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Surveying the World of Ideas

Shop 'til We Drop?
by Robert J. Samuelson

We shop, therefore we are. This is not exactly the American credo, but it comes close to being the American pastime. Even infants and toddlers quickly absorb the consumer spirit through television and trips to the supermarket ("I want that," is a common refrain). As we age, consumption becomes an engine of envy, because in America the idea is that everyone should have everything—which means that hardly anyone ever has enough. The notion that wants and needs have reached a limit of material and environmental absurdity, though preached fervently by some social activists and intellectuals, barely influences ordinary Americans. They continue to flock to shopping malls, automobile dealers, cruise ships, and health clubs. There are always, it seems, new wants and needs to be satisfied.

Although consumerism now defines all wealthy societies, it's still practiced most religiously in its country of origin. Indeed, Americans have rarely so indulged the urge to splurge as in the past decade. Look at the numbers. In 2002, consumer spending accounted for 70 percent of U.S. national income (gross domestic product), which is a modern American record, and a much higher figure than in any other advanced nation. In Japan and France, consumer spending in 2002 was only 55 percent of GDP; in Italy and Spain, it was 60 percent. These rates are typical elsewhere. Even in the United States, consumer spending was only 67 percent of GDP as recently as 1994. Three added percentage points of GDP may seem trivial, but in today's dollars they amount to an extra $325 billion annually.

This spending spree has, in some ways, been a godsend. Without it, the U.S. and world economies would recently have fared much worse. During the 1997-1998 Asian financial crisis, the irrepressible buying of American consumers cushioned the shock to countries that, suddenly unable to borrow abroad, had to curb their domestic spending. Roughly half of U.S. imports consist of consumer goods, automobiles, and food (oil, other raw materials, and industrial goods make up the balance). By selling Americans more shoes, toys, clothes, and electronic gadgets, Asian countries partially contained higher unemployment. U.S. trade deficits exploded. From 1996 to 2000, the deficit of the current account (a broad measure of trade) grew from $177 billion to $411 billion.

Later, the buying binge sustained the U.S. economy despite the onslaught of bad news that, by all logic, should have been devastating: the popping of the stock market "bubble" of the 1990s; rising unemployment (as dot-com firms went bankrupt and business investment—led by telecommunications spending—declined); 9/11; and a string of corporate scandals (Enron, WorldCom, Tyco). But American consumers barely paused, and responded to falling interest rates by prolonging their binge. Car and light-truck sales of 17.1 million units in 2001 gave the automobile industry its second-best year ever, after 2000. The fourth- and fifth-best years were 2002 (16.8 million units) and 2003 (an estimated 16.6 million units). Strong home sales buoyed appliance, furniture, and carpet production.

To some extent, the consumption boom is old hat. Acquisitiveness is deeply embedded in American culture. Describing the United States in the 1830s, Alexis de Tocqueville marveled over the widespread "taste for physical gratification." Still, the ferocity of the latest consumption outburst poses some interesting questions: Why do Americans spend so much more of their incomes than other peoples? How can we afford to do that? After all, economic theory holds that societies become wealthier only by sacrificing some present consumption to invest in the future. And if we aren't saving enough, can the consumer boom continue?

Let's start with why Americans spend so much. One reason is that our political and cultural traditions differ from those of other nations. We do some things in the private market that other societies do through government. Health care, education, and social welfare are good examples. Most middle-class Americans under 65 pay for their own health care, either directly or through employer-provided health insurance (which reduces their take-home pay). That counts as private consumption. In countries with government-run health care systems, similar medical costs are classified as government spending. The same thing is true of education. Although U.S. public schools involve government spending, college tuition (or tuition for private school or pre-school) counts as personal consumption. Abroad, governments often pay more of total educational costs.

It's also true that the United States saves and invests less than other nations—investment here meaning money that, though initially channeled into stocks, bonds, or bank deposits, ultimately goes into new factories, machinery, computers, and office buildings. Low U.S. saving and investment rates have often inspired alarm about America's future. In 1990, for instance, Japan's national savings rate was 34 percent of GDP, more than double the U.S. rate of 16 percent. By outsourcing us, Japan (it was said) would become the world's wealthiest nation. That hasn't happened, in part because what matters is not only how much countries invest but how well they invest. And Americans generally are better investors than others.

Of course, there's waste. The hundreds of billions of dollars invested in unneeded dot-com and telecom networks in the late 1990s are simply the latest reminder of that. But the American business system corrects its blunders fairly quickly. If projects don't show signs of becoming profitable, they usually don't get more capital. Wall Street's obsession with profits—though sometimes deplored as discouraging long-term investment—compels companies to cut costs and improve productivity. If bankrupt firms (Kmart and United Airlines are recent examples) can't improve efficiency, their assets (stores, planes) are sold to others who hope to do better. American banks, unlike Japanese banks, don't rescue floundering companies; neither (usually) does the government, unlike governments in Europe. Getting more bang from our investment buck, we can afford to invest less and consume more.

Our privileged position in the world economy reinforces the effect. Since the 1970s, we've run trade deficits that have allowed us to have our cake and eat it too: All those imports permit adequate investment rates without crimping consumption. We send others dollars; they send us cars, clothes, and computer chips. It's a good deal as long as we're near full employment (when we're not, high imports add to unemployment). The trade gap—now about five percent of GDP—persists in part because the dollar serves as the major global currency. Foreigners—companies and individuals—want dollars so they can conduct trade and make international investments. Some governments hoard dollars because they'd rather export than import. The strong demand for dollars props up the exchange rate, making our imports less expensive and our exports more expensive. Continuing trade deficits result.

All this suggests that the consumer boom could go on forever, because Americans always feel the need to outdo the Joneses—or at least to stay even with them. No level of consumption ever suffices, because the social competition is constant. The surge in prosperity after World War II briefly fostered the illusion that the competition was ebbing because so many things that had once been restricted (homes, cars, televisions) became so widely available. "If everyone could enjoy the good things of life—as defined by mass merchandisers—the meaning of class distinctions would disappear," Vance Packard wrote in his 1959 classic The Status Seekers. Instead, he found, Americans had developed new distinctions, including bigger homes and flashier clothes.

Four decades later, little has changed. Americans constantly pursue new markers of success and status. In 2002, the median size of a new home was 20 percent larger than in 1987, even though families had gotten smaller. Luxury car sales have soared. According to the marketing research firm of J.D. Power and Associates, in 1980 luxury brands—mainly Cadillacs and Lincolns, along with some Mercedes—accounted for only 4.5 percent of new-vehicle sales. By 2003, luxury brands—a category that now includes Lexus, Infinity, and Acura, along with Hummers and more BMWs and Mercedes—exceeded 10 percent of sales. Second homes are another way that people separate themselves from the crowd. Perhaps 100,000 to 125,000 such homes are built annually, says economist Gopal Ahluwalia of the National Association of Homebuilders. In the 1990s, comparable figures were between 75,000 and 100,000.

To critics, this "consumption treadmill" is self-defeating, as Cornell University economist Robert H. Frank put it in his 1999 book Luxury Fever: Money and Happiness in an Era of Excess. People compete to demonstrate their superiority, but most are frustrated because others continually catch up. Meanwhile, over-consumption—homes that are too big, cars that are too gizty—actually detracts from people's happiness and society's well-being, Frank argued. Striving to
maximize their incomes, workers sacrifice time with family and friends—time that, according to surveys, they would prize highly. And society’s reluctance to take money out of consumers’ pockets through taxation means too little is spent to solve collective problems such as poverty and pollution.

As a cure, Frank proposed a progressive consumption tax. People would be taxed only on what they spent, at rates rising to 70 percent above $500,000. Savings (put, for example, into stocks, bonds, and bank deposits) would be exempt. The tax would deter extravagant spending and encourage saving. Frank contended. Total consumption spending would be lower, government spending could be higher, and the competition for status would simply occur at lower levels of foolishness. The “erstwhile Ferrari driver . . . might turn instead to [a] Porsche,” he wrote. Whatever their merits, proposals such as this lack political support. Indeed, they do not differ dramatically—except for high tax rates—from the present income tax, which allows generous deductions for savings, through vehicles such as 401(k) plans and individual retirement accounts.

Still, America’s consumption boom could falter, because it faces three powerful threats: debt, demographics, and the dollar.

Over six decades, we’ve gone from being a society uneasy with credit to a society that rejoices in it. In 1946, household debt was 22 percent of personal disposable income. Now, it’s roughly 110 percent. Both business and government have promoted more debt. In 1950, Diners Club introduced the modern credit card, which could be used at multiple restaurants and stores. (Some department stores and oil companies were already offering cards restricted to their outlets.) New laws—the Fair Housing Act of 1968, the Equal Credit Opportunity Act of 1974—prohibited discriminatory lending. One result was the invention of credit-scoring formulas that evaluate potential borrowers on their past payment of bills, thereby reducing bias against women, the poor, and minorities. Similarly, the federal government encourages home mortgages through Fannie Mae and Freddie Mac, government-created companies that buy mortgages.

This “democratization of credit” has enabled consumer spending to grow slightly faster than consumer income. People simply borrow more. Economist Thomas Durkin of the Federal Reserve notes the following: In 1951, 20 percent of U.S. households had a mortgage, compared with 44 percent in 2001; in 1970, only 16 percent of households had a bank credit card, compared with 73 percent in 2001. The trouble is that this accumulation of debt can’t continue forever. Sooner or later, Americans will decide that they’ve got as much as they can handle. Or lenders will discover that they’ve exhausted good and even mediocre credit risks. No one knows when that will happen, but once it occurs, consumer spending may rise only as fast as consumer income—and slower still if borrowers collectively repay debts.

What could hasten the turning point is the baby boom. We’re now on the edge of a momentous generational shift. The oldest baby boomers (born in 1946) will be 58 in 2004; the youngest (born in 1964) will be 40. For most Americans, peak spending occurs between the ages of 35 and 54, when household consumption is about 20 percent above average, according to Susan Sterne, an economist with Economic Analysis Associates. Then it gradually declines. People don’t buy new sofas or refrigerators. They pay off debts. For 15 years or so, the economy has benefited from baby boomers’ feverish buying. It may soon begin to suffer from their decreased spending.

Finally, there’s the dollar. Should foreign demand for U.S. investments wane—or should American politicians, worried about jobs, press other countries to stop accumulating U.S. Treasury securities—the dollar would decline on foreign exchange markets. There would simply be less demand, as foreigners sold dollars for other currencies. Then our imports could become more expensive while our exports could become cheaper. Domestic supplies might tighten. Price pressures on consumer goods—cars, electronics, clothes—could intensify. This might cause Americans to buy a little less. But if they continued buying as before, the long-heralded collision between consumption and investment might materialize. (As this article goes to press, the dollar has dropped from its recent highs. The ultimate effects remain to be seen.)

Little is preordained. Sterne thinks retired baby boomers may defy history and become spendthrifts. “They don’t care about leaving anything to their kids,” she says. “There’s no reluctance to go into debt.” Their chosen instrument would be the “reverse mortgage,” which unlocks home equity. (Under a reverse mortgage, a homeowner receives a payment from the lender up to some percentage of the home’s value; upon the owner’s death, the loan is repaid, usually through sale of the house.) Maybe. But maybe the post-World War II consumption boom has reached its peak. If the retreat occurs gently, the consequences, at least on paper, should be painless and imperceptible. We’ll spend a little less of our incomes and save a little more. We’ll import a little less and export a little more. These modest changes shouldn’t hurt, but they might. The U.S. and world economies have grown so accustomed to being stimulated by the ravenous appetite of ordinary Americans that you can’t help but wonder what will happen if that appetite disappears.


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