

Asset-Backed Finance: Nuances of Consumer Lending¹



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The financial health of the U.S. consumer is under constant scrutiny. Personal consumption constitutes nearly 70% of GDP, underpinning demand for goods and services.² Lending to consumers is an industry in itself, from auto loans and credit cards to mortgages and student loans. In the context of asset-backed finance (ABF) within the consumer space, these loans represent collateral. Our key question is whether these loans will be repaid. Headlines regarding consumer health shouldn't be regarded as the defining information when making consumer lending investments: this data can be useful in informing our views, but a more nuanced assessment is required.



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Most investors will regularly review multiple consumer data metrics, including unemployment rates, consumer savings and consumer spending. At a high level, the data doesn't yet appear to indicate a dramatic deterioration in consumer health. However, it's important to examine the underlying economic data points rather than rely on the headlines, for example:

- Unemployment remains low at 4.2%³ but continued jobless claims have incrementally risen to nearly two million,⁴ indicating that re-entering the workforce is currently challenging.
- The personal savings rate is nearly 5%,⁵ which is below the peak rate during the pandemic but above 2022 levels. However, this average may be dragged up by wealthier consumers as lower-income consumers struggle, having experienced year-over-year wage growth of just 1.5%.⁶
- Student loan delinquencies have accelerated in recent weeks, with over 30% of borrowers officially delinquent on their loans.⁷ This may have corollary impacts not yet visible in the data, as some borrowers face the prospect of garnished wages.



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This kind of data can serve as an input when assessing the potential credit performance of consumer asset pools. For improved utility, this means analyzing how data values and ranges vary by borrower cohort, activity and credit product. Even then, this data is only part of the picture: to form a nuanced view on future loan losses, managers should take a holistic approach, including evaluating industry trends, regulatory risks and originators. In short, quantitative inputs must be supplemented with qualitative underwriting.

The underwriting of each loan – and the motivation for repayment – is critical when assessing expected credit performance. For example, we're wary of consumer lending reliant on automated, algorithmic methods to estimate repayment likelihood rather than conducting commonsense "Will the borrower pay?" underwriting. Within the consumer segment of ABF, our preference is toward financings for essential purchases. This could include things like HVAC (heating, ventilation and air conditioning) system financing for homes.

In other words, we want to be invested in the assets that'll be prioritized by the borrower during periods of financial stress. Consumer lending continues to be a space we assess selectively, being just one component of the vast ABF universe. We tend to find the best relative value where regional lenders have stepped back and other originators or capital providers can't participate as they deal with problems from loans made (often to subprime consumers) in 2021-22. This can create a supply/demand imbalance that favors new entrants.

ENDNOTES

¹ Source: **The Roundup**: Top Takeaways from Oaktree's Quarterly Letters—June 2025 Edition. The content is derived from or inspired by ideas in recent letters, or other materials featuring or produced by Oaktree thought leaders; the text has been edited for space, updated, and expanded upon where appropriate.

² Federal Reserve Bank of St. Louis; personal consumption expenditure represents 68.4% of GDP, as of 1Q2025.

³ Federal Reserve Bank of St. Louis, as of May 2025.

⁴ Trading Economics, as of June 7, 2025.

⁵ Federal Reserve Bank of St. Louis, as of April 2025.

⁶ BofA Consumer Checkpoint, as of May 9, 2025.

⁷ Bloomberg, as of June 24, 2025. Delinquency defined as 90 days late on loan payments.

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