HSBC Global Research

Demographics

21 August 2023

The future US consumer

Can spending keep going?

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Economics - United States

- Consumer spending has held up in recent years in the US…
- …but as the population size and shape changes…
- …spending growth is likely to evolve

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The US consumer has been remarkably resilient in recent years. Despite high inflation, numerous interest rate increases and bouts of market volatility, consumer spending has kept grinding higher. A combination of a drawdown in accumulated savings, falling inflation and a resilient labour market are keeping wallets open for now, and despite a slower pace of growth expected in the coming year, we look for US consumer spending to continue rising.

But stepping back, there are several considerations that may shape the pace and composition of consumer spending in the years ahead. Many of these centre around demographic change – with the changing population pyramid meaning a much greater share of the population over the age of 65 and a shift to fewer infants. By 2040, the US is likely to have 25% fewer school-age children than it had in 1970.

Over the next decade, the pace of working age population growth is set to slow – from roughly 0.4% per year in the past decade to closer to 0.1% – hardly growing at all. This demographic transition will drive a few spending changes: because of many people being aged in their early 30s today becoming 40-something over the next decade, this may be supportive of overall spending and home ownership rates.

An older population may bring with it more spending on healthcare, and given that this retiring generation is wealthier than previous ones (thanks to the multi-decade rise in asset prices), the shock that ageing has on spending may be smaller.

We may also see some strong cohort effects – with rapid demographic transition pulling along digital consumption, a greater focus on sustainable products and demand for experiences. The US experience with remote work being more common than elsewhere in the world may affect spending in certain areas, too.

Overall, US consumer spending may grow at a slower pace than in the past, likely a shade under 2% per year in real terms. It won't be straightforward, as some periods will see weaker growth and others may see a catch up, but there are plenty of reasons to be cautiously optimistic about demand from US consumers in the years to come.

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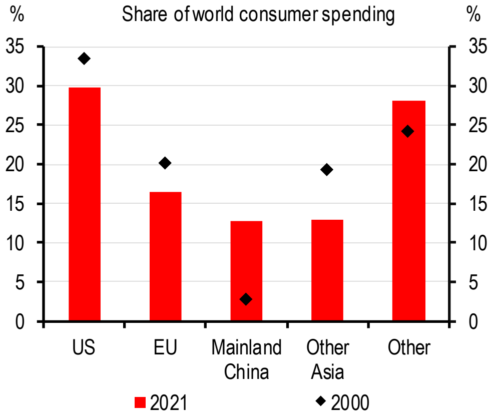
The world's number one consumer

- The US consumer remains in good health…
- …with favourable demographics and income growth…
- …likely to support certain types of spending

The world's biggest consumer

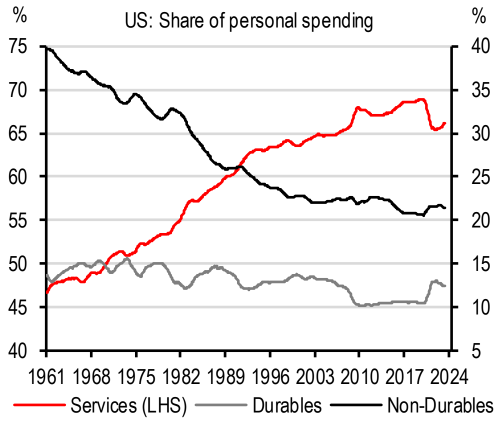
The US remains the world's most important consumer market. Despite the growth in Chinese demand in recent years, US consumer spending still accounts for roughly 30% of the global total, twice the share of the EU. This spending is heavily concentrated in services, despite the slight pullback during the pandemic, and a recovery on this front seems likely, as we outlined in *Has consumption changed forever?: Post COVID-19: What's stuck?*, 18 May 2023.

1. The US is still by-far the world's biggest consumer market…



Source: World Bank

2. …and spending is overwhelmingly on services



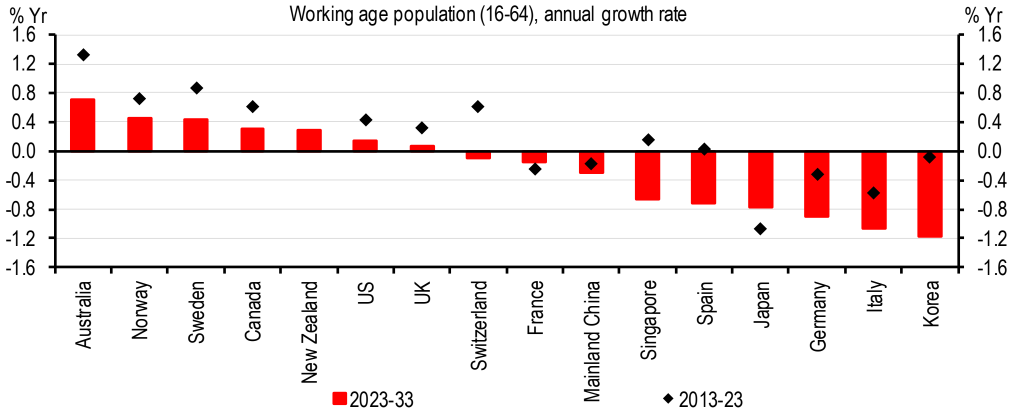
Source: Refinitiv Datastream

But how sustainable is this demand and how will it evolve? The US consumer faces several opportunities and challenges in the years to come – thanks to changing demographics, consumer tastes and social trends that are likely to determine how resilient this consumer demand proves to be.

More supportive trends than elsewhere

Compared with other developed economies, the US demographic profile gives reason for relative optimism. Its slightly younger population, higher birth rate and elevated rate of immigration means that the demographic backdrop for potential growth looks more favourable than for most European or developed Asian economies, albeit not as robust as for the smaller-population, high-immigration, developed markets (chart 3).

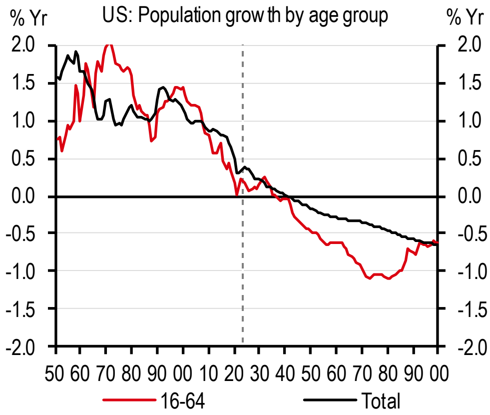
3. The US has a relatively favourable demographic picture compared to most large economies based on UN projections



Source: UN Population Division. Note: Developed markets plus mainland China shown

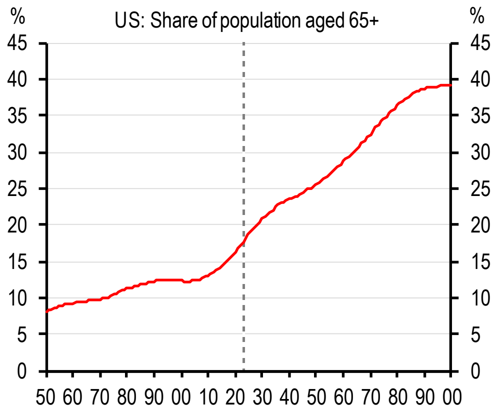
The US working-age population is set to keep rising, albeit at a slower pace than over the past decade – at least over the next 20 years – but after that it may start shrinking. However, there is an additional trend to note: a much greater share of the population will be elderly in the years to come. With the fertility rate having fallen to around 1.65 (from around 2.1 in 2008), the US population will now age reasonably quickly in the years ahead, with the share of the population over the age of 65 rising to close to 40% by the end of this century (chart 5). This clearly means a greater share of spending being in the hands of the older population – which in turn is likely to mean more spending on healthcare in the years to come.

4. US demographics are changing…



Source: UN Population Division, HSBC. Note: Dotted line shows where forecasts begin. Note: Uses the UN's low-fertility assumption for population data

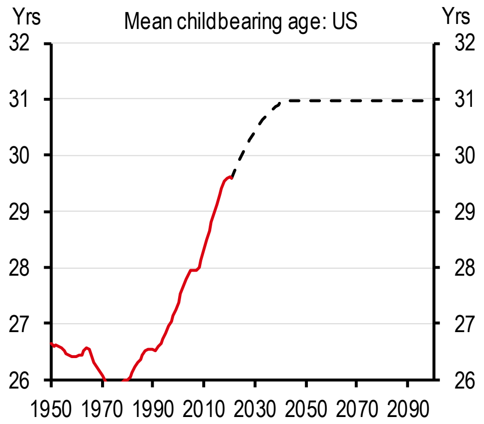
5. …with an older population



Source: UN Population Division, HSBC. Note: Dotted line shows where forecasts begin. Note: Uses the UN's low-fertility assumption for population data

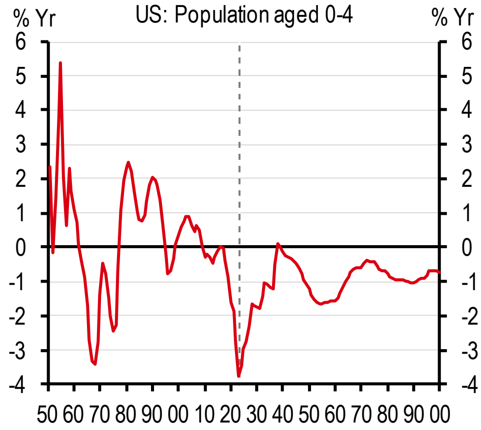
This brings with it some interesting side points. Firstly, Americans are having children later, like in much of the developed world. This plays a role in pulling down birth rates, but it also will impact the nature of spending in the economy. With more people in their late-20s being childless, this may support spending on leisure, travel and recreation amongst this age group. But, importantly, this brings with it another economic shock – the number of children being born means that the infant population in the US may well keep shrinking. And, as we outlined in *The big baby bust: Fewer babies, slower growth*, 22 August 2022, the chances are that these projections are too "optimistic" and the number of births and infants in the US (and other developed markets) drops more quickly in the years ahead.

6. Americans are having children later…



Source: UN Population Division, HSBC. Note: Dashed line shows forecasts.

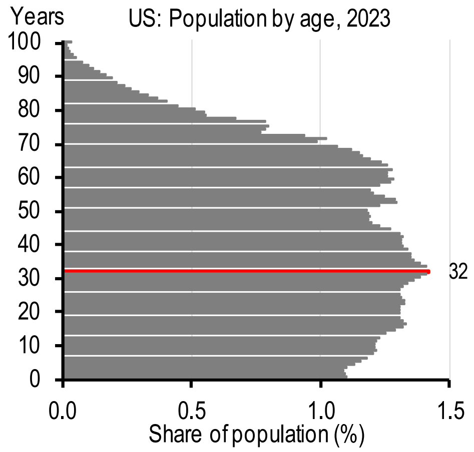
7. …and the number of children could continue to fall



Source: UN Population Division, HSBC. Note: Dotted line shows where forecasts begin. Note: Uses the UN's low-fertility assumption for population data.

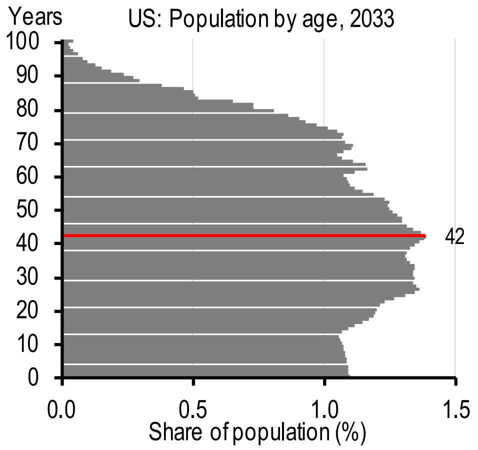
The demographic profile of the US is best seen by looking at population pyramids, as below. In 2023, the modal age of the US population is 32, with a few small bumps in the population at later ages. But over the course of the next decade, as this cohort gets older, the population pyramid starts to look less supportive at younger age groups, because of the aforementioned drop in births.

8. In 2023, the US population pyramid is reasonably healthy…



Source: UN Population Division

9. …but in 10 years' time it may not look so much

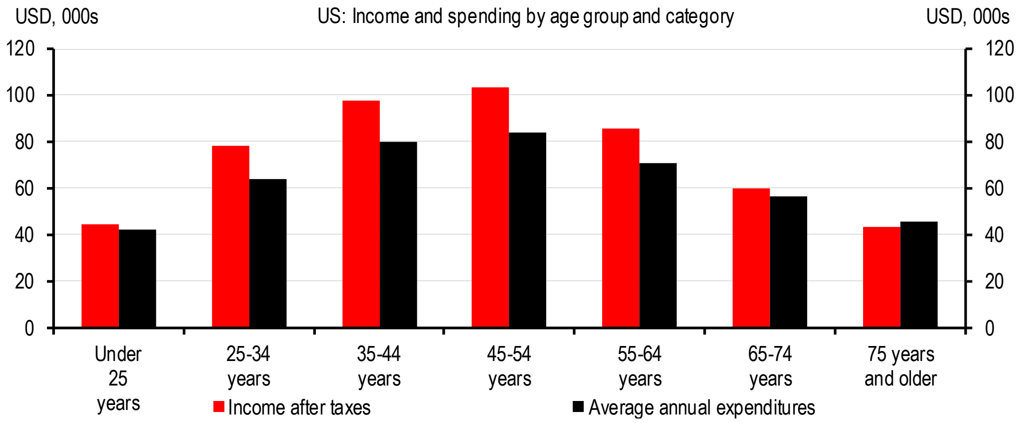


Source: UN Population Division

This shift makes a big difference to several trends. Demographics influence spending patterns in two ways: firstly, that spending patterns change as people get older (an ageing effect) and secondly that certain groups spend in different ways due to the era that they grew up in or other reasons (a cohort effect).

The ageing effect is reasonably supportive of growth, with the large number of people concentrated around their early 30s today becoming 40-something over the next decade. With spending rising with this ageing path, this could support overall demand in the economy, particularly with this large cohort.

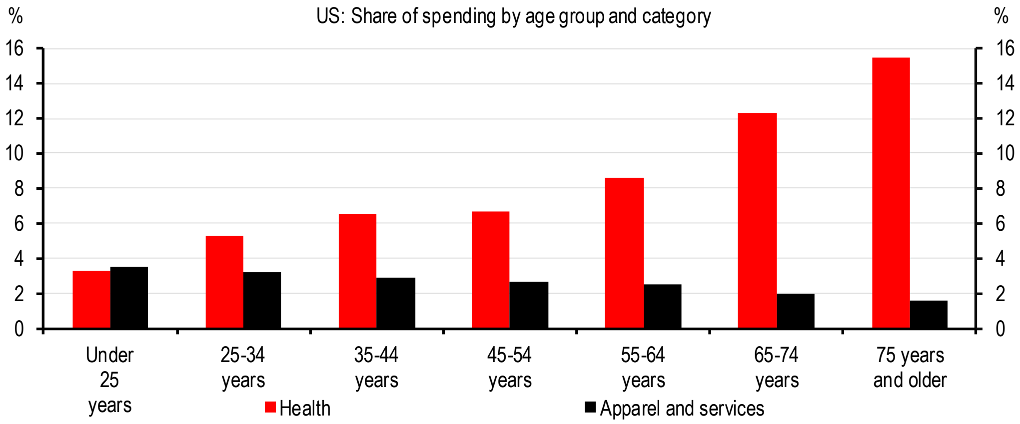
10. Income and spending peaks in 40s and 50s



Source: US Consumer Expenditure Survey (2021)

Ageing also means more spending on healthcare. There is a clear correlation between ageing, particularly above the age of 65, and healthcare demands and spending. US spending data from the Consumer Expenditure Survey shows this very clearly in a US context – and the ageing population is likely to need much more in the way of healthcare in the years to come. This will likely support some industries, creating jobs focused on providing health and personal care.

11. US spending on healthcare is clearly correlated with age

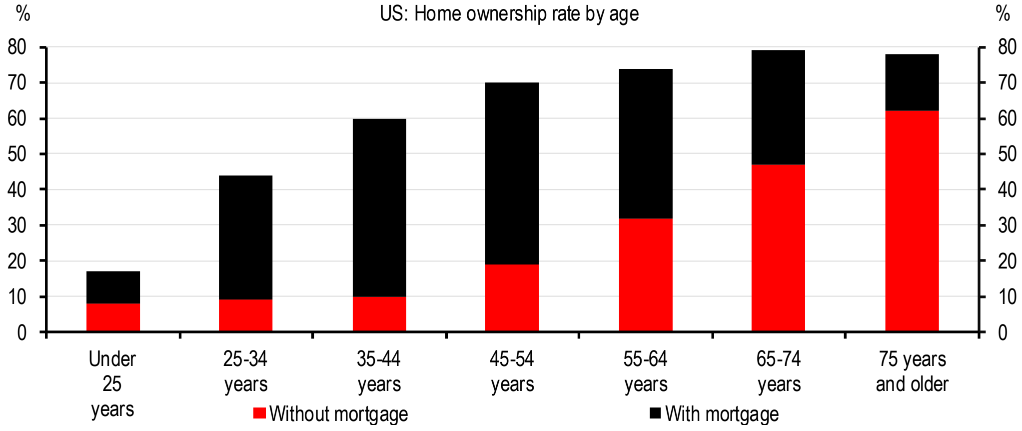


Source: US Consumer Expenditure Survey (2021)

However, another implication is that increased healthcare spending as people age may mean a diversion of funds away discretionary expenditures, such as for clothing or leisure.

One other impact of ageing relates to home ownership. It's very rare for under-25s to own homes in the US, but as people age from c25 to c 45 that ratio rises quickly as households have been able to accumulate enough funds for a down payment and incomes are high enough to support mortgage payments. This process may be slower in the coming years because of higher interest rates, but the shape of the US population pyramid is still supportive of home demand for the foreseeable future, because of the spike in the number of people ageing from their 20s and 30s into their 40s.

12. Home ownership rises with age



Source: US Consumer Expenditure Survey (2021)

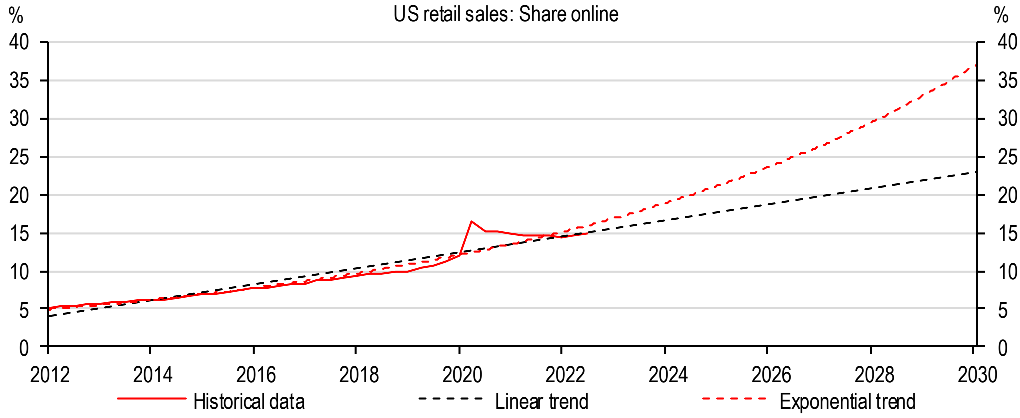
Beyond the ageing effects, there are some cohort effects, too. These are likely to involve trends that get carried by cohorts of people who have grown up in a different era to their parents. Demographic change, coupled with these cohort effects, is likely to mean that the median consumer, over time, will care more about environmental and social issues – albeit that recent criticism of environmental, social and governance (ESG) investing by some US policymakers[1] suggests that this transition might be neither smooth, nor linear. A younger generation are also likely to be more digital in the way they consume and interact with other people or services.

The latter point is one that we expanded on in a previous publication, where we highlighted how predictable changes in population cohorts in the years to come will help to drive the digitisation of the global economy. Essentially, every year we are replacing key consumers who are not as digitally-savvy with a new cohort of digital natives, who have grown up online.

This means that digital spending could be on an exponential trend – something that we flagged in *Gamechangers: How nine key themes are shaping the future of the global economy*, 2 April 2023, that human beings are bad at spotting in real time. The growth of the digital economy is likely to be one of these such trends, and so it's likely that the share of retail sales that goes online continues its pre-pandemic trend in the rest of this decade, perhaps lifting that share to north of 35% of the total. If more advances in technological solutions or cheaper logistics means that a greater share of some products can be bought easily online, this figure could easily rise more quickly – up to close to 50%.

[1] ESG backlash in the US: what implications for corporations and investors?, FT, 11 June 2023

13. Digital consumption could be on an exponential trend



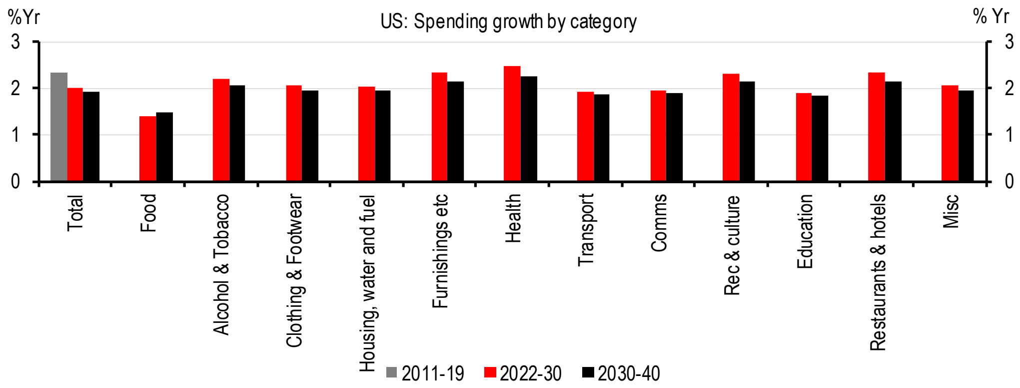
Source: BLS, HSBC estimates.

Putting it all together

In late 2022, we released a report called *The next generation of spenders: The changing tastes of a billion new consumers*, 6 September 2022, which looked at how demographics, income growth and taste changes could drive spending across a range of categories. Whilst this was a global model, not specifically aimed at the US, based on these underlying drivers, it suggested that US consumer spending growth may come in at a shade under 2% pa over the course of the next 20 years. This would be consistent with other medium-term forecasts: The Congressional Budget Office assumes roughly 1.7% per year growth in potential GDP, and over the past few decades consumer spending growth has risen more quickly than GDP. Whilst point forecasts over a longer-period need to be treated carefully, this seems to be a sensible starting point to think about the likely trend path for consumer spending in the US over the coming decades.

We may see some rotation in spending, as spending on health (due to ageing) and recreation and restaurants (due to preferences) increases more quickly as incomes continue to rise. This suggests that the rotation of spending towards many discretionary services may be structural in nature, rather than just a post-pandemic snap back.

14. US consumer spending should keep growing steadily



Source: HSBC estimates from *The next generation of spenders: The changing tastes of a billion new consumers*, 6 September 2022

This latter point is one that we looked at in more detail in *Has consumption changed forever?: Post COVID-19: What's stuck?*, 18 May 2023, which suggests that the post-pandemic rebound in services spending is likely to have more to run, given the multi-decade trends that came before and how consumer surveys suggest spending habits are evolving in real time.

Where could this be wrong?

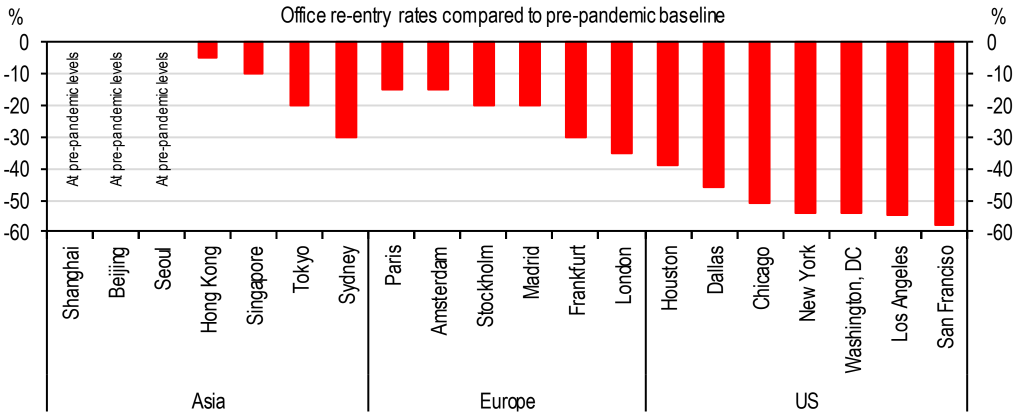
These assumptions are all relatively benign – we see plenty of reasons to suggest that US consumer spending growth could continue at a reasonably decent pace in the years to come as outlined above. But, of course, the path is unlikely to be so smooth as these longer-term projections suggest. We could see periods of much softer growth (like we forecast in 2024, with inflation-adjusted consumer spending growth of just 0.5%) or recessions.

But even within these forecasts – there are reasons why they could be wrong. Firstly, demographics projections could end up being inaccurate, either because of many fewer births (as outlined in *The big baby bust: Fewer babies, slower growth*, 22 August 2022) or if birth rates were to pick up materially in the years to come. We could see much more immigration into the US, either due to policy changes or due to more climate-induced migration globally (*Climate Change and Migration: A potential shock to demographic projections*, 25 May 2023).

Secondly, some of the spending pattern changes we expect may not come to fruition. We could see spending on services plateau after this period of strong demand, or we could see goods spending come back into vogue once many durable goods purchased during the pandemic hit their natural replacement cycle in a few years' time.

On top of this, the impact of remote work on US consumption patterns could be larger than elsewhere. As we showed in *The future of work: What follows decades of change in three years?*, 18 July 2023, the US has seen much less of a return to offices than other parts of the world (chart 15). This means that the impact on urban areas could be greater than in Europe (for example) and could weigh on spending in some parts of the economy that rely on that office footfall - potentially, for example, favouring retailers and caterers in smaller cities and suburban areas over those in central business districts, compared with pre-pandemic trends.

15. Office attendance rates are lower in the US than elsewhere



Source: JLL Research, The Future of the Central Business District, May 2023

But, of course, most of the drivers we have discussed relate to the structural story – in the near term, much will depend on the cyclical outlook – including rates, inflation and the labour market.

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