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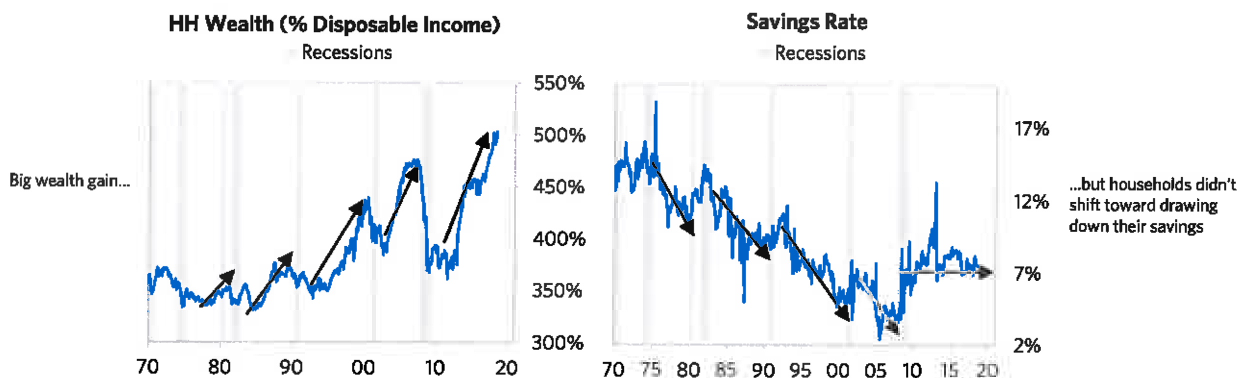
US Households Have Been More Restrained This Cycle, Making the Expansion Somewhat More Resilient

As we have described before, we expect asset prices and the US economy to come under some pressure over the next 18 months, as the Fed is planning to continue tightening at the same time that the fiscal boost is peaking and external conditions are set to slow. Whether this slowing ends up being material enough to become self-reinforcing and to require a turn toward easing is an important question, since the Fed's ability to ease effectively is limited. While we believe the risks are higher than at any point in the expansion, one consideration that points to resilience is that households haven't extrapolated past strength by borrowing or dissaving aggressively to finance spending. Below, we will describe our view on US household finances and give some color on what's been happening for households at different ends of the income spectrum.

The first set of charts below illustrates how little households have dissaved this cycle relative to prior ones, even as the economy has recovered and asset prices have boomed. This has held true even in the latter part of the expansion—households have dissaved an average amount, but this change has taken almost four times the wealth gains. In part, this may have been because households were coming out of a drawdown. That said, the fact that asset prices have risen to above highs in recent years and the savings rate has stayed stable near historical levels makes us think this wasn't the only factor.



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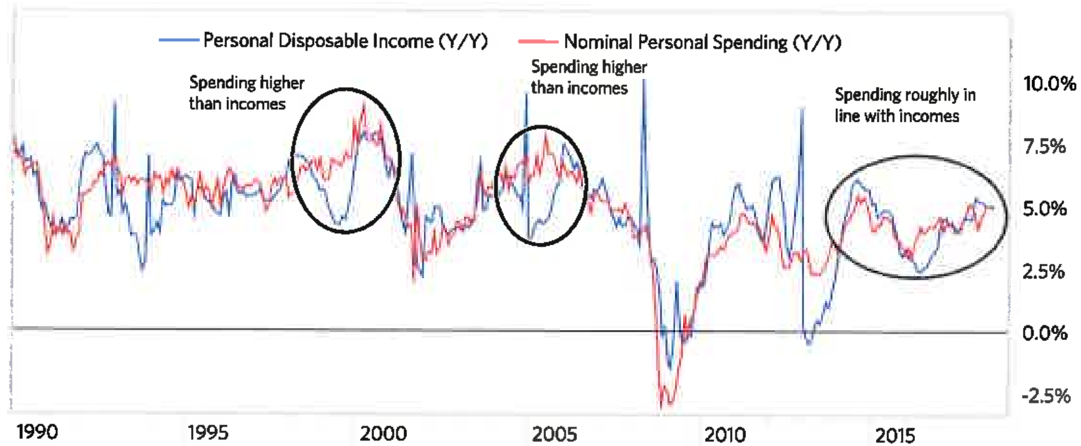
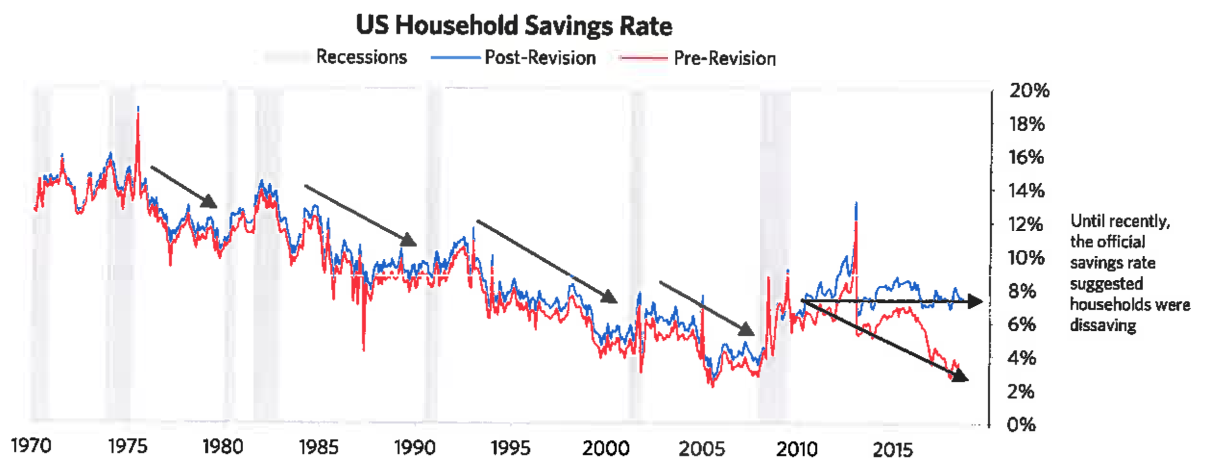
Give Feedback

Another way of seeing this is that households have only boosted spending in line with income growth, with little reliance on borrowing or dissaving.



Last Month's Revision in the Household Savings Rate Made Clear How Restrained Households Have Been, but Other Sources Have Shown a Similar Picture for Some Time

One thing to note is that until recently, the official savings rate data told a very different story, suggesting that households were drawing down their savings pretty quickly. However, as we will describe below, the fact that stats like this can be misleading and prone to revision is why we don't put too much weight on any one measure. The chart below shows the household savings rate published on Thursday, as well as the one published prior to the July revision.



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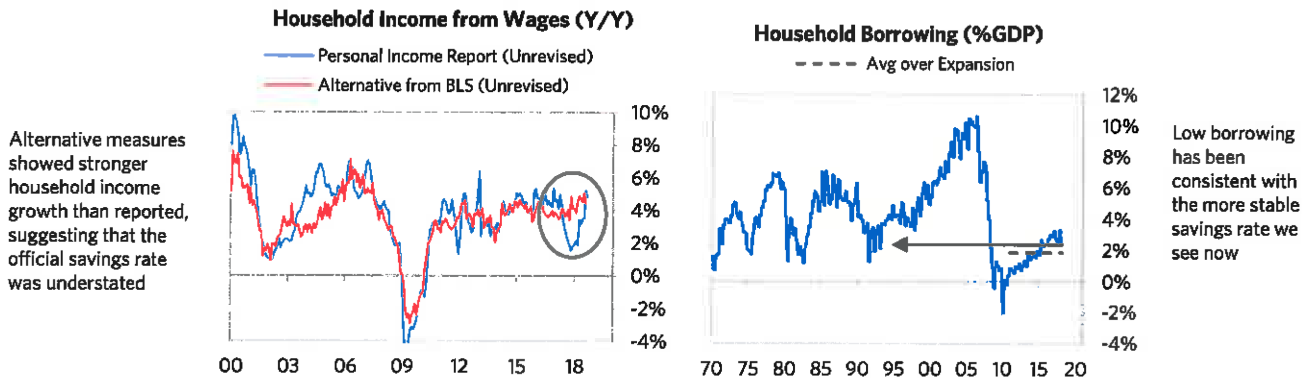
While the official data prior to the revision showed households drawing down their savings, other measures would have rightly suggested that the savings rate was more stable. For one, much of this distortion was caused by noise in the official income data, which was the result of employers deferring bonus payments following the Trump election in order to take advantage of a potential tax cut, and of this shift not being seasonally adjusted properly yet. Other measures of income growth outside of the national accounts, like the Bureau of Labor Statistics' employment report, continued to show solid income gains. In addition, one of the primary ways that households dissave is through borrowing, and as the chart on the right shows, household borrowing has been muted.



Below, we take a closer look at what caused the upward revision in the savings rate. It was driven by a revision to household income growth, specifically employee compensation (Trump tax plan related bonus deferments) as well as proprietors' income and asset income, both of which are harder to estimate. The revised data suggests that household finances are in a much healthier position than the prior version had indicated, particularly wealthier households, which are more exposed to assets/small business income, which was revised higher.

Breakdown of US Savings Rate (%GDP)

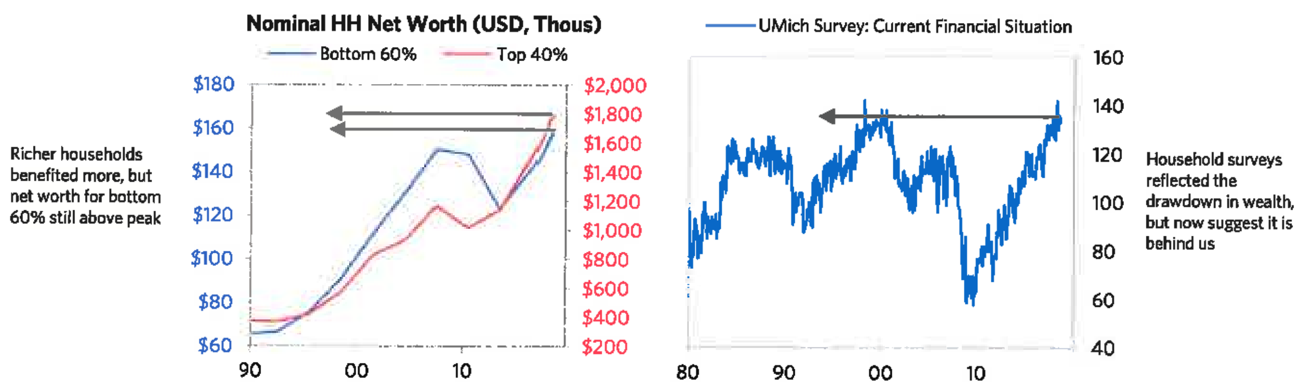
	Pre-Revision	Post-Revision	Diff	Contribution to Diff in Savings Rate
Private Income	60%	62%	1.3%	1.8%
Compensation of Employees	53%	54%	0.6%	0.8%
Proprietors' Income	7%	8%	0.7%	1.0%
Income from Govt	14%	14%	0.1%	0.2%
Income from Assets	8%	9%	1.0%	1.5%
Income from Transfers	0%	0%	0.0%	0.0%
Total Income	83%	86%	2.4%	3.4%
Less: Taxes	17%	17%	-0.2%	0.3%
Disposable Income	66%	69%	2.6%	3.7%
Less: HH Spending	64%	64%	-0.2%	0.2%
Savings	2%	5%	2.8%	3.9%
Savings Rate	3.6%	7.6%	3.9%	--

Change in income split among compensation of employees, proprietors' income, and income from assets

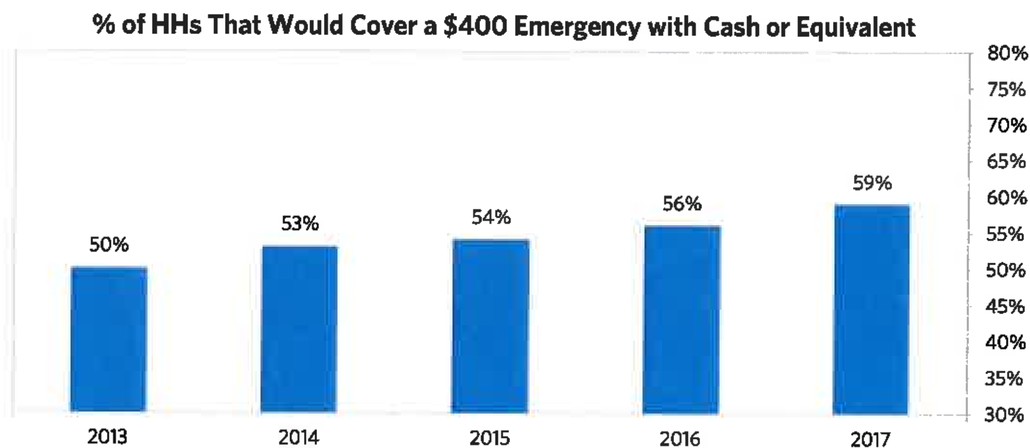
Change was to income, not to spending

Wealth Gains Have Disproportionately Gone to the Rich, but Finances Have Improved Materially Even for the Average Household

Of course, aggregate US household finances mask meaningful differences between households at the higher end and lower end of the income distribution. Wealth gains this cycle disproportionately benefited higher income households, both because they hold more of their wealth in equities and because they face less pressure to cash out during a recession (in contrast to poorer households, which sold assets to meet expenses). However, even for the average household, financial conditions have improved materially as debt levels fell and wealth rose. Nominal wealth has been above its pre-crisis peak for about a couple of years, even for the bottom 60%, and consistent with this, households report having secularly strong finances.



Although financial conditions and net worth have improved across households, one pressure that cuts the other way is that many households at the low end of the income distribution are still in a pretty precarious financial situation. That said, to some extent this has likely always been the case (i.e., savings are negligible for poorer households), and there has been some modest progress over the course of this cycle.



Fed Survey: Report on the Economic Well-Being of US Households in 2017

Another pressure that has cut the other way is income gains. While there has been modest wage growth over all this cycle, wages for less wealthy households still lag their typical growth, particularly for people in the middle of the income distribution.

Pre-Tax Income Growth by Quintile

	0-20%	20-40%	40-60%	60-80%	80-100%
2010-2016	2.4%	1.3%	1.8%	2.5%	4.0%
Average Since 1990	2.7%	2.8%	2.8%	3.1%	3.7%
Diff	-0.4%	-1.5%	-1.1%	-0.6%	0.2%

Households in aggregate have been much more cautious in increasing their spending this cycle, not extrapolating the significant gains in employment, incomes, and assets they've enjoyed so far. In line with this, they've largely relied on income gains to fund spending increases versus borrowing or dissaving to boost spending further. This is one consideration that on the margin makes it more likely that the expansion will be more resilient.

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