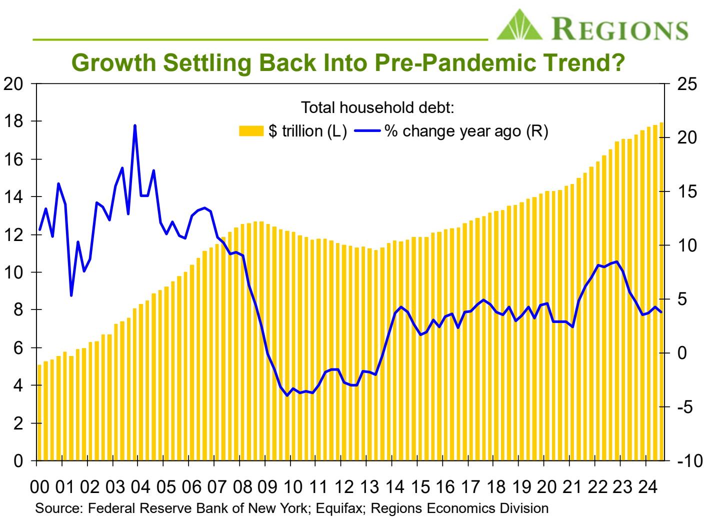
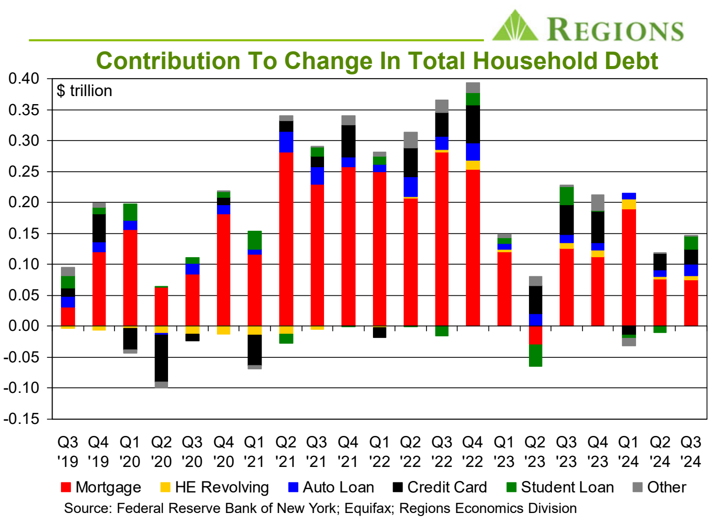
Q3 2024 Household Debt and Credit: Growth In Debt Settling In; Delinquecies Push Higher

- Total household debt rose to $17.943 trillion in Q3 2024, an increase of $147 billion from Q2
- Mortgage balances rose by $75 billion in Q3 while outstanding credit card balances rose by $24 billion
- As of Q3, 3.54 percent of outstanding household debt was in some stage of delinquency, up from 3.20 percent in 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, which shows total household debt rose to $17.943 trillion in Q3 2024, an increase of $147 billion from Q2. Total mortgage debt outstanding rose by $75 billion in Q3 while outstanding credit card debt rose by $24 billion and auto loan debt rose by $18 billion. At the same time, balances on home equity lines of credit (HELOC) rose by $7 billion, the eighth consecutive quarterly increase after what had been a lengthy run of contracting balances in this segment. On an over-the-year basis, total household debt was up by 3.77 percent in Q3, and over the past several quarters growth has settled back into the range that prevailed in the years prior to the onset of the pandemic. HELOC balances posted a double-digit year-on-year advance for the third straight quarter, and while the over-the-year increase in outstanding credit card balances was the smallest such increase since Q4 2021, that is more a reflection of how rapidly credit card debt has grown over this span as the year-on-year increase in Q3 was 8.1 percent. The overall delinquency rate on household debt rose to 3.54 percent in Q3 from 3.20 percent in Q2. While that is still well below the 4.73 percent delinquency rate posted in Q4 2019, it is worth noting that the 30-day delinquency rate rose to 1.11 percent in Q3, matching the 30-day rate posted in Q4 2019 and up from 0.95 percent in Q2. The upward push in the 30-day delinquency rate over the past several quarters suggests later-stage delinquency rates will also move higher over coming quarters. That leaves the question of whether the overall delinquency rate on household debt will push past the pre-pandemic threshold or will push higher but level off shy of that mark. Barring a pronounced deterioration in labor market conditions over coming quarters, the latter would seem more plausible than the former, but the actual answer will only come with time.





That the overall delinquency rate on household debt has remained easily below pre-pandemic norms has masked pockets of more significant financial stress across age and income cohorts and across debt categories. As we've discussed in prior editions of these write-ups, many younger and lower-income borrowers, with some degree of overlap between these groups, have experienced greater difficulty in meeting repayment obligations, particularly those who have exhausted whatever pandemic-related financial buffers they once had at their disposal. Delinquencies across borrowers in these groups have been a key driver of rising credit card delinquencies over recent quarters. While this has been a topic of considerable discussion, what also stands out to us the transition of mortgage loan balances into early-stage delinquency. One reason this is noteworthy is that, as we've recounted in these write-ups, mortgage loan originations have been so heavily concentrated amongst borrowers with credit scores of 760 or higher over the past several years. To that point, since Q1 2019, borrowers in this credit score bucket have accounted for two-thirds of the total dollar amount of mortgage originations. The question here, however, is the same question that looms over the aggregate delinquency rate, i.e., whether we are seeing mortgage

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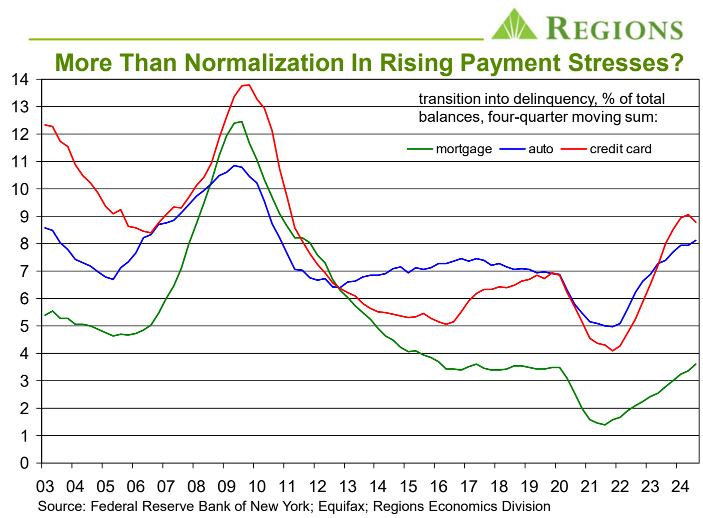
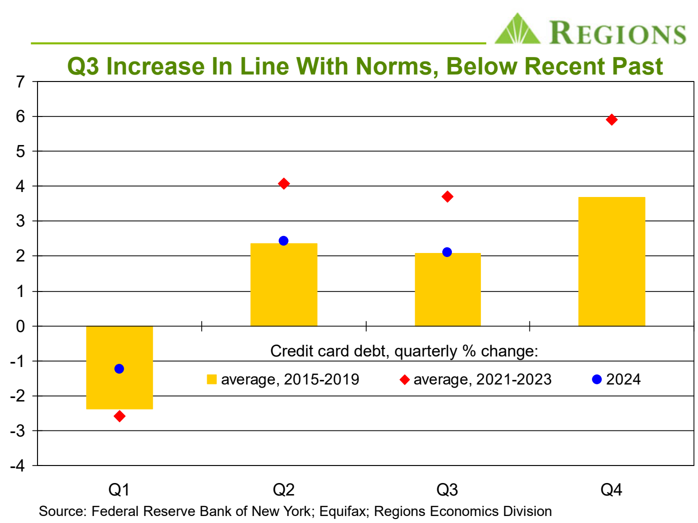
delinquencies simply revert back to pre-pandemic norms or whether something less benign is in the works. It is worth keeping in mind that, prior to falling further during the early stages of the pandemic, early-stage delinquencies as reported by the Mortgage Bankers Association were already at the lowest rates in the life of the data, in large measure reflecting the more stringent underwriting standards in place in the years since the Great Financial Crisis. In that sense, it is reasonable to wonder whether even lower mortgage delinquency rates could, or should, have been expected to be sustained.

It is also worth noting that, as seen in the chart to the side, that the rate at which mortgage loan balances are transitioning into delinquency has returned to the pre-pandemic rate, which at the time was notably low. While the transition rate for mortgage debt began rising well ahead of mortgage interest rates turning sharply higher in 2022, it largely coincided with the sharp acceleration in inflation that began in the spring of 2021, though a causal relationship that early on would seem more difficult to establish. Either way, this is clearly something that bears watching in the quarters ahead. As is also seen in the chart, there was modest improvement in the rate at which credit card balances transitioned into delinquency in Q3, though it is too soon to declare, at least with any degree of certainty, that we've seen the cyclical peak. At the same time, however, the rate at which auto loan balances transitioned into delinquency nudged higher in Q3. As a reminder, the New York Fed reports transition rates on an annualized (i.e., four-quarter moving average) basis, as a means of getting around what is a high degree of seasonality in the data.

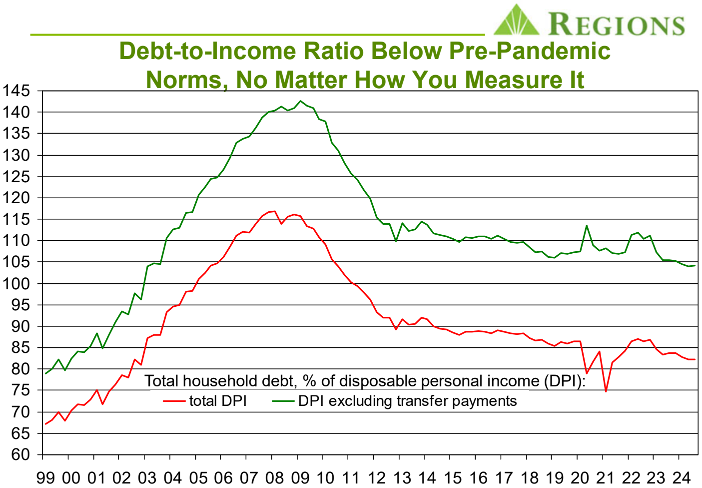


Growth in outstanding credit card debt has slowed, sequentially and on an over-the-year basis though, as noted earlier, that is a bit of a dubious distinction given how rapidly credit card balances had been growing over the prior several quarters. What is worth noting, however, is that the quarterly increases in credit card balances in the middle two quarters of 2024 were more or less in line with pre-pandemic norms. As we've frequently noted in these write-ups, there are clear, and strong, seasonal patterns in outstanding credit card balances. In any given year, growth is far and away stronger in the fourth quarter than in any other quarter, while the first quarter in any given year tends to see balances decline, these tendencies are merely a reflection of holiday season shopping (Q4) and the subsequent paying down, at least in part, (Q1) of those balances. The middle two quarters of any given year tend to see moderate growth in outstanding balances. What has stood out over the past few years, however, is the extent to which the quarterly increases seen over the second, third, and fourth quarters exceeded pre—pandemic norms for those quarters. This can be seen by the red diamonds in the nearby chart. As the chart also shows, the sequential increases more or less normalized during the middle two quarters of this year. Whether that reflects a natural slowing after a period of such rapid growth, the effects of moderating inflation, or growth in consumer spending falling back in line with income growth – as we've for some time been noting was occurring – cannot be determined with any degree of certainty, but the most likely explanation is that it is some combination of all three factors. Again, it is simply too soon to say, but the combination of moderating growth in outstanding balances coupled with improvement, albeit modest, in the rate at which balances are transitioning into delinquency at least raises the possibility that the worst is behind us in terms of early-stage credit card delinquencies. As a side note, we expect the sequential increase in Q4 2024 to be well smaller than the average Q4 increase seen over 2021-2023, in keeping with our forecast of the smallest annual increase in holiday season sales since 2018.



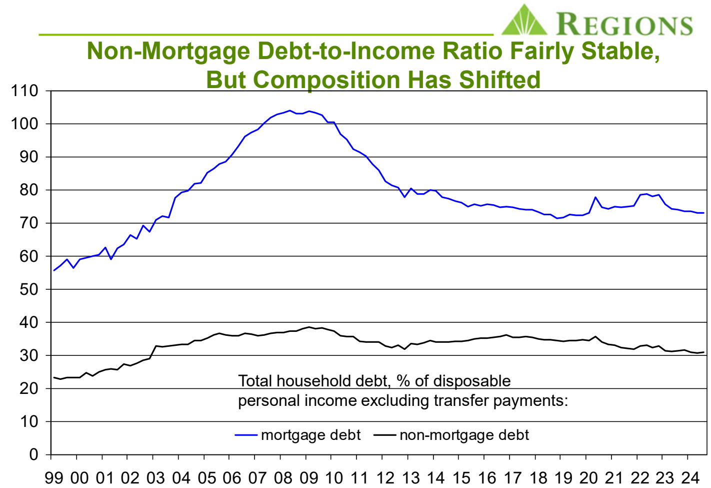
Though growth in credit card debt and transitions into delinquency on credit card debt slowed in Q3, the headlines and accompanying media accounts continue to be dominated by the level of credit card debt. Though we can't claim to know just what $1 trillion will buy you these days, one thing we do know is that $1 trillion of credit card debt will buy a seemingly endless stream of dramatic headlines, and that is true more broadly each quarter with whatever the newest, latest "record high" level of total household debt happens to be. Sure, they're all big numbers, but they mean little without being put in any sort of context. For instance, while we've seen a steady run of headlines and accounts of record high levels of household debt, we've seen very few mentions of the fact that growth in after-tax personal income has outpaced growth in total household debt over the past several quarters, as had been the case for years prior to the onset of the pandemic. Put differently, the ratio of household debt to disposable (after-tax) personal income has fallen to a more than two-decade low, leaving aside the sharp dip during the early phases of the pandemic. Debt-to-income ratios are generally seen as an indicator of the sustainability of debt growth and the ability to service that debt. Though obviously not perfect measures, as is true of any aggregate measures, debt-to-income ratios are nonetheless an important tool to help put growth in debt into proper context.

Debt-to-Income Ratio Below Pre-Pandemic Norms, No Matter How You Measure It



Source: Bureau of Economic Analysis; Federal Reserve Bank of New York; Equifax; Regions Economics Division

Non-Mortgage Debt-to-Income Ratio Fairly Stable, But Composition Has Shifted



Source: Bureau of Economic Analysis; Federal Reserve Bank of New York; Equifax; Regions Economics Division

The first chart above shows the path of the household debt-to-income ratio using two different measures of income. The red line shows the debt-to-income ratio as most commonly measured, i.e., total household debt as a percentage of disposable personal income. The green line shows the debt-to-income ratio using disposable personal income excluding transfer payments as the measure of income, which we see as the more relevant measure of income if one is using the ratio as a gauge of the ability to service debt. Our reasoning simply reflects the fact that, while included in the measure of personal income, many transfer payments do not actually reflect cash transfers to the household sector but are instead payments made to service providers on behalf of households. The two most prominent examples of these non-cash transfers are Medicare and Medicaid, which combine to account for almost one-half of total transfer payments in the personal income accounts. Moreover, we'd argue that even those transfers, such as Social Security and Unemployment Insurance, that do reflect cash transfers are used mostly, if not exclusively, to cover spending on necessities and, as such, should not be counted in the pool of income available for debt service (i.e., monthly principal and interest payments on outstanding debt). Simply put, though not a perfect measure, we see after-tax income excluding transfer payments as a more accurate gauge of the pool of income households have at their disposal to meet debt service obligations. Obviously, our measure yields a higher debt-to-income ratio as it is based on a narrower measure of income, but as seen in the chart the patterns in the two measures closely mimic each other. The one notable exception is the 2020-2021 period in which sizable transfers to the household sector led to significant, but transitory, increases in disposable income and, in turn, pushed the debt-to-income ratio lower, an effect absent in our preferred measure.

Either way, the household debt-to-income ratio is, as of Q3 2024, largely in line with the trend that had been in place in the years prior to the pandemic and far below the record high seen in the mid-2000s. As the second chart above indicates, that record high largely reflected households gorging on mortgage debt; recall that the prominence of cash-out refinancing during that time allowed households to replace other forms of debt with lower-rate mortgage debt, hence the relative stability of the ratio of non-mortgage debt to after-tax income during this time. One value in segregating household debt into mortgage and non-mortgage debt, as done in the second chart above, is that it enables us to better put the recent growth of credit card debt into context. Growth in credit card debt has easily outpaced growth in other forms of household debt over the past several quarters, but the net result is that the ratio of non-mortgage debt to disposable personal income excluding transfer payments has been fairly stable over this time.

Again, this is an aggregate measure, and for those lower-income households who have had to become more reliant on credit card debt to facilitate spending, the ratio would be well above the aggregate measure. This illustrates a shortcoming in the data but at the same time helps illustrate a general point worth keeping in mind even if it goes largely ignored in accounts focused on "record high" levels of credit card debt. The shortcoming in the data is that we simply do not have cuts of the various data series along income lines, so while it would be informative and useful to be able to estimate debt-to-income ratios across various household income cohorts, we simply do

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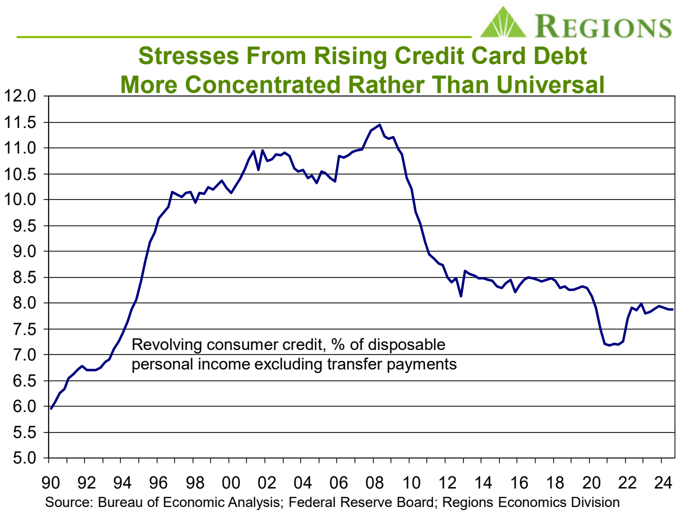
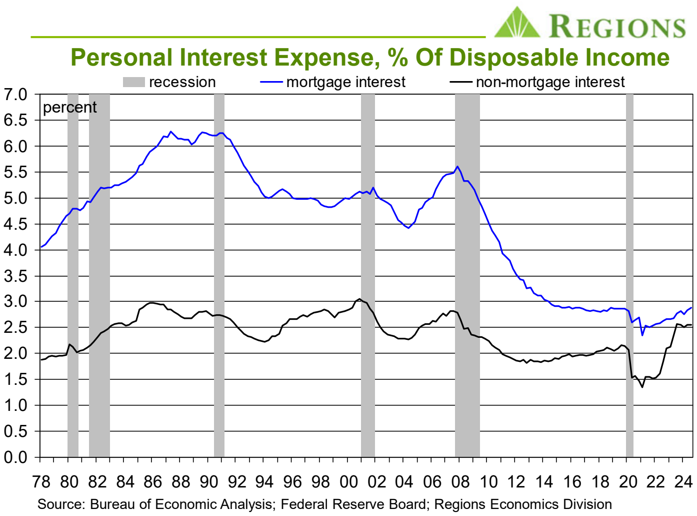
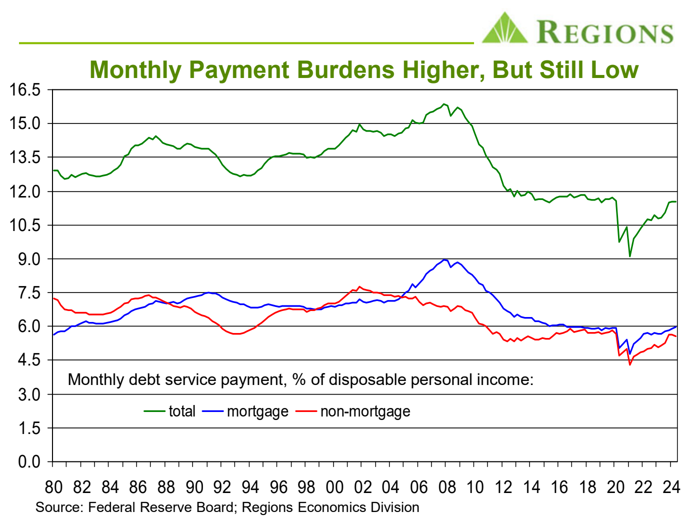
not have the data that would allow us to do so. That said, many will no doubt be surprised by the relative stability in the ratio of non-mortgage debt to ex-transfers disposable income over the past several quarters. This gets us to the broader but often overlooked point, which is that stresses from high levels of credit card debt are much more localized than globalized.





The first chart above shows the level of outstanding revolving consumer credit, from the Federal Reserve's measure of consumer credit, as a percentage of disposable personal income excluding transfer payments, or, what would be a segment of the broader measure of non-mortgage debt discussed above. The dip seen in 2020-2021 reflects the extent to which many households used portions of the pandemic-related transfers to pare down debt, primarily credit card debt. The broader point, however, is barring this distortion, the ratio as of Q3 2024 was 7.88 percent, largely unchanged from the prior five quarters and the lowest since mid-1994. Again, not every household will have this low of a ratio but, were credit card debt a more pressing burden across a wider swath of households, the aggregate ratio would be much higher. The second chart above does show the rising toll taken by the combination of higher interest rates and rapid growth in credit card debt, as interest expense on non-mortgage debt has risen sharply over recent years. Still, with growth in credit card debt slowing and interest rates on credit card debt heading lower, even if at a slow pace, growth in non-mortgage interest expense should slow over coming quarters.



The increase in interest expense on non-mortgage debt is reflected in the rising debt service burden on non-mortgage debt shown in the chart to the side (note the Federal Reserve's measures of debt service burdens are based on disposable personal income inclusive of transfer payments). The effects of higher mortgage interest rates are also visible in the chart. Still, though having risen from the lows driven by pandemic-related transfer payments, overall household debt service burdens are still modestly below where they were prior to the pandemic – when, by the way, both interest rates and debt balances were lower. This is again an illustration of the extent to which personal income has grown, fueled largely by more rapid growth in labor earnings. And, yes, the obvious caveat about aggregate measures holds here as well. The broader point here, however, is that debt service burdens remain highly manageable for most households. To be sure, a deterioration in labor market conditions that is more pronounced than our baseline outlook at present anticipates looms as a downside risk, as this would put after-tax personal income on a much lower trajectory than we at present anticipate will be the case. This would, in turn, lead to a more pronounced and more broadly based increase in delinquencies on household debt than would be implied by our baseline outlook.

Our focus in this edition of these regular write-ups has been on delinquencies and debt service burdens. Though by no means intending to downplay concerns along these lines, we do think it useful to add context, often missing from discussions of these issues. In keeping with our expectations for the labor market, consumer spending, and the broader economy, we expect growth in household debt to slow further in the quarters ahead, with at least some relief on the interest rate front helping to mitigate debt service burdens.