter standards/supply?
  - Could be a sign of stress for some borrowers (eg young student borrowers)
Explanations, implications and outlook

- Whatever the causes, these factors are increasing personal savings for these borrowers

- Existing stock of debt likely to “age in place”
  - If rates go up, strong incentives to continue in low rate mortgage
  - Leading to slow increase in pay-down/saving

- Could be offset by increase in equity withdrawal or purchase borrowing
  - But little sign of that yet