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ECONOMIC PERSPECTIVES

DOMESTIC CONSUMERS: BIGGER SAVERS THAN PREVIOUSLY THOUGHT

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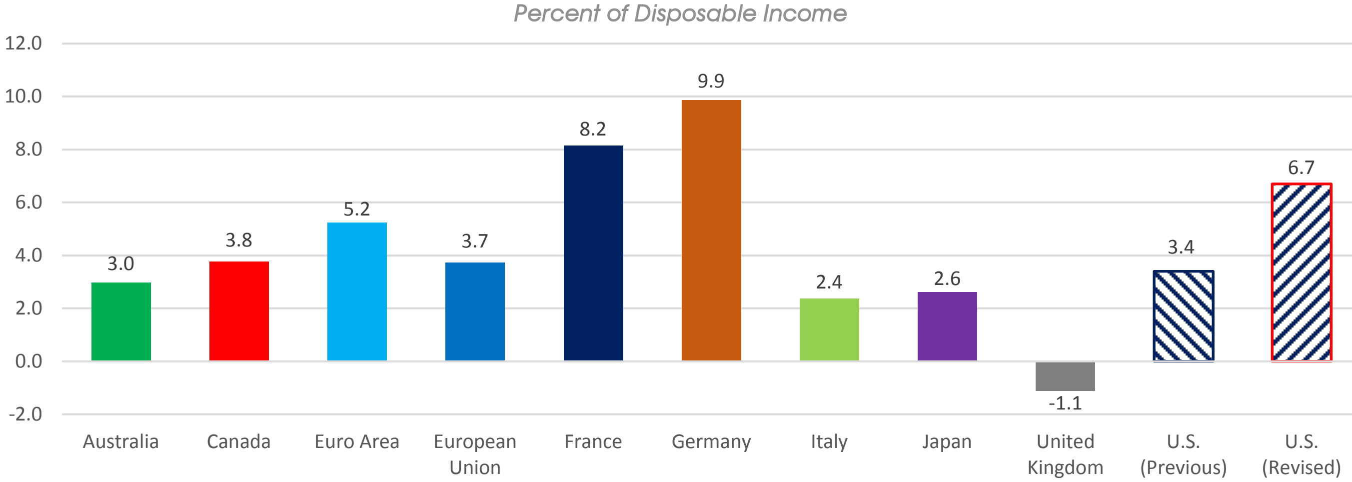
HIGHLIGHTS:

- » *U.S. Personal Savings Rate Much Higher than Previously Thought*
- » *Domestic Consumers Saving Considerably More Since the Great Recession*
- » *Adjustments to a Variety of Components Boosted Personal Income Estimates*
- » *Lower Personal Tax Payments and Consumer Outlays Also Added to Personal Saving*
- » *Revised Personal Saving Rate Now Closer to Flow-of-Funds Measures*
- » *Increases in Household Net Worth Are Yet Another Positive Saving Development*
- » *Tight Labor Markets and Healthier Savings Behavior Will Continue to Buoy Spending*

U.S. PERSONAL SAVINGS RATE MUCH HIGHER THAN PREVIOUSLY THOUGHT

American consumers have long been chided for their allegedly extravagant ways. With few exceptions, the percentage of funds saved out of personal disposable income by domestic residents has lagged behind those of other industrialized nations and even-larger groupings such as the Euro area or the European Union (see Exhibit 1). Trending lower over the past three years, the 2.7% personal saving rate originally reported for last fall was the lowest reading since the economy entered the Great Recession in the third quarter of 2008. That picture changed dramatically last month, however, when the Bureau of Economic Analysis (BEA) released a comprehensive update of the National Income and Product Accounts (NIPA).

Exhibit 1: Annual Household Saving Rates
Percent of Disposable Income

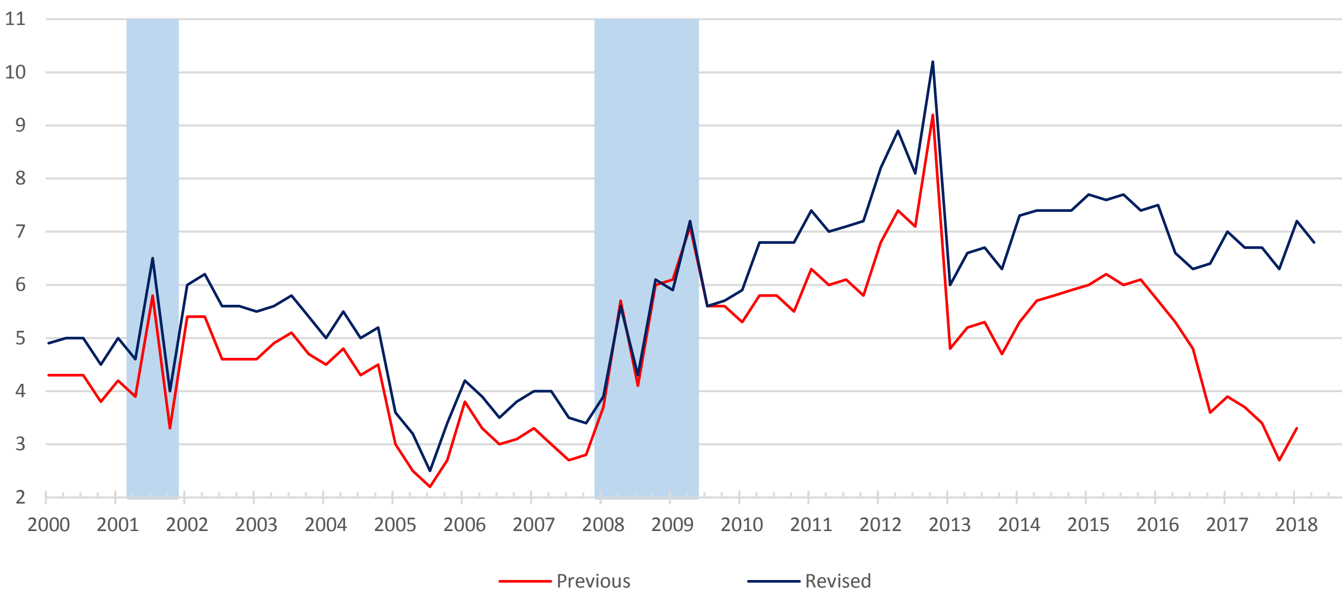


Notes: Using the Organization for Economic Cooperation and Development concept, net household saving is defined as the subtraction of household consumption expenditure from household disposable income, plus the change in net equity of households in pension funds. Observations are for 2017 except for France and the U.K. which are for 2016. Sources: Organization for Economic Cooperation and Development and U.S. Bureau of Economic Analysis.

DOMESTIC CONSUMERS SAVING CONSIDERABLY MORE SINCE THE GREAT RECESSION

Along with the advance report on second-quarter GDP, the BEA released a comprehensive update to NIPA data going all the way back to 1929. While the severity of the Great Recession and pace of the subsequent recovery in real business activity since the spring of 2009 were left virtually unchanged, the same could not be said for the personal saving rate. Indeed, now averaging 7.1% over the course of the current expansion, the proportion of disposable personal income left unspent by consumers is now a hefty 1.6 percentage points higher than previously thought (see Exhibit 2). Perhaps even more important, in contrast to the near halving of the personal saving rate since the end of 2016, the closely followed metric has actually remained fairly steady near 6.75% and well above the 4.6% average posted over the prior cyclical upturn.

Exhibit 2: U.S. Personal Saving Rate
Percent of Disposable Income

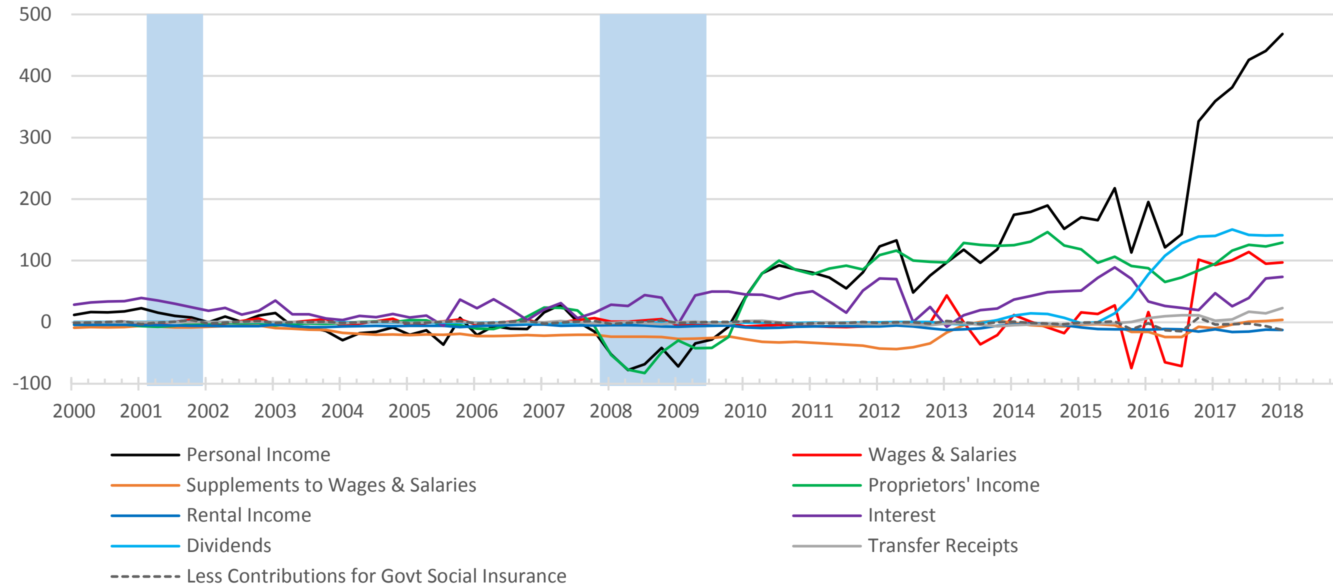


Note: Shaded areas denote recessions. Source: U.S. Bureau of Economic Analysis.

ADJUSTMENTS TO A VARIETY OF COMPONENTS BOOSTED PERSONAL INCOME ESTIMATES

The upward adjustments to the personal saving rate over the course of the current economic expansion were primarily attributable to significantly higher estimates of personal income. Indeed, at a revised $17.3 trillion, personal income in the first quarter of this year was a hefty $468.2 billion, or 2.8%, higher than previously thought. Several components contributed to the reported boost in personal income over the past five years (see Exhibit 3, following page). Correcting for underreportings using newly available Internal Revenue Service (IRS) tax-gap data, nonfarm proprietors' income, i.e. earnings from unincorporated businesses, was adjusted $108.6 billion higher on average over the 2013-2017 period. Moreover, based on the IRS Statistics of Income series, personal dividend income was boosted by $113.2 billion in 2016 and by $143.3 billion in 2017, while a methodological change incorporating measures of the implicit financial services of credit unions and savings institutions augmented interest payments received by consumers by $25.6 billion and $45.9 billion, respectively, in those years. Incorporating expedited information from state employment offices across the country, the BEA boosted their earlier estimate for wages and salaries last year by $100.6 billion. The state data from the Bureau of Labor Statistics' *Quarterly Census of Employment and Wages* form the basis for all but a fraction of the BEA's wage and salary estimates.

Exhibit 3: Sources of Revisions to Personal Income
Billions of Dollars

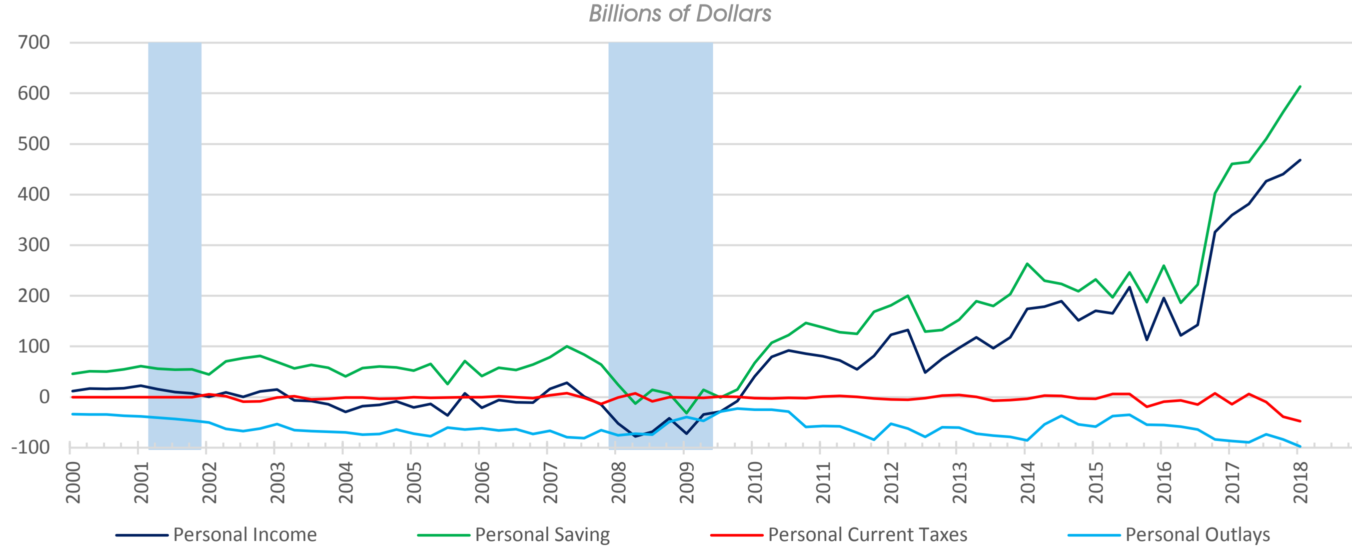


Note: Shaded areas denote recessions. Source: U.S. Bureau of Economic Analysis.

LOWER PERSONAL TAX PAYMENTS AND CONSUMER OUTLAYS ALSO ADDED TO PERSONAL SAVING

Higher estimates for a variety of personal income items were not the only factors boosting the personal saving rate: both personal tax payments and consumer outlays were marked lower (see Exhibit 4). Personal current taxes were pared by \$5.9 billion in 2016 and by \$14.0 billion last year, while the whopping \$47.7 billion downward adjustment to levies paid by consumers in the first quarter pared the effective tax rate by almost 80 basis points to 13.2%. At the same time, the BEA's earlier projections overestimated consumer outlays throughout the current expansion. Revised lower figures for consumer outlays accounted for approximately one fifth of the upward adjustment to personal saving over the 2016-2017 span.

Exhibit 4: Sources of Revisions to Personal Savings Series
Billions of Dollars



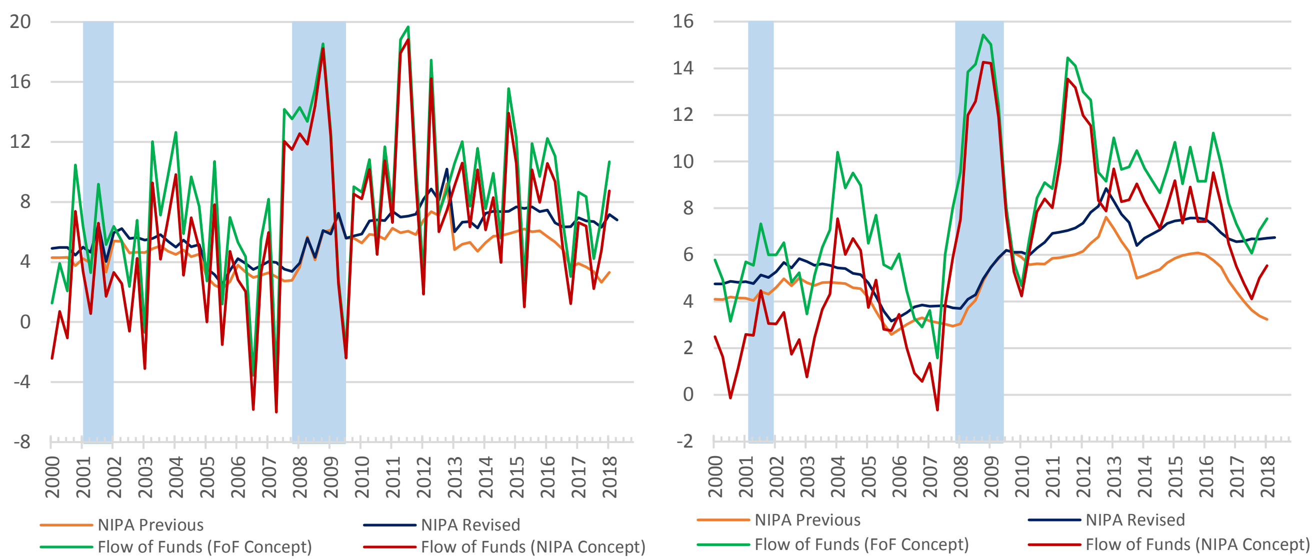
Note: Shaded areas denote recessions. Source: U.S. Bureau of Economic Analysis.

REVISED PERSONAL SAVING RATE NOW CLOSER TO FLOW-OF-FUNDS MEASURES

The revisions to the personal saving rate as a result of the comprehensive update of the NIPA accounts also pushed the BEA series closer to alternative measures provided in the Federal Reserve Board in the quarterly Flow of Funds (FoF) report (see Exhibit 5). The Federal Reserve measures personal saving in two ways. The first is calculated as the net acquisition of financial and real assets less the increase in household liabilities. The second further subtracts net investment in consumer durable goods, making it conceptually closer to the NIPA gauge. While the two measures are compiled using different underlying data and definitional differences exist, they should in theory move in tandem with the NIPA series over time. During the first quarter of this year – data for Q2 will be released by the Fed in the third week of September – the FoF personal saving rate stood at a lofty 10.7%, while the measure excluding net investments in durable goods clocked in at 8.7%. Both were at their respective highest levels since the spring of 2016. At 7.2% of disposable personal income, the NIPA updated figure remained below the two FoF estimates for the winter quarter, but the gap was considerably smaller than previously thought. Smoothing the data using four-quarter moving averages – the FoF series being particularly volatile – reveals that the NIPA and FoF (NIPA concept) series have been fairly close over the past four years.

Exhibit 5: Comparison of NIPA and FoF Saving Rate Measures

Percent of Disposable Income (Left) & Four-Quarter Moving Averages (Right)



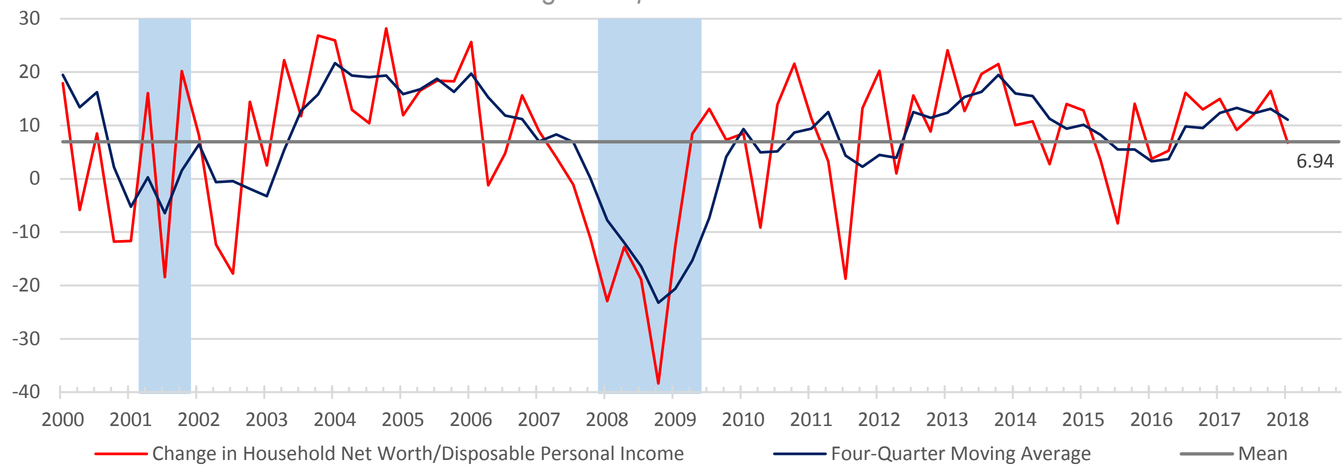
Note: Shaded areas denote recessions. Sources: U.S. Bureau of Economic Analysis and the Board of Governors of the Federal Reserve System.

INCREASES IN HOUSEHOLD NET WORTH ARE YET ANOTHER POSITIVE SAVING DEVELOPMENT

Data contained in the Federal Reserve Board’s quarterly FoF report can be used to construct yet another personal saving measure worthy of discussion. As an alternative to the aforementioned NIPA and FoF savings gauges, we could look at changes in household net worth as a percentage of disposable personal income. Here, net worth is estimated by taking the difference between the value of household assets and liabilities, with the one caveat that bond holdings are valued at cost and not at market prices. While extremely volatile on a quarterly basis for a variety of reasons – the numerator includes capital gains, is not seasonally adjusted and likely suffers from some measurement problems – the average ratio of changes in net household worth to disposable personal income over the course of the current expansion at 9.9% is little different from the 10.2% recorded over the course of the 2002-2007 cyclical upturn (see Exhibit 6, following page). The 6.7% posted in the first quarter was a touch below the 6.9% average since 2000, but gains in equity and homes prices since the winter suggest that a rebound is probably in the offing when second-quarter data is released.

Exhibit 6: Alternative Measure of Financial Well Being

Percentage of Disposable Personal Income



Note: Shaded areas denote recessions. Source: Board of Governors of the Federal Reserve System.

TIGHT LABOR MARKETS AND HEALTHIER SAVINGS BEHAVIOR WILL CONTINUE TO BUOY SPENDING

Real consumer spending advanced at an annualized clip of 4.0% in the second quarter – the strongest showing since the fall of 2014. While some slowing from that pace likely is in the cards during the summer quarter, a variety of factors should support solid gains in consumer purchases over the balance of the year. Buoyed by rosy appraisals of current economic conditions, consumer confidence remains near lofty levels last recorded in 2000. Robust hiring over the foreseeable future, eclipsing new entrants into the civilian labor force, will continue to put downward pressure on the civilian unemployment rate. Continuing tightness in labor market conditions hint that employee compensation may soon pick up in a more meaningful way. Added to the above, the healthier picture of personal saving activity points to a powerful support to the economic expansion going forward.

QUESTIONS / COMMENTS?

The *Economic Perspectives* newsletter is authored by the FHLBNY's Financial Economist, Brian Jones. Contact your Relationship Manager at **(212) 441-6700** to discuss the information shared in this newsletter and any potential business opportunities with the FHLBNY as your partner.