Center for American Progress

# America's Middle Class Still Losing Ground

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# Introduction and Summary

America's middle-class families are still struggling. With the current economic downturn, economists, policymakers, and pundits alike now recognize what many middle-class families have long been feeling: that their financial security is in decline. Although economists so far have not officially announced the beginning of a recession this year, the sharp downturn in economic growth certainly has made things worse for families who have been struggling for years with massive amounts of debt, declining incomes, and rising prices.

For the past two years, the Center for American Progress has calculated a number of middle-class financial security indicators to measure how many families have the financial resources for a spell of unemployment, for a medical emergency, for both, or for an unspecified economic emergency equal to three months of their income. Our figures demonstrate the financial and economic roller coaster ride that America's middle class has been on.

The trends since 1989, the first year for which we have data, showed an increase in middle-class security through the 1990s. After 2000, however, the situation deteriorated very quickly—all of the gains in middle-class economic security were erased within a few years. We have now updated the figures to reflect the trends for 2006 and 2007 and to include more accurate data for 2005 than we had before. All the measures we tracked either decreased further or stayed at their already low levels from 2005 (See chart on page two). Data to 2008 is not available, but there can be no doubt that with worsening economic conditions middle class economic security is taking an ever harder hit. The new data underscore that:

- **The sharpest deterioration in middle-class financial security is associated with the cost of a medical emergency.** We estimate that only 33.9 percent of families had enough wealth in 2007 to cover the cost of a medical emergency, down from 35.0 percent in 2005 and 43.7 percent in 2000 (See table on page 3). This deterioration comes as a result of less wealth and higher costs of medical emergencies.[1]

- **Drops in personal wealth have contributed to the decline in middle-class financial security.** Because house prices started to fall and debt continued to rise in 2007, we also observed the share of families who could weather an unspecified emergency equal to three months of income decrease to 29.4 percent in 2007, from 30.5 percent in 2005 and 39.4 percent in 2000.

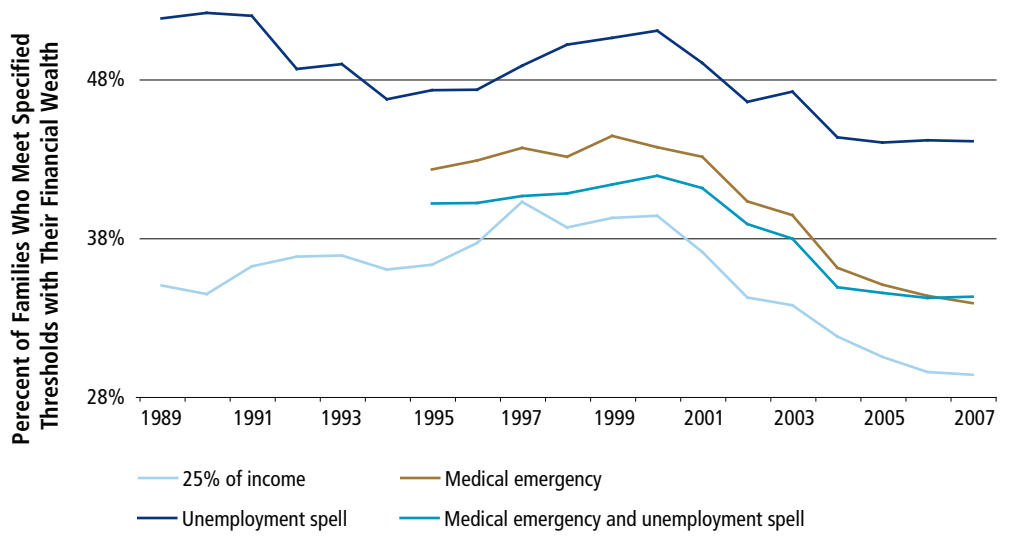
- **The share of families who had enough resources to cover a spell of unemployment has declined since 2000.** In 2007, 44.1 percent of families had enough wealth to cover a spell of unemployment, little changed from 44.0 percent in 2005 but still down from 51.0 percent in 2000. Unfortunately, the 2007 data likely reflect only a temporary respite from decline since the labor market has substantially deteriorated in 2008, beyond the time series data presented here.

Rising middle-class financial insecurity after 2000 is the result of several factors. Incomes have fallen as a result of the weakest job growth since the Great Depression, flat wages, and declining benefits. At the same time, prices for necessary items, such as food, energy, housing, and transportation, have all risen sharply. Finally, personal wealth has been decimated, first by the mortgage boom, which allowed more families to build wealth by purchasing homes but also required them to take on higher debt levels, and then by the bursting housing bubble, which of course depleted the value of those home investments, and then by much weaker financial markets.

Providing America's middle class with more financial security is a tall order. It will require serious efforts to ensure that incomes rise in a growing economy, and that families can build wealth in preparation for inevitable emergencies and to invest in their future. It will also require investing in more energy efficiency and alternative fuels so that energy price shocks do not throw families for a loop. And it will require progressive health insurance reform.

In the pages that follow, we will detail the deteriorating financial health and well-being of the American middle class, describe the public's clear awareness of the problem, and then point out briefly in our conclusion the variety of progressive policy alternatives to help restore middle-class vitality and with it U.S. economic vigor.

**RISING MIDDLE-CLASS FINANCIAL INSECURITY**
***By all our measures, America's middle class is under siege***



**MIDDLE-CLASS FINANCIAL SECURITY INDICATORS**
***How many families can weather financial emergencies, 1989 to 2007***

| Year | Have three months' worth of income in financial wealth | Can cover a medical emergency | Can cover an unemployment spell | Can cover medical emergency and unemployment spell |
|---|---|---|---|---|
| 1989 | 35.0 | n.a. | 51.8 | n.a. |
| 1990 | 34.5 | n.a. | 52.2 | n.a. |
| 1991 | 36.2 | n.a. | 52.0 | n.a. |
| 1992 | 36.8 | n.a. | 48.6 | n.a. |
| 1993 | 36.9 | n.a. | 48.9 | n.a. |
| 1994 | 36.0 | n.a. | 46.7 | n.a. |
| 1995 | 36.3 | 42.3 | 47.3 | 40.2 |
| 1996 | 37.7 | 42.9 | 47.3 | 40.2 |
| 1997 | 40.3 | 43.7 | 48.8 | 40.6 |
| 1998 | 38.7 | 43.1 | 50.2 | 40.8 |
| 1999 | 39.3 | 44.4 | 50.6 | 41.4 |
| 2000 | 39.4 | 43.7 | 51.0 | 41.9 |
| 2001 | 37.1 | 43.1 | 49.0 | 41.1 |
| 2002 | 34.2 | 40.3 | 46.6 | 38.9 |
| 2003 | 33.8 | 39.4 | 47.2 | 37.9 |
| 2004 | 31.8 | 36.1 | 44.3 | 34.9 |
| 2005 | 30.5 | 35.0 | 44.0 | 34.5 |
| 2006 | 29.5 | 34.3 | 44.1 | 34.2 |
| 2007 | 29.4 | 33.9 | 44.1 | 34.3 |
| 1989–2007 | –5.6 | n.a. | –7.7 | n.a. |
| 1989–2000 | +4.4 | n.a. | –0.8 | n.a. |
| 1995–2000 | +3.1 | +1.4 | +3.7 | +1.7 |
| 2000–2007 | –10.0 | –9.8 | –7.0 | –7.6 |

Notes: All figures are percent of households. Changes are in percentage points. Calculations are based on Pareto interpolation of data from the Board of Governors of the Federal Reserve System, Release Z. 1 Flow of Funds Accounts of the United States, Washington, DC: BOG, and from the Board of Governors of the Federal Reserve System, Survey of Consumer Finances, Washington, DC: BOG. Full data, definitions, and methodology are available in Christian Weller and Eli Staub, 2006, Middle Class in Turmoil: Description of Methodology and Discussion of Findings, Washington, DC: Center for American Progress and Washington, DC: Service Employees International Union. "n.a." indicates that data are not available. Please note that the data in this table are not directly comparable with the figures from the tables presented in the original report since those were based on the Survey of Consumer Finances, whereas the calculations here are based on the Flow of Funds.

# The Middle Class Knows It's Losing Ground

Americans realize their financial health is increasingly at risk. The effects of the economic trends detailed in the previous table and chart are the culmination of declining incomes, rising prices, and decreasing wealth, all of which weigh heavily on the American public—especially since they worsened in 2008. A July 2008 Gallup poll showed that 87 percent of Americans believe that economic conditions are worsening overall at the moment, which is up from 78 percent at the start of 2008.[2] Additionally, half of the respondents assigned the economy a "poor" rating.

According to a recent Rockefeller Foundation/*Time* Magazine survey, 72 percent of those polled believe that Americans in general are less secure now than they were 10 years ago. This is up from the 63 percent of respondents who felt this way in 2007.[3] Additionally, 47 percent of respondents said that they are worried about their personal economic security—almost double the 24 percent who felt this way in 2007.

It is not just a vague feeling of insecurity, either. In June 2008, 15 percent of respondents to a Gallup poll said that they were no longer able to afford the cost of driving or commuting, and 11 percent said that the price of gas had affected their budget and standard of living to the extent that they either had little to no disposable income or their budgets were being destroyed.[4] Thirty-seven percent of respondents to the 2008 Rockefeller/*Time* Magazine survey reported that they had failed to pay a bill on time in the last year, up from 28 percent a year before, while a quarter said they had not gone to a doctor because of the cost, up from 18 percent in 2007.[5]

These are not just snapshots of the current situation. According to a spring 2008 national public opinion survey conducted by the Pew Research Center, just 41 percent of Americans feel that they are better off now than they were five years ago, while 31 percent feel that they are worse off.[6] This is the most pessimistic assessment of short-term personal progress in the 44 years that Pew has been asking the question.

Additionally, a growing number of Americans believe that it is becoming more difficult to maintain a middle-class lifestyle. Seventy-nine percent of self-defined middle-class families believe that it is more difficult to sustain their standard of living today than it was five years ago, while 65 percent felt that way in 1986.[7] All this public polling data reflects Americans' intrinsic understanding of the burgeoning economic and financial headwinds they face as the U.S. economy turns south after seven years of economic growth.

## Families see no income gains in weak labor market

The economic data confirm the economic pressures that Americans are feeling. It starts with a weak labor market that never really recovered after the last recession at the turn of the century, but also includes sharply higher prices and deteriorating personal wealth since then.

After the U.S. economy emerged from its last recession in November 2001, it continued to lose jobs for another 20 months, reaching its lowest level in August 2003. The years thereafter, however, were not marked by particularly fast job growth. In the end, from March 2001 through the end of 2007, the U.S. monthly job growth averaged an annual rate of 0.6 percent, less than one-third of the job growth of previous business cycles.[8]

Securing a job also doesn't necessarily mean what it used to. Hourly wages, after accounting for inflation, grew by a total of only 2.1 percent from March 2001 to December 2007. Inflation-adjusted mean weekly earnings grew by an even more anemic 1.2 percent during the same period.[9] Furthermore, the share of people with employer-sponsored health insurance dropped to 59.7 percent in 2006, the last year for which data are available, down from 64.2 percent in 2000.[10] Over the same period, the share of private-sector workers with an employer-sponsored retirement savings plan declined to 43.2 percent from 50.3 percent.[11]

With the start of 2008, the labor market took a turn for the worse. The U.S. economy lost a total of 438,000 jobs in the first six months of 2008, and average monthly job growth was only 1,300 jobs over the 12-month period ending in June 2008. This was a substantial decline from the average monthly job growth of 142,900 jobs in the previous 12 months, and 194,700 in the 12 months before that. These figures highlight starkly the slowing job market.[12]

With mounting job losses, the unemployment rate rose, too. The national unemployment rate hit 5.5 percent in May 2008—the highest rate since October 2004—and remained at that level in June 2008. Minorities have been disproportionately affected by the weakening labor market. The June 2008 unemployment rates were 9.2 percent for African Americans, and 7.7 percent for Latinos, compared to 4.9 percent for whites.[13]

Wages also fell over the first half of 2008. Hourly earnings decreased in inflation-adjusted terms by 1.2 percent, and weekly earnings dropped by 1.5 percent between the end of 2007 and June 2008. Consequently, hourly wages were only 0.9 percent higher than at the start of the current business cycle, and weekly wages were actually lower by 0.3 percent.[14]

## Families have to pay more for basics

Higher prices for basic necessities exacerbate the pain of a weak labor market for middle-class American families. In particular, the rising costs of gasoline and food weigh heavily on consumers' budgets so far this year. In April 2008, the national average price of regular unleaded gasoline easily shattered an inflation-adjusted record that had stood since March 1981, and they have only continued to climb since then. According to the Energy Information Administration, the national average price for regular unleaded gasoline stood at $4.05 per gallon in June

2008, the most recent complete month for which data are available.[15] This is a 26.5 percent year-over-year increase, adjusted for inflation, and a painful 133.1 percent increase since March 2001.[16]

Related to the recent upsurge in the price of gasoline are increases in transportation costs, which were 11.4 percent higher in June 2008 than they were the previous June and 33.5 percent greater than they were in March 2001.[17] And then there's the cost of groceries. As a quick comparison of last week's grocery bill to one from last year shows, food prices have jumped in recent months. Nominal food prices increased overall by 5.3 percent between June 2007 and June 2008—and by a notable 24.4 percent since March 2001.[18]

In addition to food and gasoline, families are also paying more for other necessities that they cannot simply cut out of their budgets. Costs associated with medical care increased by 4.0 percent between June 2007 and June 2008, and by 35.0 percent since March 2001.[19] Fuels and utilities cost 12.3 percent more in June 2008 than they did in the previous year, and a notable 48.1 percent more than in March 2001.[20]

Finally, and perhaps most alarmingly for the long-term financial health of the middle class, college tuition increased by 6.4 percent between June 2007 and June 2008.[21] This gateway to the diploma that many say holds the key to the middle class is up an astonishing 66.9 percent from March 2001.[22]

## Family wealth has been decimated

The final part of the middle-class insecurity trifecta is diminishing household wealth. For much of this business cycle, sharp increases and record amounts of household debt had an adverse effect on total wealth. Since the second half of 2007, financial market troubles, sparked by the fallout from the subprime loan crisis and the weakening economy, have also reduced asset values.

With the cost of seemingly everything increasing while families' incomes remained stagnant, families used their rapidly appreciating homes as emergency ATMs. The results were swiftly rising debt levels that reached ever new record highs. From March 2001 to March 2008, the last quarter for which data are available, household debt relative to personal disposable income grew almost four times as fast as it did during the 1990s. Consequently, household debt averaged 132.4 percent of disposable income in the first quarter of 2008, slightly lower than the record high of 133.5 percent set in the previous quarter.[23]

This translated into less financial security over time. Total financial wealth (the difference between assets and debt) relative to disposable income fell far short of the lofty peaks of the 1990s.

The wealth destruction due to the stock market crash at the beginning of this decade, the subsequent mortgage boom—which carried many middle-class families deeply into mortgage debt—and the ensuing collapse of the housing bubble, is breathtaking. Financial wealth relative to disposable income reached an all-time high of 406 percent at the end of 1999 before falling sharply in the wake of the stock market crash of the early 2000s, and then recovering slowly. Still, it had only climbed to 307.1 percent of disposable income by the third quarter of 2007, before dropping again as financial market troubles started to mount and as financial

wealth-to-income fell to its lowest level since the third quarter of 2004. To put it differently, had financial wealth relative to disposable income stayed at the level of late-1999, American households would have had an additional $13.0 trillion in financial wealth.

To some degree, this loss of wealth was offset by higher house values, although the last few years are still characterized by a massive loss of total personal wealth. Total personal net worth was equal to 617.9 percent of disposable income at the end of 1999. By early 2008 it had fallen to 532.9 percent—again the lowest level since the third quarter of 2004. Had the ratio of wealth to personal disposable income remained as high as it was at the end of 1999 through early 2008, then families would have had an additional $8.9 trillion in personal wealth. Family wealth clearly suffered from the onslaught of a stock market crash, a mortgage boom, and a bursting housing bubble.[24]

## The trifecta of middle-class financial insecurity is taking its toll

All measures of household economic distress have been rapidly moving higher. For instance, the share of mortgages entering foreclosure stood at a record high of 1.0 percent in the first quarter of 2008, after rising for an unprecedented eight quarters in a row. Consequently, the share of all mortgages in foreclosure reached a record high of 2.5 percent in early 2008.[25]

Other measures of household economic distress are also quickly moving higher. The personal bankruptcy rate—bankruptcy filings relative to total population—rose to 2.7 filings per 1,000 in the fourth quarter of 2007, an increase of 85.2 percent from 1.5 cases per 1,000 people in the first quarter of 2006, right after changes to the bankruptcy code were enacted.[26]

What's more, the share of credit card loans that are being written off due to defaults (known as the charge-off rate) reached 4.7 percent in the first quarter of 2008. This marked an increase of 50.2 percent from the first quarter of 2006, which was again heavily influenced by the changes to the bankruptcy code. Finally, the charge-off rate for credit cards in the first quarter of 2008 was the highest level since the fourth quarter of 2004—not counting the artificially high charge-off rate of the fourth quarter of 2005, just before the new bankruptcy law went into effect.[27]

# Conclusion

It has escaped few observers that America's middle-class families are struggling. The combination of falling incomes, rising prices, and disappearing wealth are abundantly displayed in the economic data, in news reports, and in polling results. Nor is this a recent phenomenon. Instead, it is characteristic of the current business cycle that started in early 2001. The financial security of America's middle class has dropped since early 2001, easily erasing all gains made during the 1990s.

Because this is not an isolated phenomenon, but rather a longer-standing trend, it will require serious leadership on economic policy to reverse course. The policy response will have to fall into three separate areas. First, the incomes of middle-class families will need to rise in a growing economy. Stronger labor market institutions and broader benefits coverage will be necessary to correct the disappointing trends of the past few years, in which a growing economy and high profits stood opposite declining incomes and disappearing benefits.

Second, families must be able to build wealth as a cushion against unavoidable emergencies and as a tool to invest in their future. Progressive saving incentives are a first strong step toward building more wealth for low-income and moderate-income families, as are improved health insurance coverage and stronger pensions.

Third, families need to become better insulated from price shocks for basic necessities. Increased energy efficiency, more investment in alternative fuels, and greater investments in information technology and efficiency in the health care sector can make a substantial difference in this area.

These steps will not happen by themselves. They will require strong political leadership from policymakers, who understand the struggles of America's middle class and who are willing to pursue policies that can rebuild economic security, instead of simply ignoring the obvious signs of mounting troubles. The fillip to our economy will be renewed economic growth, but this time broad-based growth that helps restore vitality and vigor to America's middle class, and offers more opportunities for lower-income Americans to work and save their way toward the American Dream.

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# About the Authors

Dr. Christian E. Weller is an Associate Professor of Public Policy at the University of Massachusetts Boston and a Senior Fellow at the Center for American Progress. His expertise is in the area of retirement income security, macroeconomics, money and banking, and international finance. He is also a research scholar at the Political Economy Research Institute at the University of Massachusetts Amherst. Prior to joining the Center, he was on the research staff at the Economic Policy Institute, where he remains a research associate. Dr. Weller has also worked at the Center for European Integration Studies at the University of Bonn in Germany, under the Department of Public Policy of the AFL-CIO in Washington, D.C., and in banking in Germany, Belgium, and Poland. Dr. Weller is a respected academic with more than 100 academic and popular publications. His academic publications have appeared in the *Journal of Policy Analysis and Management*, the *Journal of Development Studies*, the *Cambridge Journal of Economics*, the *Journal of International Business Studies*, the *Journal of Aging and Social Policy*, and the *Journal of Economic Issues*, among others. His popular writings have been published in the *New York Times*, *USA Today*, and the *Atlanta Journal Constitution*. He is the co-author (with E. Wolff) of *Retirement Income: The Crucial Role of Social Security* (Washington: Economic Policy Institute, 2005) and co-editor (with T. Ghilarducci) of Employee *Pensions: Policies, Problems and Possibilities* (Ithaca, NY: Cornell University Press, 2007). In 2006, he was awarded the Outstanding Scholar-Practitioner Award from the Labor and Employment Relations Association. In 2007, he was elected to the board of the Labor and Employment Relations Association, one of the country's largest associations for professionals in the fields of labor and employment relations. His work is frequently cited in the press and he is often a guest on national TV and radio programs. Dr. Weller holds a Ph.D. in economics from the University of Massachusetts at Amherst.

Amanda Logan is a Research Associate with the Economic Policy Team at the Center for American Progress. Her work largely focuses on issues surrounding lower- and middle-income American families, including prices for necessities, wages and benefits, economic distress such as bankruptcies, and how they view economic policy. Amanda has been with American Progress since 2006 where she first worked as Special Assistant for Economic Policy. Prior to joining the Center, Amanda interned at the Center for Economic and Policy Research, the European Parliament, the National Low Income Housing Coalition, and the Idaho National Laboratory. She has appeared on radio programs and her work has been referenced in national media outlets such as *The New York Times*, *The Nation*, *U.S. News and World Report*, CNN, and NBC Nightly News. A native of Idaho Falls, ID, Amanda graduated summa cum laude from Moravian College in Bethlehem, PA with a bachelor's degree in economics and political science.

# Endnotes

1 Due to data limitation, we forecast the cost of a medical emergency based on the methodology detailed in Christian Weller and Eli Staub, 2006, Middle Class in Turmoil, CAP Economic Policy Report, Washington, DC: Center for American Progress. This forecast is based on the share of people who are not covered by health insurance. Since health insurance data for 2007 are not available, we assume that the share of the uninsured remained the same in 2007 as in 2006. If the share of the uninsured increased, the cost of a medical emergency is likely higher in reality than our forecast. Thus, we could very well understand the actual deterioration in middle-class security.

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16 Authors' calculations based on Energy Information Agency, "Monthly Retail and Gasoline and Diesel Prices." Last updated July 14, 2008, available at http://tonto.eia.doe.gov/dnav/pet/pet_pri_gnd_dcus_nus_m.htm and Authors' calculations based on U.S. Department of Labor, Bureau of Labor Statistics, "Consumer Price Index," July 16, 2008, available at http://www.bls.gov/cpi/home.htm.

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