

Money and You: To spend or not to spend, that is the question

by *Carrie_Schwab_Pomerantz*

It won't surprise anyone that we talk plenty about personal finance at my office — about the importance of saving and investing for the future, and about finding ways to make that process easier and more effective for people. But lately, the big topic of conversation has focused more on spending than investing. The discussion gets boiled down into something along these lines: "On the one hand, I think I should be saving my money. The economy is in the tank, and it looks like things could get worse. On the other hand, I think I should be spending my money. The economy is in the tank, and if we don't spend, aren't things bound to get worse? What am I supposed to do?"

Of course, this dilemma isn't new. In fact, this topic has taken me back to my college economics class and what economist John Maynard Keynes called "the paradox of thrift." The rational approach to economic uncertainty is to save, to build a surplus in case something truly dire happens, like the loss of a job or a serious reduction in income. But in a recessionary climate, what the economy needs is for people to spend. It's not for nothing that President Obama's recent initiative is referred to as the "economic stimulus plan." It has many aims, but one of them is to get money into the hands of consumers so that they can provide a catalyst to get the economy moving toward recovery. Consumer spending has fueled the economy for years (though now the secret source of that fuel is out: credit). And the government, banks and businesses all want consumer demand to pick up. They want us — they need us — to buy cars and homes, to go to the mall, to take vacations, to eat out.

Hence the paradox of thrift. To paraphrase Hamlet: "To spend or not to spend (i.e., save). That is the question."

There is no right or wrong answer here except for this one: You must act in your own self-interest. And I bet most of you know exactly what that means.

— If you're over-extended with credit, you should "save" by paying down your debt (you can make your monthly budget a lot more manageable by reducing or eliminating debt; start with high-interest, non-deductible debt first).

— If you're ill-prepared for retirement, you should invest in your long-term future (and now may turn out to be an excellent opportunity to buy stocks relatively cheaply).

— If you're worried about your livelihood, you should be putting every extra cent into an emergency fund and you should be looking for ways to cut down your day-to-day spending.

Even if you're flush with cash, the current environment might give you ample reason to defer a little spending and do a little more saving for your family's financial future.

At the same time, there's no reason to turn into a miser as long as you're in good financial shape. Let's be frank: Now is a great time to buy a car or remodel your house; companies are more than willing to offer discounts on all kinds of products and services, and many are willing to negotiate the price. If you need something and you can afford it, go for it. And if you can invest for tomorrow while spending today (to cite a few examples: re-insulating your house, installing energy efficient windows or replacing an old, inefficient water heater), you'll generate dividends of your own for years to come.

One of the things we've learned from this economic crisis is that our prosperity was closely linked to consumer spending. But that doesn't mean that linkage is essential to future prosperity. And I would much prefer seeing people prepare themselves for their own futures " by reducing debt, by saving and investing " rather than trying to give our economy a short-term lift by embarking on a shopping spree. So to my mind it comes down to this: Act in your own economic self-interest. Save and spend in ways that make sense for you and your situation. Let the government worry about the big picture; you keep your eyes on the small picture that illustrates your needs and your realities " and do what is right for you.

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