

US consumer remains wealthy, despite debt woes

Global economic update: July 2010

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While it is well documented that the US consumer has become highly indebted with low savings, it is not always well understood that despite the high level of debt, the US consumer remains extremely wealthy. The US remains the largest economy in the world; and consumer spending remains the backbone of the US economy

Mortgages responsible for debt

In terms of debt, at the end of the first quarter of this year, US total household debt was measured at a substantial \$13.97 trillion. Most of this was due to home mortgages making up 74% of the total and consumer credit made up 17%. Household mortgage debt rose by a massive 104.3% from after 9/11 to the first quarter of 2008. That is an increase of \$5.4 trillion in a period of just seven years.

During this time the number of new homes built rose from an annual rate of 1.55 million houses to over 2.2 million homes a year in early 2006. The total number of US homes increased from 119.3 million in 2002 to 130.8 million in 2008. That is a rise of 10.8 million homes in six years. Unfortunately, around 14.4 million homes are now currently vacant, which is extremely high and 40% more than the number of homes built during the housing boom.

US consumers try to pay off debt

US consumers have been trying to deleverage. Consumer debt (excluding mortgage debt) fell by a significant \$96 billion over the year. In addition, US mortgage debt declined by a substantial \$256 billion over the same time period. These declines coupled with a rise in personal income, has meant that the ratio of US household debt to personal disposable income has fallen from 131.4% in the first quarter of 2009 to 125.9% currently. While this ratio would still be considered relatively high by historical standards, it is meaningfully below the peak of 136.4%, which was recorded in 2008. Debt servicing costs has also been on the decline, dropping from almost 14% of disposable income in early 2008 to around 12% currently.

The fall-off in household debt is naturally reflected in a rise in household savings, which has grown marginally from a low of less than 1% of disposable income in early 2008 to 3.6% currently. Overall the consumer has clearly had some success in paying off debt relative to the peak of the credit crisis, but the improvement has not been spectacular.

Value of household assets fell, but still in line with long-term trends

In terms of assets, at the end of the first quarter of this year, the value of US household assets amounted to \$68.53 trillion. The value of household assets fell by a staggering \$17.5 trillion during the credit crisis, but they have since risen by \$6.1 trillion, mainly as a result of a \$5.5 trillion improvement in the value of financial assets.

As a result of the increase in assets values over the past year, the net worth of US households rose to \$54.56 trillion at the end of the first quarter of 2010. That is \$6.3 trillion higher than a year-ago, but still \$11.2 trillion below the record level set in 2007. US net wealth is now nearly five times that of household disposable income. The current ratio is actually exactly in-line with the long-term ratio, which dates back to 1952, although there have been times when the ratio has risen over 600%.

Overall the US consumer remains extremely wealthy by historical and international standards; despite the high level of debt and the impact of the credit crisis.

Global economic outlook

Economic growth returns as household spending and business investment show signs of revival. But sustained growth remains uncertain as economic recovery remains uneven across countries and regions

Helped by a combination of extensive fiscal stimulus packages and expansionary monetary policies, most economies registered positive growth in late 2009 and early 2010. Trade figures have also improved significantly with world trade volumes 17% higher than a year ago, but still 5% below the corresponding level in 2008. World trade is expected to grow by around 7% in 2010, having declined by 13.1% in 2009. However world economic recovery is uneven across countries and regions. While growth prospects for many emerging and developing countries are encouraging, economic activity is subdued and below potential in many developed economies.

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