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## 2021 Midwestern Bankruptcy Institute

# Koger Lecture: The Wall of Debt, and Other Economic Legacies of COVID-19

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# The Pandemic of 2020-2021: The Wall of Debt and Other Economic Legacies of COVID-19

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Co-Chairman, Guggenheim Securities

Presentation to the ABI/UMKC Midwestern Bankruptcy Institute  
September 30, 2021

\*Prepared with the assistance of Josh Mendelsohn and James Daugherty of Guggenheim Securities

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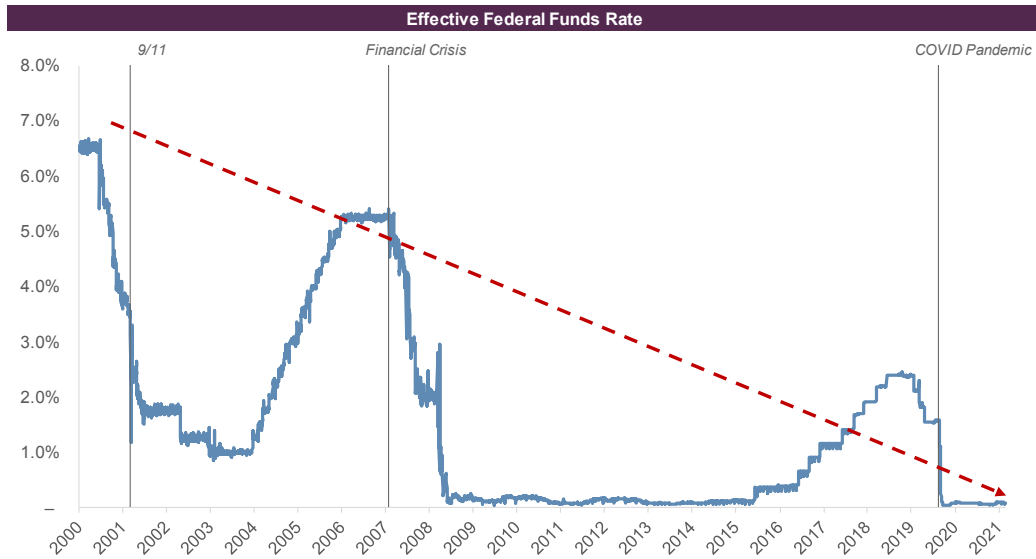
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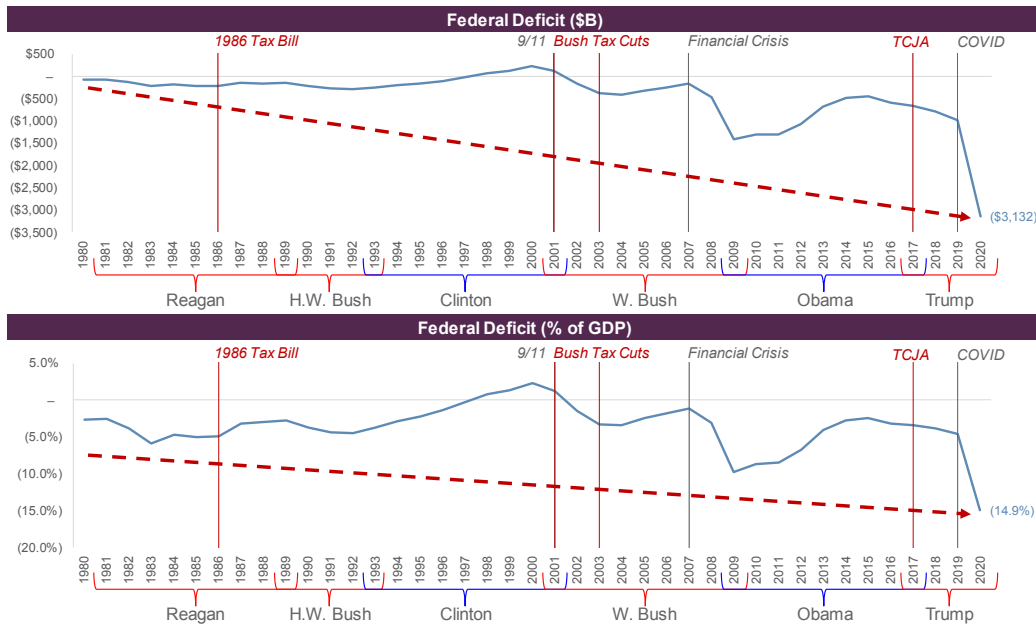
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Evolution of the Fed Funds Rate – A Long Slide Down to the Zero Bound



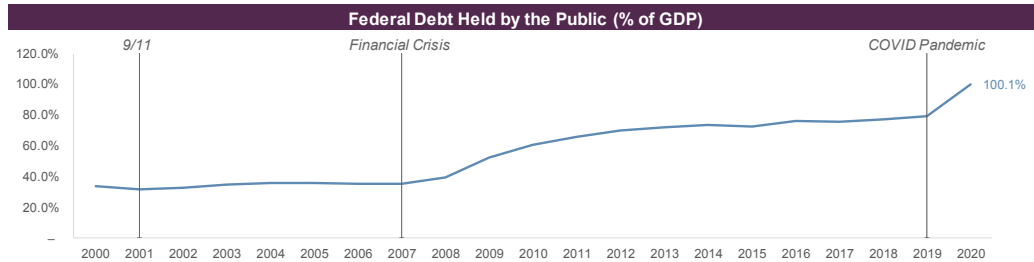
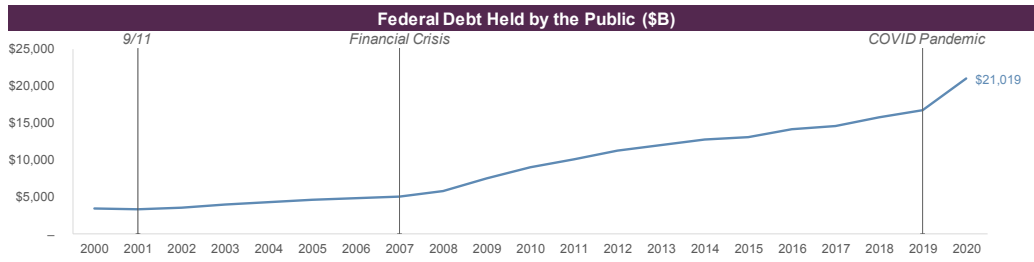
Source: Bloomberg.

Running Historic Government Deficits During an Economic Expansion



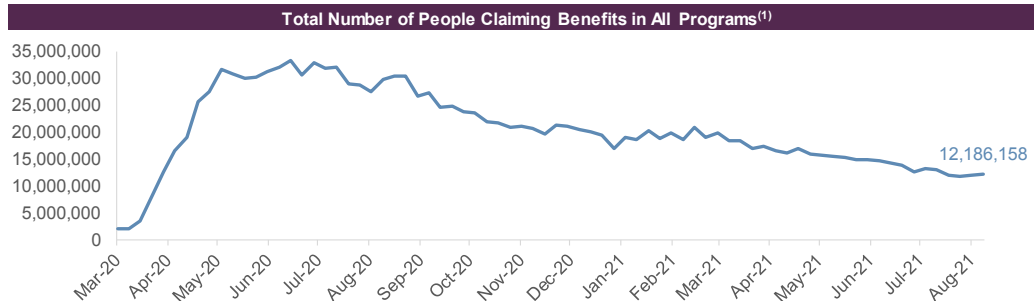
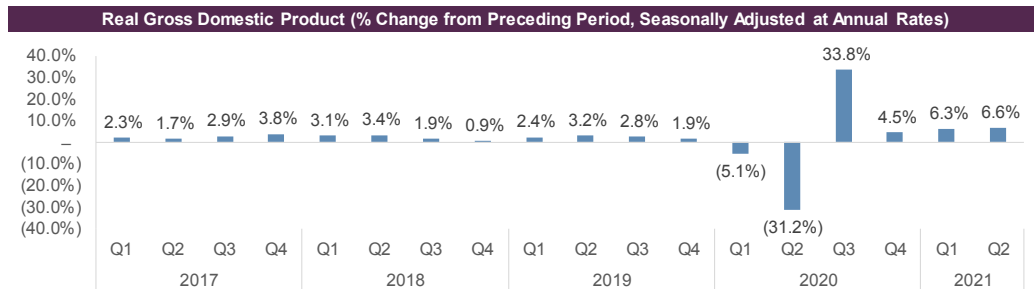
Source: Congressional Budget Office.

And Growing Public Debt Faster than the Economy Was Growing



Source: Congressional Budget Office.

Then the Pandemic Struck in Q1 2020 and the Staggered State Shutdowns and Persistent Infection Rates Significantly and Adversely Affected GDP and Employment



Source: BEA, United States Department of Labor.

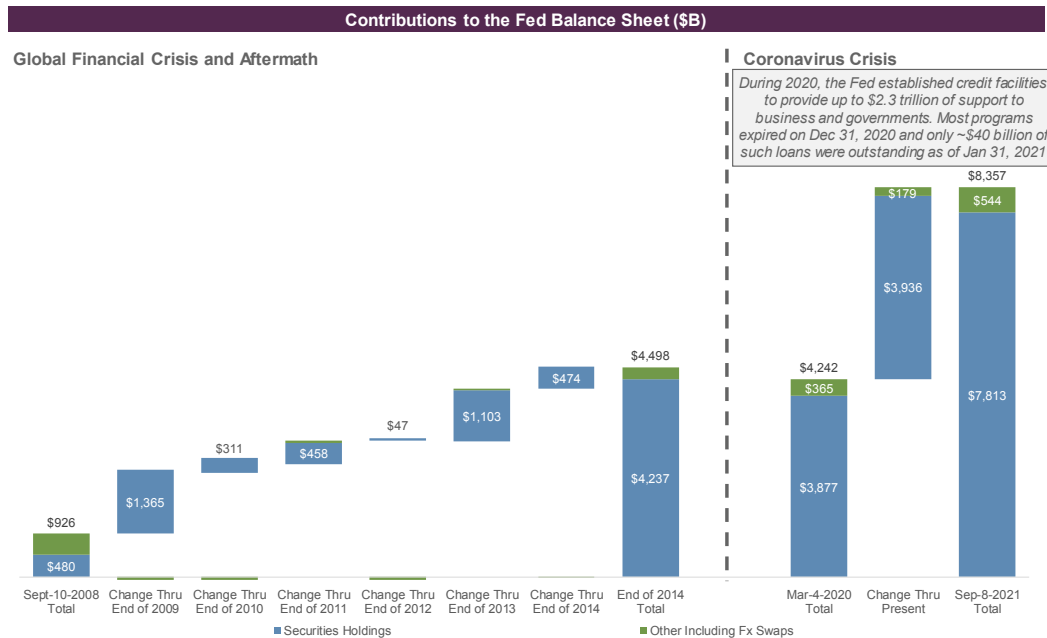
(1) Includes regular state, federal employee, newly discharged veteran, pandemic unemployment assistance, pandemic emergency UC, extended benefits, state additional benefits, and STC/Workshare unemployment programs.

The Federal Government's Response to Date

U.S. COVID-19 Response			
	Allocated Amount	Committed / Disbursed	Deficit Impact
Federal Reserve	\$6.52 trillion	\$3.50 trillion	N/A
Administrative	\$886 billion	\$722 billion	\$143 billion
Legislative	\$5.90 trillion	\$4.59 trillion	\$5.17 trillion
+ Loan Programs	\$1.56 trillion	\$1.28 trillion	\$1.05 trillion
+ Payroll Protection Program	\$835 billion	\$835 billion	\$808 billion
+ Economic Injury Disaster Loans	\$475 billion	\$252 billion	\$50 billion
+ Airline Industry Support	\$86.5 billion	\$80.1 billion	\$55 billion
+ Other	\$163.5 billion	\$112.9 billion	\$137 billion
+ Income Support	\$896 billion	\$805 billion	\$865 billion
+ Unemployment Benefits	\$706 billion	\$649 billion	\$691 billion
+ Other	\$190 billion	\$156 billion	\$174 billion
+ Health Spending	\$662 billion	\$369 billion	\$652 billion
+ Direct Payments	\$869 billion	\$815 billion	\$869 billion
+ Tax Policy	\$577 billion	\$387 billion	\$430 billion
+ State & Local Funding	\$884 billion	\$675 billion	\$882 billion
+ Other Spending	\$454 billion	\$245 billion	\$428 billion

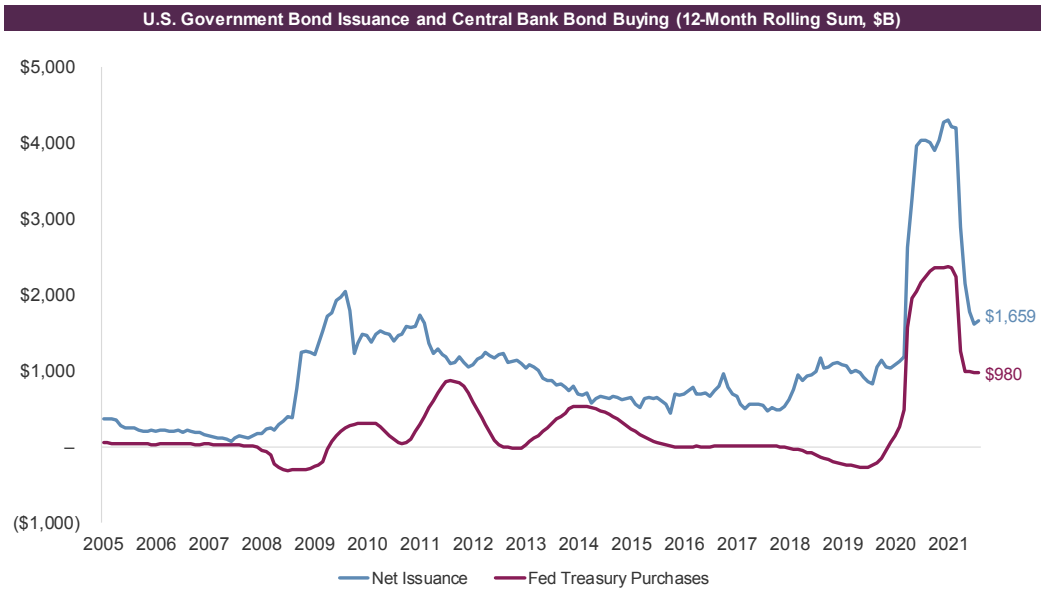
Source: CRFB's COVID Money Tracker as of September 10, 2021.

The Federal Reserve Went Where No Fed Has Gone Before: Intervention in the Corporate Credit Markets, Disintermediating the Banks



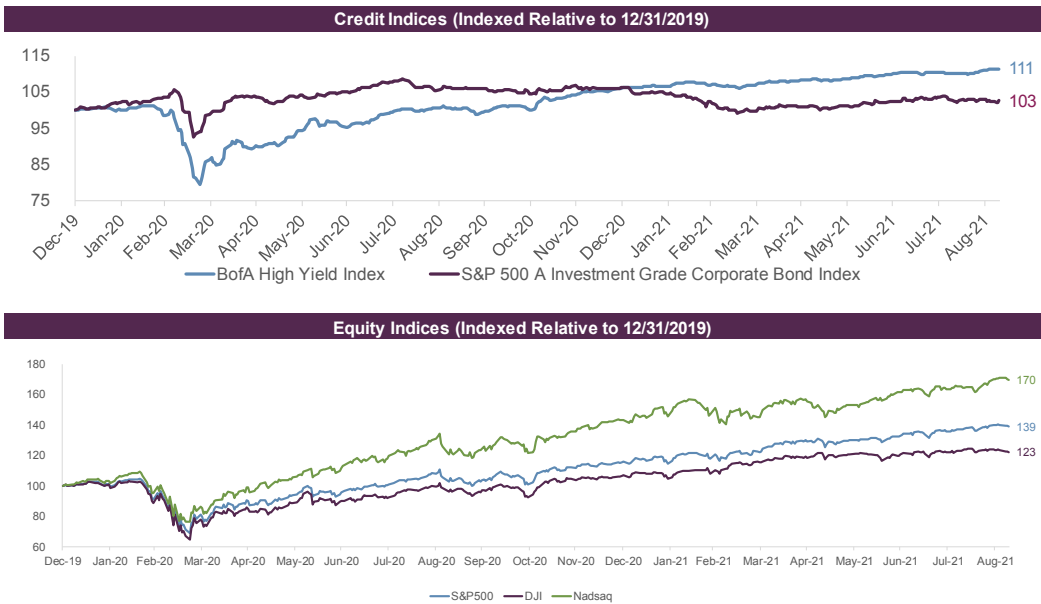
Source: Bao et. al., Johns Hopkins University, Center for Financial Stability.

And Dramatically Increased the Pace of Its Bond Purchases in the Secondary Market to Keep Up with Treasury’s Net Issuance so as to Hold Treasury’s Borrowing Costs Down as the Federal Deficit Skyrockets



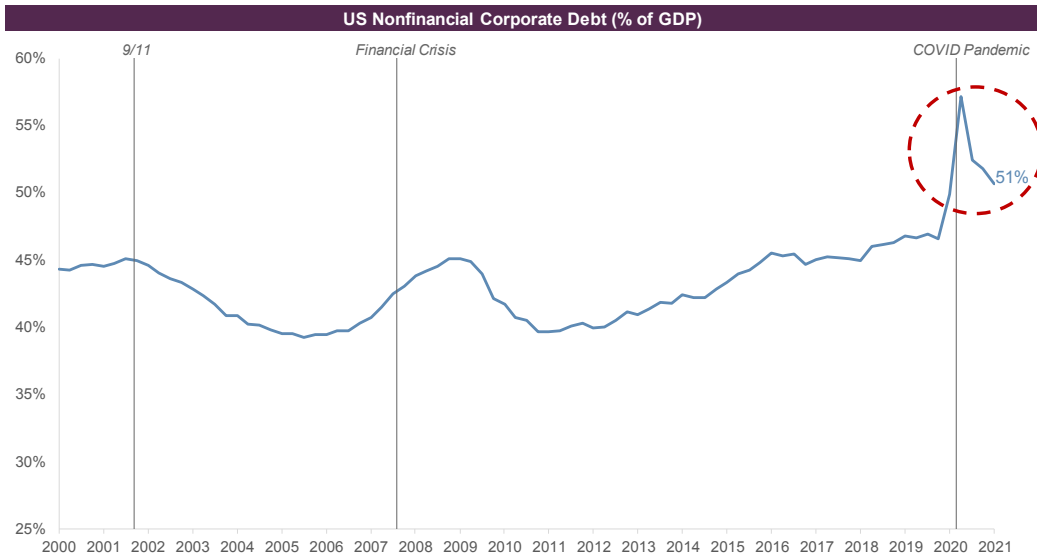
Source: Sifma, FRED.

The Federal Government’s Response to Date Has Rallied Corporate Credit and Equity Markets from March Lows



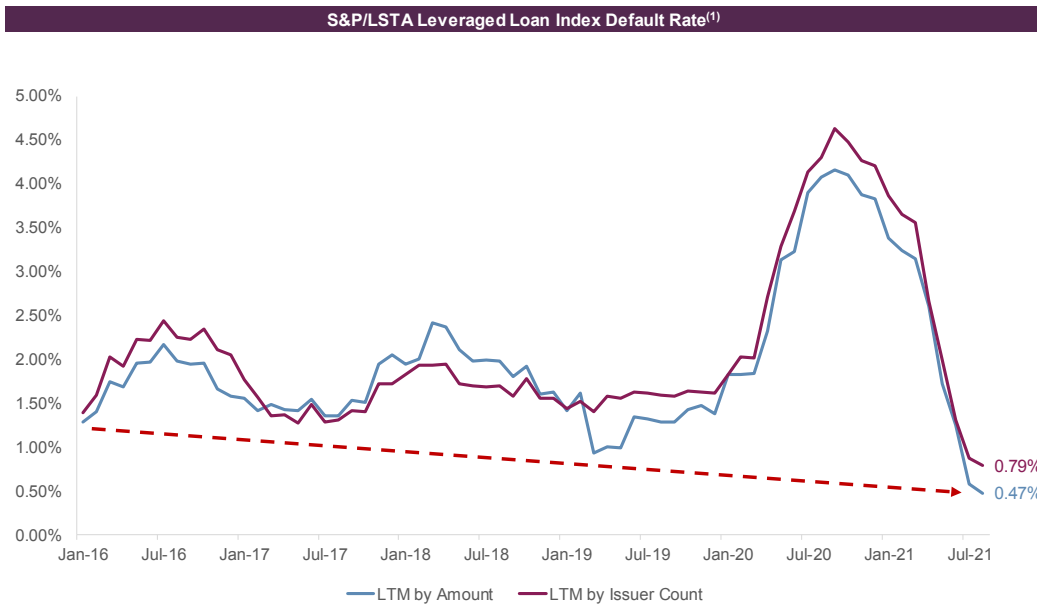
Source: Bloomberg.

Highest Corporate Debt to GDP in American History



Source: FRED.

The Economic Dislocation and Demand Shock Created by the Failure to Get the Spread of the Virus Under Control Led to a Significant Increase in Leveraged Loan Default Rates, Which Have Since Recovered

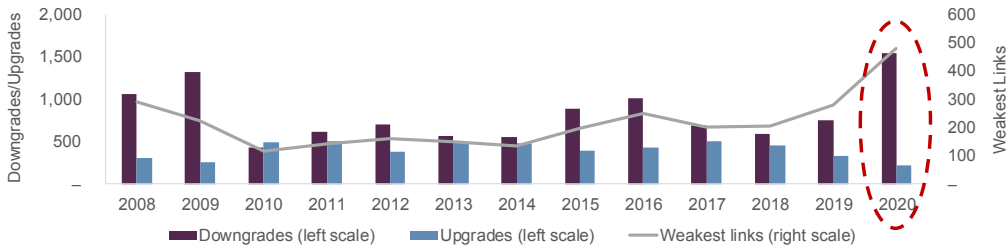


Source: LCD.

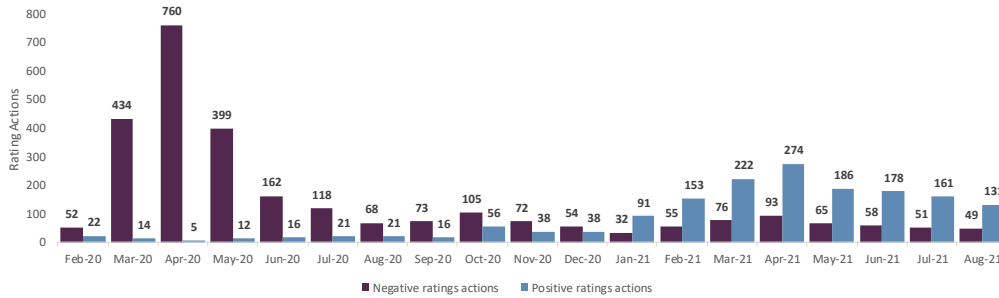
(1) Default defined as (1) company filing for bankruptcy, (2) facility gets downgraded to D by S&P (not due to below par buybacks), (3) interest payment is missed without a forbearance. LTM default rate by amount is equal to the sum of all defaulted amounts in the last 12 months divided by the total amount outstanding of performing loans 12 months ago. LTM default rate by issuer count is equal to the count of defaulted issuers in the last 12 months divided by total issuers not in default 12 months ago.

## Despite the Recent Slowdown of Negative Rating Actions, the Risk of Future Defaults Is Still High Following the Largest Number of Downgrades Since the Financial Crisis

S&P Upgrades, Downgrades and Weakest Links<sup>(1)</sup>



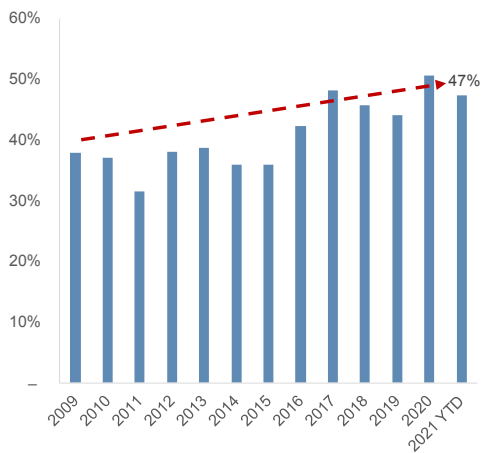
S&P Ratings Actions (Feb '20-Aug '21)



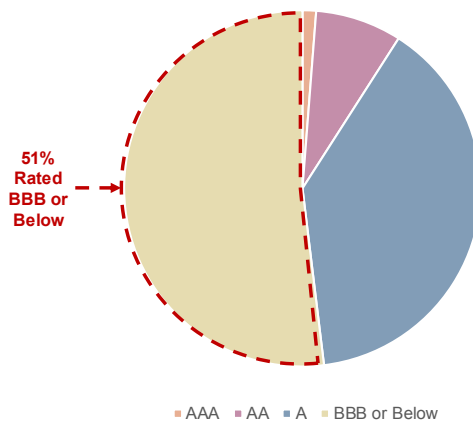
Source: S&P Global Ratings.  
 (1) Weakest Links defined as issuers rated 'B-' or lower by S&P Global Ratings with negative outlooks or ratings on CreditWatch with negative implications.

## Approximately Half of Investment Grade Debt Issued and Outstanding Is Now at the Lowest Rung of the Credit Rating Scale

% of Investment Grade Issuances Rated BBB or Below<sup>(1)</sup>



Composition of Investment Grade Debt Outstanding<sup>(2)</sup>

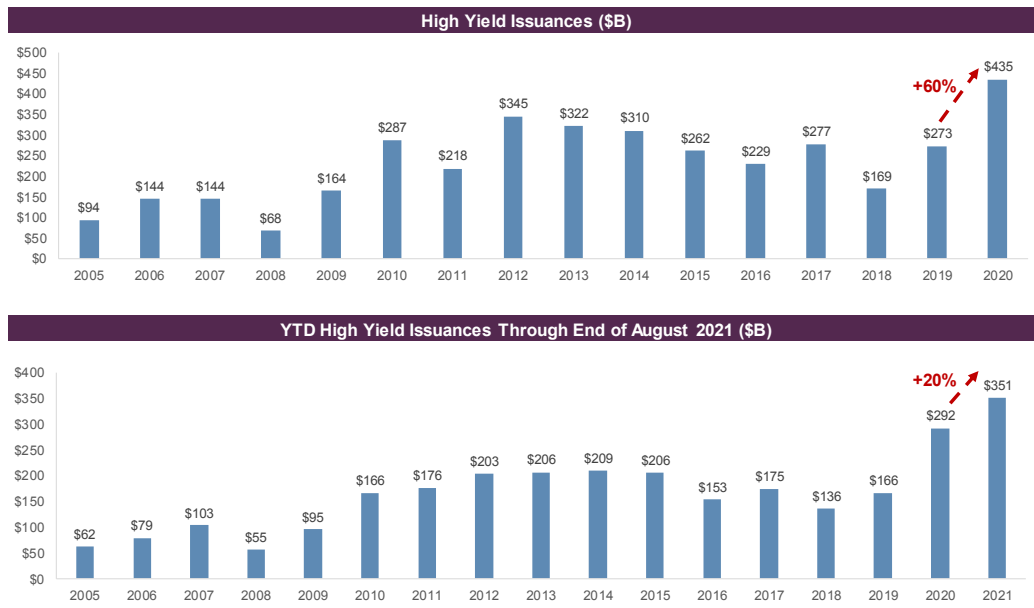


Source: LCD, Bloomberg, ICE BofA US Corporate Index.

(1) Per S&P LCD Comps.

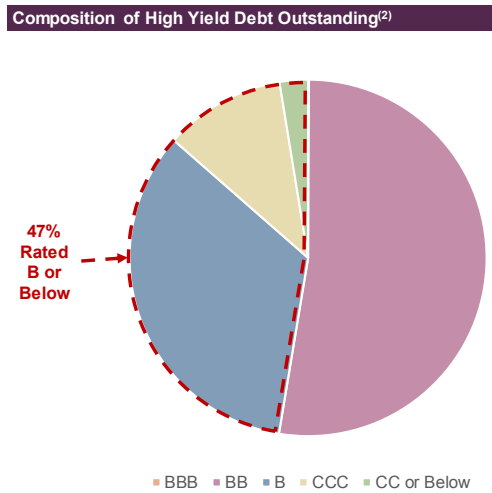
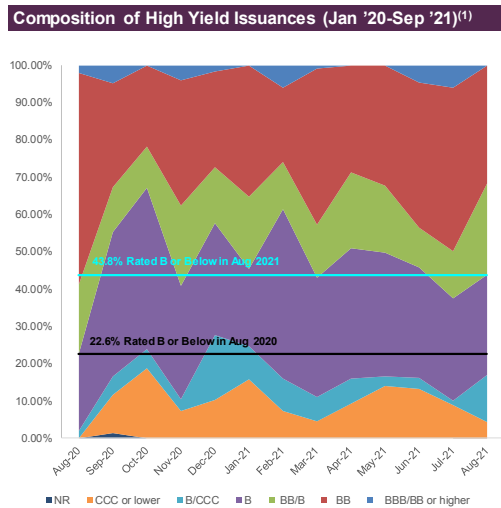
(2) Represents composition of ICE BofA US Corporate Index, which tracks the performance of US dollar denominated investment grade rated corporate debt publicly issued in the US domestic market. To qualify for inclusion in the index, securities must have an investment grade rating (based on an average of Moody's, S&P, and Fitch) and an investment grade rated country of risk (based on an average of Moody's, S&P, and Fitch foreign currency long term sovereign debt ratings). Each security must have greater than 1 year of remaining maturity, a fixed coupon schedule, and a minimum amount outstanding of \$250 million.

And Speculative Debt Issuances are Booming, as 2020 Saw Record High Yield Issuances and 2021 YTD Is 20% Above Last Year's Pace



Source: S&P LCD Comps.

Speculative Grade Issuances Appear to Be Deteriorating in Credit Quality

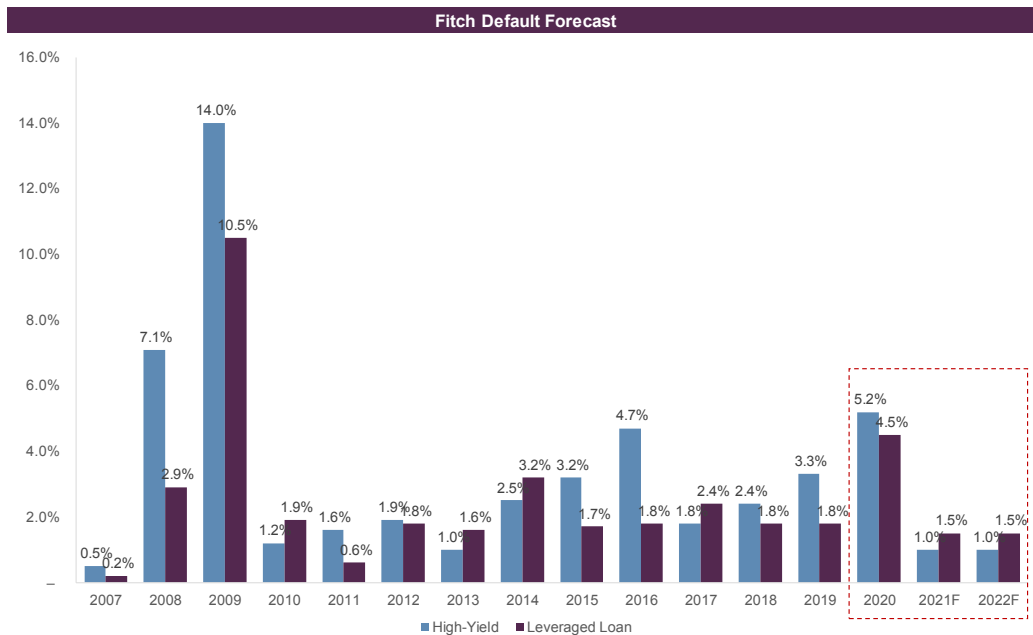


Source: LCD, Bloomberg, ICE BofA US High Yield Index.

(1) Per S&P LCD Comps.

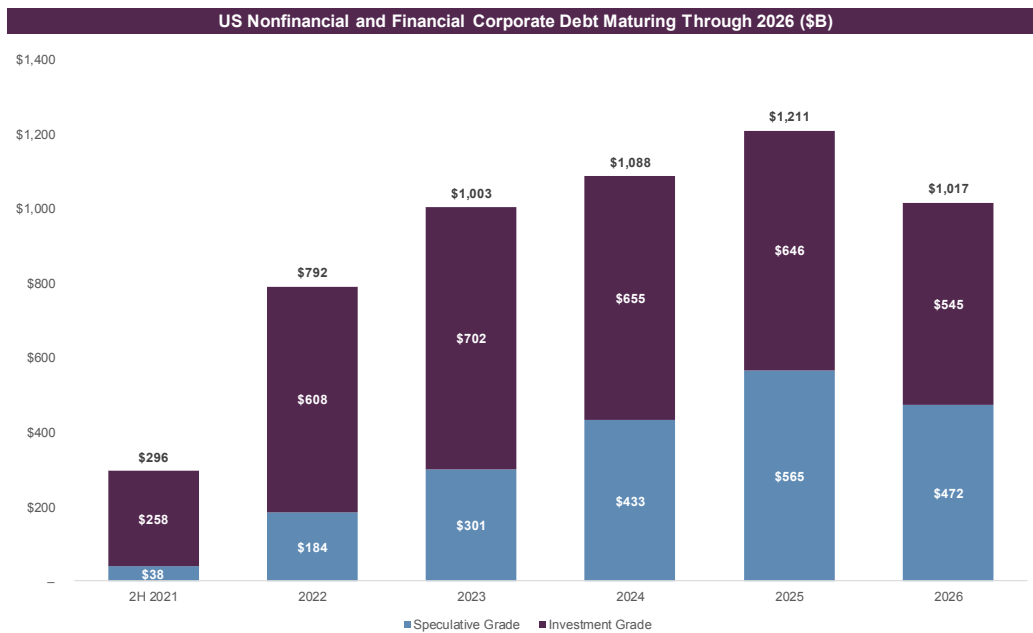
(2) Represents composition of ICE BofA US High Yield Index, which tracks the performance of US dollar denominated below investment grade rated corporate debt publicly issued in the US domestic market. To qualify for inclusion in the index, securities must have a below investment grade rating (based on an average of Moody's, S&P, and Fitch) and an investment grade rated country of risk (based on an average of Moody's, S&P, and Fitch foreign currency long term sovereign debt ratings). Each security must have greater than 1 year of remaining maturity, a fixed coupon schedule, and a minimum amount outstanding of \$100 million.

Default Rates Initially Rose to Their Highest Levels Since the Financial Crisis, Though the Near-Term Forecast Shows Near Decade Lows



Source: Fitch.

COVID Has Left US Corporates with a Wall of Debt Increasing to Over \$1 Trillion by 2023



Source: S&P Ratings.

# U.S. Debt Statistics

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MORTGAGE, STUDENT LOAN, CREDIT CARD, & AUTO LOAN




## U.S. Mortgage Debt

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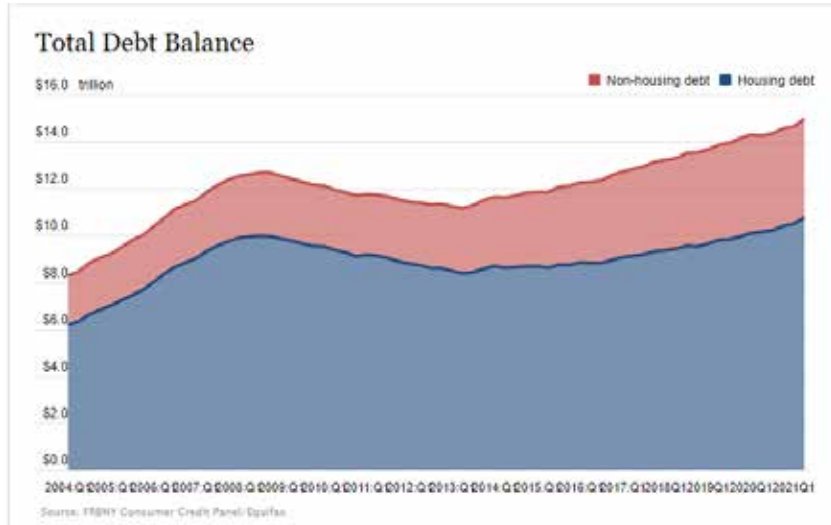
At the end of 2<sup>nd</sup> quarter 2021 there was \$10.44 trillion in outstanding mortgage debt (FRBNY Consumer Credit Panel/Equifax)

At the end of January 2021 approximately 5.9% of mortgages were in some stage of delinquency, dropping below 6% for the first time since March 2020 (Black Knight)

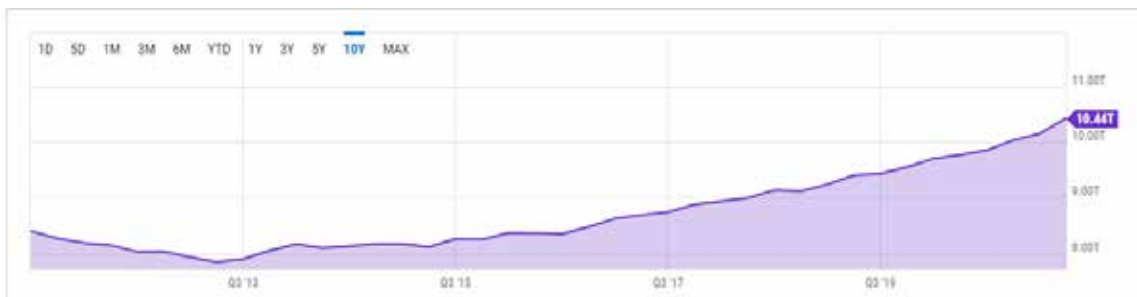
As of week ending July 11<sup>th</sup>, 2021 3.50% of mortgage loans are in forbearance equating to approximately 1.75 million homeowners (Mortgage Bankers Association)



## Outstanding Mortgage Debt (Blue)



## US Mortgage Debt over 10 Years



# U.S. Student Loan Debt

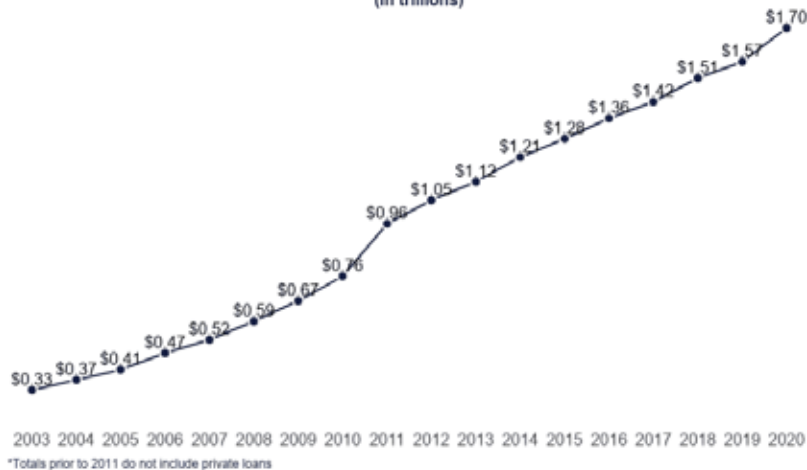
As of Q2 2021 there was approximately \$1.57 trillion in outstanding student loan debt comprising ~42.9 million borrowers (FRBNY Consumer Credit Panel/Equifax)

As of Q2 2021 5.7% of student loan debt was in delinquency or default (New York Federal Reserve Bank)

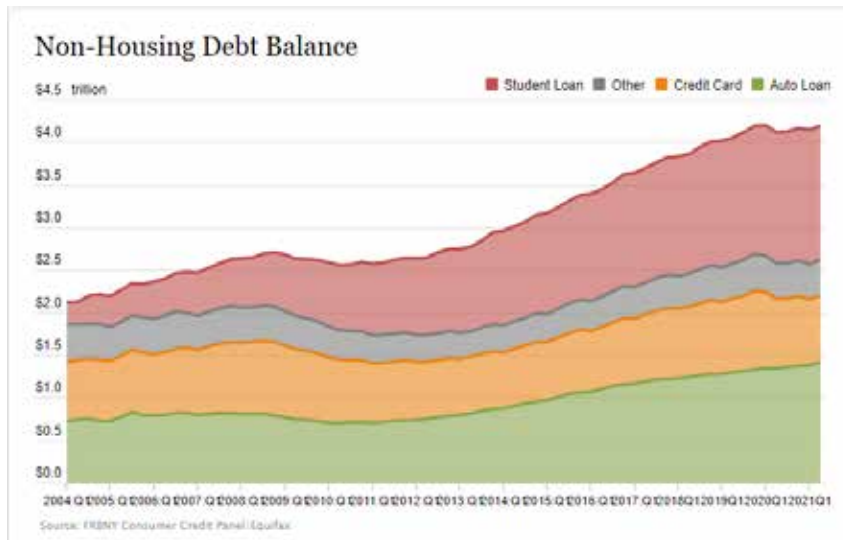
Approximately half (22.2 million) of student loan borrowers are in forbearance (Federal Student Aid)



**Historic Total\* National Student Loan Debt Balance**  
(in trillions)



## Outstanding Non-Housing Debt



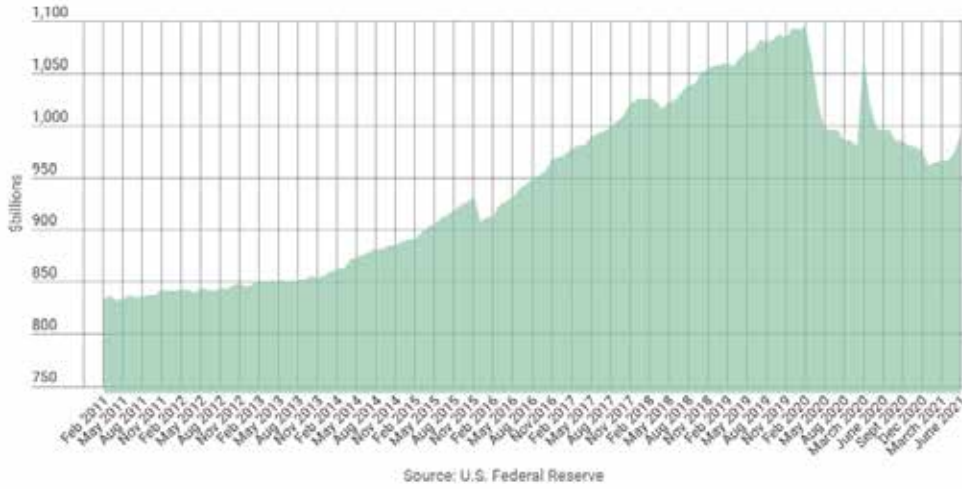
## U.S. Credit Card Debt

As of Q2 2021 there was approximately \$788 billion in outstanding credit card debt (FRBNY Consumer Credit Panel/Equifax)

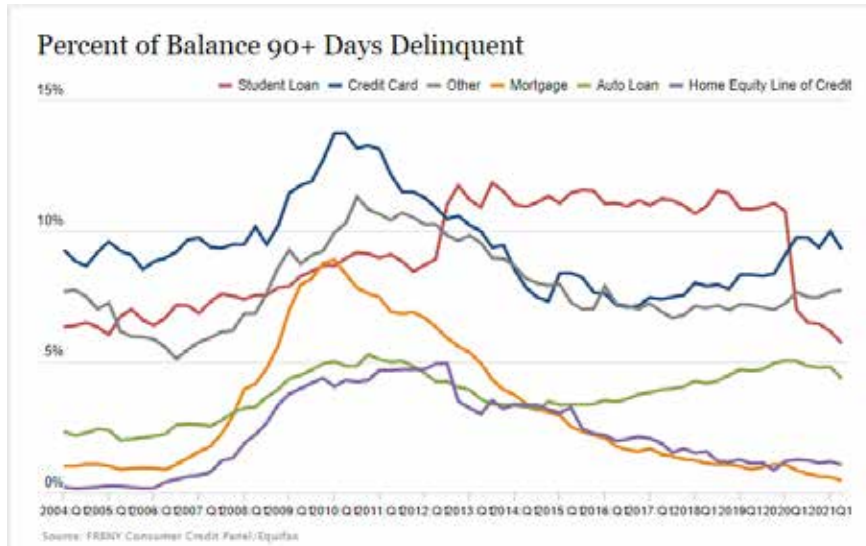
As of Q2 2021 credit card delinquency was 9.3% (FRBNY Consumer Credit Panel/Equifax)

Over the last 10 years credit card debt has grown by approximately \$90 billion dollars (FRBNY Consumer Credit Panel/Equifax)

Revolving (credit card) debt, 2011-2021



% Percent of Delinquent Debt



# U.S. Auto Loan Debt

As of Q2 2021 there was \$1.42 trillion in outstanding auto loan debt (FRBNY Consumer Credit Panel/Equifax) covering approximately 84.7 million auto loans (Transunion)

As of Q2 2021 auto loan delinquency was 4.4% (FRBNY Consumer Credit Panel/Equifax)

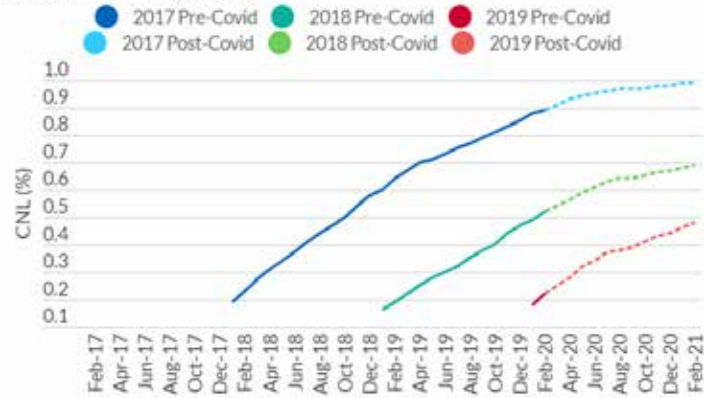
As of March 2021 prime auto loan 61+ day delinquency was .22% (Fitch Ratings)

As of March 2021 subprime 61+ day auto loan delinquency was 3.76% (Fitch Ratings)

## US Auto Loan Debt over 10 Years



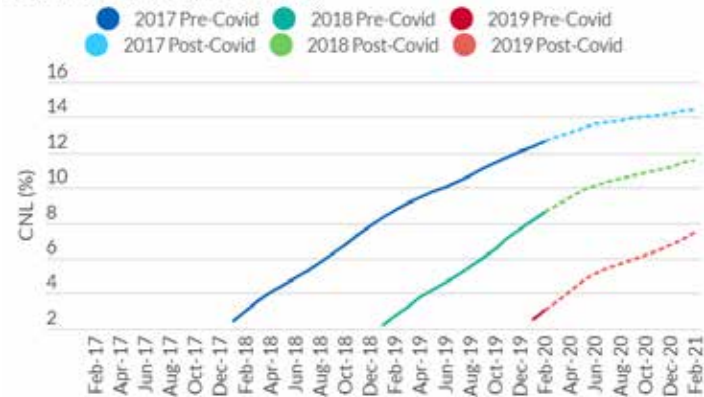
Prime Auto Loan Cumulative Net Losses Consistent with Pre-Pandemic Performance



Note: CNL - Cumulative Net Losses. The charts only include CNL data from transactions that were outstanding as of the Feb. 2021 payment date.  
Source: Fitch Ratings.



Subprime Auto Loan Cumulative Net Losses Consistent with Pre-Pandemic Performance



Note: CNL - Cumulative Net Loss. The charts only include CNL data from transactions that were outstanding as of the Feb. 2021 payment date.  
Source: Fitch Ratings.



# Faculty

**Hon. Michelle M. Harner** is a U.S. Bankruptcy Judge for the District of Maryland in Baltimore, appointed in 2017. Prior to her appointment to the bench, she was the Francis King Carey Professor of Law and the Director of the Business Law Program at the University of Maryland Francis King Carey School of Law, where she taught courses in bankruptcy and creditors' rights, business associations, business planning, corporate finance and the legal profession. Judge Harner lectured frequently during her academic career on various topics involving corporate governance, financially distressed entities, risk management and related legal issues. Her academic scholarship is widely published, with her publications appearing in, among others, the *Vanderbilt Law Review*, *Notre Dame Law Review*, *Washington University Law Review*, *Minnesota Law Review*, *Indiana Law Journal*, *Fordham Law Review* (reprinted in *Corporate Practice Commentator*), *Washington & Lee Law Review*, *William & Mary Law Review*, *University of Illinois Law Review*, *Arizona Law Review* (reprinted in *Corporate Practice Commentator*) and *Florida Law Review*. Judge Harner has served as the Associate Reporter to the Advisory Committee on the Federal Rules of Bankruptcy Procedure, the Reporter to the ABI Commission to Study the Reform of Chapter 11, and most recently chaired the Dodd-Frank Study Working Group for the Administrative Office of the U.S. Courts. She also served as the Robert M. Zinman ABI Resident Scholar for the fall of 2015. Judge Harner is an elected conferee of the National Bankruptcy Conference, an elected Fellow of the American College of Bankruptcy, and an elected member of the American Law Institute. She previously was in private practice in the business restructuring, insolvency, bankruptcy and related transactional fields, most recently as a partner at the Chicago office of the international law firm Jones Day. Judge Harner received her B.A. *cum laude* from Boston College in 1992 and her J.D. *summa cum laude* from The Ohio State University College of Law in 1995.

**Richardo I. Kilpatrick** is the managing partner of Kilpatrick & Associates, PC in Auburn Hills, Mich., and specializes in creditors' rights and insolvency law while focusing on corporate, consumer and commercial litigation and bankruptcy, real property remedies for creditors, real property transactions and general corporate counseling. He is a past president of the ABI and has served on the board of directors for the American College of Bankruptcy. Mr. Kilpatrick is a member of the State Bar of Michigan, the U.S. District Courts for the Eastern and Western Districts of Michigan, the Sixth Circuit Court of Appeals and the U.S. Supreme Court. He was inducted as a Fellow into the American College of Bankruptcy in March 1999 and appointed to its board of directors in July 2001. In October 2008, Mr. Kilpatrick was invited to be a conferee at the National Bankruptcy Conference. As a member of the National Bankruptcy Conference, he worked with Hon. Thomas Small on the NBC's Small Business Proposal, a portion of which was incorporated into the Small Business Reorganization Act of 2019. Mr. Kilpatrick also served as a member of the Judicial Conference Advisory Committee on Bankruptcy Rules from August 2011-17, where he worked to directly craft, tweak, update and change bankruptcy rules in an ongoing effort to improve the practice of bankruptcy for all involved. He is Board Certified in Consumer Bankruptcy Law by the American Board of Certification. Mr. Kilpatrick received his B.A. in economics in 1973 from Harvard University and his J.D. in 1982 from the University of Michigan Law School.

**James E. Millstein** is the co-chairman of Guggenheim Securities, LLC in New York, the investment banking and capital markets business of Guggenheim Partners, a global investment and advisory firm. Prior to joining Guggenheim in 2018, he was the founder and CEO at Millstein & Co. His representative engagements at Guggenheim include advice to Fannie Mae in connection with its potential recapitalization, to Knighthead Capital and Certares Management in connection with their acquisition of Hertz out of chapter 11, and to the Governor of the State of California in connection with PG&E's chapter 11. His representative engagements at Millstein & Co. include advice to the Commonwealth of Puerto Rico in connection with the management of its \$75 billion of institutional indebtedness, to US Airways in connection with its acquisition of American Airlines out of chapter 11, and advice to Caesars in connection with its financial restructuring in chapter 11. From 2009-11, Mr. Millstein was the CRO at the U.S. Department of the Treasury, where he was responsible for oversight and management of the Department's largest investments in the financial sector and was the principal architect of AIG's restructuring and recapitalization. Prior to joining the Treasury, he served as managing director and global co-head of Corporate Restructuring at Lazard from 2000-08. Before joining Lazard, he was partner and head of the Corporate Restructuring practice at Cleary, Gottlieb, Steen & Hamilton. Mr. Millstein is a lecturer in law at Columbia Law School, where he teaches a course on private capital, and an adjunct professor of law at Georgetown University, where he has taught a course on the federal regulation of financial institutions. A Fellow of the American College of Bankruptcy, he was a commissioner on ABI's Commission to Study Reform of Chapter 11. Mr. Millstein also serves on the Investment Committee of Mill Point Capital, a private-equity firm formerly affiliated with Millstein & Co. He received his B.A. in politics from Princeton University in 1978, his M.A. in political science from the University of California at Berkeley in 1979 and his J.D. from Columbia University School of Law in 1982, where he was a Harlan Fiske Stone Scholar.