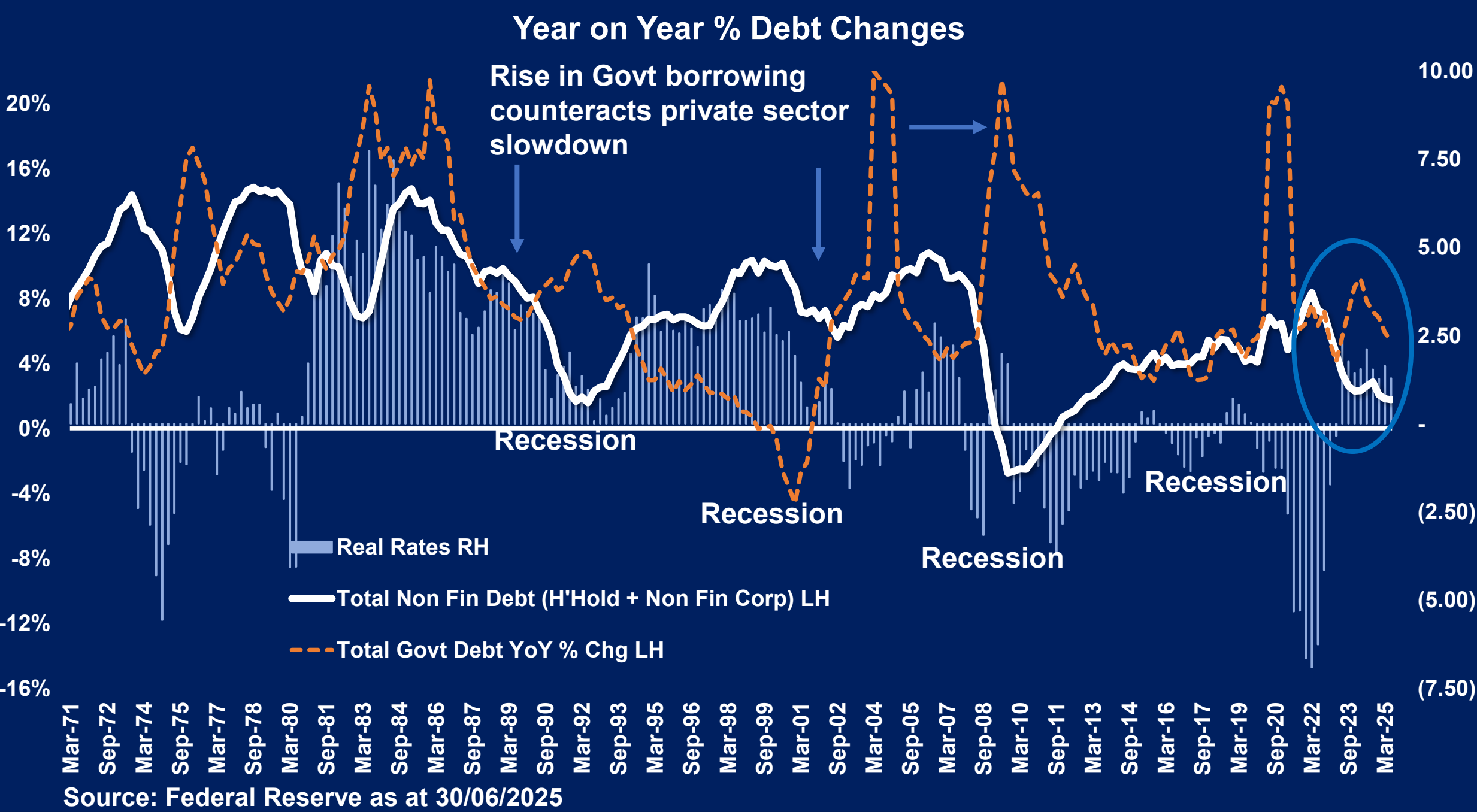


Credit Contraction

Credit growth in the US is stalling and approaching levels which in previous times have signalled recession. The classic policy response would see governments ramp up borrowing (spending) to counteract the private sector slowdown. Simple in theory perhaps less so in practice. For one, today’s fiscal deficits are already at the highest levels on record outside of recession or war. Secondly, interest rates remain problematically high for a Treasury Department desperately looking to ease the interest burden on the debt, while thirdly, stubborn inflation is contributing to a reduced appetite for long dated government bonds. A lot is therefore riding on the Fed to ease the interest rate pressure, at a time when growth does appear to be weakening but inflation remains sticky. Cut too aggressively and risk unleashing more inflation on an irate electorate who cannot afford it. Wait too long and risk a recession at a time when governments can’t afford it.



Rubrics Fixed Income Macro View

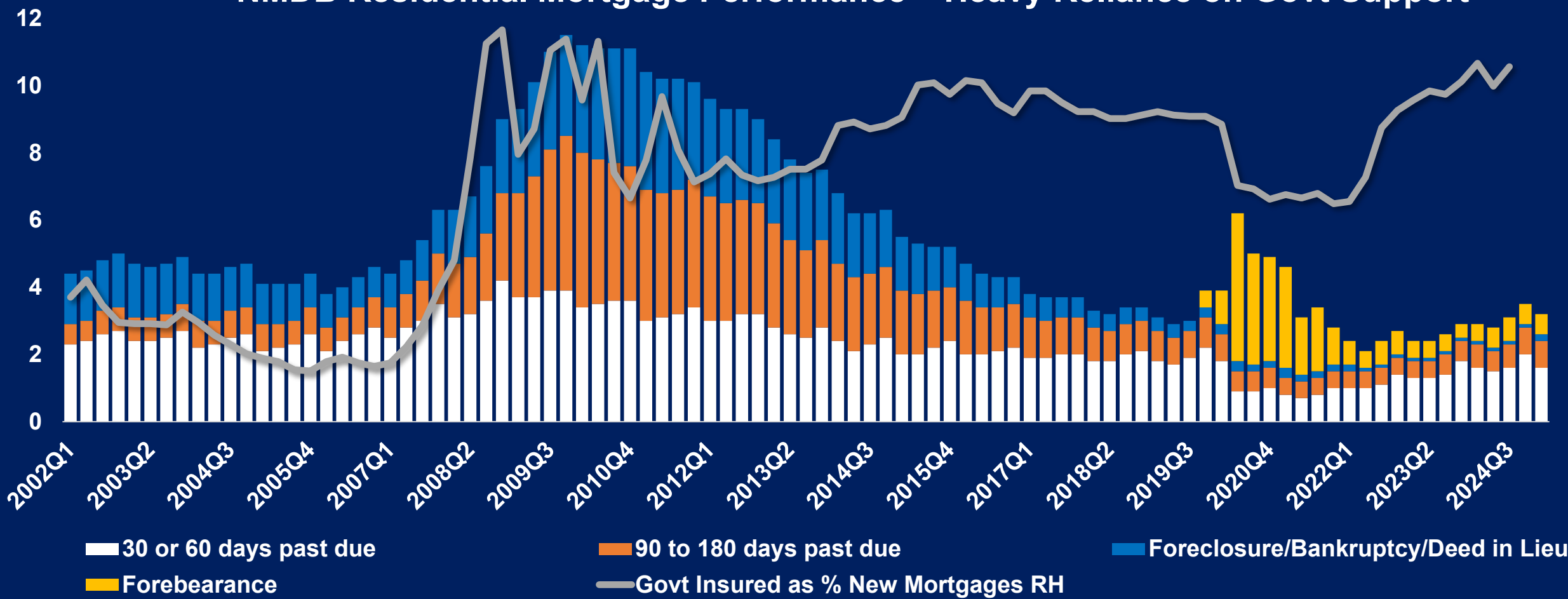
27 March 2025

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Household – Mortgages

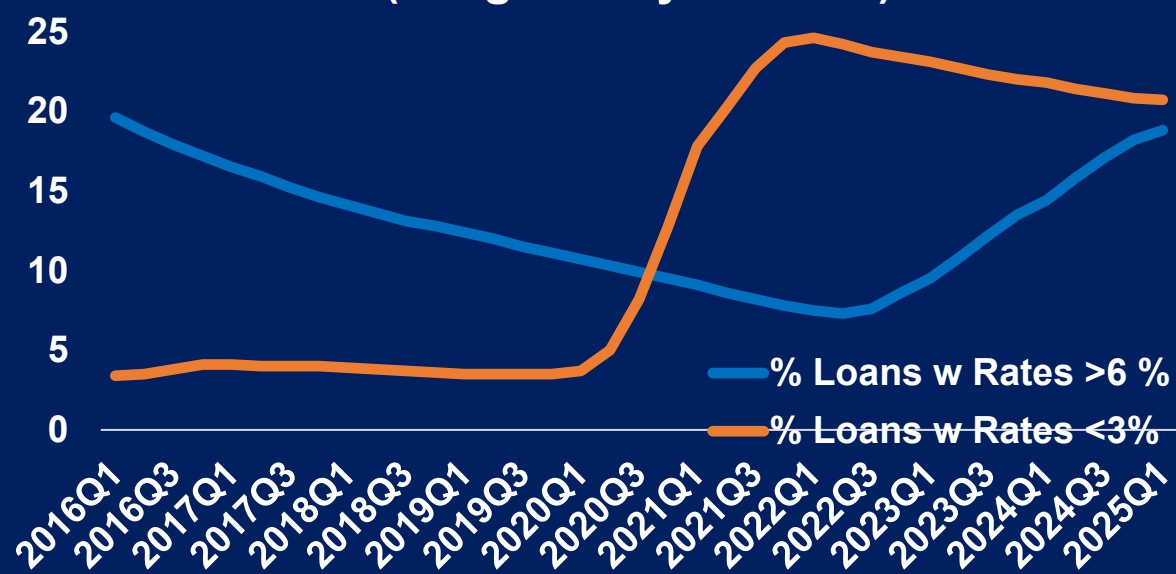
The collapse in housing affordability since the emergence of higher interest rates (along with elevated prices) has seen a corresponding decline in mortgage debt. A look underneath the surface however reveals the problems extend beyond just affordability. Of the historically low number of mortgages take out in the last few years, a record number (30%) rely on some level of government support in terms of mortgage guarantees (e.g. FHA, VA, USDA). With certain forms of relief set to expire in 2025/26 and as average rates on outstanding mortgages continue to rise, it seems a lot more than 100bps of rate cuts would be required to reignite a lending cycle.

NMDB Residential Mortgage Performance – Heavy Reliance on Govt Support



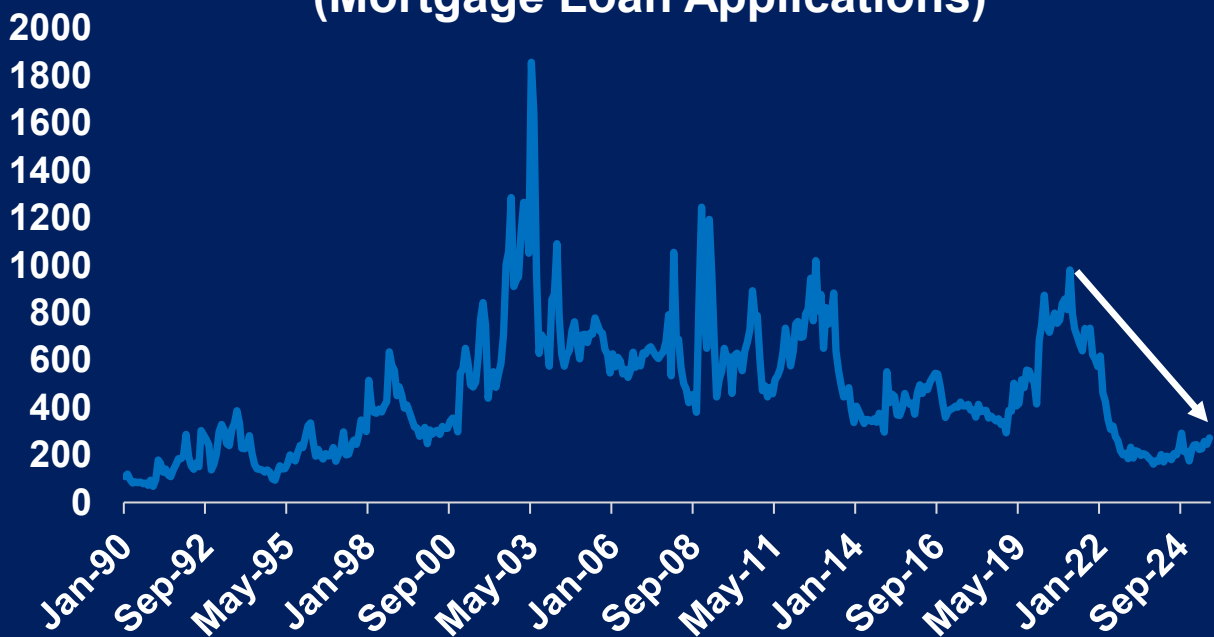
Source: FHFA as at Q1 2025

Mortgage Rate Outstanding (Weighted by # Loans)



Source: FHFA as at Q1 2025

MBA US Market Index (Mortgage Loan Applications)



Source: Bloomberg as at 31/07/25

Rubrics Fixed Income Macro View

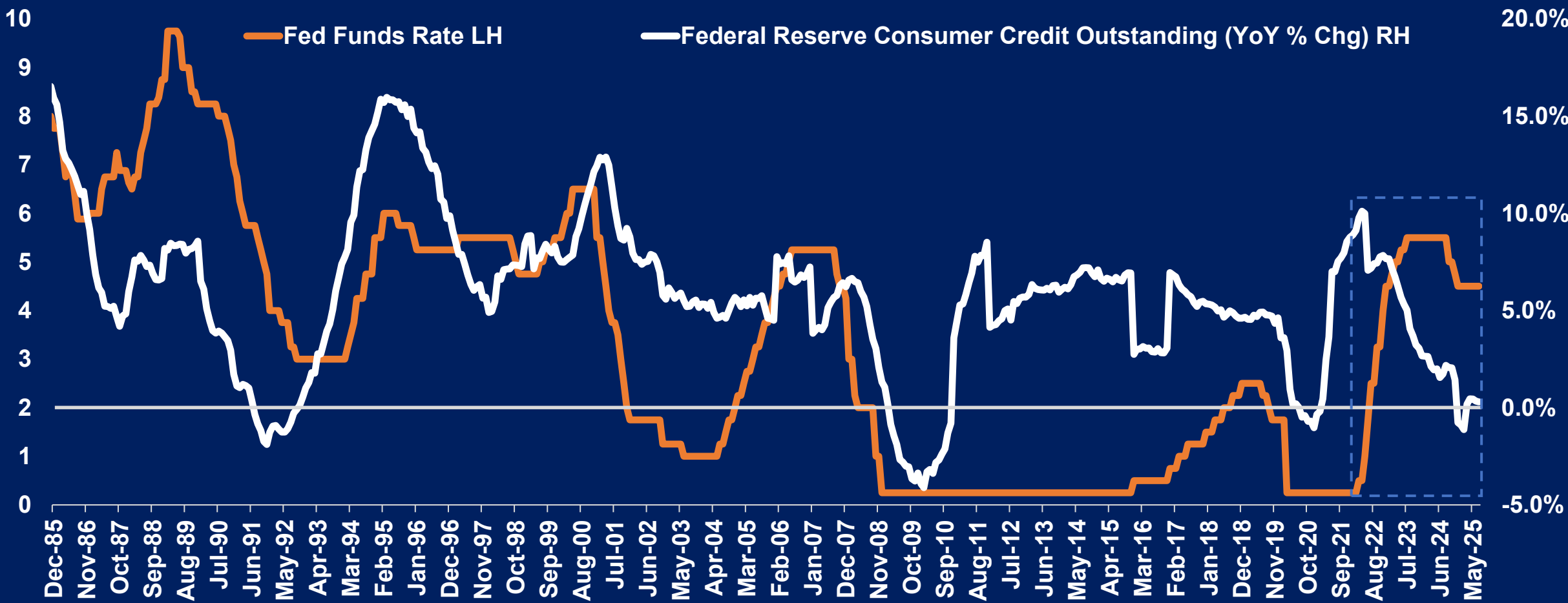
17 March 2025

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Household – Consumer Credit

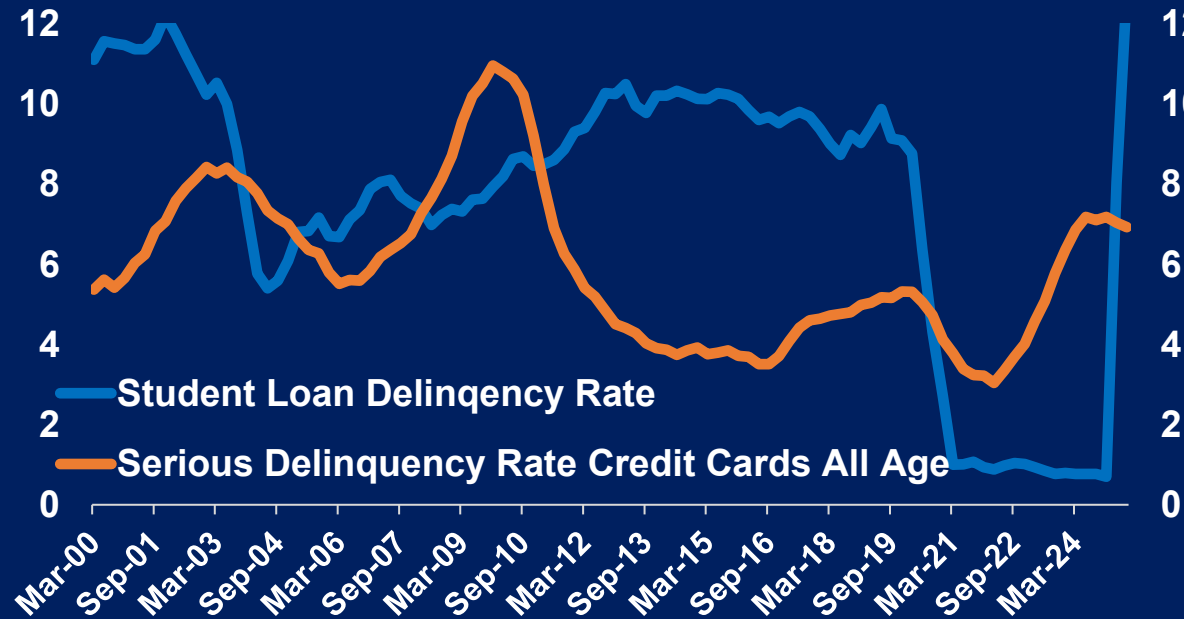
The year-on-year change in total outstanding consumer credit is approaching negative territory which once again raises question marks over the health of the consumer. With delinquencies on credit cards, auto loans and now student loans at elevated levels and showing no sign of abating, the extent to which the top 10% of earners can keep aggregate consumption moving in the right direction is highly debatable. Beyond that is the question of whether or not a consumer default cycle is extending beyond the lowest cohort of earners and if a few hundred basis points in rate cuts will be enough to stop it accelerating.

Consumer Credit Turning Negative



Source: Bloomberg as at 30/06/25

Household Debt Delinquency 90 Day+



Source: Bloomberg as at 30/06/25

Share of Spending by Top 10%

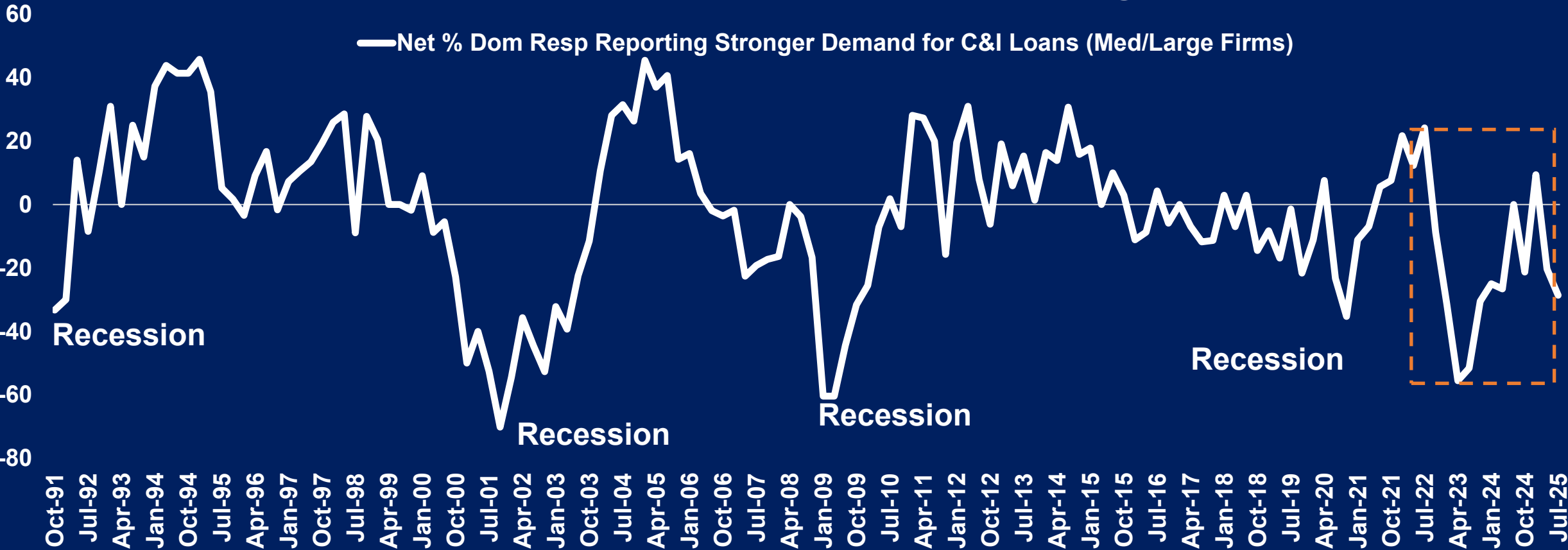


Source: Bloomberg as at 30/06/25

Corporates

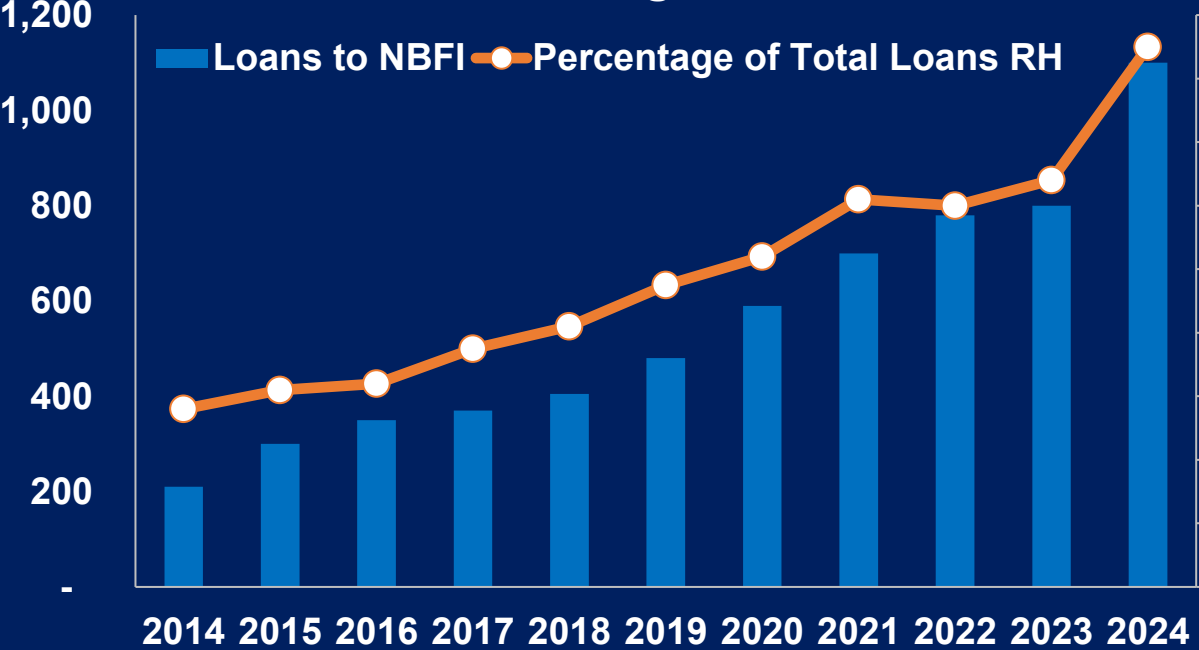
Demand for credit in the corporate sphere is also showing signs of a sizeable slowdown. One clear exception to this is Private Credit, where capital continues to flow both directly from institutional investors (e.g. insurance companies) and indirectly from banks. As assets continue to grow, the trend in funding has shifted away from LBO/MBO financing and towards Refinancing and Dividend Recapitalisation reflective perhaps of a decline in new lending opportunities. Alongside this indications are that stress in the asset class continues to build, with PIK financing for example representing an increasing share of overall deals. The fact that banks have increased their exposure has added an additional layer of systemic risk – something the Fed would be foolish to ignore.

Demand for Corporate Credit Slowing



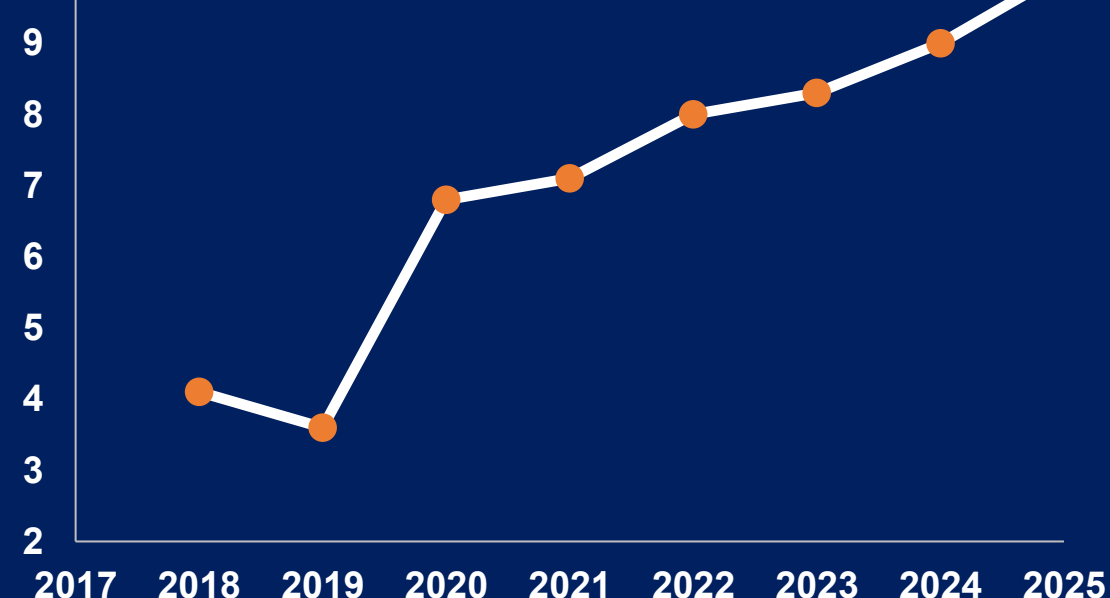
Source: Bloomberg as at 31/08/25

Bank Lending to NBFIs



Source: S&P Global as at 31/12/24

Private Credit - PIK Interest as % Total Income



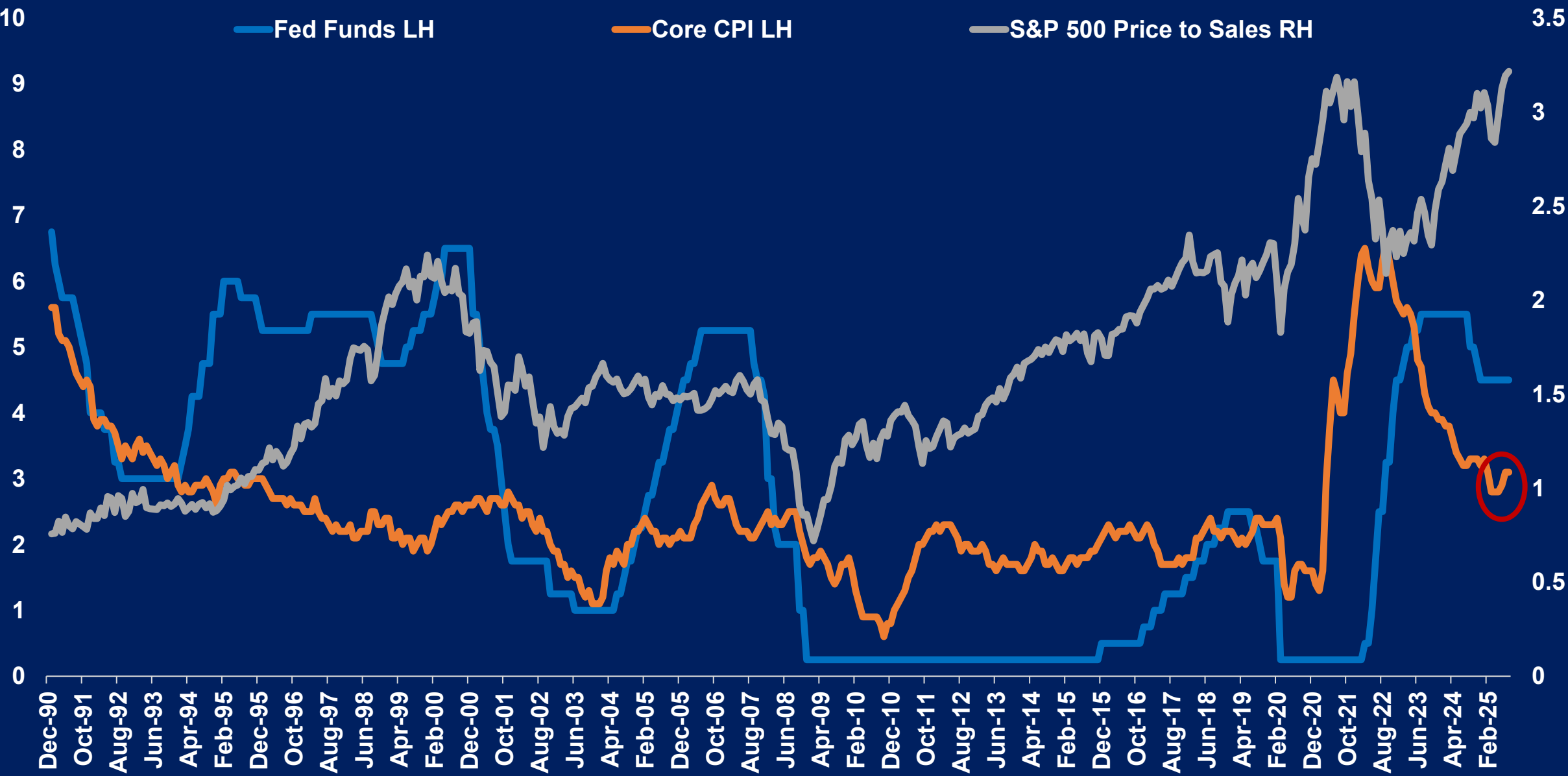
Source: Fitch as at 30/06/25



Bottom Line

Demand for credit at current interest rates is contracting to the point where continued growth momentum must be under threat. While the Federal Reserve will not doubt be conscious of this, they would also be well advised to recognise that inflation remains well above target and trending in the wrong direction. You have to go back nearly 30 years to find an instance of the Fed cutting with core inflation on or around current levels (excluding last year) while to say financial markets are exuberant feels like an understatement. It does seem therefore they are in a no-win situation – overly dovish signalling risks the wrath of the bond market but acting too late risks a possible credit crunch. If the latter will a few hundred basis points of rate cuts be enough to unlock the credit malaise or will something far more drastic be needed?

Fed Funds Rate vs CPI and S&P 500



Source: Bloomberg as at 31/08/25



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