Daily Note

PANDEMIC SAVINGS: THE K WRIT LARGE

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- **US households have $1.6tn in "excess" savings**
- **But the demographic mix of savings mean they won't be the key to high inflation**
- **Besides, not all savings are forced; portfolio rebalancing is also at play**

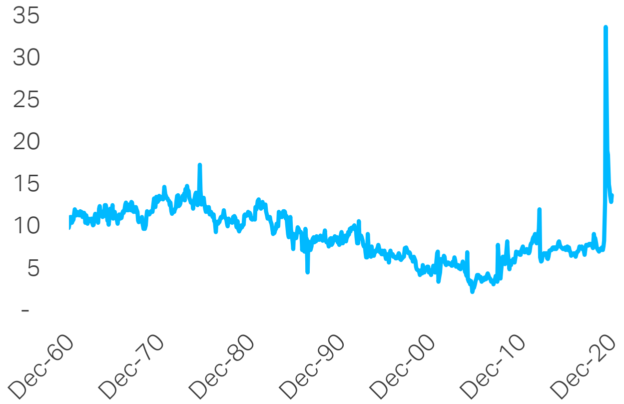
Inflation continues to occupy centre stage in investor discussions globally. In the US, the debate has swiftly moved towards overheating concerns in light of Biden's proposed $1.9tn stimulus bill. A key concern for inflation vigilantes – even before taking on board the Biden plan – has been that households have accumulated large savings on their balance sheets, which will be spent *forcefully* when restrictions ease and vaccines put the pandemic behind us. They need only point to January retail sales to show how a cheque ($600 in late December/January) can transmit directly to activity. With its focus on (even more) generous stimulus checks and unemployment insurance, the Biden plan will boost savings further, encouraging a (more) rapid spending spree once lockdowns end. Meanwhile, supply-side hurdles, rising input costs and higher commodity prices will exacerbate inflationary pressure.

Headline figures overestimate the "excess" savings that households have accumulated since the outbreak of the pandemic. To be sure, the personal saving rate *will* fall as consumers spend more of their disposable income on eating out, going to the theatre and on holidays, for example. But those expecting households to aggressively run down their *stock* of savings will be disappointed. There could be a burst of inflation in the immediate term, especially in the services sector, but it will be short-lived unless there is a meaningful improvement in the labour market. We focus on the US in this note, but these observations apply elsewhere too, especially in the UK and the euro area.

The personal saving rate in the US rose sharply to 34% in April 2020, the highest level since such monthly data became available in 1959. Generous government support and limited spending opportunities

Households savings have surged

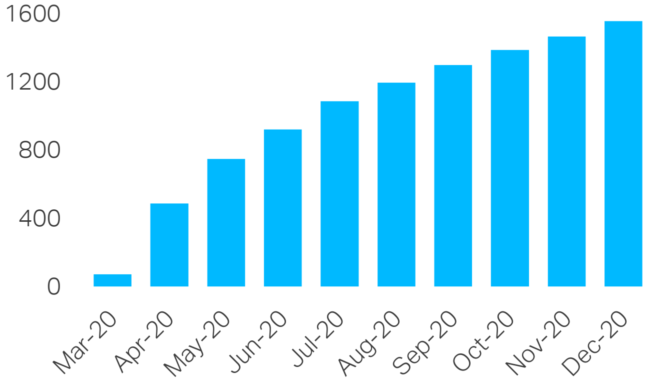
Personal savings as % of disposable personal income



Source: Datastream, TS Lombard

$1.6tn in "excess" savings

US personal income account, accumulated "excess" savings during the pandemic, $ bn



Source: Datastream, TS Lombard

Book a video meeting with our analysts here due to restrictions boosted savings. The rate has since fallen, but remains higher than the pre-pandemic level. Back-of-the-envelope calculations show that US households have accumulated $1.6tn in "excess" savings during the period March-December. These figures do not include the $600 stimulus checks and unemployment insurance payments that were approved in December as part of the $900bn stimulus bill.

But not all of these savings are forced. Households have built up precautionary buffers as well because they are uncertain about the economic outlook over the next year. For instance, an NY Survey showed that 40% of respondents expect the unemployment rate to rise over the next year. Although the share has come off from the pandemic high of 51%, it has been on the rise again since October. Similarly, the net percentage of respondents expecting their financial situation to improve over the next year is the lowest since such data became available in 2014 (barring the pandemic trough).

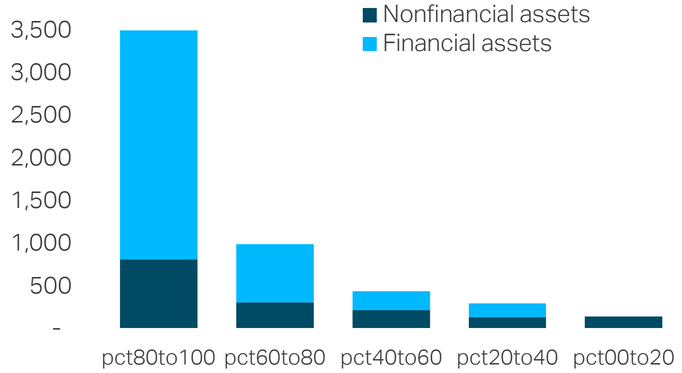
The distribution of savings is highly skewed towards higher-income households, which have a lower marginal propensity to consume (see left-hand chart below). The impact of the pandemic has been highly uneven. Low-wage jobs in hospitality and other services sectors have been decimated while high-wage jobs have been relatively safe. High-income earners spend more on services activities, which have been forced to shut down, boosting their savings. In addition, the stimulus checks have not been well-targeted and those who are employed and in relatively high-paying jobs have received such checks. Separately, the increase in pent-up demand is less than what headline figures suggest. For instance, the consumption of durable goods during the pandemic has surged well above its trend rate of growth.

Some savings reflect households rebalancing their portfolios towards safer and liquid assets. The biggest increase in households' assets has been through their holdings of liquid components such as checkable deposits, currency, time deposits, and short-term investments. While this may suggest that there could be boost in transaction demand on the horizon, there are two caveats to keep in mind. First, 67% of the increase in liquid assets during the period Q1-Q3 2020 has been in the top income quintile. Second, households have been rebalancing their portfolios towards safer assets. Once uncertainty eases, they will want to replenish their share of non-liquid financial assets, which has fallen rapidly over the last year.

Consumers are willing to spend only a fraction of their stimulus checks and unemployment insurance on consumption. According to a NY Fed Survey, 36% of stimulus checks given under the CARES Act were saved and 35% were used to pay down debt. The rest was used for consumption (26%) and for donations (3%). The share of savings was higher for those earning more. Consumers expect to increase their savings if they were to receive more checks. In sum, consumer spending on services will rise swiftly as households spend more of their *income*, not necessarily because they are running down their *stock* of savings. We discuss these themes in detail in our Global Financial Publication, which we will publish later this week.

Increase in assets concentrated in high-income households

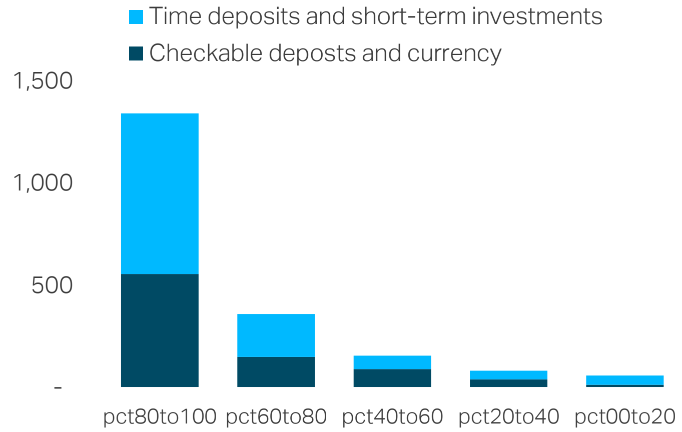
Change in assets by income percentiles, $ bn, Q3 2020 versus Q4 2019



Source: Fed, TS Lombard

Who is holding liquid assets?

Change in liquid assets, (Q3 2020 versus Q4 2019), $bn



Source: Fed, TS Lombard