ECONOMIC UPDATE REGIONS
August 4, 2021

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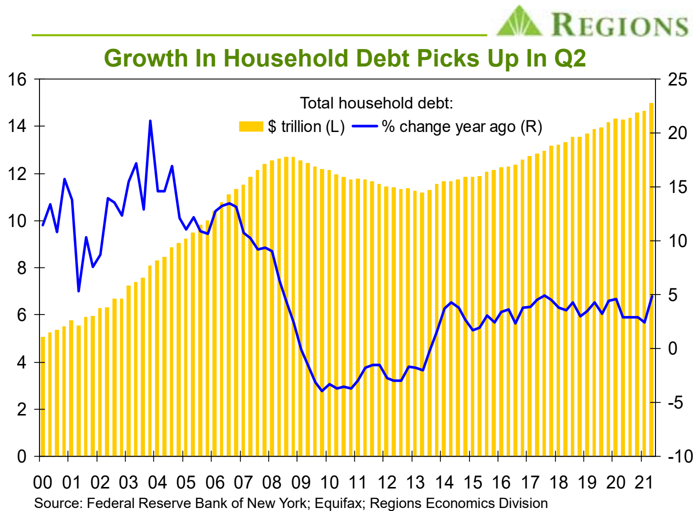
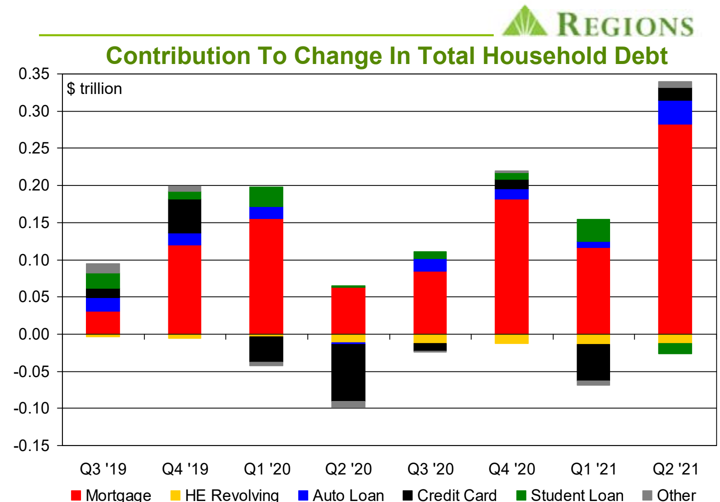
Q2 2021 Household Debt and Credit: Debt Growth Picks Up, Payment Burdens Remain Low

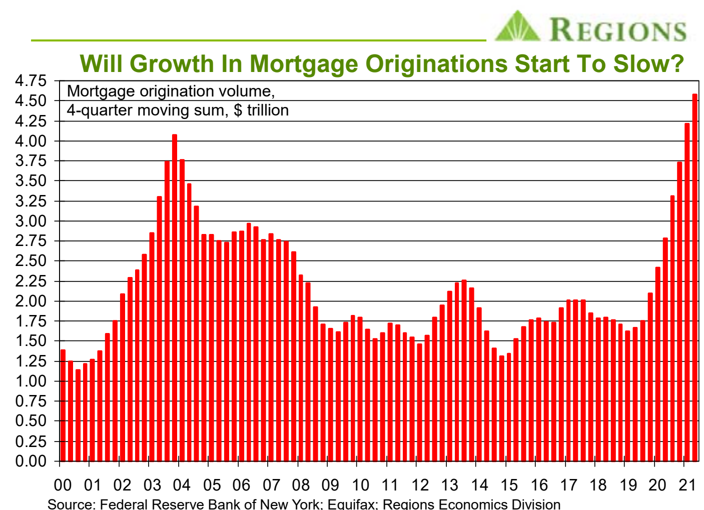
- Total household debt rose to $14.957 trillion in Q2 2021, an increase of $313 billion from Q1 2021
- Mortgage balances rose by $282 billion in Q2, non-mortgage debt increased by $31 billion
- As of Q2, 2.70 percent of outstanding household debt was in some stage of delinquency, compared to 3.05 percent in Q1

The Federal Reserve Bank of New York (New York Fed), in conjunction with Equifax, has released their latest quarterly report on trends in household debt. Total household debt rose to $14.957 trillion in Q2 2021, a $313 billion increase from Q1 2021 and the fourth straight quarterly increase after total debt declined slightly in Q2 2020. Mortgage debt accounted for the bulk of growth in total household debt in Q2, rising by $282 billion; after having declined in Q1 total non-mortgage debt increased by $31 billion in Q2, but the level of total non-mortgage debt nonetheless remains below the level as of Q4 2019. The increase in non-mortgage debt in Q2 was accounted for by growth in auto loans, credit card debt, and other forms of household debt, as outstanding home equity line balances and student loan debt declined. The overall delinquency rate on household debt fell to 2.70 percent in Q2 from 3.05 percent in Q1.





On an over-the-year basis, total household debt increased by 4.84 percent in Q2 2021, the largest such increase since Q3 2017. Still, growth in total household debt remains in the fairly narrow range that has prevailed since mid-2014 when a prolonged period of deleveraging came to a close, and growth in total household debt remains significantly below the rates that prevailed prior to the 2007-09 recession. Total mortgage debt was up 6.81 percent year-on-year in Q2, the largest such increase since Q1 2008, with auto loan debt up 5.36 percent, student loan debt up 2.15 percent, and other forms of household debt up 0.72 percent. In contrast, outstanding home equity line balances were down 14.13 percent year-on-year, making Q2 2021 the 46th consecutive quarter in which balances were down year-on-year, while credit card debt outstanding was down 3.67 percent year-on-year, the fifth straight quarter in which credit card debt was down year-on-year.



Mortgage originations, which include refinances, totaled $1.218 trillion in Q2 2021, marking the fourth consecutive quarter in which originations topped the $1 trillion mark. Indeed, over the past four quarters, mortgage originations have totaled $4.580 trillion, the largest four-quarter total in the life of the New York Fed's data. It is worth keeping in mind that the accelerating pace of house price appreciation has played a role in the growth in mortgage origination

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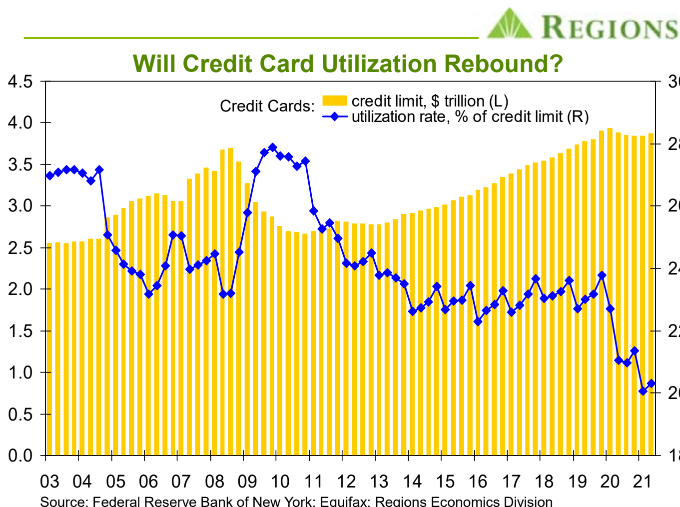
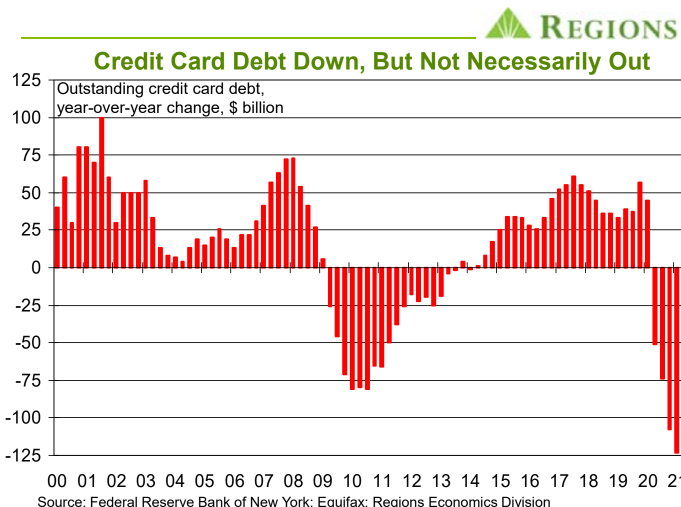
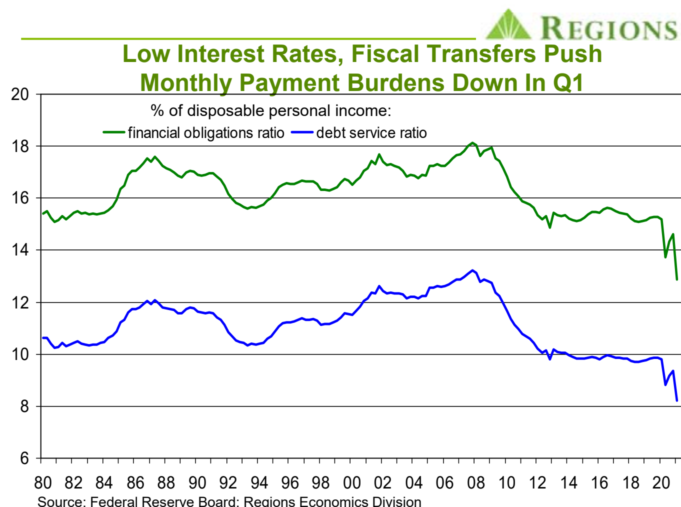
volume, which in Q2 more than made up for in an uneven performance for home sales and a pullback in mortgage refinancing. New home sales declined in Q2 while existing home sales rose modestly, but higher prices more than offset any drag from slowing sales volume. Data from the Mortgage Bankers Association (MBA) show the average loan size on purchase mortgage loan applications rose to $404,820 in Q2 2021, easily the highest on record and up 20.5 percent from the average loan size in Q2 2020. At the same time, refinancing activity tailed off a bit in Q2 while the MBA data show the average loan size on applications for mortgage refinancings fell to the lowest level since Q4 2018. It is uncertain how mortgage origination volumes will hold up in Q3; new home sales are likely to remain somewhat soft, in part reflecting builders focusing on clearing backlogs of unfilled orders as opposed to pushing new sales, while limited inventories and affordability constraints are weighing on existing home sales. At the same time, given the recent declines in interest rates, there could be another spurt of mortgage refinancings to support overall origination volumes. Still, even if the dollar volume of mortgage originations does slip in Q3, the level is likely to remain elevated.





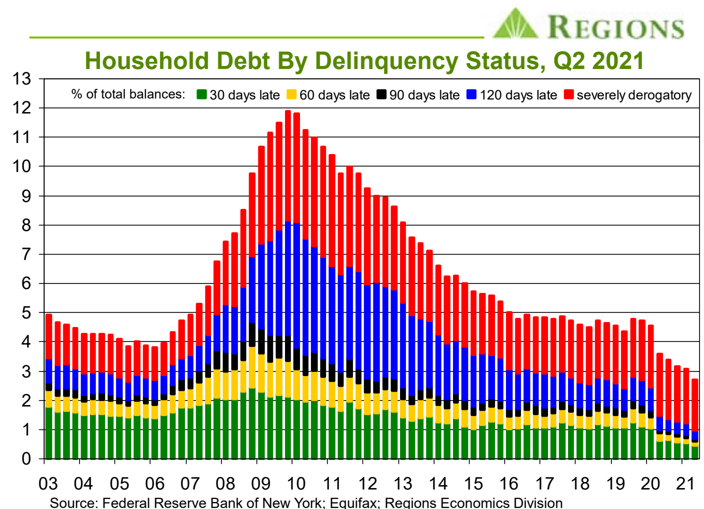
Credit card debt outstanding rose by $17 billion in Q2 2021, and while credit card utilization rose off of what in Q1 2021 was the lowest credit card utilization rate in the life of the New York Fed's data, the utilization rate remains well below pre-pandemic norms. Even with the modest increase in Q2, the level of credit card debt outstanding is $30 billion below the level as of Q2 2020 and is down 15.1 percent from the level as of Q4 2019. When the economy basically shut down and over 22 million people lost their jobs in the early phases of the pandemic, few would have imagined that would be followed by a sharp decline in credit card debt. But, three rounds of Economic Impact Payments and generous supplemental unemployment insurance benefits were powerful supports for household cash flows while at the same time lingering restrictions on many services industries held down consumer spending. Many households took advantage by building up saving and paring down debt, particularly credit card debt. It is not unexpected that, with the Economic Impact Payments having run their course, supplemental unemployment insurance benefits being scaled down before fully expiring in September, and services spending rebounding strongly, credit card debt would be increasing. That said, it is worth noting that there are strong seasonal patterns in credit card utilization, as can be seen in the first chart above – in any given year, utilization tends to fall in Q1 (a post-holiday pause), then rises through the balance of the year, peaking in Q4. It is also worth noting that the increase in credit card debt seen in Q2 2021, up 2.21 percent from Q1, is right in line with the typical Q2 increase. As such, it remains to be seen whether credit card utilization is simply reverting back to typical seasonal patterns, though from a much lower base, or whether Q3 and subsequent quarters will see outsized increases in utilization as disposable personal income reverts back to more normal growth patterns and household savings are further pared down. Our sense is that utilization rates will end up falling back in line with pre-pandemic norms, though it may take some time to get to that point.



The combination of lower non-mortgage debt, low interest rates, and disposable personal income being propped up by generous fiscal transfers led to a significant decline in monthly household debt service burdens in Q1. Both the household debt service ratio and the broader household financial obligations ratio fell to the lowest on record in Q1 2021, which is the latest available data point. As noted above, however, with fiscal transfers having largely run their course and labor earnings resuming their normal role as the biggest driver of growth in personal income, monthly

debt service burdens will start to push higher, and when the Q2 data are available they will likely show a modest increase. Still, with interest rates remaining so low and growth in household debt likely to remain moderate, any increases in monthly debt service burdens are likely to be gradual. It is also worth noting that prior the pandemic monthly debt service burdens were bumping along at what at the time were the lowest in the life of the data, reflecting the prolonged period of deleveraging in the aftermath of the 2007-09 recession and what subsequently was a much slower pace of growth in household debt than had prevailed in the years prior to that recession. That, to us, will be the relevant marker over coming quarters, i.e., whether monthly payment burdens fall back into line with pre-pandemic norms or push above them, and we think the former is more likely than the latter.

Overall delinquencies fell further in Q2 2021, with 2.70 percent of household debt in some stage of delinquency, down from 3.05 percent in Q1 2021 and 203 basis points below the overall delinquency rate in Q4 2019. Low interest rates and generous fiscal transfers have helped push delinquency rates lower, so it will be worth monitoring the performance of household debt now that fiscal transfers are providing much less support for personal income than has been the case over recent quarters. Note that early-stage delinquencies (i.e., combined 30-day and 60-day delinquency rates) have fallen to the lowest in the life of the New York Fed's data. Forbearance plans have played a role in the decline in the overall delinquency rate (note that reporting conventions differ as to whether balances in forbearance are reported as being delinquent), injecting some uncertainty into the path of delinquencies in coming quarters as many of the forbearance periods now in place come to an end.



In terms of mortgage debt, the New York Fed's data are in line with data from the Mortgage Bankers Association (MBA), showing inflows into delinquency having been declining for quite some time now and are now at the lowest in the life of the data. One factor behind this pattern is that mortgage loan originations have been highly concentrated amongst borrowers with higher credit scores. In 2020, 69.8 percent of all mortgage loan originations were to borrowers with credit scores of 760 or above, and in Q2 2021 that share was 71.3 percent. Whether that is an equitable or desirable allocation of mortgage credit is another question for another day, but in terms of the discussion here this is a key factor behind the long-running improvement in mortgage loan performance. The obvious caveat here is that roughly 1.7 million mortgage loans remain in forbearance, and many forbearance periods will be ending in the months ahead (in the MBA data, mortgage loans in forbearance are reported as delinquent, which is the main reason late-stage delinquency rates remain elevated). It is reasonable to assume that some borrowers now in forbearance will need assistance beyond the end of their forbearance period and that at least some of these loans will progress to foreclosure. Still, given notably lean inventories of new and existing homes for sale and considerably stronger equity positions, any increase in foreclosures figures to be much less disruptive to the housing market than was the case in the last cycle, particularly as the number of foreclosures will not come close to that seen in the last cycle.

The pandemic and the efforts to stem its spread and the policy response brought about profound changes in patterns of economic activity and in household finances. What remains to be seen is whether, or to what extent, any of these changes will be lasting. Even without the Delta variant of the COVID-19 virus throwing a wrench into the works as activity was starting to normalize, it would have taken several more quarters to answer that question. Clearly, there are pockets of financial distress in the household sector that will bear watching in the months ahead. On the whole, however, lower debt service burdens have left households on firmer financial footing than would have seemed likely at the onset of the pandemic.

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