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America's debt safety-net

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Abstract

This article evaluates the often under analyzed relationship between transformations in US liberal welfare capitalism and the growth in household indebtedness. Using young adults (under-35s) and senior citizens (over-65s) as examples it consider how, alongside profound transformation in financial markets, important changes in the US liberal welfare capitalism contributed to households demand for ever-larger amounts of debt. Here, we focus on three key developments: (1) transformations in the labour market regime; (2) the promotion of asset-based welfare, and; (3) the use of debt as a safety-net. Young adults and senior citizens were affected by these trends in a multiplicity of ways but a common thread runs through the highly variegated experiences: rapidly rising indebtedness. Essentially debt became a panacea during this period; it was used to fund investment, consumption and as a safety-net. This suggests that transformations in the form and content of welfare capitalism are relevant factors when assessing the causes of rising household indebtedness. The credit-asset bubble may have occurred 'outside' the logic and processes of welfare reform but, nonetheless, were linked through the everyday practices of households which used debt to cope with changing welfare provision and instability in labour markets.

America's debt safety-net

Introduction

This article evaluates the rapid escalation of American household debt levels in relation to the changing dynamics of liberal welfare capitalism. Successive debates about the form, content, and purpose of welfare state reform outlined how different political traditions and institutional complexes shape reform measures. In the American case some emphasizes structural pressures, like globalization or the aging population (Schwartz 2007), as key factors creating the permanent austerity that challenge the survival of the post-war welfare state (Pierson 2007). Others emphasize ideational change brought about by neoliberalism or managerialism as instigators of welfare sate reform (Squires 1990; Clarke and Newman 1997). More often than not these detailed analyses and debates about the content and processes of welfare state reform only consider the potential effects on citizen's everyday life.

In contrast, this article takes as its starting point the outcome of rising indebtedness during the 2001-2007 credit/asset bubble and attempts to draw linkages with transformations in labour market structures and welfare state provisions. Rising indebtedness may have been an unplanned outcome of changes in the liberal welfare regime; nevertheless, rising debt levels are as much about government provisioning for households and practices in labour markets as they are about the machinations of financial markets. The credit-asset bubble may have occurred 'outside' the logic and processes of welfare reform but, nonetheless, were linked through the everyday practices of households which used debt to cope with changing welfare provision and instability in labour markets.

Therefore, alongside the profound transformation in financial markets that facilitated the 2001-2007credit/asset bubble there were also important changes in the US liberal welfare regime that contributed to households demand for ever-larger amounts of debt. Here, we focus on three key developments: (1) transformations in the labour market regime; (2) the promotion of asset-based welfare, and; (3) the use of debt as a safety-net. Households were affected by these trends in a multiplicity of ways but a common thread runs through the highly variegated experiences: rapidly rising indebtedness. Essentially debt became a panacea during this period; it was used to fund investment, consumption and as a safety-net.

Firstly, long term transformations in the US labour market regime led to slow income growth, employment insecurity and declining non-wage benefits. Persistently slow income growth resulted from the complex interplay between the exercise of economic governance by the state and trends within the private sector. The longstanding consensus on low inflation proved an important ideational shift in US economic governance (Temple 2000; Kirshner 2001; Blyth 2002; Widmaier 2007); it promoted dampening wage-led inflation through flexible labour markets and active labour market policies but also facilitated low nominal interest rates that fundamentally changed savings patterns. At the same time American business adopted a logic of 'permanent restructuring' entailing endless rounds of restructuring, downsizing and outsourcing while pushing hard against wage growth and cutting back on non-wage benefits.

Secondly, the vision of asset-based welfare became the guiding idea governing the liberal welfare regime during the boom years. With all asset classes on a long ascent the notion of an asset-owning democracy appeared plausible, as new access to credit and asset markets seemed to allow any individual to build long-term wealth. Pension policy became shaped by the notion of the American 'investor subject'(Langley 2006; Langley 2007) where individuals provided for their own future financial security by investing in asset markets. Of course, this mass investment culture was supported by low interest rates that decimated savings accounts and promoted investment-based savings products (i.e. mutual funds). Another key tenant of asset-based welfare was the financialization of homeownership (Aalbers 2008; Schwartz

2008). Housing was no longer about simply having a secure dwelling and long-term investment; homeownership became a vehicle for wealth creation and consumption as well as poverty reduction (through subprime lending). Francis Castles (1997) first explored the 'really big trade-off' between homeownership and welfare provision in the American context, but when combined with the effects of the credit/asset bubble it proved particularly problematic for many households. The 'home' is simultaneously a dwelling, a store of wealth and a reserve of cash (equity withdrawal). The home also contributes to wealth redistribution over the life-cycle and consumption smoothing and, as such, homeownership mimics many of the primary functions of the liberal welfare state (Castles 1997; Kemeny 2005). As housing became subsumed by the credit/asset bubble and the government came to rely on housing to provide welfare functions, the subsequent downturn damaged the financial security of many American households that used their primary residence as a form of social protection.

The guiding principle of asset-based welfare is one of the entrepreneurial individual that uses the new access to cheap credit to make sound and profitable investments. This notion extends beyond homeownership and retirement savings to include education and employment. Students get education loans as an 'investment' in higher future earnings and better jobs. Workers build investment portfolios to create wealth not available through wage-income and to protect against uncertainty.

When asset-based welfare was insufficient, debt became a safety-net for many households. Welfare state retrenchment created conditions where households used debt to replace eroding public provisions for social insurance and services. There is growing evidence that households are using debt to cover rising medical expenses and during times of unemployment (see: DeNavas-Walt, Proctor et al. 2003; Doty, Edwards et al. 2005; Sullivan 2008). In 2004, one-third of households reported using credit cards to cover basic living expenses, on average, four out of twelve months (Wheary and Draut 2005, p.11). Also, reduction in government funding for higher education contributed to rising cost and, as a result, a dependence on debt to access a university education. University education is not always included in analyses of welfare state provision; nevertheless, public universities in the US have long been regarded as a government service and funding cuts are usually justified through retrenchment logic. The inter-linkages between education, labour markets, and government funding provide sufficient basis for its inclusion as part of welfare state provisions. Therefore, most people can now only access the higher incomes, greater benefits and employment security traditionally available to university graduates by borrowing heavily.

These factors demonstrate how American households used debt to cope with slow wage growth, as a stop-gap during unemployment, to supplement roll-backs in non-wage benefits, and to replace declining welfare provisions and funding for government services. To examine these trends more closely we will focus on two different age groups: young adults (households with head under-35) and senior citizens (with head over-65) to show how rising indebtedness is linked to transformations in the US labour market regime and welfare state provisions.

One of the key purposes of the liberal welfare state regime is to support economic stability by smoothing out fluctuations in income and/or consumption of households, in particular for the most financially insecure. Whether its direct income transfers to the retired or unemployed or funding for higher education and skills training, liberal welfare capitalism serves as a vital buttress to economic growth and stability. Under this welfare regime young adults and senior citizens are a residual social stratum usually deemed politically worthy of a state support. Their links to specific forms of state support such as pensions, health care, or education provide a basis for considering the outcomes of changes in the liberal welfare regime. Moreover, young adults and senior citizens provide two interesting examples of the potentially long term negative effects of heavy borrowing during the recent credit boom. They illustrate how general economic trends, like low interest rates and welfare state retrenchment, manifest differently across age groups; but, also demonstrate remarkably similar trends of rising indebtedness and increased financial insecurity.

Importantly, the sheer level of indebtedness incurred by these two groups since 2001 undermines the prevailing 'life-cycle' assumptions that dismissed the negative consequences of extensive borrowing in a credit/asset bubble as merely a rational response to market conditions.[1] As a concept the life-cycle stage assumes a balance between income, assets, savings and debt changes across an adult's lifetime. According to the Life-Cycle Permanent Income Hypothesis (LC-PIH) model, the very young will have low incomes, limited savings and assets, and will borrow relatively more. As individuals acquire longer employment histories, income, savings and assets are assumed to increase. Upon retirement, individuals are assumed to go into a phase of dis-saving in which assets and savings are depleted to replace employment income. This also assumes stable levels of economic growth, labour markets with low unemployment, individuals with stable working careers and a numerical balance between birth cohorts. Policy makers used these assumptions to dismiss rising debt levels among the young adults and senior citizens as a predicable outcome of the life-cycle model, without considering the unique consequences of the credit/asset bubble that made both groups considerably worse off. Therefore, the aim here is to draw attention to the fact that your 'stage of life' is as important as the political and economic times you live in.

Age of Insecurity: liberal welfare capitalism and the credit bubble

Esping-Andersen's (1990) initial outline of the American liberal welfare state regime emphasized the importance of inter-linkages between employment policy, labour markets and welfare system. Over the past three decades the long-term cumulative effects of labour market and welfare reform substantially transformed it to a mere shadow of Epsing-Andersen's typology. Combined with the credit/asset bubble during most of the last decade Crouch (2009) and Young (2009) claim you get a form of *privatized Keynesianism*, where economic stability, effective demand and welfare provisions are intimately tied up with housing and undulations of capital markets rather than employment and production. In this sketch of the turn of the century the American economy's rising household debt is a function of depressed wages and easy credit. Earlier notions of a 'finance-led growth regime' (Aglietta 1998; Boyer 2000) also addressed how easy credit and liberalized markets offered a form of asset-based welfare to American households struggling with competitive labour markets and stagnating wages. Here access to credit provides the means for asset-based wealth gains in housing and the stock market, which provide the necessary additional income to make up for stagnating wage growth. This provides a mainly top-down framework of cause and effect between governance, market developments and households. By contrast, those using a liberal governmentality framework address how changes in economic governance sought to construct and impose notions of individual risk creating a culture for entrepreneurial investor subjects to flourish (de Goede 2004; Langley 2006; Langley 2007; Aitken 2008). The focus is mainly on the future financial security of households' aspect of welfare state provision, either through pension provision or housing wealth. In both structural and discursive accounts financial markets and asset-based welfare are seen as a direct substitute for welfare state services.

We change track from this line of enquiry by considering how rising household indebtedness is associated with changes in the form and content of American liberal welfare capitalism. We do so by looking at the experience of young adults and senior citizens over the past two decades to show how indebtedness has risen in step with transformation in the welfare state regime. The intergenerational dynamics of welfare reform and housing are typically framed in terms of conflict, be it in private pension funds, social security, public financing of government services or the winners and losers of the recent housing boom (Jensen 1995; Hamil-Luker 2001; Kohli 2002; Mortensen and Seabrooke 2008). The size of birth cohorts resulting from changing birth rates (for example the relatively numerous Baby Boomers compared with the decreasing birth rates of the last decades), interplay with economic assumptions about the income and wealth life-cycle. This creates a conflict where the young pay, often unsure if the same services will be available to them in the future, and the old benefit with no consideration of the fiscal implications.

Certainly young adults and senior citizens were affected in different ways by the recent credit and asset bubble but witnessed similar outcomes: rising indebtedness and growing financial insecurity.

The American labour market regime has undergone successive rounds of corporate restructuring supported by the ideational consensus in favour of global competitiveness (or neoliberalism more broadly). This effectively released the business community from its historical responsibilities to its employees. In the past, American corporations provided jobs, health care, pension plans, and even subsidized credit to its employees; which all contributed to the wealth and prosperity that embodies the vision of American economic superiority. Today, the American business ethos is one obsessed with continuous restructuring by shedding jobs, pushing hard against wage growth, and significantly reducing or eliminating non-wage benefits, like health care and pensions, for non-management workers (Cutler and Waine 2001). Young adults are usually in a comparatively weak position and make up the bulk of temporary or contract workers, making them vulnerable to job loss. Rollbacks in non-wage benefits offered by employers also particularly affect this group because health care coverage is very expensive for young families with small children. Similarly, senior citizens coped with cutbacks in non-wage benefits from employers, namely pension provisions and health care coverage for retired workers. In both cases the trend of reducing non-wage benefits meant less health care coverage and rising health care costs creating new impetuses to borrow.

One of the most significant developments in liberal welfare capitalism, particularly in the US, has been the explicit and deepening reliance of housing to provide social insurance, protection, wealth and long-term financial security. Castles (1997) and Kemeny's (2005) argue that a housing policy that promotes owner occupation hinders welfare state development because renters and owners have different sensitivities to taxes and interest rates. Schwartz and Seabrooke (2008) develop this typology further in their notion of 'Varieties of Residential Capitalisms' which demonstrates how housing finance systems also have important complementarities with the larger economy, including welfare state structures. In the US, recent pressures to curtail demands for social protection are closely related to increased pressure to promote a homeownership society (Schwartz 2008).

The long history of US housing policy and its fostering of the 'American Dream' (Wright 1983; Carliner 1998) was crafted by multiple government agencies dedicated to promoting homeownership as a panacea for everything from wealth-creation to neighbourhood renewal (Ronald 2008; Seabrooke 2010). America's recent residential property boom was made possible by financial innovation and regulatory changes alongside long-standing taxation policy that favoured homeownership by making mortgage interest payments tax deductible.

The inclusion of more detailed analyses of housing policy and financing to our understanding of different welfare state regimes provides additional avenues for investigating the outcomes of welfare reform. But, to date, the overwhelming focus has been on how housing is used as a form of wealth creation to substitute private and employment based welfare provisions. There has been comparatively little consideration of how the debt used to access homeownership or acquired against existing housing wealth also contributes to financial insecurity. During the recent housing boom young adults needed more leverage (or borrowing many multiples of income) to own a home because incomes did not keep pace with the rapid ascent of house prices. The current levels of leveraged investment, in addition to all the other forms of borrowing young families have, suggests owning a home may compound—rather than protects against—long term financial insecurity. This is in contrast to senior citizens who borrowed against the value of their homes, using them as ATMs to cash-out rising property values. The majority (60%) of senior citizen households earning less than $40,000 per year, who borrowed heavily against the equity in their homes because social security and savings income, no longer provided sufficient means to pay for rising health care and living costs (McGhee and Draut 2006).

Imperatives of fiscal restraint and retrenchment of public services has dominated Federal and State-level political agendas for over two decades (Folbre 1987; Burrows and Loader 1994; Peck 2001). The post-2001 credit/asset bubble masked many of the consequences of these reforms as easy credit mediated the effects of slow income growth, declining benefits and employment insecurity. These processes deepened the financial insecurity of young adults and senior citizens as debt is used as a safety-net in the face of rising living costs and unforeseen events. Most senior citizens rely on social security and Medicare and often debt replaced benefits that did not keep pace with the rising costs of health care and living expenses. Young adult's relatively weak position in the labour market, lower income levels, and ever dwindling unemployment benefits, meant debt is used as a temporary stop-gap because of limited access to publicly funded benefits. Many young adults also face rising education costs (Dēmos 2007), as governments no longer offer the same level of funding for a university education and have gradually removed social support for when they are unemployed. The rising costs of health care, education and lack of social support created conditions where debt is being used as a 'plastic safety net' (Draut 2006). For many households these processes converge when slow income growth, higher living costs, health problems, temporary unemployment or emergencies make recourse to debt a necessity *not* an option.

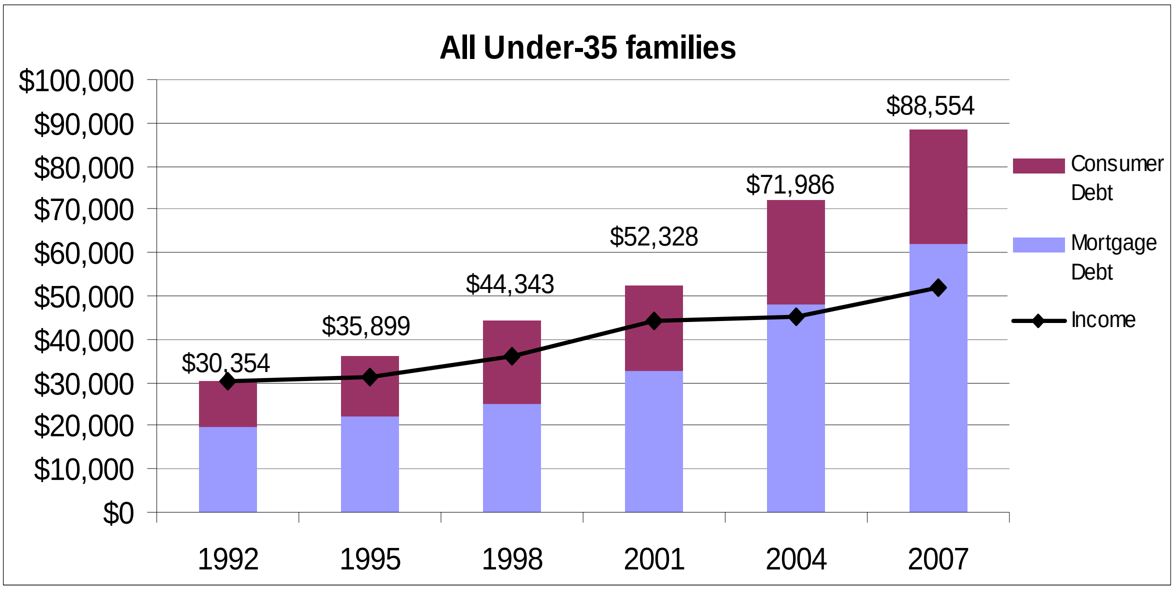
In debt to get ahead: Young adults in pursuit of financial security

High debt levels in the early stages of working life are all too often uncritically accepted as a necessity for young adults to begin building assets and long-term wealth holdings. The growth in overall debt levels, especially compared to income levels, since 2001 suggests that indebtedness is threatening—not aiding—young adults prospects for long-term financial security. Part of the problem is contextualizing young people's borrowing over their life time, where debt is seen as necessary and temporary when compared to the wealth gains that (might) be realized latter in life. Many see indebtedness as a necessary 'risk'. Today the sheer amount of debt now required to access homeownership and/or get an university education, two things previously considered standard middle-class entitlements and cornerstones of liberal welfare capitalism, undermines the commonly held life-cycle assumptions. These assumptions ignore the equally plausible possibility that high debt levels early in working life can intensify financial insecurity if indebtedness becomes a lifelong necessity. Especially if income, savings and assets never exceed cumulative debt levels or servicing costs create a sustained drain on income.

Young adults relatively weak position in the labour market as the 'new hire', temporary or contract workers makes them particularly vulnerable to job loss. Moreover, their lower income levels and limited time in the labour market creates a unique level of insecurity compared to other age groups. Many of the reforms to the US labour market regime, such as holding down wages, part-time flexible and contract work, have meant the working conditions faced by today's young adults are substantially different than those of the previous generation. For example, young adults are particularly hard hit by rollbacks in non-wage benefits offered by employers, especially heath care coverage, just at a time when many are starting families (Draut 2006). Without access to the same level of unemployment benefits and other welfare provisions today's young adults use debt to finance temporary short-term drops in income. A recent survey found that forty-five percent of under-35s reported using credit cards in the last year to pay for basic living expenses, such as rent, mortgage payments, groceries and utilities (Dēmos 2007, p.3).

The credit/asset bubble created a rapid escalation in debt levels carried by young adult households. Access to cheap credit mediated the effects of their weak position in labour markets and lack of public and private employment benefits. Young adults could, temporarily at least, continue consuming and living a lifestyle that became the norm in previous decades. In graph one, we see that throughout the 1990s average total debt outstanding tracks closely with average income levels and total debts increase by approximately $14,000. In the 2000s total debts outstanding increased by just over $44,000, or 215% for mortgage debt and 150% for consumer debt, compared to 70% growth in annual pre-tax incomes over the same period. Income levels may no longer be sufficient to pay housing, bills, and health care costs. This trend suggests that indebtedness will now be a pervasive feature of life for those who were young adults during the recent credit/asset bubble.

GRAPH 1: Young adults average outstanding debts and income



Source: *Survey of Consumer Finances, All families with head under 35, n=4010(1992); 4429 (1995), 4149 (1998), 4030 (2001), 3769 (2004), 3510 (2007)*

Getting an education is supposed to be one way young adults can improve their weak labour market position. In the US, your level of education is the single most important factor in determining potential life time earnings (Breen and Jonsson 2005) and is widely considered one of the most important things a young adult can do to ensure higher long-term financial security (Machin and Vignoles 2004). Of course the higher lifetime earnings figures are derived from data of the past thirty-years and may not be the most accurate predictor of the next thirty years. Also, this claim fails to account for a level of debt now required to complete university and the lower incomes for university graduates due to 'education inflation'. Or, how the growing number of college educated workers devalues the income gains achieved by the qualification which undermines the assumptions about the future benefits of higher educational attainment. The cultural and economic importance of a university degree as basic entitlement of middle-class children, or ticket to the middle-class for the poor, legitimizes borrowing heavily to get a degree as an acceptable risk.

Rising educational debt needs to be understood in the context of the long period of retrenchment in government funding and support for higher education. In 1992, the introduction of the unsubsidized federal student loan program was justified because a degree was seen as an investment and, since students were the primary beneficiaries of the higher incomes from education, they should bear the additional costs (Baum and O'Malley 2002). Much of the language used to justify student loans, and their corresponding higher debt levels, depicts educational attainment as an investment. The recent furore in the UK over higher tuition fees reinforced this rhetoric as higher costs were associated with the higher incomes university graduates can, supposedly, expect justifying debt as 'an investment' in future earnings.

Importantly access to credit prevents the more insidious problem of the rising costs inhibiting middle-class children from accessing higher education. The average inflation-adjusted cost of higher education has increased 165 percent between 1970 and 2005, and even public universities have tripled tuition fees since 1980 (Garcia, 2006; Dēmos, 2007a, p.2). At the same time funding for government bursaries, such as the 1965 GI Bill and the Higher Education Act, which guarantee affordable university education for all that qualify has not kept pace with the escalating costs of education. No federal administration or state legislature has addressed the intensifying problem of financial barriers to education; instead, credit has become the main vehicle for most students to gain access to a university education. The 2002 National Student Loan Survey revealed that over 70% of students agreed that student loans were very or extremely important in allowing them access to education after high school, while 72% said student loans were very or extremely important in allowing them to pursue graduate studies (Baum and O'Malley 2002).

TABLE 1: Young adults average income, debts outstanding, repayment for high school and college graduates

	High school diploma/GED			**College Degree**		
	Income	Total Debts Outstanding	Annual Repayment	Income	Total Debts Outstanding	Annual Repayment
1992	$25,619	*$23,068*	$4,228	$42,594	*$50,050*	$8,060
1995	$27,162	*$26,909*	$4,775	$42,560	*$57,752*	$8,034
1998	$30,099	*$31,280*	$5,247	$50,822	*$61,614*	$7,882
2001	$35,563	*$36,137*	$5,958	$67,736	*$86,958*	$11,612
2004	$35,026	*$45,361*	$5,881	$63,947	*$117,813*	$12,048
2007	$40,300	*$66,088*	$9,216	$77,844	*$149,389*	$15,059

Source: *Survey of Consumer Finances, selected families with head under-35, with High School Diploma n= 1318 (1992), 1516 (1995), 1294 (1998), 1358 (2001), 1201 (2004); 1110 (2007)With College Degree n= 1429 (1992), 1429 (1995), 1399 (1998), 1220 (2001), 1273 (2004), 1175 (2007)*

Table 1 compares the income, debt and repayment levels of under-35 households with a high school diploma and a college degree. As is expected, income levels for high school graduates are much lower than for college graduates, but the much higher debt levels for those with a college degree goes some way in offsetting the overall gains of getting a college degree. For instance, total debt outstanding for high school graduates is 150% of pre-tax income levels and 194% for college grads. In addition to education loans, university students are actively targeted for a plethora of credit products because they are regarded as more profitable by credit card lenders as they tend to hold revolving balances longer (Kara, Kaynak et al. 1994; Levesque Ware 2002). Credit card use among students is not just for consumer purchases: 27% of students used credit cards to pay for part of the costs of an undergraduate education, such as tuition or books (Baum and O'Malley 2002). Students extensive use of credit cards has become so prolific it is euphemistically referred to as 'yuppie food stamps' (Manning 2000). Carrying such high debt levels while at school adds additional financial pressures after graduation, when loan repayments begin. Most students graduate from university at 24 and will carry student loan debts well into working life. That being said, high school graduates still fare worse when it comes to income growth: 57% compared to 83% for college grads, over the two decades from 1992. So, getting a university education still ensures higher income levels and faster income growth, but it does not protect against long-term repercussion of the debt levels required to get a degree in the first place.

The overwhelming importance of homeownership to American households, as their only major asset and increasingly their key source of social insurance and protection, means getting on the housing ladder is an important element in establishing financial independence and security for young adults (Arnett 1998; Kennedy 2004). Rapidly ascending property prices, especially in major metropolitan areas where most young adults live, raised the bar for entry into the housing market. The problem of affordability was addressed by easier access to credit. Loosening mortgage lending requirements by allowing smaller down payments and calculating total mortgage amounts based on monthly interest payments (compared to multiples of annual household income) allowed bigger mortgages to match higher house prices. Slow income growth meant young adults used leverage (borrowing ever higher multiples of income) to get on the housing ladder. Also, since larger mortgage payments are tantamount to a bigger tax break the consequences of the rapidly inflating housing bubble were partially obscured. Easy credit did little to improve homeownership rates: according to the SCF under-35s owning a home increased by a meagre 4% from 1992-2007. Suggesting that homeownership was not extended to the previously excluded, rather the problem of access and affordability created by the property bubble was mainly solved by excessive leverage.

TABLE 2: Young adults average income, debts outstanding, repayment for owners and renters

	Own				***Rent***		
	Income	Mortgage Debt	Consumer Debt	Annual Repayment	Income	Consumer Debt	Annual Repayment
1992	$43,673	$53,395	$13,614	$10,531	$22,540	$8,999	$1,977
1995	$42,516	$57,800	$17,787	$10,807	$24,345	$11,684	$2,372
1998	$53,830	$64,168	$23,408	$12,424	$24,834	$16,796	$2,270
2001	$64,708	$81,478	$26,477	$14,995	$30,575	$15,443	$2,738
2004	$65,083	$115,475	$30,995	$15,967	$30,935	$18,986	$2,393
2007	$76,505	$152,656	$35,787	$21,129	$34,753	$20,077	$2,719

Source: *Survey Consumer Finances, selected families with head under-35, Own n=1465 (1992); 1806 (1995), 1335 (1998), 1416 (2001), 1401 (2004), 1355 (2007); Rent n=2545 (1992), 2623 (1995), 2814 (1998), 2614 (2001), 2368 (2004), 2155 (2007)*

Table 2 points to the ambiguities of leveraged homeownership, compared to renting, for under-35 in establishing financial (in)security. Homeowners have higher income than renters, but also considerably higher debt levels. In 1992, homeowners had average total debt levels equal to 153% of annual income; by 2007 total debt was 250%. Homeowners have higher consumer debt levels, potentially due to the additional costs associated with owning a home and/or the cost of servicing mortgage debts from take-home income, requiring greater recourse to consumer credit facilities for daily expenses (Sharpe 1997). Of course renters still pay living costs that are subsumed under mortgage payments for homeowners. One way to see the potential problems of borrowing heavily to buy a house, compared to renting, is the annual cost of servicing debts as claim against income: in 2007, average annual repayment for homeowners was $21,129, in 2007, and $2,719 for renters.

This suggests, rather than proves, the downside of homeownership and questions the degree to which leverage can foster long-term financial stability. If young adults must borrow significantly more to own a home, and thus subscribe to additional financial obligations, there is the possibility that such high debt levels early in life may create a life time of indebtedness rather than build wealth. Moreover, there can be little doubt that the current economic downturn and falling property prices will disproportionately affect the young as they got on the housing ladder in the midst of an asset-price bubble and are more susceptible to job losses.

Borrowing to live—Senior citizens struggle to stay afloat

Depleting savings and wealth holdings is expected when individuals retire from the workforce and no longer have access to regular wages. Yet the amount of savings and wealth holdings required to fund retirement is beyond the financial capabilities of most households. This is precisely why the US government, in 1935, created social security in order to protect the retired, as well as disabled and survivors (widows and orphans), from poverty and destitution. More recently, retired households also have access to savings, investments and company pension plans to supplement income after they have left the workforce. However, the specific political and economic conditions of the last decade meant senior citizens increasingly rely on debt to supplement stagnating social security payments, abysmal savings rates, poorly performing investment plans and roll-backs in company pensions. Most often, debt is incurred by borrowing against the equity in the home. With property prices rising, senior citizens, like many other families, used their homes as proverbial ATMs by cashing out some of the (higher) value of their property. But the costs of repaying these loans create new and often very high claims against their fixed-incomes: 'turning what should have been comfortable retirements into hand-to-mouth existences' (Punch 2003, p.36)

Slow income growth and the rising living costs unique to senior citizens is a key reason why their debt levels grew so quickly over such a short period of time. The low nominal interest rates that fuelled easy access to credit decimated returns from traditional savings accounts. Senior citizens tended to follow the general trend of transferring traditional savings accounts into market-indexed investment plans because they were widely considered the 'safest' or 'less risky' form of investment. Froud et al. (2010) simulated these effects and is worth quoting at length:

> The simulation therefore demonstrates how the decline in nominal rates of interest after 1980 (and in real rates from the early 1990s) was a great misfortune for modest income earners trying to save for retirement. The post-2000 Greenspan and post-2007 Bernanke monetary policies of stabilising and stimulating the US economy by reducing interest rates towards zero were then a catastrophe for low and middle income savers. Such policies completely undermine the rationale for long term saving through pension, insurance or deposit account because no feasible level of saving from limited income will generate a large enough fund (p.161).

Pronounced market downturns in 2001 and 2007, in which most household investment portfolios had only just made back what was lost six years previous, meant that the amount required to fund a comfortable retirement is beyond the reach of most income earners. The failure of financial markets to provide sufficient returns for retired households to live on is compounded by the Federal government's efforts to cap social security payments. Eighty-four percent of households aged 65 and over receive social security benefits, while 40% claim social security as their largest source of income (AARP Policy Research Institute 2006). As one of the largest expenditures in the US federal budget, social security benefits have steadily declined under the auspices of retrenchment. Faced with an aging population and a declining birth rate, successive US administrations attempted to 'plug the fiscal gap' by capping social security benefit pay-outs. To meet this end, the US government fundamentally changed how it measures the Consumer Price Index (CPI) with the explicit aim of saving $1 trillion by correcting the 'over-indexing' of social security from 1997 to 2007 (Boskin, Dulberger et al. 1996, p.15).

The largest components of senior citizens household expenditures are health care, prescription drugs, housing, fuel, and food—which have all had prices rising faster than the Consumer Price Index used to index their social security payments (Federal Interagency Forum on Aging-Related Statistics 2006; Purcell 2006). Senior citizens were adversely affected by the overall increase in health care costs over the past decade: paying health insurance premiums or uninsured health problems were listed as the biggest concerns among senior citizens (Employment Benefit Research Institute 2008). Many already retired households have had to accept the consequences of successive rounds of corporate restructuring seeking to reduce ‘legacy costs’ in company-sponsored medical coverage and pension plans. In 2003, only 38% of large employers offered medical coverage to retired employees compared to 66% in 1988 (Dēmos 2007, p.3). As private sector benefits declined most seniors became even more reliant on state support, such as social security and Medicare benefits, to maintain basic living costs. For low-income seniors dwindling state subsidies for Medicare means that without medical insurance they must contribute up to a third of their income to health care related expenses (Public Policy Institute 2003). Most often these expenses are for prescription drugs, which for those covered under Medicare still averages $860 a year in out-of-pocket expenses (Zeldin and Rukavina 2007). Gaps in health care coverage for the elderly leave many seniors to shoulder soaring medical expenses at a time when they are encountering more frequent, and serious, health problems.

Senior citizens are using debt to supplement the slow income growth which has not kept pace with the rising living costs unique to over-65s (Hurst and Willen 2007). Typically this took the form of borrowing against their primary residence. We can see the effects of home equity loans (HELs) by comparing ‘all families’ with heads over-65 (on the left) to those ‘with mortgage holdings’. While annual income levels for all families appears relatively healthy, this is mainly because the SCF over-samples wealthy households which tend to be older (Getter 2007). Also, mortgage debt levels are relatively small because most senior citizens own their home’s outright. Nevertheless, what we see is that throughout the 1990s average mortgage debt is below $9,000 but begins to increase rapidly post-2001 with the most pronounced increase between 2004 and 2007 (approximately $12,000) coinciding with the height of the credit boom. Even with the mediating effects of wealthy retired households, average total debts outstanding (which include both mortgage and consumer loans) was 30% of pre-tax income levels in 1992, and 52% in 2007.

TABLE 3: Senior Citizens average income, outstanding debt and repayment for all families and families with mortgage holdings

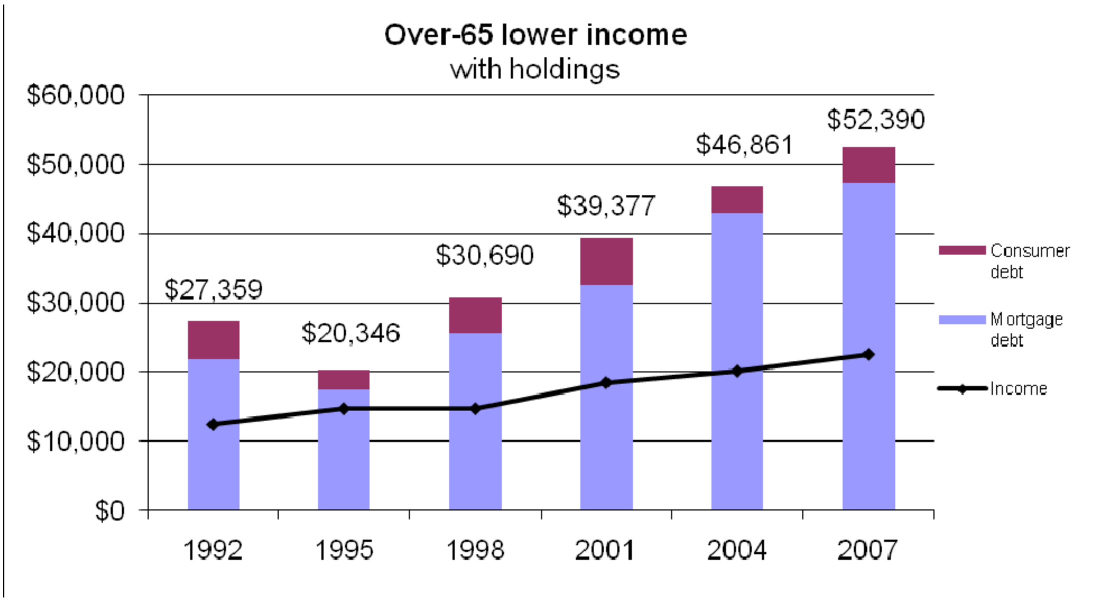
	All Families				***With Mortgage Holdings***		
	Income	*Mortgage debt*	*Total Outstanding*	*Repayment*	*Mortgage debt*	*Total Outstanding*	*Repayment*
1992	$26,593	$4,845	$7,902	$1,715	$33,937	$41,285	$8,678
1995	$32,569	$5,700	$8,136	$1,786	$34,245	$39,731	$8,001
1998	$38,153	$8,953	$12,382	$2,755	$46,803	$58,298	$11,445
2001	$47,419	$13,018	$17,064	$3,346	$62,188	$71,331	$13,008
2004	$50,179	$17,996	$30,189	$4,105	$71,004	$83,743	$11,311
2007	$68,792	$30,060	$36,023	$5,441	$106,116	$117,897	$16,130

Source: *Survey of Consumer Finances, households with head over 65: All families n=4520 (1992); 4705 (1995) 4515 (1998), 4540 (2001), 4401 (2004), 4800 (2007); With Holdings n=749 (1992), 890 (1995), 922 (1998), 963 (2001), 1134 (2004), 1372 (2007)*

The right side of the table isolates only those over-65 households with loans secured against the primary residence. Throughout the 1990s, mortgage debt levels grew by around $17,000, but the most rapid growth is post-2001, with debts increasing by $44,000. Moreover, by including consumer debts in the total outstanding debt category it becomes clear that other debt sources contribute to staggering levels of indebtedness for people who largely live on fixed incomes and are without full-time employment. Average annual debt repayment amounts are three times higher for families with mortgage holdings compared to all (over-65) families.

Graph two shows the average income and debt levels for the 60% of over-65 households that earn less than $40,000 in pre-tax income. Average income levels increased by $10,000 over two decades, while average total debt levels grew by $25,000 over the same period, suggesting senior citizens supplemented their minimal income growth with new debts, especially after 2001. Average mortgage debts grew much more than consumer debt, but average total debt outstanding reached a staggering 233% of pre-tax income levels in 2007. The cost of servicing these new loans creates additional claims against largely fixed-incomes: in 2007, the annual cost of debt repayment was equivalent to 36% (or $8,200) of annual pre-tax income levels.

GRAPH 2: Senior Citizens average income and outstanding debts for households that own home and earning less than $40,000



Source: *Survey of Consumer Finances, selected households with head over-65, with mortgage holdings and earning less than $40,000 (Bulletin Categories 1 and 2), n=171 (1992), 194 (1995), 213 (1998), 236 (2001), 316 (2004), 333 (2007)*

The easy credit conditions post-2001 facilitated many over-65 households with fixed incomes to borrow against the existing equity in their home, or even more problematically, against the inflated value of their home because of the property bubble. The credit market for senior citizens has grown so large that the retail credit industry has developed new debt collection strategies to target the emotional vulnerabilities of elderly people, such as persistent phone calls and debt collection notices, with the aim of selling additional third-party products like second mortgages and viaticles (Punch 2004). Pressures to make repayments on outstanding debts is often used to compel senior citizens to agree to viaticles–which involves the selling of life insurance to third parties for one-off or monthly payments (Vincentini and Jacques 2004). But it was not only HELs, senior citizens became an extremely lucrative market for all types of credit providers because their fixed incomes make them more likely to revolve balances and stay in repayment status longer (Mathur and Moschis 1994; Lichtenstein, Chen et al. 2003). Therefore, the overall effect of rising living costs, stagnating private sources of income and declining state support has been a growing reliance on debt to bridge the gap between income and the cost of essential goods and services.

Conclusion

This article highlights the cumulative effects of transformations in the American labour market regime, welfare state retrenchment and the homeownership welfare trade-off—combined with the effects of the credit/asset bubble—in contributing to young adults and senior citizens using debt as a safety-net. These conclusions extend the analysis of the causes of indebtedness beyond the creditor-debtor relationship to include the continual re-structuring of public and private provisions for social protection and benefits. Exposing how transformations in labour market structures and welfare state regimes are relevant when assessing the causes of rising indebtedness in the household sector.

By moving beyond framing the excesses of the recent credit bubble using the narrow conception of the creditor-debtor relationship we see that a wide cross-section of American society was made significantly worse off. It is important to recognize that debt-financed consumption did a great deal to fuel US economic expansion during the boom years (Montgomerie 2009). For all the rhetoric that rising household debt levels signal a loss of prudence and the abandonment of thrift as the cultural guideposts for sound family finances, regular use of debt to transcend the limits of income became the lifeblood of the US economy. Without it, American households could no longer be the 'consumers-of-last resort' for all globally produced goods, while governments and the business community would have to face the political fallout from the destruction of the American way of life. Therefore, it is not that debt is being used, rather how and why. Here we saw how debt supplemented slow income growth by leveraging in order to buy a home or deplete home equity holdings, funded daily consumption, and substituted for declining government and employment benefits such as paying for medical bills, as a stop gap during unemployment, or funding a university degree.

The 2007 financial crisis not only exposed the failure of liberalized financial markets but also the broader politics of abandonment that leaves the poor, the old and the young to cope with the failings of the American economy and political system through unsustainable borrowing. Too often private debt is replacing public provisions for social stability because the American government and business community absconded from their responsibilities to workers, citizens, and systemic economic stability whilst continuously depending on workers/consumers to drive economic growth. Rising asset prices and skyrocketing profitability blinded many to the large cracks already present in the edifice of financialized expansion. Free-market logics framed easy credit as a step toward greater financial inclusion for groups previously excluded from mainstream financial services. Credit scoring was heralded as proof of the efficiency and expertise of financial markets to adequately price risk. The prevailing ideological assumptions saw escalating debt levels as part of the wealth-effect and believed that households were acting as rational calculating agents astutely using debt to acquire new assets. In the same way life-cycle assumptions dismissed the rising indebtedness of young adults and senior citizens ignoring the systemic threats of driving already financial fragile groups further into debt through extensive lending. Dislodging this economic rationale and disentangling the intricate links that bind financial markets to the everyday coping strategies of households is proving more difficult than organizing successive bailouts for the financial services industry.

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[1] It is important to note at the offset that this article does not offer an intergenerational analysis. Basic age categories of under-35 for young adults and over-65 for senior citizens were drawn from the Survey of Consumer Finances (SCF) to observe income and debt trends over the past two decades. The SCF is a cross-sectional not a panel survey preventing any concrete conclusions about intergenerational differences.

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