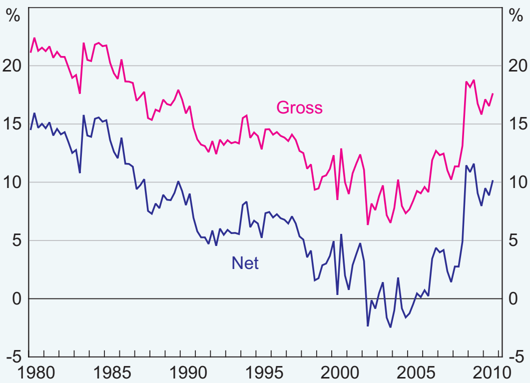
Box C
The Increase in the Household Saving Ratio

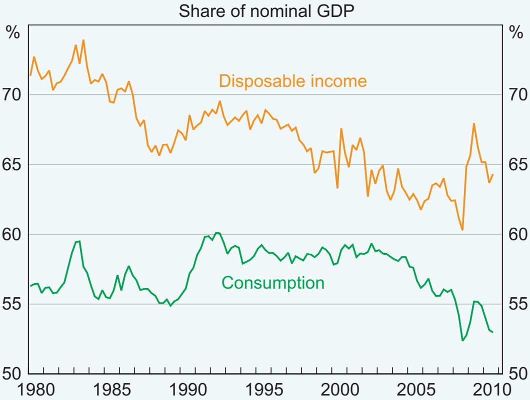
The household saving ratio is estimated to have increased sharply in recent years. After falling for over two decades to a low point of around minus 2 per cent, household saving (net of depreciation) has increased since the mid 2000s (Graph C1). It is now estimated at 10 per cent of household disposable income, which – abstracting from the period in late 2008 and early 2009 that was affected by the government stimulus payments – is the highest saving ratio in over 20 years. While estimates of saving are prone to significant revision – since they are measured as the difference between household income and consumption, two very large aggregates that are subject to measurement errors – and there are also several definitional issues as to what should constitute saving, this is nonetheless a significant turnaround in the saving ratio.[1]

Graph C1
Household Saving Ratio
Per cent of household disposable income



Source: ABS

Graph C2
Household Sector Income Account
Share of nominal GDP



Source: ABS

The decline in the measured saving ratio during the 1980s and 1990s occurred against the background of financial deregulation, falls in nominal interest rates, a significant increase in the ratio of household debt to income and a rise in household wealth (including capital gains on housing assets). Although there was a fall in the share of national income that accrued to the household sector, these other factors contributed to stronger growth in consumption spending during this period. In contrast, the increase in household saving since the mid 2000s has reflected a period of strong increases in household income and a more modest pace of household spending (Graph C2).

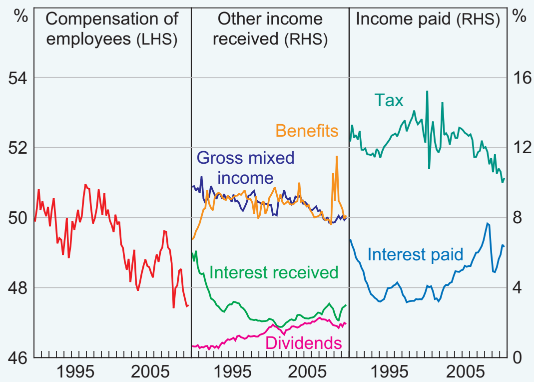
1 Recent revisions to historical saving ratio estimates have been especially large, in the order of 5–7 percentage points. There are several conceptual issues concerning the measurement of the household saving ratio, and different approaches can produce very different trends: see ABS, Australian System of National Accounts, 2002–03, Cat No 5204.0, 'New Analytical Measures of Income, Saving and Wealth', for a detailed discussion of the household saving measure. For an alternative approach to measuring the saving ratio, see 'Box D: Capital Gains and Measures of Household Saving', *Statement on Monetary Policy*, May 2006.

Since 2004, nominal household disposable income has grown strongly, at an annual average rate of 7.3 per cent. This is slightly faster than the growth in nominal GDP over that period, which was boosted by the rise in the terms of trade. The growth in income has mostly reflected strong growth in after-tax wage and salary compensation, due to a buoyant labour market and income tax cuts (Graph C3).

Despite the solid rises in income over a number of years, the growth in nominal household consumption has remained quite modest, at an annual average of 5.4 per cent since 2004. Until mid 2008, this occurred in the context of rising interest rates as monetary policy was tightened. In the past two years, consumption has grown at an annual nominal rate of just 3.8 per cent. With household incomes growing strongly and the pace of consumption growth remaining quite low since 2004, the household saving rate has increased markedly.

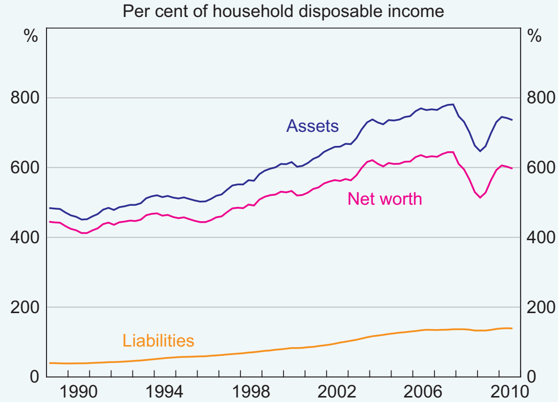
The moderation in consumption spending and corresponding rise in the saving ratio appear to reflect a change in households' attitudes towards debt and financial vulnerability, after a long period when lower interest rates and financial deregulation saw a significant rise in household indebtedness. Initial signs of a change were apparent around the middle of the decade, when there was a cooling of the earlier housing boom. There appears to also have been a more significant change in attitudes and behaviour following the onset of the global financial crisis and the sharp fall in equity markets and wealth, as well as the slowing in the domestic economy in late 2008 and general increase in uncertainty (Graph C4). This change in behaviour is apparent in other indicators, including the increase in housing equity injection since the middle of the decade and surveys that show an increased share of households that believe bank deposits or paying down debt are the 'wisest place for saving.' The modest rate of increase in household indebtedness suggests that household behaviour remains cautious. However, there are a few factors – including the recovery in household net worth over the past 18 months and the improvement in the labour market – that would suggest that growth in household consumption is unlikely to remain as low as over the past couple of years.

Graph C3
Household Disposable Income
Share of nominal GDP



Source: ABS

Graph C4
Household Net Worth
Per cent of household disposable income



Sources: ABS; APM; RBA