Societies and Inflation

With Particular Relation to its Effect on Consumer Demand

MR. ROBIN W. GAGE

(Mr. Gage is a senior member of the staff of the CWS Retail Management Services Group. The views expressed are, of course, his own and not necessarily those of the Group or the Society.)

In this brief contribution on the likely effects of inflation on the sales levels of retail societies, it is not the intention to make any fundamental analysis of the causes, or the likely outcome, of the inflation that currently grips the British economy. Indeed, the question both of the cause, and likely outcome, of the inflation is still the subject of debate amongst economists, and, frankly, to accept any one set of arguments at the present time is to give the economists more credit than they deserve. The best among them admit they cannot fully understand the situation. Instead of a generalised discussion, what has been attempted is to construct a practical guide, given certain basic assumptions, as to the likely effect on consumer demand for the major categories of goods sold by Co-operative societies.

Decline in Consumer Expenditure

For practical purposes the assumptions implied in the consideration of demand outlined below are those which are made by the Government, and most reputable independent economic forecasters, covering the next eighteen months or so. Without going into great detail these forecasts predict a decline in consumer expenditure (in real terms) of around about 1 - 2% from current levels. This is arrived at generally by predicting an overall price inflation of around 19%, wage increases of something rather more than this, but total personal income being cut back behind the rate of price increase by a combination of unemployment - probably around the one million mark - and possibly Government measures (either to restrict wage increases or to take a bigger tax revenue). In other words the prediction is for a rather less affluent but essentially very similar economic situation to the current one. In practice it makes little difference to the purpose of this paper whether these forecasts are worthy of acceptance or not, for unless something very similar to this happens, the changes in our economic situation are likely to be so great that it is, literally, almost anybody's guess what will happen.

On the other hand, on the basis of this type of development we can make some fairly confident predictions, in broad terms of what is likely to happen to consumer demand, in terms of the goods sold by retail societies, as a direct result of the predicted 1 - 2% decline in real purchasing power. (For the purposes of the comments below we have assumed a 2% decline.) These predictions take account only of spending power, not of any other market trends.

The forecasts of the effects a cut in living standards (or real wages) are likely to have on purchasing patterns are based on the "income elasticity of demand" for the various commodities and products. This is in fact a fairly complicated economic statistic. It is arrived at by a lengthy comparison of the relationship of income and consumption at a single point in time, and when finally calculated it shows, approximately, how much consumption of a particular product is likely to be affected by a 1% change in income level. The actual figures used in the comparison are drawn from Government publications - The Family Expenditure Survey for non-food, The National Food Survey for food.

Effects on Dry Goods?

Across the board, a 2% decline in purchasing power is likely to lead to a decline in expenditure on food of 0.5%, and on dry goods (durables, clothing and footwear, hardware and other non-durable household goods) of slightly over 2% - about 2.1%. In the field of dry goods the product categories most likely to suffer from a decline in real wealth are:-

Menswear
Children's wear
Soft furnishings and household textiles
Furniture and floorcoverings
Miscellaneous dry goods (hardware, toys, jewellery, etc. combined as one category)

In all these categories, consumer spending is likely to contract at a greater rate than purchasing power. All these categories are likely to suffer a real decline of around 2.5% - 3.5% in terms of cash sales (excluding the effect of inflation) because of spending power being reduced.

The non-food categories which will be least affected by a decline in spending power are:-

TV rental
Ladies' wear
Footwear
Other clothing (hats, gloves, piecegoods, etc.)
Electrical appliances

In all these categories we would expect that there would be rather less impact - ranging from practically no measurable effect on TV rental, to a decline of about 1 - 2% on the other categories.

In terms of the most recent experience available these are the effects that a decline in real spending power is likely to have on consumer expenditure. Of course, it must be remembered that the level of spending power is only one of the influences on market trends. There are other factors which may well influence the market - such as Government credit restrictions, supply difficulties, and basic market trends (i.e., a product going out of fashion) which will affect market demand. These predicted changes are not therefore in fact market forecasts for 1975; they are factors which should be used to take account of the likely changes in real income levels, when making forecasts (so that, for example, if based on market trends one expected sales in 1975 of £100,000 in both TV rental and menswear, then because of the predicted change in purchasing power these should be modified to £97,000 for menswear, and remain basically unchanged for TV rental).

Effects on Food Trade?

In the area of food trade sales we can make rather fuller predictions, using the same elasticity technique, because there are more available statistics relating purchasing patterns to income levels.

Of itself a 2% decline in real income will make very little difference to the demand for cigarettes and tobacco. Liquor sales, however, will be more responsive and should decline by about 2.5% (although again this is in total, and may well be more than offset by the trend to higher home consumption, so that the 2.5% decline again should only be applied to the expected value for 1975).

As stated above, in terms of actual food products, by which we mean food for in-home consumption, not confectionery or meals out, etc., the general effect will be considerably less than for most non-food products - a real decline in expenditure of under 1% is predicted. By and large, as will be the case also for non-food items, the decline in spending will be a combination of reduced quantities purchased and of "trading down" within a product. The products which appear most likely to see noticeable "trading down" are:-

Beef and Veal	Onions
Mutton and Lamb	Apples
Bacon and Ham	Soft Fruit (fresh other than grapes)
Cooked Meats	Dried Fruit
Chicken and Poultry	Cakes and Pastries
Fresh Fish	Plain and Chocolate Biscuits
Canned Fish	Breakfast Cereals
Quick Frozen Fish	Rice
Potatoes and Other Root Vegetables	Pickles and Sauces
Fresh Green Vegetables	Salt

For all these food products we would expect there to be a movement towards cheaper cuts or quality, or brands. These are the products where reduced income levels should have a noticeably greater effect on the money spent, rather than on the actual quantity bought. For all other food products it seems likely that quantity and expenditure are likely to be affected equally. The following are the products whose volume sales are most likely to be affected by the decline (2%) in spending power.

Decline in Quantity	Products
about 3% - 5%	Quick frozen fruit, shellfish, fresh coffee.
about 2% - 3%	Yoghurt, Q.F. chips and potato products, all quick frozen vegetables, cooking oils, fruit and vegetable juices.
about 2%	Nuts, fresh fat fish, Q.F. peas, Q.F. beans, ice cream and mousses, cream.
about 1% - 2%	Rabbit and game, Q.F. fish (white), wholemeal and wholewheat bread, mushrooms, spreads and dressings.

about 1%	Cucumber, lettuce, canned potatoes, poultry other than broilers, crisp-bread, QF meat, all fresh fruit (other than rhubarb and possibly apples).

Increase in Quantity	Products
about 1% - 2%	Coffee essence, pre-packed "old" potatoes (Jan-Aug), canned milk puddings.
about ½% - 1%	Beef sausages, canned peas, flour, pre-packed main crop potatoes (Sept-Dec).
under 1%	Large white sliced loaf.

Very few foods are in fact likely to gain any substantial benefit from a generally reduced spending power.

Many Other Factors

Apart from the products itemized above, the quantities of products sold are not likely to be affected substantially by a reduction in real spending power of the order predicted. Again, however, it must be stressed that we have here considered the effect only of a change in spending power upon consumption patterns. There are, of course, many other factors involved in setting the pattern of consumer spending - the changing nature of consumer tastes and needs, changing patterns of product supply or product innovation or noticeable disparate changes in the relative price of competing goods, for example. All these factors can be expected to be again present in 1975. For this reason the figures given above cannot be regarded as actual predications of market changes in 1975. They are solely an estimate of where, and to what extent, a reduction in spending power is most likely to have an influence. For example, the heavy representation of frozen foods in the list of products does not mean we are predicting an actual decline (of about 2%) as implied in the above lists, in the frozen food market. What we are in fact saying is that consumption of these foods will be depressed in 1975 (by about 2%) from the level we might otherwise have expected, due to a reduction in real spending power. However, the strong trend to increased frozen food consumption - due to changing food preparation habits, consistent product innovation, increased availability of refrigerators, and so on - that we have seen over recent years will still be present. We therefore expect 1975 to show a continued increase in frozen food expenditure (due to the established market trend) but a very much slower rate than in recent years (due to lower real spending power).

In conclusion, it may be worth re-emphasising that the whole of this examination of likely influences depends very much on the economy being kept on a reasonably even keel, and thus allowing consumption patterns in broad terms, to follow past experience. At least we might draw some encouragement from the fact that all current indicators are reasonably hopeful for Co-ops, at least from the sales side, if not from the profitability aspect. There is no evidence of any basic changes in shopping or consumption patterns as yet, and contemporaneous developments - particularly rapidly increasing petrol costs and mildly redistributive Government activity on earning power - should give Co-ops some competitive advantages in the, as yet, very uncertain future.