CONSUMER FINANCIAL PROBLEMS

NEW PROBLEMS IN FAMILY SPENDING: THE CONFUSED AMERICAN FAMILY

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I have three ideas about the confused modern American family. They are related to a most interesting question about why American families are the richest in the world and yet so often in debt.

Briefly, these are the three ideas: First, we should be careful to avoid false and anti-social answers to the question about why American families are increasingly getting into debt. We need to consider the possibility that the real answer may be that families are terribly confused about what standard of living they ought to have.

Second, we should recognize that this confusion is not only the fault of the borrower. The confusion is probably the result of tremendous changes taking place in our society.

The third idea is that American society is certainly going to keep on changing. And with change, we are apt to witness the rise of new standards and morals about borrowing and saving money. And some of us are going to disagree with new standards.

Some of us get pretty alarmed when we read about our present $56 billion dollar short-term consumer credit. We might even be pardoned for saying that many consumers are in so deep that they can't possibly get out. Of course, some people have been saying that for decades. Yet, somehow most debtors manage to manage their debts.

I agree that there must be a limit but I don't think that the real problem is whether or not the debt will be liquidated. It continues to be right along. The real problem is: "Why has it become so common for families to have such worries and guilt feelings about their debts?"

Many of us are familiar with the guilty suspicion that our neighbors are having less difficulties with paying their bills that we are having with ours. Actually, this may not be true. Do you recall the study made a while ago in some of the wealthier suburbs of New York, where men were earning from $12,000 to $30,000 a year, and the average family there was spending about 40% or more than its annual income. It also found that every Tom, Dick, and Harry in the block believed that he was just about the only man who had to borrow so much in order to live so well. Tom felt guilty because had had to borrow $500 to buy a hi-fi set while his neighbor, Dick, could afford to go to Bermuda. Dick felt guilty about owing $500 for his "fly now-pay later" Bermuda vacation, when his neighbor, Tom, could afford expensive hi-fi sets.

Tom and Dick illustrate a lot of boring statistics. You and I know that it has become quite common among American families, except the very poorest and the very richest, to owe enough money to feel anxious and guilty.

Individual worries aren't the only new problems to high level consumer debt. Some economists mention it as a factor in the instability of our economy. And some socioligists have mentioned it as a factor in social disorganization. Psychiatrists mention it as a factor in the climbing rate of mental illness.

So the fact that relatively well-off families are becoming more and more willing to incur debt is an important change in our society.

One of the consequences of this change, especially for "young marrieds" and the "growing families" is that this system is promoting debt as a way of life. In other words, more families want more possessions right now than they can afford on a cash basis and consumer credit is made to order for them.

Why have an increasingly large number of families changed from paying cash to assuming debt?

There are many answers but I think that most of them can be classified as one of three types of unsatisfactory theory.

The first theory is found in most consumer-economics textbooks and in the FRB's excellent six-volume study of consumer credit. This answer says that people always have wanted more things than they can afford at a given time, and consumer credit was a natural evolution of merchandising methods to satisfy these wants.

This answer says that people used to buy laundry service from a man who owned a laundry, transportation from a man who owned a livery stable, etc., but presently, they buy their own washer-drier, their own automobile and their own TV set. They can do this because they can get credit to buy these expensive machines.

Now, all this, is true but it is no complete answer. Sure, people have always wanted more than they had, but Noah couldn't have paid for the Ark on the installment plan because plans didn't exist then. Credit is so much a natural evolution of distribution methods that you can't help but wonder why it almost never existed until our own century.

Part of the answer is simple. Throughout most of history, borrowing and lending at interest had been considered immoral and has been strictly tabood. The lender was usually considered a parasite and often a criminal. The borrower was usually considered improvident and a sucker, and even a sinner.

What changed such morals? I call this "natural development" answer the "socially-non-curious" theory because it isn't serious about what made people's morals change. The danger of this answer or theory is that it assumes that the user of credit is economically rational. It assumes he is not confused by our moral traditions, and is acting by some kind of sensible standard. I think the credit manager who assumes that every loan applicant knows what he is doing is asking for trouble.

The other two kinds of inadequate theory do offer an answer to what happened to traditional morals. Their answer is, people are becoming more immoral. There are the "naive moralists" who blame high debt levels on immoral individuals, and the "sophisticated moralists" who blame it on a bad system that forces people into debt. The former (naive moralists) are people like John Keats who says that immoral people are imitating the government's philosophy of deficit spending and that we are becoming a nation of immature people who like to open Christmas presents the week before Thanksgiving. Or men will William Whyte, the sociologist, who says borrowers are immoral because of a contagious social-psychological neurosis called "budgetism"; or Eugene Barnes, a psychologist who believes that people today have no "credit conscience."

I don't see how these explanations explain enough especially when you consider that year on year, the same percentage of different income classes have personal debts. About 1/3 of factory-worker families are in debt; about 1/2 of white-collar workers are in debt even though their average income is higher than the self-employed. It seems a strange thing when the same percentage of individuals decide to be immoral year after year in the different groups of our society. It's a little like criminals. Criminals have been considered immoral, and society has generally worked on them to mend their ways. But when we realized that slums turn out high percentages of criminals we began to examine the environment. We still don't know what causes criminals but at least we no longer kid ourselves into believing that we have explained the whole business by saying that criminals are immoral individuals.

In much the same way that slums help produce criminals, white-collar jobs help produce debtors. More white-collar workers have debts than self-employed people whether the income of the self-employed is higher, lower, or the same. It would seem, therefore, that the social system is involved in some way.

I think the sophisticated moralists recognize this fact. The naive moralists still insist that borrowers are basically immoral but they blame the system for making them that way. John McPartland, the novelist, blame the "Easy credit system" for tempting him. A. C. Spectorsky, the sociologist who conducted the study in the wealthy New York suburbs, blames the "status" system. John Galbraith, the economist, blames the whole economic system for just plain overselling consumer goods.

All of them, I think, offer parts of an adequate explamation. Perhaps they explain too much. The system they mention do pressure us all the time. But how do you explain that, year after year, 1/3 of blue-collar workers do not have debts, nor do 2/3 of the self-employed, nor 1/2 of the white collar workers.

Besides, history shows that it is best to be suspicious of every generation which says that the younger generation is becoming more and more immoral. As often as not it has turned out that the morals were changing, and that often the new morals were better for their times.

We have to remember that before social morals were established, it was perfectly all right for a man to knock any other man over the head and drag away his property and his woman. I suspect that most of us who have a wife are most grateful for the change in morals since that time.

Basic personal morals like the Ten Commandments remain generally unchanged. But specific little morals, in areas like economic and political behavior, change with the times. Economic behavior that produced the Robber Barons of just two generations ago, and which was admired or at least accepted at the time, would now be immoral and illegal.

I now come to my point. I have a hard time persuading myself that the majority of American families using credit today are immoral. It seems to me that when a set of morals becomes obsolete, and when we do not have a workable set of standards to replace the old ones, people become confused and begin experimenting until a suitable set of new morals is developed and accepted. I am of the opinion that the rapid expansion of consumer credit represents that kind of experimenting, caused by that kind of confusion.

Let's consider the confusion that might make the former morals regarding thrift and debt become obsolete. In our early economy, capital had to be created largely by thrifty acts of individuals. Therefore, the virtue attributed to thrift, along with the moral taboo on using credit for consumer goods, were essential in causing a rapid rate of economic growth.

Thrift also had important motives for the individual. Before 1900, success came along usually with the "expansible possession"--that is, your little farm and little shop or business required even more thrift in order to get capital to become a big estate or a big factory.

But in recent decades, things have changed for the economic system and the individual. It appears at present that the system can form capital easier than it can maintain purchasing power. And the individual does not as often find success with the expansible possession. Instead he pins his hopes on the forward-looking job. To make the most of your job or position, thrift is not of much help. What you need more is to demonstrate with your style of living that you're the kind who was made for bigger and better things--even if you have to borrow to do it!

So, it seems to me, that for both the system and the individual, times have changed and it makes more sense to attach moral virtue to spending than to thrift.

By pointing this out, I am only attempting to get some kind of more rational explanation to understand the trend toward debt as a way of life. I'm sure it will be wise today for the individual to have enough savings to meet the common emergencies without paying interest rates. But you do have to fight against a lot of new pressures.

This is by no means a full explanation of the eagerness for credit today. Perhaps social change could have removed the moral restrictions on credit without resulting in a $56 billion consumer debt if American families weren't so eager to borrow. I have the feeling that this eagerness may be the result not of confusion about changing morals, but confusion about standards of living.

Your level of living is based on the amount of money you spend. Your standard of living is the way you feel you must live. One man's standard may require a shack by the seashore, one good suit and regular meals. Another man's standard may require a tri-level home, two cars and a yardman.

Where do these standards come from? Through most of human history they simply become a part of people during the process of growing up in a family. Chances are that most of us in this room came from a middle class family. Chances are a majority of us had grandfathers or even fathers who were farmers, immigrants or factory workers with less education than we have. The point I want to make is that not one of these generations could live according to the standards of the preceding generation because each one lived in a different environment. And millions of American families have had the same kind of history.

In a situation where each generation is living in a different kind of world from the proceeding one, of what use are many of the living standards of our grandfathers or even our fathers?

Without traditional standards of living, each of us has to experiment with his own. We are generally guided by our own ambitions, by standards of our friends, the Joneses who have debts we don't know about. Or maybe we are guided by the mass media--TV, motion pictures, magazines.

If, under these circumstances, the average American family were not confused about an approximate standard of living, you would have something really difficult to explain.

So far, I have discussed two of the ideas mentioned: the idea that the growth of consumer credit is not so much a matter of immorality as a consequence of confusion, and that this confusion isn't rooted in bad psychology as much as in perfectly normal social change.

My final idea is that credit managers or institutions might take intelligent guesses about future changes, and work to influence these changes in constructive directions. Trying to predict change in human behavior is a risky business as some sociologists and economists have discovered. But it is an interesting speculation.

This is my guess. Near the beginning of this century, credit institutions and others helped make it respectable for people to admit that they needed to borrow in emergencies. At mid-century, it was standard practice for young families to place heavy mortgages on their future earnings in order to start out with a standard packet of durable goods when they were first married and needed it most. Right now this packet might include a stove, refrigerator, washing machine, a car, a television set and a record-player. By the end of this century, who knows--a dishwasher, family-size airplane, clothes that you toss into the ash-can after a few week's use--well, you guess!

If you permit me to do some crystal-gazing, I would predict that the trend will be more use of "buy now, pay later" until we begin to gradually ease out of this form of credit that inspired ownership into a system of less and less ownership and more and more continuous renting of the goods and services we need. If this happens credit will have a very different meaning.

In the future, it is not unlikely that various social insurances will reduce the frequency of real emergency loans; that some of the extremely expensive revolving credit plans and credit-card schemes will be outgrown and, who knows, we may have enough mature voting citizens who will insist on requiring all consumer credit contracts to reveal all the costs of credit in a common language easily understandable to all people.

And perhaps we ought to do our part to minimize the obsolete barriers of worries and guilt that keep people from talking about their use of credit. Far too many people are like the man who went to the psychiatrist. He worried all the time; the doctor asks about how he lives; and he lists numerous expensive habits. The doctor says, "This is wonderful, why worry?" The client says he's making only $5,000 a year. The psychiatrist's answer was, "My friend, you're not sick. You're simply over-extended and over-confused."

And that's where you and I came in.