Savings: the two-sided wildcard for growth

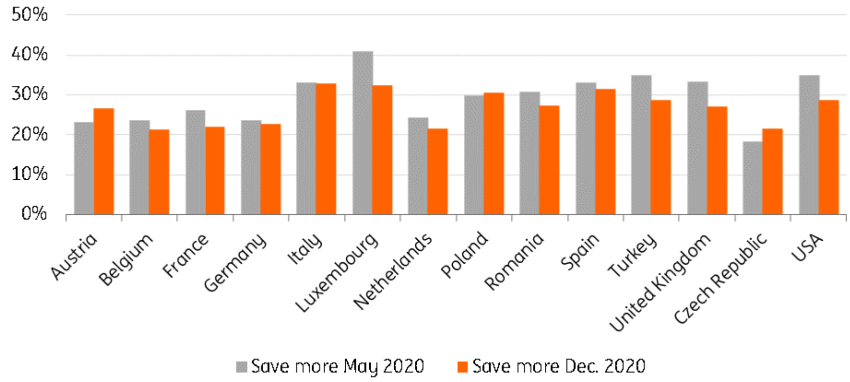
In the first lockdown, surging savings rates across the Western hemisphere were mainly the result of involuntary savings. As a result, the reopening of economies led to an almost full reversal of the excess savings into consumption. In 2021, the rotation from savings into consumption could be much more uneven on both sides of the Atlantic

Source: Shutterstock

The savings-consumption rotation during the first lockdown

The first lockdown saw an unprecedented surge in savings in the US and Europe. 'Involuntary savings' was the buzz phrase of the moment. With people suddenly sitting at home, retail stores, restaurants, bars and cultural events all closed, savings rates increased significantly. Planned vacations had to be cancelled, also adding to the increase in savings. The fact that these savings were mainly involuntary is also reflected in the relatively muted fall in consumers' willingness to spend. With the reopening of economies, savings dropped and consumption surged. In fact, the flow of savings equalled the flow of consumption almost entirely in the second and third quarters.

Did you save more or less?



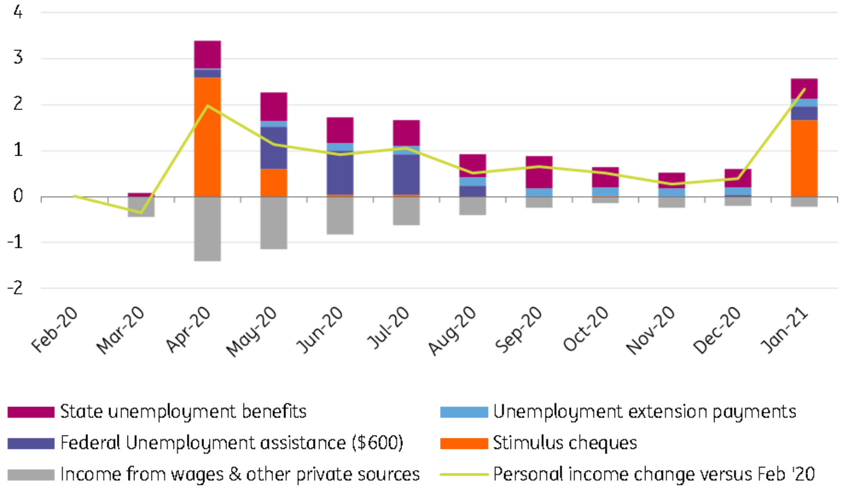
Source: ING International Survey

In the eurozone, short-time work schemes helped support household incomes. Unemployment rates remained relatively stable and the fear of potential job losses was high but short-lived. Savings rates across the eurozone surged on the back of involuntary and precautionary savings. According to European Commission surveys, the assessment of households' own financial situation worsened but only to historic averages and not below. Interestingly, the intention to save did not drop again in the third quarter, while excess savings were reduced and private consumption surged. The countries hit most by the crisis saw only half of these excess savings in 3Q actually spent in that quarter. In all countries, the savings rate remained higher than before the start of the crisis. This suggests that a larger part of the population increased savings as a precaution and not simply due to the lack of spending opportunities.

In the US, the story is slightly different. Rather than adopt the European style furlough schemes which were designed to preserve jobs, the US government took the decision to avoid interfering directly in the labour market. Instead, they chose to strengthen the financial safety net for those who lost their jobs by extending the duration of unemployment benefits, expanding the number of people who could receive them and then initiating a new $600 weekly Federal unemployment benefit to boost incomes. In consequence, the University of Chicago calculated that 69% of unemployment benefit recipients actually earned more money being unemployed than when they were working. The median recipient received 134% of their previous after-tax compensation.

This has promoted a broad strengthening of the US household balance sheet with cash, checking and savings deposits increasing by $2 trillion between 4Q 2019 and 3Q 2020 while outstanding credit card balances have fallen to a four-year low. Given the upscaled and expanded unemployment benefits and the $1200 CARES Act stimulus payment, increases in US savings are likely to have been spread more broadly across the income spectrum versus Europe. ING’s own international savings survey backs this up based on responses to who has increased savings rather than run them down.

Factors that have boosted US household incomes each month (annualised change in income versus February 2020 - USD tn)



Source: Macrobond, ING

The savings-consumption rotation during the second lockdown

Savings increased again during the second lockdown but in the eurozone, the willingness to spend has weakened, falling to the lowest level since June. This drop masks significant changes between what are basically two groups; the countries which entered a second lockdown in November like France or Belgium and the countries which entered a strict lockdown only at the end of 2020, like Germany. The former have seen a very subdued willingness to spend since the initial spike after the reopening, while the latter saw the hit to consumer confidence only recently. Overall, the willingness to spend remains low, which argues against a sharp surge in consumption once economies reopen. In fact, it looks as if involuntary savings have been replaced by precautionary savings. At the same time, however, don't forget that a reopening will boost demand for services like hospitality, leisure and culture as well, something that is not fully captured by traditional surveys.

It is also worth noting that consumption has not collapsed as much as it did during the first lockdown as both retail stores and customers have been able to adapt to new circumstances, shifting towards online shopping, and fewer planned expenditures had to be cancelled. Therefore, with the more subdued downswing, an accentuated rebound looks less likely.

Unlike Europe, the US did not enter a full second lockdown with the most onerous restrictions experienced only by Californians. Now that California's stay at home order has been rescinded and New York and other cities are again open for eat-in dining there is more opportunity to spend.

Recent data has shown that the improved financial position of US households means that when presented with a windfall payment, such as the latest $600 stimulus cheque, consumers have the confidence to spend it. This contributed to a 5% month-on-month jump in retail sales in January with daily credit and debit card transaction data from www.tracktherecovery.org indicating that the bulk of the additional spending came from lower income households.

This is an encouraging precedent for the outlook for consumer spending since President Biden is proposing to raise the extra Federal weekly unemployment benefit back to $400 per week after it was tapered in 2H20 while also providing an extra $1400 individual stimulus payment. He also has aspirations to raise the minimum wage to $15/hour nationally, which if implemented would further boost the earning power of lower income households.

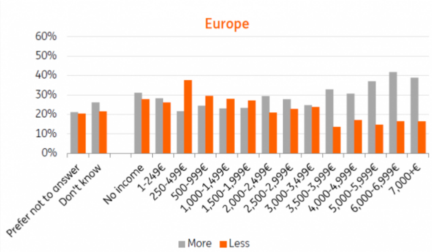
With the US Covid vaccination programme gaining momentum, there is a realistic chance of a broad economic reopening in mid to late 2Q 2020, including for consumer services, leisure and hospitality. This is potentially one to two quarters ahead of Europe. US job opportunities will therefore improve more swiftly, with surveys already suggesting that households expect jobs to become more plentiful, which could boost the chances that households use some of their accrued savings for spending over coming months. Significantly, the unemployed also have the guarantee of robust unemployment benefits to fall back on should they fail to find work.

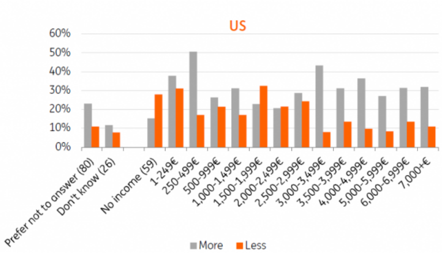
Outlook: Pent-up demand or too elevated expectations?

Looking ahead, the key question for the economic outlook is whether the great rotation between savings and consumption in 2Q and 3Q will repeat itself or whether the latest increase in savings will be left unspent. The US and eurozone patterns differ significantly mainly due to two factors: the distribution of savings across different income categories and the sheer size of the income subsidies.

An important determinant of potential consumption is the distribution of excess savings across the different income groups. In theory, the propensity to spend is lower in high-income households than in low-income households. Against this background, the results of an ING survey give interesting insights. While in the eurozone between 30% and 40% of the higher-income households saw their savings increase during the pandemic, only around 20% of the lower-income households reported higher savings. In the US, these numbers are much more dispersed across the entire income range.

Changes in savings behaviour according to income





Source: ING International Survey

The size of the direct income subsidies has also been much larger in the US than in the eurozone. While in the eurozone even short-time work schemes mean at least a small drop in disposable income, the fact is that at least initially almost 70% of US unemployment benefit recipients earned more money due to the government support than when they were working. Additional payments of $1200 and $600 (with a third proposed payment of $1400) helped further improve the financial position of millions of households.

Fiscal stimulus more targeted to the lower-income US households should lead to a stronger boost of private consumption than the more indirect stimulus in the eurozone. Also, the second lockdown seems to have anchored fears of potential job losses in the eurozone, shifting involuntary savings to precautionary savings. This is not something we have seen in the US.

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