MARKET BRIEF

Debt Consolidation in a Rising Rate Economy

From 2020 through 2022, there was record growth for bankcard originations (reaching 21.6M in Q3 2022) and balances (totaling $931B as of Q4 2022). During this period, unsecured personal loans (UPLs) also reached historic levels for originations (5.6M — the third highest number on record after peaking the prior quarter — by Q3 2022) and balances (a new record high of $222B in Q4 2022).[1] Alongside these unprecedented card and UPL volumes, the share of UPLs used for credit card consolidation increased; roughly 54% in Q3 2022 versus pre-pandemic levels in Q3 2019.[2]

To determine whether debt consolidation loans are a worthwhile focus for lenders during uncertain times, TransUnion conducted a study guided by the following questions:

- Which consumers are leveraging UPLs for debt consolidation (“consolidators”)?
- How does consolidating debt impact credit scores?
- How do credit behavior and payment trends for consolidators compare to loans not used for consolidation?
- Do consolidators perform better or worse than non-consolidators on resulting UPLs?

To identify different types of debt consolidators, we created a definition within the study for debt consolidation.[3] We then examined the profiles, credit data and behaviors of credit card consolidators and UPL refinancers versus UPL borrowers who originated loans for other purposes. These borrower groups were compared across several metrics for UPLs originated between April 2021 and September 2022, including: changes in credit balances and bankcard utilizations, impacts on credit scores, and relative loan performance.

Key findings

- Credit card consolidators were more likely to be in prime and above risk tiers, whereas UPL refinancers and non-debt consolidators were weighted toward below prime.[4]
- Credit card consolidators showed a 57% decrease in card balance total after consolidating, but 18 months later, on average, credit card consolidators' balances returned to close to previous levels.[5]
- Regardless of risk tier at time of origination, UPL refinancers consolidated into larger and longer-term loans, resulting in higher loan payments.
- On average, credit card consolidators' credit scores increased by 18 points upon UPL origination, and continued to have a net improvement 18 months after consolidating for prime and above consumers. Meanwhile, UPL refinancers and non-debt consolidators saw minor declines in their credit scores — changes that persisted across all risk tiers at least 18 months after consolidating.[6]
- Across all risk tiers, credit card consolidators and UPL refinancers had lower incidences of serious delinquencies over time when compared to non-debt consolidators.[7]

Implications for lenders

Our study indicated debt consolidators are an attractive market for lenders as they perform better on average than consumers who are not taking steps to consolidate debt.

To effectively pursue this market, lenders can leverage credit data to identify potential borrowers likely to benefit from debt consolidation or seeking a debt consolidation loan. Additionally, lenders can leverage non-credit-based marketing data to help tailor messaging to identified prospects. When correctly applied, insights from credit and marketing data can lead to better-informed prescreen strategies, as well as stronger approaches to underwriting and marketing messaging that is more apt to resonate.

[1] TransUnion US Consumer Credit Database.

[2,3,4] TransUnion US Consumer Credit Database; Transunion research and analysis. Definition for debt consolidation: UPLs of $2,000+ that were originated alongside an aggregate bankcard balance reduction between 25-125% of the UPL loan amount, or alongside existing UPLs being paid off that in total are 25-125% of the UPL loan amount.

[3,4] VantageScore® 4.0 risk ranges: Subprime = 300–600, Near prime = 601–660, Prime = 661–720, Prime plus = 721–780, Super prime = 781+.

[5,6] The 18-month period is based on UPLs originated in April 2021 that were tracked through October 2022.

[7] Delinquencies were calculated based on consumers who originated a UPL in Q2 2021 and were ever 60+ days past due in the 16 months after the quarter of origination.

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