EDITORIAL

HOW TO SPEND IT? SHIFTING CONSUMPTION PATTERNS AND COVID-19

The Covid-19 pandemic is having a profound impact on household expenditures. The volume has dropped and its composition has changed significantly. As restrictions are gradually lifted, services such as recreation, food services and accommodation, which have seen a big reduction in demand due to the restrictive measures, could thrive, to the detriment – at least relatively speaking – of spending on goods. For the strength of the early phases of the recovery, pent-up demand is an important factor. It plays a smaller role in the services sector, which could mean that countries with a larger services sector not only have suffered more from restrictive measures but could also face a bigger challenge during the recovery.

The Covid-19 pandemic is having a profound impact on household expenditures. The volume has dropped and its composition has changed significantly. The former has caused a jump in the savings rate as the hit to household income was cushioned by income support measures (furlough schemes, transfers) whereas people could not go out – or at least not as much as before – and spend. The change in composition resulted from restrictive measures to bring the virus under control, but also reflected an adaptation to the new environment. On-line sales grew strongly, the demand for second homes in the countryside picked-up, home renovation activity increased, etc. In the coming months, more and more businesses and venues are expected to re-open and one wonders whether spending patterns will shift again. This could mean that services such as recreation, food services and accommodation, which have seen a big fall in demand due to the restrictive measures, could thrive, to the detriment – at least relatively speaking – of spending on goods.

Clearly, the answer matters at the sector level but also for the strength of the recovery in general. The latter point is related to the role of pent-up demand. Recessions or – in the case of a pandemic – restrictions on mobility, imply that certain expenditures won't or can't be made. Moreover, given the uncertain economic climate, people might postpone making big ticket purchases. When the situation normalises, pent-up demand is unleashed with people celebrating the possibility to meet with friends over a beer or, when feeling financially more secure, keen to buy a new car. However, there is a fundamental difference between durable goods and services. The demand for the former will typically be postponed during a recession, but it doesn't vanish. In the example of buying a car, the car dealer will sell abnormally few cars when times are bad, whereas sales will be above normal during a recovery. In the case of services such as leisure or hospitality, lost business during a recession or lockdown is, to a large degree, lost forever. People will not try to make up for all the trips or restaurant visits they have not been able to make during lockdown. Moreover, as the support measures will be withdrawn as part of the normalisation process, some over-indebted businesses might close down definitively after the pandemic. This could make the recovery very choppy.

This should not stop services from being very dynamic in the initial phase of a recovery, something which is currently happening in the US as reported in the recently release Beige Book. In addition, the Business Leaders Survey of the Federal Reserve of New York revealed that *"leisure and hospitality firms saw a particularly large increase in activity in the April survey, their first increase since the pandemic began, and there were sturdy increases in the retail and wholesale trade sectors as well."*[1] Nevertheless, recent research brings a cautionary note. In the US, there is strong empirical support for the theoretical argument "*that recoveries from demand-driven recessions with expenditure cuts concentrated in services tend to be weaker than recoveries from recessions biased towards durables*"[2]. This difference is explained by pent-up demand, which plays a smaller role in the services sector. This analysis is particularly relevant for the Covid-19 induced recession which, as illustrated in the tables, saw bigger demand declines in services, causing significant changes in the relative weights of expenditure items. It could also mean that countries with a larger services sector not only have suffered more from restrictive measures but could also face a bigger challenge during the recovery.

China provides interesting insights on the development of retail sales in a post-lockdown world. On-line sales maintained their increase in market share. *"As a result of online sales' surge and physical stores sales' contraction, online sales' share of overall retail sales jumped from 20.7% at the end of 2019 to 24.9% at the end of 2020. As outbound tourism remains restricted, effective pandemic containment in mainland China has redirected higher-income households' planned spending on overseas trips to domestic spending instead, especially on luxury goods and big-ticket items."*[3] Chinese household spending also shows the role of lingering concern about the sanitary situation. As restrictions were eased, sales of movie and theatre tickets rose strongly, to 136% of the level reached the previous year, but subsequently declined to 56%.[4] Pent-up demand was clearly short-lived.

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1. *April Regional Service-Sector Survey Points to A Long-Awaited Rebound,* Federal Reserve of New York, Liberty Street Economics, 16 April 2021.
2. De*mand Composition and the Strength of Recoveries*, Martin Beraja and Christian K. Wolf, 20 February 2021.
3. *China's consumer market recovery under the Covid-19 pandemic*, IHS Markit, 2 February 2021.
4. Source: IHS Markit (2021).

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US REAL PERSONAL CONSUMPTION EXPENDITURES BY PRODUCTS GROUP (AS % OF PERSONAL CONSUMPTION EXPENDITURES)	Q4 2019	Q1 2020	Q2 2020	Q3 2020	Q4 2020
Personal consumption expenditures	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**
Goods	**36.0%**	**36.7%**	**39.4%**	**39.9%**	**39.5%**
- Durable goods	13.6%	13.4%	14.7%	15.7%	15.6%
- Motor vehicles & parts	4.0%	3.8%	4.2%	4.4%	4.4%
- Furnishings & durable hhld equipment	3.1%	3.1%	3.4%	3.6%	3.5%
- Recreational goods & vehicles	4.6%	4.7%	5.7%	5.8%	5.7%
- Other durable goods	2.0%	1.9%	1.7%	2.2%	2.2%
- Nondurable goods	22.6%	23.4%	24.9%	24.4%	24.2%
- Food & beverages purchased for off-premises consumption	7.4%	8.0%	8.8%	8.2%	8.1%
- Clothing & footwear	3.1%	2.9%	2.7%	3.2%	3.2%
- Gasoline & other energy goods	3.3%	3.2%	2.9%	3.1%	3.0%
- Other nondurable goods	8.6%	9.0%	10.0%	9.7%	9.6%
Services	**64.3%**	**63.8%**	**61.6%**	**61.3%**	**61.6%**
- Household consumption expenditures	61.7%	60.6%	57.6%	58.2%	58.6%
- Housing & utilities	16.5%	16.8%	18.7%	17.2%	17.1%
- Health care	16.9%	16.5%	15.0%	16.2%	16.7%
- Transportation	3.4%	3.2%	2.3%	2.6%	2.6%
- Recreation	3.8%	3.5%	2.1%	2.6%	2.6%
- Food services & accomodations	6.3%	5.9%	4.3%	5.3%	5.1%
- Financial services & insurance	6.5%	6.6%	7.2%	6.7%	6.8%
- Other services	8.5%	8.3%	7.6%	7.5%	7.6%

US REAL PERSONAL CONSUMPTION EXPENDITURES BY PRODUCTS GROUP (Q4 2019 = 100)	Q4 2019	Q1 2020	Q2 2020	Q3 2020	Q4 2020
Personal consumption expenditures	**100.0**	**98.2**	**88.8**	**96.8**	**97.3**
Goods	**100.0**	**100.0**	**97.2**	**107.1**	**106.7**
- Durable goods	100.0	96.7	96.3	112.0	111.6
- Motor vehicles & parts	100.0	92.0	92.2	106.5	106.3
- Furnishings & durable hhld equipment	100.0	99.0	97.0	110.4	108.9
- Recreational goods & vehicles	100.0	101.2	110.0	122.1	121.6
- Other durable goods	100.0	95.2	77.9	107.7	109.3
- Nondurable goods	100.0	101.7	97.7	104.5	104.1
- Food & beverages purchased for off-premises consumption	100.0	107.0	105.5	106.9	106.2
- Clothing & footwear	100.0	89.9	76.1	98.7	99.1
- Gasoline & other energy goods	100.0	95.4	77.4	90.7	88.8
- Other nondurable goods	100.0	102.9	103.0	108.4	108.3
Services	**100.0**	**97.4**	**85.1**	**92.3**	**93.2**
- Household consumption expenditures	100.0	96.5	82.9	91.4	92.5
- Housing & utilities	100.0	99.9	101.0	101.2	101.3
- Health care	100.0	95.6	78.9	92.7	95.9
- Transportation	100.0	92.6	59.7	75.9	75.2
- Recreation	100.0	90.3	48.6	65.2	66.8
- Food services & accomodations	100.0	91.0	60.7	80.3	78.8
- Financial services & insurance	100.0	99.5	99.2	100.7	102.1
- Other services	100.0	96.8	79.4	85.6	87.4

SOURCE: BEA, BNP PARIBAS