September 15, 2023

Economic INSIGHT

Rising Household Wealth Supports Spending as Savings Run Dry

Resilient. The U.S. consumer has been surprisingly resilient, continuing to spend on everything from travel and dining out to new cars and medical services, ramping up purchases, despite rising prices and higher borrowing costs. While clearly losing momentum from peak levels, expenditures surpassed expectations again last month. And, as a consumer-based economy, the ongoing positive pace of expenditures continues to fuel expectations of a soft landing, whereby the Fed can tighten policy enough to tame inflation without killing the consumer and by extension, the broader economy.

But can the consumer maintain this pattern of positive spending? Can the consumer continue to carry the economy? It depends. While household wealth is rising for some, others are increasingly reliant on debt or other temporary and dwindling sources of funds to supplement spending particularly as energy costs rise. In other words, it is a tale of two very different consumers. There is still quite a bit of spending power in the U.S. economy, but persistent inflation and higher rates are increasingly eroding buying power, particularly for those at the bottom.

RETAIL SPENDING BOOSTED BY HIGHER GAS PRICES

Retail sales were surprisingly robust in August, rising 0.6%, the largest increase in three months. Although with revisions to earlier months, the annual pace, while still firmly in the black, continued to slow from 2.6% to 2.5%. The majority of the rise, furthermore, was centered on elevated pump prices, with gasoline station sales rising over 5% for the month, the most since March 2022, while categories like sporting goods and furniture declined over 1%. Excluding gasoline alone, sales rose a more meager 0.2%, the slowest pace since March.

With core sales advancing at a five-month low, the monthly uptick in activity appears to be less a reflection of mounting consumer strength and more an indication that higher gasoline prices are already seeping through, forcing some consumers to divert funds from other areas of expenditures or more rapidly eat through (pandemic) savings to fill up the family car with higher cost fuel.

SAVINGS, A TEMPORARY WINDFALL

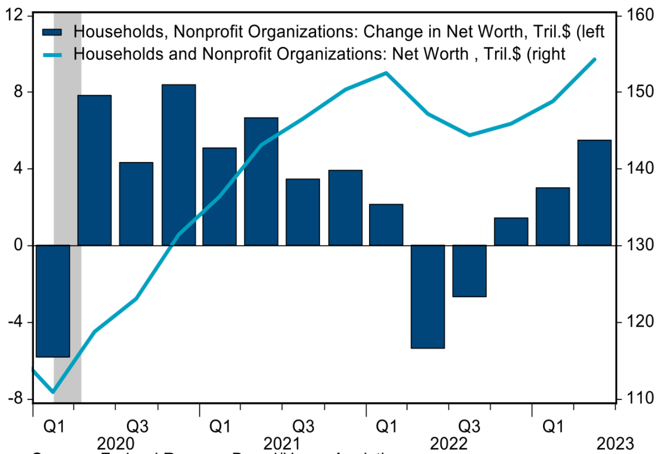
Due to massive fiscal outlays during the pandemic to the tune of $6T, households rapidly accumulated unprecedented levels of stored wealth. In fact, excess savings, or

Lindsey M. Piegza, Ph.D.
Chief Economist
piegzal@stifel.com

Lauren G. Henderson
Economist
hendersonla@stifel.com

STIFEL

the amount of additional savings on top of the presumed pre-pandemic trend, totaled over $2T. But over the course of three years, consumers were all too willing to spend those additional funds, reducing excess savings to “just” $500B as of March. Additionally, according to the Federal Reserve Bank of San Francisco, excess savings are expected to be entirely depleted by the end of the current quarter.



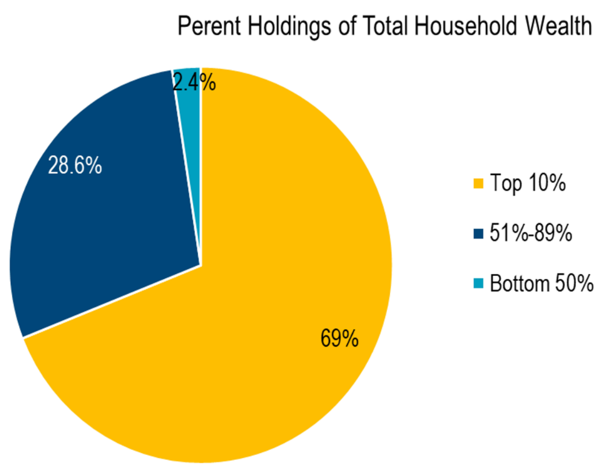
Source: Federal Reserve Board/Haver Analytic

But does that mean the consumer is done for? Is the consumer poised to fall off a cliff? Not necessarily. At least not yet. After all, household wealth is once again on the rise. Just like – excess – savings, household wealth also surged during the pandemic thanks to the administration’s extremely generous fiscal policies, but began to decline as stimulus largely dried up. Reaching a peak of $152T in Q1 2022, household net worth dipped to a low of $144T two quarters later.

More recently, however, wealth is once again on the upswing, thanks to a still solid labor market and sizable asset appreciation. While cooling somewhat, companies continue to add roughly 236k new payrolls each month, and real income growth started out the year at the fastest pace since early 2021. Additionally, historically low interest rates for more than two years, coupled with a multi-year deficit of supply boosted real estate values ($2.4T), while a stronger-than-expected “recovery” led to solid corporate earnings fueling the equity market ($2.6T). As a result, household wealth rose $3T in the first quarter and $5.5T in Q2, reaching a record high of $154T, suggesting still a significant amount of consumer buying power despite the loss of earlier pandemic-related savings … at least for some.

A GROWING DIVIDE OF GROWTH

While the latest data suggests household wealth accumulation has accelerated beyond its pre-pandemic rate, not all households have equally benefited from this growth in net worth. Lower income households, for example, are less likely to own property or have a stake in the equity market, precluding them from benefiting from this massive run up in valuations, and growing the divide between asset holders and non-asset holders. According to Federal Reserve Bank of St. Louis, the top 10% hold



Source: Federal Reserve Bank of St. Louis

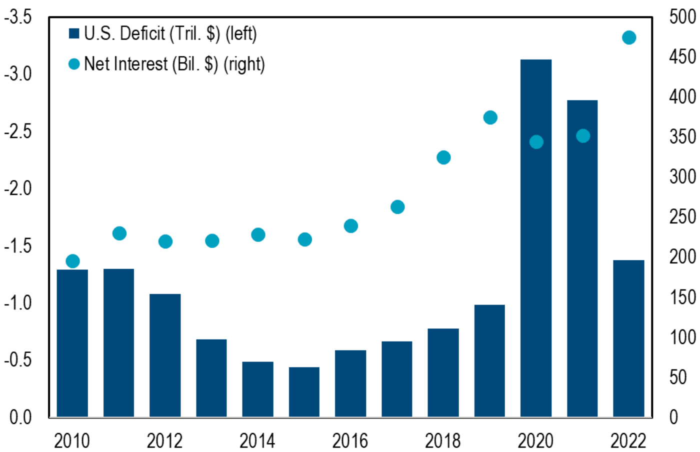
STIFEL

near 70% of the wealth, while the bottom 50% holds less than 3% .

As a result, many Americans – or at least those not feeling wealthier over the past few years – are increasingly turning to temporary supports to maintain a more robust level of spending. Credit card debt, for example, has jumped over 16% in the last year with total household debt reaching $17.1T, a new record high. 401k hardship withdrawals have also picked up, rising 36% in the second quarter alone. Additionally, with the dust from trillions in pandemic stimulus not yet settled, trillions more in new fiscal support is making its way into the system. While government assistance is not the ideal way to create a sustainable, growing economy, it will aid in continuing to artificially prop up investment and the consumer.

END GAME

As the Fed continues on a pathway to price stability, borrowing costs are likely to rise further, compounding pressure on the average consumer and the domestic economy. Should the U.S. economy avoid a significant downturn or asset repricing, rising household wealth may be sufficient to mask pockets of weakness or soften an outright decline in broad-based consumption. Under recessionary conditions, however, such a favorable outcome becomes less likely assuming a sizable market correction would wipe out at least a portion of the asset-based wealth accumulation.



Source: Congressional Budget Office

In either scenario for those less able to withstand elevated costs, consumption is likely to slow – significantly – further, particularly as energy costs push higher with gas prices already reaching a 10-month high and student debt payments set to resume in less than three weeks. While further fiscal support or "putting it on plastic" will act as a partial offset, unfortunately for some, even under the best conditions pain cannot be entirely avoided.

Lindsey Piegza

Ph.D., Chief Economist

piegzal@stifel.com

[1] *Figure represents 2023 average thus far.*

[2] *Link to report: https://www.federalreserve.gov/releases/z1/20230908/html/recent_developments.htm*

[3] *Link to report: https://www.stlouisfed.org/institute-for-economic-equity/the-state-of-us-wealth-inequality#:~:text=The%20 top%2010%25%20of%20households,2.4%25%20of%20total%20household%20wealth*

[4] *Student loan payments resume in October.*

DISCLAIMER