Americans in Debt

Americans are buying more than ever and paying for it with loans and credit. Mounting debt should serve as a wake-up call for over-leveraged households.

U.S. household debt rose to $17.29 trillion in the third quarter -- up $3.1 trillion since the end of 2019.*

Americans are at it again. Spending beyond their means and racking up debt. The latest New York Federal Reserve *Quarterly Report on Household Debt and Credit* shows that, as of September 30, aggregate household debt balances have grown to over $17 trillion, continuing an upward trajectory since 2013 -- one that has accelerated in recent years. All categories of debt registered increases, but of particular concern is the rise in credit card and auto loan balances. Credit card debt now tops $1 trillion, and car loan balances stand at $1.6 trillion.[1] As of June 30, the average cardholder has $6,568 in credit card debt, up 10% from a year earlier.[2] The average loan for a new car now tops $40,000, with an average payment of over $700 per month.[3] Ouch!

Falling Behind

On their own, these seemingly grim statistics do not pose that big of a concern. Household debt levels vary with economic cycles, and debt service ratios (monthly debt payments as a percentage of disposable income) have been higher in the past. But delinquencies have also climbed. In fact, more and more Americans are falling behind on their car loan and credit card payments than at any time in more than a decade.[4] The rate of households becoming delinquent or entering serious delinquency (behind by 90 days or more) on their credit cards is the highest since the end of 2011. And subprime auto loan delinquencies are worse now than they were during the financial crisis.[5]

Do *You* Have Too Much Debt?

If you find that you have been taking on more debt lately, here are some common signs to watch for that might indicate you are taking on too much.

- **Your credit card balance keeps growing.** Credit card debt is one of the most expensive types of debt. Interest rates on unpaid balances can run 20% or higher. Ideally, you should pay your full balance every month. But if you do maintain a balance and find that it's growing, it may be time to cut back.
- **You spend over 36% of your gross pay on debt service.** Banks typically look at this ratio when you apply for a loan. If you exceed it, your possibility of being declined is greater, and if you do get approved, you may have to pay a higher rate of interest.
- **The total amount you owe, not counting a mortgage, exceeds your annual income.** Although debt burden is more about required payments than it is about outstanding balances, it should still serve as a warning if your

non-mortgage debt exceeds your gross income. That amount of debt can take years to pay down and cost thousands in interest.
- **Your credit score is under 650.** A high debt balance does not necessarily translate to a low credit score. But the total amount owed does factor into your score. If your score falls below 650, it may impair your ability to get future credit or increase the rate you pay for it.

How Can You Reduce Your Debt?

How much debt can you afford? That depends on your personal situation, as well as your ability to service the debt. But if you, like many Americans, are looking for ways to reduce your debt, consider the following steps.

- **Pay off high interest rate debt first.** Begin with your highest rate credit cards and eliminate the balance as aggressively as possible. Just paying off a little more each month can significantly reduce your payback period and the total interest paid.
- **Avoid the "minimum payment" trap.** Pay more than the minimum on your credit cards. Making only minimum payments will significantly increase the amount you'll eventually pay.
- **Transfer high-rate debt to lower rate loans.** Consolidating credit card debts to a single, lower rate card saves more than postage and paperwork. It also saves in interest costs over the life of the loan. What's more, you may be able to pay off higher rate credit with lower rate loans, such as a home equity line of credit.
- **Borrow only for the long term.** The best use of debt is to finance things that will potentially gain in value or increase your income, such as a home or an education. Avoid using your credit card for concert tickets, vacation expenses, or meals out. By the time the balance is gone, you'll have paid far more than the cost of these items and have nothing but memories to show for it.

By analyzing your spending, controlling expenses, and establishing a plan, you can reduce -- and perhaps eliminate -- your debt, leaving you with more money to save today and a better outlook for your financial future.

*Federal Reserve Bank of New York, *Household Debt and Credit Report*, November 2023.

[1]Ibid.

[2]MoneyGeek, *Average Credit Card Debt in America,* updated November 4, 2023.

[3]Bankrate, *Average car payments in 2023*, October 9, 2023.

[4]The Washington Post, *Delinquencies rise for credit cards and auto loans, and it could get worse*, August 30, 2023.

[5]CNN Business, *U.S. credit card balances see largest yearly leap on record*, November 7, 2023.

