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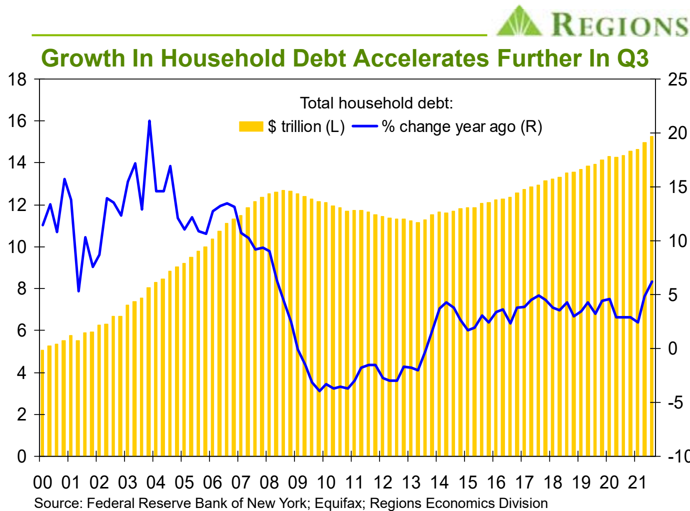
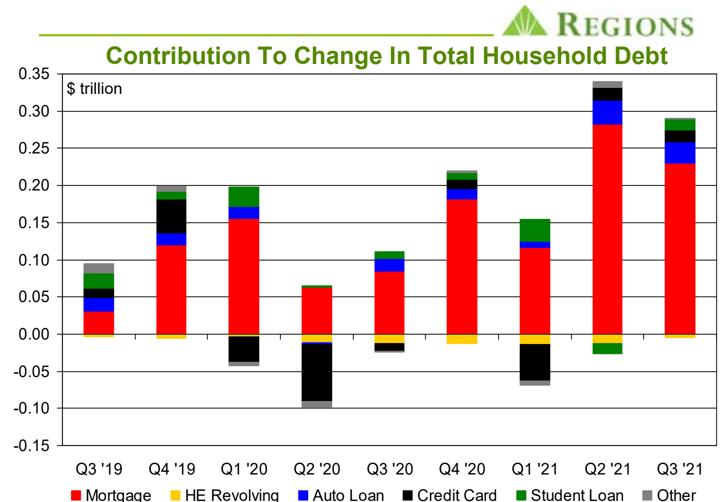
Q3 2021 Household Debt and Credit: Debt Growth Accelerates, Payment Burdens Still Low

- Total household debt rose to $15.243 trillion in Q3 2021, an increase of $286 billion from Q2 2021
- Mortgage balances rose by $230 billion in Q3, non-mortgage debt increased by $56 billion
- As of Q3, 2.70 percent of outstanding household debt was in some stage of delinquency, unchanged from Q2

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 $15.243 in Q3 2021, a $286 billion increase from Q2 2021 and the fifth straight quarterly increase after total debt declined slightly in Q2 2020. Mortgage debt again accounted for the bulk of growth in total household debt in Q3, rising by $230 billion; total non-mortgage debt increased by $56 billion in Q3, but the level of total non-mortgage debt nonetheless remains below the level as of Q4 2019. The increase in non-mortgage debt in Q3 was accounted for by growth in auto loans, credit card debt, and student loans, with outstanding home equity line balances declining, marking the 40th consecutive quarterly decline and 49th decline in the past 50 quarters. The overall delinquency rate on household debt held steady at 2.70 percent in Q3.





On an over-the-year basis, total household debt increased by 6.20 percent in Q3 2021, the largest such increase since Q1 2008. Note from the first chart above that growth in total household debt had held within a fairly narrow range since mid-2014, when the prolonged period of deleveraging after the 2007-09 recession came to a close. It remains to be seen whether Q3 marks a lasting break-out from that fairly narrow range or a short-lived burst, though our sense is that over-the-year growth will be slower in Q4 2021. Either way, growth in total household debt nonetheless remains significantly below the rates that prevailed prior to the 2007-09 recession. Total mortgage debt was up 8.22 percent year-on-year in Q3, the largest such increase since Q1 2008, with auto loan debt up 6.10 percent, student loan debt up 2.46 percent, and other forms of household debt up 1.44 percent. In contrast, outstanding home equity line balances were down 12.43 percent year-on-year, while credit card debt outstanding was down 0.37 percent year-on-year, the sixth straight quarter in which credit card debt was down year-on-year. That, however, is mainly a reflection of how deep the decline in credit card debt was over the first half of 2020, and with credit card debt outstanding having risen sequentially in both Q2 and Q3 and almost surely set to do so again in Q4, that run of over-the-year declines won't be extended.

While mortgage debt remains the main driver of growth in total household debt, mortgage originations slowed in Q3 2021, and the $230 billion in total mortgage debt outstanding in Q3 was smaller than the $282 billion increase in Q2. Still, total mortgage originations topped $1 trillion in Q3, the fifth consecutive quarter in which this was the case. Home sales were a mixed bag in Q3, with the number of new home sales falling from Q2's level while the number of existing homes sold increased. At the same time, data from the Mortgage Bankers Association (MBA) show the average loan size on purchase mortgage loan applications fell to $398,020 in Q3 from $404,820 in Q2, which in part reflects FHA and VA loans accounting for a higher share, both in terms of numbers of loans and dollar volumes, of mortgage originations in Q3 than was the case in Q2. Going forward, home sales are likely to remain uneven over the remainder of 2021 and into early-2022. Inventories of existing homes for sale remain a meaningful drag on existing home sales, and inventories fell in each of the final two months of Q3. At the same time the pace of existing home price appreciation is slowing sequentially, i.e., the

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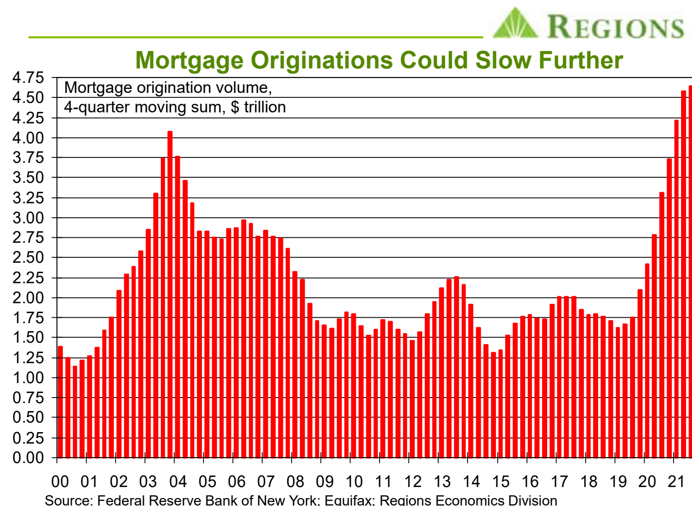
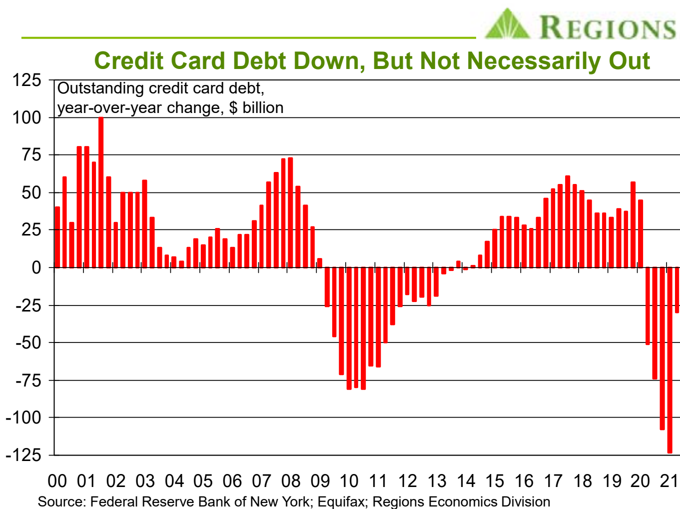
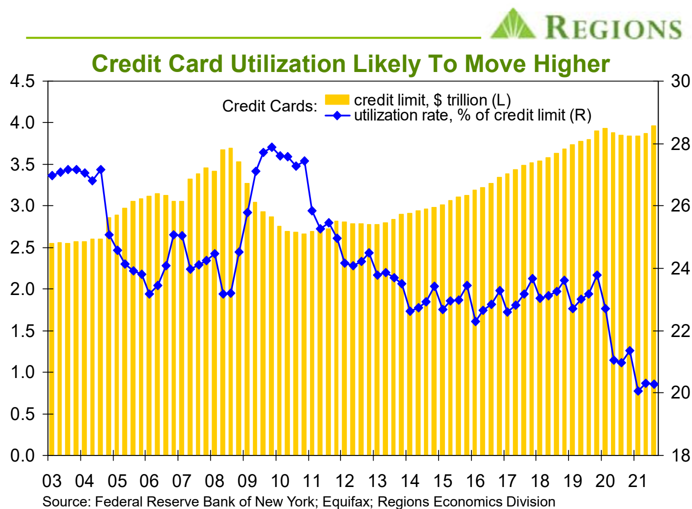
month-to-month and quarter-to-quarter increases have clearly slowed, although over-the-year growth remains close to 20 percent. As for new home sales, while builders have begun to lift the self-imposed caps on sales put into place earlier this year, new home sales are still being limited by materials and labor shortages, and delivery times on new homes are significantly stretched. Moreover, sales are likely to be soft in early-2022, reflecting some degree of payback for how aggressively sales rose earlier in 2021. In short, mortgage origination volumes from home purchases could slip in Q4 2021 and Q1 2022 before turning higher. Mortgage refinancing remains sensitive to changes in mortgage interest rates but, as we are seeing in the latest weekly data, still responds to dips in mortgage interest rates. So, though perhaps not to the same extent seen over the past several quarters, mortgage debt will remain the biggest driver of growth in total household debt.



Credit card debt outstanding rose by $17 billion in Q3, matching the increase seen in Q2. Still, at $804 billion in Q3, credit card debt is virtually unchanged from where it was in Q3 2020 ($807 billion) and remains far below where it was in Q4 2019 ($927 billion). Keep in mind, however, that credit card utilization was significantly disrupted during the pandemic, and we expect utilization patterns to normalize over the quarters ahead. Credit card utilization/balances have typically followed very pronounced seasonal patterns, with balances rising modestly over the second and third quarters of any given year, followed by a significant increase in the fourth quarter and subsequent significant decline in Q1 as holiday spending splurges are paid off (at least partially). Those patterns had been in place for many years before being disrupted by the pandemic.



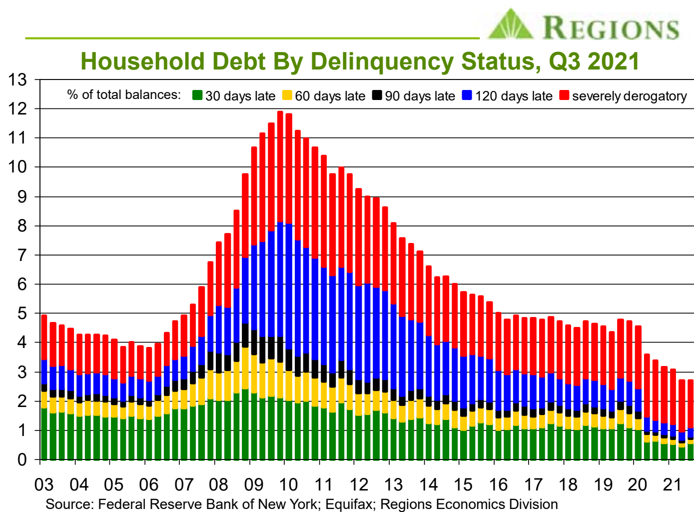


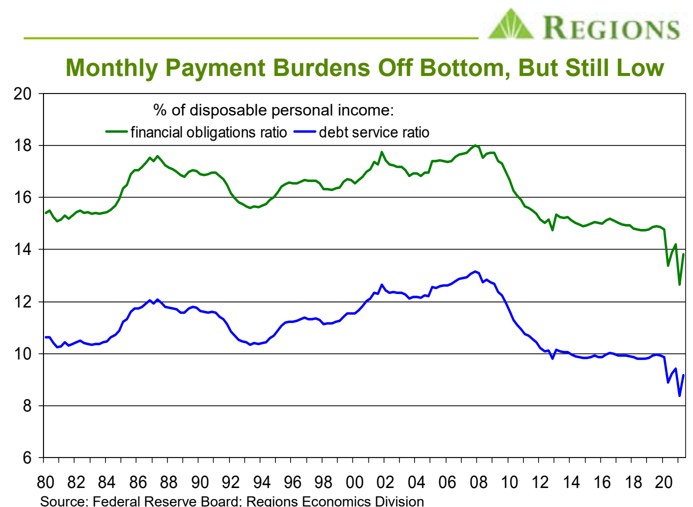
With much of the economy coming to an abrupt halt at the onset of the pandemic and over twenty million jobs being lost over March and April 2020, consumer spending fell sharply, helping to account for the decline in outstanding credit card debt in Q1 2020, which was much larger than the typical Q1 decline. Consumer spending fell even more severely in Q2 2020, but this reflected the extent to which spending fell in the month of April before rebounding in May and June. Yet, even though consumer spending recovered over the final two months of Q2 2020 and continued to rise through Q3, credit card debt outstanding continued to decline through Q3 2020. This was largely a function of the first round of Economic Impact Payments (EIP) in April 2020, which survey data such as the Census Bureau's *Household Pulse Survey* showed was used to pay down debt and build up saving to a much greater degree than to facilitate spending. Though there was an increase in outstanding credit card debt in Q4 2020, it was much smaller than the typical Q4 increase. With two more rounds of EIP in Q1 2021, outstanding credit card debt fell substantially in Q1, with the decline significantly larger than the typical Q1 decline.

That outstanding credit card debt rose in both Q2 and Q3 2021 seemingly marks a return to more normal seasonal patterns of credit card usage. We think it interesting to also highlight patterns on the other side of the ledger, i.e., patterns in lenders' behavior. At the onset of the pandemic, credit card issuance fell sharply, particularly for subprime borrowers, and lenders also pulled in credit limits on many accounts. This can be seen in the second chart above by the dip in aggregate credit card limits. Recall that in the early stages of the pandemic lenders were bracing for significant credit losses, in part because few could envision the magnitude of the fiscal policy

response, particularly in the form of financial transfers to the household sector. As such, widespread credit losses did not materialize, and over the past few quarters the number of new credit card accounts has risen, as have available credit card lines, with larger increases in Q3 2021 than in prior quarters. As such, even though outstanding credit card debt rose in Q3, credit card utilization, or, outstanding balances as a percentage of available lines, fell slightly.

We look for increases in both available credit card lines and outstanding credit card debt in the quarters ahead, but expect the latter to outpace the former, such that the credit card utilization rate begins rising. With pandemic-related transfer payments having largely run their course and saving buffers in the household sector beginning to thin out, it is likely that consumers will turn back to credit cards to help facilitate spending. This could be especially the case with lower-income households, for whom sharply higher prices for food, energy, and shelter mean there is less room for discretionary spending. With these households likely to have smaller, or no, saving buffers, resorting to credit cards, or using cards more intensively, may be the only option other than dramatically cutting back on discretionary spending, particularly during the height of the 2021 holiday shopping season. Even if we are correct in expecting credit card utilization to begin rising, it will take some time before the credit card utilization rate returns back to its pre-pandemic range.





As noted above, contrary to fears in the early phases of the pandemic, there was no surge in delinquencies/defaults. To be sure, forbearance programs played a key role in avoiding such an outcome. But, it is also noteworthy that early-stage delinquencies (or, 30-day and 60-day delinquency rates) actually fell significantly beginning in Q2 2020, which in part reflects the impact of generous fiscal transfers to the household sector. Still, while the overall delinquency rate on household debt held steady at 2.70 percent in Q3, the 30-day delinquency rate rose to 0.56 percent from 0.46 percent in Q2. To be sure, this is still roughly one-half of where the 30-day rate was prior to the pandemic, but it is still worth noting. That the overall delinquency rate was unchanged reflects longer-duration delinquency rates falling slightly in Q3. More broadly, just as patterns in debt usage continue to normalize in the quarters ahead, so too will delinquency rates. In other words, with financial buffers thinning out and prices for necessities rising at rapid rates, it is reasonable to think that delinquency rates would push higher, with the bigger question being to what extent.

As the second chart above shows, monthly payment burdens, expressed as a share of disposable personal income, are off of the all-time low seen in Q1 2021 – a low which in part reflects the extent to which the second and third rounds of EIP boosted disposable personal income in Q1. But, even before the pandemic, a prolonged period of deleveraging in the household sector combined with "lower for longer" interest rates had resulted in a meaningful decline in monthly payment burdens relative to historical norms. Payment burdens rising back to those pre-pandemic ranges would not necessarily be cause for alarm. It also helps to recall that, while pandemic-related transfer have largely run their course and household financial buffers will thin out in the quarters ahead, we are seeing robust growth in labor earnings, far and away the largest single component of personal income. Strong growth in labor earnings acting as a support for growth in ex-transfer personal income should check any increases in monthly payment burdens.

As we've noted in prior editions of this write-up, the pandemic and the efforts to stem its spread and the aggressive policy response brought about profound changes in patterns of economic activity and in household finances. Though some of these changes may prove to be lasting, it is also clear that patterns in economic and financial activity are beginning to normalize. The starting point for this normalization process was household financial positions that, in the aggregate, were stronger than was the case prior to the pandemic. So, while the sequential changes in outstanding household debt, delinquency rates, and monthly payment burdens clearly merit attention, the relevant benchmark will be how they stack up against pre-pandemic values.

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