EUROPEAN ECONOMICS UPDATE

23rd Feb. 2016

How have euro-zone consumers spent their oil savings?

- **Euro-zone consumers have spent a lot of their savings from falling oil prices on clothing and, to a lesser extent, furniture and electronics. This boost is unlikely to last and if oil prices rise gradually as we expect, spending growth in these sectors in particular seems set to slow quite sharply.**
- **We explained in a recent *Update* that euro-zone consumers appear to have spent, rather than saved, much of their windfalls from lower oil prices.** (See our *European Economics Update*, "Euro-zone consumers have spent their oil windfalls," 1st Feb. 2016.) In this note, we take a closer look at *how* they have spent that money. The detail of the monthly retail sales figures provides the clearest indication.
- While the *value* of retail sales rose by 1.5% in 2015, the *volume* of sales increased by a healthier 2.8%, as falling prices encouraged consumers to buy more. Price declines have, of course, been concentrated in energy. But demand for energy is relatively price inelastic (there are limits to how many more car journeys people will make as the price of petrol falls, for example). Accordingly, Chart 1 shows that since petrol prices embarked on a steep downward leg in October 2014, the *volume* of automotive fuel sales (included in the breakdown of retail sales) has been little changed while the *value* has dropped.
- **This has left consumers with more to spend in other areas.** Clothing sales, historically quite responsive to changes in real disposable income, seem to have received the largest boost. Sales values increased by 5% in the year to October 2015 before a weather-related decline in November. (See Chart 2.) And with clothes prices broadly stable over that period, sales *volumes* rose by around the same amount. By contrast, in the previous twelve months, clothing sales values and volumes both rose by less than 0.3%.
- Sales of electronics and furniture also seem to have benefitted, rising by 3% in value terms and by 2.5% in volumes in the year to October 2015, after stagnating in the previous year.
- **There are no timely data on spending on services.** But there may have been a positive impact on car sales – new car registrations rose by 10% y/y in December, perhaps partly reflecting the dual effect of increased real incomes and lower running costs. But it seems unlikely that such major purchases would be driven by a fall in oil prices which may prove temporary.
- Looking ahead, our forecast for the price of Brent crude to rise to $60pb by the end of next year points to a renewed pick-up in spending on fuel. **So unless nominal incomes rise sharply, which we doubt will happen, spending on other goods is likely to slow again.** And, even if the oil price stays the same, the boost to spending *growth* will fade. Indeed, this may already be happening – the euro-zone retail PMI fell for a third month running in January and both the German and French GDP figures show that consumption growth slowed in Q4.
- **The upshot is that consumers, the main engine of last year's GDP growth, are unlikely to increase their spending so enthusiastically this year. And the sectors which seem to have benefitted most from oil windfalls, most obviously clothing, are also likely to see the biggest reversals in their fortunes.**

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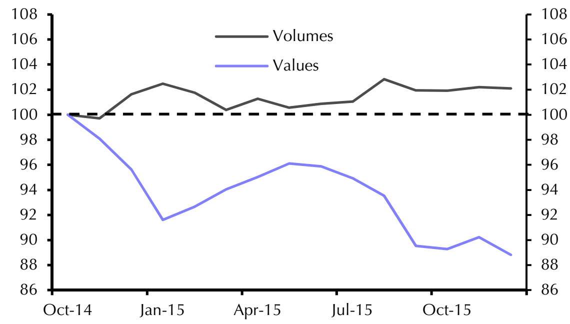
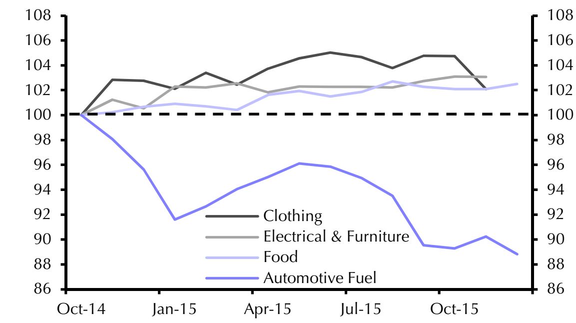
Chart 1: Automotive Fuel Sales (Oct. 2014=100)



Source – Thomson Datastream

Chart 2: Euro-zone Retail Sales Values (Oct. 2014=100)



Source – Thomson Datastream