

## Next meltdown issue might be credit-card debt

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The housing bubble. The credit crunch. The automobile industry meltdown.

Just when you thought all of the economic dominoes had toppled, experts say another one is about ready to tip.

Consumer credit-card debt - driven by years of spend now and pay later - might be the next blow to the nation's ailing economy.

Credit repairman Walter Howe sees it every day.

"It's almost like awakening a sleeping giant," said Howe, an adviser at Diamond Capitol in Whittier.

As unemployment rises and the housing and banking crises intensify, Howe said he sees more people trying to rid themselves of unmanageable credit-card debt.

"I'm seeing a lot of people go straight to bankruptcy," he said. "I'm seeing a lot more of that."

He mentioned one client who came in a few days ago who had about a dozen credit cards and was \$16,000 in debt. Another client, also with about a dozen cards, used one to pay off the others. He had accumulated about \$38,000 in debt.

"At the end of the day, they say, 'I've just got to walk away from it,' " he said.

Begging for a bailout

The issue has consumer advocates queuing up behind banks, defaulting homeowners and automakers for a federal rescue.

A proposal by an alliance of financial

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industry interests - banks, brokerage firms, insurance agencies and consumer advocates - would have allowed as much as 40 percent of credit-card debt to be forgiven for consumers who don't qualify for existing repayment plans.

But allowing banks to defer debt wasn't an option for the Office of the Comptroller of the Currency, the agency that rejected the pilot plan Wednesday.

Still, the action demonstrated the urgency of an economic landscape in which consumer credit-card defaults are yet another wound for banks already bleeding from losses in the housing and security markets.

"Consumers built up a massive amount of debt over the past few years, because they felt rich," said economist Chris Thornberg of Beacon Economics.

Rising mutual fund and home values spurred confidence and spending on credit.

And banks obliged.

"A lot of banks lent a lot of money to a lot of people they should have never lent money to," Thornberg said.

But the risks were hidden.

Refinancing homes to pay off credit cards became difficult once home values tanked, Thornberg said. It hasn't helped that as those values tanked, ailing homeowners used their credit cards to pay bills. And since IRS rules changed in the 1980s, consumers no longer can write off credit-card interest on their taxes.

The result is that Americans are saddled by about \$900 billion in credit-card debt, according to the latest available Federal Reserve figures.

And lenders are beginning to feel the pain from defaulting credit card customers.

The largest banks, for instance, set aside between

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\$1 billion and \$3.5 billion in the third quarter for losses on credit card loans as their profits plummeted.

Credit-card charge-off rates - the extent to which banks give up on collecting debt - rose to 6.8 percent in August, up 48 percent from a year earlier, according to Moody's Investor's Service.

Store-branded cards' charge-offs reportedly rose 2.4 percentage points to 8.1 percent in the past year, reflecting the high interest of 20 percent or more that makes it harder for consumers to pay their bills, according to a report in USA Today.

American Express announced Monday that it would become a bank holding company, which would give it greater access to the Treasury's bailout money for banks.

This looks familiar

Problems with credit-card debt could very well resemble the mortgage-debt problems at the core of the nation's

woes.

"If those delinquency rates go up too much, it will be very difficult for the banks to break even," said USC professor Lars Perner, who specializes in consumer psychology.

Credit-card debt can be bought and packaged to investors in the form of securities, just like mortgages were. Those securities also can be vulnerable to defaults, said Lawrence Weinman, a Los Angeles-based financial advisor.

"As the defaults increase, you are going to have the same problem again . . . and you'll have potential problems in the financial and credit markets," Weinman said.

The result is that credit card issuers are pulling back, and so are consumers going into the holidays and beyond, experts said.

"The epic buying spree is over," said Peter Schiff, who runs Connecticut-based investment firm Euro Pacific

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Treasury officials said they hoped to invest about \$50 billion from the \$700 billion bailout fund to help companies that issue credit cards, make student loans and finance car purchases. Treasury Secretary Henry Paulson said such a plan could be enacted in a few weeks.

But the damage might already have been done, some said.

Retailers such as Mervyns and Circuit City are filing for bankruptcy, and consumers are thinking twice before they use plastic.

"It's something you can be in denial about," Perner said. "But after a while, it catches up with you."

*The Associated Press contributed to this report.*

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