With Stocks Surging, Americans Are Saving at 12-Year Low

U.S. household net worth has risen from $56 trillion in 2008 to $97 trillion in the third quarter of 2017. It is natural for people to spend a bit of their rising lifetime savings when asset values are increasing. Economists call that a "wealth effect."

But when taken too far it can be a red flag that markets are getting overheated and households overextended. Previous busts—in the mid-2000s and the late-1990s—were preceded by periods of rising asset values and especially low saving.

The U.S. household saving rate dropped in December to its lowest level since the height of the 2000s housing boom, when many Americans were drawing on rising equity in their homes to spend on vacations, new cars, appliances and more.

This time they aren't feasting on debt as aggressively as they did back then, which should leave them less vulnerable should another downturn hit the economy. However, they have shifted decidedly away from a postcrisis rush to save for the future, which could leave them exposed if stocks or other assets take a sudden turn for the worse.

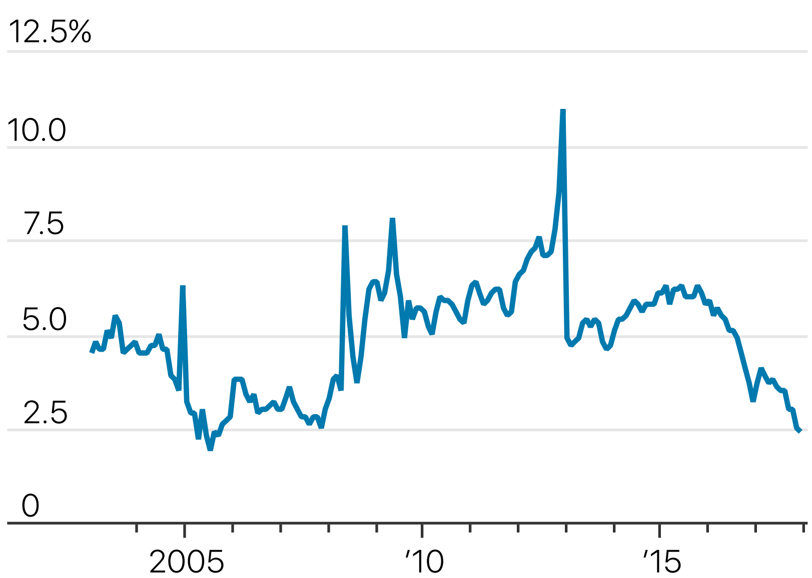
The saving rate was 2.4% of disposable household income in December, the Commerce

Department said Monday. That was the lowest rate since September 2005, not long after then-Federal Reserve Chairman Alan Greenspan began warning about froth in housing markets.

Rainy Day Retrenchment

Americans' rate of saving dropped to a 12-year low in December as consumers spent more, reflecting their modestly higher incomes and confidence in the economy. Personal saving as a percentage of disposable income:

Source: Federal Reserve Bank of St. Louis



The saving rate had risen to 6.6% when the recession ended in June 2009.

Clara Soh, a health-care consultant, said her investment property in Portland, Ore., has more than doubled in value since she bought it in 2009, and she is thinking about selling to reap the capital gain. Feeling confident, she recently took a ski vacation to Japan and bought a new van.

"I felt like I could afford to," Ms. Soh said.

Confident about their employment prospects and seeing their portfolio and property increase in value, consumers currently feel their "assets are doing the saving for them," said financial adviser Lawrence Glazer, managing partner at Mayflower Advisors LLC in Boston.

Investors are tapping into retirement accounts for expenses "out of overconfidence rather than desperation," he said, noting that "everybody and their brother is renovating their kitchen and bath right now."

Aaron Parrish, a senior financial adviser at Triad Financial Advisors Inc. in Greensboro, N.C., said one of his clients, a divorcee and retired therapist, gave $56,000 in total to her two daughters and their spouses last year. "She would not have felt comfortable doing that if we did not have such a good year in the market," he said.

Some economists say it is too soon to ring alarm bells. The saving rate may have been depressed in December by households deferring income to 2018 in anticipation of lower tax rates, and by spending in anticipation of a tax windfall this year.

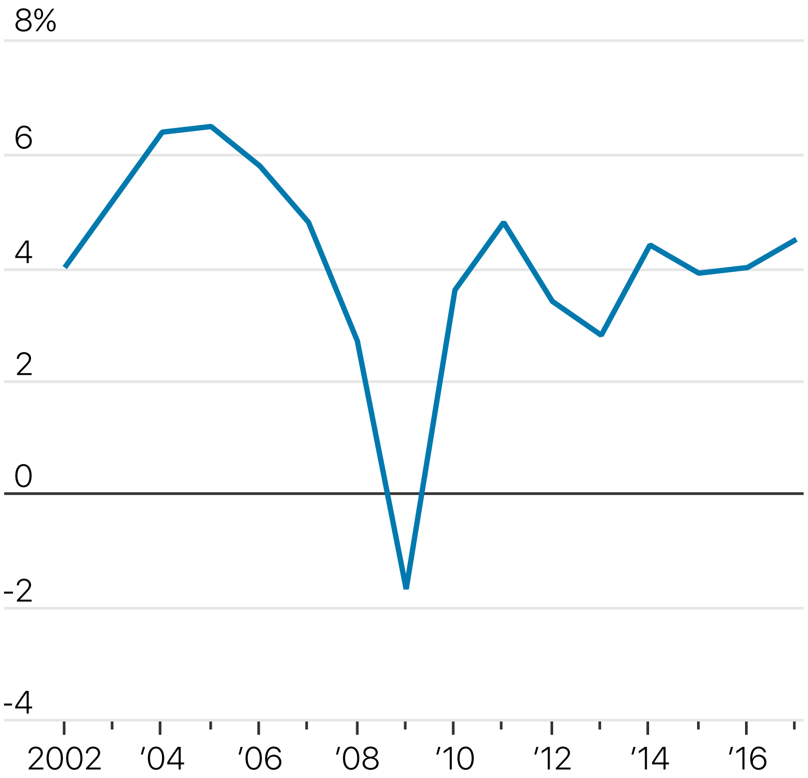
Shifts in the saving rate due to tax changes have precedent. The rate tanked in January 2013, to 4.9% from 11% the month before, when a payroll tax break expired and ate into take-home earnings.

"If the saving rate is still down in the 2%'s by mid-2018, then you can begin to worry, but any anxiety over this now will almost certainly prove to be misplaced," said Stephen Stanley, chief economist of Amherst Pierpont Securities.

...But spending has continued to rise

Personal consumption expenditures, annual percent change

Source: Federal Reserve Bank of St. Louis



The spending spree, meanwhile, is adding fuel to the economy. Consumer spending expanded at a 3.8% annual rate in the fourth quarter, with big gains in cars. That helped overall economic output expand at a 2.6% rate, above the 2% trend that has prevailed since the early 2000s.

"More and more, people want to live now," said Sheila Padden, owner of Padden Financial Planning LLC in Chicago. "Nobody's going crazy; they might be taking a trip or considering a vacation home. It's not extreme spending."

Economists said income gains would be key to keeping household spending on a steady course and household finances from getting overextended. That means the economy will depend on steady hiring and could benefit if wages start rising.

Moreover, the $1.5 trillion tax cut passed by Congress and signed by President Donald Trump in December could help in the near term.

Some of that tax cut will go directly to households in the form of lower individual income-tax rates. Some of it will be passed on by companies enjoying lower corporate rates.

A list compiled by Americans for Tax Reform, a conservative advocacy group that favors lower taxes, said Monday that at least three million Americans are receiving bonuses in the wake of the tax changes, and 275 companies have announced wage and salary increases, bonuses, or 401(k) match increases directly related to the cuts.

The path of debt is another wild card. Household debt levels aren't much higher now than they were in the mid-2000s boom, even though wealth and incomes have risen. Household debt levels fell from $14.2 trillion in 2007 to $13.4 trillion in 2011 and then rose back to $15.1 trillion by the third quarter. Moreover, low interest rates have held down the cost of servicing that debt.

Still, some economists said the recent rise is another sign that households could be on a path toward overextending themselves.

"Debt is climbing and we're not paying adequate attention to what could happen when those kinds of things go south," said Jonathan Morduch, an economics professor at New York University.

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