September 26, 2024

Global Credit Weekly:

A (still) bifurcated U.S. consumer

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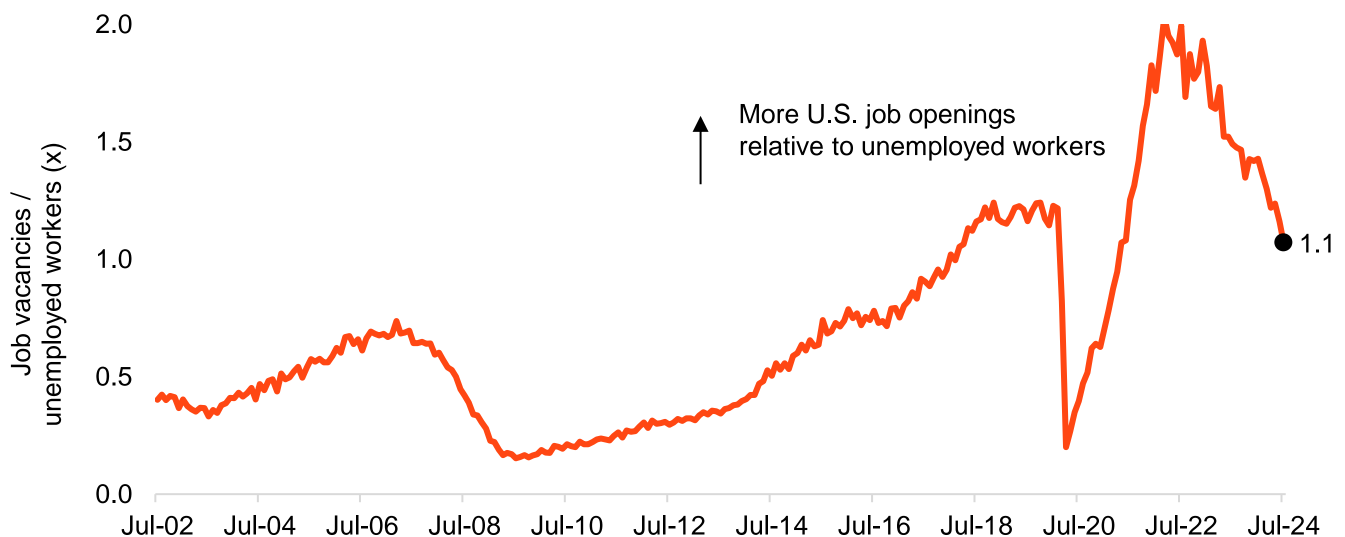
Key takeaways

- The health of the U.S. consumer – which drives 68% of U.S. gross domestic product (GDP) – has been closely watched by market participants over the past several months, as mixed commentary from a range of retail and consumer companies has pointed to more cost-conscious behavior. That focus further intensified this week following a downbeat consumer confidence survey, which highlighted respondents' more negative sentiment on the availability of "plentiful jobs." And of course, the potential for further weakening in the U.S. labor market had already been on investors' radars given the recent increase in the unemployment rate and the triggering of the "Sahm rule" recession indicator.
- That said, there is not a "one size fits all" U.S. consumer, in our view. Higher-income consumers have benefited from significant gains in assets they own (homes and investments). Meanwhile, lower income consumers are facing headwinds from higher debt service costs and elevated price levels (in absolute terms) in recent years (even if the *year-over-year rate of inflation* is improving).
- In this *Global Credit Weekly*, we provide another "temperature check" on the financial health of the U.S. consumer and find that the trend of bifurcation that we highlighted in May remains firmly in place. We believe these developments are important for corporate credit investors to monitor for three reasons. First and foremost (and as mentioned above), U.S. consumer spending is a significant driver of overall economic activity. The current pace of above-trend growth in the U.S. (note: 3Q2024 GDP is tracking at +2.9% per the Atlanta Fed's GDPNow) has been a key tailwind behind the resilience of corporate credit spreads so far this year and will determine the sustainability of corporate credit's relatively tight spread valuations. Second, the USD IG and USD HY corporate credit markets have meaningful, *direct* sector exposure to consumer spending categories (detailed within). Third, the bifurcation which remains evident in the U.S. consumer is likely to drive persistent dispersion (performance, fundamentals) across sectors and issuers.

Exhibit 1: The U.S. labor market has rebalanced to its pre-pandemic level

The ratio of U.S. job vacancies to U.S. unemployed workers, both seasonally adjusted



Source: BlackRock, Bureau of Labor Statistics. Captures data through July 31, 2024.

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The U.S. consumer retakes center stage

The health of the U.S. consumer – which drives 68% of U.S. gross domestic product (GDP) – has been closely watched by market participants over the past several months, as mixed commentary from a range of retail and consumer companies has pointed to more cost-conscious behavior.

That focus further intensified this week following a downbeat consumer confidence survey, which highlighted respondents' more negative sentiment on the availability of "plentiful jobs." And of course, the potential for further weakening in the U.S. labor market had already been on investors' radars given the recent increase in the unemployment rate and the triggering of the "Sahm rule" recession indicator.

That said, there is not a "one size fits all" U.S. consumer, in our view. As we have outlined previously, higher-income consumers have benefited from significant gains in assets they own (homes and investments). Meanwhile, lower income consumers are facing headwinds from higher debt service costs and elevated price levels (in absolute terms) in recent years (even if the *year-over-year rate of inflation* is improving).

In this *Global Credit Weekly*, we provide another "temperature check" on the financial health of the U.S. consumer and find that the trend of bifurcation that we highlighted in May remains firmly in place. We believe these developments are important for corporate credit investors to monitor for three reasons:

- First and foremost (and as mentioned above), U.S. consumer spending is a significant driver of overall economic activity. The current pace of above-trend growth in the U.S. (note: 3Q2024 GDP is tracking at 2.9% per the Atlanta Fed's GDPNow, as of September 18th) has been a key tailwind behind the resilience of corporate credit spreads so far this year and will determine the sustainability of corporate credit's relatively tight spread valuations.
- Second, the USD IG and USD HY corporate credit markets have meaningful, *direct* sector exposure to consumer spending categories, as shown in Exhibit 2. And of course, consumer spending factors into many other sectors shown below, indirectly.
- Third, the bifurcation which remains evident in the U.S. consumer is likely to drive persistent dispersion (performance, fundamentals) across sectors and issuers. Exhibit 16 illustrates some of the recent shifts at the sector level. For example, retailers, leisure, airlines, gaming and lodging underperformed the broader index QTD despite outperforming in 1H2024.

Exhibit 2: The consumer sectors are sizable in the corporate credit market

Sector market value totals ($bn) and weights (%) for the Bloomberg USD IG and USD HY Corporate indices

	USD IG		USD HY	
	Market value ($bn)	Index weight (%)	Market value ($bn)	Index weight (%)
Banking	$1,579	22.4	$12	0.9
Basic Industry	$186	2.6	$74	5.6
Brokerage, Asset Mgrs., Exchanges	$108	1.5	$12	0.9
Capital Goods	$380	5.4	$142	10.6
Communications	$581	8.2	$195	14.5
Consumer Cyclical	$508	7.2	$269	20.1
Consumer Non-Cyclical	$1,104	15.7	$153	11.4
Electric	$598	8.5	$35	2.6
Energy	$501	7.1	$158	11.8
Finance Companies	$87	1.2	$52	3.9
Insurance	$342	4.8	$36	2.7
Natural Gas	$50	0.7	$0	0.0
Other Financial	$3	0.0	$16	1.2
Other Industrial	$34	0.5	$18	1.3
Other Utility	$13	0.2	$0	0.0
REITs	$190	2.7	$29	2.2
Technology	$641	9.1	$104	7.7
Transportation	$150	2.1	$35	2.6
Total	$7,055	100	$1,340	100

Source: Bloomberg, BlackRock. As of September 25, 2024.

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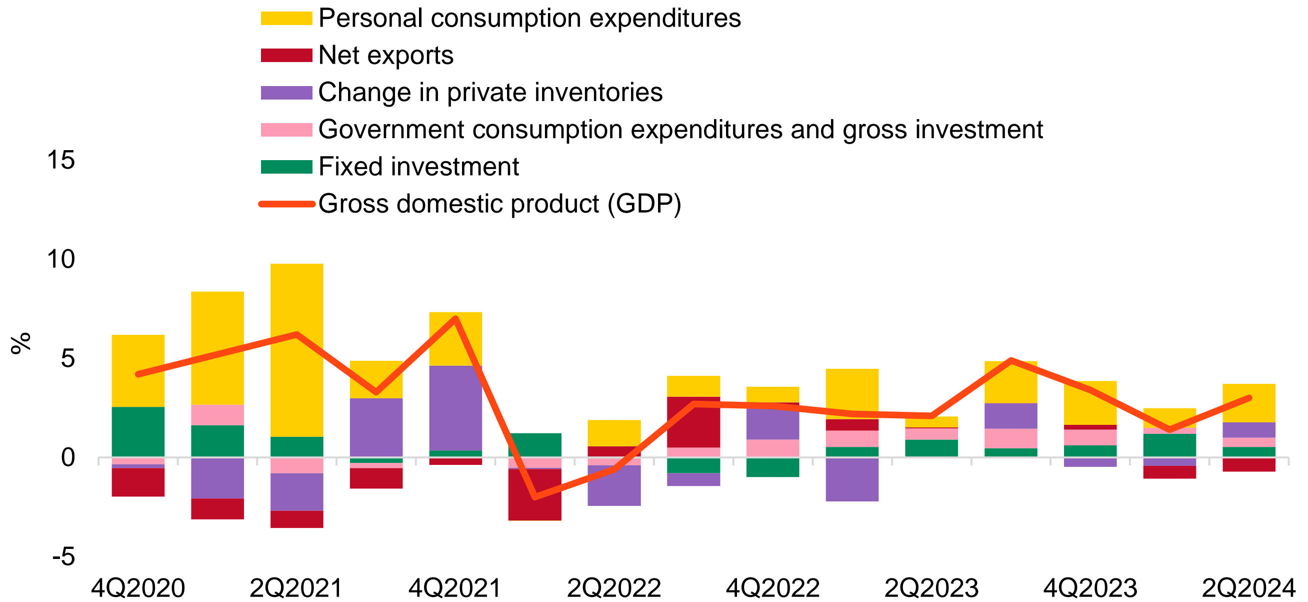
Exhibit 3: Personal consumption expenditures supported solid U.S. GDP growth in 2Q2024
Contributions to quarter-over-quarter real U.S. GDP growth (%), seasonally adjusted at an annualized rate



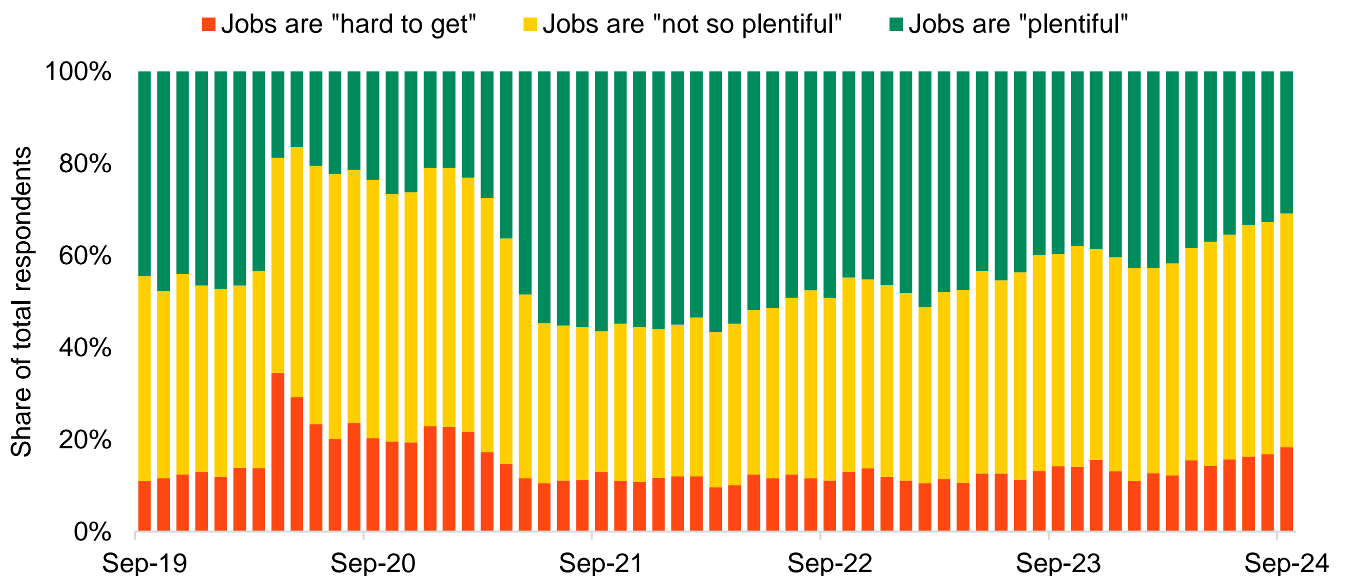
Source: Bureau of Economic Analysis, Bloomberg, BlackRock. As of June 30, 2024 (most recent available).

Consumer survey signals some concern about the U.S. labor market

We first start by unpacking the most recent data. The Conference Board's latest Consumer Confidence Index (published September 24th) came in lower than anticipated at 98.7 (down from 105.6 in August and vs. Bloomberg's consensus estimate of 104). The factors influencing this decline in consumer confidence are multifaceted and include consumer concerns about recent slowing in the labor market.

Notably, consumers were asked to assess the current job market by selecting one of three possible metrics: "jobs are plentiful," "jobs are not so plentiful," or "jobs are hard to get". The share of consumers who responded that jobs are "plentiful" fell for the seventh consecutive quarter (Exhibit 4).

Exhibit 4: The share of consumers that believe jobs are "plentiful" has gradually declined since February 2024
Share of consumers who responded that jobs are: "hard to get", "not so plentiful" and "plentiful" each month



Source: Consumer Confidence Survey by The Conference Board, BlackRock. As of September 2024.

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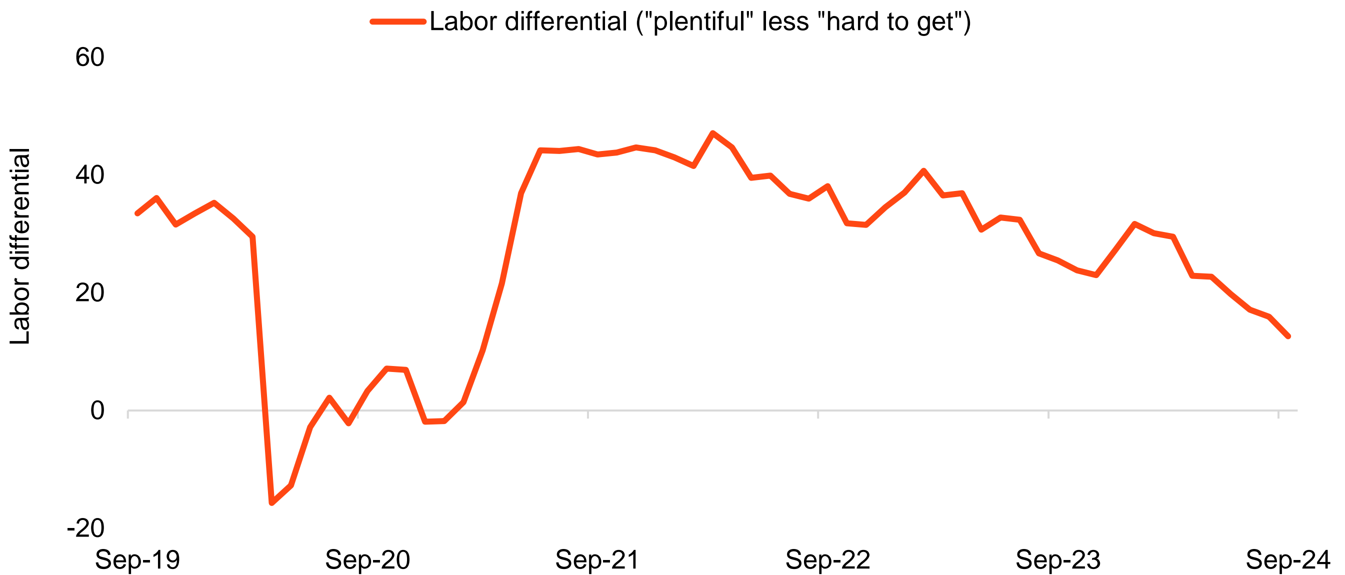
The labor differential, defined as the share of respondents who selected jobs are "plentiful" minus the share of respondents who selected jobs are "hard to get," fell to its lowest level since March 2021 (Exhibit 5), suggesting consumers currently have a more cautious view of the labor market than they have in recent history.

As we have highlighted previously, most of the rebalancing (cooling) in the U.S. labor market over the past several months has been driven by reduced hirings (as seen in the narrowing jobs-workers gap; Exhibit 1) and not an increase in layoffs (as new jobless claims have been relatively contained). In our view, the key risk is if corporate *layoffs* accelerate from here – as those types of actions tend to have more negative "second round" effects on the economy.

Exhibit 5: The labor differential shows consumers are wary about the labor market
Share of consumers who responded that jobs are "plentiful" minus the share of consumers who responded that jobs are "hard to get" each month



Source: Consumer Confidence Survey by The Conference Board, BlackRock. As of September 2024.

There is not a "one size fits all" consumer

While such aggregate survey measures can be informative to monitor for directional trends, the data show the trend of bifurcation among the U.S. consumer remains firmly in place.

Before diving into the details, it is important to put some of the market moves of the past few years in context. As we last highlighted in July, higher-income consumers (who tend to be asset *owners*) have benefited from gains in the housing and investment markets over the past few years. For example, the S&P CoreLogic Case-Shiller U.S. National Home Price Index has increased by 54% from year-end 2019 to July 31, 2024 (most recent). And the value of the S&P 500 has increased by 78% from year-end 2019 to September 25, 2024.

On the other hand, lower-income consumers, who are more likely to rent (Exhibit 6) and carry debt balances, have experienced headwinds from higher borrowing costs and elevated price levels (in absolute terms) in recent years (even if the *year-over-year rate of inflation* is improving). This helps explain, in our view, some of the "conflicting" data points released about the financial health of the U.S. consumer in recent months (per widely tracked economic data).

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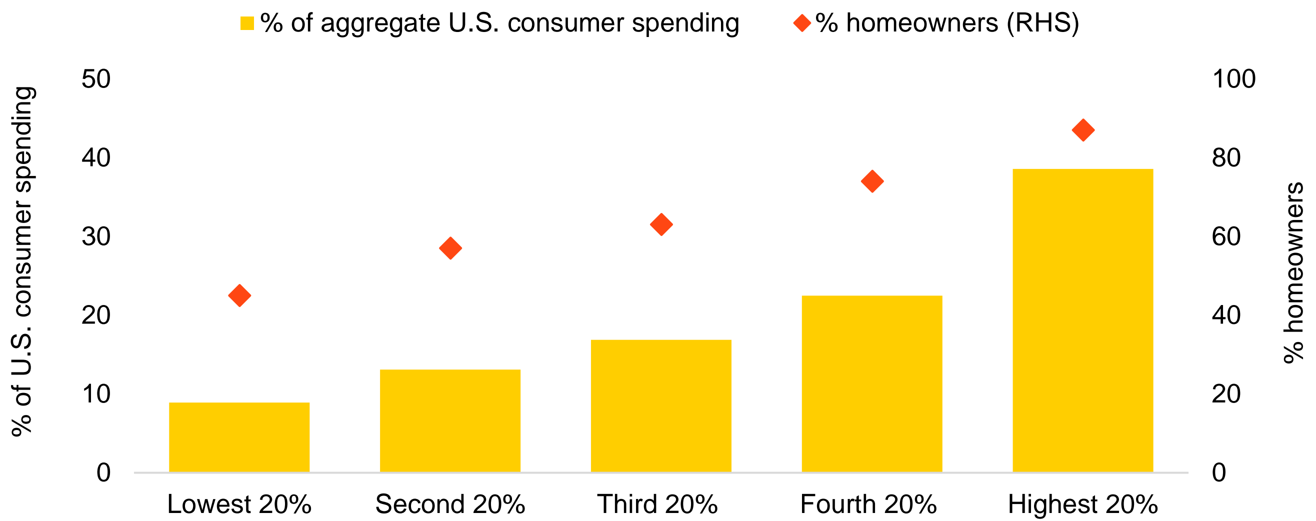
Exhibit 6: The U.S. consumer remains bifurcated by spending levels and home ownership
U.S. annual aggregate expenditures by consumer income quintile, and the share of consumers in each cohort that are homeowners (RHS)

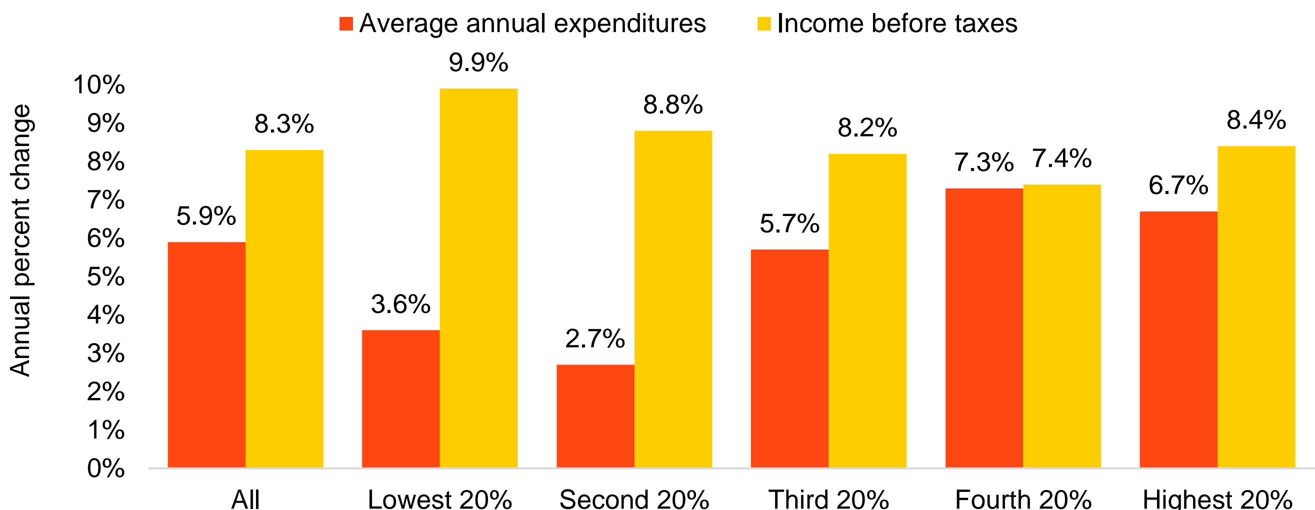


Source: BlackRock, U.S. Bureau of Labor Statistics Consumer Expenditure Survey (September 2023 - reflects data from 2022, most recent of granular data).

The most recent Consumer Expenditure Survey from the U.S. Bureau of Labor Statistics (partial results were published September 25th) highlights how consumers across income cohorts adjusted their spending in 2023. The key takeaway from Exhibit 7, in our view: the two lowest income cohorts generated the smallest increases in spending (3.6% and 2.7%), *despite capturing the largest increases in income* (9.9% and 8.8%).

Indeed, according to the Conference Board's most recent survey (which closed September 17th), confidence declined across most income groups, with the largest decline among those earning less than $50,000/year. By contrast, consumers earning more than $100,000/year have remained most confident, on average, over the last six months.

Exhibit 7: The two lowest income cohorts generated the smallest increases in spending
Annual percent change in average expenditures and income before taxes in 2023, by income quintile



Source: BlackRock, U.S. Bureau of Labor Statistics Consumer Expenditure Survey (September 2024 – reflects data from 2023).

Further, a recent study from the San Francisco Federal Reserve (SF Fed) found that "pandemic-era wealth", defined as additional liquid assets accumulated by households due to pandemic-related changes in government income support and personal consumption decisions, varied significantly between high-income households (top 20%) and middle- to low-income households (bottom 80%). There were two notable differences between the groups, as it relates to pandemic-era wealth: (1) the middle- to low-income households spent down their pandemic wealth by late-2021, while high-income households did so by mid-2022; (2) The decline in this wealth coincided with rising credit card delinquency rates, which more severely affected the middle- to low-income group. Further, the authors note that following the pandemic, higher rates allowed high-income households to disproportionately grow their wealth via investments in money markets.

Delinquencies: frequency vs. severity

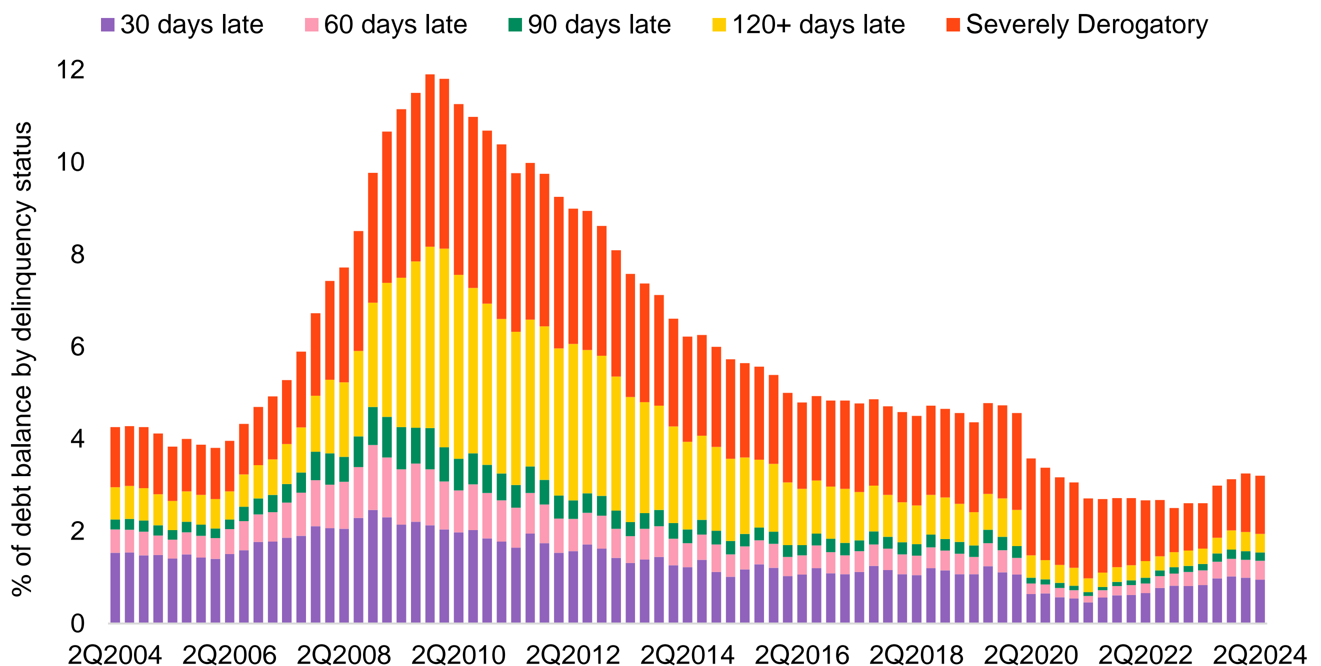
Debt delinquency data from the Federal Reserve Bank of New York (NY Fed) also shows a split among consumers. For example, delinquent borrowers now carry a higher debt burden than in the past, yet the proportion of current borrowers remains above the 10-year average.

As such, the share of total delinquent debt has increased to late 2020 levels but remains below the post-financial crisis average of 6.8% (from 2010-2019; Exhibit 8). That said, debt that is "severely derogatory," or accounts that are delinquent and have reports of a repossession, charge off to bad debt, or foreclosure, accounts for the largest segment of delinquent debt, suggesting that borrowers that reach "severely derogatory" status on their debt struggle to become current again.

Further, Exhibit 9 illustrates a meaningful decline in the share of consumers with collections, dropping by over 60% since its peak in 2013. Today, only about 5% of consumers have collections. However, the average collection amount has grown, reaching a record high in 3Q2023. Again, this suggests that struggling consumers are taking on a larger burden. In other words, the severity of delinquencies appears to be increasing in the current cycle.

This bifurcation is similarly evident in a study by the Philadelphia Federal Reserve, which also found that delinquent consumers carry a larger debt burden. This again suggests that consumers who are further behind on payments (i.e., 90+ days delinquent) are less able to become current compared to (1) past patterns of this specific cohort and (2) the 30+ and 60+ days delinquent cohorts.

Exhibit 8: Total delinquent debt balance is increasing, but remains modest relative to history
Share of total outstanding debt that is delinquent, by delinquency status



Source: New York Fed Consumer Credit Panel/Equifax, BlackRock. As of 2Q2024.

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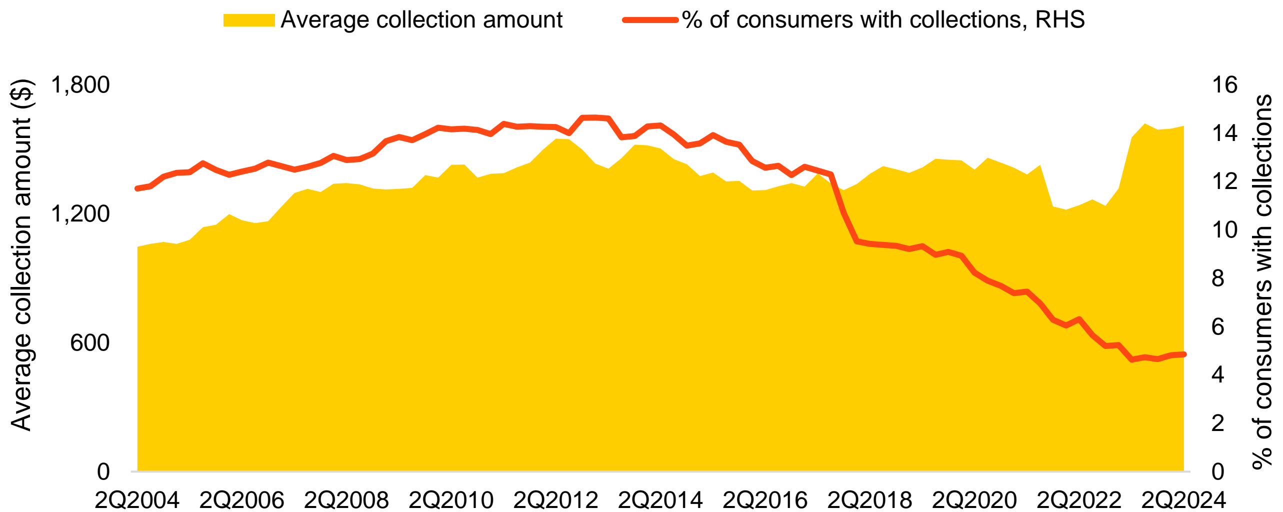
Exhibit 9: The average collection amount for delinquent consumers has grown in recent years
Average collection amount and share of consumers with collections from third-party collections



Source: New York Fed Consumer Credit Panel/Equifax, BlackRock. As of 2Q2024.

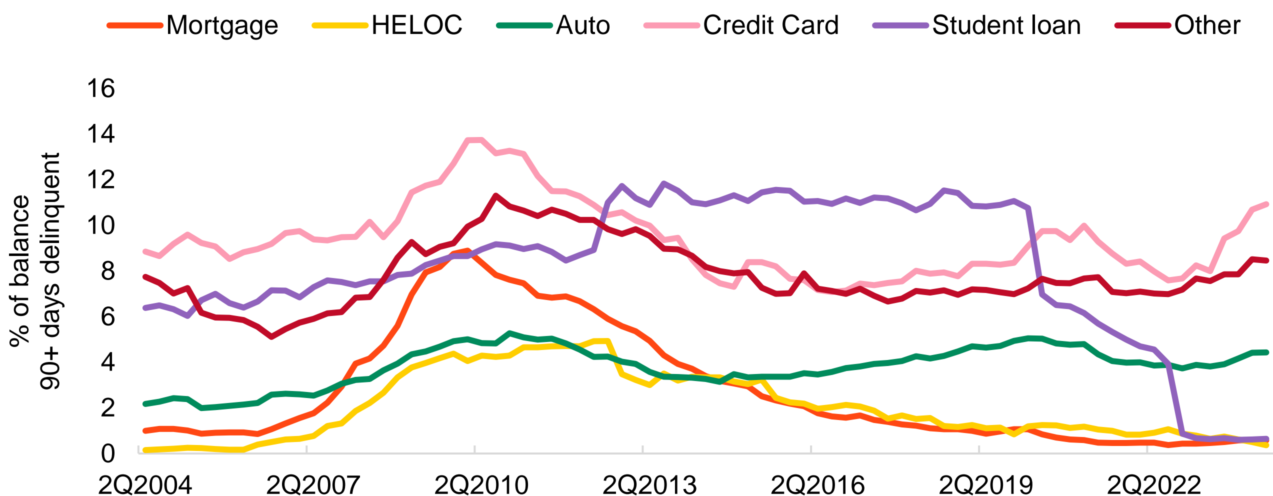
Not all credit types are created equally

Beyond dispersion in borrower performance, there is significant dispersion across credit *types* (i.e., credit card, auto, mortgage, etc.). As of 2Q2024, 11% of all credit card balances are severely delinquent (i.e., 90+ days delinquent), making it the loan category with the largest share of balances severely delinquent (Exhibit 10). Delinquencies are also elevated in the 'Other' (defined in footnote below) and Auto credit categories, with 8.45% and 4.43% of balances severely delinquent in 2Q2024, respectively.

Meanwhile, mortgage and home equity line of credit (HELOC) delinquencies remain very low – suggesting that consumers are prioritizing staying current on home-related debt (a topic we discussed recently). Strong home price appreciation has likely encouraged homeowners to protect the value of their home. We expect this pattern to persist. That said, the strength of the U.S. labor market will remain a critical ingredient to this view.

Importantly, while student loan payments resumed in late 2023, student loan delinquencies will not be reported to credit bureaus until September 30, 2024, so student loan delinquencies are likely understated until 4Q2024 data is available.

Exhibit 10: Housing-related delinquencies stay modest, while others rise
Percent of balances seriously delinquent (90+ days delinquent) by loan type



Source: New York Fed Consumer Credit Panel/Equifax, BlackRock. As of 2Q2024. "Other" includes consumer finance (sales financing, personal loans) and retail (clothing, grocery, department stores, home furnishings, gas etc.) loans.

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Higher rates have curbed mortgage refinancing activity

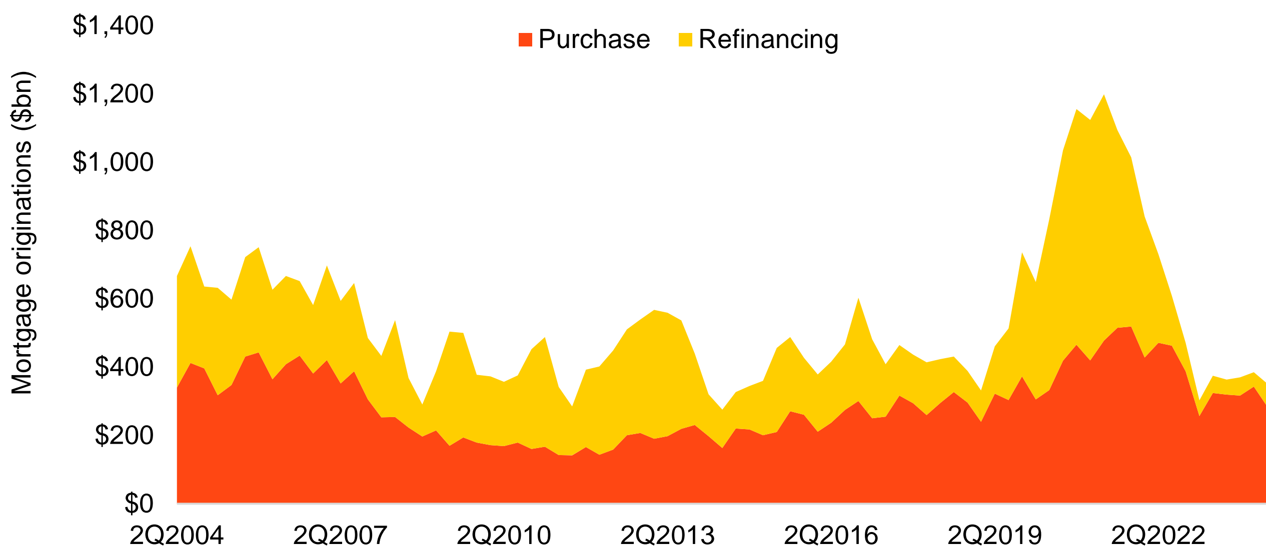
As aforementioned, home values have significantly increased over the past few years, highlighting the bifurcation between homeowners and non-homeowners. Low interest and mortgage rates immediately following the onset of the pandemic led to a surge in refinancings and mortgage originations, with both reaching record highs (Exhibit 11). This is a similar trend to the wave of refinancing that occurred in the corporate credit universe.

According to the Federal Housing Finance Agency, 96% of borrowers in the U.S. have fixed-rate mortgages. By year-end 2023, nearly 70% of mortgages outstanding in the U.S. had interest rates 3 percentage points lower than the current mortgage rates prevailing at the time, according to the NY Fed, making refinancing unattractive and "locking in" home equity. According to a March 2024 working paper by the Federal Housing Finance Agency, 63% of those borrowers have a fixed rate below 4%.

As this trend has persisted, the share of mortgage balances originated in the last two years continued to decline, reaching an all-time low in 2Q2024 (Exhibit 12).

Exhibit 11: Mortgage refinancings and purchases declined as interest rates increased

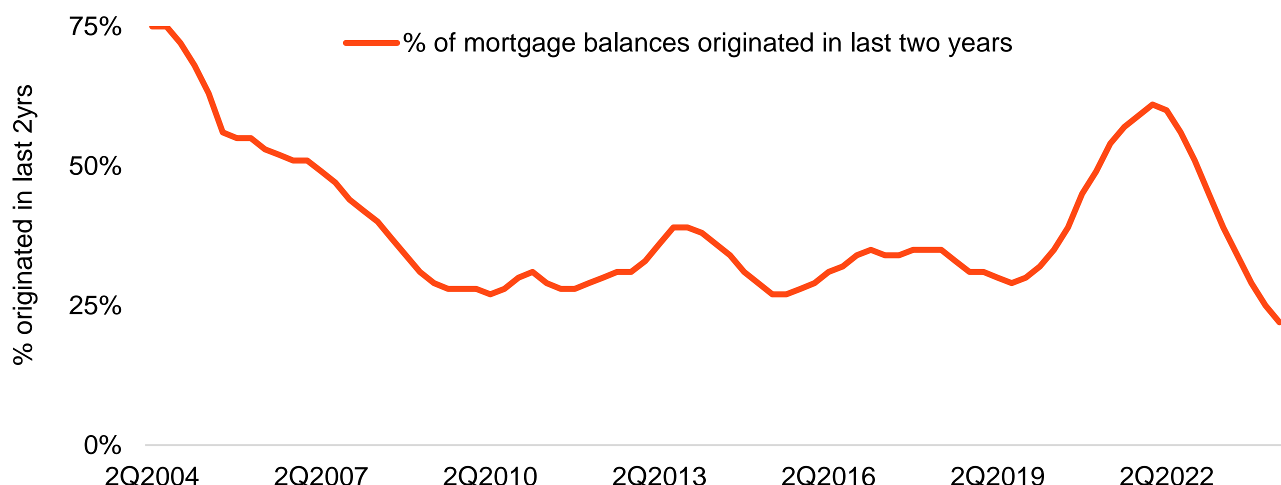
Mortgage originations, by type



Source: New York Fed Consumer Credit Panel / Equifax, authors' calculations from Mortgage Lock-In Spurs Recent HELOC Demand, BlackRock. As of 2Q2024.

Exhibit 12: The share of outstanding mortgages balance originated in the past two years reached an all-time low

Percent of outstanding mortgage balances originated in the last two years



Source: New York Fed Consumer Credit Panel / Equifax, authors' calculations from Mortgage Lock-In Spurs Recent HELOC Demand, BlackRock. As of 2Q2024.

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Some consumers are accessing home equity via HELOCs

Given the home price appreciation over the past few years, we next turn to how this value might be accessed by U.S. consumers, in order to support spending. For context, home equity lines of credit (HELOCs) are secured, and the credit limits are generally constrained relative to the home's value and the owner's equity in the home. For example, the aggregate value of the first mortgage and HELOC limit are capped at a certain percentage of the home value, typically 80 percent, according to the NY Federal Reserve.

Another factor influencing the availability (and size) of a HELOC is the homeowner's access to credit, which is informed by factors such as their credit score and current bank lending standards. While access to HELOC credit has skewed toward higher quality borrowers for much of the last two decades, disruptions in the regional banking system in March 2023 have historically led to even tighter consumer bank lending standards (as represented by data from the Senior Loan Officer Opinion Survey (SLOOS); Exhibit 13).

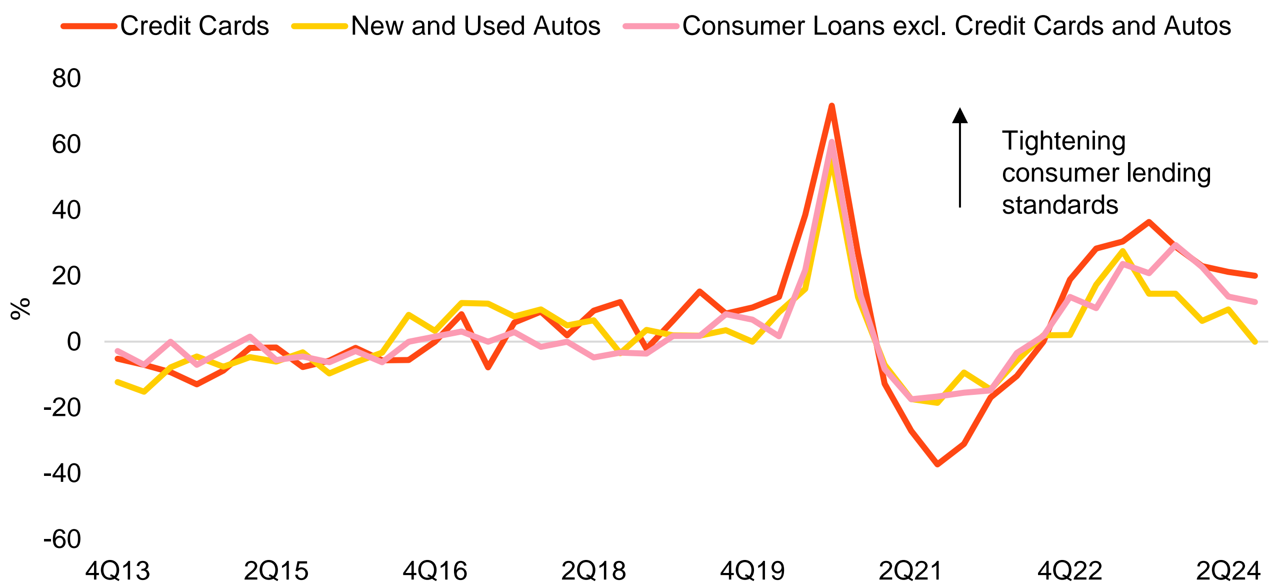
These tighter bank lending standards have, in turn, accentuated the concentration on higher quality borrowers (Exhibit 14). For example, from 2003-2007, borrowers with credit scores of less than 620 and 620-759 received, on average, 2.5% and 43.1% of total aggregate credit limits, respectively. However, in the period following the global financial crisis (from 1H2010 to 1H2024), the share of credit extended for these borrowing groups fell by over 50%, to an average of 1.1% and 19.9% of total aggregate credit limits, respectively.

A similar (albeit, less material) shift ensued following the regional banking disruption in 2023. Indeed, the share of HELOC credit limits for the two lowest rated cohorts fell further, to only 0.8% and 18.5%, respectively, while the share of HELOC credit limits to borrowers in the highest credit score cohort increased further, to 80.7%.

Today, borrowers are using HELOCs as a tool to access liquidity in their home's equity without losing their low mortgage rates. As such, balances of HELOCs have increased 20% since 2021 but remain low relative to the historical dataset (Exhibit 15). Notably, HELOC issuance concentration among high-quality borrowers emphasizes further consumer bifurcation – those who own homes have enjoyed growth in equity and can now access additional liquidity because of it.

Exhibit 13: U.S. bank lending standards for some consumer loans are still tightening, on net

Net percentage of domestic respondents to the July 2024 Senior Loan Officer Opinion Survey (SLOOS) tightening standards on consumer loans



Source: BlackRock, Board of Governors of the Federal Reserve System. July 2024 SLOOS was released on August 5, 2024.

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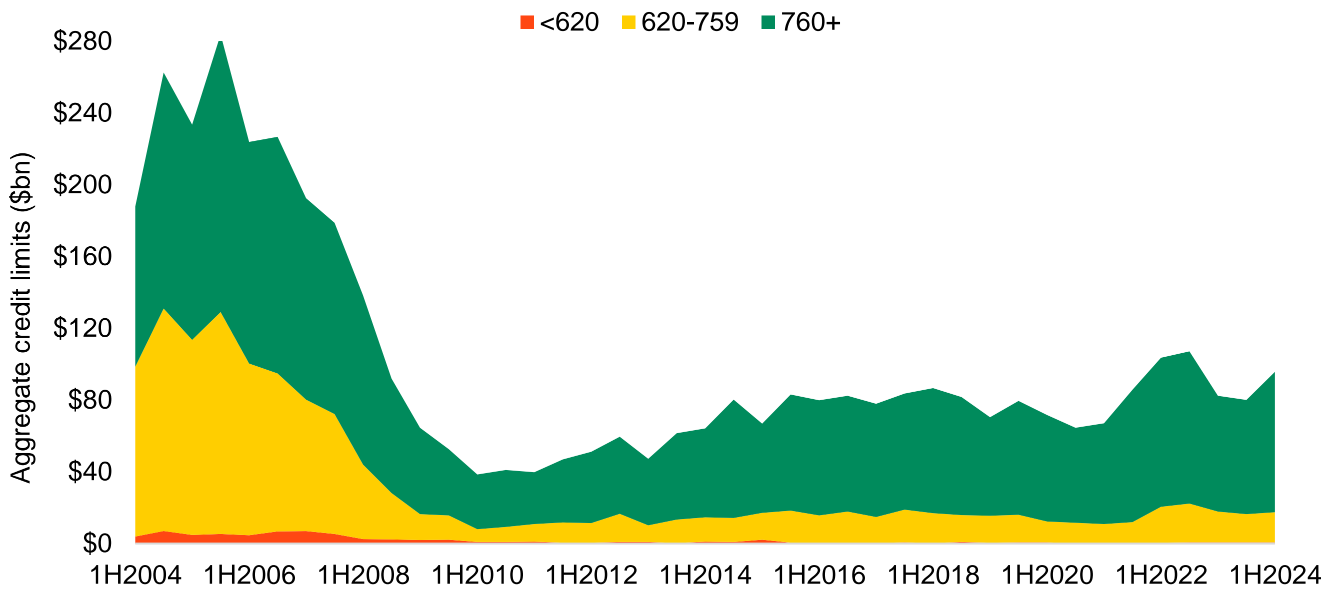
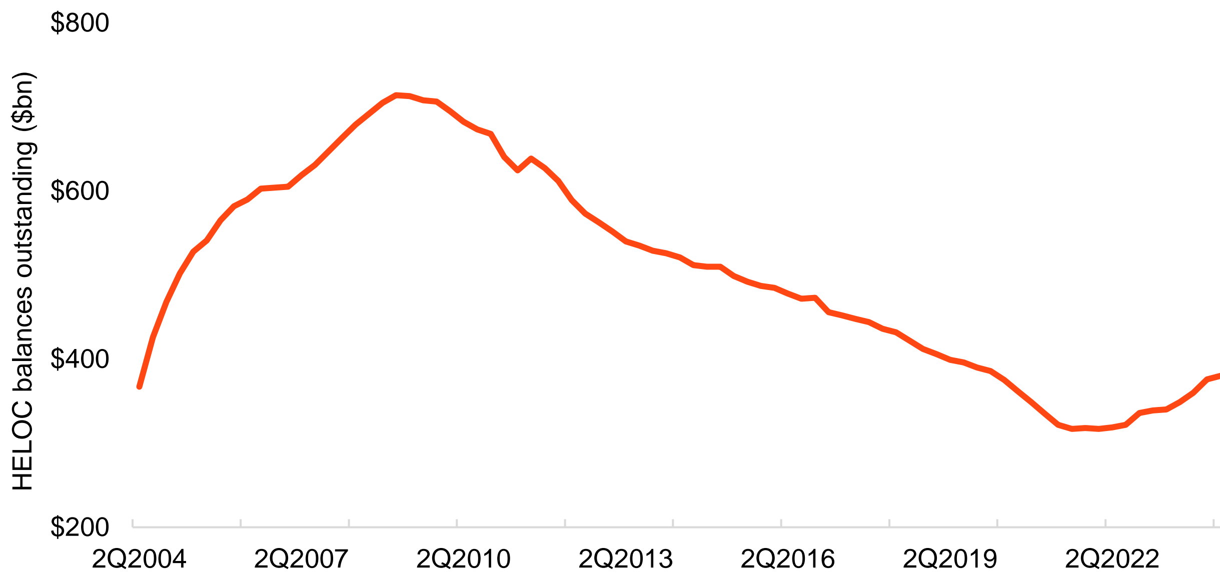
Exhibit 14: The majority of the aggregate value in HELOC credit limits is issued to high-quality borrowers
Aggregate credit limits of newly opened HELOC lines by credit score at origination



Source: New York Fed Consumer Credit Panel / Equifax, authors' calculations from Mortgage Lock-In Spurs Recent HELOC Demand, BlackRock. As of 2Q2024.

Exhibit 15: Balances on HELOCs have increased by 20 percent since 2021
Aggregate balances on home equity lines of credit (HELOC), in billions



Source: New York Fed Consumer Credit Panel / Equifax, BlackRock. As of 2Q2024.

Exhibit 16: Certain consumer-focused sectors are somewhat underperforming QTD
Quarter-to-date (QTD), year-to-date (YTD), and first half of 2024 (1H2024) total returns by sector for the Bloomberg USD Corporate High Yield Bond Index

	Total QTD index return (%)	Total YTD index return (%)	Total 1H2024 index return (%)
USD HY Index	5.1	7.8	3.0
	Total QTD return by sector (%)	**Total YTD return by sector (%)**	**Total 1H2024 return by sector (%)**
Wirelines	16.1	14.8	-0.8
Cable Satellite	10.2	4.9	-4.1
Pharmaceuticals	8.3	20.2	11.4
Healthcare REITs	8.1	13.6	5.8
Office REITs	8.0	5.4	-2.2
Natural Gas	7.2	7.7	0.8
Wireless	6.8	0.5	-5.2
Media Entertainment	6.5	4.3	-1.7
Tobacco	6.0	12.5	6.3
Technology	5.8	9.0	3.7
Healthcare	5.5	10.2	5.1
Health Insurance	5.5	6.9	1.6
Transportation Services	5.4	7.4	2.5
Consumer Products	5.0	7.6	2.8
Electric	4.9	6.9	2.3
Life	4.9	10.9	5.9
Banking	4.9	8.4	3.8
Home Construction	4.8	7.9	3.2
Consumer Cyc Services	4.6	7.6	3.3
Packaging	4.6	6.3	2.0
Other Financial	4.5	10.0	5.6
Other REITs	4.5	7.5	3.3
Finance Companies	4.5	8.0	3.7
Building Materials	4.4	7.6	3.4
Retail REITs	4.4	9.8	5.2
Food and Beverage	4.2	7.4	3.7
Restaurants	4.2	6.3	2.8
P&C	4.1	6.6	2.5
Environmental	4.1	7.7	4.1
Retailers	4.1	10.7	7.2
Brokerage, Asset Mgrs., Exchanges	3.8	9.0	5.1
Leisure	3.8	7.8	4.2
Airlines	3.8	7.3	4.0
Chemicals	3.8	7.8	4.3
Diversified Manufacturing	3.7	7.7	4.2
Metals and Mining	3.7	6.7	3.1
Lodging	3.6	6.4	3.2
Supermarkets	3.6	5.7	2.5
Midstream	3.4	7.5	4.4
Gaming	3.4	6.9	3.3
Aerospace/Defense	3.3	7.0	4.0
Paper	3.3	8.8	5.8
Construction Machinery	3.3	5.1	2.2
Refining	3.3	6.7	3.3
Other Industrial	3.1	7.9	4.8
Automotive	2.8	6.1	3.6
Independent	2.8	7.4	4.7
Oil Field Services	2.7	7.2	4.6
Railroads	0.8	-0.7	-1.5

Source: Bloomberg, BlackRock. As of September 25, 2024. **The figures shown relate to past performance. Past performance is not a reliable indicator of current or future results.** Index performance returns do not reflect any management fees, transaction costs, or expenses. Indices are unmanaged and one cannot invest directly in an index.

Unless otherwise stated, all reference to $ are in USD.

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