

# Perspectives

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## The State of the American Consumer

The U.S. economy has long been driven by consumers, with consumption constituting more than two-thirds of GDP growth: As the consumer went, so went the economy. More recently, robust consumer spending has fueled positive domestic GDP growth and helped buoy the prices of financial assets. That said, there are now signs that these trends may be shifting. For instance, delinquency rates across various consumer loan types have ticked up, as have debt burdens as a share of overall household income. Additionally, personal savings rates in the U.S. have now dropped below long-term averages. From a big picture perspective, what do these trends mean for the overall health and growth of the economy?

### LONG-TERM TAILWINDS

A resilient American consumer, whose spending accounts for roughly two-thirds of U.S. GDP, has supported both the domestic economy and equity markets in the years following the pandemic. Indeed, the recent environment has been conducive to consumer strength, as massive government stimulus including lost wage assistance, child tax credit expansions, and direct checks added around \$1.8 trillion to the coffers of individuals and families. The low interest rate regime prior to 2022 also served as a tailwind for the financial health of many households, as debt burdens as a share of total income dropped to multi-decade lows. The result of these dynamics was a high level of consumer spending across durable goods (+28.6% since the pandemic started), non-durable goods (+13.6% since the pandemic started), and services (+7.4% since the pandemic started). The complete pattern of spending across this spectrum can be observed in Exhibit 1 on the following page.

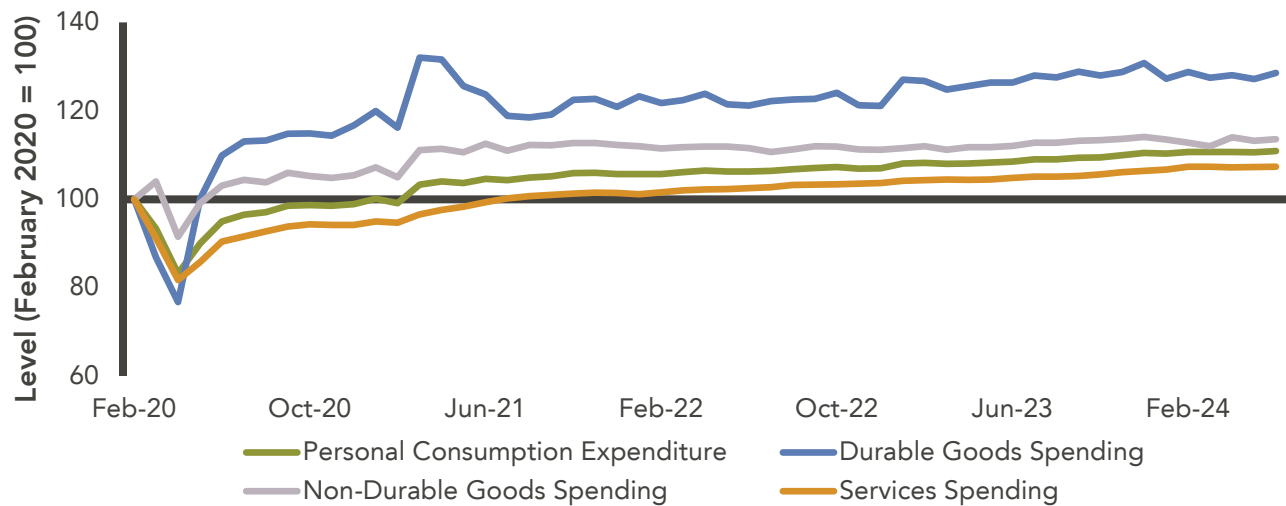


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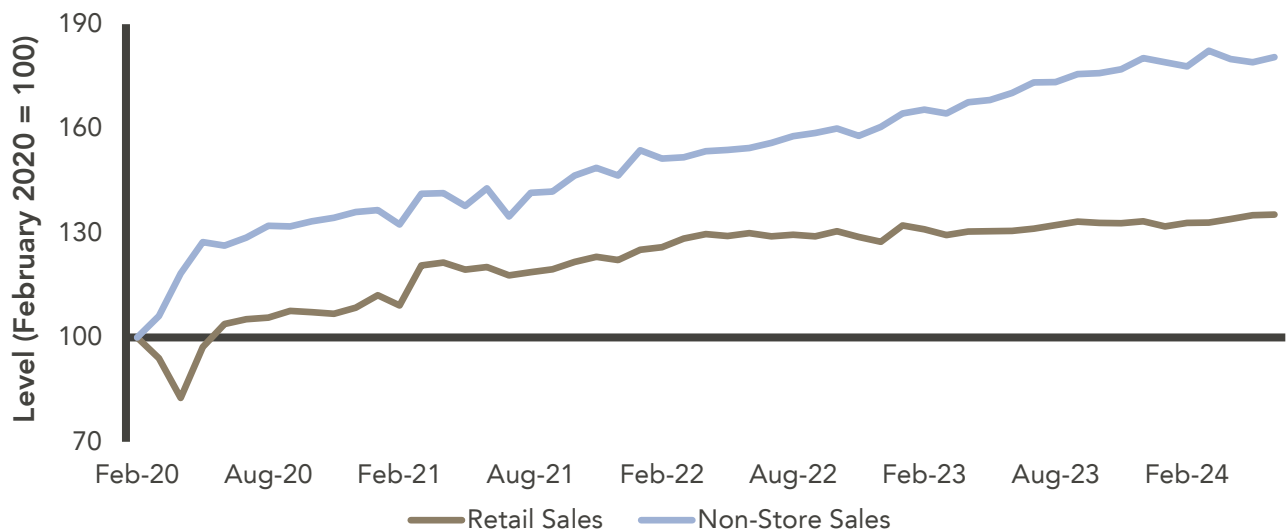
Exhibit 1: Goods and services spending increased in the wake of COVID-19



Source: Deloitte, Federal Reserve Bank of St. Louis, U.S. Department of Commerce, U.S. Bureau of Labor Statistics, The Wall Street Journal as of June 30, 2024

Before outlining the drivers of these elevated spending levels, it is important to highlight the rise of e-commerce activity relative to overall consumer spending. During the pandemic, many companies turned to online sales channels for survival. Consumers quickly followed suit, as more than two-thirds of Americans pivoted towards online shopping. These shifts have largely persisted to date. As can be seen in Exhibit 2, e-commerce activity has surged since February 2020, while consumer spending at brick-and-mortar retail locations has also climbed higher during that time.

Exhibit 2: E-commerce spending activity has been robust following the onset of the pandemic

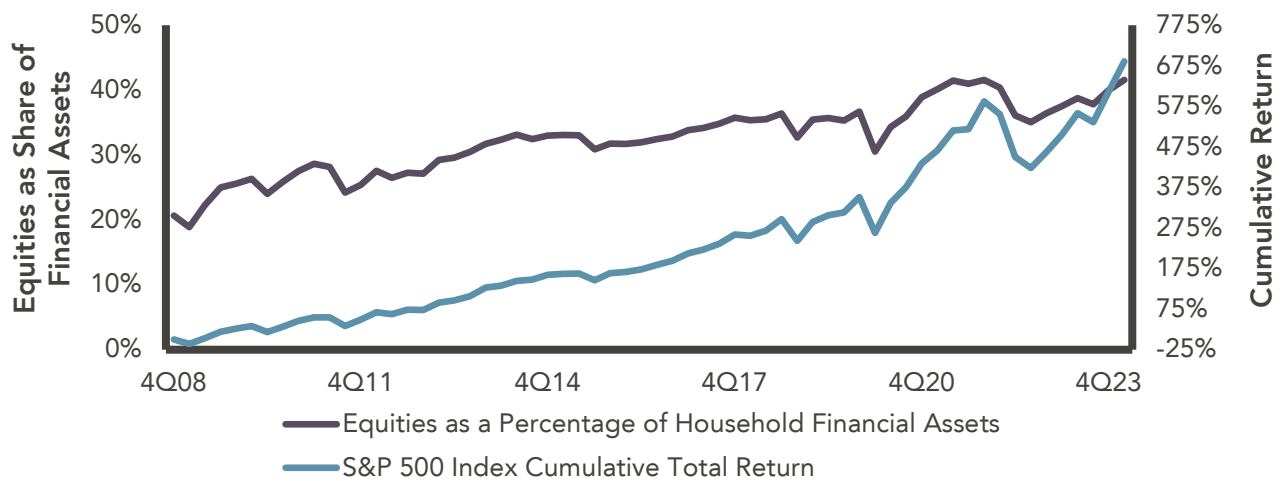


Source: Deloitte, Federal Reserve Bank of St. Louis, U.S. Department of Commerce, U.S. Bureau of Labor Statistics, The Wall Street Journal as of June 30, 2024

What has allowed consumers to spend at these clips? The ease of online shopping is clearly a contributing factor, as is wage growth, which has trended above long-term averages since 2020. As it relates to purchasing power, Americans have also benefitted from robust market performance. Over the last decade, public equities have increased both in value and as a percentage of overall household financial assets. These dynamics in tandem with appreciating home prices have driven the wealth effect, which indicates

that individuals spend more as the value of their assets increase. Even those consumers with static incomes and higher costs of living have felt richer as a result of stock market gains.

▣ **Exhibit 3:** Higher rates of stock ownership have helped drive wealth and spending higher

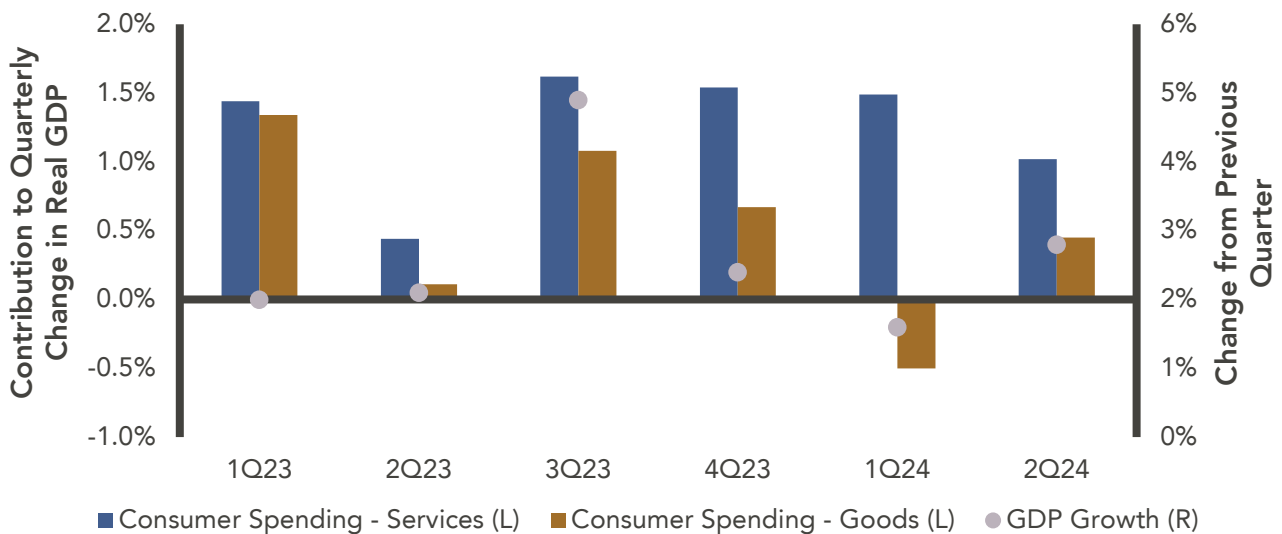


Source: Bloomberg, Federal Reserve Bank of St. Louis as of March 31, 2024

## EMERGING HEADWINDS

While the previous section speaks to long-term consumer strength, consumption appears to be slowing. To that point, growth in spending, particularly across durable and non-durable goods, has largely faded over the last year. Spending on services has been more consistent, but bears watching to see if last quarter's drop is the start of a longer-term trend.

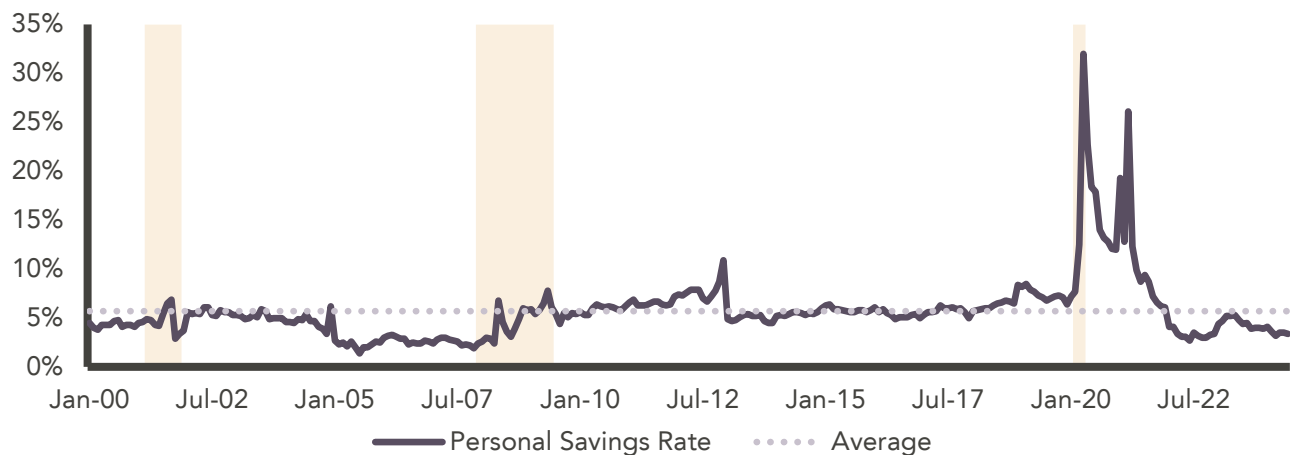
▣ **Exhibit 4:** The last two quarters have seen lower contributions from goods spending to overall GDP growth



Source: U.S. Department of Commerce, The Wall Street Journal as of June 30, 2024

What could be driving this drop in spending? One possible explanation is that Americans have less disposable cash now than four years ago. During the pandemic, the U.S. personal savings rate exceeded 30% thanks to stimulus programs and stay-at-home orders. Since early 2021, however, that rate has dropped as consumers spent those excess savings which undoubtedly has supported GDP growth. The most recent savings rate for U.S. households was roughly 3.4%, which sits meaningfully below the 5.7% long-term average.

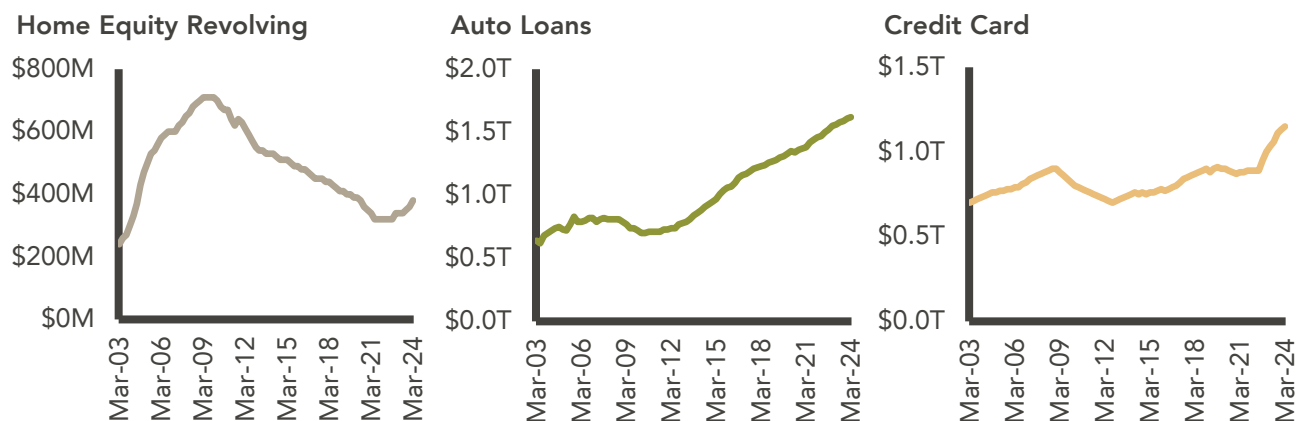
Exhibit 5: The personal savings rate in the U.S. has fallen below long-term average levels



Source: Federal Reserve Bank of St. Louis as of June 30, 2024. Shaded regions indicate periods of recession.

A lower personal savings rate is not the only portent of a weakening consumer. According to Bloomberg, since 2020 Americans have added roughly \$3.4 trillion in new debt across loan types including home equity, auto, and credit cards. Current credit card balances are up roughly 25% from the first quarter of 2020, a high not seen in over four decades. Overall household debt in the United States now stands at nearly \$18 trillion.

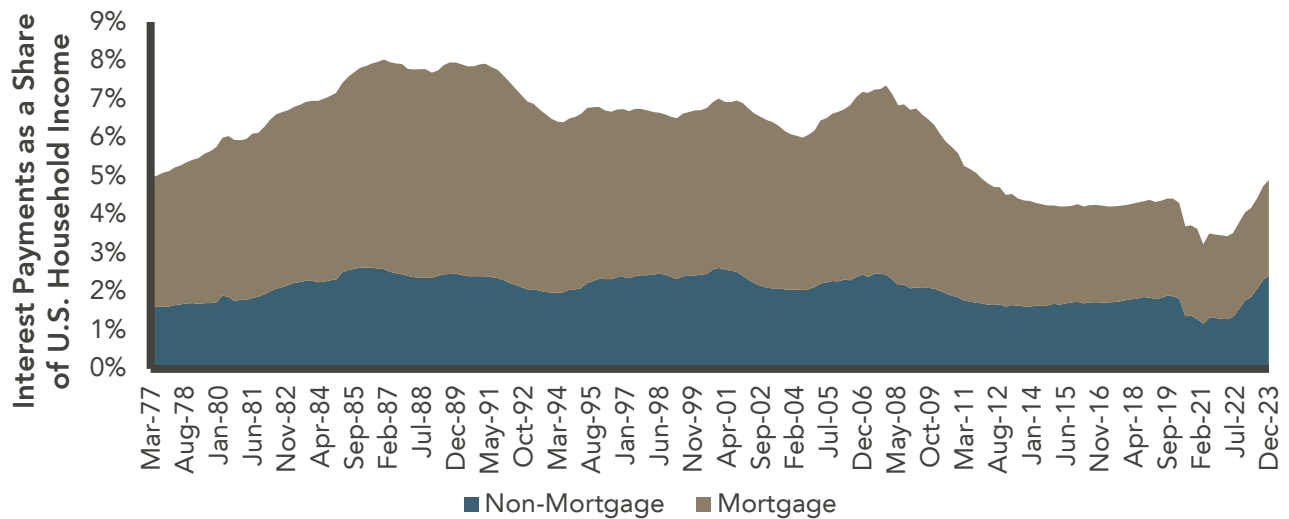
Exhibit 6: Consumers have added roughly \$3.4 trillion in debt since the pandemic



Source: Bloomberg, Equifax, Federal Reserve Bank of New York Consumer Credit Panel as of March 31, 2024

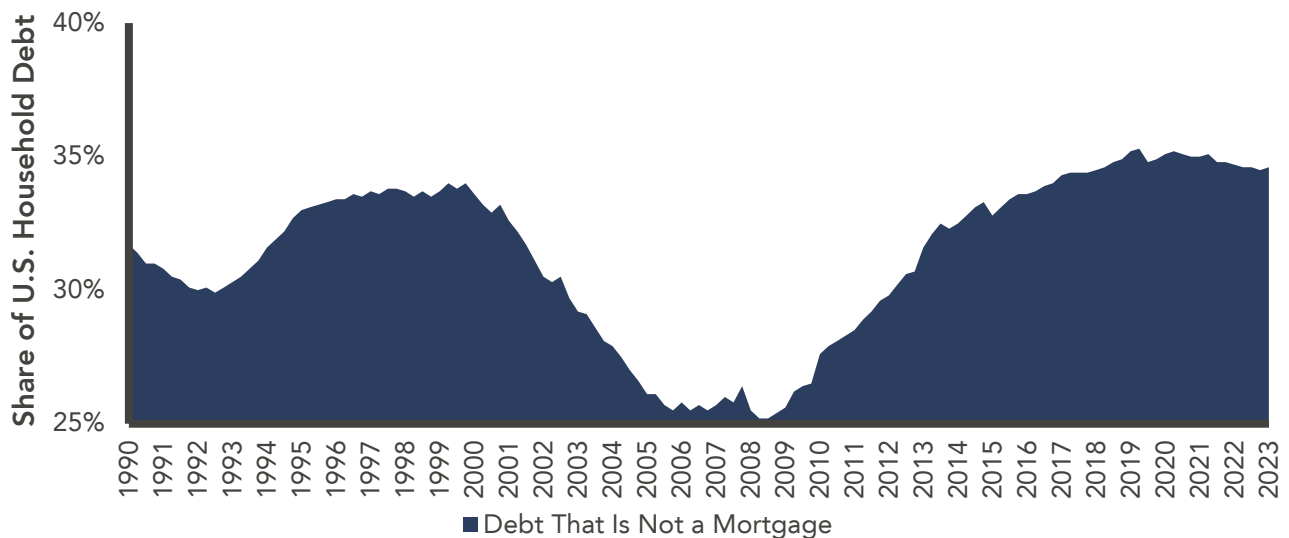
This increase in liabilities has led to higher debt burdens as a share of total household income. To that point, mortgage interest payments represented roughly 2.5% of household income in the U.S. at year-end, which is 50 basis points higher than the figure from early 2021. Perhaps more striking, however, has been the change in interest payments related to non-mortgage debt as a share of total income over that same period. Non-mortgage interest payments represented less than 1.2% of total income in early 2021, compared to more than 2.4% at 2023 year-end. The magnitude of this change is understandable given the higher and more variable rates associated with non-mortgage debt. Readers may also be interested to know that as of year-end, non-mortgage debt as a share of total household debt sat at a near multi-decade high. Currently, over one-third of household debt in the U.S. is not from a mortgage, up from roughly one-fourth in the years following the Global Financial Crisis. The fact that non-mortgage debt often carries higher and more variable interest rates could further slow consumption patterns, particularly since it is a growing piece of overall debt profiles.

- **Exhibit 7:** While still below levels from prior decades, the share of household income consumed by debt payments has increased in recent time



Source: Bloomberg, Bureau of Economic Analysis as of December 31, 2023

- **Exhibit 8:** Non-mortgage debt represents a large share of U.S. household liabilities, and these liabilities often bear higher rates

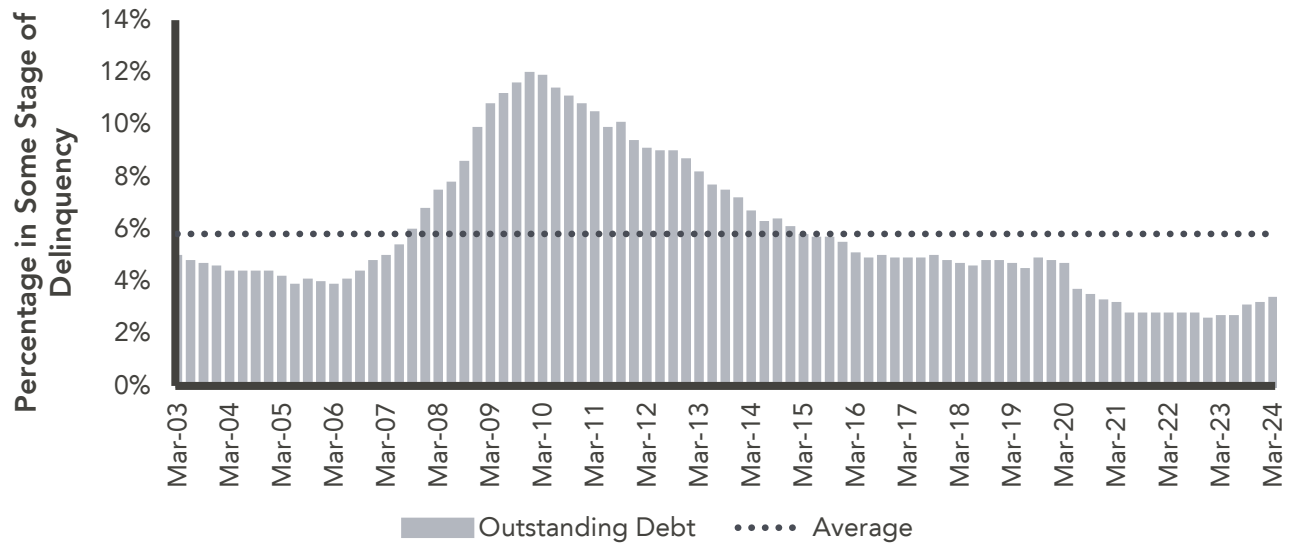


Source: Bloomberg, Federal Reserve Bank of New York as of December 31, 2023

Growing delinquency rates are another concerning trend. At the end of the first quarter, nearly 9%<sup>1</sup> of credit card loans transitioned into 30+ days delinquency, more than double the figure from two years ago. A similar trend exists for the auto loan space, where around 8% of debts are now transitioning to delinquent (up from a pandemic-era low of less than 5%). According to Bloomberg, nearly 3% of all auto loans are now 90+ days delinquent, which equates to roughly three million vehicles. It is not a stretch to argue that growing delinquency rates are a product of higher interest rates as well as higher overall debt levels. As debt levels rise and interest costs soar, consumers face increasingly more difficult decisions in terms of deciding which loans — and how much — to repay while also balancing rising costs of necessities like food and shelter.

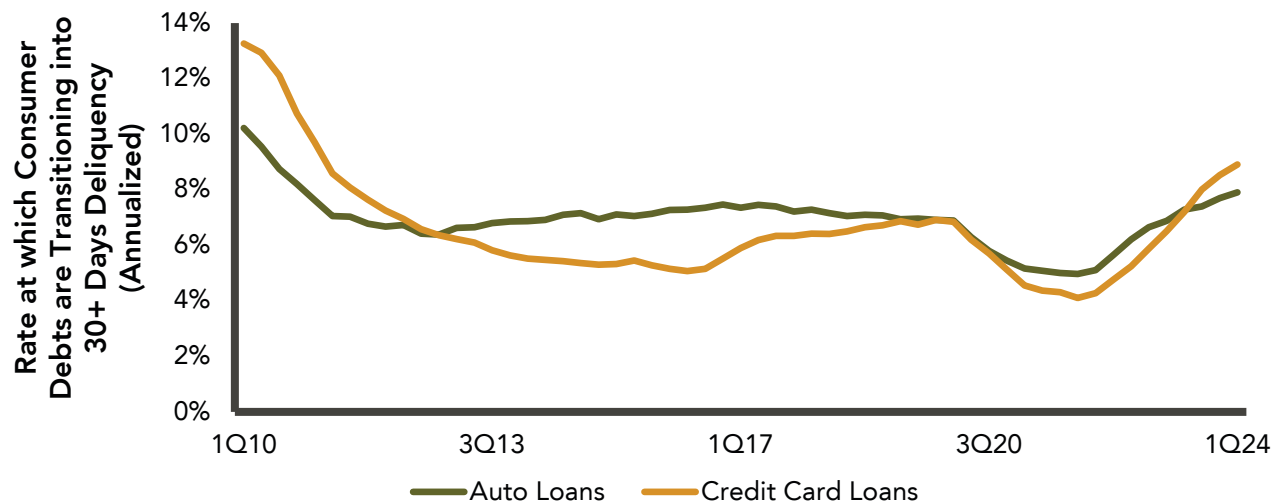
<sup>1</sup> On an annualized basis

Exhibit 9: Aggregate debt delinquency rates have ticked up in recent months



Source: Bloomberg, Equifax, Federal Reserve Bank of New York Consumer Credit Panel as of March 31, 2024

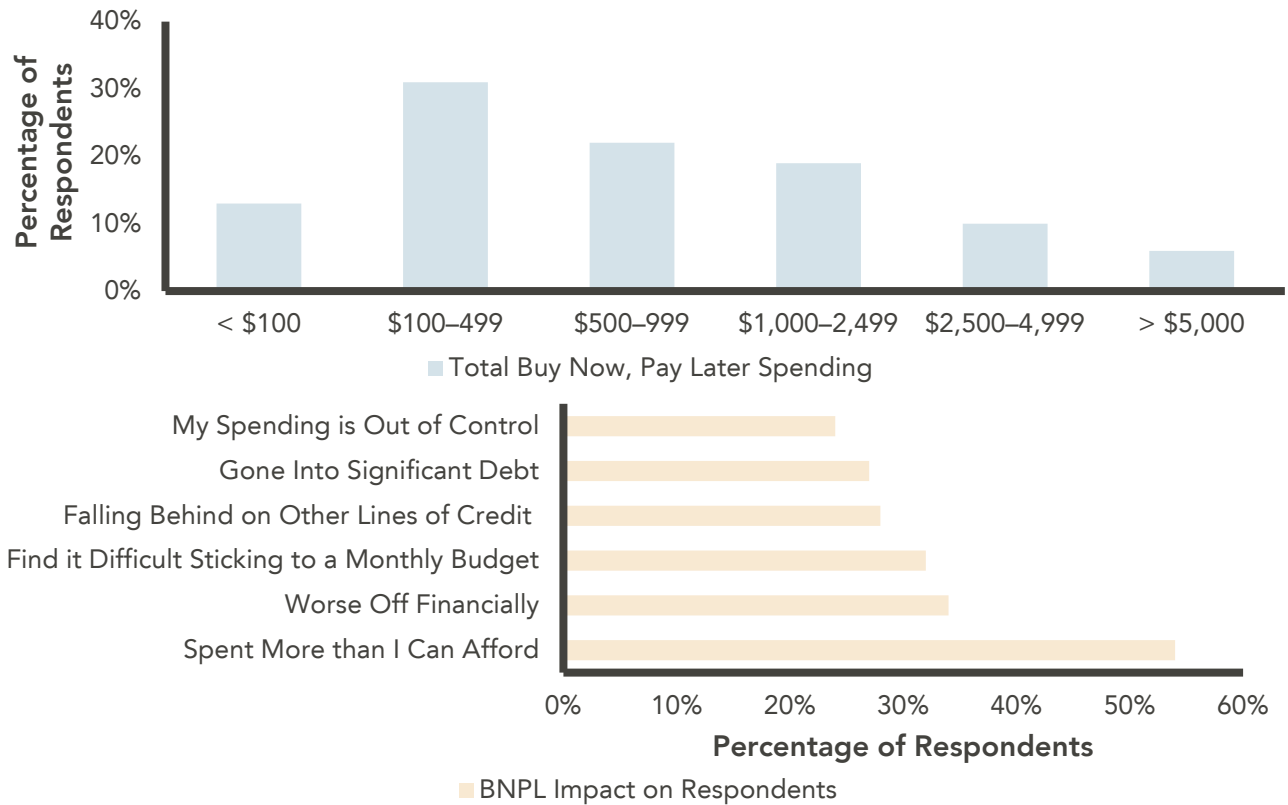
Exhibit 10: Credit card and auto loans are moving into delinquent status at the fastest pace in several years



Source: Federal Reserve Bank of New York, The Wall Street Journal as of March 31, 2024

The proliferation of buy now, pay later ("BNPL") programs is also noteworthy. These programs, which allow individuals to divide payments into installments, have seen a significant increase in popularity in recent years. According to Bloomberg, by 2028 the total BNPL market is expected to approach \$700 billion. Interest rates for BNPL loans vary depending on the provider and the length of the plan. For instance, many traditional plans offer 0% interest rates if payments are made on time, however, longer-term plans can carry rates as high as 35%. A recent survey conducted by Harris found that more than a third of respondents had spent over \$1,000 via BNPL programs. The survey also found that more than 40% of consumers who owe money to BNPL services were behind on payments, while nearly 30% were delinquent on other debt because of spending on these platforms. At this point, the concern is not necessarily the dollar amounts financed via BNPL programs, but moreso how this pattern aligns with the other mounting sources of consumer debt and the ultimate toll this will exact on GDP growth.

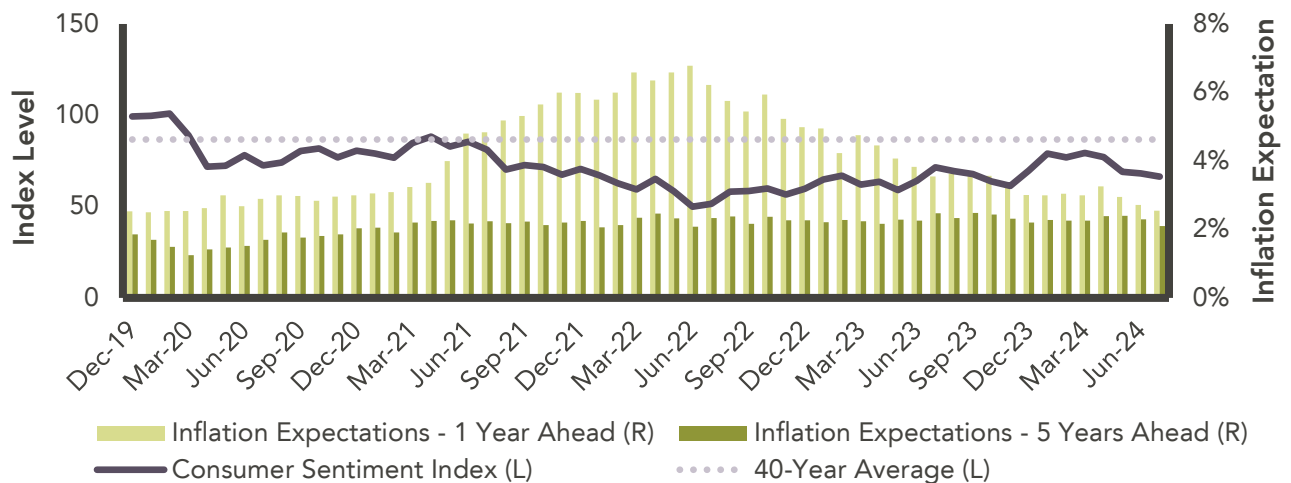
Exhibit 11: A recent nationally representative survey related to BNPL usage paints a concerning picture



Source: Bloomberg, Harris nationally representative survey of 2,066 U.S. adults conducted April 19–21, 2024

In light of these growing debt levels, how are consumers actually feeling about the current environment and their prospects going forward? Interestingly, the University of Michigan Consumer Sentiment Index has actually increased over the last two years. Albeit, this was off a low base as the index sat below its long-term average for nearly three years. The most recent reading just dropped to an intra-year low, however, so similar to the recent dip in consumer spending this index bears watching in future months. A rebound would suggest a positive outlook on behalf of consumers which should bode well for future economic growth.

Exhibit 12: Consumer sentiment has edged up over the last two years but remains below average

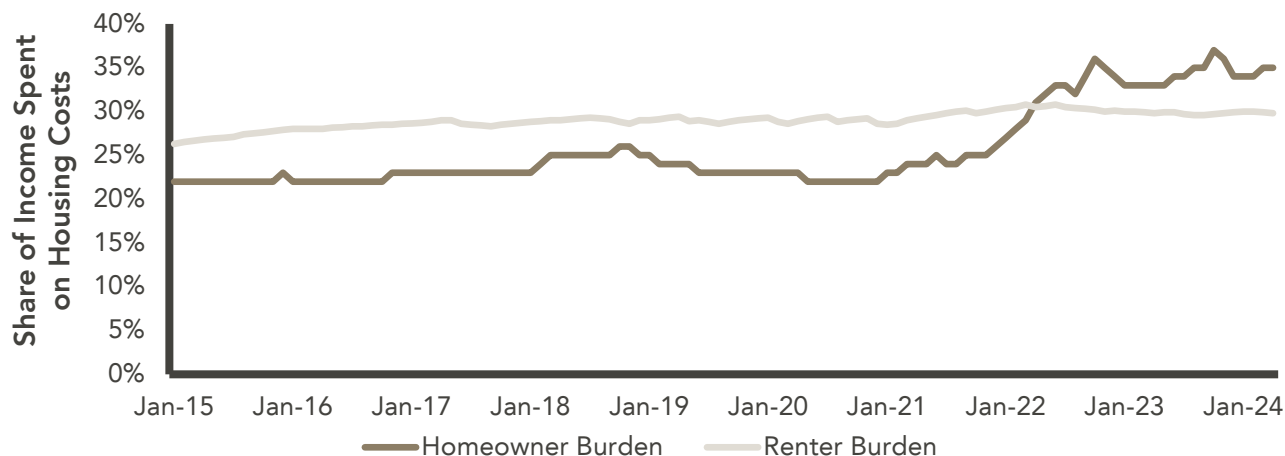


Source: Bloomberg, University of Michigan as of June 30, 2024

## HOUSING MARKET IMPACTS

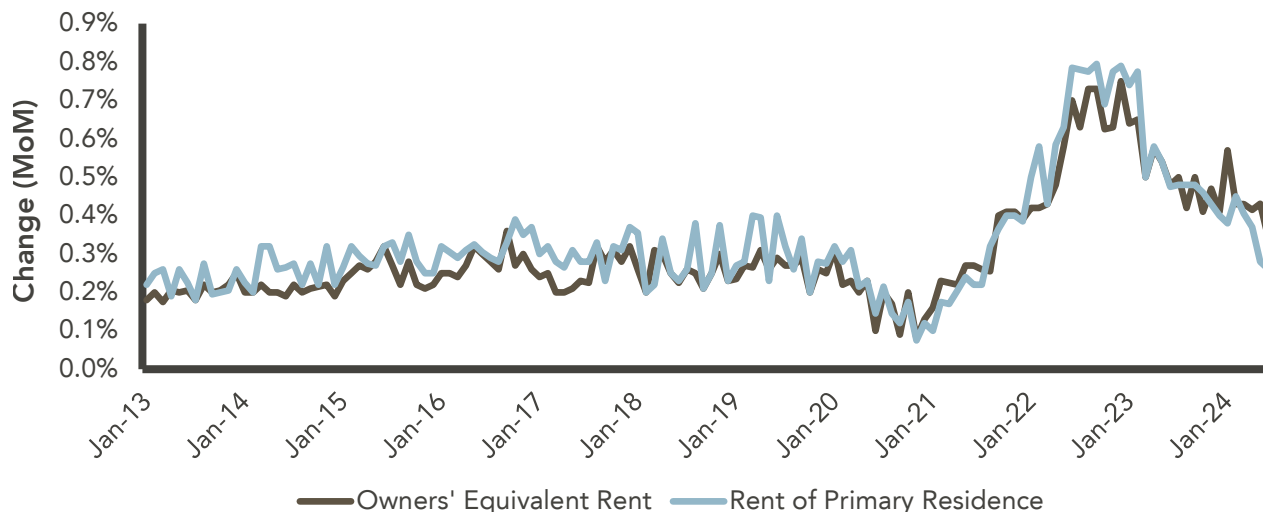
Finally, the current housing market deserves mention for its potential impact on consumption patterns. In short, the cost of a new mortgage is materially higher than two years ago as the run-up in rates naturally increased monthly payment amounts. Furthermore, housing prices have risen amidst a low supply environment. Unsurprisingly, housing-related expenses now represent a notably higher share of total income for homeowners. Rents have risen in a similar fashion, though have started to cool more recently. Nonetheless, according to a Harvard University study, a record-high 22 million renter households now spend more than 30% of their income on rent and utilities. This figure represents an increase of roughly two million households over the last few years and according to the study, offsets any improvements in cost-burden rates that were recorded in the five years prior to the COVID-19 outbreak. Collectively, the higher cost of owning or renting a primary residence leaves consumers with less disposable income for other goods and services. When combined with higher debt costs, the concerns around future consumption patterns are understandable for the majority of Americans.

Exhibit 13: Housing expenses as a share of income for both owners and renters have risen since 2015



Source: Bloomberg, Zillow as of April 30, 2024. Homeowner burden is the share of income spent on housing costs including mortgage, property taxes, and homeowners' insurance for the typical U.S. home. Rent burden is the share of income spent on market rate asking rents of typical unit.

Exhibit 14: Rent prices appear to be normalizing but remain an obstacle for consumers

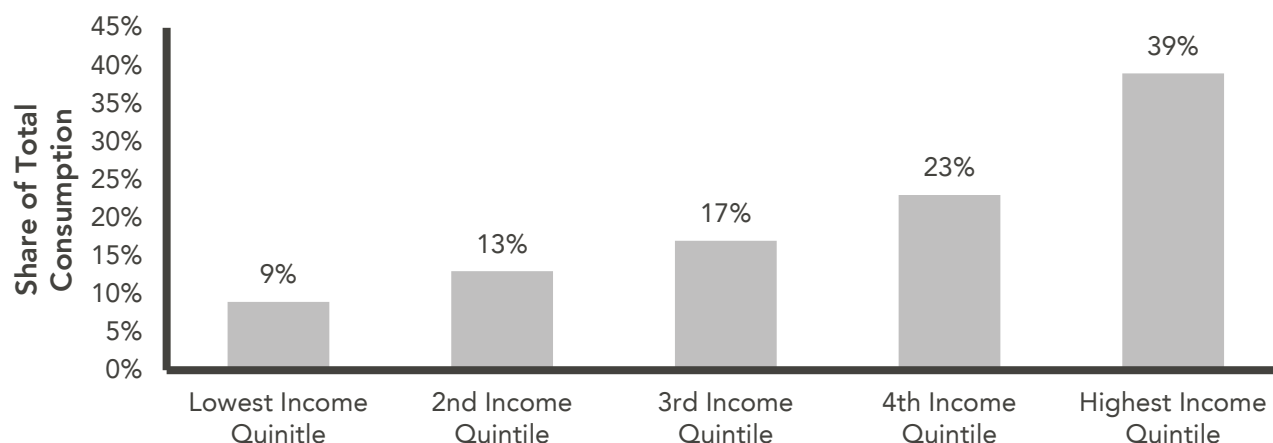


Source: Bloomberg, U.S. Bureau of Labor Statistics as of June 30, 2024

## CONSUMER BIFURCATION

American consumers are a diverse group and certain subsets of the population appear to be taking on water faster than others. First, however, it is helpful to illustrate how overall spending is driven by different income categories. To that point, the top 20% of income earners constitute the bulk of consumption, accounting for nearly 40% of overall consumer spending in the U.S. The second-highest quintile accounts for nearly 25% of spending, while those in the lowest quintile account for less than 10%.

📌 **Exhibit 15:** High earners account for nearly 40% of consumption in the U.S. and are less likely to have their spending limited by economic fluctuations

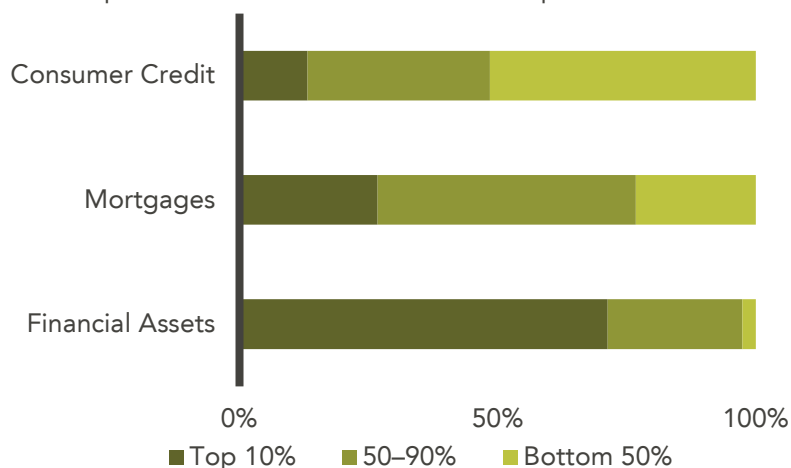


Source: Plante Moran, U.S. Bureau of Labor Statistics as of June 30, 2024

As it relates to the distribution of assets and liabilities across consumers, the wealthiest U.S. households own the vast majority of financial assets (i.e., equities), which provide another source of disposable income as well as wealth accumulation. As such, this supports the demographic's consumption patterns even in weaker economic cycles. Conversely, the bottom half of earners hold just 13% of all financial assets while at the same time being responsible for a disproportionate amount of higher interest rate consumer debt. This group has also seen its share of total debt increase since the pandemic.

These dynamics are cause for both optimism and pessimism. On one hand, since the bulk of overall consumption in the U.S. is driven by wealthy Americans largely insulated from financial headwinds, a weaker average consumer may not have a disastrous impact on GDP growth. At the same time, a significant and economically vulnerable subset of the population has become increasingly burdened with costlier debt and less disposable income. Exhibit 16 at right highlights the stark contrast between the richest and poorest Americans when it comes to their balance sheets.

📌 **Exhibit 16:** The wealthiest U.S. households own the bulk of interest-earning assets, the middle class has the biggest share of mortgages, and the poorest Americans hold the most expensive consumer debt



Source: Bloomberg, Federal Reserve Distributional Financial Accounts as of March 31, 2024

## CONCLUSION

What does all of this information mean for consumers and impact on GDP growth? The mounting pressures via debt, housing costs, and lower savings have already reduced consumption patterns, but not enough to push the economy into a recession. Looking forward, interest rates are likely to drop, perhaps as soon as next month. While the ultimate impact will appear on a lagged basis, lower rates should reduce longer-term debt costs and promote economic expansion. The disproportionate distribution of wealth and consumption patterns will have varying degrees of impact on individuals and likely slow the overall growth rate. Nonetheless, overall consumption is expected to maintain a positive trajectory, therefore improving the likelihood of a soft landing for the U.S. economy. ■

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