What Factors Determine Whether Households Spend Less than Income?

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Continuing a decade long trend, the rate of personal saving of American households continues to decline. In June 2007, personal saving as a percentage of disposable personal income was 0.6 percent (Bureau of Economic Analysis, 2007). Without a financial cushion, families have little protection against the effects of income loss due to unemployment, disability or death of a primary income earner. Insufficient savings can also have adverse consequences for the community. Home or business ownership are difficult to achieve without savings.

The research analyzes household spending relative to income. The life-cycle hypothesis of savings (Ando & Modigliani, 1963) proposes that households will attempt to smooth consumption over the life-cycle by borrowing when young, saving at mid-life, and withdrawing from savings when retired. Data for the study are drawn from the 2004 Survey of Consumer Finances which is sponsored by the Federal Reserve Board of Governors (Bucks, Kennickell, & Moore, 2006). The analysis includes only working households (N = 3,478).

The analysis includes descriptive statistics, Chi-square tests, ANOVA, and logistic regression. The average age of the head of household was 44 and the average number of years of education was 13 years. Seventy-three percent of the household heads were white, 62% were married or living with a partner. Sixty-two percent were homeowners. Forty-four percent spent less than income, 37% spent equal to their income, and 19% spent more than income.

The regression showed that households with a head aged 51 and older were more likely than those with a head age 35 or younger to spend less than income. This is consistent with life-cycle theory which suggests that saving is greatest at mid-life. Also, households headed by a man, a person with a college degree, those with household income in the upper quartile of the income distribution, and those with a saving and investing horizon of a few years or longer were more likely to spend less than income compared to households headed by a woman, a person with only a high school education, with income in the bottom quartile, and those whose saving horizon was less than one year, respectively. Tolerance for risk was positively related to spending less than income.

References

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