Cross-Sectional Patterns of Mortgage Debt During the Housing Boom: Evidence and Implications

Chris Foote, Lara Loewenstein and Paul Willen
FRB Boston

FDIC Consumer Credit Symposium
Washington, DC
October 28, 2016
Disclaimer

- I am speaking today as a researcher and as a concerned citizen
- not as a representative of:
  - The Boston Fed
  - or the Federal Reserve System

- When I say “we”, I don’t mean Janet and me.

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- Explosion in debt
- Not income
- Why?
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Household Mortgage Debt (left scale)

Personal income (right scale)
Explaining the boom

- Credit Expansion in early 2000s
  - Helped constrained borrowers
    - Marginal borrowers
    - Constrained borrowers
    - Drive up house prices (also relaxes constraints)
- Unconstrained borrowers?
  - Wealth effects?
- Relative balance sheet shift in debt to constrained
- Old Question: Why credit expansion?
- Revisit shift
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Credit Expansion

- Constrained
  - Low Income
  - Low Credit Score

- Unconstrained
  - High Income
  - High Credit Score

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Why?
- Securitization
- Deregulation
- Over-regulation
- Optimistic HPA Beliefs?

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Low Income
Low Credit Score

Relative Shift

Unconstrained
High Income
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   - No gender, race

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Finding 1: Reallocation was across cities not within them

- Distribution of debt shifts
- What if we look within cities?
- Change in distribution was across cities
- Reallocation to constrained should occur within cities.

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Cross Section of Debt

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Finding 2: No relative increase in debt among low income households

- Debt shifts up across all income
- Regressions show no change in slope
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Foote, Loewenstein & Willen (FRB Boston)
Finding 2': Most new debt went to high income households

- Debt highly skewed toward rich people
- In 2006

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</tr>
</tbody>
</table>

- In $, most debt went to the rich.
Finding 3: Relative changes in originations offset by terminations

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- If we only had prime, boom would have resulted in big shift in debt to high income areas.

Contributions of Mortgage Types to Total ZIP-Level Debt Growth, by Initial Income Group of ZIP Code: 2001-2006

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Why?
- Securitization
- Deregulation
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- Optimistic HPA Beliefs?

Credit Expansion

Constrained
Low Income
Low Credit Score

Relative Shift

Unconstrained
High Income
High Credit Score

- New insight: Everyone took out more debt
- Why?
  - Something that made everyone borrow more
  - Not just constrained people
- Candidate: Change in beliefs about HPA

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- New view: Subprime allowed low income to keep up
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