Governor Martha Seger
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I appreciate very much this opportunity to address your 45th Annual Credit Conference. Any organization that has been in business for 45 years must be providing something valuable to its members. The number of you here today attests to the strength of your organization. Very soon the Nation will be celebrating National Consumers Week, and sometimes there is a tendency to forget that we're all consumers -- including you credit grantors. The slogan for this year's National Consumers Week is "Consumers Buy Service." Certainly it appears that the service you've received from the association has kept you, as its consumers, "buying." I congratulate you on having such a longstanding vital group.

As indicated by your nice introduction, one of my responsibilities is for oversight of the Board's consumer credit rules -- which implement a number of federal laws like Truth in Lending. In order to help us administer them better, the Board has a 30-member Consumer Advisory Council. It's composed of representatives of industry, consumer groups, local government, and academics. Over the years we've been fortunate to have a number of distinguished representatives of your industry -- and indeed your organization -- on our Council. Ted Spurlock from Penny's was recently a member. We're looking forward to having Ralph Spurgin from The Limited Credit Services join us this year.

Since you´re the people who see, first hand, the burden of government regulations, and hopefully sometimes their benefit, we value very highly your input to the Federal Reserve Board´s work -- particularly on such responsibilities as administering Truth in Lending, the Equal Credit Opportunity Act, and the Fair Credit Billing Act.

I´d also like to thank Don Badders, not only for this invitation, but for his trips to the Board over the years to talk about your industry with our staff -- first as a representative of TRW on credit reporting, and more recently as President of the National Foundation for Consumer Credit on the Consumer Credit Counseling Services. We always welcome input like that, and Don has been more than willing to provide the kind of education that´s so necessary if we are to do our jobs adequately.

Let me first turn to the level of consumer debt. Once again this issue received a good deal of public attention recently when it was reported that such debt rose at a relatively strong annual rate of about 10-1/2 percent in January. In order to put this number in some perspective, I´d like to review, briefly, the pattern of growth in consumer credit.

Consumer credit expanded rapidly after the Second World War until the 1950s. This was stimulated by the high rate of new family formation and more positive attitudes about debt than in the prewar period. In addition, there was a good deal of pent up demand, and creditors liberalized their credit terms. During this period annual increases often exceeded 20 percent.

For the next 20 years, the growth of consumer debt fluctuated with the economy. Then in the mid-1970s it again resumed a high rate of growth, before slowing substantially during the recessionary period from 1980 through 1982. But, by 1984 consumer debt was surging ahead at a 20 percent clip. While this was the peak of its recent annual growth, in the last five years consumer installment credit has expanded by $287 billion, and the total of installment and home mortgage debt, by $1.05 trillion. These numbers sound high, but alone they don't give a picture of the burden of such debt.

One way to measure the burden of debt is by the ratio of consumer instalment debt to disposable personal income. In 1983 that ratio began what was a virtually uninterrupted rise from 14 percent until it reached 19 percent in 1986, about where it is today. At the same time, total household debt grew at an average of about 12 percent per year, considerably faster than the growth of the economy in general. These numbers, and others, have caused a good deal of concern about the amount of consumer debt outstanding relative to income.

However, some believe that the level of indebtedness is not likely to be a serious problem. Although consumer debt has risen substantially, the increase has been about matched by the growth of total financial assets. And those assets considerably exceed liabilities. Moreover, a large part of the growth in debt is held by upper income households. In addition, changes in the manner of granting credit may give an upward bias to the figures.

Increases in the length of automobile loans, for example, and the availability of "convenience" credit -- by this I mean credit card borrowings that are paid in full each month -- may somewhat inflate indicators of debt burden.

However, I must admit I am somewhat of a pessimist when it comes to our debt burden. The household sector in fact experienced some increase in debt management problems during the fourth quarter of last year. Mortgage delinquencies rose sharply -- the first such increase in two years. Delinquency rates on consumer loans and the number of personal bankruptcies both climbed fairly steeply. Delinquencies on closed-end installment loans at banks jumped to 2.56 percent after several quarters near the midpoint of a 15-year range. The major automobile finance companies reported little change in their car loan delinquencies during the fourth quarter, but then experienced a fairly big increase in January. The number of personal bankruptcies, which rose very sharply in 1985 and 1986, the second quarter. However, quarterly increases of 6 and 3-1/2 percent during the remainder of the year have returned this series to an upward path.

And certainly there are other suggestions that the level of debt is high. For example, about 15 million households in the U.S. now pay more than 50 percent of their disposable personal income to service their debt. Many banks have had major credit card charge offs. In short, although the picture is mixed, for a considerable number of families -- particularly in parts of the U.S. suffering economic difficulties -- servicing debt has become very difficult. And all of this, of course, is occurring in a period of a strong economy. The obvious question is what happens if the economy trends down.

I'd like to turn more specifically to the bankruptcy issue where the numbers are truly alarming. For 1987 as a whole, bankruptcy filings rose 10 percent. Added to increases of 20 and 32 percent in 1985 and 1986, bankruptcies have risen 62 percent in three years. These numbers are bad enough, but unfortunately, no very satisfying explanation exists for the large increase in bankruptcies since early 1985. Since the late 1960s, bankruptcies typically have declined or risen only marginally during years of economic growth. Until 1985, double-digit rates of increase were generally restricted to periods of recession, but this is no longer the case.

Obviously, the rapid expansion in consumer debt along with some relaxation of lending standards has laid the necessary groundwork for a rise in bankruptcies. It is not clear, however, that either the volume of debt or its quality has been greatly out of line with what has been typical during past periods of economic expansion.

The regional unevenness of the economy's expansion has contributed to the rise in bankruptcies to some extent, but bankruptcies still exhibit a marked uptrend even when the troubled "oil patch" and "rust belt" states are removed from the calculations.

Bankruptcy law has undergone two major revisions in the past ten years. A major overhaul in 1979, which certainly made bankruptcy a more attractive option to troubled debtors, undoubtedly contributed to the 1980-81 surge in bankruptcies. No doubt our friends, the lawyers, contributed to this when they began to advertise how easy it was to declare bankruptcy. But amendments in 1984 served mostly to tighten provisions considered too lenient, so that the legal environment seems unlikely to have provided any additional boost to bankruptcy filings recently, other than continuing the trend started by the 1979 changes.

One troubling aspect is that the social stigma of declaring bankruptcy is probably a good deal less than in times past. That attitude is reflected in the nonpayment of student loans, where $6 billion is in default. Many schools have default rates of over 40 percent. The Wall Street Journal recently reported that at 115 schools all the students defaulted on their loans due for a first payment in 1986. But, while changing attitudes have probably imparted a general upward bias to bankruptcies over time, it is hard to attribute such a sudden and pronounced increase as begun in 1985 to this factor alone.

In the absence of a single reason to explain the rise in bankruptcies, it appears that the combination of several factors -- a somewhat larger than typical expansion of debt, the still depressed condition of some regional economies, more liberal bankruptcy law, and the greater acceptability of bankruptcy as a remedy for debt problems -- must together account for the rise. Whatever the reasons, the bankruptcy rates are a serious problem, both for you and for the bankrupt.

Well, what should one do about the high level of consumer debt and bankruptcy? Certainly passing more laws is not the answer. We have a full panoply of credit laws both at the state and federal level. One particularly good response that I know is close to your hearts -- the Consumer Credit Counseling Services set up under the National Foundation for Consumer Credit.

These organizations represent the best in American life -- private sector organizations dealing effectively with a social problem. And in this case isn't it terrific that such services can serve the mutual interest of both credit grantors and consumers. When last I knew, there were over 300 such services in large metropolitan areas serving nearly 180,000 families per year. In about half the cases families receive advice on how to work out their credit problems through better management of their budget. The other half, of course, require a more formal debt management program. And what a record these services have! The last figures I saw suggested that over $180 million had been returned to creditors through these plans, and thousands of consumers were once again current on their obligations. Isn't that a better way than bankruptcy, where the damage to the individual consumer's reputation is often underplayed? And certainly it's a better way than foreclosure, bankruptcy, and charge-off for the creditor.

Let me mention one other subject -- consumer education. That's not a new subject, I know. Your organization has been involved in it for years. But I think it's easy to underestimate the importance of such education, provided it's done properly. I'm pleased to say that one of my themes at the Federal Reserve has been consumer education that is well targeted and well designed to meet the real needs of consumers -- not just with the emphasis on regulations we in government sometimes put on such things.

When you think about it, many of the consumer laws which the Congress has enacted basically require consumer education -- whether about rates of interest, how to correct billing errors, or how to obtain your credit report. Ensuring that consumers are well informed is a goal no one should quarrel with. If so, shouldn't we all -- both the private sector and the government -- try to meet that goal through voluntary consumer education, rather than waiting for additional legislation? In short, let me encourage you to expand what I know is already a fine program of educating the American consumer about credit.

Thank you for having me. Good luck on your convention.