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THE QUALITY OF CONSUMER INSTALMENT CREDIT

GEOFFREY H. MOORE
NATIONAL BUREAU OF ECONOMIC RESEARCH

AND

PHILIP A. KLEIN
THE PENNSYLVANIA STATE UNIVERSITY AND
NATIONAL BUREAU OF ECONOMIC RESEARCH



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THE QUALITY OF
CONSUMER INSTALMENT CREDIT

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Authors of empirical studies are perpetually dissatisfied with the state of the data on which they must base their findings. Always they long for material with which to test new relationships of possible importance, in the hope of being able to produce a definitive solution to whatever problem they are examining. It was this hope which persuaded us to wait until now to present our findings, though we realize that there are still important gaps in our knowledge, the filling in of which must await data not now available.

We have incurred obligations of many kinds and to many persons and institutions in the process of obtaining and analyzing the data for this study. We are indebted, first of all, to those who assisted in the preparation of the 1956 paper, and to whom we there expressed our thanks. We are especially indebted to our coauthor in that initial endeavor, Thomas R. Atkinson. Not only are many of his original insights still to be found in the pages which follow but also he was kind enough to read an early version of the present manuscript and to make many helpful suggestions.

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P. A. K.

Foreword

I feel unduly honored to be asked to provide a brief foreword to this volume, placing it in its context within the National Bureau's quality of credit program as a whole. Its authors, and especially Geoffrey Moore, have had much more to do with the design of that program than I, and their study of consumer instalment credit was well under way before I became director of the program. I played a very small role in the design and execution of this study.

Nevertheless, it has special importance, and I should like to stress its contributions. The credit quality program has had several objectives. It sought first of all to effect improvements in the data relating to credit quality, which earlier National Bureau studies had shown were seriously inadequate. Second, it sought to devise methods by which "quality" could be quantified, so that "credit quality" could be measured statistically. Third, it sought to analyze the relationships between changing credit quality and business cycles, and to assess the significance of the changes that have occurred since World War II.

The several studies that have constituted the credit quality program—three have been issued and a half-dozen are under way—should be seen as building blocks designed in combination to work toward these objectives.¹ But the present volume deserves special mention for its contributions to the data and to methods of analyzing them, as well as because of the importance of the credit sector that it investigates.

The months and indeed years of work the authors devoted to collecting the statistics set forth in their study have in fact resulted in

¹ The published reports are by Albert M. Wojnilower, *The Quality of Bank Loans: A Study of Bank Examination Records*, 1962, Martin H. Seiden, *The Quality of Trade Credit*, 1964, and Thomas R. Atkinson, *Trends in Corporate Bond Quality*, 1967. In preparation are reports on corporate direct placements, municipal bonds, agricultural credit, residential mortgage credit, a statistical compendium on credit quality, and a summary volume.

substantial improvements in instalment credit quality data, both private and governmental. In their final chapter, the authors urge a program of still further improvement in the statistics of instalment credit, to whose potential value their work attests.

This volume develops the concepts of *ex ante* and *ex post* credit quality, first set forth in a pioneering article by Moore in 1956.² These concepts provide much of the methodological framework of the other credit quality studies. In addition, throughout the volume there are methodological innovations designed to measure and test changing credit quality on both a "cross-sectional" and a time-series basis.

Finally, there is the growing importance of instalment credit in the contemporary American scene. Instalment debt, like household debt in general, has expanded more rapidly than other major types of debt over the postwar years. In addition, the ratios between aggregate consumer instalment debt and debt service, on the one hand, and aggregate consumer income, on the other, have so risen in the postwar years as to cause some concern. This concern takes one or both of two forms. One is lest the household sector become overburdened by indebtedness, with a consequent weakening of credit performance. A different, but no less serious, concern is lest the relatively high plateau that has been reached in recent years in the ratio of consumer debt service to personal income may mean that the buoyancy contributed to the economy by the steady rise in instalment credit in the postwar years can no longer be anticipated.

Moore and Klein draw no definite conclusions regarding these latter matters. But their work will be of interest to those who wish to form judgments regarding them.

² "The Quality of Credit in Booms and Depressions," *Journal of Finance*, May 1956.

JAMES S. EARLEY
*Director, Quality of
Credit Program*

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