

Intelligent Money

Current thinking from Haven Financial Advisors

Personal Saving in America



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Special Notes of Interest:

- The poverty rate among seniors has fallen from 30% to 10% since 1965

Most Americans are concerned about their retirement. However, the evidence is mixed as to how successful we are at saving for it. Economists look at measures like the **Personal Savings Rate** to get a handle on the extent to which we are deferring consumption for our golden years. Issued monthly, this figure is calculated by subtracting everything we spend -- from mortgage payments to a night on the town -- from our disposable income which is personal income minus taxes and other fees to government agencies.

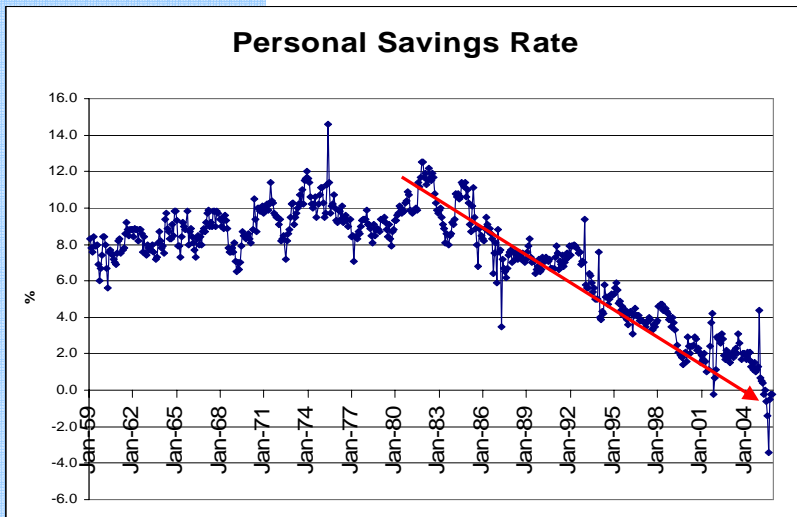
It is notable the Personal Savings Rate has fallen precipitously in the recent past. During the 1980s, it averaged 9.0%. It has fallen consistently since then. In fact, the saving rate was negative for all of 2005 -- the first time since the Great Depression. See the chart below.

Yet wealth accumulation continues apace as family assets like homes and investment securities continue to increase in value. Many observers see the real estate boom as the key variable that

sustains American consumption into the 21st century. Since 1999, the average family home equity increased by over two thirds -- one third in the last two years! Families view their homes like ATM's, using home equity loans and refinancings to pull out cash and support a higher level of spending. See the chart below.

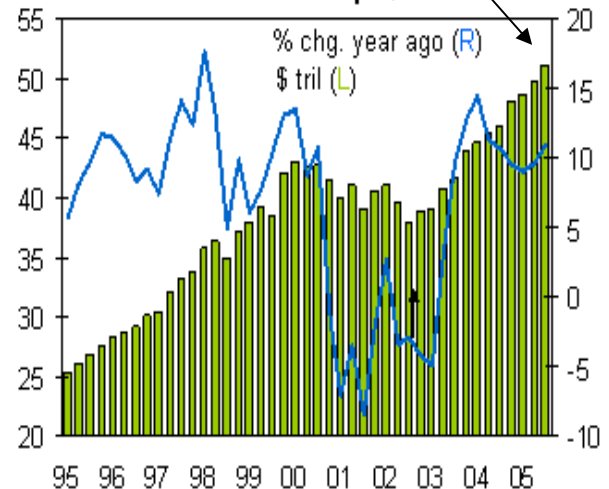
A key question is whether these consumer spending patterns are sustainable. While housing and stock markets can turn on a dime, consumption patterns tend to be more persistent. The American consumer is taking on more debt and, as such, is becoming more sensitive to the cost of borrowing.

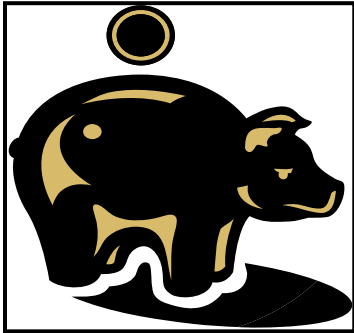
One key indicator that suggests increased strain on the consumer is the **Debt Service Ratio**. This figure is an estimate of the ratio of debt payments to disposable personal income. Right now it is at its highest point (13.75%) since figures were compiled in 1980. In each of the last three quarters, a



The average household is now worth \$458,000

Household Wealth Tops \$50 Trillion





Personal Saving (Cont)

successive record high has been set.

The good news is that there is no clear evidence that the consumer can't handle these increased obligations. In fact, credit card delinquencies hit a 10 year low while consumer loan delinquency is at an all-time low. While low income borrowers with small balances are suffering higher delinquencies, their impact on the overall economy is minimal.

Personal bankruptcies certainly swelled in 2005 but that development is primarily an artifact of bankruptcy law changes. Millions of people lined up to file under the more

liberal personal bankruptcy code that was eclipsed last October. Bankruptcy reform legislation was signed in April and became effective October 17. The bill would force some filers who currently file under Chapter 7, which eliminates nearly all debt, to instead file under Chapter 13 and agree to a repayment plan.

The United States remains a job creation engine with a buoyant housing market. Thus far, favorable employment conditions and asset prices have enabled the American consumer to take on more debt and save less. Nevertheless, consumer debt remains a dark cloud on the horizon.

Favorable Credit Developments in Emerging Markets

Bonds issued in emerging markets continued to shine in 2005. The asset class as a whole gained nearly 10% in 2005. The three year trailing return was almost 16%. In light of the low yields in the developed markets such as the United States and Europe, what factors are driving the bullish returns in these smaller economies?

There are strong fundamental reasons why emerging market bonds from places like Brazil and Russia are doing well. These countries have become export powerhouses. Russia has been exporting expensive natural gas to Europe and Brazil is a major agricultural producer. Consequently, their foreign exchange reserves have grown dramatically and, with that, their credit ratings have improved. In fact, there have been three times as many credit upgrades

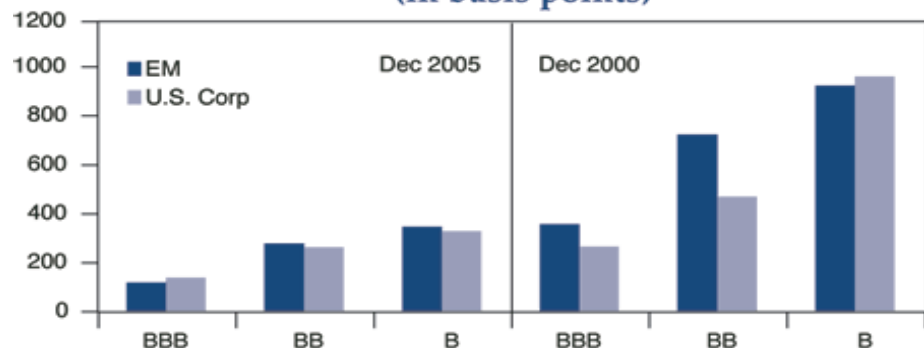
as downgrades among emerging market credits in the past two years. Many emerging markets, flush with foreign reserves, are retiring external debt early.

At another level, the investor community has become less provincial in its outlook. Emerging markets are no longer penalized just for being small. Today, the focus is on the credit rating of an issuer rather than its geographic origin. In December 2000, a BB credit in an emerging market would still have to pay interest that was nearly 2.5% higher than its USA counterpart with the same credit rating. In December 2005, both borrowers would pay about the same amount of interest. Reduced segmentation in the fixed income markets has benefited investors in emerging markets.

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**Yield Premium Over Treasuries
(in basis points)**



Source: JP Morgan, Merrill Lynch