PHOTO BY STEPHEN KENNEDY

Clipping Costs

Market swings affect household budgets

Like many others, the housing crisis forced Kelly Snyder's family to take a hard look at the household budget.

As a stay-at-home mother of two young children, Snyder and her husband relied on his job as a remodeling contractor for their income.

Unfortunately, the slowdown that hit the entire economy—and housing in particular—also resulted in a significant decline in the number of customers willing to consider home improvement projects. A year after the official start of the last recession, Snyder's family was feeling the pinch.

"During the last three months of 2008, we had no income," said Snyder, who lives in a suburb of Kansas City. "We have always tried to live below our means, but during that time, we were forced to pull from our savings because no one wanted to spend money on housing."

The potential for little or no future income led the Snyders to search for ways to cut back. One place in particular, the monthly grocery bill, seemed to be a logical place to start.

Snyder began researching ways to save money at the supermarket, and soon, she caught on to what has since become a burgeoning trend—scouring newspaper inserts and websites for the latest coupons and discounts from manufacturers, retailers and others.

Within a few months, Snyder became an expert in penny-pinching techniques, and by using coupons and carefully planning her shopping trips, she has cut her family's grocery bill from about $800 a month to less than $300. Now, through her own website and by offering seminars at offices and churches across the Kansas City metro area, Snyder passes on her knowledge to others on the best coupon-clipping strategies and other budget-cutting tricks

"Even though we are spending much less on groceries, we are eating better and are even able to increase the amount of organic food we buy," Snyder said. "If you can take off just $100 a month from your grocery bill, it will add up."

Snyder doesn't count herself among the "extreme couponers" featured on reality television shows who stockpile large amounts of goods just to save money. But, her more modest approach highlights some of the steps households across the country took when the economy turned for the worse.

Over the last several decades, the stock market and the housing market have experienced numerous booms and big busts. Households' overall wealth is largely dependent on these two markets, so changes in the value of stocks and homes have a direct impact on how much people spend.

"Changes in household wealth, primarily in the housing and stock markets, can have a measurable impact on overall consumption," said Oklahoma City Branch Executive and Economist Chad Wilkerson, who, along with Associate Economist Megan D. Williams, recently studied the effects of household wealth swings, which can be difficult to measure and vary from state to state.

Accumulating wealth allows households to save for retirement, grow assets to provide for heirs, build up emergency funds and determine current consumption. The stock market plays a role in determining household wealth and, ultimately, consumption, but the housing market's impact is likely stronger, the economists say.

"Consumption can be more sensitive to changes in the housing market," Williams said. "As home prices continue to fall across the country, the question is, 'How will that affect household wealth?'"

Measuring household wealth

In their analysis, Wilkerson and Williams constructed estimates of housing and stock market wealth for each state, with a focus on the Tenth Federal Reserve District, which includes all or parts of Missouri, Nebraska, Kansas, Oklahoma, Wyoming, Colorado and New Mexico.

The economists' state estimates of household wealth relied on data on stock dividend income from the Bureau of Economic Analysis and the Fed's Flow of Funds report, as well as housing data from the Federal Housing Finance Agency and the U.S. Census Bureau, among other sources.

For the Tenth District, the economists discovered that estimated per capita housing and stock market wealth was nearly as high as the nation as a whole. However, Wilkerson and Williams found wide variations among individual states:

- Wyoming and Colorado were the wealthiest Tenth District states. Stock market wealth in Wyoming is more than twice that of the nation or any other Tenth District state. The researchers attributed this to the fact that Wyoming has no personal or corporate income tax, making it an attractive place to hold financial assets. In both states, housing wealth is nearly 20 percent higher than the nation, reflecting relatively higher home prices.
- Nebraska and Kansas have household wealth levels that are similar to the nation. Housing wealth in the states is well below the national average due to lower home prices, but the states' stock market wealth is larger than the rest of the nation, which may be due to higher-than-average incomes.
- Missouri, New Mexico and Oklahoma have household wealth that is slightly lower than the nation. New Mexico's lower stock market wealth could be due to the fact it has

the lowest per capita income in the District. Household wealth in Missouri and Oklahoma is hampered by home prices that are some of the lowest in the nation.

In addition, the pattern of growth in wealth has varied somewhat from national trends. "Over the last two decades, stock market wealth in the District has generally tracked the national pattern," Wilkerson said. "There is a larger gap between the nation and the District when it comes to housing wealth."

Wilkerson and Williams' analysis puts the Tenth District's current household wealth at 98 percent of the national average, but during the housing boom in 2005, it was about 90 percent of the national average. After the farm, energy and real estate busts in the 1980s, it was even lower, totaling about 85 percent of the national average.

Notably, Kansas, Nebraska, Oklahoma and Wyoming have seen especially strong wealth gains over the past 20 years, buoyed in part by stable home prices.

"These states were hit exceptionally hard by the energy and ag crises in the 1980s," Wilkerson said. "They had more room to rebound in the 1990s, and the momentum carried through the 2000s as they've seen steady home prices compared to the rest of the nation since 2005."

During the housing boom, Wilkerson adds, housing wealth on the national level rose quickly as home prices across the country skyrocketed. Home prices were steadier in the Tenth District, which limited housing wealth in the region but resulted in relatively fewer problems during the national crash.

While home prices didn't rise quickly in the District, these relatively stable home price increases meant prices didn't have as far to fall when the crash came, and in fact, the national home price collapse has been three times greater than in the Tenth District, Williams said.

Economic effects

As households accumulate wealth, the results are sometimes not seen until several years or decades later when, for example, retirees begin to tap the assets they've built up during their working years or when wealth is transferred to heirs.

However, data on consumption and income suggest that changes in wealth during the 2000s did have an impact on short-term

KELLY SYNDER found several ways to cut household costs and offset the current economy's effects on the household income, including the use of coupons and bargain shopping for items her family needs.

PHOTO BY GARY BARBER

household consumption. The clearest example can be found in that decade's housing boom.

"In the first part of the decade, spending on consumption rose faster than disposable income," Wilkerson said. "The difference was probably a result of families drawing on their wealth."

Housing wealth was the likely source, Wilkerson adds. Much of the wealth households have in the stock market is tied up in restricted retirement or pension accounts, making the funds less accessible than housing wealth, which could easily be tapped through home equity loans during the boom. This wealth can translate into more spending.

Studies cited by Wilkerson and Williams suggest that for every $1 increase in housing wealth, consumption by households can rise by 6 to 10 cents, compared to just a 2-cent increase in consumption for every $1 increase in financial wealth.

This effect also works in the opposite way. A 2010 study by economist Jeremy Leonard found that households might have reduced their consumption during the housing collapse even more than they expanded it during the boom. Leonard suggests households expected home prices would continue to fall, so they reduced their consumption in anticipation of future declines in household wealth.

For Snyder, the coupon-clipper whose household income also depends on the housing sector, uncertainty in the housing market played a significant role in her spending decisions and strategies to save money.

"The recession has definitely increased the way people think about what they're buying, and how much they're paying for it." Snyder said. "People aren't getting raises, yet costs have increased. You've got to find a way to cut somewhere."

The outlook

The forecast for the housing market continues to look cloudy, Williams and Wilkerson say. If current trends hold, home prices in the United States could continue falling. Though home prices in the District have held up better than the nation in recent years, some states could experience a downturn in housing wealth, given current imbalances in their housing sectors.

However, long-term housing price prospects appear "somewhat better" in the Tenth District than the nation, Wilkerson says. As long as ratios of home prices to incomes remain within their current ranges, the region's housing market could fare relatively well.

Of course, there will be variations among states.

"If home prices continue to decline on a national level, consumption could be hit in a sizable way," Wilkerson said. "This impact could be felt in some Tenth District states."

That worry is one reason why Snyder plans to continue her penny-pinching strategies.

She might not be alone among other Tenth District households.

"It does take work to find ways to save, but I'll keep doing it because I have been successful at it," she said. "It goes beyond the grocery store. We're negotiating prices for other things, like insurance, and we'll absolutely continue to look for more places to save."

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BY BILL MEDLEY, TEN CONTRIBUTING WRITER

FURTHER RESOURCES

"BOOMS AND BUSTS IN HOUSEHOLD WEALTH: IMPLICATIONS FOR TENTH DISTRICT STATES"
by Chad Wilkerson and Megan D. Williams
KansasCityFed.org/publications

COMMENTS/QUESTIONS are welcome and should be sent to teneditors@kc.frb.org.