The Rapid Fallout from Resumed Student Loan Repayment

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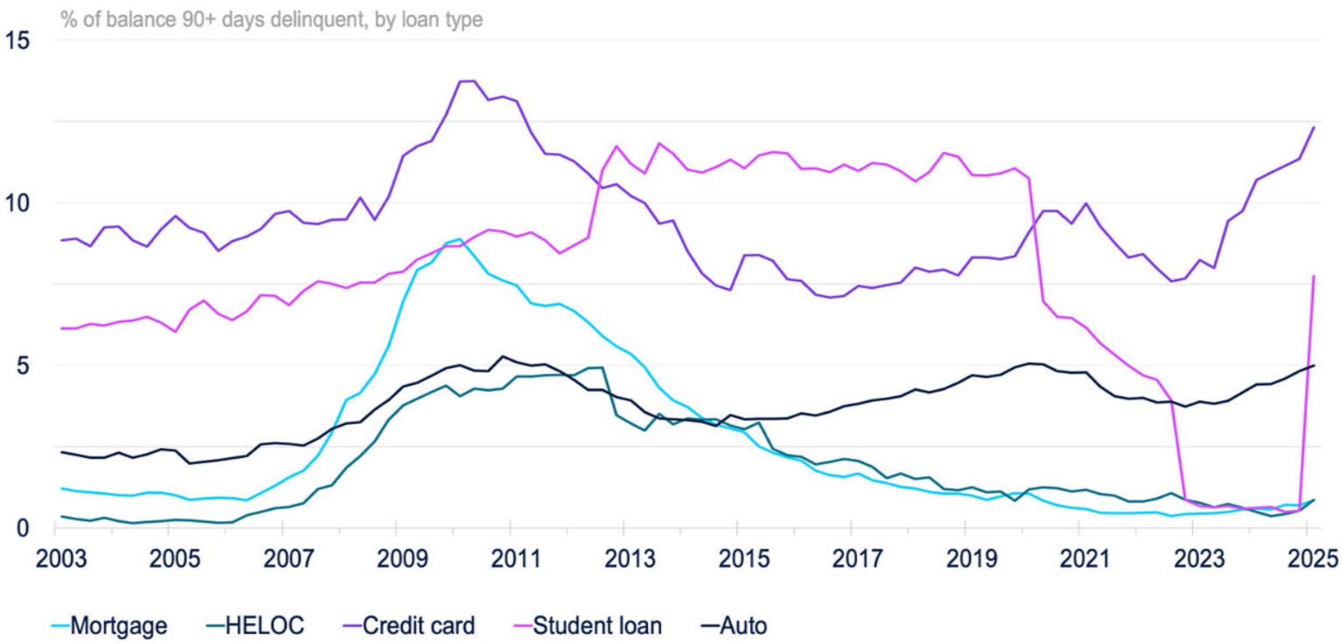
Federal student loan payments have resumed after a multi-year pause, reshaping the credit landscape for tens of millions of Americans and carrying broad implications for the securitized credit markets. More than 40 million borrowers benefited from pandemic-era forbearance, which suspended payments and shielded credit scores for more than three years.

Although this relief officially ended in September 2023, a 12-month “on-ramp” period followed, during which missed payments were not reported to credit bureaus. The “on-ramp” period temporarily delayed the credit impact of resumed obligations, artificially supporting borrower credit profiles through September 2024. That grace period ended when the U.S. Department of Education recently resumed collections on defaulted federal student loans, the effects of which were readily apparent.[1] Nearly six million borrowers, representing around 8% of total student loan balances, were 90+ days delinquent as of Q1 2025, according to the New York Federal Reserve (Figure 1).

Enforcement mechanisms, including tax refund offsets, federal government payment offsets, and wage garnishments, are once again active, placing renewed pressure on borrowers’ disposable income. As the effects of these developments cascade, they are expected to contribute to increased financial stress on the affected cohorts, placing downward pressure on FICO scores and further raising their borrowing costs.

We see two notable effects for securitized credit investors. First, the student loan situation stands as a case in point regarding the importance of holistic underwriting beyond a cursory look at FICO scores. Second, as credit dispersion and issuer differentiation increase with the resumption of student loan payments, investors must stay disciplined and agile given the pace of recent changes.

FIGURE 1: Student loan delinquencies jumped once the Federal grace period ended (% of balance 90+ days delinquent, by loan type).



Source: New York Fed Consumer Credit Panel, Equifax.

Impact on FICO Scores

The return of mandatory payments collided with persistent inflation and elevated living costs, compounding the financial strain on affected borrowers. Nearly 30% of these delinquent borrowers could enter default by July, according to TransUnion, likely triggering an enforcement mechanism.

A study by the New York Federal Reserve (Figure 2) reveals the extent and speed of the credit deterioration:

- More than 2.2 million borrowers who became newly delinquent on their student loans saw their credit scores drop more than 100 points;
- 3.2 million borrowers who became newly delinquent went deeper into subprime territory;
- and 2.4 million of the newly delinquent borrowers that started with scores above 620 experienced substantial declines in their credit scores and could face higher rates or limited credit access.

FIGURE 2: The resumption of student loan repayments has dealt a significant blow to the affected borrowers in just a few months.

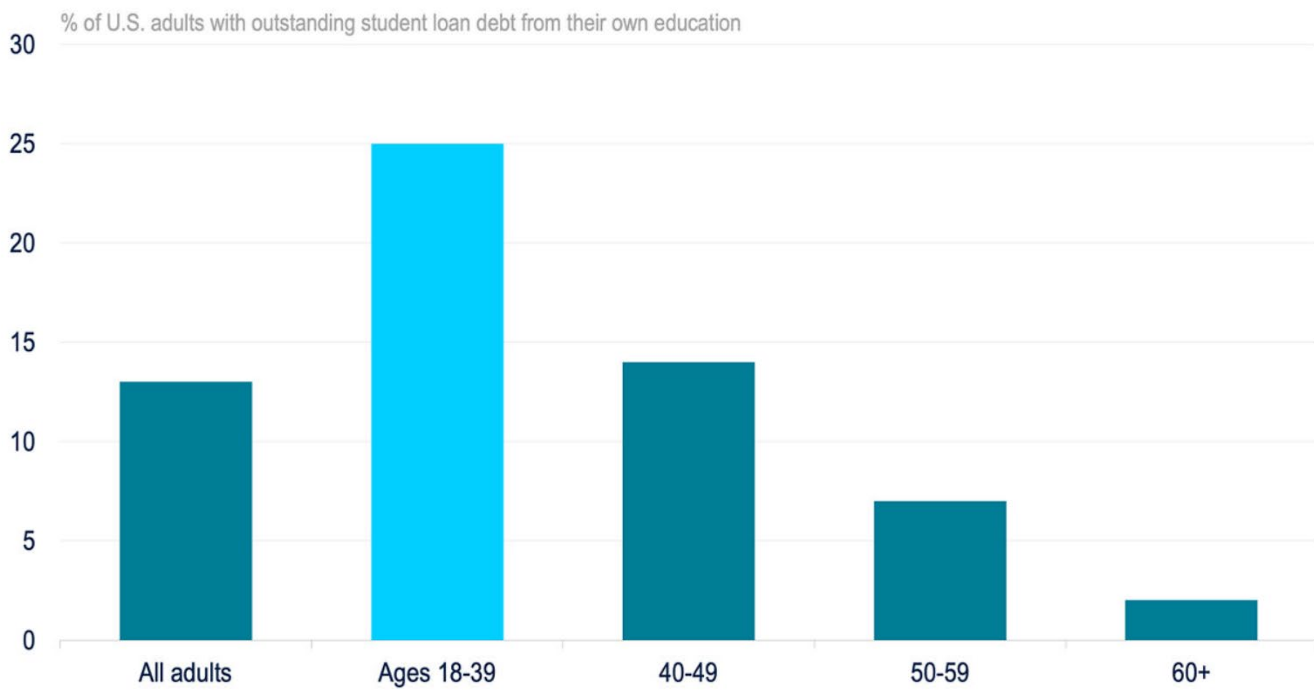
Credit score group	Count (millions)	Share of newly delinquent population (%)	Average credit score change
< 620	3.2	56.6	-74
620 - 719	2	35.9	-140
> 720	0.4	7.5	-177

Source: New York Federal Reserve Consumer Credit Panel and Equifax.

Implications for Securitized Credit Markets

With nearly 13% of U.S. adults carrying student loan debt (Figure 3), the implications for securitized credit markets, particularly consumer ABS, could be substantial. The most pronounced effects will likely be in asset classes lower in the consumer payment hierarchy and on lenders that did not incorporate the risks of then-dormant student loan obligations in their underwriting process.

FIGURE 3: The prevalence of U.S. student loan debt (% of U.S. adults with outstanding student loan debt from their own education).

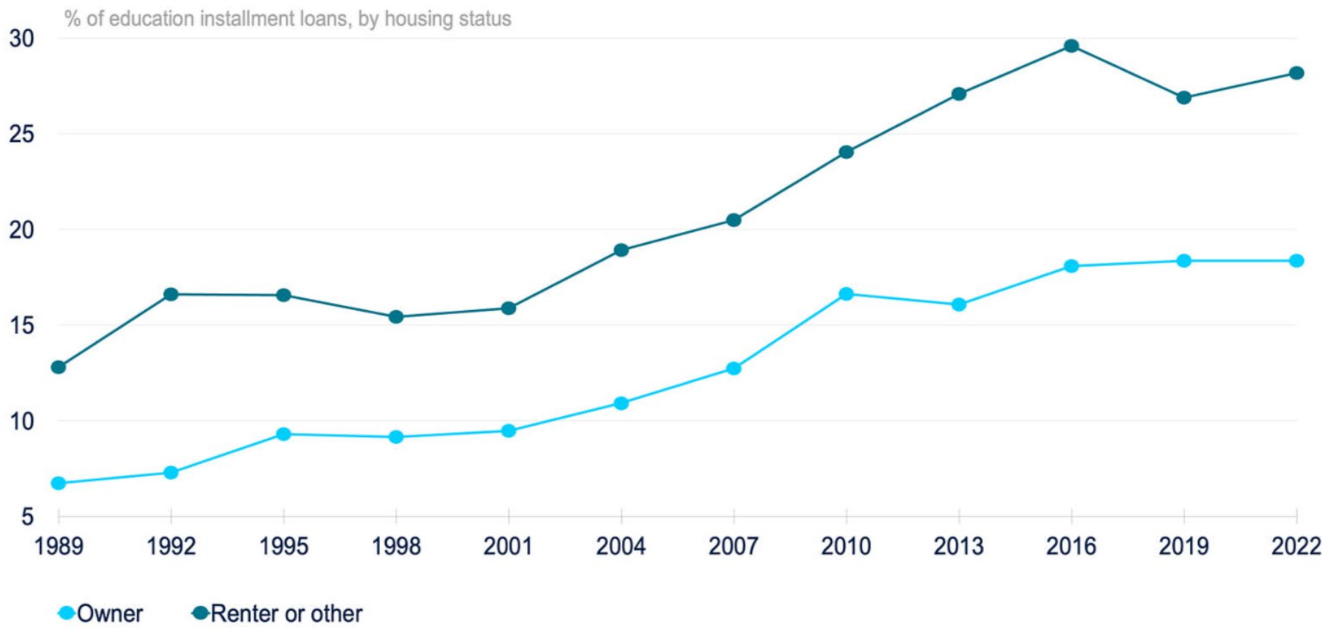


Source: PEW Research Center

Lenders with underwriting models that relied heavily on credit scores during the forbearance period may now face elevated default risk, as borrowers who appeared "prime" through 2024 begin to show signs of financial distress. Fewer than 1% of the newly delinquent student loan borrowers maintained FICO scores greater than 700 as of April 2025, down from 15% in January 2025, according to FICO. Subprime and over-leveraged borrowers are especially vulnerable, as resumed student loan payments tighten household budgets, which may become even more constrained with enforcement actions. However, the subset of lenders that proactively incorporated student loan obligations into their underwriting models, despite the temporary reporting pause, are better positioned to navigate this transition.

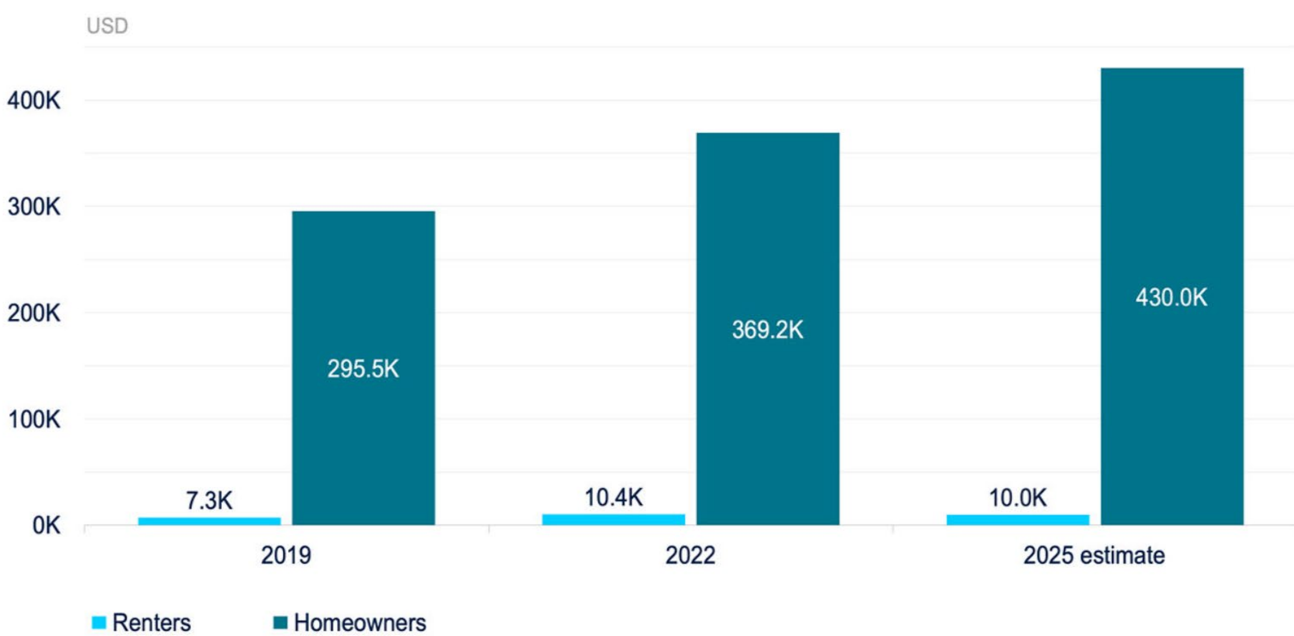
Student loan borrowers are more likely to rent than own homes (Figure 4). Even before student loan payments resumed, renters faced a financial disadvantage after missing out on rising home values, which widened the net worth gap between renters and homeowners (Figure 5). The resumption of student loan payments is expected to place additional strain on renters' finances, which could lead to weaker rent collections in multifamily housing, particularly those serving lower-income tenants. The impact will vary by region: tight rental markets in the Northeast and Midwest may replace delinquent tenants more easily, while oversupplied markets in the Sunbelt may face greater challenges. Regardless, the impact to the consumer will undoubtably be meaningful and warrants close analysis going forward.

FIGURE 4: The student loan burden falls mostly to renters (% of education installment loans, by housing status).



Source: New York Federal Reserve Survey of Consumer Finances. Represents % of respondents with student loan debt.

FIGURE 5: The disproportionate median net worth of homeowners and renters (USD).



Source: Federal Reserve Survey of Consumer Finance and National Association of Realtors

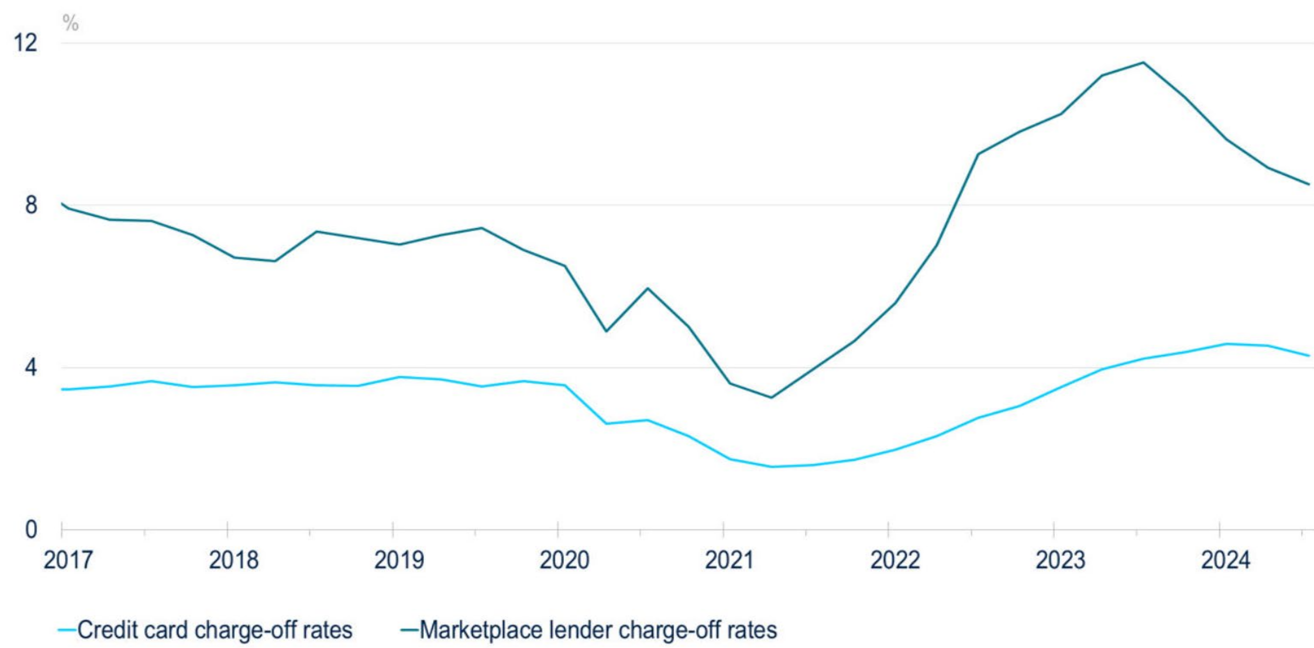
The mortgage market appears relatively well insulated thanks to the government-sponsored enterprises (GSEs), which continue to account for student loan payments in their underwriting, regardless of payment pauses. Most of the non-agency mortgage sector, which generally mirrors GSE underwriting practices, is therefore expected to be similarly shielded from the effects of student loan payment resumption. While smaller portions of the non-agency market that rely on alternative underwriting criteria may feel some pressure, the typically low loan-to-value (LTV) ratios on these homes should limit potential losses. As a result, overall mortgage credit performance is unlikely to undergo significant disruption, though declining credit scores could pose challenges for some first-time homebuyers seeking to qualify for loans.

Conclusion

For securitized credit investors and loan originators, the current environment demands a more nuanced approach to underwriting. Traditional static credit scores may no longer provide a reliable measure of financial risk. Lenders that look beyond surface-level metrics and incorporate broader indicators of borrower resilience will be better equipped to navigate the next phase of credit normalization.

A final example emphasizes our concluding point. Indeed, the ability to adjust underwriting criteria in real time proved critical in 2022-2023 as issuers responded to inflationary pressures that strained borrowers' cash flow. At that time, marketplace lenders - i.e., online platforms that connect borrowers with credit - saw a sharper rise in charge-offs than credit cards, which use a time-tested, holistic underwriting approach (Figure 6). This divergence was driven by multiple factors - including underwriting practices, sourcing channels, and investor demand - that ultimately resulted in marketplace lenders' underperformance relative to credit cards. There was also dispersion within each sector as certain lenders adapted more effectively than others.

FIGURE 6: The 2022-2023 underperformance of marketplace lenders vs. credit cards (%).



Source: PGIM, Federal Reserve, dv01 (a securitized data provider)

As student loan repayments resume, similar patterns of credit dispersion and issuer differentiation will likely re-emerge as well. As such, investors will not only need the discipline to avoid cursory underwriting practices, but will also require the processes and systems to monitor credit performance in real time in order to adjust positioning accordingly given the rapid pace of change. Ultimately, the more nimble investors and issuers can be, the better they will be able to navigate the cascading effects on the consumer.

1. "Collections Coming for Millions of Student-Loan Borrowers," The Wall Street Journal, May 5, 2025.

Source(s) of data (unless otherwise noted): PGIM Fixed Income, as of June 2025.
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