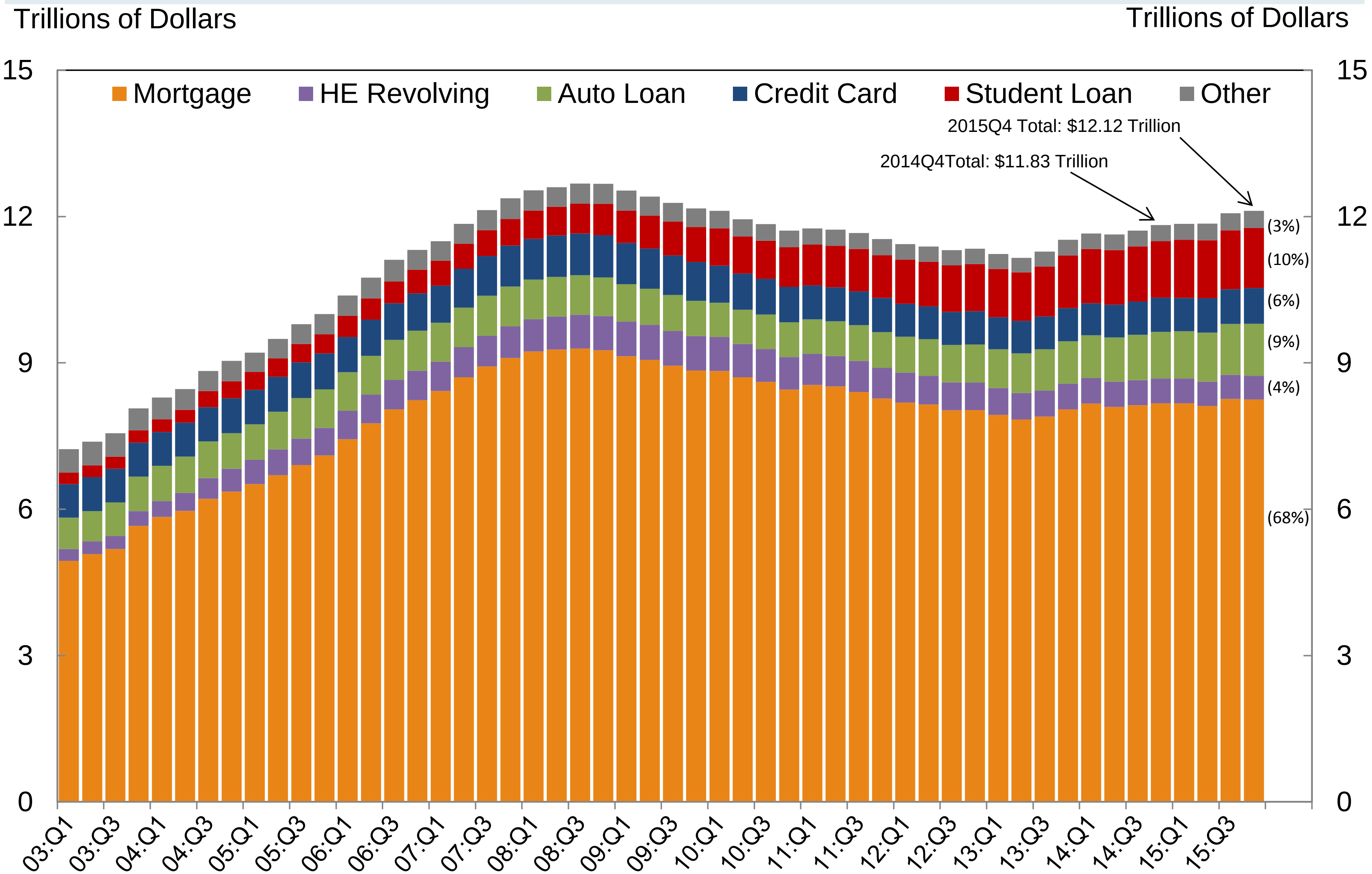
Household Debt and Credit
2015 in Review

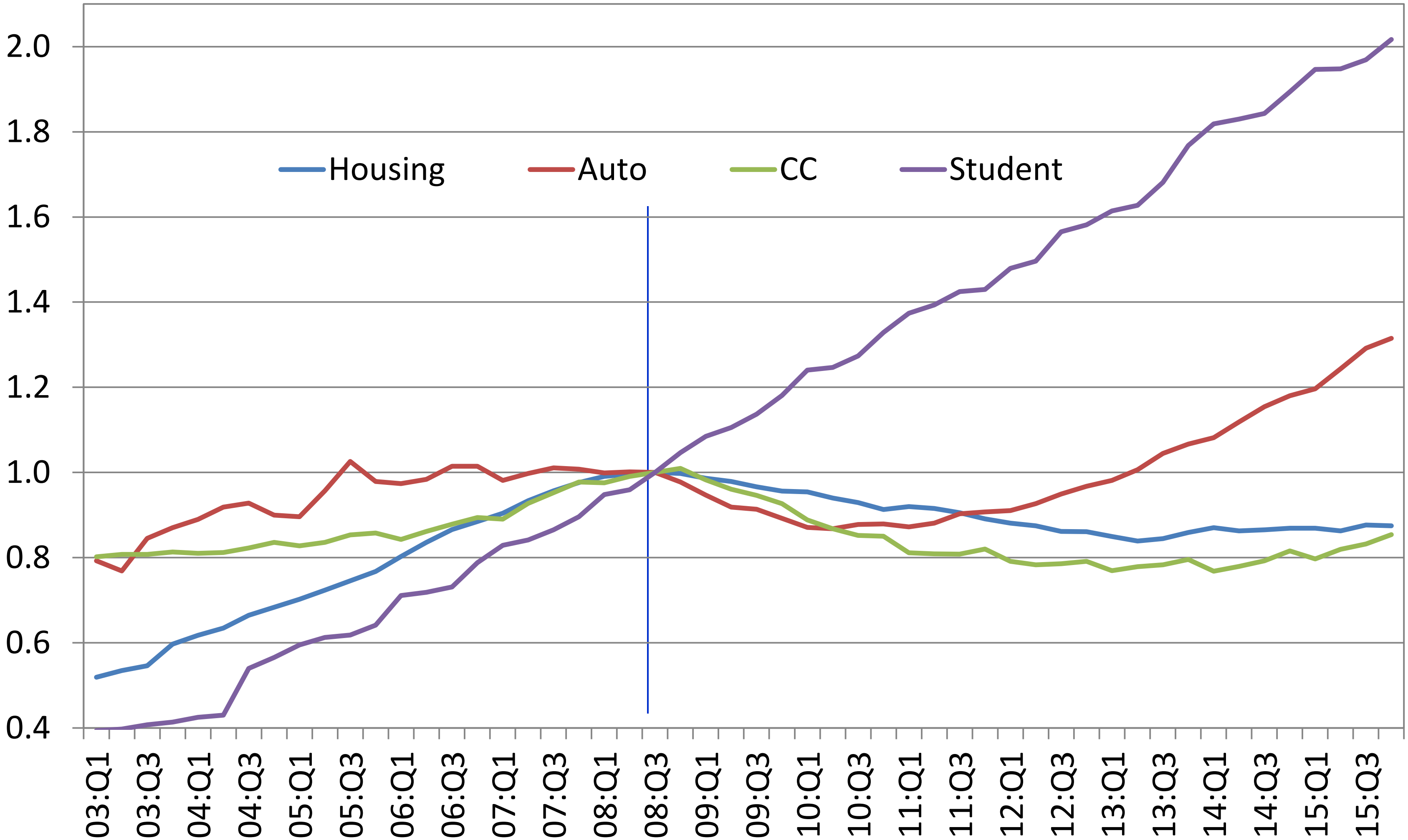
Andrew Haughwout

Total Debt Balance and its Composition

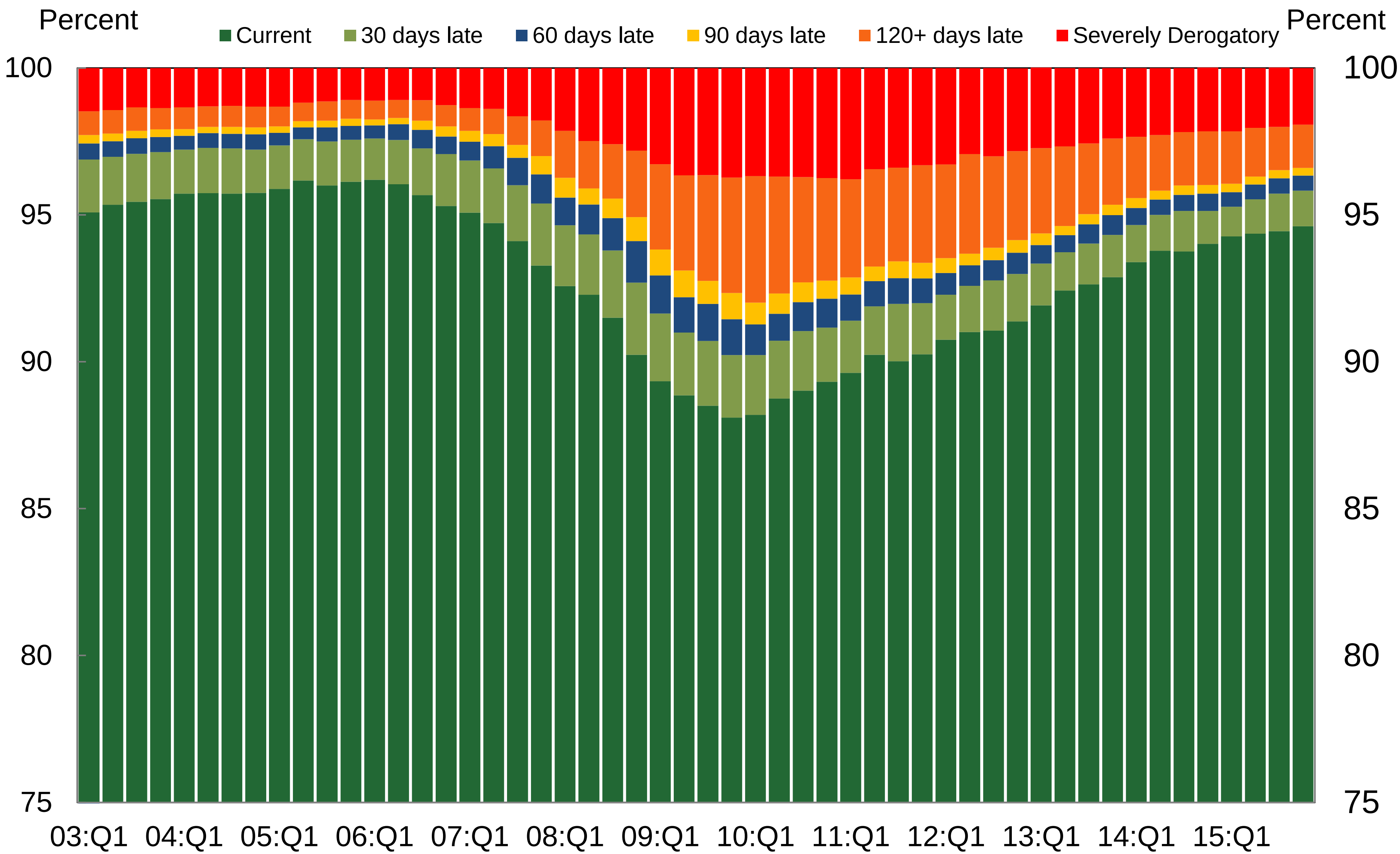


Source: FRBNY Consumer Credit Panel/Equifax

Auto and Student Debt Growth has Outstripped Mortgage and CC

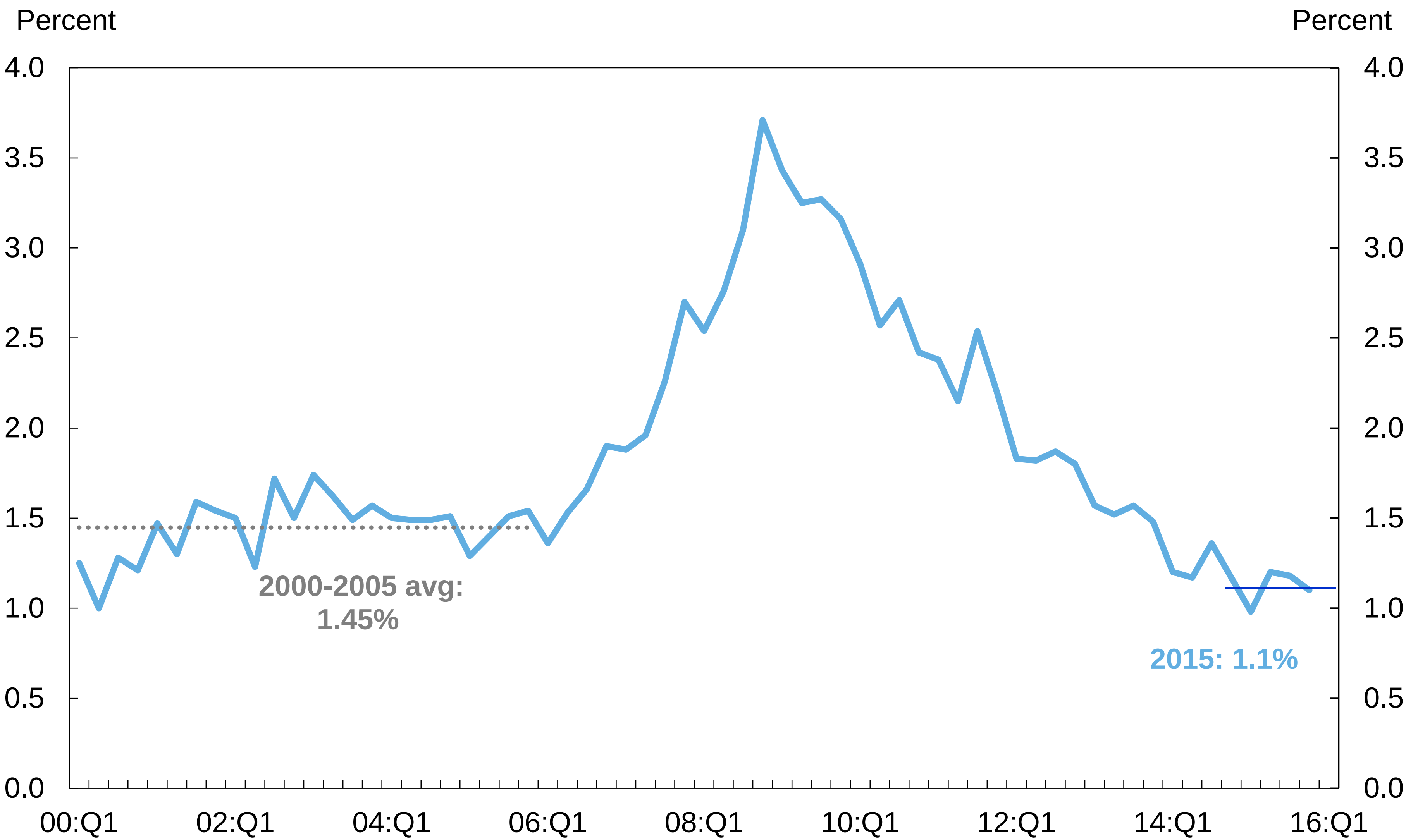


Total Balance by Delinquency Status



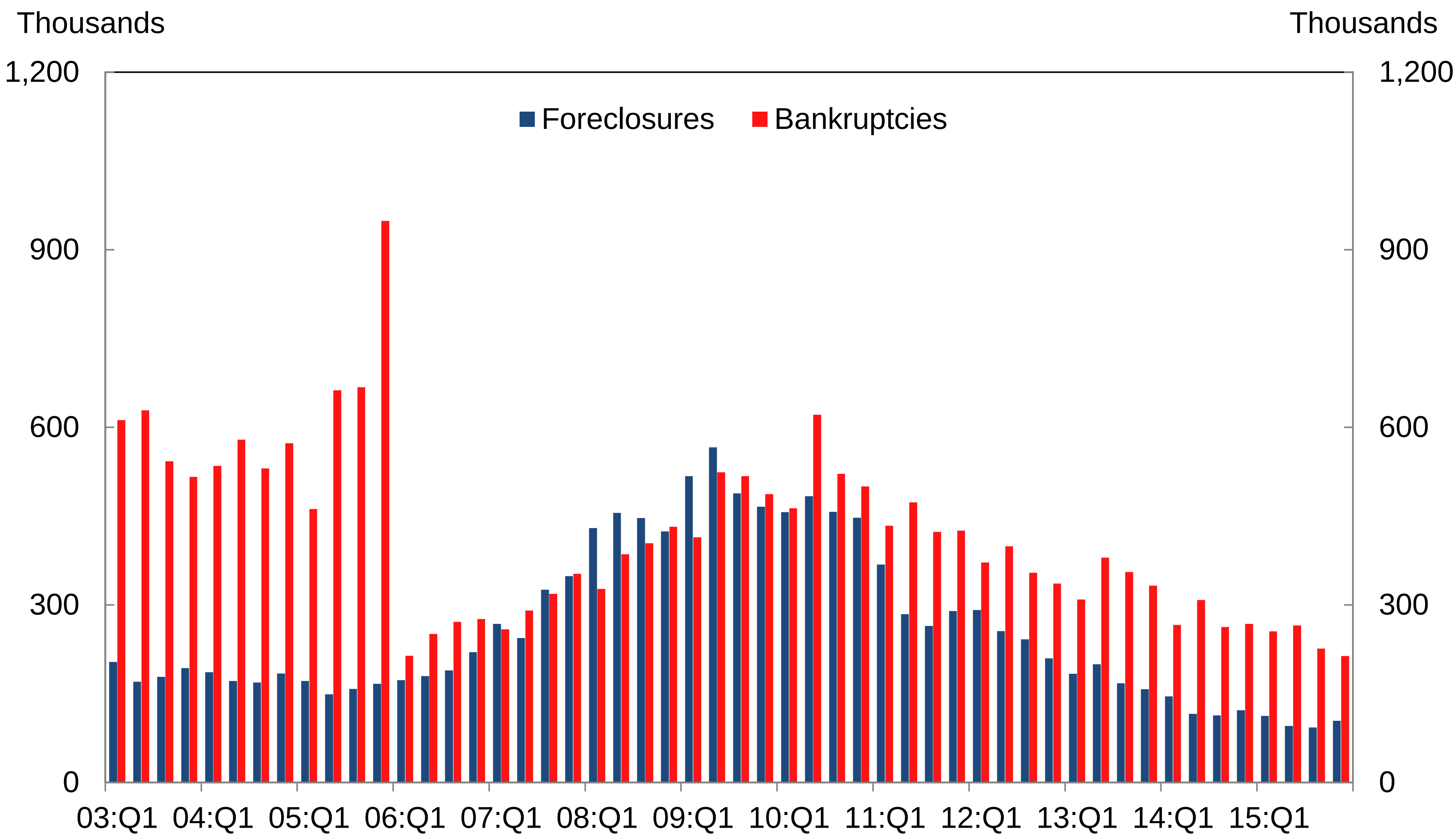
Source: FRBNY Consumer Credit Panel/Equifax

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

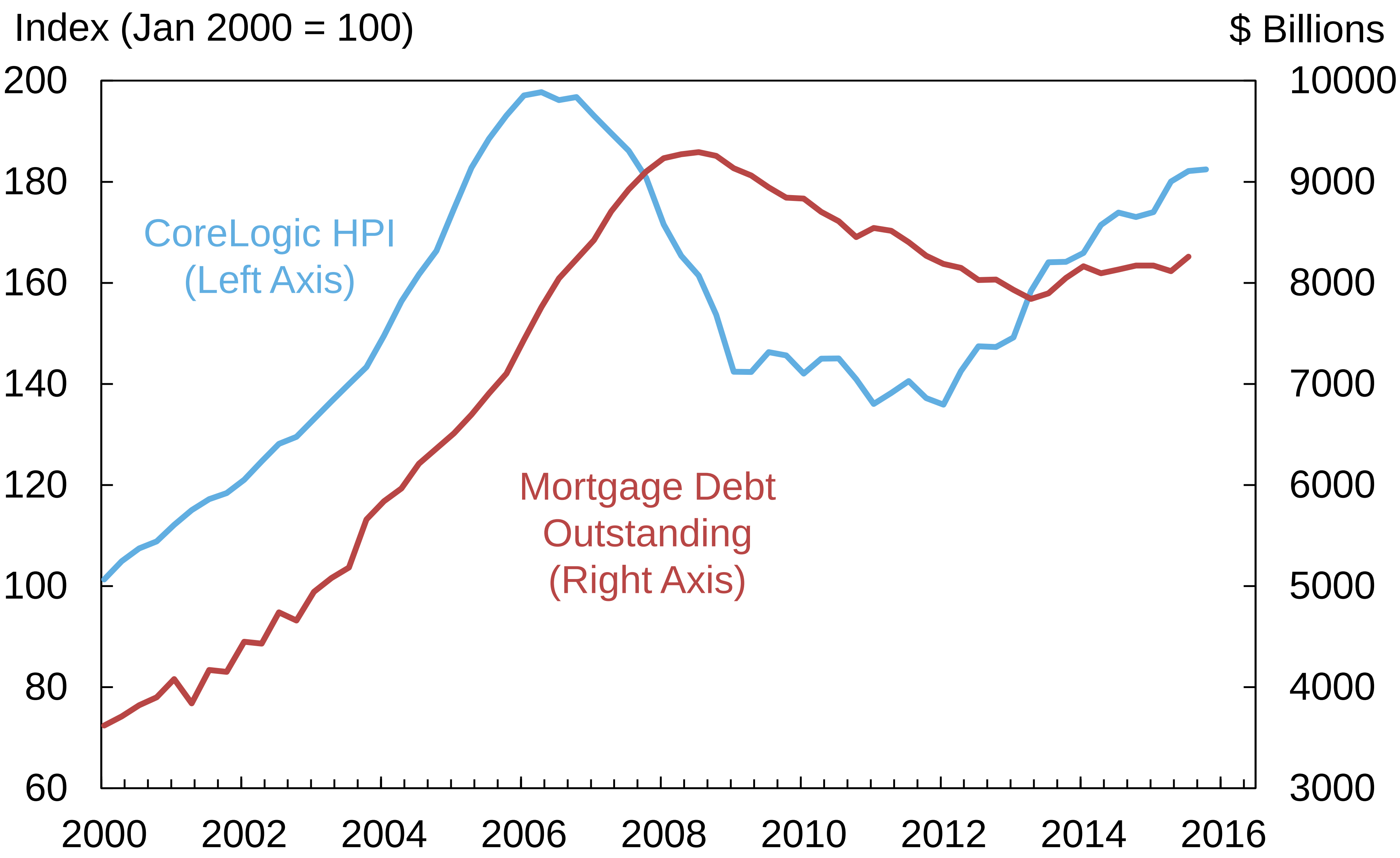
- Delinquencies continued to decline
  - At year end 5.4% of debt was delinquent, lowest since early 2007
  - New foreclosures are at the lowest level we've seen
    - Data begin in 1999
  - Bankruptcies also trending down
  - Student loan delinquency remains high
- Total household debt rose $289 billion, 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

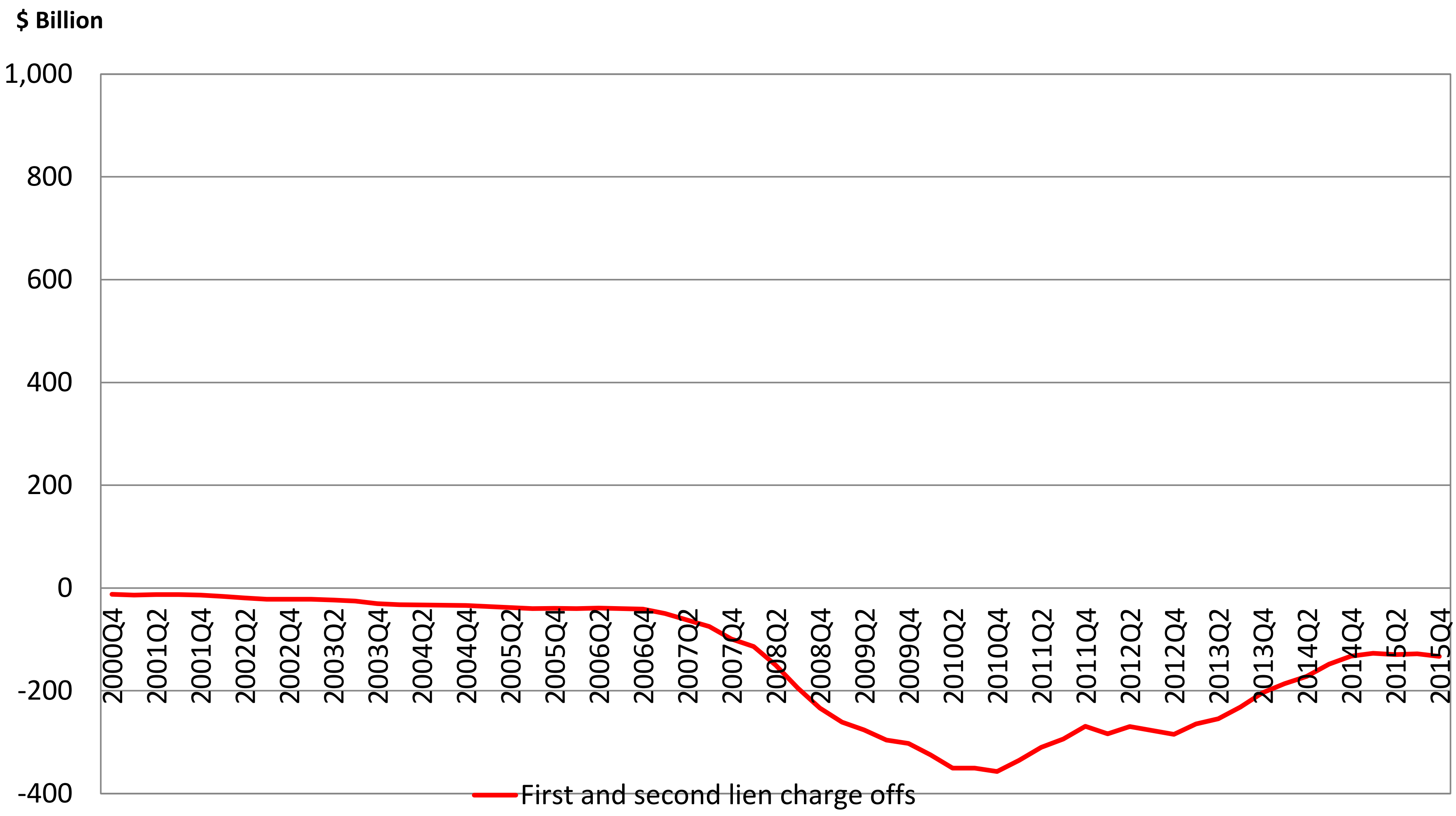


Source: FRBNY Consumer Credit Panel/Equifax and CoreLogic

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

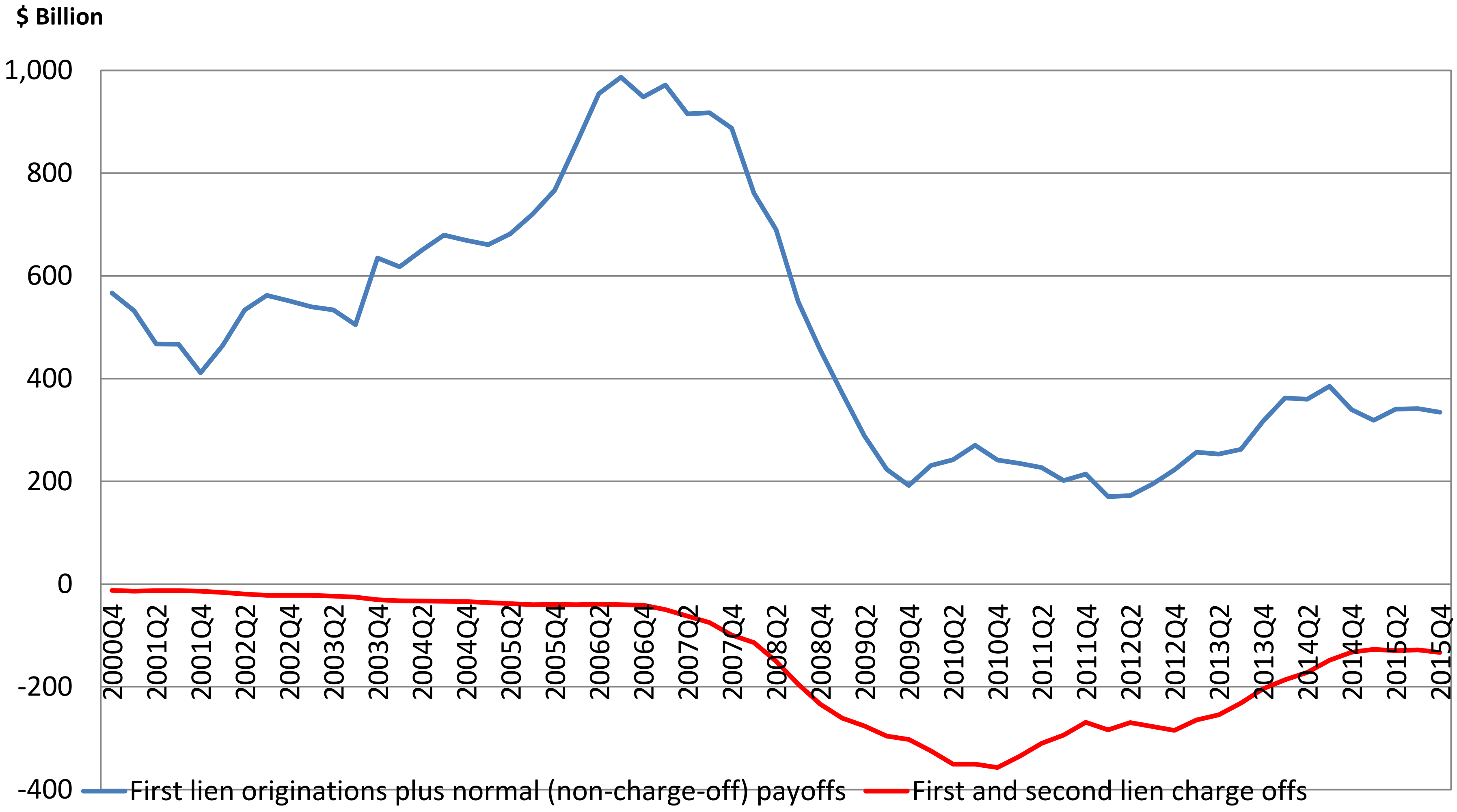


Source: FRBNY Consumer Credit Panel/Equifax

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

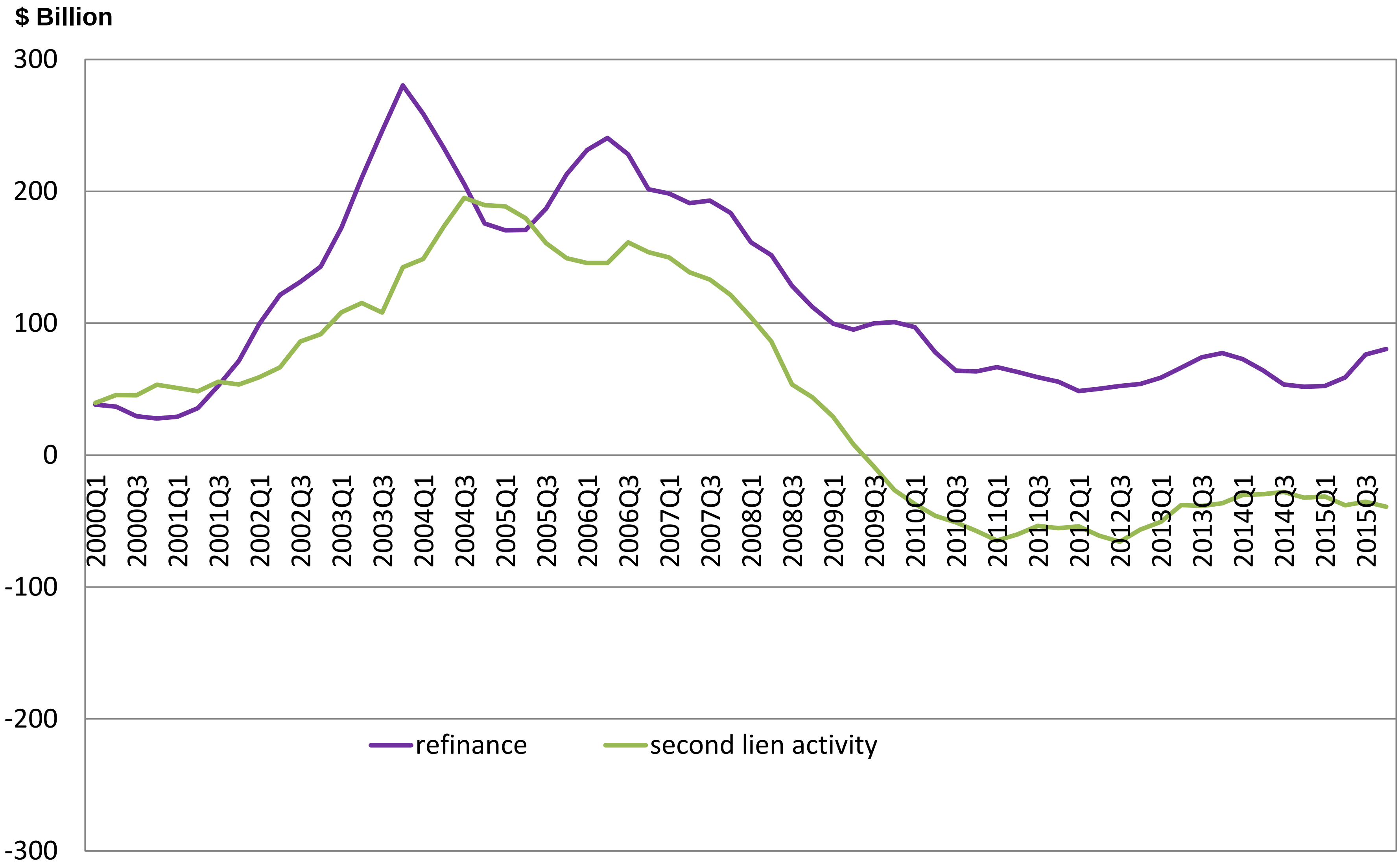


Source: FRBNY Consumer Credit Panel/Equifax

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 (eg, 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

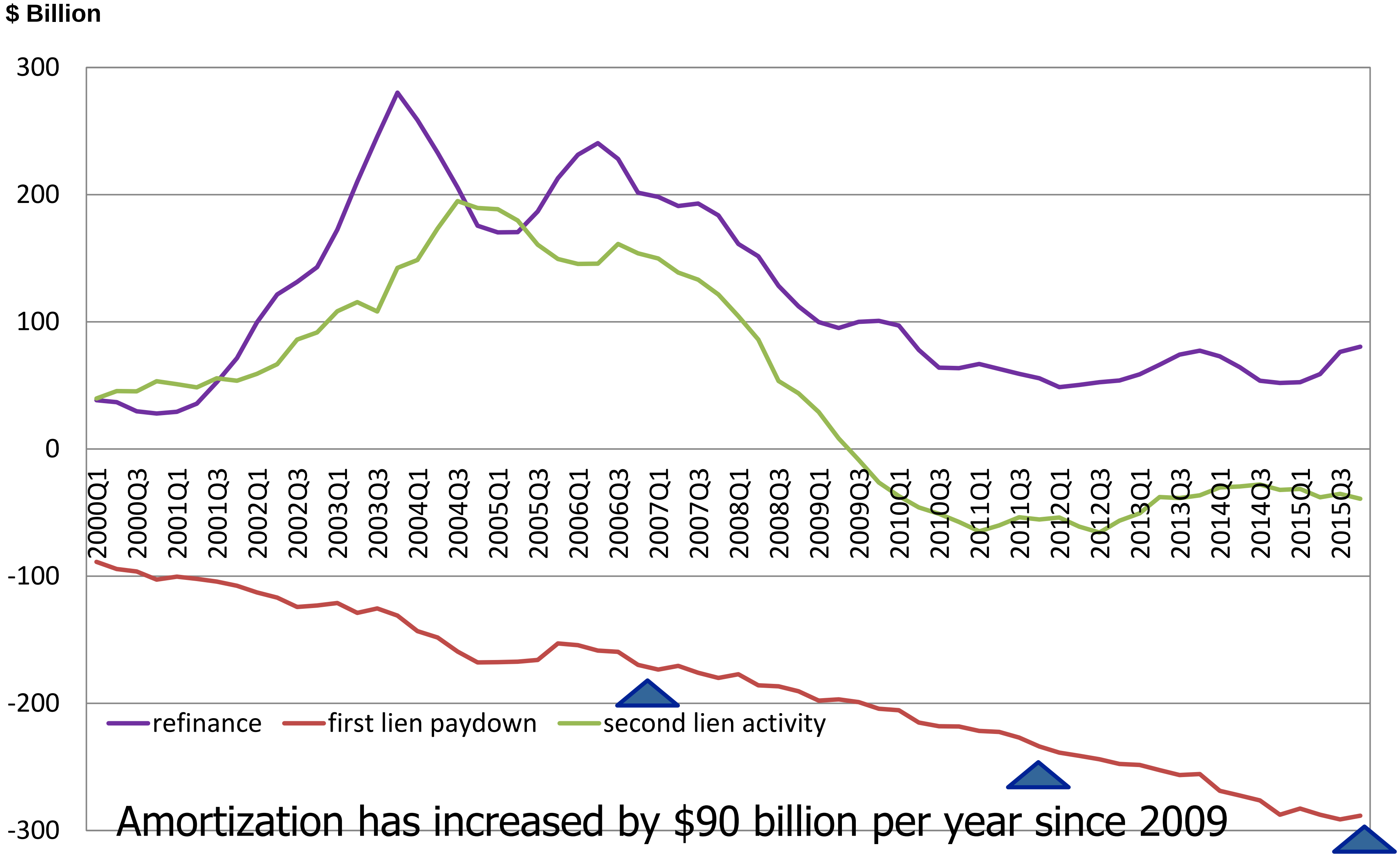


Source: FRBNY Consumer Credit Panel/Equifax

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

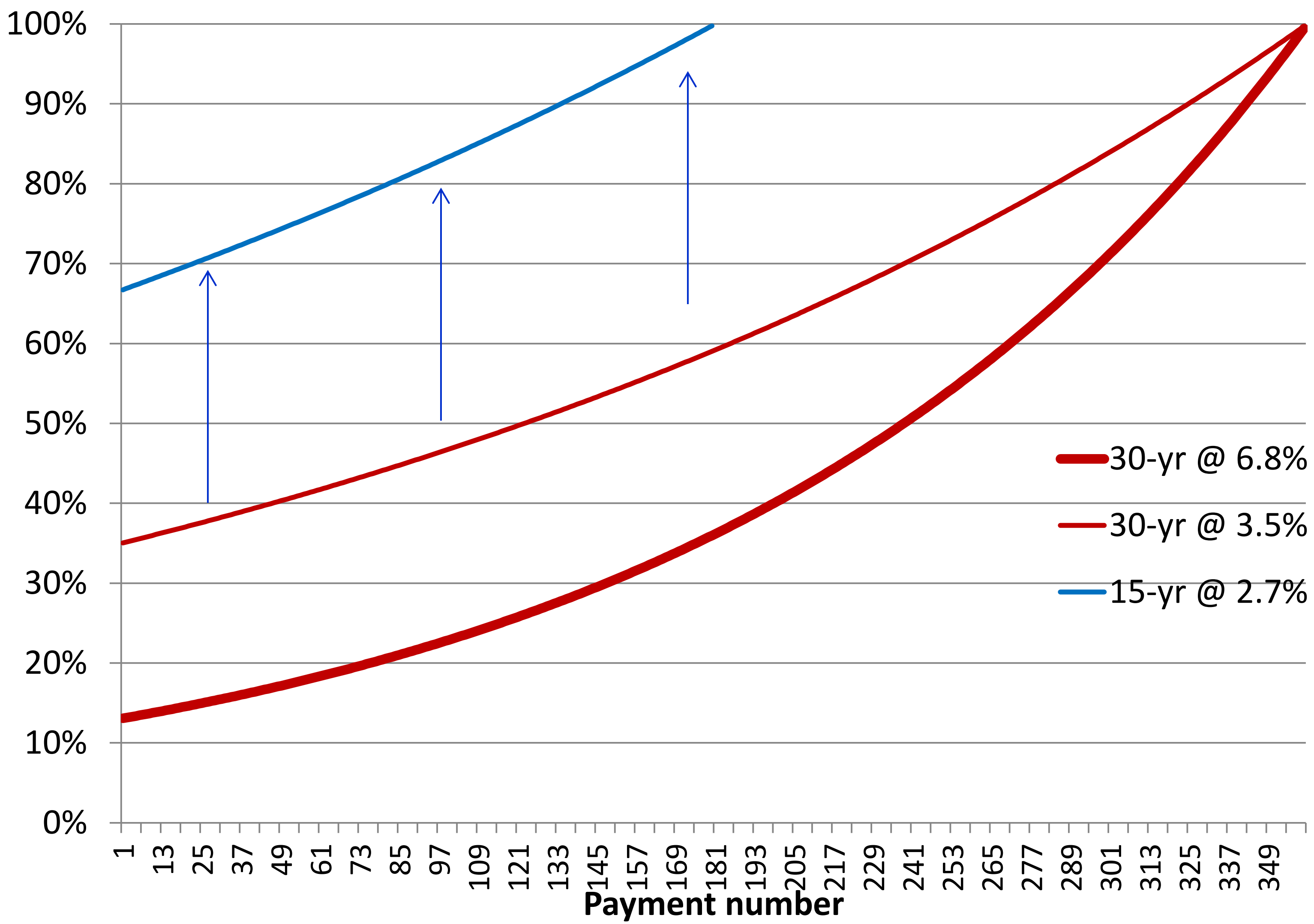
Fact 4: First-lien principal pay-down has grown a lot



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



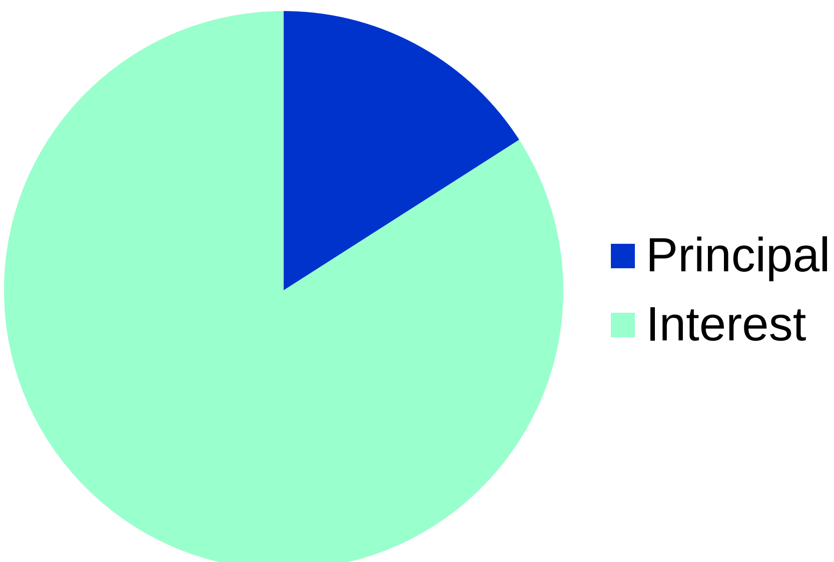
Source: Authors' calculations

Savings from refinancing a $200,000 mortgage

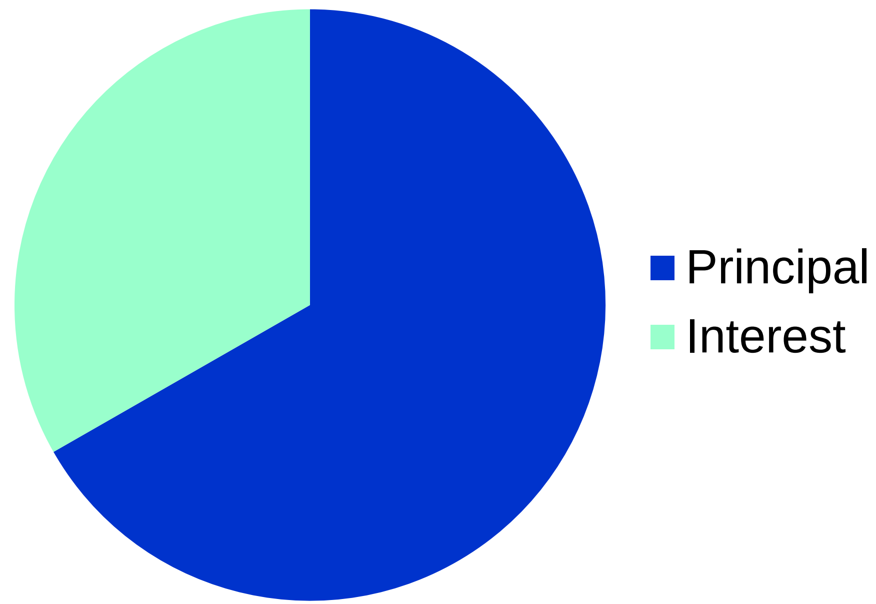
30-yr @ 6.8%, pmt 78

15-yr @ 2.7%, pmt 1

Assumes borrower income of $75,000 finances all payments



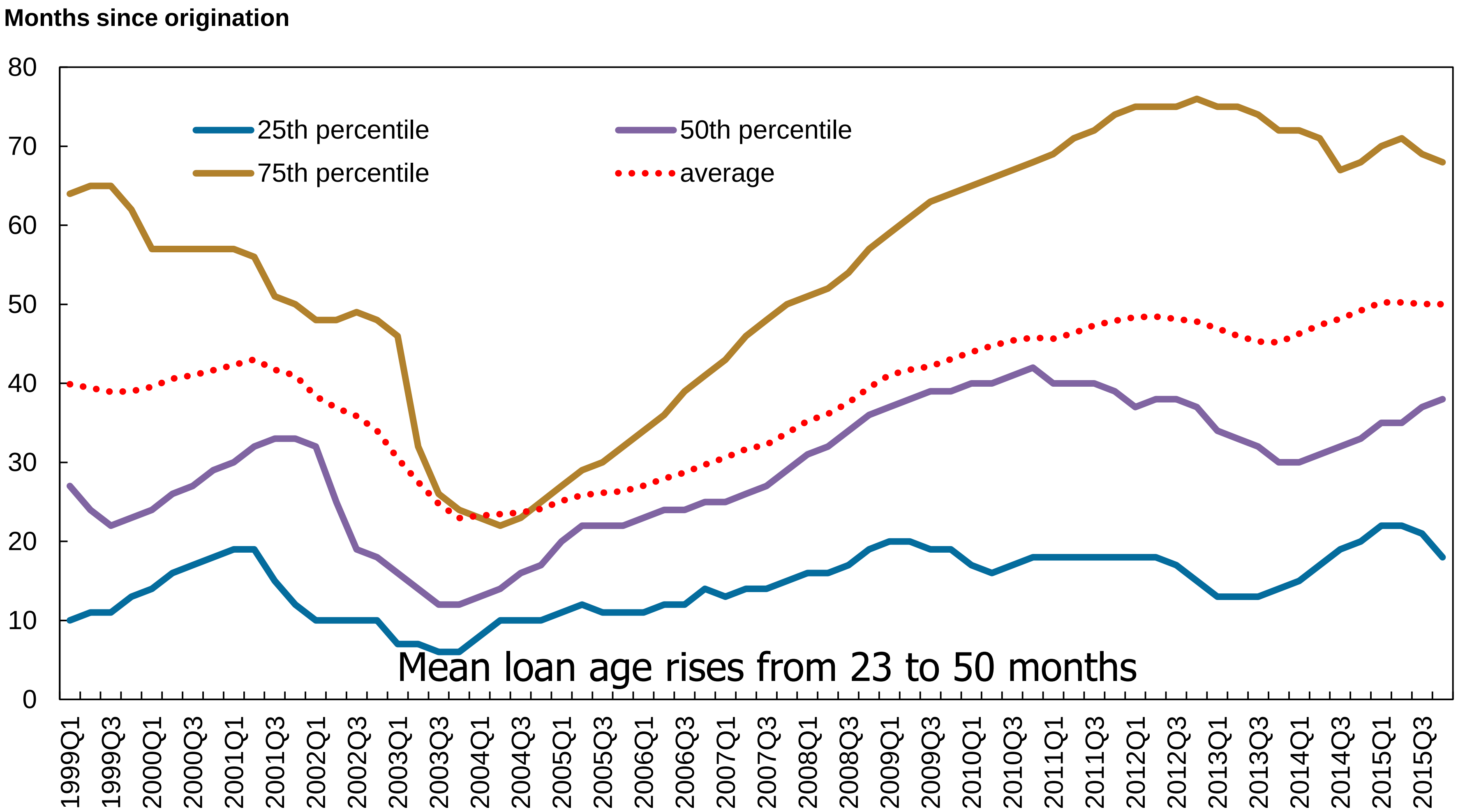
Payment $1,303
Principal $ 263 (4.2% of income)



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

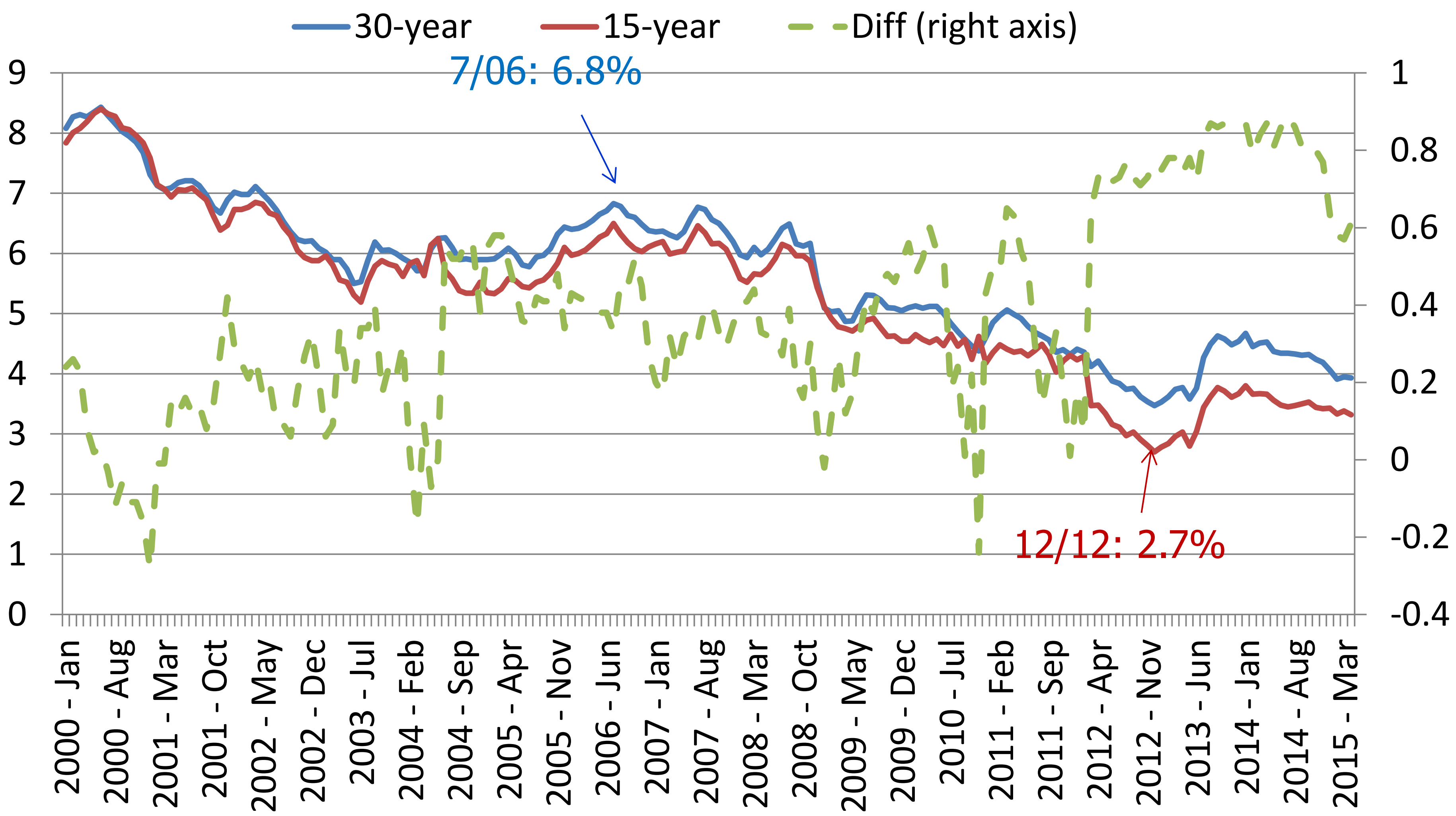
Source: Authors' calculations

Stock of outstanding debt has aged since 2003

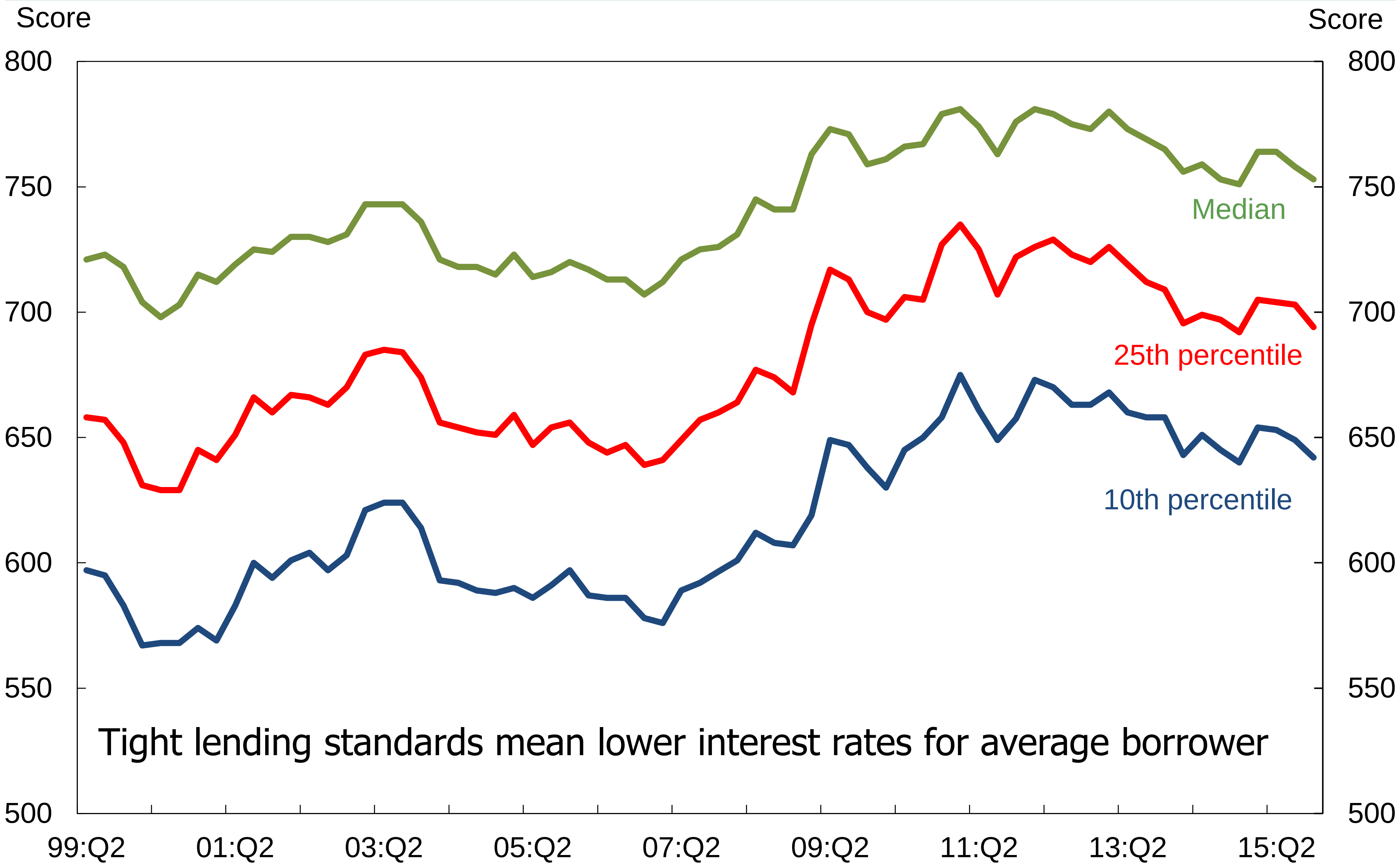


Source: New York Fed Consumer Credit Panel / Equifax

Mortgage rates much lower, especially for 15-year



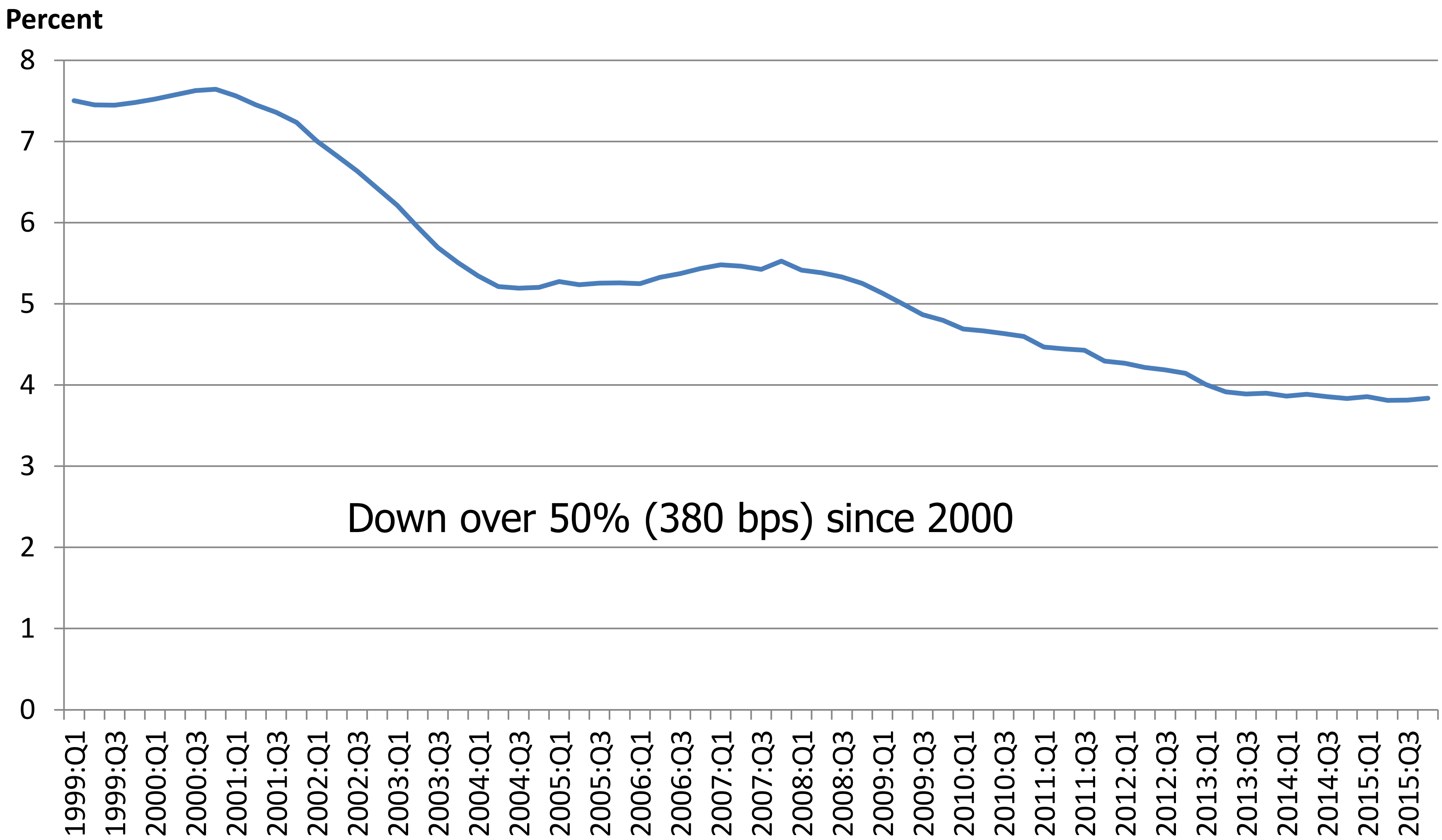
Credit Score at Origination: Mortgages*



Source: FRBNY Consumer Credit Panel/Equifax

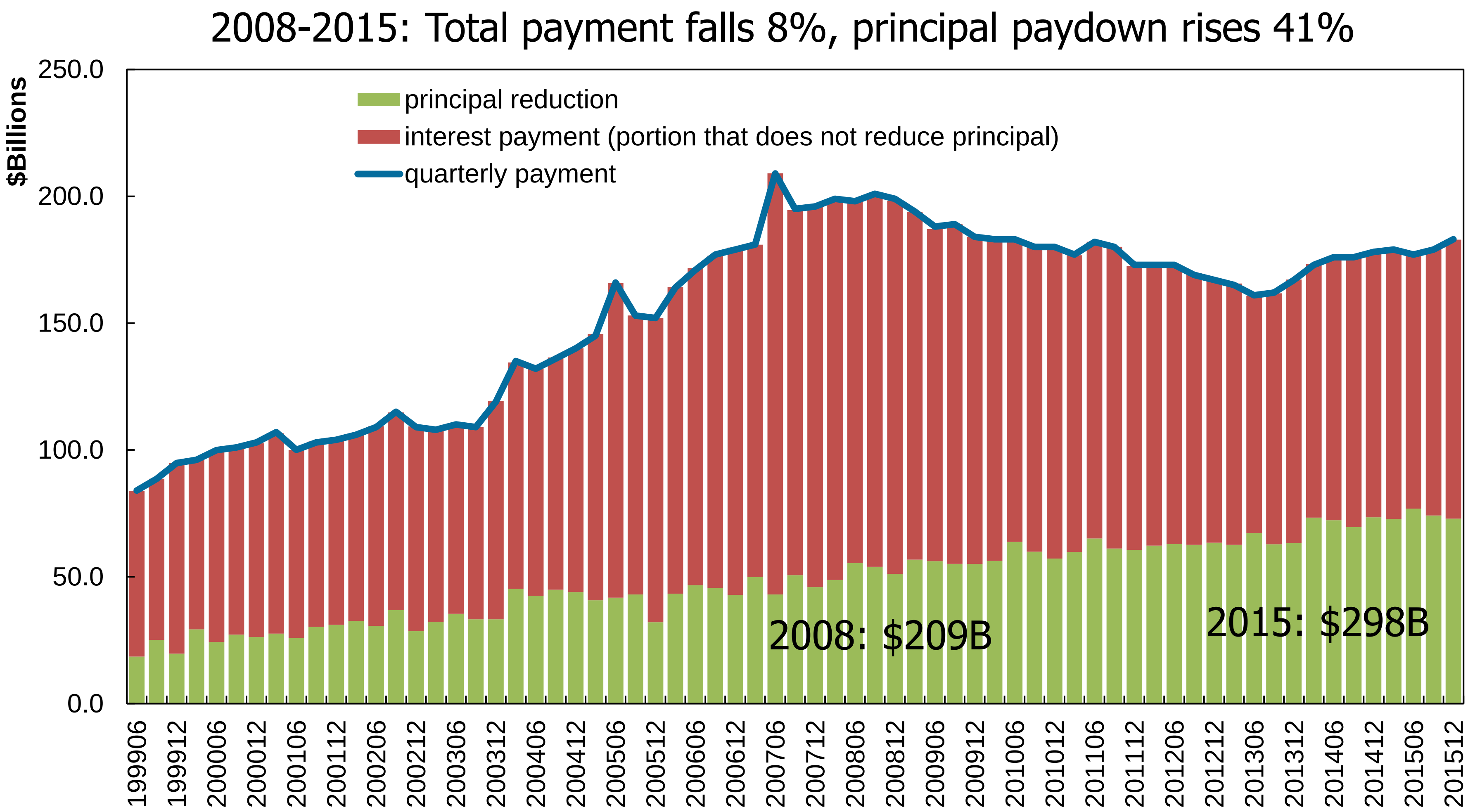
* Credit Score is Equifax Riskscore 3.0; mortgages include first-liens only.

Effective rate on outstanding mortgages has fallen



Source: Bureau of Economic Analysis

Mortgage payments and their composition



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 refinances 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