Piling on the Debt

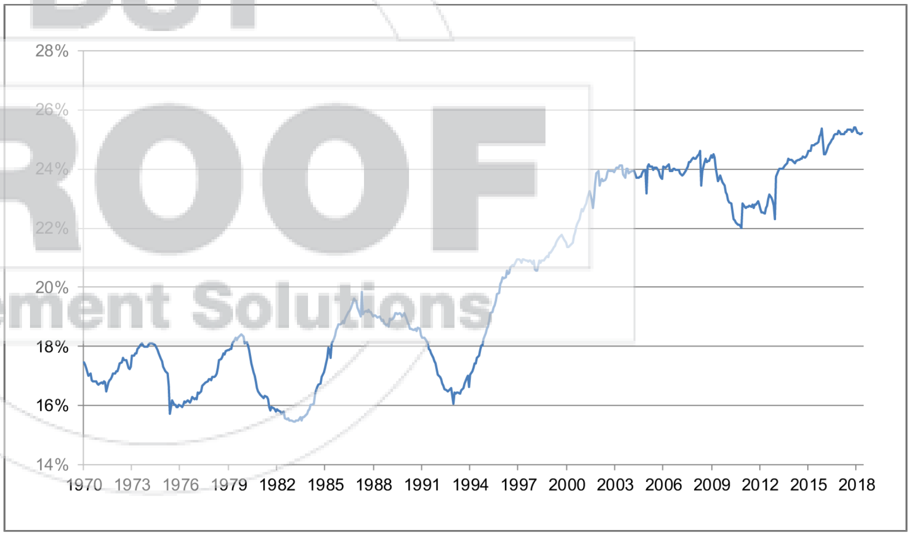
Americans are buying more than ever and paying for it with loans and credit. Mounting debt should serve as a wake-up call for over-leveraged households.

Household debt grew to over $13.3 trillion as of June 30, topping even 2008 financial crisis levels.

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 June 30, aggregate household debt balances had grown to $13.3 trillion -- topping the previous record of $12.7 trillion set during the financial crisis in 2008. Household debt is now 19% higher than the post-financial-crisis trough reached during the second quarter of 2013.[1] In fact, consumer credit has been on an upward trajectory since 2010, increasing for 16 consecutive quarters as of June 30, 2018. What's more, household debt is also hovering near a peak of 25% of disposable income, well above its historical average of about 21% since 1970.[2]

I Owe, I Owe[2]

Total consumer credit owned and securitized, outstanding as a percentage of disposable personal income:



Thankfully, the booming American economy makes the higher debt levels sustainable -- for now at least. Charge-off and delinquency rates remain moderate, and mortgage defaults have actually declined in recent quarters. But if and when the economy does eventually stumble, many households will likely struggle to keep up with their growing debt burden.

What Americans Owe[3]

Average mortgage balance	**$173,995**
Average auto loan balance	**$27,667**
Average household credit card debt	**$15,654**
Average total household debt	**$131,431**
Average debt service ratio	**15.5%**

Do *You* Have Too Much Debt?

Here are some common signs to watch for that might indicate you are taking on too much debt.

- **Your credit card balance keeps growing.** Credit card debt is one of the most expensive types of debt. Interest rates on unpaid balances typically run 18% 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.** This is the ratio banks typically look at 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 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 670.** 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 670, it may impair your ability to get future credit or increase the rate you pay for it.

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.

[1]Source: Federal Reserve Bank of New York, *Quarterly Report on Household Debt and Credit, 2018: Q2*, August 2018.

[2]Source: Board of Governors of the Federal Reserve System (US), Total Consumer Credit Owned and Securitized, Outstanding [TOTALSL], retrieved from FRED, Federal Reserve Bank of St. Louis.

[3]Sources: Nerdwallet, 2017 American Household Credit Card Debt Study; The Federal Reserve Household Debt Service and Financial Obligations Ratios. Debt balances are as of September 2017 for households carrying that type of debt. Debt service ratio represents household debt service payments and financial obligations as a percent of disposable personal income, seasonally adjusted.

