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Consumer Morsel

Fewer jobs, tighter belts?

13 December 2022

Key takeaways

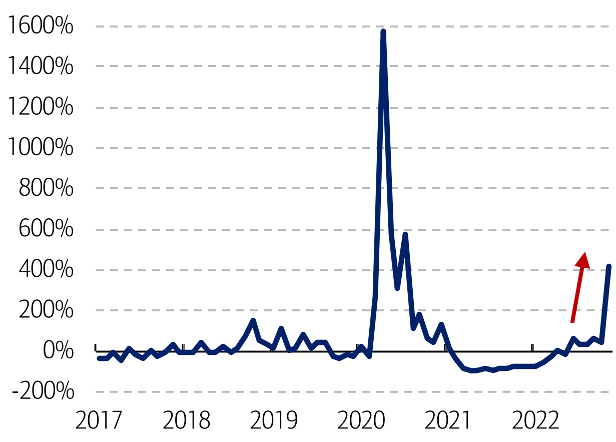
- The labor market is key to consumer resilience, and fears of an imminent slowdown are mounting. The November Challenger report showed a more than 400% year-over-year (YoY) increase in announced job cuts. Bank of America internal data shows that job losses this year have had a larger impact on the consumer than in the prior years.
- Specifically, we find that customers who experienced pay disruptions saw a 20% reduction in their median bank balance four months after that pay disruption, compared with just a 6% decline for the control group. They also reduced cumulative discretionary spending by 35% and necessity spending by 22% over the same four-month period.
- This suggests that if the labor market continues to slow next year with more consumers experiencing pay disruptions, consumer spending, especially for discretionary items, could be significantly reined in. But, for now, labor markets remain tight and the percentage of customers earning again within four months since pay disruption is in line with prior years.

Understanding pay disruptions with Bank of America data

A historically tight labor market and rising pay growth has been the main driver of US consumer resiliency this year. But despite continued strong payroll numbers, worries around an imminent downturn are growing. For example, major technology companies have announced large-scale layoffs in recent months and even more recently, consumer companies have made similar announcements. The November Challenger survey also showed a more than 400% YoY increase in job cuts (Exhibit 1).

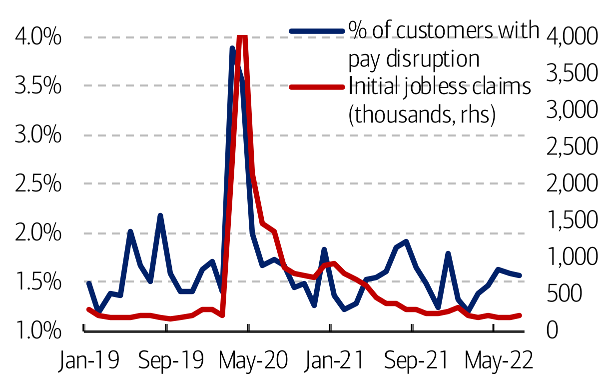
So, should we worry? We turn to Bank of America internal data to understand recent developments in the labor market and how job losses could impact consumers' financial health and spending patterns.

Exhibit 1: Total announced job cuts (%YoY, monthly)
Announced job cuts surged by over 400% YoY in November



Source: Challenger, Gray and Christmas by Haver Analytics

Exhibit 2: Share of direct deposit customers with pay disruptions and Department of Labor's initial jobless claims (non-seasonally adjusted)
Share of customers with pay disruptions was at 1.6% in July 2022



Source: Bank of America internal data, Department of Labor for initial jobless claims. Data as of July 2022. Data point for claims on April 2020 was not shown due to high volatility.

One way to understand job losses is by looking at customers with 'pay disruptions' - those who have stopped receiving their paychecks through direct deposit (DD). Specifically, in order to reduce short-term noise in the data, we define the sample of customers with pay disruption as those who have received their paychecks through DD at Bank of America for at least three consecutive months, followed by missing DD for the subsequent three months. The caveat is that with this methodology we might be capturing some customers who have voluntarily left the job market or who have switched to a different bank for their payroll deposit. However, we still believe it to be generally reflective of people experiencing the loss of a job.

Exhibit 2 shows that the share of Bank of America direct deposit customers who experienced pay disruption was just 1.6% in July 2022, the same as the 2019 annual average. Note that, by definition, this means these customers did not receive DD in August, September and October 2022. We find this data to generally echo trends in initial jobless claims from the Department of Labor, which stood at 224k in July 2022, also similar to the 2019 annual average of 218k. Moreover, both series spiked in March 2020 as workers were laid off when businesses were shut down due to strict social distancing polices.

Drawing down savings to support spending

What are the consequences for consumers of job losses? Intuitively, a drop in income would be expected to lead to drawdowns on savings to finance spending, as well as reduced spending. Economists generally believe that the degree of consumer response to such a negative income shock relates to whether the shock is anticipated or unexpected. But, for simplicity, we make no such distinction in the below analysis.

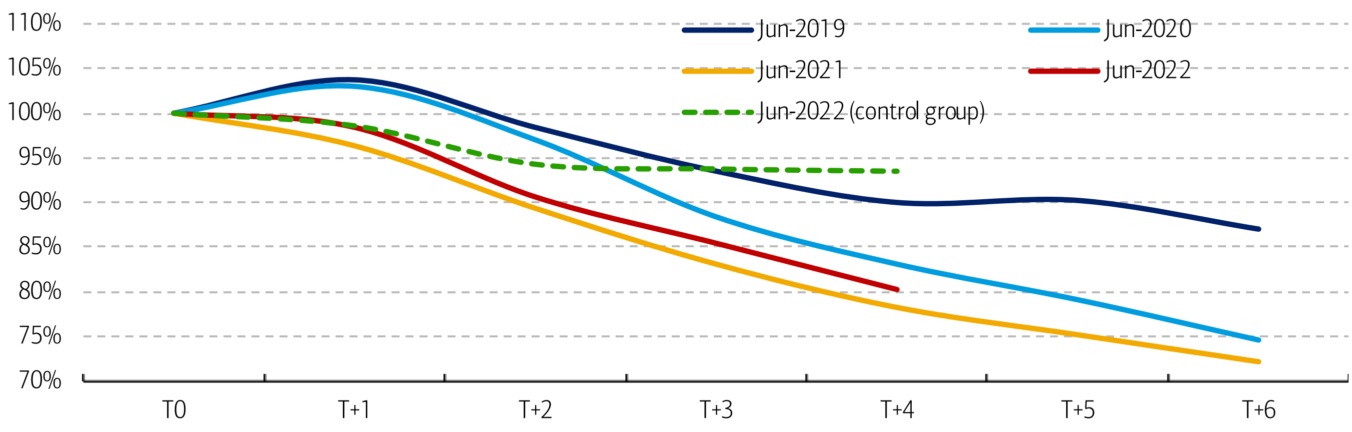
Using the same definition for "customers with pay disruption" as above, we specifically look at those who received their last paycheck in June of each year. June is chosen as a reference month for two reasons. First, it has been relatively uneventful for the past three years (i.e. no distribution of stimulus or surge in Covid cases which could distort savings and spending data). Second, Bank of America data used in this analysis goes through October 2022, leaving us with enough months of data following the pay disruption to understand trends in savings and spending patterns.

Let's first take a look at consumers' bank balances. As Exhibit 3 shows, median bank balances for the group of customers that experienced pay disruptions over the past four years all decreased in subsequent months but the rates of change were different. The rate of decline in 2022 (red line) and 2021 was the steepest while that of 2019 was the slowest.

In our view, the faster pace of decline in 2022 versus 2019 likely reflects the impact of higher inflation. For example, the Consumer Price Index (CPI) in June 2022 was over 15% higher than in June 2019. This means consumers needed to take out more money from savings this year than in 2019 to buy the same things. Meanwhile the fast drawdown in 2021 was likely due to pent-up demand for spending, even for people who had pay disruptions, following the relaxation of Covid restriction rules and distribution of stimulus. In both 2021 and 2022, median bank balances have been much more elevated compared to historical standards, which could also explain the change in savings drawdown behaviors.

Focusing on the 2022 data, we find that customers with pay disruptions saw a 20% reduction in their median bank balance four months after their last paycheck. Importantly, for those with no disruption (i.e. the control group) the decline in median bank balances was just 6%. As we discussed in the latest Consumer Checkpoint, median bank balances across income groups have been dropping steadily and gradually. But our data suggests that any deterioration in the market could see to an even faster drawdown of savings going forward.

Exhibit 3: Change in deposit balance following pay disruption (% change relative to last month of pay)
Pay disruptions led to a fairly steep drawdown on bank balances



Source: Bank of America internal data. Note T means the last month of paycheck received through direct deposit.

Discretionary spending always the first to go

We also find that as well as dipping into savings at a faster rate, an increase in pay disruptions could lead to a sharp pullback in spending, particularly in discretionary items.

Again, focusing on customers who received their last paycheck in June of each year, we found that they tended to cut spending immediately following pay disruption. At the onset, total card spending per customer dropped by 23% in July 2022, the steepest one-month drop for the past four years (Exhibit 4). In our view, the larger impact in 2022 relative to prior years could be due to a lack of stimulus as well as high price levels. By the fourth month following pay disruption in 2022, total spending was down roughly 27% relative to June's level.

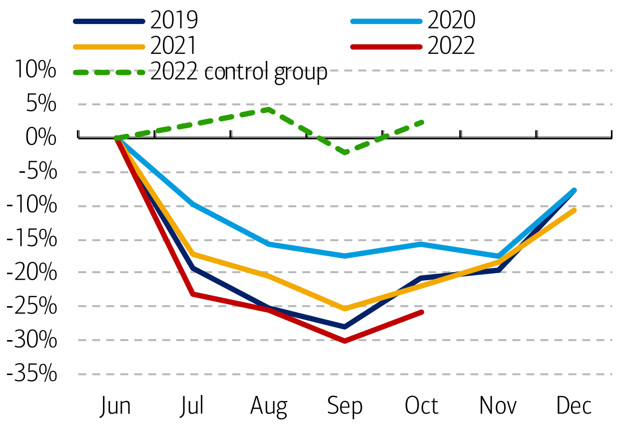
Unsurprisingly discretionary spending is harder hit than necessity spending (Exhibit 5). Our estimate suggests that over the four months following June 2022, those with pay disruptions reduced cumulative discretionary spending per customer by 35% and necessity spending per customer by 22% than what they would have spent absent pay disruptions.

Census Bureau data suggests retail sales in October are usually of comparable levels to June of the same year, suggesting the drop in spending for those with pay disruptions was not due to seasonality. Similarly, spending for the control group (those who continued to receive paychecks through DD after June) actually ticked up slightly over the same time period (Exhibit 4).

Note 2020 saw the smallest pullback given that spending levels were already depressed from COVID-related restrictions. The decline in spending was also smaller in 2021 vs 2022, confirming our above-mentioned view that pent-up demand for spending likely mitigated the downside.

Exhibit 4: Change in total card spending following pay disruption (% change relative to June (last month of pay) of each year)

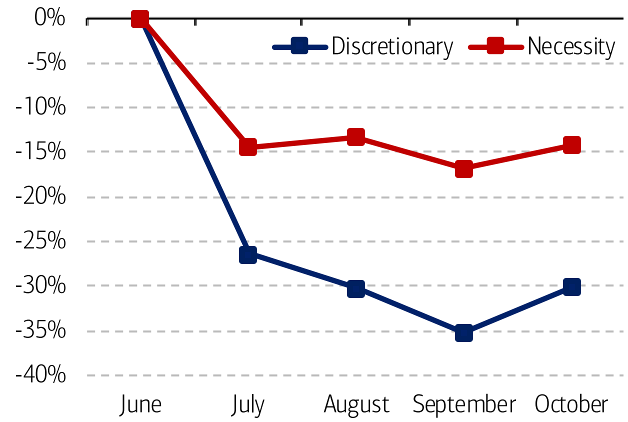
By the fourth month following pay disruption in 2022, total spending was down roughly 27% relative to June's level



Source: Bank of America internal data

Exhibit 5: Change in discretionary and necessity spending following pay disruption in June 2022 (% change relative to last month of pay)

Discretionary spending is harder hit than necessity spending after pay disruptions



Source: Bank of America internal data. Necessity spending includes food, utility and gas. Discretionary spending includes all other card spending.

Weaker labor market means weaker spending

What does this mean for the consumer outlook? BofA Global Research forecasts a labor market slowdown next year with the unemployment rate ticking up to 5.3% by the end of 2023 from 3.7% in November 2022. If this materializes, it would be expected to present meaningful downside pressure for consumer spending next year, particularly discretionary spending. They also forecast real consumer spending to grow only 0.1% YoY in 2023, down from the projected 2.6% for this year.

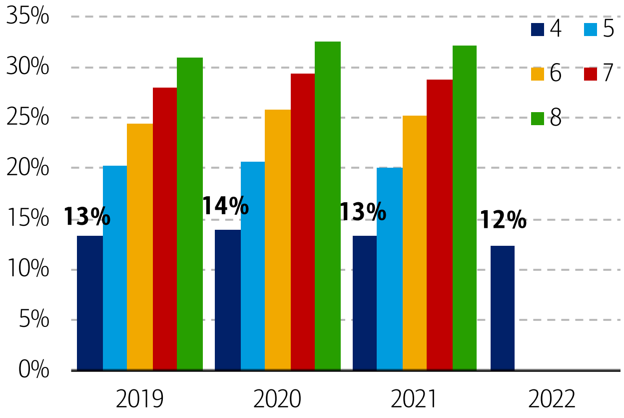
But, for now, labor markets remain tight despite signs of slowing and most of those who have lost their jobs are still able to re-enter the workplace. The Bureau of Labor Statistics' jobs report showed that the US economy on average added over 270k jobs per month between September and November, still higher than the average monthly gain of 190k between 2015 and 2019 (Exhibit 7).

In our data the percentage of people earning again within four months is in line with prior years: In 2022, 12% of people who experienced pay disruption in June started to receive labor income again by October. This is close to the 13% in 2019 and 2021 and 14% in 2020 (Exhibit 6).

We will keep monitoring how people who are experiencing pay disruptions are faring going forward. It will provide valuable insights into the trajectory of spending and deposit buffers next year.

Exhibit 6: Percentage of people with pay disruption starting to receive DD again

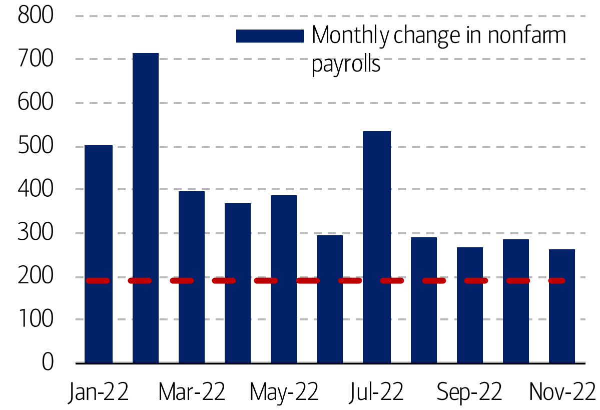
Workers with pay disruptions are starting to receive paychecks again at a similar pace in 2022 to in prior years



Source: Bank of America internal data

Exhibit 7: Monthly change in nonfarm payrolls (thousands, seasonally adjusted)

US economy on average added over 270k jobs per month between September and November



Source: Bureau of Labor Statistics

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Sources

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Methodology

Selected Bank of America transaction data are 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 are not comprehensive; they are 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.

Sample of customers used in this analysis include consumer households who have a direct deposit account with Bank of America.

Bank of America credit/debit card spending per household includes spending from active US households only. Only consumer 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 financial services companies. The data are 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.

Unless otherwise stated, data is not adjusted for seasonality, processing days or portfolio changes, and may be subject to periodic revisions.

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

Disclosures