Column

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Medicine for economies

WE OFTEN OVERLOOK WHAT MAKES AN ECONOMY healthy. I read stories about reducing the deficit, spurring on businesses, rewarding the job creators, but none address America's dependence on consumer spending for its gross domestic product (GDP). Debates rage over what we count, but most sources claim that more than 70 percent of our GDP comes from consumer spending, compared to 55 percent during the 1950s.

For many Americans, the 1950s were the glory years. We baby boomers grew up playing with many fewer toys, living in much smaller houses, eating much smaller meals, and we generally view the time as patriotic and happy. Whatever the exact proportion attributable to business and government (the other two drivers of GDP) during the 1950s, it was, to the satisfaction of most economists, clearly larger than it is today. Yet as a nation we have taken a number of steps that have left our economy ever more dependent on consumption.

What big forces rolled back contributions of business and government? I think the root causes are overlooked.

First, back in 1954, just over a third of the U.S. workforce belonged to a union. This meant that business had to spend more, which upped its contribution and made consumers wealthier—thereby also upping consumers' contribution. Further, unions train their members through apprenticeship programs, so business had a steady supply of capable and qualified workers, the lack of which is often a problem now for businesses looking to hire. Today, 12 percent of the workforce is in a union. Our workers receive a smaller share of the corporate spending budget, so profits rise but spending does not.

The second cause, a shift in the American psyche, is harder to quantify. Saving has fallen off, while spending has become respectable. It may be that we feel pulled to spend by advertising that bombards us, but it is also true that we no longer honor the hardworking, simple-living, solid-saving person. Perhaps the availability of credit lulls us into thinking the rainy day will never come.

When I was quite young, a man told me that of course he could afford a better car, but being wasteful wasn't Christian. Wow. Even if you substitute "a good person" for "Christian," that's a rare sentiment today.

A third factor is the influence of Wall Street on corporations. While in the 1950s top executives were paid 20 times what average workers received, today that figure is 204 times. This pay differential is generally granted as a reward for stock performance—the theory is you want the CEO's interest to be in synch with the investors'. Good stock performance is the result of two factors: rising corporate earnings and a larger profit margin. Spending now on something that might pay off in five years might help future CEOs but doesn't help now; stretching out maintenance expenses or cutting quality does. Average corporate profit margins during the 1950s were in the high 20 percent range; today they are in the high 30s. That's nice for shareholders and executive bonuses but lousy for growing the economy.

Then there's government. Government spending is dependent on two factors. The U.S. government must have the money to spend (collected via either tax revenues or borrowing), and it must have permission to spend, granted by Congress. Records from the Office of Management and Budget show a slight creep in spending of about 1 percent of GDP since the 1950s. The big contributor is health-care costs, but although the Affordable Care Act might bring government spending (relative to businesses and consumers) more in line with the 1950s, it still hasn't come close to taking up the slack left by lagging business spending.

So what's needed to grow the economy? Since corporations are unlikely to shift the executive incentives, perhaps we need to levy an "alternative tax" on these corporations. Ronald Reagan introduced this tax, which requires individuals to pay at least a base tax, loopholes or not. But the same isn't true for corporations.

We could eventually train and incentivize saving, but in the short term that will dampen the economy. Corporations could be given incentives to contribute more, though it is hard to see how. But government can spend right away. An alternative tax on corporate profits would make that possible. The ever-growing profit margins among companies aren't good enough for Americans—the nation needs the cash.

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