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
Disclaimers

This document is provided by SMBC Nikko Securities America, Inc. ("SMBC Nikko"), the US-registered broker-dealer affiliate of Sumitomo Mitsui Banking Corporation, for informational purposes only. This document was prepared by SMBC Nikko's economist(s). The views statements, assumptions and forecasts expressed herein are those of the author(s) and do not reflect the judgment of any other person or of SMBC Nikko, it does not constitute an offer, or solicitation of the sale or purchase, of securities or other investments. The information contained herein is obtained or derived from sources believed to be reliable, but SMBC Nikko and the author(s) make no representations as to its accuracy or completeness. In some cases, such information may be incomplete or summarized. This document has been prepared based on assumptions and parameters determined by the economist(s) in good faith. The assumptions and parameters used are not the only ones that could have been selected, and therefore no guarantee is given as to the accuracy, completeness, or reasonableness of any such quotations, disclosures, or analyses. Past performance is not a reliable indicator of any future results.

This document has been prepared for and is directed at institutional investors and other market professionals and is not intended for use by retail customers. It does not take into account any specific investment objective, financial situation, or particular need of any recipient. The information contained herein should, for whatever purpose, be used solely at the discretion and responsibility of the recipient. SMBC Nikko and its affiliates do not accept any liability or responsibility for any results in connection with the use of such information. Recipients are responsible for making final investment decisions and should do so at their own discretion after conducting a careful examination of all documentation delivered prior to execution, explanatory documents pertaining to listed securities, prospectuses, and other relevant documents, and their own independent analysis and assessment of the merits of any transaction. The financial instruments discussed may be speculative and may involve risks to principal and interest.

Conflicts of Interest Disclosures

The views statements, assumptions and forecasts expressed herein may differ from those expressed in globally branded research produced by SMBC Nikko or its affiliates. The trading desks of SMBC Nikko and its affiliates trade or may trade as principal in the financial instruments that are the subject of this material, and the author(s) of this document may have consulted with the trading desks while preparing this document. The proprietary interests of SMBC Nikko and its affiliates may conflict with those of the recipient. SMBC Nikko and its affiliates may seek to do business with the companies mentioned in this material and the trading desks may have accumulated, be in the process of accumulating, or accumulate long or short positions in the financial instruments mentioned and may have acquired them at prices no longer available. The trading desks may also have or take positions inconsistent with the views expressed in this document or may have already traded on those views.

This material is not a research report, and neither this material nor its author(s) is subject to SMBC Nikko policies and procedures that apply to the globally branded research reports and research analysts of SMBC Nikko and its affiliates or to legal requirements designed to promote the independence of investment research. It is not subject to any prohibition on dealing ahead of the dissemination of investment research. This means that on the date of this document, SMBC Nikko, its affiliates, and their respective directors, representatives, or employees, may have a long or short position in any of the instruments mentioned in this document and may make a market or trade in instruments economically related to the securities, derivatives or other underlying assets mentioned herein, in each case either as principal or as agent.

No part of the author(s) compensation was, is, or will be, directly or indirectly related to the specific recommendations or views expressed herein. The personal views of authors may differ from one another.

Distribution, possession or delivery of this document in, to or from certain jurisdictions may be restricted or prohibited by law. Recipients of this document are required to inform themselves of and comply with all such restrictions or prohibitions.