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Stimulating Consumption Won't Help Economy **by Sheldon Richman**

Many politicians, economists, and pundits — under the influence of Keynesian “economics” — worry that Barack Obama’s stimulus package won’t be stimulative enough because too much of the money might go to people who won’t spend it.

Typical is this recent [editorial paragraph](#) from the *New York Times* about the tax-cut component of Obama’s plan:

“The proposed tax break — up to \$500 for individuals and \$1,000 for families — makes good sense for low- and middle-income Americans, because the money is likely to be spent quickly, thus boosting demand in a contracting economy. But higher up the income ladder — a couple making \$200,000 a year is in the top 9 percent of households — tax cuts are likelier to be saved than spent, providing relatively little stimulus.”

The *Times* here, like so many others, attributes our economic problems to insufficient demand. We aren’t consuming enough, either because we don’t have the money to spend or because we just don’t want to spend it. Since we are stuck in this stubborn situation, so goes the Keynesian argument, the government must increase aggregate demand either by spending money itself or by putting money in private hands. But the problem, as the *Times* sees it, is that some of those private hands will grasp the money and won’t let go. They will — O Horror! — save it. Or, if you can imagine such a thing, they might pay down debt.

Anyone with common sense and innocent of Keynes’s crackpot views will wonder what the fuss is. Saving and paying off debt are generally seen as wise for individuals, so it makes no sense that they are bad for society as a whole. Yet that is what we our “leaders” expect us to believe.

Ask yourself: can you consume your way to prosperity? Of course not. So how can a society do so? Greater consumption is the effect not the cause of economic growth, yet this is so contrary to conventional wisdom that you can read newspapers and watch news programs for months without seeing this truth expressed.

To say the recession was caused by diminished demand is to say that the recession was caused by the recession. The fact is, people are holding on to their cash *because* the economy is in recession and they are uncertain about the future. As we'll see, it is exactly under these circumstances that people *should* be saving.

The idea that consumption needs to be stimulated is ridiculous on its face. Consumption is fun. It's saving that takes effort. Not long ago the American people were scolded for consuming too much and saving too little. Now it's the opposite. Will the scolds please make up their minds!

As noted, falling consumption is not the cause but rather the effect of recessions. So government-boosted demand, made possible by deficit spending and expansion of money and credit, can't be the solution. Recessions follow ill-advised government policies that channel investment into unsustainable projects, that is, projects that conflict with economic reality, such as the government-created housing boom, which misdirected billions of dollars into finance and construction. The recession is the process of correcting the errors that government policy encouraged. This correction involves the liquidation of inappropriate projects and therefore unemployment. Resources have to be redirected to projects consistent with economic reality. But resources are not malleable Play-Doh. They are specific machines, tools, and materials in particular places whose adaptation to new projects (when possible) is not costless. Workers may need to be trained for new jobs.

This process takes time and money, that is, investment. Investment requires saving. And saving requires deferred consumption. So this is a good time for people to save.

Saving is a form of spending. When a person abstains from consuming, he makes his money available to entrepreneurs who will buy capital goods and materials and hire workers. Saving is not inimical to a thriving economy. Quite the opposite.

So why doesn't the recession end quickly? The process takes time, but government also slows it down by creating uncertainty about what new meddling it will engage in. That's what is happening now. The best thing the politicians can do is lighten the burden of government. Now!

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