

## *The Economy in Perspective*

*New Year's resolutions...* You know the drill: On New Year's Eve, you write a list of three or four critical wrongs that you swear to right in the year ahead. Some of us—the real masochists—even drag last year's embarrassing list out of its hiding place and read it before repeating the ritual. Perennially resolute, we vow to lose weight, stop smoking, and get more exercise. This year, let us also promise to raise the level of economic discourse and improve our treatment of certain subjects.

Consumer spending tops the list of mistreated subjects. Consumer spending accounts for about two-thirds of all purchases in the U.S. economy, dwarfing the business, government, and foreign sectors. This makes it a tempting subject for economic pundits in search of a whipping boy. During the 10-year expansion of the 1990s, the American consumer was severely chastised for his unruly ways—his declining saving rate, his increasing debt burden, and his growing indifference to declaring bankruptcy—and the righteous prayed for his speedy return to the fold.

Now it turns out that the righteous are in less of a hurry to reform the consumer. Ever since the recession began, much has been made of the profligate consumer's healthy influence on the U.S. economy. Retailers have used all their wiles to lure customers and convince them that now is not the time to bolster their savings accounts. After all these years, what's a little more debt anyway? Throughout the holiday shopping season, press reports focused on the resilient consumer, hoping against hope that he would not tucker out. Where once the active consumer was pilloried for his grasping, acquisitive ways, now he is glorified as the nation's economic linchpin, a veritable patriot.

There should be less moralizing about the consumer. Like corporations, consumers respond to incentives and act in what they perceive as their best interests. Without delving into the relative merits of the personal saving rate for gauging household saving, we may just say that this measure progressively declined as the expansion, the stock market, and consumer confidence advanced. The saving rate attained notoriety when it hit zero in 2000. Why did saving decline? Many households became wealthier and expected to remain so in the future. Financing new homes and automobiles made sense to households because the income to support the debt appeared stable; the interest rates associated with the debt continued to decline; and the prices of many consumer goods dropped, presenting great

bargains. Now that households are less wealthy than they were just a few years ago and have different expectations about their future wealth, the personal saving rate has begun to rise again toward its longer-term average—although, at 4%, it is still only about halfway there. Consumer retrenchment makes sense.

The economy evolves partly from the choices consumers make collectively, but individual consumers should bear no personal responsibility for that outcome. In particular, consumers cannot simultaneously prop up today's economy through increased spending and bolster tomorrow's economy through increased saving.

International trade is next on the list of mistreated subjects. Nations have decided, by and large, that open trade borders provide a better way to raise living standards than restrictive markets. The international trading system encompasses a complex array of bilateral and multilateral agreements, prima facie evidence that nations still manage their trade to some degree. During the past decade, however, as a result of these agreements, trade barriers have come down considerably and the cross-border movement of goods, services, and capital has mushroomed globally.

Global competition benefits consumers by providing access to a broader range of suppliers who must compete on price and service. In the United States, consumer prices for durable goods have been declining for five years, with intensified global trade likely playing an important role. U.S. exports and imports have each been increasing at rates faster than overall spending, a sign that companies located here are competing successfully abroad.

U.S. state and local government officials compete vigorously to attract companies—U.S. or foreign—looking for a local presence; they even routinely offer generous subsidies to clinch deals. Newcomer companies create jobs and pay taxes; these are, of course, the reasons why governments outside the region are constantly on the prowl for companies willing to locate in their regions. Comments about unfair trade occasionally ring true, but more often they obscure the most important points. Citizens in one place benefit as much by selling merchandise to buyers in another state as by selling to buyers in another country. Those citizens benefit from the economic prosperity of their trading partners, wherever and wherever they are.

We could make the list of subjects longer, but this year we resolved to be brief.