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SFA Research Corner

When the Small Tail Wags the Large Dog: Looking Beneath the Consumer Credit Headlines

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At the center of today's structured finance market is a critical paradox: macro-level economic indicators show a remarkably resilient U.S. consumer, yet portfolio-level credit performance reveals deep patches of stress. For ABS and RMBS investors, relying on headline averages has become a distinct risk. Credit performance is no longer a story of broad economic health, but one of extreme concentration—a dynamic where a relatively small, highly stressed cohort of borrowers is dictating overall performance trends.

To look beneath the headlines, the SFA Research Corner sat down with Vadim Verkhoglyad, Chief Economist at dv01, following his presentation at SFA's 2026 Research Symposium. In this interview, Verkhoglyad breaks down the "three S's" of consumer behavior, explains why a small "tail" is wagging the broader credit dog, and identifies the new, underappreciated variables—from localized property insurance spikes to shifts in unsecured debt consolidation—that are reshaping risk analysis today.

The Average vs. the Distribution

1. One of the symposium's central takeaways was that the American consumer appears relatively healthy overall, even as some groups face real financial pressure. Who is feeling that pressure most, and how should we think about the size and significance of those groups?

I would say the most acute pressure is in very predictable segments that are nonetheless significant. Those include:

1. People with no FICO scores or those who are undocumented. There's ample evidence that credit to this cohort has been functionally cut off, so to the extent they are struggling to make ends meet, the avenues that were available for them two years ago are not.
2. Lower-credit borrowers—not to be confused with lower income, though there is clearly correlation. Credit tiering has been the most important differentiator of behavior post-2022.
3. Homeowners facing a surge in insurance premiums. They have certainly gone up nationally, but there are local pockets where insurance premiums have tripled or more over the past five to six years. In that scenario, the fundamental cost of homeownership may come into question even if the homeowner doesn't have a mortgage.
4. Goes without saying, but anyone at near-prime or lower FICO scores that is also experiencing cash-flow shortages.

2. At the symposium, you described this dynamic as a smaller "tail wagging a much larger dog." What does that tell us about the financial health of today's consumer?

Every sector today faces a form of concentration problems, where a huge portion of their defaults are concentrated in weaker attributes.

For instance, the TransUnion monthly report shows that north of 85% of serious delinquencies in credit cards are in the near-prime or below credit scores. This is slightly misleading because they are using updated credit scores, so of course someone seriously delinquent will have a terrible credit score.

However, even using original FICO, we see similar behavior across sectors. In the mortgage market writ large, over 60% of delinquency growth over the past year has occurred in either the FHA or Non-QM space, while both sectors account for less than 25% of total combined originations.

In auto, the problem of subprime delinquencies is ever present, with subprime auto delinquencies accounting for well over two-thirds of all auto delinquencies—with a very wide range depending on how you determine what subprime is—but just 25% of volumes.

Notably, this tail-wagging issue isn't just about credit performance, but increasingly about volumes as well. Less publicized is the fact that student debt, when including unpaid interest, has a massive skew of balance concentration—more than any other sector including mortgages. Fifty-three percent of student debt is held by just 14% of borrowers (those who owe more than $80,000 including unpaid interest), with a staggering 21% of all debt held by the 2.5% of borrowers who owe over $200,000.

3. Within that smaller tail, where do you see the most acute or potentially underappreciated pressure?

I think it's the same four categories I mentioned in question 1. The two most acute ones to me are undocumented borrowers and those with spiking insurance premiums.

Mainly because the other two categories aren't new; this is basic credit underwriting. However, these two are only a few years old, and households have certainly not adapted. For the undocumented borrowers, they are facing unprecedented changes in their lifestyle. For the higher insurance premiums, this is very much a slow-bleed situation until it isn't.

4. Familiar measures such as FICO scores, income levels and headline delinquency rates may not tell the full story. What might investors miss if they rely too heavily on those traditional indicators?

Excellent point. Post-GFC lending, particularly in more fintech-enabled lender-focused space, has significantly expanded the available credit metrics for investors to evaluate through a number of methods. From bank verification to exposing more of the credit report, investors can effectively re-underwrite FICO, achieving a granularity that was largely unheard of from an investor standpoint 10 years ago.

Today the analytical focus has shifted from just a credit snapshot to really a full engagement with the borrower—which is why so many fintech lenders have gone public, embraced bank charters, or expanded their footprint. The golden goose for everyone is underwriting to true free cash flow and being top of borrower wallet for both repayment and future needs.

This isn't new. In many ways, this is the pre-1980s traditional bank underwriting model, except existing entirely digitally and without personal relationships, and with a different entity wearing the ultimate risk versus the one that underwrote the loan.

What lenders and investors alike are trying to understand, beyond credit score, is:

1. True free cash flows today
2. Future borrowing needs and propensity to re-leverage in times of stress
3. Ability to retain the borrower after the first loan or dealing with a permanent refinancer.

What gets missed by relying on just basic credit scores—FICO or Vantage—is thinking they are the only indicators of a borrower's willingness to pay. They're not.

During the GFC, we learned how critical LTV and negative equity position were to borrower sentiment. LTV became a willingness-to-pay attribute. We're seeing the same factor play out in subprime auto today, with performance differences across LTV buckets looking staggeringly different today than even two to three years ago. Lenders have been slow to re-adjust pricing accordingly, to their own detriment.

What Borrower Behavior Is Telling Us

5. You offered a behavioral way of thinking about affordability: Can households maintain their standard of living without taking on more debt? What does that perspective tell us, particularly in a K-shaped economy?

This is one of the crux questions as it relates to a possible K-shaped economy because it calls into question what K-shaped is. I've argued that measuring household behavior is a function of the three S's of household behavior—Spending, Saving, and Sentiment.

For the Spending section, the K-shape is unquestionable; it's absolutely driven by higher-income and/or older households. This spending pattern is also mimicked in Sentiment (except that it seems nearly every household, rich or poor, is experiencing negative sentiment). If that's where we end the discussion, we can accept the K-shape.

However, on the savings portion, multiple data sources suggest the K-shape is entirely absent. Savings rates among lower and middle incomes have only grown over the past four years, despite multi-decade-high inflation, economic uncertainty, and even categorical understatement of financial strength in source data.

Moreover, the segment that would represent the most acute sign of "spending beyond means"—meaning non-mortgage consumer borrowing—has been even slower, or in 2025/2026 outright negative on a nominal basis (and deeply negative on a real basis).

Moreover, it's worth looking at what households are actually spending their money on. In this regard, household spending for decades has shifted away from discretionary to necessity spending. At the moment, by some measures, 80–90% of total household spending is in the necessity category, up substantially from historical trends, and the portion has only grown more in recent years.

This is a long answer, but it's a very nuanced issue. In our minds, households can absolutely afford their current lifestyles because we haven't seen them exhibit any evidence of borrowing in order to deal with the recent spate of inflation.

6. Lower-income consumers have reduced their debt considerably since the pandemic. How can we distinguish healthy deleveraging from something less positive, such as reduced access to credit?

Excellent question. There are a few ways we can assert this.

First, the only other time we've seen a decline of this magnitude was during the GFC. At that time, charge-offs and reduced credit access WERE the story; they weren't part of it. This is reflected in numerous sources—credit card charge-offs, but even more visibly, the tail end of the Federal Reserve report shows the number of accounts in collections. That's your weakest loans because they've already been charged off and are sitting with collection agencies.

We feel extremely confident that today's deleveraging is primarily voluntary rather than involuntary. The Federal Reserve charts show that, pre-GFC, 8–10% of consumers had an account in collections. That rose considerably post-GFC, peaking at 14.6% in 2013.

Today's rate is 4.9%, half the pre-GFC figure and 66% lower than GFC levels—and only slightly above the record low of 4.6% in 2024. For another illustration, the ICE Mortgage Monitor shows aggregate mortgage delinquencies are barely above their record lows of 2024, and still 30% below pre-GFC levels.

Lastly, there are some ancillary metrics you can look at to show that even the absolutely most vulnerable segments of the population on an income level are showing material improvement as well.

The FDIC publishes a study showing the percentage of households considered unbanked or underbanked. That ratio has been going progressively down over the past 15 years, a process that really accelerated post-COVID. For context, the state with the highest portion of unbanked people (Mississippi) today has an unbanked rate less than that of the AVERAGE state 10 years ago.

Another illustration is that the past five years have NOT seen rapid growth in high-cost credit—payday/pawn/title, etc.

There's also no evidence of any material credit tightening, especially post-2023. The aforementioned decrease in No-FICO lending has entirely shifted into subprime lending (which is weaker credit than No-FICO borrowers, as performance data suggests), so that decline wasn't credit-driven but politically driven.

We're seeing more and more credit channels becoming available. But most importantly, all the traditional metrics of credit capacity are at basically their best levels EVER, but people are just not taking on more debt.

7. Unsecured consumer loans are increasingly being used to consolidate credit card debt and lower monthly payments. What can subsequent performance tell us about whether borrowers are finding lasting relief—or simply creating room to borrow again?

Unfortunately, observing borrower behavior post-debt consolidation is difficult, if not impossible, directly. However, we can see signs of this behavior in the debt itself.

Remember that consolidation loans are fully unsecured, and are usually the first priority of default if borrowers are under stress. If there was evidence of borrowers massively re-leveraging after paying down the credit card debt, you would see really high delinquency rates 1–6 months—in the case of pure fraud or extremely spurious borrowers—or 6–18 months in the case of highly levered borrowers that really can't resolve their financial circumstances.

This is the opposite of what we've seen in consumer unsecured over the past three years. Since Q3 2023, the sector has seen improving performance at a scale unprecedented in its history. The improvement is such that it went from by far its worst performance in history in late 2023 to today seeing record highs for metrics like curing and new delinquencies, and trending well below historical comps for charge-offs.

That behavior really tells us the consolidation IS having the desired effect, a trend reinforced by the origination trends over the past two years.

Credit card went into a strong period of declining growth starting in late 2024—with outright negative NOMINAL growth (deeply negative adjusted for inflation) for the bottom- and middle-income cohorts.

At the same time, the debt-consolidation unsecured space posted record after record of volumes, crossing the $5 billion monthly threshold in 2025, and an astounding $7+ billion in monthly volumes in June/July of this year.

What Would Change the Story?

8. Today's stress appears concentrated rather than systemic. What changes in borrower behavior would tell you that the story is becoming broader—and what should investors be watching most closely?

In order to see it at the magnitude where it becomes a systemic rather than isolated problem—I would argue 2022 was an isolated problem, specifically around certain types of problematic lending rather than aggregate consumer debt problems. We'd look for the following:

- Rapid non-mortgage credit growth
- Most of that growth happening outside of the top two income cohorts—the exact opposite of the post-COVID behavior, where more than 90% of consumer credit has gone to these top two cohorts
- Rapid growth in either new, unproven forms of credit, or particularly expensive forms of credit—notably payday loans, title, etc.
- An extreme loosening of credit standards in traditional products—mortgages, credit cards, unsecured, etc.—in order to keep up growth and not cede market share to new entrants.

Verkhoglyad's insights point to a more nuanced consumer credit picture. Measures including lower consumer borrowing, historically low levels of accounts in collections and improving performance in unsecured debt consolidation suggest continued resilience, even as financial pressure remains concentrated among certain borrowers and credit segments. For structured finance market participants, this may mean that it has become increasingly important to look beyond aggregate measures and traditional credit scores. More granular measures of borrower cash flow, leverage and localized risks can provide additional context for understanding where stress is emerging. The question is not simply whether consumer credit deteriorates, but where that deterioration occurs, how concentrated it remains, and whether isolated pockets of stress begin to broaden.