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Free Enterprise: Clunking along while oozing cash

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A specter is haunting the world - the specter of clunkers.

The powers that be in many industrialized nations, it seems, have entered into an alliance to rid the planet of old cars. The stated objective is to provide incentives to buy "new, more environmentally friendly vehicles" while trading in "old gas-guzzling cars or trucks."

Europe's three biggest economies - Germany, Great Britain and France - had all implemented "Cash for Clunkers" programs early during the economic downturn.

In fact, the reports coming from Europe about significant increases in automobile purchases gave the impetus to set up a similar project in the United States. In Germany alone, the sales of cars jumped by 27 percent compared to the same period the year before during the first seven months of the "Abwrackprämie" or "wrecking rebate."

When the same kind of program was jump-started in the U.S. three weeks ago, it was expected that the budgeted funds would be sufficient to replace 250,000 not fuel-efficient vehicles. Shortly thereafter, additional money had to be allocated when the money engine that drove the rebates threatened to run dry.

On Friday, the Department of Transportation (www.dot.gov [1]) announced that, so far, 338,659 "dealer transactions" totaling \$1.4 billion had been submitted to the CARS program (Car Allowance Rebate System, see also <http://www.cars.gov> [2]), far outracing the original estimates.

Thus, after getting the green light and promises of either \$3,500 or \$4,500 in rebates, American consumers - as had Europeans before - have decided to take the "free money" and run with it.

Although some questions still remain regarding the true environmental impact of this program (in Germany, many of the old cars that were supposed to be wrecked found their way to other countries), it is indisputable that it has been successful as a stimulus measure.

However, economists (being the "kill joys" they are) have released some numbers, which may recommend taking the foot off the gas pedal regarding such giveaways.

Ulrich Blum und Sabine Freye, researchers at the prominent "Halle Institute for Economic Research," suggested in their analysis (<http://tinyurl.com/pyu5gm> [3]) that the cost may have been underestimated.

A look under the hood reveals that, apart from the fact that most of the expenditures are debt financed and will incur interest payments (but that is true for most stimulus measures), it is also likely that more car-mechanics will lose their jobs because of fewer repairs being requested by customers.

Furthermore, the two economists found clear evidence that these temporary measures simply lead a significant number of consumers to change the schedule of already planned purchases or forego other planned purchases. In that sense, the rebates are as inefficient as temporary tax holidays, and they may explain the discouraging U.S. retail sales numbers outside of automobile purchases released this week.

All of this needs to be weighed against the benefits - including multiplier effects through additional orders for suppliers of car manufacturers and increased sales-tax receipts at the local and state level - when such rebate programs are under consideration.

In an economic emergency, the argument may be that capitalism has nothing to lose but its "old cars" and that it has a clean world to win. However, the environmental fig leaf on such stimulus measures should not be allowed to cover the truth. "Cash for Clunkers" is just another financial liability for the road ahead.

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