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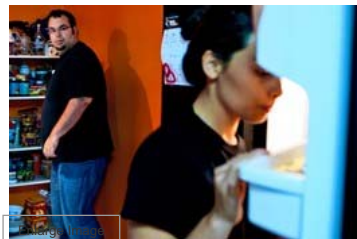
By JON HILSENATH and RUTH SIMON

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Anita Bullock-Morley, a 36-year-old speech therapist in Atlanta, is one who talks about her old borrowing habits like a recovering drug addict: "My life is so much better not having that haunting debt."



Rich-Joseph Facun for The Wall Street Journal

Jason Jacobs and his wife Kathy Jacobs, at home in Richmond, Va., are among those who are reducing debt.

She used savings to help pay for her wedding last year. And after wiping out the balance on two dozen credit cards—and swearing off boutique-label purchases and fancy vacations—she is working her way through \$50,000 in student loans and the \$215,000 left on her mortgage. Ms. Bullock-Morley is among a generation of Americans who were taught the value of saving as children but had to learn the hard way how to spend wisely.

Since the financial crisis erupted, millions of Americans have ditched their credit cards, accelerated mortgage payments and cut off credit lines that during the good times were used like a bottomless piggybank. Many have resorted to a practice once thought old-fashioned—delaying purchases until they have the cash.

As a result, total household debt—through payment or default—fell by \$1.1 trillion, or 8.6%, from mid-2008 through the first half of 2011, according to the Federal Reserve Bank of New York. Auto loan and credit-card balances in August had their biggest drop since April 2010, the Federal Reserve said.

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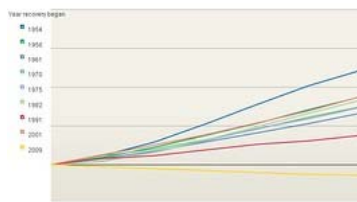
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"Households appear to have made some progress in deleveraging, but many still face elevated debt burdens and reduced access to credit," Janet Yellen, the Federal Reserve's second-ranking official, said Friday during a speech in Denver.

Deleveraging should help the U.S. economy in the long-run, putting households on a sounder footing and easing the nation's reliance on the savings of Chinese and other foreign nationals. But there are short-term dangers.

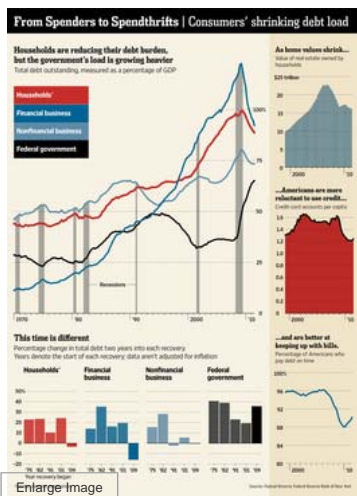
During the Great Depression, economist John Maynard Keynes warned of a so-called paradox of thrift: When everyone turns frugal, everyone suffers. Synchronized thrift slows the economy, according to Keynes, which hobbles income growth and makes people even stingier in a pernicious cycle.

Some experts worry that is happening now. Since the recession ended in mid-2009, the U.S. economy has expanded at a 2.5% annual rate, far slower than the average growth of 4.3% during the first two years of the previous four recoveries.

"Folks aren't borrowing," said Jim Ernest, executive vice president at Provident Credit Union in Redwood Shores, Calif. "They are paying down debt and continuing to save." Since January, 12% of the credit union's mortgage customers have made at least \$1,500 in extra payments.

Nearly 300 borrowers have made at least \$1,000 in additional payments on car loans from Provident, said Mr. Ernest, who confessed he sometimes can't sleep—Provident's loan portfolio has shrunk by a quarter since the end of 2008.

The change in attitude stretches far beyond Mr. Ernest's credit-union members: two-thirds of Americans polled online in July by U.K. research firm Absolute Strategy Research said they planned to either reduce their debt within a year or stop borrowing altogether.



[Enlarge Image](#)

[Redacted text]

Finance professors Atif Mian of the University of California at Berkeley and Amir Sufi at the University of Chicago found that households with the most debt were the likeliest to cut spending on big-ticket items.

Turbulent financial markets and turmoil in Europe also have caused some investors to retreat to the sidelines, where they plow money into reducing their debt rather than risk it in stocks.

Historically, deleveraging after a financial crisis is long and painful. In a 2010 study of 15 crises since World War II followed by deleveraging, economists Carmen and Vincent Reinhart concluded that economic growth and inflation-adjusted home prices fell in most countries during the decade after the crisis, while unemployment grew.

The current U.S. belt-tightening might have an unusually big impact because the last borrowing bubble was so big.

From 1997 to 2007, household debt ballooned from 66% of economic output to 98%, according to Federal Reserve data. As of June, the percentage had since been whittled down to 89%.

Number of the Week: GDP 6.7% Below Potential

It looks as if, despite everything, gross domestic product picked up in the third quarter, easing fears that the U.S. was on the cusp of another recession. But that doesn't mean the economy is anywhere near where it needs to be.

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More**Debt Stays High in Much of World****When a Credit Union's Customers Won't Borrow**

2009 and the end of the second quarter of 2011, according to TransUnion LLC.

Some economists and bankers say the deleveraging crunch has begun to ease. Student borrowing and auto loan balances are up from a year ago. Mark Zandi, chief economist of Moody's Analytics in West Chester, Pa., says the deleveraging process is winding down.

Yet this month's third-quarter earnings reports from U.S. banks show how leery many Americans remain over borrowing, despite record-low interest rates. Reluctance is widespread even among borrowers with excellent credit. According to Mr. Zandi, about 25% of deleveraging is by Americans who could get new loans but are paying down debt.

[Wells Fargo](#) & Co., the nation's fourth-largest bank in assets, announced meager 1% growth in loans from last year's third quarter. Loan demand remains so weak that deposits are piling up, hurting profit margins at Wells Fargo and thousands of other U.S. financial institutions. A Wells Fargo spokesman said although deposits were rising faster than loans, contributing "to a lower net-interest margin," the company was "very pleased" with its third-quarter loan growth.

Eager for new business, Citizens Equity First Credit Union, based in Peoria, Ill., offers its best customers new-car loans with a rock-bottom interest rate of 2.4% and promises to absorb paperwork costs when borrowers refinance a car loan by another lender.

[American Express](#) Co. chief financial officer Daniel Henry told investors Wednesday that "consumers have decided to deleverage more" and the shift in behavior is creating a challenge for the entire industry.

Many people say they feel worse financially, despite shedding debt. One big reason: The value of U.S. real estate has declined by more than \$6.6 trillion since late 2006, according to Fed data, prompting some Americans to feel like they are falling behind even as they tidy up their finances.

"We're not trying to jump-start the economy. We're trying to be better off in the long run," said Charles Allen, 33, of Crofton, Md., who owes \$350,000 on a house he could sell for only about \$300,000. "Instead of buying a big-screen TV or an Xbox, I'd like to be paying off this debt."

Mr. Allen puts cash in envelopes marked for food, car maintenance, clothes, home repairs and entertainment. He spends only that money, using any leftover to pay down debt. Once upon a time, he said, he used to toss credit-card bills into drawers, figuring he would deal with them later.

Carol Ford, a consultant who lives in Redwood Shores, Calif., pays an extra \$100 a month on her mortgage try to get a handle on the debt. "I realized I had been fooled by people having me refinance my house several times," she said.

Ms. Ford said she pulled out cash when she refinanced because she believed claims that it would be easy to refinance or sell her house at a higher price. "I fell for their blandishments," she said of lenders.

Joseph Kovar, a certified public accountant and financial planner in Danville, Calif., said two of his clients recently tapped their 401(k) retirement accounts to pay debts, even though Mr. Kovar advised them of the high tax penalties.

Another client got a large bonus that could have made it possible to buy a more expensive home. Instead, Mr. Kovar's client paid down a portion of a 30-year mortgage and refinanced to a 15-year loan. "People are not taking those excess funds and spending them," he said. "It's why we are ...treading water in the economy."

Samir Arsan of Redwood City, Calif., who works in commercial real estate, is trying to pay at least \$270 extra a month on his used-car loan. Once the \$10,000 loan is paid off, he plans to step up payments on his mother-in-law's mortgage and then the loan on his own home.

American households closed 103 million credit-card accounts. And credit-card payments exceeded purchases made with plastic by an estimated \$116 billion between the end of the first quarter of

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"This year, I've done well," said Mr. Arsan, 54. "But I don't know what is coming down the pike. I'm hoping to lower my debt service so I can survive any additional problems the economy might have."

He has no plans to replace his two cars: a 1998 van and 2000 Mercedes-Benz. He isn't alone. Nearby dealership Cammisa Hyundai boosted its repair staff from 10 to 14 employees last year.

Car sales rebounded to record highs for two months this summer, before settling back in September, said Ralph Walker, Cammisa's assistant service manager: "People are still coming in but it's more an absolute need for a purchase than a want for a purchase." He said more buyers pay cash.

For many Americans, the process of reducing debt feels like a marathon. Jason Jacobs, 32, of Richmond, Va., wants to move to Paraguay with his wife to become a Christian missionary and open a foster home. That won't happen until he pays down a chunk of more than \$180,000 in debt. He said that could take until the end of 2014 or longer.

The debts include \$4,000 in credit cards, \$30,000 for student loans and an \$8,000 loan for energy-efficient windows for his home. The windows, he said, were a mistake. Mr. Jacobs also hopes to shave enough off his \$139,000 mortgage to have equity in the property, which has fallen in market value since he bought it for \$150,000 in 2005.

To increase the odds of hitting his target, Mr. Jacobs is embracing a frugal life. He funnels about \$650 a month into shrinking loan balances.

Automated bank payments keep him disciplined. Mr. Jacobs keeps an envelope in a desk drawer that is allocated \$300 a month for food. He spends only what's in the envelope.

Soon, a new envelope will get \$160 a month for movies, clothes and other items. Instead of shopping at malls, Mr. Jacobs hunts for deals at secondhand stores or on websites like eBay and Craigslist.

"We've decided that we're not going to buy really new things," said Mr. Jacobs.

Abandoning the mortgage is out of the question, he said: "It's my responsibility to pay for it, since it was my decision to buy the house."

Write to Jon Hilsenrath at jon.hilsenrath@wsj.com and Ruth Simon at ruth.simon@wsj.com

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