The recent economic slowdown has shrunk federal revenues, reduced projected budget surpluses, and drawn policymakers' attention to a difficult dilemma. Fulfilling benefit promises under Social Security and Medicare will be easier if the economy grows rapidly. This, in turn, depends on how much the nation saves and invests. Because federal surpluses add to national saving, some believe that the recent tax cut should be scaled back and federal spending curbed. Doing so, however, could erode the chance of a quick economic rebound in the short term.

From this perspective, our saving in the past few decades has been dismal. The net national saving rate has been declining since the mid-1970s. The latest data show that the upturn of the 1990s has reversed, leaving today's net national saving rate at a meager 1.6%, a historical low. Sharply rising personal consumption expenditures contributed significantly to the drop in saving over the past few decades. Recently, government consumption as a share of the net national product has also increased, accelerating the saving decline. Lower saving is mirrored in net domestic investment, although the latter has been sustained at higher rates by foreign borrowing. Net domestic investment, which accelerated sharply during the record growth spurt of the 1990s, has plateaued for the past two years.

The steep growth in personal consumption suggests that U.S. households are not saving enough for retirement. A recent study concludes that even if Social Security and Medicare deliver promised benefits, workers who are close to retirement must save at very high rates if they wish to retire with their current living standards intact.