MARCH 2018

CONSUMER CREDIT TRENDS

FOR DALLAS COUNTY

Federal Reserve Bank of Dallas

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"Consumer Credit Trends for Dallas County" is a research report from the Community Development Department at the Federal Reserve Bank of Dallas. It is part of a series that focuses on the credit activity of residents in selected counties in Texas and includes information on loan volumes in major credit categories and loan repayment levels. The views expressed in the report are the authors' and do not necessarily reflect official positions of the Federal Reserve System. For more information, contact Emily Ryder Perlmeter at Emily.Perlmeter@dal.frb.org.

CONSUMER CREDIT TRENDS

FOR DALLAS COUNTY

Except for Student Loans, Delinquencies Largely Down Since Recession

Access to affordable credit is a key component of an individual's ability to cultivate a strong financial position and participate fully in the economy. Loans are necessary financial tools that most Americans use to purchase homes, cars and other goods or pay for college. Restricting access to debt can limit access to these asset-building opportunities.

At the same time, easy loan access has its downsides. One concern is that large balances with high interest rates can keep borrowers trapped in a debt cycle or otherwise prevent them from meeting their payment obligations. In worst-case scenarios, these consequences can multiply when adequate consumer protections are not in place, leading to large-scale and negative impacts on the economy. [1]

Useful indicators of the financial health of an economy include the number of credit consumers, total loan volume and the percentage of loans that are delinquent or not repaid. While such credit trend data are available on the state and national level, little analysis has been done on a county and subcounty level. With this in mind, the Federal Reserve Bank of Dallas and the Center for Public Policy Priorities partnered to examine and report on debt trends and the credit health of Dallas County, using data from credit bureau Equifax.[2] This report is the first in a series. Analysis of other Texas counties will be forthcoming in 2018.

In Dallas County, 85 percent of potential borrowers have a credit report, with credit card debt the most utilized among the major loan types.[3] Predictably, loan volumes have climbed in the postrecession period, and balances have surpassed their prerecession heights for all the major loan types except credit cards. Average balances are unsurprisingly highest for mortgage loans, though student loan balances are swiftly rising. Regulations have tightened, and serious delinquencies have largely recovered in the postrecession period. But student loans tell a different story.

CREDIT CONSUMERS AND CREDIT SCORES

This report analyzes who is borrowing, how much they're borrowing and their level of delinquency by credit score across major loan types.

Credit scores are calculated based on information in a consumer's credit report—including the number of loans and whether they are paid on time. The scores are calculated by the three major credit bureaus—Equifax, Experian and TransUnion—and are intended to help lenders predict future delinquency rates. This report uses Equifax scores, which range from 300 to 850: The lower the score, the greater the risk of serious delinquency.

In Dallas County, the geographic dispersion of credit scores is related to that of income: ZIP codes with lower median incomes tend to also have lower median credit scores *(Chart 1)*. Much of this population is located in the southern sector of Dallas. These ZIP codes also have higher concentrations of people of color. In Dallas and elsewhere, median incomes for black and Latino residents lag behind those of white residents.

The geographic connection is not surprising given the nation's history of racial discrimination in the credit market. Through the 1970s, black Americans hoping to access credit, mortgages and housing faced significant barriers, many of which were codified in government policies. The Federal Housing Administration refused to insure loans in communities that had what they considered "undesirable" racial makeup.[4] Without such insurance, banks would not grant mortgages in these neighborhoods, which were lower income and less white. This practice is known as redlining. Generations of people of color lacked the opportunity to build assets through homeownership, and others were steered toward certain neighborhoods and higher-cost loans.

While the Equal Credit Opportunity Act of 1974, the Community Reinvestment Act of 1977 and other legislation were eventually passed to protect all consumers, the effects of the discrimination endure today.

Credit score categories in Dallas County are predictably correlated with the average serious delinquency rate, defined as the percentage of the loan balance that is at least 90 days past due or written off as a loss or foreclosure *(Table 1)*. Prime borrowers (scores of 680 and above) have a serious delinquency rate close to zero. Deep subprime borrowers (scores below 550) have serious delinquency rates over 30 percent. A little over half of Dallasites have prime credit, and 30 percent—or 393,000 borrowers—have subprime or deep subprime scores of below 620.

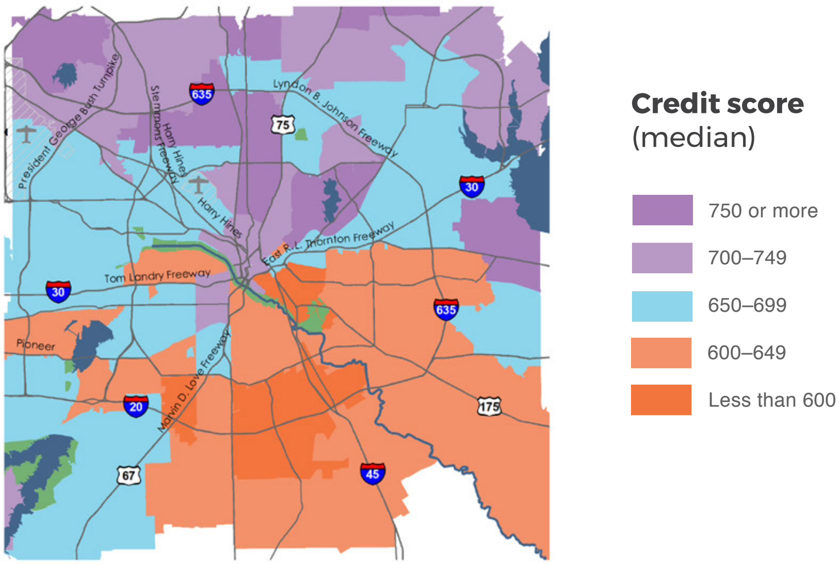
TABLE 1. Credit Score Categories Intended to Help Predict Delinquency Rates

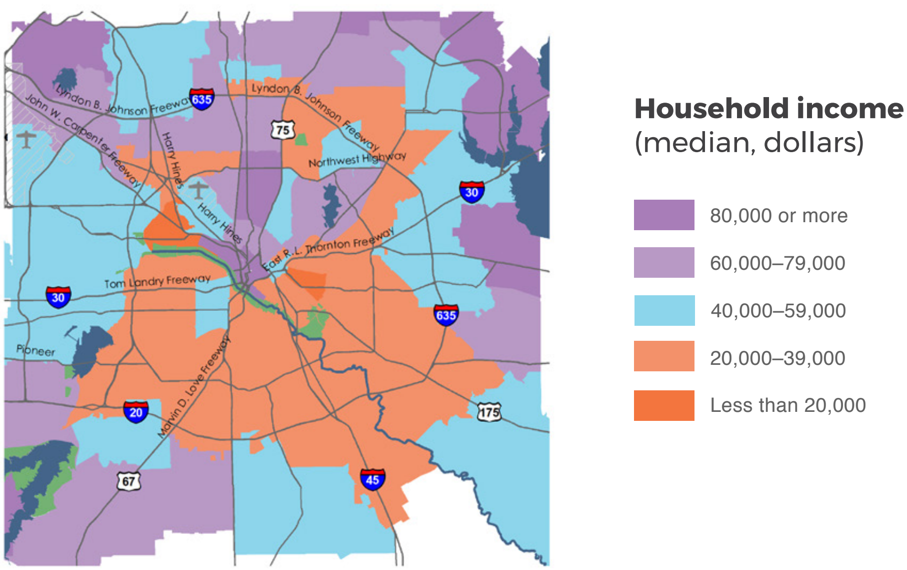
Category	Credit score range	Number of borrowers	Average serious delinquency rate, percent
Prime	680 and above	705,780	0.06
Near prime	620 - 679	215,660	1.51
Subprime	550 - 619	194,460	9.34
Deep subprime	Below 550	198,840	30.25

SOURCES: Federal Reserve Bank of New York Consumer Credit Panel/Equifax; authors' calculations.

CHART 1. Credit Scores Related to Income, Share a Similar Geographic Pattern

The map colors depict areas of greater Dallas County according to credit score and income. The light and dark orange regions reveal that lower credit scores are largely in the southern reaches of the city where lower median household incomes are found.





NOTES: Data are as of March 2017. The Equifax Risk Score was developed by credit scoring agency Equifax and predicts the likelihood of a consumer becoming seriously delinquent (90-plus days past due). The score ranges from 300 to 850 (the lower the score, the greater the delinquency risk).
SOURCES: Federal Reserve Bank of New York Consumer Credit Panel/Equifax; authors' calculations.

TYPES OF LOANS AND LOAN VOLUMES

This report considers four major loan types for individual borrowers—mortgage, credit card, auto and student.[5] These are the most commonly held types of debt and, together, they represent 95 percent of the loan volume in Dallas County *(Table 2)*.

TABLE 2. Loan Volumes Vary Widely by Loan Type and Risk Score

Category	Percent of all borrowers	Mortgage loan volume (percent), \$48.2 billion	Student loan volume (percent), \$10.9 billion	Auto loan volume (percent), \$10.9 billion	Credit card volume (percent), \$5.7 billion
Prime	53.7	81.6	34.5	47.9	64.4
Near prime	16.4	9.2	17.9	18.6	19.0
Subprime	14.8	5.2	19.8	17.1	10.4
Deep subprime	15.1	4.1	28.1	16.7	7.7

SOURCES: Federal Reserve Bank of New York Consumer Credit Panel/Equifax; authors' calculations.

Lower credit scores have other implications. They signal higher risk to lenders, who often restrict credit for these groups. As such, the percent of loan volume carried by deep subprime borrowers is far smaller than the loan volume carried by their prime counterparts.

This is particularly evident in the mortgage market, where deep subprime borrowers carry just 4 percent of debt. This was not always the case; an expansion of credit took place in the early 2000s. In 2009, borrowers with credit scores under 550 represented 14 percent of all mortgage borrowers and held 12 percent of the overall loan volume.[6] After the Great Recession, lending standards tightened. This was one factor in restricting access for many borrowers, especially those with poorer credit.

The Effect of Federal Policy on Credit Card Balances

The average Dallas resident with a credit card carried over $7,000 from 2001 through 2009. Average balances declined after the recession, which coincided with the passage of the Credit Card Accountability Responsibility and Disclosure (CARD) Act of 2009.

The CARD act placed restrictions on the fees credit card companies can charge, limited hikes in interest rates and required all companies to assess a borrower's ability to pay before granting credit. A subsequent reduction in late fees and overlimit fees was directly attributable to the act.

Studies by the Consumer Financial Protection Bureau have also shown correlations between the act and decreased overall consumer credit card costs as well as restricted credit access for young and subprime borrowers. Since 2009, the average credit card balance in Dallas County has declined by $1,988.

–Emily Ryder Perlmeter

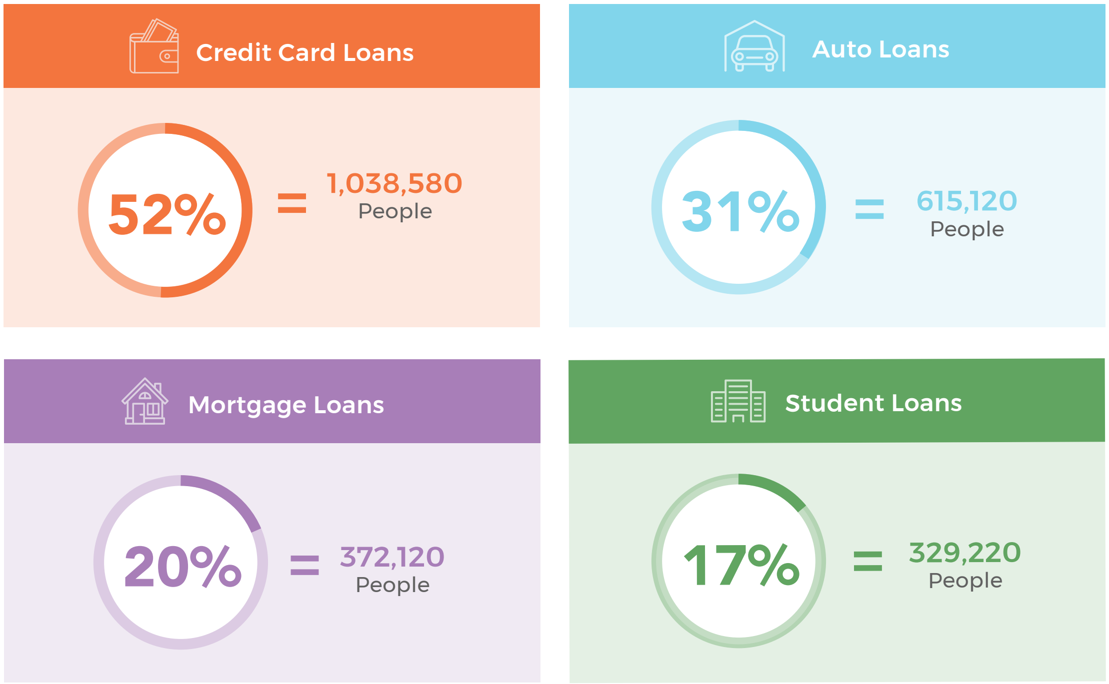
Economic policies affected the credit card industry as well, with the 2009 passage of the Credit Card Accountability Responsibility and Disclosure (CARD) Act (*see the sidebar, "The Effect of Federal Policy on Credit Card Balances"*).

Typically, implications for lower credit scores include smaller approved loan amounts and higher interest rates.[7] The notable exception to this is student loans. The student loan market differs because of the involvement of the federal government, which originates and guarantees debt for students. Loans are not offered based on credit score or credit history; rather, Congress sets interest rates and borrowing limits. Without a credit check, students from all credit backgrounds are offered the same borrowing limit and price of debt. Private student loans are still available, but they are used far less often than federal student loans and make up about 10 percent of the total student loan volume.

Because access to credit is so vital to participation in the economy, the number of credit consumers out of the total possible number of borrowers can be an important measure of a local economy's credit inclusion. A lower consumer credit percentage may signal lower inclusion. With 85 percent of residents 18 and older having a credit score, Dallas County falls short of the statewide average of 86 percent and the national average of 90 percent. Credit scores are available only for consumers who have at least one line of credit. Once a credit line is active, it can take up to six months for a credit bureau to calculate a score.

Looking at the four major types of loans, nearly 52 percent of residents have at least one credit card account *(Chart 2)*. Just under a third of people 18 years or older have an auto loan, whether from a financial institution or a car dealership/financing company. Twenty percent of residents have a mortgage and 17 percent have student debt.

CHART 2. Credit Card Debt Most Widely Used in Dallas County

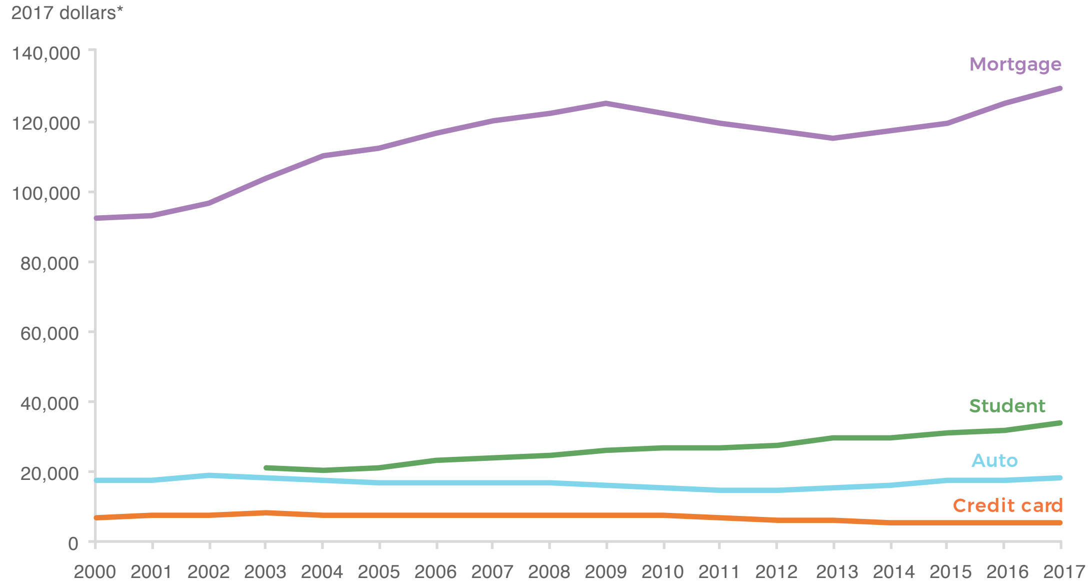


NOTE: Data are for 2016 and are based on the population 18 years and older
SOURCES: Census Bureau, 2016 population estimates; Federal Reserve Bank of New York Consumer Credit Panel/Equifax; authors' calculations.

Not surprisingly, the dollar amount of mortgage debt dwarfs that of all other types of loans. The average mortgage balance was $129,633 in 2017 for Dallas County residents who had a mortgage. Student loans had the second-highest average balance at $33,256 but the fewest borrowers. Those with auto debt carried $17,774 on average, and credit card accounts averaged $5,461.

Chart 3 shows the 18-year trend of average debt for each loan type, adjusted for inflation. While the real value of average auto debt has remained somewhat stagnant since 2000, average mortgage debt has soared 41 percent. At close to $130,000, mortgage balances in Dallas County have recovered from the postrecession decline and are higher than their previous peak in 2009.

CHART 3. Mortgage Volumes Highest; Student Loan Balances Fastest Growing



*Average loan amounts for Dallas County residents for major loan types, adjusted for inflation.
NOTE: 2017 data are based on estimates through March.
SOURCES: Federal Reserve Bank of New York Consumer Credit Panel/Equifax; Consumer Price Index; Bureau of Labor Statistics; authors' calculations.

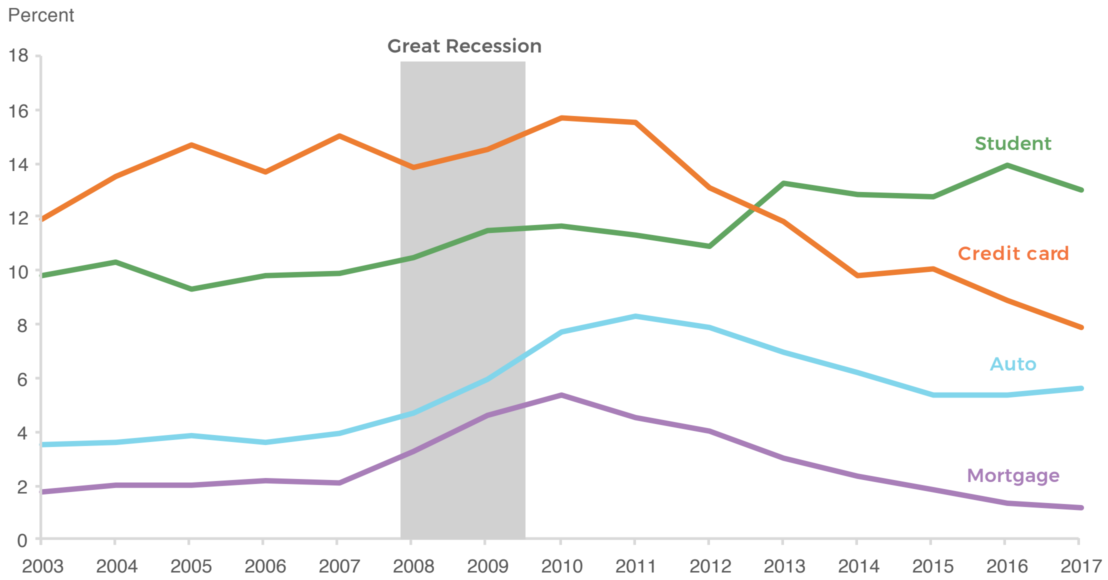
Student loans have seen the largest percent increase in the average balance. In 2003, the first year Equifax student loan data were available, balances were within a few thousand dollars of auto loans. Presently, the average student loan balance is nearly twice that of auto debt. In fact, average student debt is up 60 percent since 2003. This growth rate is not surprising when considering skyrocketing tuition costs, increases in graduate student loans and the lack of restrictions on this type of credit.[8]

SERIOUS DELINQUENCY RATES

Serious delinquencies are indications that loans are in danger of default. This status can have serious ramifications for a consumer's credit report and ability to borrow in the future. The timeline for defaulting on a loan varies by loan type and servicer but most often occurs after three to six months of missed payments. For some types of federal student loans, default kicks in at 270 days, or about nine months.

Most of the major loan types in Dallas County experienced similar patterns of rising serious delinquency through 2010, followed by a tapering off after the Great Recession *(Chart 4)*. Mortgages had the overall lowest rate of serious delinquency, even at the height of the crisis. This may be due to the greater loan amounts required for home mortgages and the greater borrowing restrictions that come with them.

CHART 4. Serious Delinquencies Trend Down for All but Student Loans



NOTES: The chart is based on the percent of overall loan volume that is seriously delinquent. Serious delinquencies include loans 90 days past due and 120 days past due and those charged off to bad debt, repossession or foreclosure. Delinquencies reflect all student loans, including those in deferment. 2017 data are based on estimates through March.
SOURCE: Federal Reserve Bank of New York Consumer Credit Panel/Equifax.

Historically, credit cards have had high rates of delinquency, peaking in 2010 at nearly 16 percent. The rates have since declined to less than 8 percent. Auto loans, too, saw high rates of serious delinquency in 2010 and 2011, followed by a steady decline. In 2017, auto loans did experience an uptick of 0.2 percent for loans 90-plus days past due, but the change so far has been very small.

Student loans in Dallas County buck the overall trend. Not only have student loan balances continuously increased, but delinquencies have as well. From 2009 to 2011, student loans saw only a minor increase in delinquency. In the years since, serious delinquencies have continued to climb. At 13 percent, the rates of seriously late student loan payments now outpace those of every other major loan type. This fact, coupled with the increasing average loan balance, suggests that student loans necessitate a deeper look.

STUDENT LOAN CONCERNS

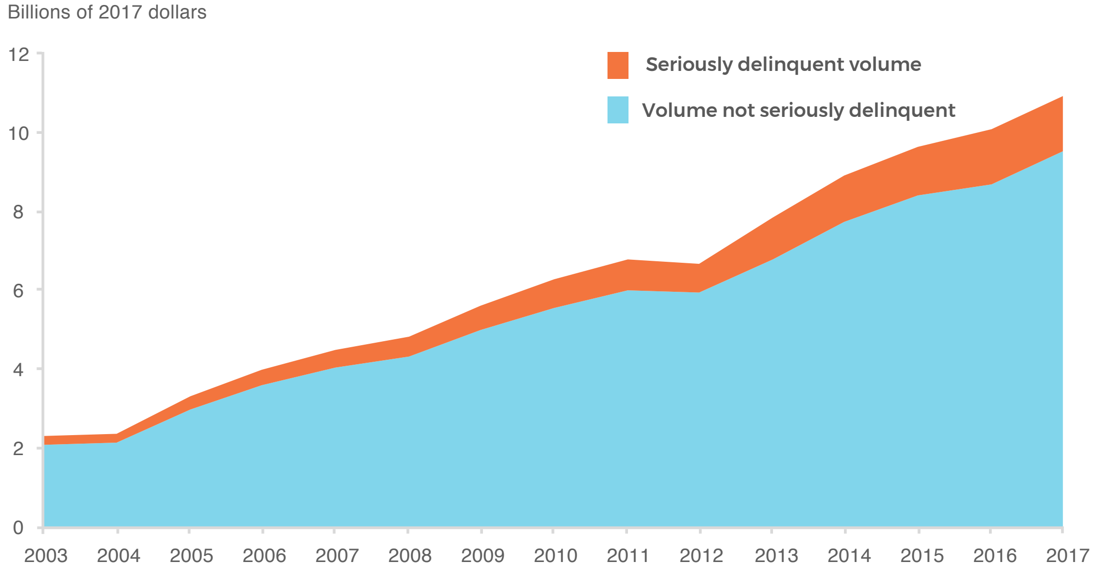
Aggregate Loan Volumes, Average Balances Up

Average student loan balances dwarf median (midpoint) balances, $33,256 to $16,667. This indicates that borrowers at the high end of the distribution have particularly large debt amounts. Average balances have climbed 60 percent since 2003, while median balances have risen 59 percent. This suggests that similar balance growth has occurred for borrowers at both the low and high ends of the spectrum.

The aggregate volume of student loans for all Dallas County borrowers has soared 380 percent since 2003, accounting for inflation. This increase is due both to growth in the number of borrowers and an increase in the average balance carried by each borrower.

While the total debt has risen, the amount of debt that is seriously delinquent has shot up. Chart 5 shows this widening gap between the volume that is not seriously delinquent and the volume that is. As of March 2017, Dallas County had over $1.4 billion in outstanding student debt that is at least 90 days past due; this volume represents a 535 percent increase since 2003, adjusting for inflation.

CHART 5. Student Loan Volume Climbs; Rate Highest for Seriously Delinquent Balances



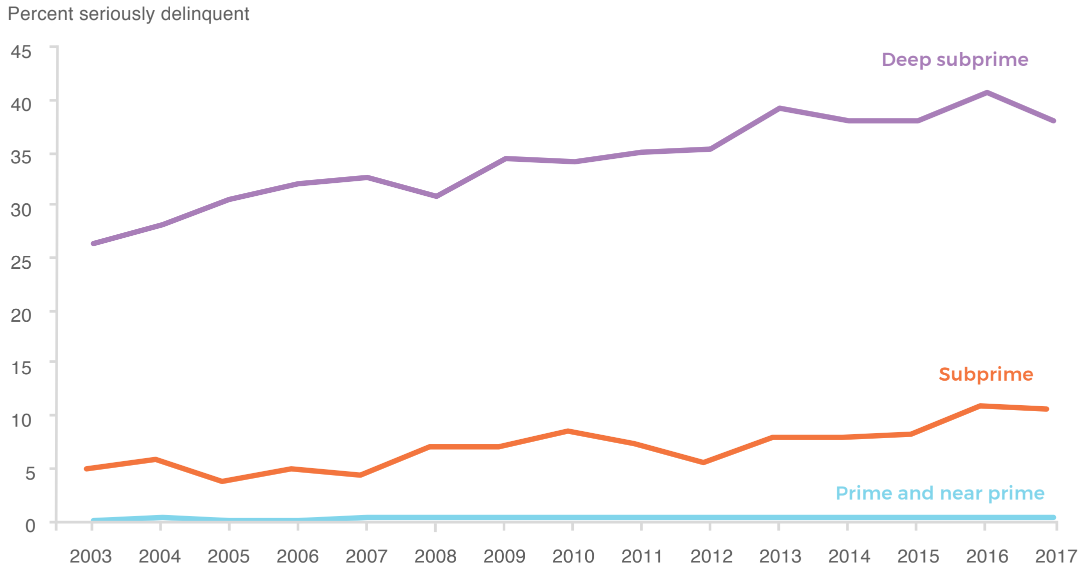
NOTES: Data are adjusted for inflation. Loan volume reflects all student loans, including those in deferment. 2017 data are based on estimates through March.
SOURCE: Federal Reserve Bank of New York Consumer Credit Panel/Equifax.

Serious Student Loan Delinquencies Soar for Low Credit Scores

Credit scores can play a significant role in delinquency outcomes. Serious delinquencies are less than half of a percent for prime or near-prime Dallas student loan borrowers, compared with 10.7 percent for subprime borrowers *(Chart 6)*. For those with deep subprime credit, serious delinquencies are a staggering 38 percent.

These findings are expected; credit scores are calculated based on the risk of being 90 days or more past due. However, as Chart 6 indicates, the gap between prime and subprime delinquencies has been steadily widening since 2003. Serious delinquencies have increased 5 percentage points for subprime borrowers and 12 percentage points for deep subprime borrowers, while prime or near-prime rates have remained mostly stagnant. Given that the portion of borrowers with credit scores below 620 has remained around 50 percent since 2003, this suggests that the rise in serious delinquency rates is not due to an increasing population of borrowers with subprime credit. Rather, these data indicate that student loan performance may be worsening overall for this group. Additionally, student loans are less likely to be discharged, so many consumers remain saddled with the severely derogatory portion of their debt over time.

CHART 6. Gap Widens Between Prime, Subprime Serious Student Loan Delinquencies



NOTES: Data include student loans in deferment. 2017 data are based on estimates through March.
SOURCE: Federal Reserve Bank of New York Consumer Credit Panel/Equifax.

As noted, access to federal student loans is not based on credit score. This has implications for loan performance and may at least partially explain the high rates of serious delinquencies. Another important issue impacting delinquencies is college completion. Studies have shown that student loan delinquencies are not correlated with larger balances, but rather with the inability to graduate and earn a degree. The rate of delinquency for those who leave college with no degree is twice as high as it is for those who earn an associate degree and four times as high as it is for those earning a bachelor's.[9]

The disproportionate number of subprime and deep subprime borrowers and their climbing delinquency rates are concerning. But limiting loan availability could restrict access to college, particularly for those with lower incomes, who are more likely to have subprime credit. Given how strongly correlated higher education is with future earnings,[10] college is critical to helping lower-income individuals build assets and move up the economic ladder.

Increasing college completion could be strategy for improving outcomes. Knowing the power of government action and regulation to influence credit access and outcomes, it's paramount that the nation strike a balance between lower delinquencies and improved college access.

LOOKING AHEAD: CONSUMER CREDIT PATTERNS

Future consumer credit profile reports will put the most recent data in context and give a more complete picture of credit inclusion and performance trends in Dallas County. Now that the nation is more than eight years past the Great Recession, average mortgage balances may grow, particularly in Dallas as average home sales prices continue to rise. The downward trend of serious delinquencies for most debt types is a positive sign for Dallas, though the small uptick in auto loan delinquencies should be monitored. For student loans, the problem of growing delinquencies among subprime and deep subprime borrowers begs deeper research and policy discussion.

Notes

[1]See "Subprime Mortgage Crisis," by John V. Duca, FederalReserveHistory.org, Nov. 22, 2013, www.federalreservehistory.org/essays/subprime_mortgage_crisis.

[2]The Federal Reserve Bank of New York Consumer Credit Panel/Equifax consists of detailed Equifax credit report data in quarterly increments from 1999 to the present for a unique longitudinal panel of individuals and households. The panel is a nationally representative 5 percent random sample of all individuals with a Social Security number and a credit report; it is also matched to individuals living at the same address as the primary sample members. The resulting database includes approximately 40 million individuals in each quarter. The data do not contain demographic information such as gender, race, ethnicity or income.

[3]We estimate the number of credit borrowers out of total potential borrowers by dividing the number of people with a credit report in the Equifax database by the number of residents in Dallas county who are at least 18 years of age. For more information about the credit economy and credit inclusion across the nation, visit www.newyorkfed.org/data-and-statistics/data-visualization/community-credit-profiles/index.html#inclusion.

[4]See "Community Reinvestment Act of 1977," by Michael Berry and Jessie Romero, FederalReserveHistory.org, www.federalreservehistory.org/essays/community_reinvestment_act.

[5]Mortgage data include only for first liens. Credit cards are revolving accounts offered through a bank, credit union or national credit card company. Auto loans are those used to finance the purchase of a car, whether through a mainstream banking institution or a car dealership/financing company. Student loans include government loans as well as loans offered through private companies.

[6]The exception is PLUS loans, available to graduate students and parents of undergraduate students; although interest rates are the same for borrowers, approval depends on not having an "adverse credit history" as defined here: https://studentaid.ed.gov/sa/sites/default/files/plus-adverse-credit.pdf. See "Federal Versus Private Loans," StudentAid.gov, U.S. Department of Education, https://studentaid.ed.gov/sa/types/loans/federal-vs-private.

[7]Trends in Student Aid 2016, College Board, 2016, https://trends.collegeboard.org/sites/default/files/2016-trends-student-aid.pdf.

[8]Tuition and fees for four-year public universities have doubled since 2000, adjusting for inflation. See "Published Tuition and Fees Relative to 1986–87, by Sector," CollegeBoard.Org, https://trends.collegeboard.org/college-pricing/figures-tables/published-tuition-and-fees-relative-1986-87-sector.

[9]See "A Trillion Dollar Question: What Predicts Student Loan Delinquency Risk?" by Alvaro Mezza an Kamila Sommer, Federal Reserve Board of Governors, FEDS Notes, Oct. 16, 2015, www.federalreserve.gov/econresdata/notes/feds-notes/2015/trillion-dollar-question-what-predicts-student-loan-delinquency-risk-20151016.html.

[10]See the chart "Unemployment Rates and Earnings by Educational Attainment, 2016," Bureau of Labor Statistics, Oct. 24, 2017, www.bls.gov/emp/ep_chart_001.htm.

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