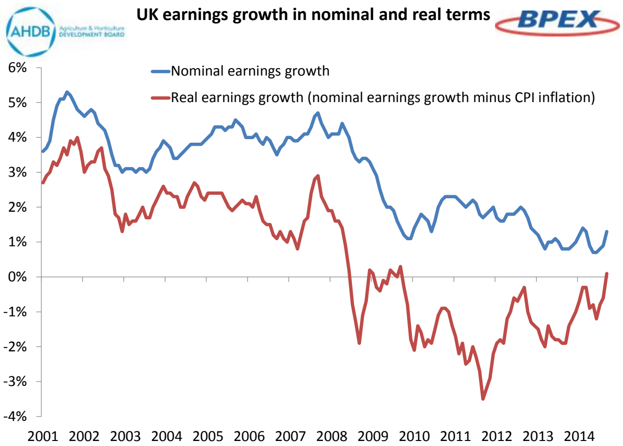
Will improving economic conditions increase food sales?

The UK economy is picking up speed; GDP growth, low inflation, and falling unemployment all point to a brighter economic future. This article examines whether this favourable news will lead to a rise in retail sales.

GDP grew by 0.7% in the third quarter of 2014, the seventh consecutive quarter of growth. Unemployment now stands at 6%, contrasting with September 2013 when 7.6% of the workforce were actively seeking work. Inflation is at a 5 year low - in September it stood at 1.2%. However, wage growth continued to lag behind inflation until September, when data recorded a positive move for the first time in four years.

Pay growth has slowed considerably since the financial crisis of 2008. Private sector pay increases have been hamstrung by weak productivity, making it difficult for employers to increase pay and remain competitive. The public sector, which employs 5.7 million people, accounting for around 20% of the working population, had pay frozen for 3 years in June 2010; pay rises for 2013/14 were capped at 1%. However, in the latest period earnings increased in real terms for the first time since September 2009.

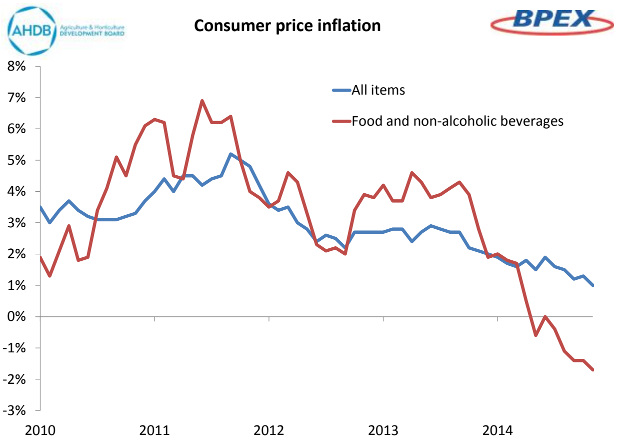


Source: Office for National Statistics

Consumer confidence is also improving, the GfK index, which has been carried out monthly for the European Commission since 1995, fell to -37 at the peak of the financial crisis but currently stands at -2. A separate consumer confidence survey from research group Nielsen showed consumer confidence in October at its highest level since the third quarter of 2007.

Evidence from the food retailer trade body IGD suggests that this improved confidence may not translate directly to increased spending. Over two thirds of shoppers still say that saving money is a priority when grocery shopping. Mintel report that, after bills, the most important spending priority for UK consumers is saving money and in-home food is not likely to be one of the main beneficiaries of any spending increase. A further look at some of the data collected by Mintel shows that a third of respondents would describe their financial position as 'tight', 'struggling' or 'in trouble'. IGD research shows a similar picture. When asked if they expected to be worse off than they were last year, a notable 33% of respondents agreed; this compares to 40% in 2013.

There is some optimism - less than 10% of shoppers expect prices to increase in the next year. This perception is confirmed by Kantar Worldpanel data which shows grocery inflation falling for 13 successive months to stand at -0.2% for the 12 week period ending 12 October 2014. This trend is backed up by other data sources, including official consumer price indices, which show declining food prices. Price competition among the 'big 4' supermarkets and hard discounters has been an important factor in this deflation.



Source: Office for National Statistics

There seems to be a reluctance to stretch the family budget and the reason may lie in the protracted squeeze on pay packets since the financial crisis. The downturn bit hard and was long lasting, leaving the average worker in Britain approximately £5,000 a year worse off compared to 2008, nearly 20% below where their income level would be had wage growth continued in line with inflation. It is almost 100 years since similar economic conditions prevailed.

Many British shoppers though, regardless of their current situation or how they see their future financial position, have acquired shopping habits during the recession that will take some time to change. The 'savvy shopper' might be here to stay. Shoppers are likely to continue to be less loyal to supermarkets and brands, may visit two or more stores on a shopping trip and use promotions and coupons more often.

There is no doubt that the improvement in economic conditions is welcome, particularly the real terms pay increase. The problem is that consumers still do not have the disposable income that was available pre-recession. Although they expect things to improve in the future and they are better off than 6 months or a year ago, they are much worse off compared to 2008. Only a long-lasting, sustained economic recovery will solve this.