MIGHT LOWER INCOME CONSUMERS BENEFIT MORE FROM THE ECONOMIC RECOVERY?

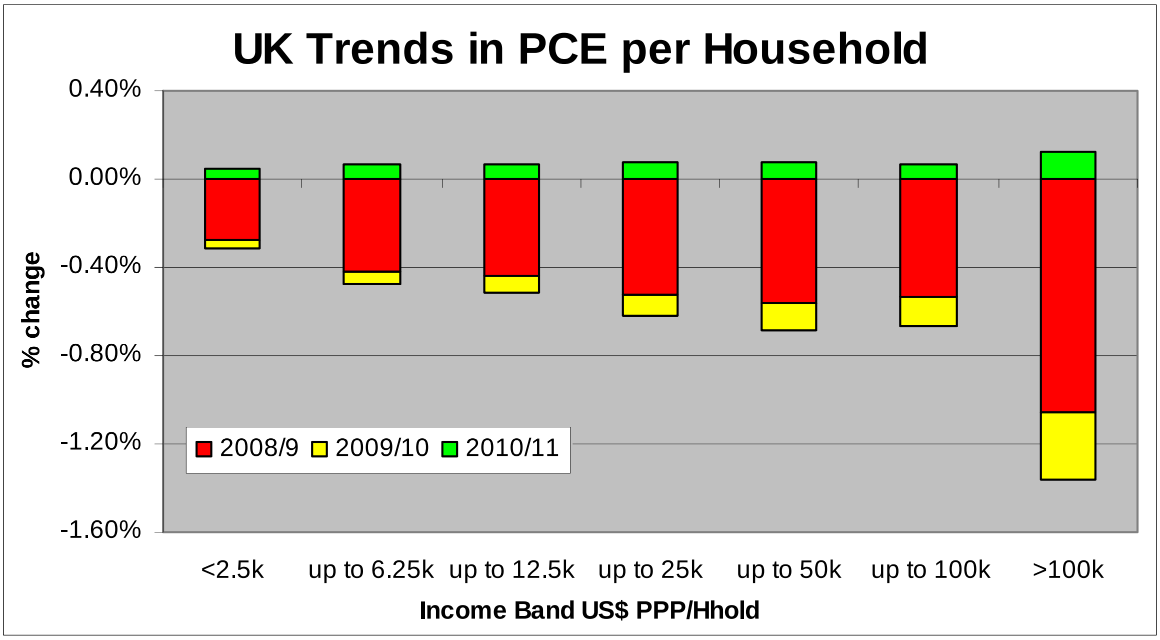
A recent article in the Daily Telegraph ("Disposable income set to decrease") has prompted us to look again at the possible implications by income group in the UK, rather than at an aggregate level. In particular to look at how the recent recession and financial crisis in the UK has affected consumption growth of different households, ranked by their income group. We wanted to find out whether there had been any noticeable impact on income distribution, and to see whether different income groups had been affected by the downturn and recovery unevenly, or whether all the income groups had experienced roughly similar effects.

Here is the story so far!

Nationally, in 2009, consumer expenditures were reduced by just over 6% in constant terms, a very large year on year drop!

The Rich get squeezed in a Recession!

There were 15% fewer households in the top income groups, but around 45% more living on subsistence. Average expenditure fell across every income group – but unevenly.



In 2008/9, losses ranged from just over 1% for the top income group, to a much smaller 0.2% for those on the lowest incomes. For the bulk of households, losses in the region of 0.5% were experienced.

The losses worsened for all income groups in 2009/10, with continued inequality. By the end of this year, we expect the upper income groups to have lost a total of (-1.4%) to the lower income group's (-0.4%0. **In total, by the end 2010, we expect consumer spending to have fallen by a cumulative 7.5%**

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But, a word of caution!

- 20% of the population in lower income groups, accounting for 5% of PCE, will only see a drop of 0.4% over 2008/10.
- 12% of the population, accounting for 30% of spend, will see a drop of over 1% in the same period.
- adjusting for fixed costs such as rents, fuel, etc., is likely to have a disproportionate effect at lower income levels.

For 2010/11, using third party forecasts, our model suggests a very modest recovery, with a slightly better performance for the upper income groups. **By the end of this year we expect consumer spending nationally to have fallen cumulatively by 6.7%** compared with the level attained in 2008.

When we look forward another 2 years, it is noticeable that the strength of the recovery is weaker than the strength of the downturn and consumption is projected to recover more quickly for those with expenditures more than $100k, - and, surprisingly, for those households with incomes between $25k and $50k per annum : the rich really do get richer, but over the past few years they will have got poorer, faster!

Nationally consumption is expected to decline by around 7.5% by the end of 2010. After this, a recovery sets in. But even by the end of 2013, we are still expecting consumption to be 3.5% below where it was in 2008. For a country where PCE is normally expected to rise year by year, this will be a shock.

While expenditures in the upper income groups recover more quickly, by the end of 2013, the rich are still proportionately worse off than they were in 2008. Some may say this is approximate social justice for the high earning and spending bankers. However, this is less good news for the sellers of high value added consumer goods.

And what of the impact of the 'austerity', which is expected to follow the UK government's publicized government budget spending cuts.

Our suggestion is that high earners are going to be hit more badly by the downturn and the subsequent austerity, and so is their spending. Although their consumption spending recovers faster, it has much more ground to make up. Is this a more socialist outcome than the voters thought possible when they cast their votes in May 2010? If it is an outcome the government is seeking, it may suggest a "soak the rich" approach masquerading as "fairness", which we think is a rather unexpected outcome. At the very least, it suggests that the underlying situation is rather different from the way it is sometimes presented in the press.

Analysis of this type can be done in more detail using TLE Business Monitor type models, which in addition to looking at income dispersion and demographics, takes explicit account of the sources of income by income group, and differences in expenditure patterns and weight of spending on necessities. The models are flexible and can be adapted to fit the needs of specific clients with different industry backgrounds.

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