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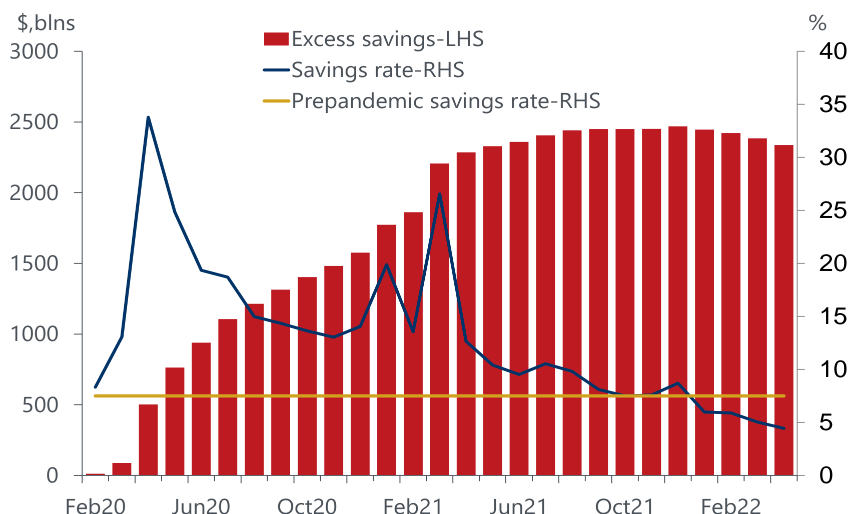
Research Briefing | US

Extent, pace of excess savings drawdown key to pace of growth

- **US households have started to draw down the excess liquid savings they accumulated during the pandemic but pinpointing the extent of the drawdown is difficult given the way data are reported. We estimate excess savings may have plunged more than $600bn as of April – more than four times the decline implied by the reported monthly personal income data, as individuals paid record taxes following the April 15 deadline.**
- **The rate at which excess savings is drawn down in the coming months and quarters has important implications for consumer spending and GDP growth. Our baseline forecast assumes households will use $1.1tn of their excess savings by the end of 2023. A drawdown of half that amount would knock 1.2ppts off real GDP growth in 2022 and 0.2ppts off growth in 2023. Conversely, a drawdown of twice the amount in our baseline, which would nearly deplete excess savings, would lift GDP growth by 2.2ppts in 2022 relative to our baseline and by 0.4ppts in 2023.**
- **How much surplus savings are depleted going forward will be heavily influenced by the distribution of these savings among households. If the remaining excess savings are concentrated among upper-income households, they may decline more slowly now that tax season is over. Unfortunately, Federal Reserve figures on household balance sheets that show excess savings concentrated among upper-income households may have become less reliable during the pandemic.**
- **Households who have exhausted their savings may be borrowing more to maintain spending in the face of high inflation. However, the lowest-income households may both lack a savings cushion and have limited credit availability, forcing them to curtail their spending, particularly on non-discretionary items and services.**

The April personal income and spending data showed a decline in households' excess savings of $132bn from their December peak of $2.47tn, leaving a still-sizable cushion of $2.33tn **(Chart 1).**

Chart 1: Excess savings are declining, but a cushion of more than $2tn remains...or does it?



Source: Oxford Economics

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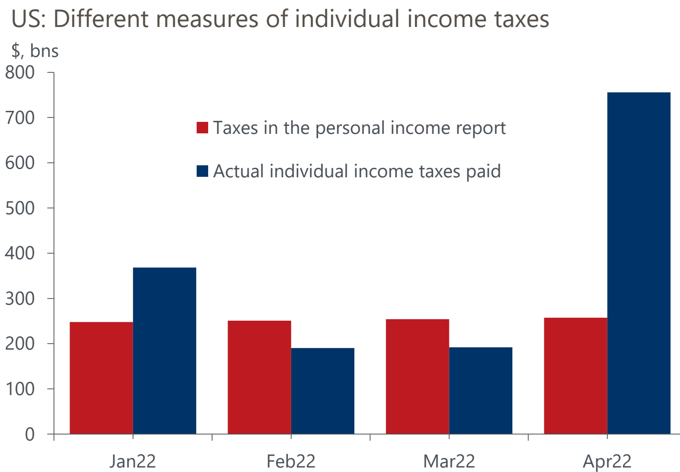
Extent, pace of excess savings drawdown key to pace of growth

The April data – which included downward revisions to disposable income and savings for January through March – likely understates the actual drawdown of savings in 2022 so far. In the personal income data, estimates of individual income taxes are spread roughly evenly across the 12 months of the year, rather than being recorded in the months in which they occur. Actual individual income taxes, which soared to a record level following the April 15 tax date, were much stronger in the January-April period than the figures in the personal income data. We estimate that actual individual income taxes, both federal and state and local, totaled $1.51tn in the first four months of the year compared to $1.01tn assumed in the personal income reports. **(Chart 32).**

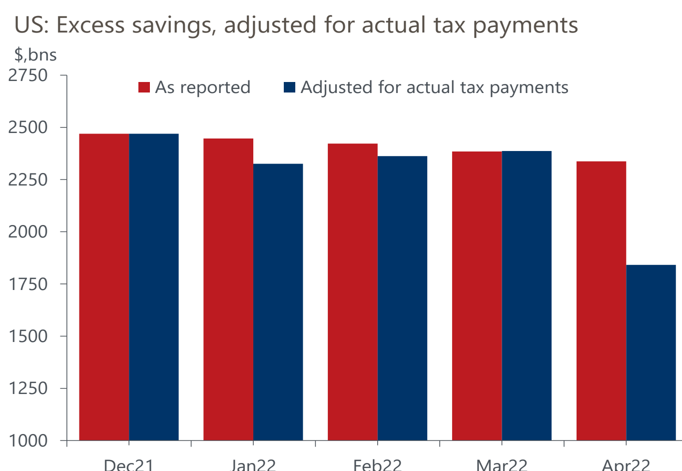
Chart 2: Actual income taxes paid during January-April were much greater than reported in personal income data



Source: Oxford Economics

Adjusting disposable income to account for actual tax payments – and therefore savings, which in the personal income data are the difference between disposable income and outlays – implies a plunge in excess savings of more than $600bn, to $1.8tn as of April (**Chart 4**).

Chart 3: Excess savings may have fallen below the $2tn mark in April

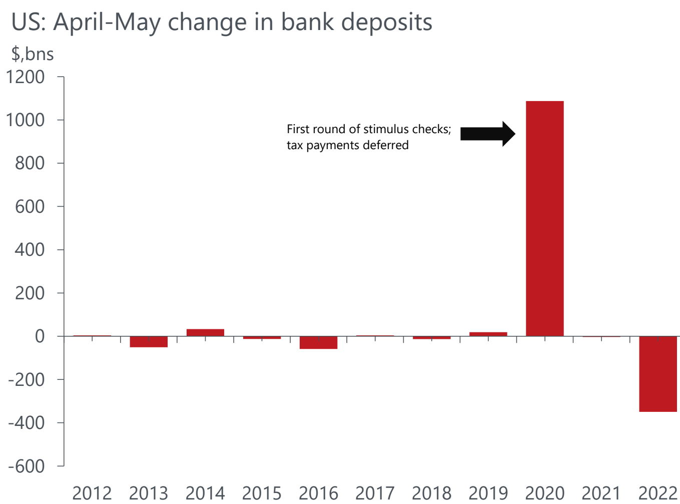


Source: Oxford Economics

Other data sources suggest a large decline in households' liquid savings following the April 15 tax deadline. Deposits at commercial banks, excluding large time deposits, can fluctuate around tax payment deadlines. However, those deposits plunged about $350bn in April and May combined (tax payments related to the April deadline often spill into May), a significant outlier compared to changes in deposits in those two

months over the past 10 years (**Chart 5**). After falling sharply in April and May, bank deposits have stabilized so far in June.

Chart 4: Bank deposits plunged as individuals paid record tax bills



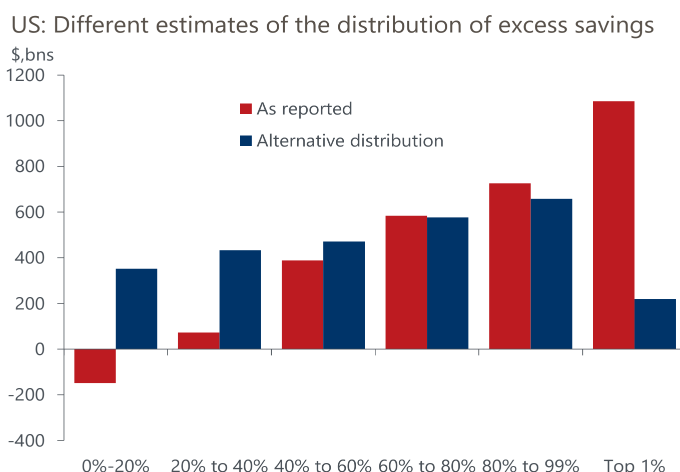
Source: Oxford Economics

Importantly, looking ahead the personal income data will tend in many months to overestimate taxes relative to actual tax payments and therefore underestimate disposable income and savings. By the end of 2022, however, estimates of the excess savings drawdown based on the data as reported and actual tax payments should converge.

What happens to savings going from here?

Our forecast for personal income and consumer spending assumes that households' excess savings will decline by about $1.1tn to $1.36tn by the end of 2023 from their Q4 2021 peak of $2.47tn. The pace at which excess savings are depleted going forward depends heavily, in our view, on how those savings are distributed among income groups (**Chart 5**). To the extent savings are concentrated among upper-income households, we think they may be drawn down gradually now that large tax payments are in the rear-view mirror. Savings are likely to be depleted more quickly if they are more evenly distributed, given lower- and middle-income households' greater propensity to spend, particularly in an environment of high inflation.

Chart 5: Who holds the excess savings? A range of scenarios is possible



Source: Oxford Economics

The Federal Reserve's quarterly data on household balance sheets showed that excess savings (as reported) continued to be heavily skewed toward upper-income households at the end of the first quarter, with the

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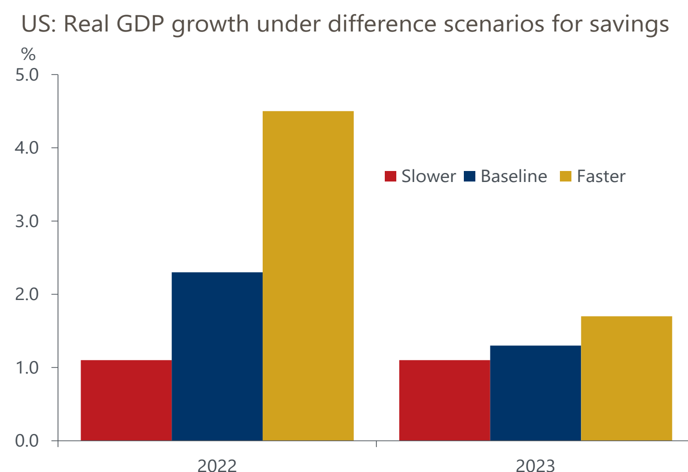
top quintile holding about two-thirds of the surplus savings, and the top 1% alone holding 40%. The data also implies that those in the bottom quintile have accumulated a savings deficit relative to their pre-pandemic savings patterns. Unfortunately, the data are only through Q1 and thus do not capture the impact of the surge in tax payments after the April 15 deadline. Last year, however, Federal Reserve researchers speculated that the distributional accounts data may have become a less reliable gauge of the distribution of households' liquid assets during the pandemic and estimated an alternate, much less lopsided distribution **(Chart 6).** It's worth noting that the Fed estimates of an alternate distribution were as of Q1 2021, when lower- and middle-income households may still have had savings cushions from stimulus checks and other fiscal support measures. There are many anecdotal reports describing lower- and middle-income households who have depleted the extra savings accumulated during the pandemic.

While acknowledging the considerable uncertainty surrounding who holds excess savings and how quickly it will be spent, we simulated the impact of a slower and faster rate of savings drawdown using the Oxford Global Economic Model. For the slower scenario, we assumed about $550bn in surplus savings would be tapped by the end of 2023, half of what's in the current baseline; and for the faster scenario, we assumed $2.2tn would be drawn down, twice what's in our current forecast, and nearly depleting excess savings by the end of next year. In the slower scenario, the savings rate averages about 6% through the end of 2023, above the 4.4% average in our current forecast but still below the pre-pandemic average of 7.5%. In the faster scenario, the savings rate averages around 1%.

The slower pace of savings drawdown would take a big bite out of real consumer spending growth, all else equal, reducing it from 3.3% to 1.8% in 2022 and from 1.8% to 1.4% in 2023. In this scenario, real GDP growth is lowered by 1.2ppts in 2022 to 1.1% compared to our revised forecast for growth of 2.3%, which will be incorporated in our July baseline. Real GDP growth in 2023 is reduced by 0.2ppts to 1.1% from our updated forecast of 1.3%, leaving the level of real GDP 1.2% lower at the end of 2023 **(Chart 6)**.

Chart 6: A faster or slower drawdown of excess savings could have a big impact on GDP growth



Source: Oxford Economics/Haver Analytics

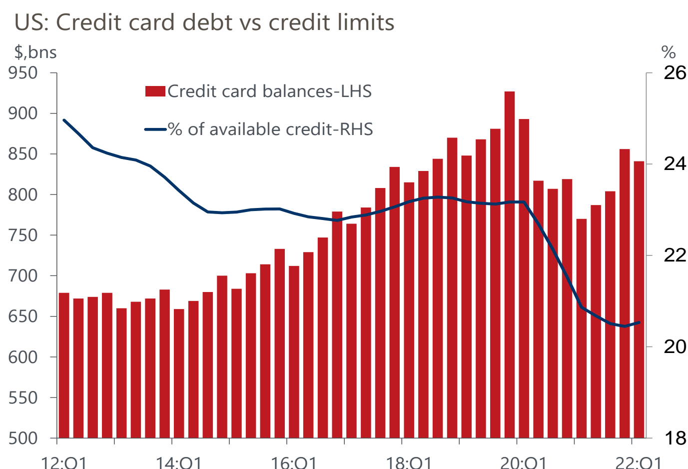
In the faster savings drawdown scenario, consumer spending growth gets a boost to 6.1% in 2022 and 2.6% in 2023. Real GDP growth is boosted by 2.2ppts in 2022 and 0.4ppts in 2023 to 4.5% and 1.7%, respectively, and the level of GDP is 2.4% higher at the end of 2023.

Are households borrowing out of need?

Households who may have drawn down their excess savings, particularly lower- and middle-income households, may need to borrow more to maintain consumption in the face of the highest inflation rates in decades. Credit-card use has been growing at a rapid clip in recent months, with revolving credit expanding by a record amount in March and by the second-largest amount in April, if months that contained significant benchmark revisions are excluded. So far, though, households – at least in the aggregate – aren't close to maxing out their ability to borrow with their credit cards. Data from the New York Fed showed that

as of the first quarter, outstanding credit-card debt was equal to about 21% of available credit, below the average since 1999 of 25% (**Chart 7**).

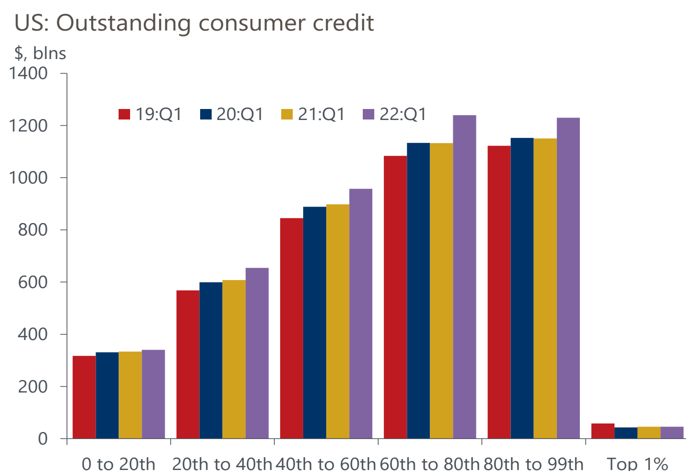
Chart 7: Use of credit-card debt has increased, but balances are well shy of limits



Source: Oxford Economics/Haver Analytics

The Federal Reserve's data on household balance sheets broken down by income showed consumer credit increasing 7.2% in the first quarter; the balance sheet data includes credit-card debt and other forms of consumer borrowing such as student and auto loans. Gains ranged from 2.0% for households in the bottom income quintile, to 9.5% in the fourth quintile**.** Outstanding consumer credit rose 6.7% in Q1 for households in the top income quintile, although for the top 1% of earners, consumer credit rose just 0.8% (**Chart 8**).

Chart 8: Most households boosted their borrowing by 6% or more in Q1



Source: Oxford Economics

The relatively small gain for the bottom income quintile may be misleading since those households may have limited access to credit. The Federal Reserve's recently released Survey of Household Economics and Decisionmaking (SHED) showed that 57% households with income below $25k had a credit card, compared to 84% of households overall. Households with a limited ability to borrow, who also have relatively little or no savings cushions, may have no choice but to curtail spending, particularly on nondiscretionary items and services as inflation remains stubbornly high.

Survey data collected by the Federal Reserve Bank of New York in April showed that households with incomes below $50,000 expected to increase their spending by 5.4% over the next year, but that increase is entirely due to more spending on essential items, which they expect to increase 9.0% (**Chart 7**). Those households now look for the spending on nonessential items to be flat, diverging from other income groups. Those earning between $50k and $100k and above $100k look for their spending on essential items

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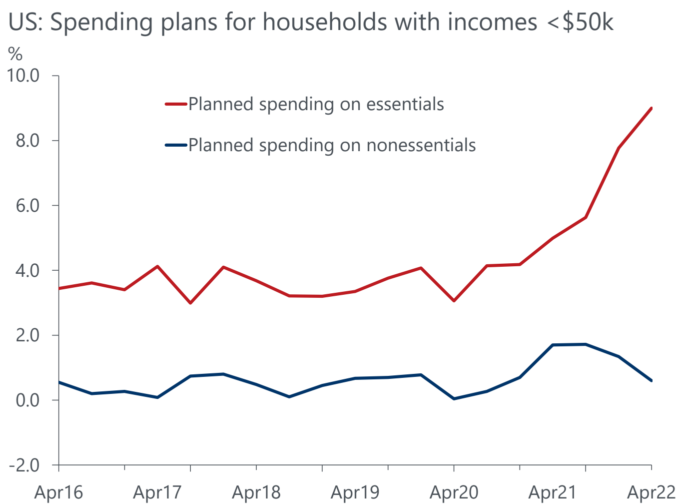
to rise about 6% for the next year and expect their spending on nonessential items to increase 3% and 5%, respectively.

Chart 9: Lower-income households plan to keep spending on nonessentials flat



Source: Oxford Economics

In sum, consumers currently face a double burden of rising prices and rising interest rates. Households in the aggregate appear to have a still-ample savings cushion, although the personal income data may overstate remaining savings due to the way taxes are treated in the data. We will continue to monitor closely the monthly readings on the drawdown of excess savings adjusted for the actual timing of tax payments. There is considerable uncertainty surrounding the distribution of excess savings among households, which could be key in determining how quickly they are used. A much slower or faster pace of drawing down extra savings than assumed in our baseline forecast could have a significant impact on GDP growth.

Most households are increasing their borrowing to support their spending. The lowest income households may have both limited or no savings and a limited capacity to borrowing, forcing them to curtail their spending.