Why Are We Saving More and Spending Less?

Have our memories of the Great Recession altered our habits?

Provided by Hatcher Financial, P.C.

Consumer spending accounts for more than two-thirds of economic activity in the United States. Lately, that spending has moderated. Across the 12 months ending in March, personal spending advanced 3.4%. That matched the gain seen in 2015.[1,2]

Is a 3.4% annualized gain in personal spending adequate? Not in historical terms. During 2014, consumer spending accelerated 4.2%. The average monthly gain in consumer spending across the past 12 months (0.28%) is roughly half the historical average seen since 1959 (0.54%).[1,2]

While the personal spending rate has slumped recently, the personal savings rate has not. In March, it was at 5.4%. It has varied between 4-6% for more than three years, staying notably above the levels seen prior to the Great Recession of 2007-2009.[3]

Has consumer psychology been altered since then? That is an interesting question to consider, and it especially begs consideration, given the fact that inflation-adjusted personal spending has declined for three straight quarters.[4]

Real disposable income (that is, disposable income adjusted for inflation) has been rising without fail. It has increased for 13 straight quarters, beginning in Q1 2013 after the payroll tax cut at the end of 2012. You would think unflagging increases in real disposable income would promote greater economic expansion, but real gross domestic product grew just 1.5% in 2013 and only 2.4% in both 2014 and 2015. Those GDP levels are well below those seen in the early 2000s, not to mention the 1990s.[4,5]

When is too much frugality a bad thing? When it risks hampering economic growth. The 5.4% personal savings rate recorded in March tied a three-and-a-half-year high. As we are well into an economic recovery, it would seem only natural for Americans to spend more than they did several years ago.[4]

Perhaps people are just not ready to do that. As a Deutsche Bank research note asserted this month, the memory of the Great Recession may be too hard to erase: "The shock of the crisis likely increased the desire to hold more savings for precautionary motives."[4]

Since 2001, Gallup has consistently asked Americans a question each year: "Are you the type of person who more enjoys spending money or who more enjoys saving money?"[6]

This year, 65% of respondents said they preferred saving and 33% of respondents said they preferred spending. That gap has never been so pronounced in fifteen years of polling.[6]

As recently as 2009, just 53% of Americans told Gallup they preferred saving while 44% indicated they preferred spending. The gap has gradually widened ever since, and it is now fairly consistent across all age groups.[6]

A little more polling history seems to affirm a perception shift. In 2006, Gallup found that 51% of Americans rated their personal financial situation as "excellent/good;" in that year, 50% of Americans preferred saving to spending. Four years later, only 41% of Americans felt their personal financial situation was "excellent/good", and 62% indicated a preference for saving. This year, 50% of Americans ranked their personal finances as "excellent/good," yet 65% preferred saving dollars to spending them. "The appeal of saving over spending shows some signs of being the new normal rather than a temporary reaction to the hard times after 2008," Gallup's Jim Norman observed last month.[6]

In its latest report on personal income and outlays, the Bureau of Economic Analysis says personal incomes were up 4.2% year-over-year as of March. Consumer prices rose but 0.9% in the same span. Unimpressive wage growth aside, it would appear that many households are nicely positioned to spend. Of course, what these two numbers do not take into account is debt: mortgage debt, student loan debt, credit card debt. The rebound in the personal savings rate surely relates to the goal of reducing such liabilities.[7,8]

The Great Recession taught America a great lesson about living within one's means. Could that lesson, as vital as it is, now be constraining the economy? As economists try to pinpoint reasons for America's slow recovery, they may want to cite the psychology of the consumer.

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Citations.

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