

THE CONSUMER MOVEMENT IS ALIVE AND WELL

Anwar Fazal*

ABSTRACT

The President of the International Organization of Consumers Unions in a letter to Dr. Colston Warne traces the growth of the consumer movement and speaks of the beginning of the 'fourth wave' of the movement, its demonstrated ability to give a multinational response to multinational issues. He speaks of the growth of the movement in developing countries and the growth of networks around pesticides, pharmaceuticals, infant foods and the dumping of hazardous products.

The consumer movement everywhere owes a great deal to Dr. Colston Warne. I owe him a great deal too for letting me walk with him during my first days in the consumer movement.

I also owe Dr. Warne a letter. Last night, I wrote that letter and I like to share it with you.

"Dear Dr. Warne

In 1934, nearly 50 years ago (7 years before I was even born), you said, 'It is likely that nothing short of a revolution will substantially alter the character of the business system or its ally, advertising.'

I like to let you know of the state of that revolution:

- o that revolution began here in the U.S. in the 1900s, the so-called 'Progressive' era, marked by the work of Dr. Wiley and 'his poison squad', Upton Sinclairs' 'The Jungle' and which culminated in the Pure Food Law of 1906;
- o that revolution that had its second wind in the 1930s, the 'New Deal' era marked by the work of Chase, Schlink and Kallet, the most significant event of which was the founding in 1936 of Consumers Union, now the world's largest consumer organization;
- o that revolution that burst out a third time with great excitement in the 1960s, marked by the work of Kefauver and the world's best-known consumer advocate, Ralph Nader, and the founding of the International Organization of Consumers Unions. Perhaps, the most stirring and hopeful event of that era was the speech by the late President J.F. Kennedy on the rights of consumers, a speech made exactly 21 years and 2 days ago - March 15. On that date groups from as diverse countries as Fiji, Finland, India, Hong Kong, Spain, the United Kingdom and a host of others celebrated for the first time this year Consumer Rights Day.

*President, International Organization of Consumers Unions.

Dear Dr. Warne, all this is familiar to you. More than that, you were so much a part of it. We need continuously to be reminded of the past, the struggle, of the starts, the bursts and the busts, the excitement, the victories, the dashed hopes. We need to celebrate more victories, and we need to learn from our failures.

Dear Dr. Warne, the eighties are seeing the beginning of a FOURTH WAVE in the consumer movement - a period during which the movement has become really global, being able to give an effective multinational response to multinational issues; it has also tasted its first major victory at the global level, a victory of health over profits, a victory that involved the protection and promotion of a natural, superior, product - breastmilk. The International Code for the Marketing of Breastmilk Substitutes, which was passed on May 21, 1981, is the first global consumer protection code.

Yes, Dr. Warne, the consumer movement is alive and well.

The struggle for the control of reprehensible and often irresponsible marketing has spawned new global networks; it has seen an explosion of interest in our work. It has drawn together groups from churches and unions, feminist groups and professionals; it has given us this nation's largest non-union boycott - that of Nestle's products, and the first global consumer boycott of its kind - a boycott very critical to the success of the campaign to protect and promote breastfeeding.

This work on breastfeeding is being coordinated by a global network called the International Baby Food Action Network (IBFAN).

New networks exist around pesticides, around pharmaceuticals, around the export of banned and severely restricted products - Pesticide Action Network (PAN), Health Action International (HAI) and the Consumer Interpol.

The consumer movement has begun to excite, to interest and to involve ordinary people in a way unprecedented in our short history. Diverse organizations are building on the strength of weak links, creating decentralised participatory structures, unencumbered by bureaucracy, which enable the maximum output of citizen groups spread throughout the world and united in a new form of solidarity. There are now, for example, efforts for global codes and other measures to put an end to unethical and harmful practices in the pharmaceutical and pesticide industries.

And consumer groups are linking the Third World with the First World, sharing and acting together.

Research in the United Kingdom shows a sonic mosquito repellent to be useless, if not dangerous, because of the false security it may give to people in malaria endemic areas. The information flows through telex machines to the headquarters in Penang, Malaysia, of Consumer Interpol, the popular name of a global citizens system of alerts on hazardous products. In Indonesia, the government on receipt of the alert from its consumer organization, bans the product!

Yes, Dr. Warne, the consumer movement is alive and well.

Take the ten largest nations in the developing world which together have a population of 2.4 billion. The representative of the People's Republic of China at the first United Nations Consultation on Consumer Protection stated: 'It is the sacred right of consumers to be protected.' India, the second largest nation of the world, has 27 consumer groups, Brazil has 62, Thailand has seven, the Philippines has four, Nigeria has three. Pakistan has one and Bangladesh and Indonesia have among the most active groups in the developing world. In Mexico, the media give out 10,000 consumer protection and information messages a day (one of my favourite messages is 'give affection, don't buy it'). The new Spanish and Korean constitutions enshrine the rights of consumers.

Yes, Dr. Warne, the consumer movement is alive and well.

But our work has just begun and we have miles to go, and like that, I guess, of the Kansas cowboy of the old days, the consumer advocates' work will never be done.

We live in a world in which 50,000 people die each day from lack of clean water and sanitation, while each minute the world spends US\$1 million on arms, on guns, bombs, tanks, missiles.

Yes, Dr. Warne, the whole world is not that much a better place - we sometimes redistribute our problems, solving one, creating another. Violence, waste and manipulation have become profitable for the merchants of death, the rapists of the earth and those who manipulate our behaviour, our fears and desires.

Yes, Dr. Warne, the whole world is still too much a Sinclair's jungle; Kallet and Schlink would today probably write '4 Billion Guinea Pigs'. Yes, much of the world is still a dark marketplace - a marketplace in which there is too much VIOLENCE.

It has been estimated in a recent book 'Prescriptions for Death' that pharmaceuticals may be responsible for a minimum of 10 to 15 million cases of injury and one million deaths each year among the 3 billion people in the developing world. Conservative figures suggest at least 375,000 people in the Third World are poisoned yearly by pesticides and, of them, at least 10,000 die because of pesticides that are very often not permitted in the countries of

origin.

We live in a marketplace in which there is too much WASTE. No figures will be enough to describe the wanton destruction and misuse of resources, of processes, of products in our society. We see the destruction of the tropical forests and the waste of meagre incomes by poor people in the Third World on useless, inappropriate products - products they do not need nor can afford. In Bangladesh, it was once said that the bulk of the vitamins bought were purchased by people who did not need them and they mostly were excreted as urine - vitamised urine is a luxury that Bangladesh can do without!

We live in a marketplace in which there is too much MANIPULATION. Probably one of the greatest behavioral changes occurred in the way in which the natural, unbeatable, self-reliant method of feeding babies with milk from the mothers' breasts was subverted and supplanted by two kinds of so-called 'modern technologies' - the technology of processed cows' milk and the technology of marketing. We see pervasive manipulation of people's behaviour through advertising and promotional tactics that border in certain industries on the criminal and immoral - offering bribes, from ballpens to women. The subversion of breastfeeding itself has been associated with health problems among 10 million infants a year. James Grant, Director of UNICEF, has said that if we can protect and promote breastfeeding we can save the lives of one million infants a year!

This fourth wave has its books too, among them:

- o 'The Circle of Poison', by David Weir and Mark Schapiro;
- o 'Bitter Pills', by Dianna Melrose;
- o 'A Growing Problem', by David Bull;
- o 'Prescriptions for Death', by Milton Silverman, Philip R. Lee and Mia Lydecker;
- o 'Drug Diplomacy', by Charles Medawar and Barbara Freese;
- o 'The Health of Nations', by Mike Muller;
- o 'Pills, Pesticides and Profits', by A. Karim Ahmed, S. Jacob Scherr and Robert Richter;
- o 'Tomorrow's Epidemic: Tobacco in the Third World', by Mike Muller.

Dr. Warne, I know you are too gentle to use harsh words and show anger. And I believe, as you do, that our means must be as humane as our ends. We both value the precious model that enables true participation of citizens in organizing our social, economic life in dignity and in safety. But sometimes you cannot but be angry.

Dr. Warne, the United States stands for many precious and valuable things. In the last few years, this precious model has been demeaned. An executive order on the subject of the export of banned and severely restricted products lasted 34 days. A measure that would have recognised a serious social responsibility by the world's greatest power that recognised human rights was dismantled. There were reports of millions of dollars being offered to government officials of very corrupt governments, to store hazardous

wastes. The Third World can become ignorant recipients of your Love Canals and your Times Beaches.

When the International Code for the Marketing of Breastmilk Substitutes was passed at the World Health Assembly on May 21 1981, 118 nations voted for it, one nation voted against it - that government was the United States!

When on December 17 1982, a few months ago, the United Nations General Assembly voted on international actions to help overcome the problem of dumping of hazardous products through the establishment of central list of such products, 146 nations, including every developed country in Europe, voted for these simple first steps. One government and only one government again voted against - the United States of America.

Dr. Warne, you will remember how Consumers' Union and yourself were subject to harrassment during the McCarthy era. The same evil methods are becoming visible again. There are attempts to colour the consumer movement as anti-free enterprise and recently your representative to the United Nations warned of an 'iron triangle' when talking to the American Enterprise Institute. She talked of the 'emergence of an iron triangle' uniting non-government organizations, Third World governments and ideologically sympathetic international bureaucrats in quest of international health and safety regulations. The Heritage Foundation, based in Washington, D.C. has recently made sinister innuendos about IPCU.

Dr. Warne, they lost when they tried such red baiting tactics with you and the Consumers Union and surely they will fail again because the truth is on our side.

And, Dr. Warne, that they pay this much attention must surely encourage us. We must be having an impact, we must be doing all right.

Yes, Dr. Warne, the consumer movement is alive and well.

You showed the way through fearless courage, through innovation of the science of consumption, through decades of stamina. Today, your work is continued in the halls of academia, when our work is considered worthy of study; our work is continued in the halls of the highest levels of governments of the world, in the forums of the United Nations, when we have achieved the dignity of resolutions, reports and even been rewarded with a Code.

It is being continued in the boycott of Ciba-Geigy's products by Swedish doctors, because of the marketing of the drug Clloquinol, banned there and in the United States, but still widely available in developing countries. It is being continued in the many thousands of people in the US and eight or so other countries where products of Nestle's (e.g. Taster's Choice) are being boycotted because of their non-acceptance in full of the WHO Code on the Marketing of Infant Formula.

These activities and those of the global networks of IBFAN, HAI, PAN and Consumer Interpol, will continue to be the cutting edge of the consumer movement. The precious work of information through testing and research will continue to give us that power to buy or not to buy and the work of public interest law groups will make laws more open and responsive to people's needs.

Dr. Warne, under your leadership, Consumers Union gave birth not just to IOCU but also very much to ACCI. ACCI represents an intellectual blood bank that is unsurpassed in the world. The reservoir of professional talent, of knowledge of skills in the field of consumer protection cannot be beaten. They have honoured you for your pioneering work. My hope is that more of them will walk the paths you have walked, that more will display the courage and stamina that you have displayed. My hope is that they will see the link between their work and the problem of consumers everywhere,

- o that an international dimension will become part of their consumerist personality,
- o that they become involved in the new exciting fourth wave not just for selfish professional reasons, not just for charity towards poor, helpless consumers in deprived countries, but because we share one earth, breathe one air, rise from one ocean - a fragile structure that calls for a new responsible consumption,
- o that they will become aware that when we are talking about consumer rights, we are talking about human rights, about precious norms for a decent life with dignity.

If the consumer movement is to be competent and relevant to these times, these challenges have to be taken. In this new paradigm, in this fourth wave, we must recognise not just the cost of living but as much the cost of survival, not just value for money but as much value for people. We have to see both the faces of high prices - the high price that hurts our pockets and the high price we pay in health, damage to our environment.

I am confident, Dr. Warne, that many more Americans will follow your footsteps and the American consumerists will rise even more strongly to help in that revolution for a more responsible consumer society that you talked about nearly 50 years ago.

Thank you, Dr. Warne, for everything. I promise to write again. Take care of yourself.

With warm regards

Anwar Fazal
President
International Organization of Consumers Unions.

P.S. Rhoda Karpatkin of the Consumers Union will be talking tomorrow about IOCU and its work. I hope many will attend that session and talk about concrete ways to strengthen

the power of consumers."

Dr. Morse

Thank you. Thank you very much for this opportunity to read this letter in lieu of delivering a lecture.

Thank you all for your patience and God bless.

MAJOR CHANGES AFFECTING CONSUMERS AND CONSUMPTION

Benjamin Senauer, University of Minnesota¹

ABSTRACT

This paper analyzes four major changes in our economy and society which affect consumers and their consumption. The major trends examined are the changing age structure of the population, the increasing diversity in family living patterns, the growing number of women employed outside the home, and the greater economic uncertainty confronting consumers.

Significant structural shifts have been occurring in our society and economy that have far-reaching implications for American consumers and their consumption. This presentation will focus on four major trends: the changing age structure of our population, the growing diversity of family lifestyles, the increased participation of women in the labor force, and the greater uncertainty of the economic environment. Most consumers have been directly affected by one or more of these changes. All of us are being affected by the broader social and economic impact of these factors.

CHANGING AGE STRUCTURE

The most significant trend in this area is the greying of our population. This change is related to two factors: the increased number of elderly among us and the maturing of the baby-boom generation, who have begun to enter middle age.

Between 1946 and 1964, 75 million children were born. Births rose from 2.9 million in 1945 to over four million in 1955 [5]. These baby-boomers, who are now 18 to 36 years old, account for one-third of the total U.S. population [9, p. 14]. What adds to the impact of this generational bulge is that the boom was followed in the late 1960's and early 1970's by a baby bust. Between 1965 and 1975, the fertility rate, the number of annual births per 1,000 women age 15-44, fell from 96.6 to 67.6 [16, p. 25]. This surge, then decline, in births has produced a cyclical pattern with enormous implications for consumption activity.

The demand for both private and public goods and services grows and shrinks in relation to the age profile of the population. The effect of the baby-boom generation on the age structure has been likened to "a pig in a python" [5]. The baby-boomers produced a tremendous surge in the number of primary, then secondary, then college students as they grew up. More recently the demand for primary, and then secondary, education has declined as the baby-bust generation has moved through the schools. Many suburban school districts have schools which were built during the early 1960's and then closed in the late 1970's. Higher educa-

tion is now just about to feel the impact of the decline in births which occurred in the 1960's. The college-age population is predicted to decline by over 20 percent during the next several years.

Over the last several years the baby-boomers have been swapping their rock concert tickets for cribs and diapers. The baby-boom generation has begun to settle down, and in many cases start to have their own children. We now, in fact, are seeing a baby boomlet, which is an echo of the baby boom. The fertility rate among women of child bearing age has not risen significantly, but the sheer number of women of child bearing age has produced a rise in the number of births. Consequently, the number of primary school students is starting to rise, again.

As the baby-boomers mature, the demand for the products and services utilized by the middle-aged is increasing, which would include banks, stock brokerages, and optometrists. The aging of the baby-boomers has produced many easily recognizable shifts in consumer marketing strategies. Much of McDonald's advertising of its fast-food places now appears to be aimed at families with young children rather than teenagers. The Levi Strauss Company has added sport coats, and even suits, to its product line. These are just two examples of the reaction of business to the decline of the youth market. Even ski resorts are trying to change their image and attract couples with children as opposed to the young and relatively carefree. Over the last decade the average age of skiers has jumped from 23 to 28 years old [14].

The other major factor behind the age structure's shift is the increasing number of elderly. Between 1960 and 1980, the overall population of the U.S. rose by 26 percent [21, p. 10]. During that period the number of persons age 60 and over increased by 50 percent to 35.6 million, those 65 and over by 61 percent to 26.8 million, and those 75 and over by 77.3 percent to 9.9 million [23]. Contrary to popular belief, most of the elderly are reasonably well-off financially, and some are very well-off, which makes them an increasingly important factor in consumer expenditure. For example, only 4.5 percent of the households headed by someone 65 and over were below the poverty level in 1979, when money income and the market value of in-kind transfers were counted. The same poverty figure for all households was 6.4 percent [19].

Since the average retiree lives a longer number of years in better health than in the past, they have had a considerable impact on industries related to recreation and leisure time. Retirees have also been a substantial factor in the redistribution of our population toward the Sunbelt. The increased number of elderly has probably had its most significant impact on the demand for health care. Health expenditures increased from 5.3 percent of the Gross National Product (GNP) in 1960 to 9.4

¹Associate Professor, Department of Agricultural and Applied Economics

in 1980, at a level of \$247.2 billion [21, p. 9]. The elderly, of course, are not the only factor behind this increase, but they are a major one.

Many of our older senior citizens, more of whom are women, require special support services. Women can be expected to live about eight years longer than men, which has added significantly to the number of single-person households, a topic that will be explored further in the next section. Widowed persons account for 13 percent of all households and most of them are widows, rather than widowers [15, p. 26].

In the future, the number of elderly will swell enormously when the baby-boom generation starts to reach retirement age. By the year 2020, projections are that 60.7 million Americans will be 60 years old and over [23, p. 7]. Just as the sheer number of baby-boomers created a youth culture in the 1960's, in which businesses that served the young, such as fast-food hamburger chains flourished; the next century may see a geriatric culture, in which those enterprises that serve the elderly prosper.

GREATER DIVERSITY IN FAMILY LIVING PATTERNS

In the 1950's and early 1960's, the ideal American family was presented as being composed of a husband, a wife, who stayed at home, and at least two, but better yet three or more, children. This was the family type featured in the commercials and television programs of the time. In the latter category, such programs as "Father Knows Best" and "Leave It to Beaver" come to mind. Obviously many households did not conform to this idealized pattern even then, but there has been a marked increase in the diversity of American family lifestyles in the period since.

A few statistics will dramatically emphasize this point. Out of the 80 million households in the United States in 1980 only 24.5 million were composed of a married couple with one or more children under age 18 [21, p. 47]. The number of single-person households has climbed from 6.9 million in 1960 to 17.8 million in 1980, and they now account for over one-fifth of all households [21, p. 46]. Families headed by women with no spouse present accounted for 9.3 percent of all families in 1960 and 14.6 percent in 1980, when they numbered 8.5 million [21, p. 48]. The proportion of children under 18 living with their mother alone has doubled since 1960.

The U.S. is splitting into smaller size households. Average household size declined by 17 percent between 1960 and 1980 from 3.33 to 2.75 persons [21, p. 44]. Recently there are indications that economic factors, the high cost of houses and mortgages, and climbing rents have caused more persons to live under the same roof. Children in their 20's are continuing to live with their parents and the elderly are moving in with their sons or daughters. Once the current recession is over, the basic trend will almost certainly be reasserted, though.

The changing patterns of family life have definite implications for consumer demand. Partly for financial reasons, but also because smaller families do not need as much space, newly built detached housing is shrinking in size. The increased number of one and two-person households is a factor in the growing popularity of condominiums and apartments. Campbell's now offers soup in a single-serving size.

If the household mentioned above was the ideal of the 1950's and early 1960's, then their dream, frequently fulfilled, was to live in a newly constructed suburban house and be able to purchase a new car as frequently as their neighbors. A recent study, "The Engines of Postwar Economic Growth", emphasizes the symbiotic relationship of highways, suburban housing, and automobiles as a crucial dynamic element in American economic growth [2]. Part of the economy's current structural problem is that although the auto-highway-housing relationship has weakened as an engine of growth, a replacement of the same magnitude has not yet developed. However, the fields of high technology and information, including education and services, particularly in the medical area, are increasingly playing the crucial dynamic role in our economy.

This country has always had a surprisingly inequitable income distribution. The top 20 percent of families, in terms of income, received 41.6 percent of the aggregate money income in 1979; whereas the bottom 20 percent received only 5.3 percent [21, p. 438]. The greater diversity of family types may be exacerbating this problem. Consider the likely difference in economic circumstances of a dual-earner professional couple without children, and an unskilled, single mother with three young children. The proportion of married-couple families below the poverty level is just 6.8 percent. However, for households headed by women with no spouse present 34.6 percent are below the poverty level [17, p. 31].

The decline of traditional family lifestyles should not be overstated, though. Traditional family patterns are still the norm. Seventy-three percent of the population lives in households headed by married couples, although the number is down from 82 percent in 1970. Three-fourths of all children under 18 live with both parents, although the number is only 42 percent for Blacks [18, 21, p. 49]. Americans are still a people that cherish family life. And the family/household unit remains the basic consumption entity within which income is pooled and consumer decisions are made.

INCREASED LABOR FORCE PARTICIPATION OF WOMEN

The rate of movement of women into jobs outside the home has been phenomenal. Today, a majority of women are in the work force. Labor force participation by women increased from 37.7 percent in 1960 to 51.6 percent in 1980 [21, p. 381]. Women now comprise 43 percent of the total labor force [21, p. 381]. Moreover, the trend has been particularly marked in recent years among married women and women with children. There are now more

wives with jobs outside the home than full-time homemakers. For married women with their husband present, labor force participation climbed from 30.5 percent in 1960 to 50.2 percent in 1980. This figure has reached 60.1 percent for married women between 25 and 44 years old. For married women with their husband present and one or more children less than six years old, labor force participation has more than doubled since 1960, going from 19 to 45 percent in 1980 [21, p. 388].

These changes have significant implications for the economy, the home, and the types of products and services demanded by consumers. In particular, Gary Becker added the concept of a time constraint to the household's budget constraint. He also showed the importance of the value of an individual's time in explaining consumer behavior [1]. The woman, who is employed outside the home, has extremely heavy demands made on her time, especially if she is a mother with children at home. Her working time, on the job and at home, may well be in excess of 60 hours per week. Employed married women cut back somewhat on their hours of housework, but still retain primary responsibility for the operation of the household. In 1975, the average number of hours per week of housework was 44 for unemployed married women and about one-half as much for those employed [7, p. 11].

These circumstances help explain the increased demand for products that either economize on time in the household or provide commercial substitutes for household activity. The microwave oven, whose primary attraction is the reduced cooking time, is an example of the former. Day care for children is an example of the latter. There were 7.5 million children needing care during the day in 1980. Estimates are there will be 40 percent more young children with employed mothers by 1990 [3]. Companies, such as Children's World and Kindercare, have sprung up to meet this demand. During this recession with its high unemployment, though, many day care centers have seen enrollment declines [10]. Interestingly, speciality stores and catalog firms appear to be other beneficiaries of the increased work force participation of women. Working women, who have more money and less time, appear to buy more by mail and at speciality shops, not having "time to run around the mall" [4]. And, of course, the increased consumption of convenience foods and meals away from home are a well-known consequence of these factors.

Twenty-two percent of employed women held professional and managerial positions in 1978 [7, p. 13]. Many of these women are members of a dual-earner household, in which their spouse is frequently also a professional. The combined salary of two professionals produces a household with a relatively high income level, which can often afford considerable discretionary spending. Young women, in this group in particular, have delayed marriage and delayed, or decided against, children. Nearly three-fourths of the women 20 to 24 were married and one-half had children in 1960; whereas only one-half were married and only one-third had children in 1980 [5]. When they do have children, time becomes very scarce for these women, but they typically can spend considerable money on the goods

and services associated with child rearing.

On the other hand, a significant group of employed women are concentrated among families, in which the husband's income alone was proving inadequate. In the 1970's many lower and middle income families found themselves under considerable pressure in their attempt to improve, or just maintain, their standard of living. These women are largely employed in the relatively low paid occupations traditionally dominated by women. The largest category of employment for women continues to be clerical, accounting for more than one-third of all jobs held by women [7, p. 13]. Even with two wage-earners, many of these families do not have much leftover to spend, after covering necessities. Many of these women have temporarily become the sole breadwinner for their families during the current recession, particularly because of the high unemployment rate among men in blue-collar jobs.

The value of unpaid work in the home is not counted as part of national production. Officially treating household production as valueless has distorted assessment of the economy. The total value of household work by adults in the U.S. in 1976 was estimated at \$752 billion, based on a specialist-cost approach, which was 44 percent of the GNP [12, p. 17]. When a family buys hamburgers at a fast-food place, the value of the labor involved in cooking and preparation is counted in the GNP. However, if the family cooked at home, the time spent in preparing the meal would be given no official economic value. As women have shifted their work out of the home and into the office and factory, and purchased goods and services have replaced household activities, the increase in national output has thus been overstated, as has the gain in the welfare of consumers.

INCREASED ECONOMIC UNCERTAINTY

Looking at the last decade or so, one change in the economic environment that stands out is the heightened uncertainty confronting consumers. During much of the 1950's and 1960's the economic norm was typified by low inflation, low unemployment, fairly steady economic growth, and low interest rates, with mortgage rates as low as 5 percent. One really cannot be blamed for looking back nostalgically at a period of such relative economic stability and certitude. In the last ten years, the economy has gone through 2-1/2 recessions, counting the dip in 1980 as a half. However, the current recession should probably be counted as more than one, because of its severity and longevity. There have also been two oil price shocks in the last decade; now there is the possibility of a precipitous decline in petroleum prices. Recently there has been a sharp reversal from double-digit inflation to disinflation, with prices actually declining at the gas station and supermarket during some months.

Given this economic setting, who would be so bold as to try to predict the economy's future. However, decisions on major consumer purchases, if they are to be rationally made, require consumers to make assumptions about future economic trends.

Choosing the right size car to buy requires an assumption about future gasoline prices. Deciding whether to rent or buy a house requires assumptions about what may happen to interest rates and inflation. If you guess wrong about gasoline prices or interest rates, you may be buying the wrong car or housing. Yet no one can predict the future course of the economy with any real surety. Faced by such uncertainty, consumers have become cautious in their spending.

Other factors, in particular high interest rates and now the recession, have contributed to consumers holding back on their purchases, especially for big ticket items. Interest rates of 17 percent for new car loans and for mortgage rates in late 1981 and early 1982, not surprisingly, choked off auto and housing sales. High unemployment affects not only the income and consumer spending of those laid off, but the expenditures of those who are employed are also inhibited by a fright factor. Twenty percent of U.S. families were impacted by unemployment in 1982 and another 20 percent were afraid unemployment might hit them [8]. The various measures of consumer confidence, which have since rebounded somewhat, fell to very low levels in 1982.

Under the weight of these effects, sales of new single-family homes fell to 413,000 units in 1982, the fewest in the 20 years which the government records cover, although a housing recovery appears to have begun toward year-end [22]. The average car's age increased from 2.86 years in 1979 to 4.25 years in 1982, as consumers responded to these factors by slowing their purchases of new vehicles and holding onto their current cars [20].

At the same time such spending cutbacks were indicating the consumer's caution, further evidence was provided by the attempt to improve their financial position. Consumers have cut their installment debt load from nearly 20 percent of disposable income in 1979 to 15 percent at year-end 1982 [5]. The savings rate, which was as low as 5 percent at times in the late 1970's, has climbed to 8 percent. And Elizabeth Allison of Data Resources argues that the real savings rate is close to 12 percent [11]. This difference exists because savings are calculated by subtracting consumer spending from earnings. And earnings do not account for unreported income or the "underground economy", which have become increasingly larger factors.

Consumers have, in addition, responded to this environment by changing their shopping behavior. Consumers are stressing quality more in their purchases and also searching for bargains. In the grocery business both warehouse stores and deluxe supermarkets, with special items and services, seem to be very viable retailing approaches given these consumer attitudes. The Dayton Hudson Corporation, as another example, has done very well, with their Target discount stores appealing to the bargain oriented and their upbeat department stores to the quality oriented. Retailers with middle range quality and prices have not fared as well. In many cases, middle-class households may follow a bargain hunting shopping strategy for one product and a quality seeking approach for another.

An overall comparison of the economy in the 1950's and 60's, with the 1970's, and the 1980's thus far, is not very favorable for the latter period. Arthur Okun developed a discomfort index, which is calculated by simply adding the inflation rate and unemployment level. That index, which is now over 14 has not been below 12 since 1972. During the last ten years the index has averaged about twice its level in the 1960's. The index was never higher than 7.4 between 1961 and 1964 [13]. Government's attempts to deal with one component of the discomfort index have produced sharp increases in the other. The challenge to economic policy is to get both inflation and unemployment down simultaneously.

Even with recovery from the current recession, only the more optimistic are predicting a return to the kind of stable, non-inflationary economic growth enjoyed previously. Consumers will likely have to continue to deal with a very uncertain economic environment in the 1980's. The next decade will undoubtedly contain significant economic surprises. Making the right consumer choices will not be easy. Even with the relevant information, consumers will still have to make, or accept someone else's, guesses about an uncertain economic future. The prudent consumer will probably continue to operate with more caution than would be required in a more certain economic environment.

CLOSING REMARKS

One might fairly ask what the topics covered in this presentation portend for the future. Thankfully, since my crystal ball is missing, such ponderings will not be attempted. In closing though, let it be said that each of these four major topics was chosen because the author views them as significant long-run trends. They should have substantial implications for consumers and consumption, similar to the effects already witnessed, and covered here, well into the foreseeable future.

REFERENCES

1. Becker, Gary S. "A Theory of the Allocation of Time," Economic Journal 75 (September 1965), pp. 493-517.
2. Bowles, John. "The Search for a New Engine of Growth," Business Week, January 17, 1983, p. 10.
3. Byrne, John A. and Brown, Paul B. "Those Unpredictable Babies," Forbes, November 22, 1982, p. 203.
4. Curley, John. "Catalogs Are Getting Specialized," The Wall Street Journal, September 13, 1982, p. 33.
5. Curley, John. "Some Think a Baby Boom Spending Spree Could Lead to Strong Economic Recovery," The Wall Street Journal, January 24, 1983, p. 25.

6. Deegan, Carol. "Baby Boom Needs to Plan Jobs," Minneapolis Tribune, November 7, 1982, p. 2F.
7. Hefferan, Colien. "The Workload of Married Women," Family Economics Review, U.S. Dept. of Agriculture, Agric. Research Service, 1982 (3), pp. 10-15.
8. Heller, Walter. "Speech to the Minnesota State Legislature, Minnesota Horizons Session," January 17, 1983, St. Paul, Minnesota
9. "A Kind Word for the Young," Forbes, December 6, 1982, p. 14.
10. King, Alfred. "Day Care Isn't Kidding About Tough Times," St. Paul Pioneer Press/Dispatch, January 31, 1983, p. 1B.
11. O'Donnell, Thomas. "Swapping Rock Concerts for Rocking Chairs," Forbes, December 6, 1982, pp. 39-40.
12. Peskin, Janice. "Measuring Household Production for the GNP," Family Economics Review, U.S. Dept. of Agriculture, Agric. Research Service, 1982, pp. 16-25.
13. Reno, Robert. "Discomfort Index Dangerously High," St. Paul Pioneer Press, September 12, 1982, p. 19A.
14. "Restyling Skiing's Trendy Image," Business Week, November 29, 1982, pp. 107-108.
15. Sheils, Merrill. "Death of the Family?," Newsweek, January 17, 1983, pp. 26-28.
16. Sheils, Merrill. "A Longer, Healthy Life," Newsweek, January 17, 1983, pp. 24-2 .
17. Sheils, Merrill. "The Work Revolution," Newsweek, January 17, 1983, pp. 29-32.
18. "Two-Parent Households Decline," Minneapolis Star and Tribune, November 26, 1982, p. 12B.
19. Uhr, E. and Evanson, Elizabeth. "Valuing In-Kind Transfers," Focus, Institute for Research on Poverty, University of Wisconsin, 6:1 (Fall and Winter 1982), pp. 13-14.
20. "Used-Car Heaven," Forbes, December 6, 1982, p. 8.
21. U.S. Dept. of Commerce, Bureau of the Census, Statistical Abstract of the United States, 1981, Washington, D.C., December 1981.
22. "U.S. Says 1982 New Home Sales Set 20 Year Low," Minneapolis Star and Tribune, February 1, 1983, p. 7B.
23. Weimer, Jon P. "The Nutritional Status of the Elderly," National Food Review, U.S. Dept. of Agriculture, Econ. Research Service, 1982, NFR-19, pp. 7-10.

NEW TRENDS IN HOUSING: PUBLIC POLICY

Patricia Baron Pollak, Ph.D., Cornell University¹

ABSTRACT

This paper presents a discussion of current policy trends affecting the housing of low income and elderly households. Increasing capital reinvestment in cities and the development of community based housing options for the elderly are addressed as examples of the increasing role of state and local government in the development of housing policy for these population subgroups.

How well we are housed is of obvious importance not only to us as individuals but to communities as well. The quality of housing and of neighborhood environment is important not only when we look at society as a whole, but also when we examine disaggregated segments of our population. It is especially significant to the elderly--because they spend more time at home and in their immediate neighborhoods than younger households do. Housing for the elderly is increasingly important to policymakers, because the elderly now vote and their numbers are increasing. Similarly, the quality of the housing stock for the low income has become a public policy issue in a liberal society; perhaps for different reasons. The poor have few choices and in contrast to the elderly, fewer advocates, today. In general, though, housing and neighborhood environment is important to all of us because it is a significant measure of the quality of life. Because it concerns all of us, it also concerns our legislators.

There are some notable new trends in housing policy which warrant mention in a forum such as this. They are policy related issues that effect a restructuring in the demand for housing and reflect a change in the focus of housing policy decision making. There are two phenomena I would like to address.

The first is the back to the city movement or the increasing capital reinvestment in inner cities which a number of observers have noted is taking place in many urban centers today.

The second is the development of a variety of community based housing options for primarily, although not limited to, the elderly.

The back to the city movement or the increase in neighborhood revitalization activity is a phenomenon whose results have been observed in portions of our older cities. What is apparently happening is a resurgence of interest, on the part of younger households of more income and wealth, to live in or near the urban core. This neighborhood revitalization influences housing in a number of ways, posing a major dilemma to policy planners and others concerned with community revitalization.

Neighborhood revitalization efforts center in older residential areas with properties in need of maintenance and repair. This primarily private renewal and revitalization effort has been called "the first success among many efforts to rehabilitate inner centers. Private urban renewal is being successfully accomplished in areas where public expenditure efforts have failed" (Zeitiz, 1979). It is believed that with revitalization comes an increase in the municipal tax base, an improvement in services and the physical rehabilitation of deteriorating areas.

Herein lies the dilemma. Evaluation of the effects of neighborhood revitalization or capital reinvestment in inner city housing is not value free. As properties are renovated, property values and speculative activity in the older in-need-of repair areas may increase. The total number of housing units as well as the number and proportion of available rental units may be reduced. As this occurs, the cost of housing to both owners and tenants increases.

The rehabilitation and renovation of areas of predominantly lower income housing by higher income/higher status groups is often referred to as "gentrification" in the literature. Coupled with gentrification, the renovation and rehabilitation of older residential buildings has been linked with displacement. Broadly defined, the term displacement describes involuntary household moves which are not due to problems or changes internal to the household. Neighborhood groups or advocates for the inner city low-income and elderly, express the fear that the process of "saving" the neighborhood, former residents will be displaced. Their question: "saving the neighborhood--but for whom?"

There have been changes in Federal policy that may be linked with encouraging the process of neighborhood revitalization. More activity today, however, seems to center in local policies that guide these revitalization efforts. The changes in policy direction have come in two areas--housing and historic preservation.

Until recently, there has been rather extensive involvement at the federal level in the provision of housing for the low income. These include programs such as Section 231, 202, 236, 221d3, 232, the rent supplement program, Section 10 and Section 8. As we all know--Federal policy in this area is changing. The direction of federal housing policy today is to rely far more heavily on private market initiatives. From the federal level we hear the terms "filtering" and reference to "trickle down" to describe the sources of low income housing. One implication of this reliance upon the private market to supply low income housing on the part of the federal government is that states are becoming increasingly interested

¹Assistant Professor, Department of Consumer Economics and Housing.

and concerned with the provision of an adequate supply of low cost housing. In turn, policies established at the state and local levels are far more likely to have significant impact on the quality of housing for the poor.

Examination of inner city neighborhood revitalization also requires inquiry into the development and policy changes regarding historic preservation. In the early years (1935 onward) both national policy and private activity in historic preservation focused on preserving and restoring individual buildings and significant sites. The National Historic Preservation Act of 1966 expanded the early mandate and broadened the application of the historic preservation program to include districts. As a result, residential structures owned and occupied as private property became eligible for participation in a variety of programs. The Tax Reform Act of 1976 and the Revenue Act of 1978 provided economic incentive through federal funding for preservation activities. They provided tax incentives for the rehabilitation and re-use of buildings in these historic districts. The Economic Recovery Tax Act of 1981 included even greater economic incentives for rehabilitation of historic buildings for commercial, industrial and rental residential uses.

At the local level, municipalities across the country have established historic preservation policies. These are frequently in the form of design or architectural review standards for property rehabilitation and are often legislated as amendments to local zoning ordinances. The restrictions imposed at the local level may, in fact, be more powerful in effecting neighborhood revitalization activity and population change than the Federal incentives--given current market conditions.

There appears to be a linkage between neighborhood revitalization and historic preservation. LeGates and Murphy (1981) have pointed out that "the areas being gentrified tend to be in areas with historically elegant units in deteriorated, but salvageable condition." Myers (1978) has suggested that "the significance of historic districting is its use as a tool of community revitalization in many places that are not "historic" in the traditional sense, but rather, "interesting." The expanded concept of historic districting means that older neighborhoods are no longer ignored but "have been elevated to areas planned for revitalization and development under the auspices of 'Historic Preservation District'" (Myers, 1978).

An important question about gentrification, displacement and neighborhood revitalization is the change in the cost of housing which is traceable to the effects of historic preservation property rehabilitation policy. It can be argued that historic preservation is a component of housing policy. However, since federal preservation policy is within the domain of the Department of the Interior, the housing implications of such rehabilitation activity are neither acknowledged nor known.

While widely publicized, the realities of the process of neighborhood revitalization have received little formal analysis. The very scale of the phenomenon and its impact on the various segments of our society have been much more the target of folklore than the recipient of systematic research. There is no agreement in the literature concerning the extent of gentrification and the resulting displacement of households in the U.S. and there is no information on the effects of displacement. Displacement, may, in fact, result in improved housing conditions for low income residents. If so, advocates for inner city low income populations would be doing a disservice by calling for anti-displacement strategies. In addition to the impacts of federal preservation policy, the impact of the adoption of local regulation governing historic districts is not known. Is policy developed at this level really discrimination disguised as environmental protection?

On the other hand, policies may serve to have economic benefits to the community as a whole. For example, the tax assessment base may be increased while at the same time low income and elderly residents may be displaced. Without information it is difficult to evaluate the results of these policy developments from any perspective.

The recent federal cut backs in housing programs make it particularly important that we understand the impact of preservation policy on housing. Federal cut-backs in funding for housing in all phases--new construction, rehabilitation, and rent subsidies for low income and elderly populations will significantly effect the supply of low income housing in both urban and rural areas.

Since the President's Commission on Housing (1982) has recommended that the Federal Government: (1) free the market to produce housing, and; (2) adopt a policy of "filtering." It is important to examine how both historic preservation tax incentives and local designation and preservation restrictions work on the market to effect housing. What happens to the supply of low-income housing, frequently in older structures, if these older structures are the target of rehabilitation and renovation? Put another way: What happens to the residents of older neighborhoods? What is the result for low income residents if housing policy relies on older structures to provide low cost housing and environmental policy encourages their restoration, rehabilitation and "upgrading"? Until we know how public policy decisions such as these impact the supply of housing in older neighborhoods, decision makers will remain uncertain which policy instruments will produce the desired effects.

A second area of relatively new trends in housing--is the recent growth in interest in the development of housing options for the elderly at the local level. Although many of the ideas are not new in themselves, the widespread public interest in the development of these options is a rather new phenomenon. These housing options focus primarily on the community resident elderly--those seniors who are living independently in the community. These comprise the majority of the senior

citizens in the United States today.

There are at least three developments in housing options for the elderly receiving widespread interest. The first is home sharing. The second is the development of secondary units, and the third, the development of home equity conversion plans. These trends appear to accomplish several objectives:

1. They incorporate the demonstrated preferences of older residents--to "age-in-place."
2. They reflect the fact that large amounts of funding for new construction is unlikely in the near future; and,
3. They make use of existing resources.

These options address the issue of the financial burden of housing costs. The burden of housing cost is a problem particularly acute for elderly renters. It is, however, a problem for homeowners as well. As the cost of property taxes, utilities and maintenance increase, housing costs are taking an increasingly larger portion of household income of homeowners as well as renters. While these costs are increasing and the expense of housing is a burden, recent research results tell us that older community residents do not want to move. That they prefer, yet are finding it increasingly difficult, to age-in-place.

Home sharing is one option that addresses these issues. It is the housing situation that results when two or more unrelated people pool resources and share a home. Shared housing enables older people to age-in-place and remain independent in the community. It is believed that both housing costs and social isolation are reduced and that emotional and physical supports are increased. For communities, shared housing can be a strategy for neighborhood and property stabilization. Shared housing also addresses the problem of shortage of affordable housing. There are two basic methods of developing shared housing:

- Match up - where a person with excess space in a house or apartment shares with one or two others.
- Group Residence - where a group of unrelated people form a household and share expenses and a single dwelling unit.

There are approximately 300 such programs in the United States today. Yet, we have no information about the number of people participating in these programs, the effect on the quality of life, or on the housing market in general. Does home sharing free housing units for younger families? Does it help restructure the demand for housing? Are people better housed? It is clear, however, that the development of home sharing programs is primarily occurring at the local level. Interest in assisting community resident elderly remain in the community, with perhaps the concurrent goal of restructuring the demand for housing, is a community based phenomenon. The main barrier to the implementation of these programs, however, may

be in local policy itself. Local zoning regulations frequently restrict the number of unrelated individuals who may share a single dwelling unit. There are to-date no federal or state policies to encourage or guide the development of such programs.

The second development in housing options for the community resident elderly is also a local phenomenon and is even more directly related to local zoning ordinances. Accessory apartments are secondary units that are developed within existing single family homes. Estimates of the number of accessory apartments nationwide are staggering. The Bureau of Census estimates there may be as many as 2.5 million accessory apartments across the country. The main opposition to permitting the development of these types of units and to development of granny flats (small secondary units added outside--but on the same property as the primary residence) is the fear that they inspire neighborhood decline. The, as yet, unanswered question is: How will single family neighborhoods change if secondary units are permitted? The critical problem is answering questions about the development of both types of secondary units is to determine if neighborhoods change because of them--or if, in fact, they make neighborhoods better places to live.

In many areas schools are closing because of declining enrollments, yet in some areas enrollment is increasing. Many communities, particularly in the suburbs, however, are one generational and are exhibiting great fluctuation in the demand for services. Secondary units enable neighborhoods to be occupied by people in various stages of the life cycle and can help smooth out these dramatic shifts and provide neighborhood stability and continuity.

Secondary units and shared housing permit the development of informal social supports. Services can be exchanged in lieu of rent. There is an increased sense of security with others near by or in the same house. Both young families and elders should benefit. Measurement of these qualitative variables is not easy.

The social benefits of these housing options appear to have implications for long term care as well. It costs approximately \$1,800 - \$2,000 per month to keep a person in a nursing home or health care facility. Granny flats, accessory apartments and shared housing are far less costly. Living independently in the community is thought to be far more beneficial to the quality of life than residence in a nursing home. Secondary units also allow the frail elderly to receive support from either children or tenants while still maintaining separate households. We need to examine means to develop secondary units from the perspective of enriching the quality of life in single family neighborhoods. Information from communities with large numbers of these units will inform us of the benefits to both families and communities of intergenerational living and of the effect on neighborhood quality.

A third development in the area of housing options

for community resident elderly is home equity conversion. Some older homeowners would like, or need, additional capital to maintain or improve their homes, pay property taxes, meet increasing utility costs, or for other expenses. The equity represented by a house puts many elder homeowners in the position of being property-rich-but-cash-poor. The traditional way of converting the equity of a house to cash is for the homeowner to sell and move. But, older homeowners who represent approximately three-quarters of elderly headed households express high degrees of satisfaction with their homes. As research has demonstrated, most do not want to sell and move. A number of ideas for converting home equity into income have been put forth. During the past few years, housing and financial specialists have been developing mechanisms to do this.

The major methods are: the Reverse Annuity Mortgage (RAM); split equity and sale/lease back arrangements; and the deferred payment loan. In all of these programs, the equity of the house is converted to cash either as a lump sum or as a monthly payment. While these options offer opportunities for some people there are also costs and risks associated.

Since home equity conversion is both complicated and confusing, it is important that appropriate consumer safeguards be provided. Care is needed to minimize the financial risks faced by elderly homeowners and the potential for failure or fraud in plans developed. For most, home equity is the single most valuable resource. Once it is depleted, there may be no other resources. There is an increasing public interest to make certain that the rights and interests of elderly homeowners are protected. Homeowners considering conversion require counselling and legal advice in order to fully understand the potential consequences of equity conversion decisions. If older homeowners are to make intelligent decisions (1) the instruments offered need to be fully and straightforwardly explained, (2) when more than one type of plan is offered the alternatives should be presented in a comparable fashion.

Comparing plans is not a simple matter. But there are criteria upon which a consumer can compare plans. These include, but are not limited to: initial cash payment; rate of return on investment; net monthly payments; present value of expected payments; equity position of the homeowner at term or after a specified period of time; tax status of payments; term and duration of monthly payments; the amount and terms of any annuity; any prepayment penalties for revoking the agreement; and, the disposal of the property at the end of the term or at reappraisal of property value. Given lack of federal leadership in this area, consumer safeguards such as these call for the development of policies at the state level.

For reverse equity and deferred payment loans, the following information should be disclosed: loan-to-value ratio; the right of the lender to escalate payments or change the term of the loan; equity position of the borrower if death occurs prior to term; rights of the homeowner on the sale

of a loan to the secondary market, and agreement on situations such as temporary move-out or diminished capacity of the homeowner. A loan plan including an annuity should compare the rate of interest the annuity earns with the mortgage interest rate to make certain that the annuity will yield sufficient income for the homeowner.

In split equity and sale/lease back arrangements older homeowners rights of lifetime tenancy under the lease should be protected. The lease should protect the homeowner against situations that could force him or her out of the home. Adequate safeguards should be provided to protect the seller in case the buyer defaults on the mortgage or monthly payments.

Until recently, public policy regarding housing options for the elderly relied on the construction of new units and the relocation of older residents to senior citizen housing. The development of these community based housing options has dramatically increased the proportion of the senior population whose housing concerns are being addressed. Yet, we do not know what the incorporation of these programs will mean for the nature of our communities (both in the long run and short run) or for the large number of "baby boomers" who will be seniors by the year 2010. It is clear that more research is needed.

More research is needed in the area of neighborhood revitalization as well. Neighborhood revitalization movement may have begun with federal incentives for the physical improvement of places. Local controls, however have become increasingly important and may in fact be more significant in guiding neighborhood revitalization efforts today. The emphasis of policy at both levels was and still is, however, place oriented. In focusing on places and physical structures--historic preservationists have not been particularly sensitive to people. Both federal and local policies leave the question of housing for low income residents unresolved.

Other questions also remain. While, neighborhood revitalization efforts are increasing in number, variety and impact, they are primarily a result of private market activity. The role of historic district designation and local law is, however, being studied. The examination of the social and economic effects of place oriented policies is important for designing policies that meet the needs of community residents. There is also increased concern for displacement, yet we do not know how much involuntary displacement there is and really do not know long term effects of "displacement" on the well being of households. Longitudinal studies of changing neighborhoods will provide answers to the questions of: Who benefits from the rehabilitation of existing housing? Who benefits from the overall improvement of neighborhoods? and, What happens to the displaced?

In one way, neighborhood revitalization and the development of housing options for elderly are new trends in housing. At the same time, these developments are examples of the shift in the locus of policy development from the federal to the state

and local levels. The significant new trend in housing is the increasing attention that housing policy activity is receiving at the state and local levels. As state and local governments struggle to develop policies, there is clearly a need for more research and for the application of the results of that research to public policy. Research can help guide public policy at these levels as governments develop agenda and search for suggestions for programs in areas that are new to them.

Our state and local governments do not have much experience in housing policy. The policies that are developed at these levels will guide our future environments. If policies have any effect at all, the programs and infrastructure that result will either support or inhibit the quality of life we want. Decisions that are made today will have long term effects. The economic and social effects of place oriented policies need to be examined and evaluated. With the shift in focus of policy development both academic research and consumers should have new opportunities to help guide the development of those policies.

REFERENCES

- LeGates, Richard T. and Murphy, Karen. "Austerity, Shelter and Social Conflict in the United States." International Journal of Urban and Regional Research, Vol 5: No. 2, 1981.
- Myers, Phyllis. Neighborhood Conservation and the Elderly, Washington, D.C., The Conservation Foundation, 1978.
- President's Commission on Housing, The Report of the President's Commission on Housing, Washington, D.C., U.S. Government Printing Office, 1982.
- Zeitz, E. Private Urban Renewal, Lexington, MA.: Lexington Books, 1979.

RECENT CHANGES IN FINANCIAL MARKETS SERVING CONSUMERS

Lawrence Shepard, University of California, Davis¹

ABSTRACT

This paper argues that inflation has been a driving force in shaping recent changes in the financial markets facing consumers. During the last 15 years, inflation has altered the savings opportunities available to consumers and the behavior of consumers' credit markets in ways that can broadly be characterized as favorable. However, evidence that the next few years promise price stability gives reason to question whether such advances will be sustained.

INTRODUCTION

While consumers participate in the equities and corporate debt markets, often indirectly through pension and insurance intermediaries, their most direct involvement in the financial markets is through personal savings and consumer credit. Aside from their obvious importance to consumers, the savings and credit markets influence capital formation and levels of aggregate demand that drive the economy as a whole. Conversely, macroeconomic factors in the broader economy have caused profound changes in the financial markets serving consumers.

This paper analyzes recent changes in the consumer savings and credit markets. It argues that the roots of those developments lie in the inflation of the last two decades and, particularly, in consumers' considered responses to that price instability. After offering tentative conclusions about the specific impacts of past inflation on the savings and credit markets, the paper examines prospects for future price stability as the United States shifts from a policy of rapid and repeated debasement of its currency to an apparent commitment to a new monetary ethic. It pronounces no judgment as to the wisdom or equity of the extreme policy remedials that have brought the United States to this juncture. Instead, it argues that consumer analysts must aspire to a greater understanding of how consumers have accommodated past inflation in their saving and borrowing behavior if they are to discern what a future which promises price stability holds for consumers.

PERSONAL SAVING

During the past two decades inflation has been largely responsible for the broad expansion of savings and cash management alternatives available to consumers. More precisely, the rapid emergence of innovative accounts and savings institutions represents the culmination of an on-going tension between Regulation Q, the Federal Reserve System provision that sets maximum nominal interest rates

paid on bank deposits, and inflation, which has moved market rates of interest to previously unknown levels. In providing interest rate ceilings on bank accounts, Regulation Q during the 1950's and 1960's has served the interests of banks and savings and loan associations because, while those institutions collectively favor lower rates on deposits, each institution has an individual incentive to offer higher rates in order to attract new deposits.² Unbridled, such competition would have been costly to the banking industry but under Regulation Q competitive inducements have historically been limited to offerings of cookbooks, piggy banks, and stuffed animals. As was true in the airline, brokerage, and trucking industries prior to their deregulation, the evidence is quite clear that Federal authorities enforced an artificial rate structure that was less favorable to consumers than rates sustainable in a competitive, unregulated market.³ Banking regulators fixed interest rates in a way that would have been illegal under Section 1 of the Sherman Act had the industry done so itself.

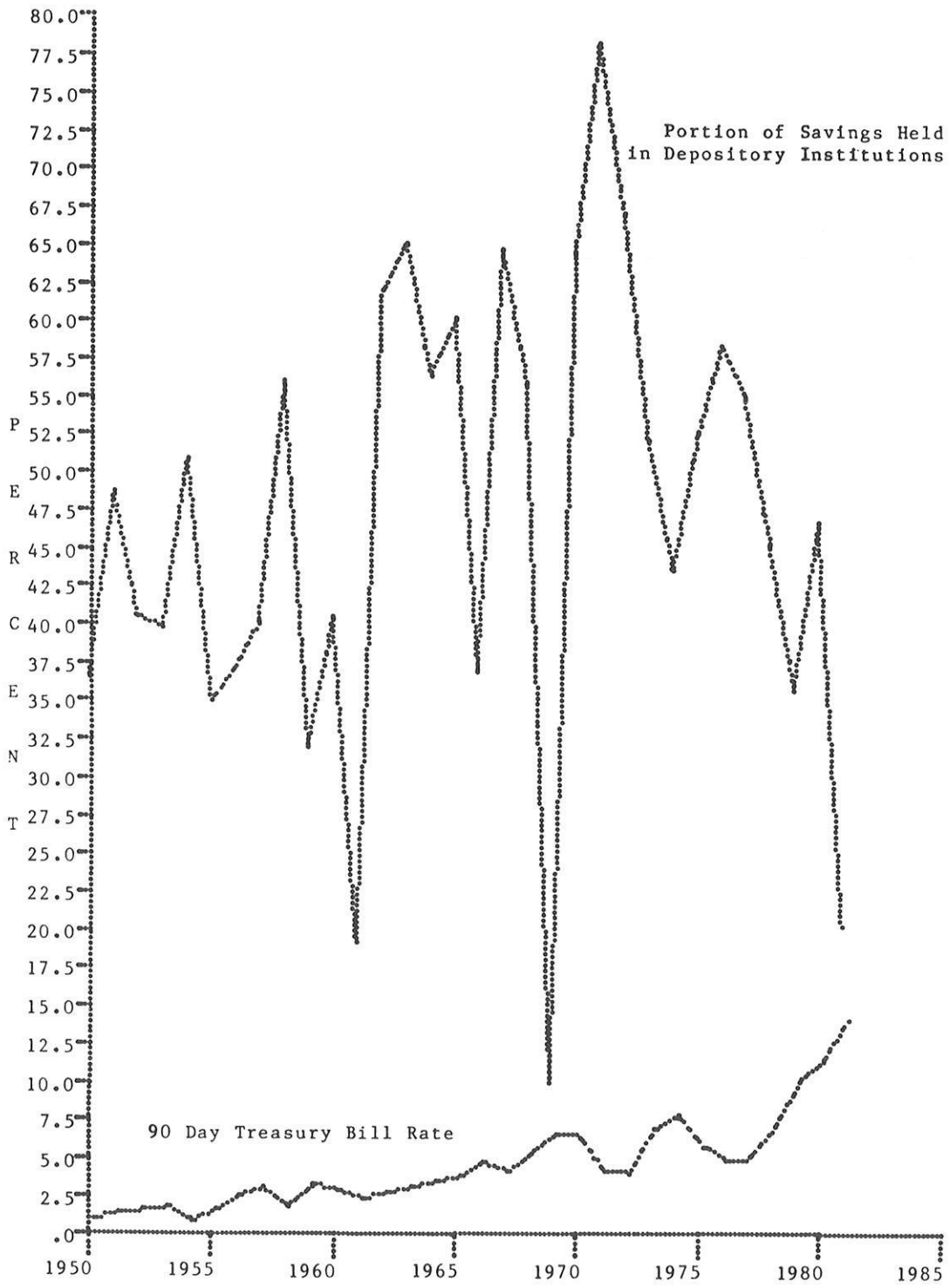
During the middle and late 1960's, passbook rates of 4 and 5 percent became unacceptable in the face of pronounced and prolonged inflation. This caused consumers who could afford the minimum purchase of \$10,000 to withdraw funds from depository institutions to purchase Treasury bills and agency securities bearing market rates of interest. The resulting flee of funds from banks and thrift institutions imposed severe liquidity problems for those financial intermediaries. Figure 1 bears evidence of this financial disintermediation beginning in 1966 and 1969, when record high interest rates coincided closely with a shift by consumers away from holdings of time and demand deposits because the rates paid by depository institutions were fixed. Throughout the 1970's the proportion of savings put in such deposits moved inversely with interest rates available in the money markets.

²Originally provided for in the Banking Act of 1933, Regulation Q is being phased out in stages between 1980 and 1985 under the Depository Institutions Deregulation Act of 1980. Responsibility for regulation of deposit interest rate ceilings has been given to the Depository Institutions Deregulation Committee [4, p. 530].

³In the case of consumer savings, of course, the Federal government has had a particular interest in maintaining artificial prices because the Treasury was itself a primary outlet for consumer savings through its Series E savings bond program which, like bank savings accounts, offered consumers rates of interest significantly below rates available to commercial lenders and wealthy consumers. See Phillips [3].

¹Associate Professor of Agricultural Economics

FIGURE 1: Disintermediation in the United States



While this behavior by consumers was entirely rational and bears evidence of the market's propensity to circumvent artificial constraints, periodic spells of disintermediation shook banks to their roots since many of their funds were invested in illiquid, long term loans. To stem the tide of disintermediation, institutions began offering certificates of deposit with rates pegged to the T-Bill rate. Initially, these were available only to large depositors but eventually minimum deposits came within the range of consumers in more modest circumstances. However, the appearance of small C.D.'s gave consumers only limited access to the money markets because those instruments denied savers liquidity by specifying 2 to 8 year maturities and associated early-withdrawal penalties.

In the late 1970's, consumers gained full access to the money markets once again despite, rather than because of, Federal authorities and the depository institutions they regulate. Beginning in 1974 and gaining full force in 1978, stock brokerage houses and mutual funds offered money market funds to individuals which combined market rates of interest and full liquidity. Operating under the Investments Companies Act of 1940, rather than under federal or state bank charters, these nondepository institutions have been highly competitive in their interest rates, check writing privileges, credit facilities, and service charges. Because they have paid market rates with total liquidity, many money market funds enabled consumers to combine their savings and checking facilities into one account, merging and simplifying the distinct savings and cash management functions. Through money market funds, consumers gained many of the elements of financial control that were available through depository institutions only to commercial depositors. The significance of these funds has been largely missed in the personal savings literature.

From an aggregate value of \$200 million in 1977, money market mutual funds attracted balances of over \$200 billion last year. As inflation drove money market interest rates to record levels, a single three month period in 1981 witnessed an inflow over of \$100 billion into money market funds from traditional accounts at banks and thrift institutions [5, p. 23]. This unparalleled growth occurred without the benefit of either Federal deposit insurance or the presence of branches in most consumer markets.⁴

So successful have been money market funds in attracting consumer deposits away from depository

⁴Money market funds, in fact, provide a high degree of security since deposits are invested in short term government debt and rated commercial paper held in trust accounts by custodian institutions. While lacking the imprimature of the FDIC or FSLIC, these highly diversified portfolios would appear to be less risky than those of typical banks, which include a variety of unrated commercial and personal debt, some of which carries lengthy maturities.

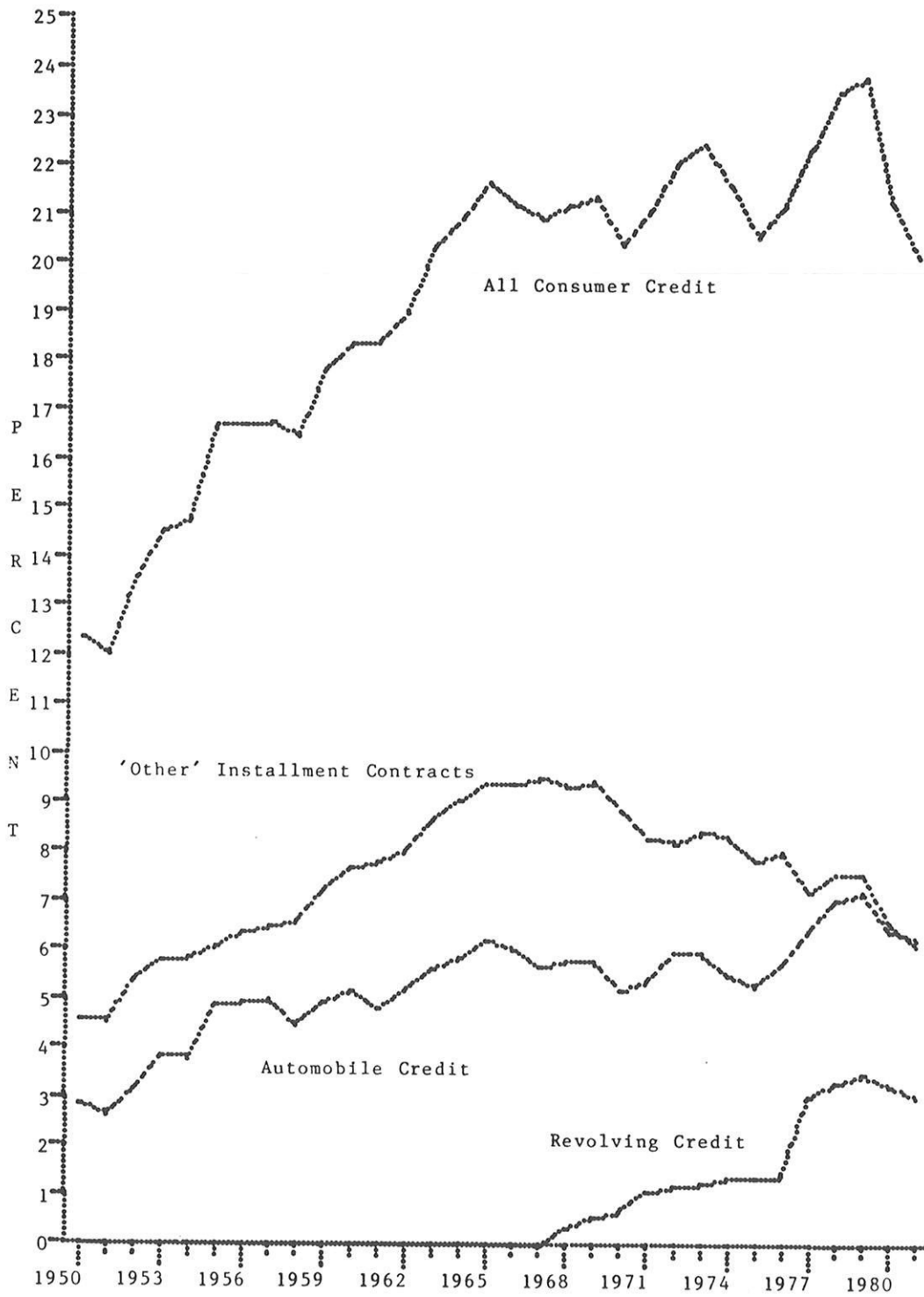
institutions that in mid-December 1982 the banking industry abandoned its historical opposition to competitive pricing on liquid consumer balances. With the industry's support, passage of the Garn Act enabled banks and savings and loan associations to offer "money market savings accounts." Aside from provisions for a \$2,500 minimum deposit and only limited check writing privileges, these savings instruments are competitive with money market funds offered by investment companies. Importantly, they provide consumers access to rates of interest fully reflective of opportunities in the loanable funds market as well as local branches and Federal deposit insurance. They also promise to stabilize both the banking industry and consumer savings patterns by effectively displacing the artificial constraints imposed by Regulation Q.

The response of consumers to the new money market savings accounts, stimulated by special premiums and temporary above market rates of interest, has been impressive: in the six week period ending January 31, 1983, one \$10 billion institution reported that \$2.3 billion flowed into the new accounts. Approximately 70 percent of funds going into the accounts were reported to be new to the institution and 50 percent were estimated to have originated in money market funds [1, p. 27]. While these belated personal savings innovations are themselves making inroads into the money market funds, they came about only because inflation and its attendant high rates of interest made untenable the traditional opposition of depository institutions to paying competitive rates of return on personal savings. Inflation and consumers' informed responses to inflation were the motive forces for reform in the personal savings market as it moved from the realm of 5 percent passbook accounts to private ownership of Treasury bills, to small savers certificates, to money market funds and, most recently, to money market savings accounts.

CONSUMER CREDIT MARKETS

Although institutional changes have not been as apparent in the consumer credit market as in personal savings, there is at least tentative evidence that price instability has played a significant and unexpected role in altering the borrowing behavior of consumers. The data reveals that between 1950 and the mid 1960's, consumers substantially increased levels of nonmortgage credit in relation to disposable income year after year (Figure 2). During this period, installment and noninstallment credit balances rose steadily from 12 percent to 22 percent of average annual disposable income. The propensity to commit ever-greater proportions of income to previous consumption continued through 1965, with only modest deference to year-to-year variations in consumer income. This pronounced trend led economic analysts as well as authors of personal finance textbooks to conclude that on an inflation-adjusted basis, average per capita credit

FIGURE 2: Ratio of Consumer Credit to Personal Income



balances would continue to double each decade as they had between 1930 and 1960.⁵

These pronouncements notwithstanding, the rapid postwar expansion in credit use ended in the mid-1960's. Thereafter, consumer credit balances appear to have levelled off in relation to income, following a cyclical course about a mean precisely equal to the level first reached in 1965 with peaks and troughs generally corresponding to vicissitudes in personal income. This phenomenon affected all types of consumer credit. After rising rapidly in the 1950's, the 1960's saw automobile credit level off as a proportion of income (Figure 2). While installment contract purchases of other consumer durables (e.g., furniture and appliances) appear to have fallen after 1965, note that the decline was almost exactly offset by the growth of revolving credit for purchases of similar goods as bank cards and department store credit cards came to replace individual loan contracts for major purchases. Overall, credit use for this class of purchases was flat after 1965. With the exception of credit for purchase of mobile homes, a minor factor, no component of consumer credit exhibited growth in relation to income after the mid-1960's. This moderation of consumer borrowing, bearing as it does on both the financial health of consumers and levels of consumer demand in the economy, has received only modest attention.

Economic theory suggests that three primary factors drive per capita credit balances: personal income, interest rates, and price expectations. Higher income is expected to encourage purchases, increasing demand for both goods and credit. Rising finance charges, of course, would have the opposite effect. The potential impact of inflationary expectations, however, is somewhat ambiguous. On the one hand, credit use may be greater in periods of inflation as consumers at the margin are motivated to borrow funds to make purchases before prices rise. However, during pronounced inflations this speculative motive may be offset by the increased risk associated with rising prices. Because inflation heightens uncertainty about the future level of one's real income, it may motivate risk-averse consumers to reduce their financial leverage in order to be better positioned to withstand future economic adversities.

The importance of personal income as a determinant of credit use is illustrated in Figure 3 where modest variations in personal income are associated with much more pronounced swings in credit balances. Likewise, the inverse relationship between interest rates and changes in real per capita credit balances is very clear (Figure 4) as interest rates rise, borrowing falls and vice versa. This relationship also prevails when changes in credit balances are superimposed on real interest rates--as represented, for example, by the level of finance charges reduced by the trailing three year moving average change in the CPI

⁵Only Yeager appears to have observed that consumers were "saturated" with credit [8].

employed as a proxy for expected levels of inflation. Just as spending behavior is determined by price adjusted variables, so borrowing and lending behavior are influenced by inflation adjusted interest rates.

Changes in income and real interest rates fail to provide an explanation for the tempering of consumer borrowing during the second part of the postwar period. Personal income rose after 1965 nearly in proportion to its increment between 1950 and 1965 and real interest rates actually fell during the later period. However, it is well known that after 1965, rates of inflation were much greater than before. Indeed, few would disagree that this price instability represented the single greatest economic shock to American consumers during the last 40 years.

In order to shed further insight into the role of inflation, a series of regressions was estimated for the 1950-1981 period linking changes in real per capita installment and noninstallment credit balances (C) with changes in personal income (Y), real interest rates (R), and expected inflation rates (P):⁶

Levels:

$$C = -391.81 + 0.37 Y - 2.88 R - 10.46 P$$

(19.51) (1.57) (4.19)

$$R^2 = .99 \qquad \qquad \qquad D.W. = 1.41$$

First Differences:

$$C = 1.30 + 1.76 Y - 0.62 R - 2.06 P$$

(4.76) (2.17) (1.89)

$$R^2 = .68 \qquad \qquad \qquad D.W. = 1.72$$

In both levels and first differences, credit use appears to be directly related to year-to-year changes in per capita income. Also in accordance with economic theory, real interest rates bear an inverse relationship to credit balances. Finally, borrowing behavior appears to bear a systematic, inverse relationship to changes in expected price levels. This relationship was persistently noted in alternative specifications of the equation

⁶Real interest rates were represented by the rates on consumer installment credit reduced by the three year lagged moving average percentage change in the Consumer Price index. Expected price changes were captured by the three year lagged moving average percentage change in the CPI. In alternative specifications of the relationships, credit use was related to personal income and nominal interest rates. These specifications provided inferior fits, giving little support for the money illusion hypothesis that consumers respond to nominal rather than real phenomena. However, such an interpretation is not at odds with the major thesis of this paper, that inflation alters credit and savings behavior.