Paul Krugman

Life without bubbles

America.

Whatever the new administration does, we're in for months, perhaps even a year, of economic hell. After that, things should get better, as President Barack Obama's stimulus plan — O.K., I'm told that the politically correct term is now "economic recovery plan" — begins to gain traction. Late next year the economy should begin to stabilize, and I'm fairly optimistic about 2010.

But what comes after that?

Right now everyone is talking about, say, two years of economic stimulus — which makes sense as a planning horizon. Too much of the economic commentary I've been reading seems to assume, however, that that's really all we'll need — that once a burst of deficit spending turns the economy around we can quickly go back to business as usual.

In fact, however, things can't just go back to the way they were before the current crisis. And I hope the Obama people understand that.

The prosperity of a few years ago, such as it was — profits were terrific, wages not so much — depended on a huge bubble in housing, which replaced an earlier huge bubble in stocks. And since the housing bubble isn't coming back, the spending that sustained the economy in the pre-crisis years isn't coming back either.

To be more specific: the severe housing slump we're experiencing will end eventually, but the immense Bush-era housing boom won't be repeated. Consumers will eventually regain some of their confidence, but they won't spend the way they did in 2005-2007, when many people were using their houses as ATMs, and the savings rate dropped nearly to zero.

So what will support the economy if cautious consumers and humbled homebuilders aren't up to the job?

A few months ago a headline in the satirical New York City newspaper The Onion, on point as always, offered one possible answer: "Recession-Plagued Nation Demands New Bubble to Invest In." Something new could come along to fuel private demand, perhaps by generating a boom in business investment.

But this boom would have to be enormous, raising usiness investment to a historically unprecedented ercentage of GDP, to fill the hole left by the con-ner and housing pullback. While that could happen, it doesn't seem like something to count on.

A more plausible route to sustained recovery would be a drastic reduction in the U.S. trade deficit, which soared at the same time the housing bubble was inflating. By selling more to other countries and spending more of our own income on U.S.-produced goods, we could get to full employment without a boom in either consumption or investment spending.

But it will probably be a long time before the trade deficit comes down enough to make up for the bursting of the housing bubble. For one thing, export growth, after several good years, has stalled, partly because nervous international investors, rushing into assets they still consider safe, have driven the dollar up against other currencies — making U.S. production much less cost-competitive.

Furthermore, even if the dollar falls again, where will the capacity for a surge in exports and import-competing production come from? Despite rising trade in services, most world trade is still in goods, especially manufactured goods — and the U.S. manufacturing sector, after years of neglect in favor of real estate and the financial industry, has a lot of catching up to do.

Anyway, the rest of the world may not be ready to handle a drastically smaller U.S. trade deficit. As my colleague Tom Friedman recently pointed out, much of China's economy in particular is built around exporting to America, and will have a hard time switching to other occupations.

In short, getting to the point where our economy can thrive without fiscal support may be a difficult, drawn-out process. And as I said, I hope the Obama team understands that.

Right now, with the economy in free fall and everyone terrified of Great Depression 2.0, opponents of a strong federal response are having a hard time finding support. John Boehner, the House Republican leader, has been reduced to using his Web site to seek "credentialed American economists" willing to add their names to a list of "stimulus spending skeptics."

But once the economy has perked up a bit, there will be a lot of pressure on the new administration to pull back, to throw away the economy's crutches. And if the administration gives in to that pressure too soon, the result could be a repeat of the mistake FDR made in 1937 — the year he slashed spending, raised taxes and helped plunge the United States into a serious recession.

The point is that it may take a lot longer than many people think before the U.S. economy is ready to live without bubbles. And until then, the economy is going to need a lot of government help.

MEANWHILE ▪ Alex Beam

Beware the toys beneath that tree

Ah, Christmastime. Store tramplings, nervous breakdowns, prickly clumps of holly showing up where you least expect them. And the annual, mindless War on Toys. It makes a fella feel gosh-darned sentimental.

Every year, like clockwork, the family of Boston lawyer Edward Swartz stages a holiday-time press conference, decrying the "10 most dangerous toys" in the stores. Every year, like beaten, groveling, guileless dogs, the media give the Swartz's outfit, World Against Toys Causing Harm (WATCH), free publicity for its dubious claims. That must be because there is so little happening in the world.

This year is no exception. WATCH "fearlessly exposed potentially dangerous toys to the general public," the nonprofit's Web site proclaims.

What are the 10 toys to avoid this Christmas? Beware the Play-a-Sound Book with Cuddly Pooh! Shun the Spiderman Adjustable Toy Skates! For heaven's sakes, don't let your children play with Kenscott's 4-foot-wide inflatable Giga Ball! "Children as young as 4 years old are encouraged to 'crawl inside' this colorful inflatable ball, in order to 'spin, tumble, [and] bounce,'" the Swartzes write, adding: "WATCH out!"

The Giga Ball sounds like a lot of fun, I suggest to James Swartz, director of WATCH and son of the founder. "Of course they are fun. We don't dispute that," he says. "Our point there is that people should at least think about how it can be used in the real world."

To be fair, the Swartzes aren't the only killjoys roaming the aisles. For a number of years, US PIRG (Public Interest Research Group) has been staging its own Christmastime publicity-gathering enterprise, "Trouble in Toyland." It publishes a slightly shorter list of hazardous toys — e.g., Littlest Pet Shop, a lead key chain that would be a bad idea to swallow — and warns: "Simply because a toy does not appear on this list does not mean th...

There is so much work to be done that a few years ago the Swartzes decided to sink their hooks into summer as well. "Summer itself is a time of outdoor fun and activity but also of peril," is the WATCH-word. So they have laid on an additional press event bewailing the many hazards that await children during the dangerous months of unsupervised leisure: campfires, water guns, tipping soccer goals, trampolines, and ... bleachers. "Between 1980 and 2003, 19 people died from injuries sustained after falling from bleachers," their Web site states.

But aren't these people mostly drunk, adult, Red Sox fans? There's nothing in this data that refers to children. "Whether they are children or not, there are still summer safety issues," Swartz says. Something tells me he doesn't want to hear about my trips to New Hampshire to buy slingshots for my sons.

Toys 'R' dangerous, Swartz and family warn us every year.

A more welcome, albeit short-lived, Christmastime tradition was the full-page ad that the Greenwich, Connecticut-based rich guy Ray Dalio took out in major newspapers decrying Yuletide commercialism. "No sooner does Thanksgiving end, than the loathsome shopping season begins — a monthlong compulsion to buy something, anything, for anyone," read Dalio's ad in last year's Boston Globe, Wall Street Journal, Chicago Tribune and other papers.

In lieu of mobbing the malls, Dalio urged you to "give people donations to their favorite charity. And request that they give donations to your favorite charities. A lot more mone... to people who ...