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Consumer Debt Is Our Economy's Achilles' Heel

By JEREMY RIFKIN

With a single presidential debate left, I've been pondering what I would ask the candidates if I had the opportunity to pose just one question. So, here it is, Vice President Al Gore and Gov. George W. Bush:

Are you at all concerned about the mounting consumer debt spreading across every demographic sector of the U.S. population?

This past week, the Commerce Department reported that for a second month in a row, in August, Americans spent more than they made, plunging the savings rate into the negative category. The savings rate is now at its lowest level—0.2%—since monthly records began in 1959.

The fact is, the "American miracle" has, to a great extent, been bought on credit. It is impossible to understand the dramatic growth of the U.S. economy and reduction in unemployment in recent years without examining the close relationship that has developed between economic expansion, job creation and the amassing of record consumer debt. Credit card companies are extending credit at unprecedented levels. Millions of American consumers are buying on credit and because they are, millions of other Americans have gone back to work to make the goods and perform the services being purchased. The result is that the economy seems to be healthier than ever.

Today, according to the Federal Reserve, Americans are spending more than they are taking in, marking the first time since the Great Depression that the country has experienced a negative savings rate. Recall that just eight years ago, the average savings rate in the U.S. was 8% of after-tax income.

An analogous situation occurred in the mid-1920s, also a period of great economic change. Electricity replaced steam power across every major industry, greatly increasing the productive capacity of the country. Productivity gains, however, were not matched by a significant increase in worker compensation. Instead, wages remained relatively flat, while many marginal workers were let go in the wake of more efficient technology. By the late 1920s, American industry was running at only 75% of capacity in most key sectors. The fruits of the new productivity gains were not being distributed broadly enough among workers to sustain increased consumption and empty inventories. So banks and retailers extended cheap credit in the form of installment buying to encourage workers to buy more. By late 1929, consumer debt was so high that it could not be sustained. Even the bull market was being stoked by record purchases of stocks on margin (using brokers' credit). Finally, the house of cards collapsed.

The short-term substitution of consumer credit in lieu of increases in income and benefits has received little attention among economists. Still, the fact remains that great technology revolutions—like the substitution of electricity for steam power—generally spread quickly, once all of the critical elements are in place. The problem is that it generally takes at least a generation after a new technology comes on line for social movements to build enough counter-strength to demand a fair share of the gains.

The same phenomenon is occurring today. Productivity gains from the information and telecommunication revolutions are finally being felt and most major industries are facing global underutilization of capacity and insufficient consumer demand. Consumer credit has become a way to keep the economic engines throttled up, at least for a time.

Today, consumer credit is growing by a staggering 9% annually, and personal bankruptcies are increasing. In 1994, 780,000 Americans filed for bankruptcy. By 1999, the number had jumped to 1.28 million. Some economists argue that the negative savings rate is not really as bad as the figures might suggest, because millions of Americans have experienced record gains in the stock market. But many of the high-tech stocks Americans hold are over-valued and likely to be the subject of continued significant "readjustment" in the months ahead. Moreover, 90% of the gains of the stock market have gone to the top 10% of households; the bottom 60% of Americans own little or no stock.

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How long can Americans continue to spend more than they make, moving deeper and deeper into commercial debt? Any number of external events could tip the scale, with potentially calamitous consequences. If, for example, the energy crisis were to deepen or the stock market were to experience a sustained downturn or major lending institutions were to pull back on their loans, the effect on all of our lives could be sobering indeed.

The new economy won't be a reality until we have found a way to distribute the productivity gains of the e-commerce revolution broadly, to ensure enough consumer purchasing power to match the increases in productive capacity. In the past, that has meant an increase in wages and benefits and a reduction in work hours. But if we allow wages and benefits for middle- and working-class Americans to remain stagnant, as they have been for nearly a decade, and instead artificially prop up purchasing power by pushing them into debt, we may squander the opportunity to create a truly new economy that works for everyone.

It's unlikely that either of the presidential candidates will focus on the troubling specter of negative savings. Yet sooner or later, we may look back at the current "prosperity" with the same cynical regard as earlier generations did at the short-lived boom years of the Roaring '20s.

Jeremy Rifkin is the author of "The Age of Access: The New Culture of Hypercapitalism Where All of Life is a Paid-For Experience" (Tarcher/Putnam, 2000).