An Introduction to the History of Debt

It is difficult to consider debt as having a history, because it seems like debt might be that impossible thing in history, something that has existed forever. In 1917, one popular historian described debt as a "semi-slavery . . . [which] existed before the dawn of history, and it exists today."[1] People, in a certain sense, have always lent money to one another: over the dinner table to a wayward brother; across a saloon bar to a good customer; over a lunch pail to a hard-pressed co-worker. But even by 1917, as that popular history was written, the ancient, personal relationship of debt was changing into something that had never happened before.

While personal lending had always existed, before 1917 it had never been legal to charge interest rates high enough to turn a profit and, equally important, lenders had never been able to resell their customers' debts or borrow against them. In short, personal debt had never been able to be a normal business. Personal debt remained disconnected from the great flows of capital—confined to the margins of the economy. The big money in America was made by turning the hard work of Americans into commodities, not by lending those workers money. The wealthy could get personal loans at banks, alongside their business affairs, but for everybody else credit remained outside the conventional economy. Why would the Carnegies and Morgans of the world want to tie up their capital in loans to steelworkers, when they could make so much more money by building steel plants? When friends and family were tapped out, loan sharks—whose interest rates dwarfed even the most subprime of lender's rates today—could provide cash, but these small-timers could never compare in power or wealth to the Gilded Age titans of steel and rail. By the end of the twentieth century, however, such petty loans to workers had become one of American capitalism's most significant products, extracted and traded as if debt were just another commodity, as real as steel. Consumer finance had moved from the shadowy margins of capitalism into its brightly lit boardrooms, remaking, in its wake, the entirety of the American economy. In *Debtor Nation*, I explain how this financial revolution happened.

Personal debt assumed a new role within American capitalism once it became legal, sellable, and profitable. These developments did not occur all at once, but happened over the course of the twentieth century, beginning after World War I, and resulting as much from entrepreneurial innovation as governmental policy. These shifts in lending and borrowing practices were neither inevitable nor obvious. Policymakers, in numerous instances, often acted with the best of intentions, seeking to solve pressing economic and social problems, like unemployment, wealth inequality, and discrimination. Yet the policies, once enacted, often had far-reaching, unexpected consequences. For lenders, figuring out ways to extend credit met with both success and failure. The short-hand way in which historians describe capitalist decision-making as "profit maximizing" obscures the gut-wrenching difficulty of discovering new ways to make money. But once discovered, whether borne by profit or inscribed in law, new ways to lend spread throughout the economy. At certain junctures, which are the focus of this book, sudden changes in the larger political, economic, and social structures surrounding debt abruptly reoriented lending practices.

These moments of transformation came from all quarters, and while the most powerful institutions—commercial banks, corporations, government agencies—frequently played the most crucial roles, those with less power in America, when organized, contributed to the changes as well. Common to all these shifts, however, were new ways of regulating and reselling debt. Regulation—either its presence or its absence—made legal lending possible, but its relative strength and enforcement propelled lending in some unexpected directions. As much innovation in consumer lending resulted from evading government regulation as from obeying it. Laws and regulations, such as those on installment contracts and mortgage loans, created standards for how debt was lent, allowing investors to evaluate the worth of the loans. With known values, debts could be sold like commodities or borrowed against like assets. All modern consumer lending relied on creditors' abilities to act as middlemen, either directly by reselling the debt or indirectly by borrowing themselves. Resale allowed lenders to extend far more money than they themselves possessed by tapping into mainstream sources of capital. These networks of indebtedness enabled capital to flow from investors to lenders to borrowers. These debt markets, essential for the growth of American borrowing, relied not only on private capital but government intervention. The government made the resale of debt possible, not just through the enforcement of contracts, but in many instances by actually creating the basic institutions for buying and selling loans—making markets—like the government-made quasi-corporation Fannie Mae.[2] Government regulators sought to control economic life by regulating positively and negatively, creating incentives for businesses or punishing them for defiance. Allocating capital to invest in consumer debt was neither natural nor inevitable and the state had the power, within limits set by profit, to guide the economy. Frequently in *Debtor Nation*, it was not by the invisible hands of the market but by the visible minds of policymakers that new financial instruments and institutions were invented, causing these moments of rapid change. These two features—regulation and resale—combined in some unexpected ways to radically expand American borrowing.

Debtor Nation begins in that heady period after World War I, when installment credit and legalized personal loans first became big business. In chapters 1 through 4, consumer credit enters the mainstream of American financial life, as business and government forge new links between consumers and capital. Consumer credit, as we know it today, did not precede the mass production economy of the 1920s. Though the core profits of American capitalism were realized through manufacturing, for the first time consumers needed financing to pay for all the goods that were turned out.[3] Usury laws, at the same time, were relaxed around the country, as progressive reformers attempted to create a profitable alternative to loan sharks for industrial workers. During the 1930s, in an attempt to right the floundering economy, New Deal policymakers devised the mortgage and consumer-lending policies that convinced commercial banks that consumer credit could be profitable, despite the bankers' long-held reluctance to lend to consumers. During World War II the government attempted to regulate installment lending in order to contain inflation, but this intervention only pushed retailers to devise debt relations outside the regulations, disseminating a new hybrid form of credit—revolving credit—across the country. The postwar world underpinned by debt emerged from these practices, developed intentionally and unintentionally through government intervention.

Following World War II, new suburbanites realized the American dream through borrowing. In chapters 5 and 6, we see how consumer credit is inextricable from the postwar dream. Borrowing was at the core of both postwar affluence and its decline, demanding a reconsideration of our nostalgia for the postwar economy. Suburban Americans left government-mortgaged homes in installment-financed cars to shop on revolving credit at shopping centers. These consumers borrowed more but they could also pay back what they owed. Americans learned to borrow in the midst of prosperity when, confident of stable future incomes, debt enabled consumers to buy more and live well. While growth persisted, indebted consumers experienced few deleterious effects. Consumers borrowed because they believed that their incomes would continue to grow in the future—and they were right. Incomes rose steadily after the war from 1945 to 1970. Money borrowed today could be paid back more easily tomorrow and—as a bonus—consumers could buy that new television today! Financial institutions lent more money, and borrowers paid it back. In a time of rising incomes that were stable, consumers' expectations and borrowing were quite reasonable.[4] Unfortunately the postwar period, which defined "normalcy" to a generation of borrowers, was the aberration.

As postwar growth transitioned into stagflation, cracks began to appear in the foundation of the economy. In chapter 7, our contemporary debt system emerges through the popularization of credit cards and debt securitization. In the 1970s, unpaid debt skyrocketed not because consumers began to borrow, but because they *continued* to borrow as they and their parents had done since World War II, but without the postwar period's well-paying jobs. Consumers of the 1980s increasingly borrowed to deal with unexpected job losses and medical expenses as much as to live the good life, returning to a credit world that had more in common with the 1920s than with the 1950s.[5] A credit system premised on rising wages and stable employment was reappropriated to shore up uncertain employment and income inequality. Though credit could be used to grapple with short-term unemployment and decreased income, in the long-term loans still had to be repaid. Credit could dampen the swings of short-term fortunes, but it could not change long-term fates. Buoyed by a long-boom in housing prices, Americans used asset-growth to substitute for wage-growth, which worked fine as long as house prices continued to rise.

Consumer borrowing in the 1970s was not new, but the amount that creditors were willing to lend was. While earlier twentieth-century lending depended on the resale of debt, that resale was always between two parties that knew each other—mortgage company and insurance company or finance company and commercial bank. These networks of resale enabled the flow of capital from investors to borrowers, but these channels of resale were necessarily limited to networks of skilled buyers and sellers. While borrowers and lenders referred to "debt markets," these highly structured, highly regulated networks bore little resemblance to the chaos of a market. After the 1970s, however, new financial instruments, asset-backed securities, allowed these networks to become markets. Credit markets were deep, anonymous, and global. Capital could come from anywhere or anyone and be invested in consumer debt. This financial marvel, born of both Washington and Wall Street, midwifed the grand expansion of late-twentieth-century borrowing, enabling Americans to borrow more even while their incomes became more precarious. Capitalist structures changed more than consumers' thriftiness.[6] Because of the clever structuring of the financial instruments, the supply of lending capital was nearly limitless.

The particular forms that borrowing took—installment contract, credit card, balloon mortgage—mattered as much as how much people borrowed. Simple aggregate statistics, while meaningful and easy to understand, do not convey how debt made consumer lives possible, or how they constrained those lives. Each chapter focuses on particular debt practices and how they were created by the struggles between borrowers, lenders, and investors in a particular historical moment. The lending methods recounted in this book are but a streamlined sample of the nearly infinite ways devised to extend credit. Yet, even within that variety, a few forms took root, proliferated, and dominated. Placing debt instruments at the center of the narrative between consumers, business, and the state, shows how the formal arrangements of debt reshaped and reflected economic power. Simply telling the experiences of individuals, without the larger story of instruments and institutions, would mask the murky processes that put borrowers into debt.

If the debt relation between borrowers and lenders always took a specific form, then behind the lenders always resided the always protean capital. For borrowers, the fungibility of money meant that one form of debt could be paid off with another. The modern debt regime relied on this convertibility, not only to transform installment contracts into personal loans or credit card debts into home equity plans, but to turn the wages of labor into debt repayment as well. The transformation of labor into capital, and debt into other debt, is the crux of how the credit economy operates. To cordon off these transformations one from another, as we do when we, for instance, sanctimoniously discuss "non-mortgage debt" separately from "mortgage debt," obscures the indispensable commutability of capital. For lenders, transforming capital into debt was the essence of their business.

Capital ultimately comes from somewhere. When we need money, most of us wonder only if we can get it, and aside from the person who gives us the money, do not really care where the money comes from. Yet, once you start to think about it, how can credit card companies finance the trillions that Americans owe them? Trillions, even to bankers, is a lot of money. The source of that capital, while finite, is vast, and over the century it began to come largely from outside banks' own coffers. The story of how lenders, bankers, and non-bankers acquired the capital to lend must therefore also be told, if we are to comprehend the history of debt. Finding new sources of capital allowed for new kinds of lending. Credit cards, which in a lender's utopia, are never paid off, are extremely capital-intensive. Only when capital can be had cheaply and in vast quantities can such lending be possible. To understand how the debt economy works, we need to know not just the last instance of lending—when we get our loan—but the vast network of capital that funds that loan. Tracking the movement of capital, and how it changes over time, explains a great deal about the ultimate choice that that lender makes in giving or denying a loan. To truly discern the operations of capitalism, we must grapple with how capital gets allocated in our economy and how this allocation affects our everyday lives.

The expansion of American borrowing deals with the very foundation of capitalism: How is capital allocated? The institutional connections of capital between different forms of capitalist enterprise made the choice to borrow—to get that auto or house or surgery—possible. The flow of capital, within and between businesses, must necessarily be at the center of that history. Yet, no sinister capitalist cabal put Americans in debt.[7] The same banal investment decisions—where can this dollar get the greatest return?—that produced our nation's wealth-producing farms and factories also produced our omnipresent indebtedness. The increasing relative profitability of consumer lending is what has driven the expansion of consumer borrowing. Debt's rising profitability attracted capital that otherwise would have been invested in other enterprises. What made our indebtedness possible was that it became profitable.

The two features of modern lending—regulation and resale—made consumer lending profitable, but the profits of investing in debt relative to other investment opportunities varied over time. In the early twentieth century, installment debt helped large manufacturing companies realize the profit on their production, but could not compare in profitability. Personal loans, while a good small business, were ignored by large banks until the 1930s, when banks began lending to consumers only out of desperation and government policy. In the postwar period, consumer debt, especially revolving credit, began to become more profitable, but was still not as profitable as retail or manufacturing. In short, consumer credit, while important, was a means to end. By the 1960s, and increasingly in the 1970s and 1980s, consumer credit became an end in itself, as a rapidly expanding profit center. The profitability of personal debt—emerging after World War I, consolidating in the postwar period, and accelerating in the 1970s and 1980s—slowly reoriented American banks and corporations away from producing and distributing goods to financing them, with dire consequences for both the long-run stability of their enterprises and for the American worker.[8]

Searching for the "human" face of capitalism has led historians to focus too much on cultural ideas of debt—neglecting the history of business and politics, fundamentally misinterpreting what has happened, and missing the opportunity to tell an all-too-human story of how our choices, large and small, have brought this debt-driven economy to pass. There exist shockingly few histories of the modern credit system and those that do exist focus on culture—framed as morality—to the exclusion of business.[9] Such elisions are not unique to the history of debt, but are endemic within the history of American capitalism. Recent historiographic debates over twentieth-century capitalism, usually framed as consumer capitalism, have largely transpired on capitalism's surface, ignoring the deeper connections of finance.[10] Cultural historians have pointed to advertising, while consumer historians, entranced by the everyday world of goods surrounding them, have largely ignored the institutions that financed and created them. Such a prioritization has been understandable given that, for most consumers, this is where capitalism intersects with their lives. How people experience the world of things is important. At the same time, historians of all stripes have tended to fetishize consumer goods, overlooking the flows of capital that brought those goods into existence.

Our financial lives cannot be understood apart from the rest of our lives. Seeing the world of finance as elite and somehow outside the purview of social history, historians have largely neglected one of the key sources of power in our society. Credit operated not in opposition to categories of race and gender but through them. Part of what makes race and gender meaningful in our society is how capitalism relies on them to organize the relations of production, distribution, and consumption. At a basic level, consumer lending depended on gender, and its associated naturalized operations of power, to legitimate systems of control between male lenders and female borrowers. In related, but not equivalent ways, lending was circumscribed and transmitted along lines of race. A simple story of how African Americans and women were excluded from credit might make for impassioned historiography but would also be inaccurate. African Americans and women always had access to credit, but not always the same credit as white men, whose credit was cheaper and easier to get. In many ways, the modern credit system of the twentieth century was built by white men for white men, leaving other Americans to borrow in older, more expensive and dangerous, ways. Mortgage lending has been the most widely discussed way in which race has shaped credit relationships, but race, in more indirect ways, has also constrained the credit options for poor, urban African Americans in the postwar period that would have been inconceivable for the rest of America. While on some level, the history of credit discrimination is an important component of the narrative of this book, I also take pains to emphasis that credit is but one part of American capitalism, whose inequities cannot be simply solved by guaranteeing raceless and genderless credit access. Politicians in the 1960s, witnessing the success of credit access for postwar white people, seized on mortgages as an easy fix for income and wealth disparities, with sometimes dire consequences. The distribution of power in an economic system structured through race and gender cannot be easily freed of those categories, particularly if the economic roles that such social categories play are not fully acknowledged. Helping to return capitalism to the center of twentieth-century historiography will bring together the divergent scholarships of financial and social history, giving us a fuller picture of the twentieth-century United States.[11]

Despite capital's global mobility, every place has produced its own unique way to practice lending and repayment.[12] Installment credit was widespread in Western Europe in the first third of the twentieth century, as in the United States. Developing similar institutions, like finance companies, Europeans provided installment credit for the same purposes as Americans—to finance their manufacturing economies. European manufacturers, especially auto manufacturers, encountered the same challenges as their American counterparts. World War II provided a decisive break between the United States and other countries. While the rest of the developed world scraped together capital to rebuild the industrial infrastructure lost during the war, the United States exulted in its prosperity, as the sole remaining capitalist superpower.[13] While other countries also had uranium, wheat, and oil, no other country possessed our surplus of capital. This abundant capital allowed the United States to finance its postwar consumer prosperity. Other countries needed capital to put into financing production, but we had enough to also finance consumption. Abundant capital made possible, but not inevitable, the forms and extent of consumer financing that developed during World War II and in its aftermath. To understand the path of American financial development, we need to pay particular attention to the hard decisions made by firms and regulators during and after the war that led to that uniquely American invention—revolving consumer credit. A truly global history of debt would compare these two trajectories in the developed world until the war, and then show how they diverged after the war until the mid-1960s, when the capital imbalance between the United States and the globe began to shift back to what it had been traditionally. The breakdown of this temporary order, most visible in the collapse of the Bretton Woods system, prefigured a transition back to a more volatile world of global integration and competition, where the flows were not nearly so unilateral and once again, capital investment was more difficult to carry out profitably. While a global history of debt would, no doubt be fascinating, it was beyond the scope of this work to do so. What is lost in comparative perspective, I hope, is gained in the specificity of the American experience. In the United States, we see the first example of an economy based upon debt that can be resold at a profit, with all its associated possibilities and dangers.

This history of the infrastructure and practices of American debt will both help us to understand the financial history of the postwar period and, more generally, to come to grips with the choices that have created our contemporary indebted society. No single cause can explain the entire history of borrowing and lending: profit motive, government policy, technological progress, and even chance all played necessary but not sufficiently all-encompassing roles. Though to be sure there were hucksters who gamed the system, the choices responsible for today's economic crisis were not hidden, but done in the open, and often with the best of intentions. More terrifying than individual malfeasance or trickery is the idea that the structure of our economy itself is fundamentally out of alignment. This fear is not new. Anxieties about America's future are as old as the republic itself and fears about debt older still. But the present organization of our economy and our lives is as it has never been before. Despite the high profit of high finance, we may not be able to build as resilient an economy from debt as we did from steel. To understand today's credit system requires understanding the history of how consumer credit and twentieth-century American capitalism co-evolved to create both our prosperity and our insecurity.