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Consumer Morsel

It takes two income groups to tango

24 August 2022

Key talking points

- Consumer spending by both higher and lower income consumers is crucial to the overall US economy. Bank of America internal data suggests relative weakness in higher income consumer spending in recent months: total card spending per household excluding grocery, gas and clothing for the higher income consumer contracted on a month-over-month seasonally adjusted basis for three consecutive months through July while remaining fairly resilient for the lower income consumer.
- Higher income groups show the most visible moderation in spending in travel-related categories while spending for clothing and jewelry remains resilient in recent weeks, which could be boosted by back-to-school season and this year's wedding boom.
- Despite some moderation in spending by higher income consumers, they remain well positioned with elevated savings, as suggested by Bank of America internal data, which could buffer the current inflationary environment.

After nearly two years of strong consumer spending growth led by the lower income consumers, the higher income consumers picked up steam this year as they unleashed pent-up demand for services spending. However, with rising inflation and financial market volatilities, there are growing concerns around a major slowdown in spending for those that are more affluent.

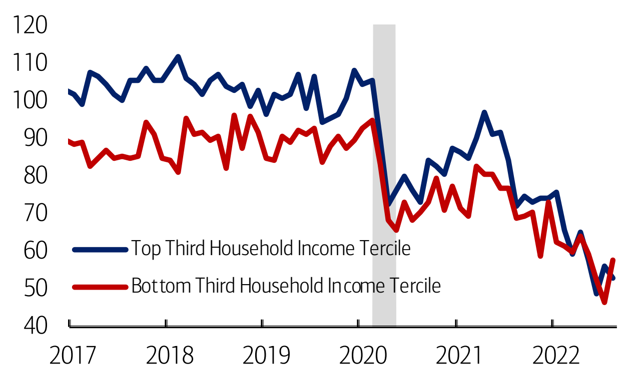
Both higher and lower income consumer spending is crucial to the overall US economy. On the one hand, the lower income households' spending can have a bigger impact on *the rate of change* for overall consumer spending given their higher marginal propensity to consume (MPC, i.e. proportion of income that is spent instead of saved). On the other hand, higher income households take up a much bigger share of overall consumer spending. Specifically, spending from the highest 20% income quintile made up nearly 40% of total consumer spending in the US in 2020, according to data from the Bureau of Labor Statistics. As a result, it is important to understand spending dynamics across income groups.

Summertime Blues

Consumer sentiment measures have fallen sharply in recent months and if history is a guide, a plunge in confidence is usually associated with a drop in real consumer spending. As Exhibit 1 shows, the University of Michigan consumer sentiment has dropped noticeably since last year for both income groups but the drop has been more severe for the higher income households: As of August, sentiment for the top third income tercile has slipped below that of the bottom third income tercile despite consistently trending higher in the past few years.

Exhibit 1: Consumer sentiment by income groups (monthly, index)

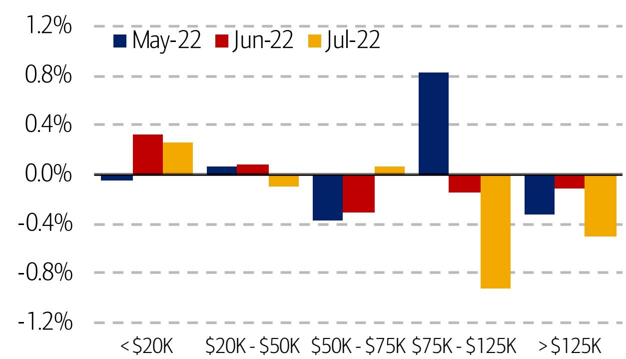
High-income households sentiment has slipped below that of low-income households in August



Source: University of Michigan/ Haver Analytics. Data as of August 2022. Shaded area means recession.

Exhibit 2: Total card spending per household excluding grocery, gas & clothing by income groups (% MoM, SA)

The highest income group saw three consecutive months of contraction in discretionary spending on a %mom SA basis



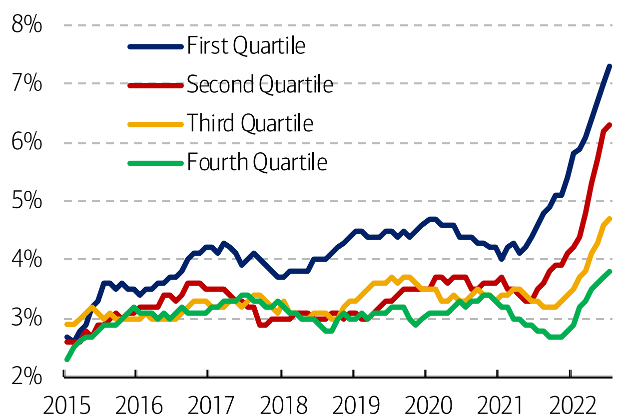
Source: Bank of America internal data.

Consequently, spending for the higher income households, based on aggregated Bank of America internal card data, seems to have weakened in recent months: total credit and debit card spending per household excluding grocery, gas and clothing for those with annual income greater than $125k contracted on a % month-over-month (MoM) seasonally adjusted (SA) basis for three consecutive months, the weakest across income groups (Exhibit 2). Note that we excluded grocery, gas and clothing because they are defined by the Census Bureau as "necessary spending". Therefore, spending on these categories are less sensitive to consumer financial situations. On the flip side, those with annual household income lower than $50k saw two months (June and July) of positive %MoM growth for card spending per household excluding grocery, gas and clothing.

Why are we seeing such divergence across income groups? We think it could be that strong wage growth for lower income consumers has been a big tailwind for lower income spending. According to the Atlanta Fed, median wage growth for the bottom income quartile consumers grew by 7.3% year-over-year (YoY) in July, outpacing headline Personal Consumption Expenditure inflation (PCE inflation) of 6.8%. However, the story is different for higher income consumers (Exhibit 3). For those in the top income quartile, median wage grew at just 3.8% YoY in July, well below any measure of inflation. As a result, negative real wage growth (nominal wage growth minus inflation) for the higher income households likely weighed negatively on sentiment as well as spending and should remain a headwind for this group of consumers. In addition, recent stock market volatilities could also impact higher income consumers' spending as they have more financial assets than the lower income consumers.

Exhibit 3: Median wage growth by income quartile (%YoY)

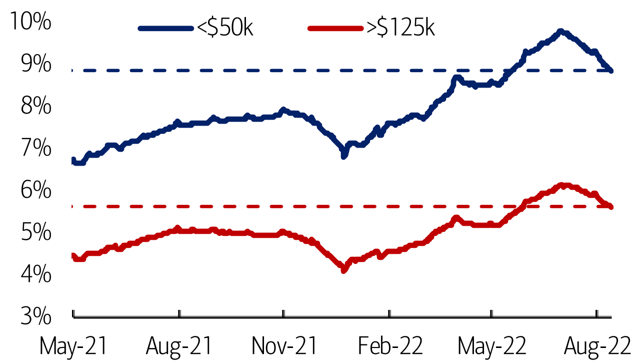
Wage growth for the top income group is below inflation, suggesting negative real wage growth



Source: Atlanta Fed. Data as of July 2022. Note first quartile means the lowest income quartile.

Exhibit 4: Gas spending as a share of card spending per household by income cohort, based on Bank of America internal data (%, 28-day moving average)

Gas spending as a share of total card spending for the lower income households dropped by a full percentage in mid-August from early July

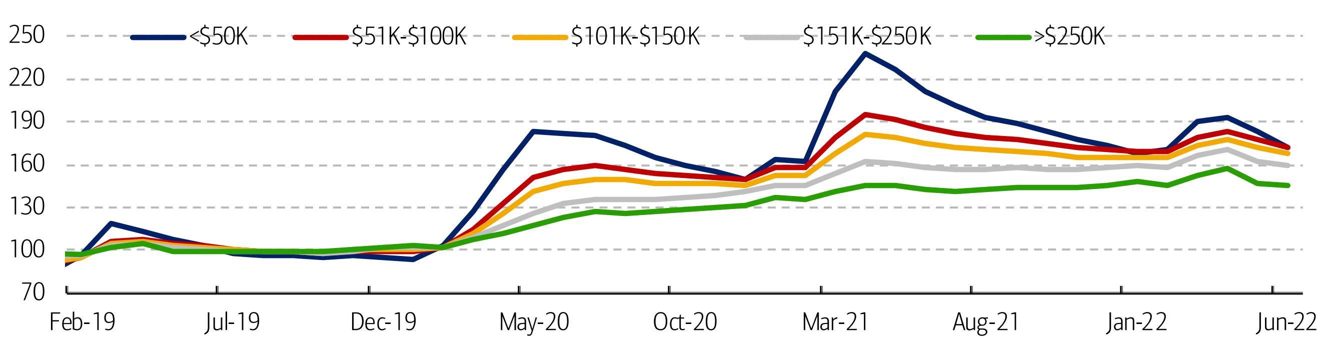


Source: Bank of America internal data. Data as of August 13 2022. Note: Gas spending include all purchase at gasoline stations which could include purchases of non-gas items.

Moreover, while gas prices have fallen noticeably in July and August, which freed up cash for consumers to spend elsewhere, the relative boost is smaller for the higher income households. Specifically, gas spending as a share of total card spending for the lower income households (<$50k) dropped by a full percentage point to 8.9% in mid-August from the peak in early July. Meanwhile for the higher income households (>$125k), gas spending as a share of total card spending only dropped by 0.5 percentage points during the same time period (Exhibit 4).

Exhibit 5: Median household savings and checking balances by income (index, 2019 average =100 for each group) for a fixed group of households (HH) between January 2019 and June 2022

Saving levels remain well up on 2019 levels across income cohorts



Source: Bank of America internal data. Data as of June 2022.

That said, moderation in spending for the higher income consumer does not mean deterioration. In fact, they remain well positioned with elevated savings, which could buffer the inflationary environment: as of end of June 2022, median household savings and checking balances for those with annual income of $151k-$250k and >$250k were up 59% and 45%, respectively, relative to their 2019 annual average (Exhibit 5).

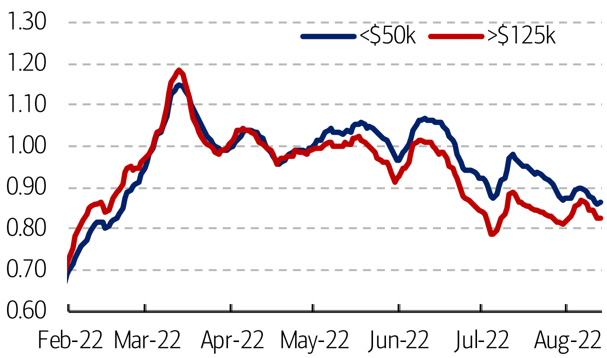
Some sectors are better than the others

While there seems to be a divergence in spending growth for the high and low income consumers, the story is different across sectors. Overall, spending seems to be moderating the most within travel-related categories for the higher income households. For non-durable goods such as clothing, higher income group continues to outpace the lower income group on a %YoY basis. For clothing specifically, spending by both income groups is boosted by this year's back-to-school season, though the boost seems to be smaller for the higher income households. Interestingly, jewelry spending for the higher income consumers remained resilient as of mid-August.

We take a look at the indexed level of spending for airline and lodging instead of the %YoY rates given that the %YoY rates are distorted by base effects from last year as the surge of the Delta variant depressed spending. As Exhibit 6 shows, airline spending per household for both the lower and higher income groups peaked in March as consumers booked summer vacations, but has leveled off in recent months, though the moderation seems to be more noticeable for the higher income households. Similarly, lodging spending per household for higher income consumers seems to be returning to its April average while that of the lower income is still 10% higher than its April average as of the week ending August 13. Discretionary services spending such as travel spending tends to be the most sensitive to household financial conditions. As such, negative real wage and deteriorating sentiment likely weighed on travel spending for the higher income consumers.

Exhibit 6: Airline spending per household, based on Bank of America credit and debit card data (index, Apr 2022 average=1 for each group, 7-day moving average)

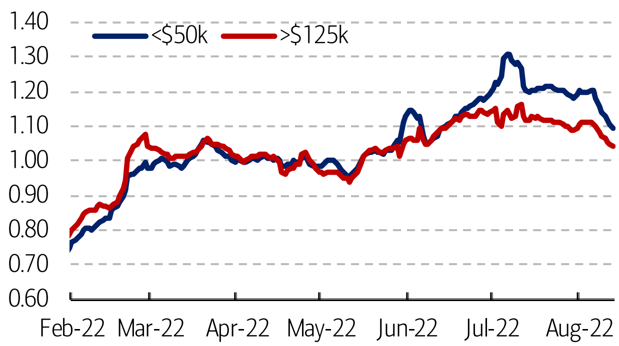
Airline spending per household for both the lower and higher income groups has leveled off in recent months, though the moderation seems to be more noticeable for the higher income households.



Source: Bank of America internal data

Exhibit 7: Lodging spending per household, based on Bank of America credit and debit card data (index, Apr 2022 average=1 for each group, 7-day moving average)

Lodging spending per household for the higher income consumers seem to be returning to its April average while that of the lower income is still 10% higher than its April average as of the week ending August 13



Source: Bank of America internal data

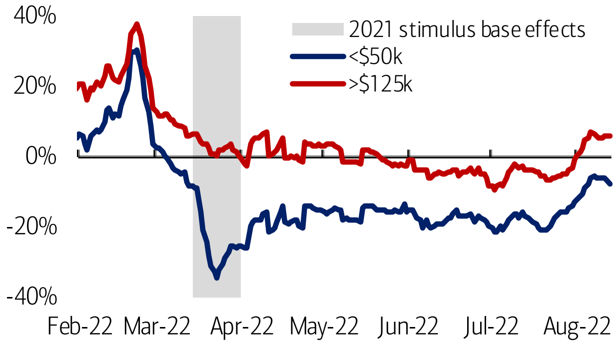
Clothing spending per household on a %YoY basis has been in the negative territory for both lower and higher income consumers since June as consumers shifted to more services spending, though there was a material shift higher in late July due to the start of this year's back-to-school season (Exhibit 8). If we look at clothing spending per household on an indexed level, it seems that the boost from the back-to-school season relative to the average spending level for clothing in April is smaller for the higher income group (Exhibit 9).

Another angle is to look at discount clothing stores vs. rest of clothing stores as we would expect the lower income consumers to usually shift to cheaper options in times of financial hardship. While we did see spending at discount apparel stores faring marginally better than spending at other clothing stores on a %YoY basis between May and July, the gap has closed more recently (Exhibit 10).

Interestingly, jewelry spending per household remains strong for the higher income households on both %YoY and level basis. One possible explanation is that jewelry spending could be benefitting from the wedding boom this year. According to wedding planning site The Knot, the total number of weddings is expected to reach 2.6 million in 2022, compared with 2.2 million in 2019.

Exhibit 8: Clothing spending per household, based on Bank of America credit and debit card data (%YoY, 7-day moving average)

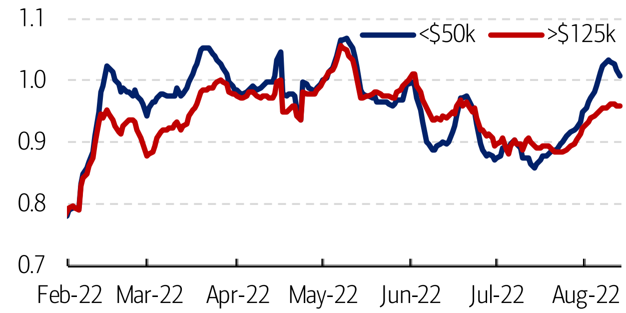
Clothing spending per household recently turned positive on a %YoY basis for the higher income consumers



Source: Bank of America internal data

Exhibit 9: Clothing spending per household, based on Bank of America credit and debit card data (index, Apr 2022 average=1 for each group, 7-day moving average)

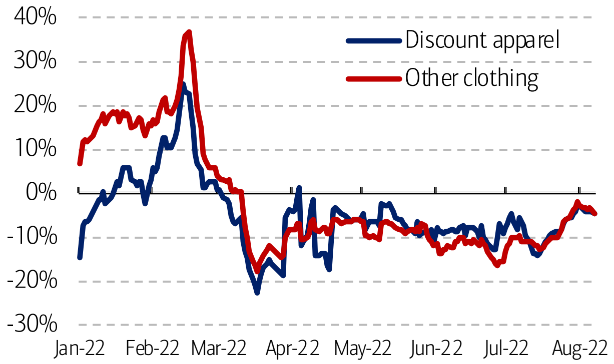
The boost from the back-to-school season relative to the average spending level for clothing in April is smaller for the higher income group



Source: Bank of America internal data

Exhibit 10: Discount apparel spending vs. other clothing spending per household, based on Bank of America credit and debit card data (%YoY, 7-day moving average)

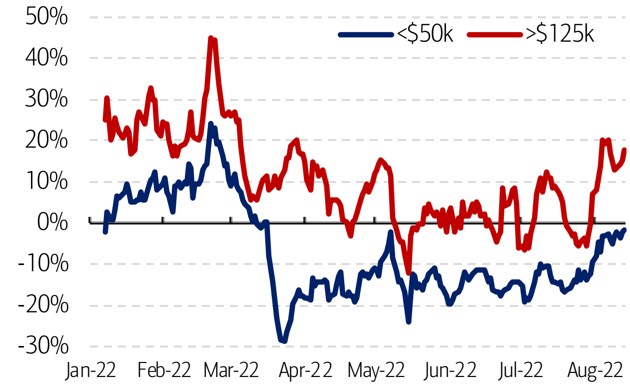
Spending at discount apparel stores and other clothing stores have been in line and negative on a %YoY as of August



Source: Bank of America internal data

Exhibit 11: Jewelry spending per household, based on Bank of America credit and debit card data (%YoY, 7-day moving average)

Jewelry spending per household remains strong for the higher income households a %YoY basis



Source: Bank of America internal data

The bottom line

Both higher and lower income consumer spending is crucial to the overall US economy. Bank of America internal card data suggests relative weakness in the higher income consumer spending in recent months: total card spending per household for the higher income consumer (>$125k) contracted on a month-over-month basis for three consecutive months while remaining fairly resilient for the lower income consumer. The moderation in spending for the higher income groups is the most visible in travel-related categories, while spending for clothing and jewelry remains resilient, which could be boosted by back-to-school season and this year's wedding boom. Despite the higher income consumers seeing some moderation in spending, they remain well positioned with elevated savings which could buffer the inflationary environment.

Contributors

Anna Zhou

Economist, Bank of America Institute

Sources

Kimberly Warren

Senior Vice President, Global Risk Analytics

Methodology

Selected Bank of America transaction data is used to inform the macroeconomic views expressed in this report and should be considered in the context of other economic indicators and publicly available information. In certain instances, the data may provide directional and/or predictive value. The data used is not comprehensive; it is based on **aggregated and anonymized** selections of Bank of America data and may reflect a degree of selection bias and limitations on the data available.

The household consumer deposit data based on Bank of America internal data is derived by anonymizing and aggregating data from Bank of America consumer deposit accounts in the US and analyzing that data at a highly aggregated level. For Exhibit 5, monthly data in the fixed cohort includes those households that had a consumer deposit account (checking and/or savings account) for all 42 months from January 2019 through June 2022.

Bank of America credit/debit card spending per household includes spending from active US households only. Only card holders making a minimum of five transactions a month are included in the dataset. Spending from corporate cards are excluded. Data regarding merchants who receive payments are identified and classified by the Merchant Categorization Code (MCC) defined by 7 financial services companies. The data is mapped using proprietary methods from the MCCs to the North American Industry Classification System (NAICS), which is also used by the Census Bureau, in order to classify spending data by subsector. Spending data may also be classified by other proprietary methods not using MCCs.

Additional information about the methodology used to aggregate the data is available upon request.

Disclosures