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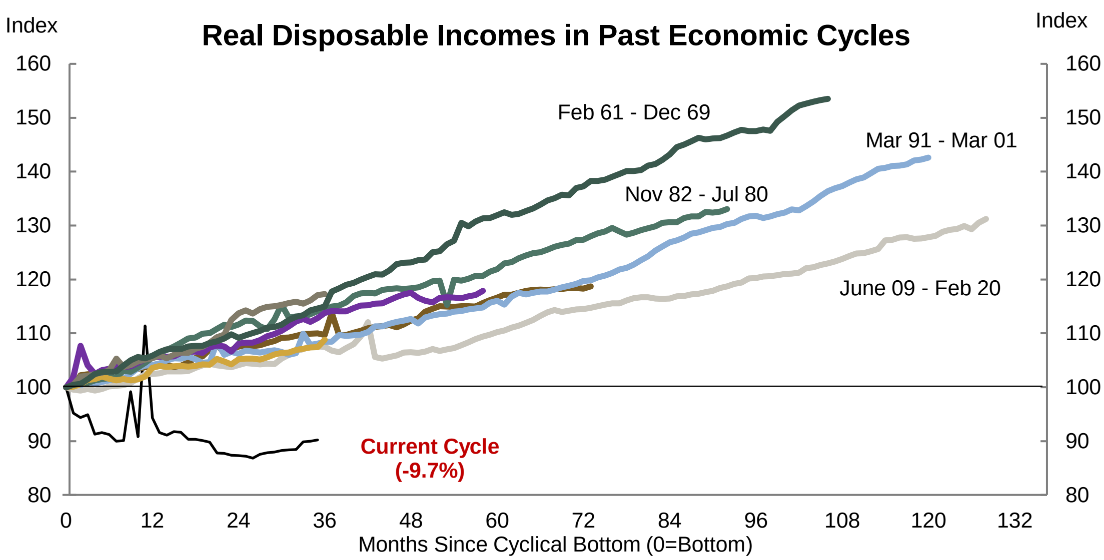
A One-Two Consumption Knockout

Real disposable personal incomes (inflation-adjusted, post-tax incomes) have fallen a record large 9.7% since the economy exited the pandemic recession (see chart below). This means US households are now *poorer* than they were at the end of pandemic recession. You read that correctly. Fiscal- and monetary-stimulus failed to instigate any pickup in productivity. As a result, an inflation problem was sparked. So much so that price growth has been, and is, exceeding income growth. Therefore, people have become poorer, and their purchasing powers have declined. Consequently, consumption is going to have to downshift from this dynamic alone, and possibly considerably so.

Even after this, there are two additional spending depressants coming down the pike. **First, there is essentially only one way for the 3.7% unemployment rate to go from here (up)**, especially considering that the Fed is attempting to *engineer* such an outcome. The FOMC sees the unemployment rate at 4.1% by yearend 2023 and 4.5% for end of 2024. Whether we see such a mild labor market downturn or something more substantial (our view), this will impinge on income growth. In fact, we estimate that every 1 percentage point increase in the unemployment rate shrinks nominal income by nearly 2%. **Second, student loan payments will be resuming in October.** This effectively is a massive tax hike estimated at approximately 1% of GDP per year. Considering that the population with student loans tends to have high marginal propensities to consume, the hit to spending could be considerable. Remember that small moves in the broader macroeconomy can lead to substantial moves for individual businesses because of their varying degrees of financial and operating leverage.

Considering that the biggest price runups have occurred in nondiscretionary items like food and housing, suggests there is a high probability that discretionary spending could fall *below* trend. **Do not forget too, that recommencing student loans means that other forms of debt (e.g.: autos, housing, credit cards) are also more likely to run delinquent. The great consumer squeeze is about to begin.**



Sources: BEA, Haver, SMBC Nikko

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