Who took on all that debt?

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The US financial crisis of 2007/2008 would not have happened without the large scale increase of mortgage borrowing by US private households. The first step in understanding this accumulation of debt is to understand which parts of the population were behind this aggregate trend. Several narratives exist in the literature. First, some authors argue it was the lower end of the income distribution which was driven into debt in order to maintain current living standards in face of stagnant or even declining real incomes (Barba and Pivetti, 2009; Kumhof and Ranciere, 2010). Second, there is the idea that the upper part of the income distribution which did not benefit from the surge in top incomes borrowed heavily in order to protect their perceived social status which is determined by their ability to spend ('keeping up with the Joneses') (Frank et al., 2014; Kapeller and Schütz, 2014; Belabed et al., 2013). Third, borrowing heavily depends on rising asset prices and the availability of collateral (Ryoo, 2015). If that were the case borrowing should be broadly distributed across the population. Only those households at the bottom of the income distribution, those unable to accumulate any wealth, should not have participated in the collective borrowing spree. While a traditional class analysis which distinguishes based on the ownership of capital is not particular useful for assessing to what extent these explanations are compatible with the data, the distribution of income needs to be taken into account for an macroeconomic analysis of the pre-crisis period. Being able to distinguish between the outlined hypotheses is important because each of them leads to substantially different policy conclusions. If borrowing was concentrated towards the upper end of the income distribution and triggered by rapidly growing top incomes and status driven expenditures, increasing the progressivity of the tax system would limit the intensity of such borrowing cascades in the future. In contrast if the lower part of the distribution borrowed in order to maintain living standards, the policy focus should be on improving the earnings perspectives of low income households. Finally if asset prices and most likely real estate prices played the key role, boosting housing supply in order to keep price rallies in check should be a policy priority.

This paper aims at shading light at the question which parts of the US household sector were responsible for the spectacular increase in household debt prior to 2007 by using a high quality dataset on income and balance sheet information of US households, the Survey of Consumer Finances (SCF). The distinguishing feature of the SCF is its use of tax information for designing the sample. This means the SCF is the only US household survey which convincingly deals with the problem of underrepresentation of rich households in conventional surveys (Eckerstorfer et al., 2015; Vermeulen, 2014) and thus is the most reliable source of information about the distribution of income and wealth apart from administrative data. In addition it provides a highly detailed picture of the household balance sheet and distinguishes between several different forms of assets and liabilities. By relying on data from the SCF this paper is the first to the author's knowledge to provide an in detail descriptive analysis of US household borrowing behaviour prior to the financial crisis and by doing so demonstrates that the distribution of income is essential for a macroeconomic analysis of the causes of the US financial crisis.

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