The State of American Credit

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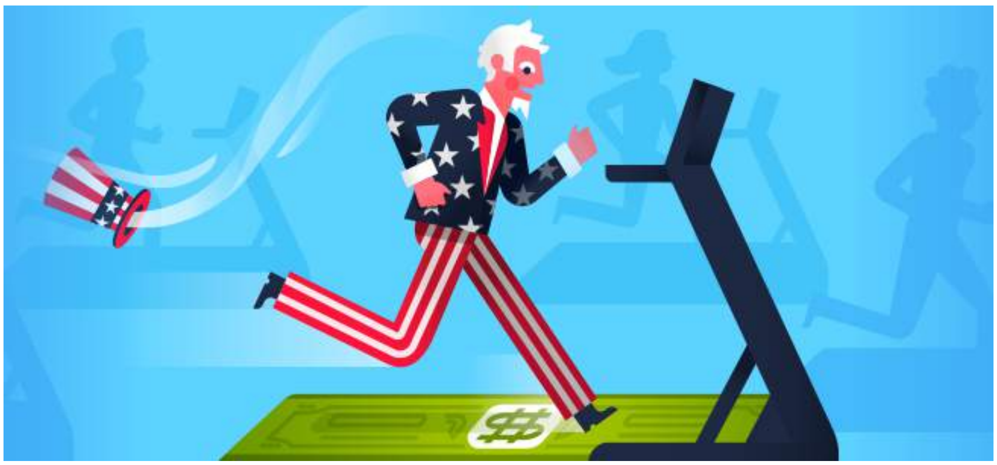


While some pundits claim the Great Recession made us a nation of debtors, experts say Americans' relationship with credit hasn't changed much in the last three decades. The situation may be difficult for many, but there are tools and tips to help better manage this debt load.

According to "The Complex Story of American Debt," a July 2015 report from Pew Charitable Trusts, 8 in 10 Americans carry debt, the bulk of it mortgage debt. The biggest debtors are from Generation X (defined by Pew as those born between 1965 and 1980), whose median household debt stands at just under $104,000. Baby boomers (born between 1946 and 1964, and approaching or entering retirement) aren't much better off. Their median household debt stands at just over $70,000.

Robert Hockett, J.S.D., Edward Cornell professor of law at Cornell University, says blaming the 2008 recession would be oversimplifying things — private debt buildup has been growing since the late 1970s. "Incomes below the top quintile seem to have been stagnant since then," he explains. Each "next generation" accumulates debt to enjoy the material benefits and lifestyle to which they became accustomed with their parents.

The Pew report supports this, indicating those who carry the most have incomes that have stagnated even as the cost of living has risen. People have started thinking of debt as a way to manage that gap. Sixty-eight percent of Pew survey respondents believe loans and credit cards have expanded their opportunities.

"Americans' relationship with debt is complicated," says Clint Key, research officer with Pew's financial security and mobility project team. "[Americans] know they need debt, but they don't feel comfortable holding it." One's debt load has much to do with each individual household's situation, plus "the total magnitude of the debt relative to household resources," Key says. For instance, mortgages tend to be valuable debt given they support the average American's largest asset — his or her home.

Average Debt Amounts, by Type

Source: 2015 American Household Credit Card Debt Study, NerdWallet

Consumers' situations become challenging, however, when they have underwater mortgages, for example. High-interest rate loans, whether for mortgages, automobiles or credit cards, can all make a consumer financially vulnerable.

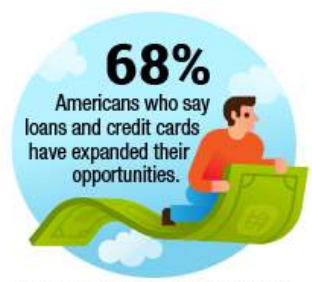
Sometimes taking on debt can help one deal with unexpected expenses, Key explains: "Maybe you take on credit card debt to pay for automobile repairs, so you can drive your car to work and keep your job."

Likewise, student loans provide opportunity: Currently, 21 percent of surveyed Americans shoulder this type of debt. But it becomes challenging when that debt isn't paying for itself — either because the recipient didn't graduate, or because he or she was unable to land a job with a commensurate salary.

"There are different types of debt that are appropriate at different times of life," says Dan Matysik, vice president, personal loans, Discover Financial Services. "A good product is one that delivers long-term benefits." Those are generally low-cost loans — with fixed interest rates and flexible repayment terms.

Consolidating debt with a personal loan can help you save money, by reducing your overall interest rate. Debt consolidation can also lock you into a more manageable fixed rate. Flexible, fixed-rate payment terms offer the option of having a longer repayment period (to reduce monthly expenses) or an accelerated option (to become debt-free quickly). Combine that with the convenience of a single payment, plus a sense of control over your finances, and this option can make a lot of sense.

"Not all debt consolidation loans are created equal," says Vicki Bogan, Ph.D., associate professor of finance at Cornell and director of the Institute for Behavioral and Household Finance. "Make sure you understand if you're paying some kind of service fee, the loan's interest rate and origination fees." Look for an option without an origination fee altogether.



Source: The Complex Story of American Debt

"The most important benefit of [debt consolidation] is it gives you an occasion to take stock of your total balance sheet," Hockett says. Once you have a clear picture of your assets and liabilities, you will become more cognizant of what you can and can't afford.

"Put together a budget," he continues. "Determine your monthly inflows and outflows."

Bogan agrees, saying that consumers oftentimes reduce their monthly expenses by getting on the phone with creditors themselves to request lower interest rates or lower monthly payments.

Consumers with multiple higher-interest debts can consolidate debt with a lower-interest personal loan, and Matysik also urges consumers to pay their bills on time (setting up automatic payments helps), plus to monitor their credit scores — something anyone can easily do through Discover's free Credit Scorecard tool.