Book Review

Whatever Happened to Thrift?: Why Americans Don't Save and What to Do About It

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Author: **Ronald T. Wilcox**
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Whatever Happened to Thrift?: Why Americans Don't Save and What to Do About It is designed to illuminate the lack of savings by individuals and families in the United States. Identified as a national crisis by the author, he states that "Americans are the world's prodigal sons, spending all their riches today and guaranteeing themselves a place in the poorhouse of tomorrow" (p. 1). He asks readers to consider the following questions: does the United States save too little, why don't we save, how can public policy increase savings, how can employers increase employee savings, and what can households do to save?

Until very recently, research reports and media outlets cited measures of the U.S. savings rate sinking to almost an all-time low, about the same as during the Great Depression. In Chapter 1, "Do Americans Save Too Little?," the author uses research results from economics, finance, marketing, and psychology as a spring board to discuss the problem of household savings; indicating that "this book is an unapologetic attempt to reinvent thrift in the United States, to find practical ways to help people consume less and save more" (p. 2). Rather than smart spending tips, the author suggests looking for meaningful solutions. There is no "one size fits all" solution. Without households choosing to save, businesses will not be able to borrow money to assist in developing the next medical cure, improve technology, or a host of other things.

The author dissects how household savings is measured. It is "simply the difference between what a household earns over a given period of time and what it consumes during that period" (p. 5). Additional measures of savings explained, compared, and contrasted include the U.S. Department of Commerce's National Income and Product Accounts (NIPA) and the Board of Governors of the Federal Reserve's Flow of Funds (FOF).

Chapter 2, "Why Americans Don't Save Enough?," attempts to help the reader understand why Americans save so little. It is divided into specific reasons why the savings record is low in the United States. The first two reasons deal with overconsumption: they are easy access to consumer credit and employees who are overworked by greedy corporations. These two reasons have low merit in the author's eyes and are what he terms shallow "cocktail theories."

Not only 'keeping up with the Joneses,' but surpassing the Joneses is the third reason. Education and income levels seem to be the pervasive thoughts regarding peer-pressure into overconsumption, leading to what the author calls a "consumption superdisparity."

American optimism, reason four for the low U.S. savings rate, has sometimes been our downfall. Feeling and believing we have control over the random events in our lives may only be an illusion. Optimism has provided great things, including the founding of our nation, but it has also led to thoughts of "we do not need to save money today, because tomorrow we will enjoy a great deal of success."

The fifth reason that Americans do not save is that baby boomers will be a very large elderly voting contingent

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who, if they have not saved adequately for retirement, will pressure legislators "to vote for measures that transfer wealth from the people who have saved responsibly to those who have not." Since this is a known possibility, many feel there is no reason to save if what they have saved will be taxed more and more.

The sixth reason for low savings rates in the U.S. stems from a comment made by Ben Bernanke, chairman of the Federal Reserve Board, related to what he called the "glut of savings." This actually relates to other developed countries' governments encouraging savings by their citizens which they then convert into U.S. Treasuries. Doing this keeps U.S. domestic interest rates low, leading to feelings that if I cannot "make" money on the money I would save, I might as well spend it.

Misunderstanding the value of compound interest is the final reason posed by the author for declining American thrift. Not realizing how compound interest works can severely diminish the motivation to save.

Given the variety and complexity of the reasons why American thrift has diminished, the author believes that the solution resides in the psychology of people and their money. This is the focus of Chapter 3, "The Psychology of Money." He begins this chapter with a discussion of financial literacy and decision making related to money. A person's attitudes, knowledge, skills, and behaviors may lead to poor financial decisions. Using statistics and survey results, the big picture is that "a large proportion of the population understands neither the full benefits of savings nor the market and institutional mechanisms for making intelligent choices about how to save." He also points out that none of us have trouble spending money; spending is easy, but saving involves thinking and developing a plan.

There are several additional topics in the third chapter related to the psychology of money including: the nature vs. nurture issue of "propensity to plan," how our mental accounting tricks us in decisions about money, overconfidence in financial knowledge and abilities which can lead to disastrous financial situations, and being fooled by randomness as we have a pattern-seeking, meaning-seeking mentality. Another psychological aspect of money management discussed in Chapter 3 is the tendency to oversimplify complex financial issues into something we feel comfortable with but yet still greatly misunderstand. While people want the freedom to make choices, too much choice often leads to no decision or a bad decision from over diversification. People also have a tendency to anchor decisions on what is familiar or known then to make adjustments and changes; individuals hate to appear stupid, so they will choose a certain/known/less risky alternative over an ambiguous/unknown potentially more profitable option. Knowledge of all these human behaviors related to financial decisions must be used to develop informed, action-oriented policies to encourage a resurgence of thrift in the United States.

In Chapter 4, "Public Policies That Will Increase Savings," the author utilizes research identified in the first three chapters to propose additional public policies to increase the personal savings rate of individuals and families. Currently, there are government actions and incentives to force and encourage families to save, for example, Social Security, tax-deferred retirement accounts, tax breaks for those who save for medical expenses, and tax relief for state-specific plans for saving for higher education. The author indicates while educating families on the importance of saving is necessary, it also is not enough anymore. Additional government action is needed. These actions include:

- Tax Consumption Rather than Income—After a short dialogue about the U.S. tax system, with some comparison to other countries with a consumption tax, the author lays out a model for how a new taxing system would look and how it would operate. He believes "supplanting the current federal income tax system with a broad-based consumption tax is the single most potent policy tool for increasing the savings rate of U.S. households."
- Create a Low-Cost Retirement Savings System for Small Business Employees—This action is proposed as an "automatic IRA." It would entail the federal government contracting with a small group of mutual funds willing to adjust funding stipulations, etc. to accommodate small businesses with small saving employees. The federal government would be the repository for the funds from the small businesses. Once the balance reached a certain amount, each employee could roll the balance from the federally sponsored IRA into a private account.
- Allow Poorer Americans to Divert Some Proportion of their Social Security Contributions to a Government-Managed Stock Mutual Fund—The author "recommend[s] that all Americans in the lowest 25% of adjusted gross income be offered the option of diverting 3% of their Social Security

contributions to a specific indexed stock mutual fund managed by the federal government" (p. 81). There would be restrictions and requirements mandated by statute. The reviewer wonders if the author would feel the same today with the financial fallout of 2008-2009.

- Require Investment Companies (Mutual Funds) to Disclose the Dollar Amount They Charge on an Individual-Level Basis—Make SEC disclosure requirements stricter and be expressed in exact dollars, not approximate percentages.
- Strengthen the Warning Statement about Past Returns in Mutual Fund Disclosures—The "past performance does not guarantee future return" warning on investment prospectuses is ignored just as the Surgeon General's warning about the risks of cigarette smoking is ignored. We figure those warnings are for other people, not us. The author recommends the word "guarantee" be replaced with "predict."
- Reinvigorate the Marketing of U.S. Savings Bonds—The author recommends the federal government rejuvenate the marketing of savings bonds, as they are available in small denominations, have long maturity dates, and are available from most employers. The financial market frequently has such high costs (minimum deposit amounts, fees, etc.) that discourage saving by low- and middle-income families. Thus, there is a need for an alternative.
- Create a Matching Savings Plan for Low-Income Individuals—The Saver's Credit program adopted in 2001 was a program to encourage saving by low-income individuals through incentives—50% rebate on federal taxes. The author recommends utilizing a targeted matching program similar to individual development accounts (IDAs).
- Emphasize Skills Important to Savings in High School Curricula—The author recommends working with school boards to show the importance of having high school students who can make a sensible household budget and use basic mathematical tools to calculate compound interest and time value of money techniques. All three of these skills are pertinent to understanding the benefits of savings and dangers of debt.

Chapter 5, "A CEO's Guide to Increasing Employee Savings," identifies the workplace as the point where many decisions are made that strongly affect the financial future of the employee and their family. Therefore, employers are at the forefront of encouraging and leading an increase in the U.S. savings rate. The author's recommendations for employers are as follows:

- Choose a Pension Plan Provider with Low Fees—Fees vary greatly among mutual funds, and high fees take away from the accumulation of employee's savings.
- Limit the Number of Mutual Funds Contained in the Pension Fund—Too many choices are confusing and often lead to no choice or bad choices by the employee.
- Do Not Take Payments from Financial Service Providers in Exchange for Offering Their Products in Your Tax Deferred Retirement Plan—Taking payments in this manner is a breach of fiduciary responsibility to act in the best interest of employees when designing a retirement plan.
- Set the Default Asset Allocation in Your Tax Deferred Retirement Plan to Something Other than 100% Cash—Dividing allocations into thirds of stocks, bonds, and cash or using life-cycle-type funds would better serve employees.
- Set Defaults on 401(k) Plans so that Employees Are Automatically Enrolled Unless They Explicitly Choose Otherwise—Set up the human resource systems so that employees must make a concerted effort to opt-out of enrollment in 401(k) plans, then follow the mandatory contribution guidelines.
- Targeted Financial Education—Focus financial education on women with below-median incomes as they are more receptive than men to accepting advice given in financial education programming according to several empirical studies that were referenced within the chapter. Also, provide financial education and resources to the opinion leaders in the company, the individuals whom others look up to for advice.
- Give Detailed, Personalized Financial Advice—Employers should utilize the ability to contract financial counselors through a registered entity through the Pension Protection Act.
- Implement Forward Contracts for Savings—Implement an automatic escalation plan that allows employees to commit to increasing their contribution to their retirement plan at the time

of their next raise. In this case, employees do not have to take an immediate cut in take-home pay, but agree to accept a smaller increase in take-home pay in the future.

- Limit Your Own Conspicuous Consumption—Employers are a reference group for many of their employees. Workers aspire to be like their employers, so if as an employer you may be living beyond your means, you employees will attempt to do so too.

"A Household Guide to Saving," the final chapter of the book, focuses on the personal saving habits of individuals and families including right and wrong habits. Taking a hard look at personal saving habits may facilitate improvements in savings rates. Suggestions include:

- Make Sure that Mental Accounting is Working for You and Not Against You—Be sure decisions to save make sense. An example used by the author is that "for most of us, to save means taking an amount of money and placing it in one or more accounts that we have mentally designated as our "savings account(s)." This narrow mental definition of savings can cause counterproductive behavior" (p. 126).
- You Really Are Not as Smart as You Think—Individuals need to heed the warning signs of overconfidence in their own capabilities because it is costing them money.
- Too Much of Your Savings May Be Getting Eaten Up by Fees and Taxes—It is a good use of your time to scrutinize fees paid and taxes withheld from investments, as both diminish the final savings outcome.
- Raise Your Anchor—We tend to rely on the familiar and the things known to us. Make efforts to learn more about all aspects of your financial life; knowledge and skills lead to improved decisions.
- Teach Your Children Well—Teach children to delay gratification and save for the future. Provide youth with learning opportunities related to financial choices through a fixed allowance. Utilize tools, such as interest, to guide your children into a financially successful life.

Summary

The savings problems we are experiencing in the United States are partially due to psychology that is a part of our human nature. There may be others to blame, such as a culture with wide disparities of income/wealth, media with constant images of consumption, and a market for financial products and services that is complex and confusing. One solution will not solve the problem; it will take a whole series of solutions to improve American savings rates.

Recommendations

Financial professionals (counselors, planners, researchers, and educators) will find the thoughts and suggestions put forth in this book to be intriguing and thought-provoking. It brings together economics, financial management, psychology, and additional disciplines to develop solutions to the savings problem in the United States. The book contains multiple suggestions that can be utilized and directly applied in financial counseling, planning, and education. While the national savings rate may be low, the current economic recession has led to an increasing personal savings rate, as reflected by data from the U.S. Bureau of Economic Analysis (BEA). The BEA has reported an increase in personal savings rates (as a percent of personal disposable income) from 1.2% in the first quarter of 2008 up to slightly over 5% in the second quarter of 2009. Would recent increases in U.S. savings rates change the suggestions and direction of the author? I do not think so. The potential solutions will only strengthen and further improve the savings levels of Americans.

With its discussion and review of research, *Whatever Happened to Thrift?: Why Americans Don't Save and What to Do About It* would be a good guided-discussion book for a graduate-level college course. It can also provide educators, practitioners, and counselors with background needed to help individuals and families increase their savings. In addition, the book provides guidance for working with policy makers to develop savings-friendly policies and with employers to create a work environment and atmosphere that fosters employee savings.

I found the author's writing style and dry wit to be interesting and intriguing. It is a book that will make you think and rethink. He has written this book to discuss a crisis we know to exist and to provide solutions we can implement and put into practice.

Reference

Bureau of Economic Accounts. (2009). *Personal savings rates*. Retrieved on August 4, 2009, from http://www.bea.gov/briefrm/saving.htm