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Consumer Morsel

How are middle-income consumers doing?

01 May 2023

Key takeaways

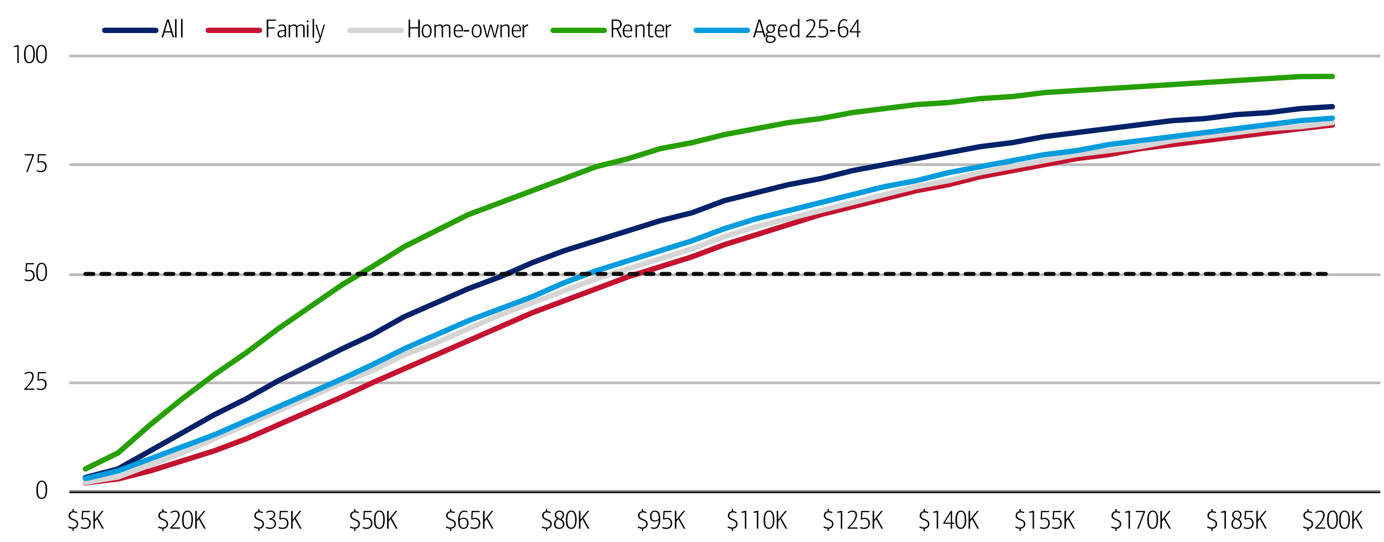
- Bank of America credit and debit card spending per household by middle-income consumers lagged the average over the pandemic. Their discretionary spending was particularly soft, with limited access to service sector activities as one explanation.
- However, there are signs of a catch-up at the start of 2023, with middle-income services spending looking fairly solid - and perhaps enjoying a good meal out once more.
- Can this persist? Well, the Bank of America Propriety Market Landscape Insights Study suggests middle-income consumers feel fairly confident near-term and still have financial buffers to draw on should economic headwinds start to blow harder.

What is the 'middle'?

People are often interested to know how households in different parts of the income distribution are faring. Right now, with the cost of living rising rapidly, there is an acute focus on how lower-income households are coping. And public policy understandably often looks at ways of ensuring the worst-off in society can be helped. We regularly cover these topics in our Consumer Checkpoint and other publications.

But it is also worth asking how people in the 'middle' are faring given plenty of US households find themselves towards the 'middle' of the income distribution. Afterall, these households are also contending with inflation, as well as anxiety over the labor market and how they will cope in any broader economic downturn.

Exhibit 1: The cumulative distribution of household income by household type (%)
The distribution of household incomes differs markedly depending on the nature of the household



Source: U.S. Census Bureau

First up, we need to ask ourselves what range of incomes would put people in this 'middle-income' group – a harder question to answer than it first appears.

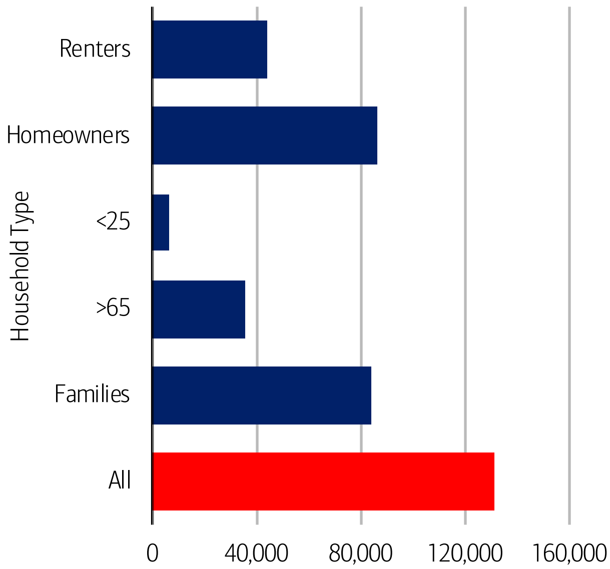
The U.S. Census Bureau publishes data on the income distribution of households and this is a good starting point. But looking at the aggregate picture can miss important nuances. Exhibit 1 shows the cumulative income distribution for various household types in the US. When we look at all households, we find that median household income is around $71,000 per year, and 75% of households have income of less than around $130,000.

But looking at 'all' households means we can be comparing people at quite different life stages. For example, younger people tend to earn less than older people who are further along in their careers. Equally, retirees tend to see their income drop as they transition from labor income to pensions and savings.

Put another way, a $70K income may feel very different to a 21-year-old versus someone aged 45 with a family to support. If we narrow our focus and look at the income distribution of households where the head of the household is aged between 25 and 64, we see that the incomes tend to be higher and the distribution shifts to reflect this. For the 25-64 age group 'middle' income rises to around $82,000, and 75% of households have income below $150,000.

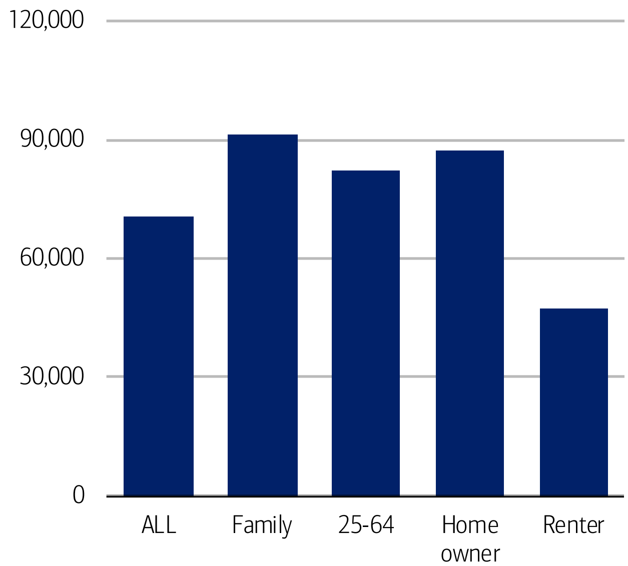
The income distribution also differs depending on whether people are homeowners or renters, or in family or non-family households. Exhibit 2 shows that around two-thirds of households are 'families' (where two or more people are related). And around the same proportion of households are homeowners. But there is considerable diversity – with significant proportions of renters and people living in non-family structures. As a result, median income varies across these household types (Exhibit 3).

Exhibit 2: Household numbers by household type ('000, 2021)
The make-up of households is diverse...



Source: U.S. Census Bureau

Exhibit 3: Household median income by household type ($)
...and median income varies across household types



Source: U.S. Census Bureau

The upshot is that in defining the range of incomes that make up this middle-income group, we need to take a flexible and pragmatic approach. Because the incomes of people tend to rise as they age, buy a house, have children, etc., it makes sense to consider the upper-income threshold for what counts as being in 'the middle' as being some distance above where simply looking at median income across all households might put it.

How is the middle doing?

What is the "middle" for our discussion?

In this analysis, using Bank of America internal data on card spending per household, we define the 'middle' as being households with income between $50,000 and $125,000. Across all household types, this corresponds to around the 40th to 75th percentile of household income, and just looking at households aged 25-64 it corresponds to around the 30th to 70th percentile – so broadly symmetric around the median. In other words, depending on the distribution you look at, around 35% to 50% of US households lie in this income range. In the charts that follow we look at total card spending per household looks across all households in our data.

What do we find?

Exhibits 4 to 6 plot the level of Bank of America debit and card spending per household for the middle-income and all income groups from 2019, indexed to 100 in January 2020. It appears from our data that spending was somewhat softer over the pandemic for the middle-income group relative to all incomes. Interestingly, this seems to be both a necessity (defined as food, beverages, utilities and gasoline) and discretionary (defined as total spending less necessity spending) story, though with the most marked divergence in discretionary spending.

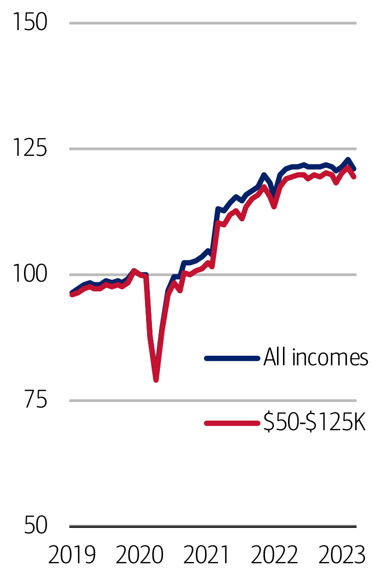
Why might the middle-income group have been lagging?

On the discretionary side, this likely reflects partly the impact of stimulus payments and other fiscal support over the pandemic. While many people in the middle-income group received these payments, lower-income households received a proportionately larger benefit, thereby supporting their spending more than for the middle-income group. Another pandemic-related reason could be that the middle-income group tends to spend a higher percentage of their budget each month on services rather than goods, and over the pandemic some of these services were unavailable (such as dining out).

A final reason is the labor market. When the economy was opening up in 2022, the labor market rebounded strongly. But some of the fastest jobs and wage growth was in lower-wage sectors, which has likely helped support lower-income spending relative to middle-income spending.

Exhibit 4: Total card spending per household (monthly, index Jan 2020=100)

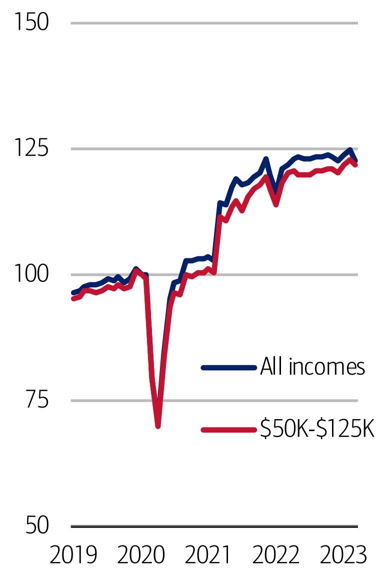
Middle-income spending has lagged the average....



Source: Bank of America internal data

Exhibit 5: Total card discretionary spending per household (monthly, index Jan 2020)

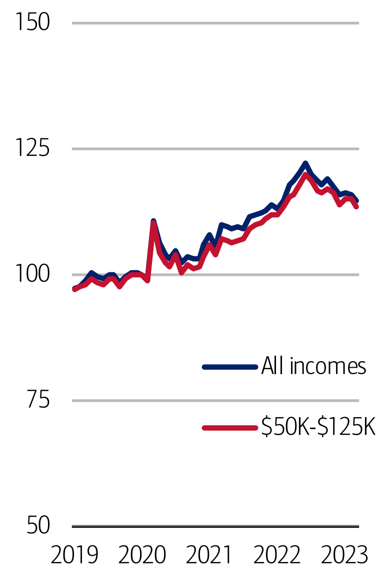
But very recently there has been some catch-up of middle-income discretionary spending



Source: Bank of America internal data. Discretionary spending is defined as total card spending minus necessity spending.

Exhibit 6: Total card necessity spending per household (monthly, index Jan 2020)

Necessity spending has also been marginally weaker in the middle-income group

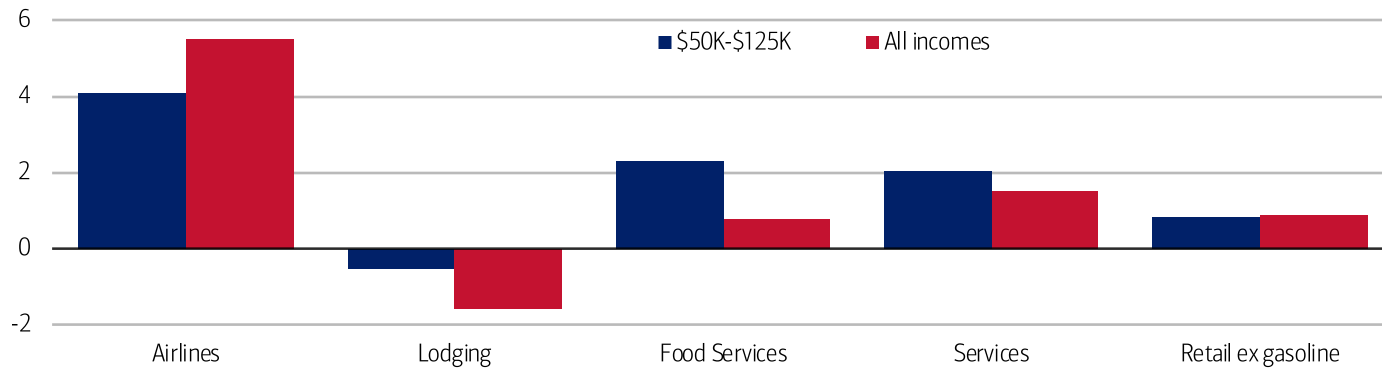


Source: Bank of America internal data. Necessity spending is defined as card spending on food, beverages, utilities and gasoline. .

But the 'good news' is there appears to be some signs that discretionary spending for the middle-income group is catching up with the average in 2023 (Exhibit 5). Digging into this, Exhibit 7 shows it seems to be a 'services story,' with middle-income growth in services spending over 2023 Q1 outstripping the average. In particular, food services, which includes restaurants and bars, showed solid growth for middle-income households, while lodging spending seems to be holding up better for this group than others as well.

Exhibit 7: Bank of America card spending per household, % change 2023 Q1 from 2022 Q4 (seasonally adjusted)

Middle-income groups are spending more on services, particularly dining out



Source: Bank of America internal data

Where to now?

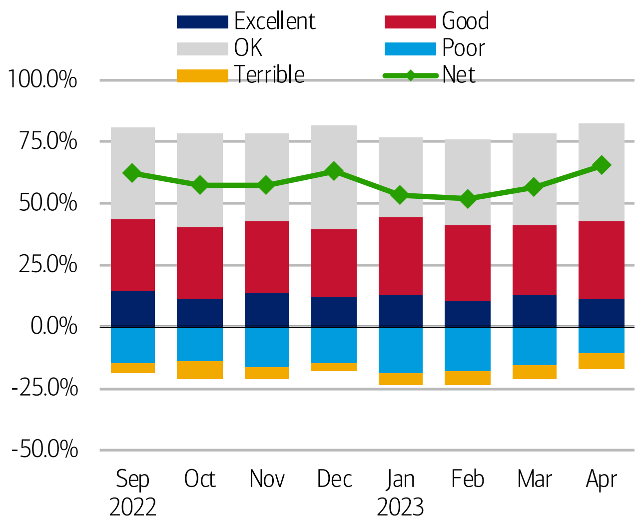
Can this better-than-average performance of the middle be sustained?

The April 2023 Bank of America Proprietary Market Landscape Insights Study ('Insights Study') provides some grounds for optimism. This survey asks Bank of America customers and non-customers a series of questions each month about how they view the economy and their own finances. It allows us to look at the specific sentiment of the middle-income group across a wide range of questions.

Exhibit 8 shows the Insights Study survey responses for the middle-income group to the question 'how do you feel about your finances?' Interestingly, since the start of the 2023 survey, respondents appear to be feeling *more* positive – those answering 'excellent/good/ok' have been increasing relative to those answering 'poor/terrible.' And when we look at how people expect their finances to evolve (Exhibit 9), there is little evidence that more respondents are expecting things to get worse. These findings stand in contrast to fairly negative talk of recession in the media over this period.

Exhibit 8: Survey responses to the question 'How do you feel about your finances?' (%)*

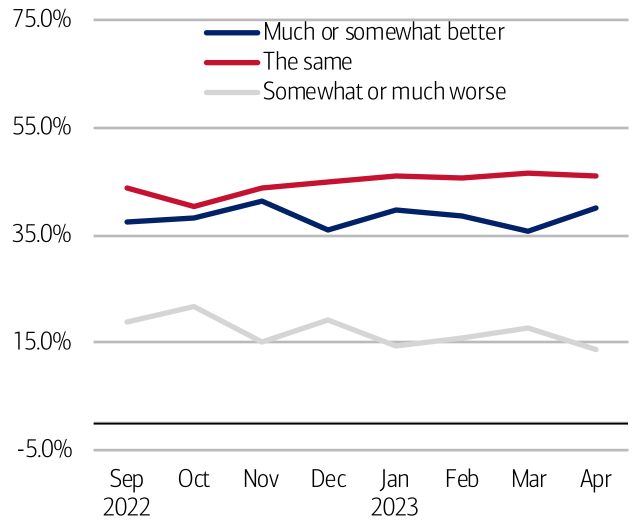
People are feeling better about their finances than they were at the start of 2023



Source: Bank of America Proprietary Insights Study. * Terrible/Poor responses are multiplied by -1 so bars add to the net position.

Exhibit 9: Survey responses to the question 'What are your expectations about your finances in 6 months?' (%)

The middle-income group is not expecting a deterioration in its own finances in six months

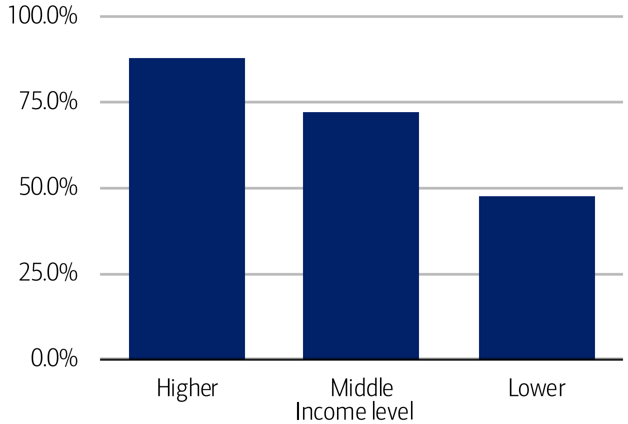


Source: Bank of America Proprietary Insights Study.

One reason this group may be feeling more upbeat is that they appear to be coping OK with the impact of inflation on their budgets. Exhibit 10 shows responses to a question on how much people have left over after paying for necessities. It plots the percentage of people saying they have an excellent/good/ok amount left over for lower-, middle- and higher-income groups. The middle-income group's assessment appears more positive than for lower-income respondents. This might reflect that middle-income consumers are not as exposed as lower-income consumers to the rising cost of rents, while food and other necessities also form a smaller share of their overall budgets.

Exhibit 10: Survey responses to 'The amount you have left over each month after paying for the basic necessities for yourself and family', % responding Excellent/Good/OK

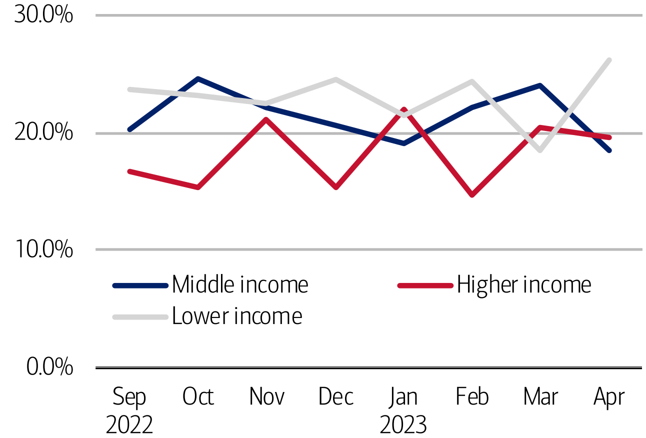
Middle-income consumers offer a fairly favorable assessment of the amount they have left over after paying for necessities



Source: Bank of America Proprietary Insights Study. Higher income defined as over $150K, middle income between $50K to $150K, lower income below $50K.

Exhibit 11: Survey responses to expectations for the state of the local economy in next six months: % responding 'somewhat' or 'much' worse

There has not been a deterioration in expectations for the local economy



Source: Bank of America Proprietary Insights Study

Additionally, Exhibit 11 shows no clear signs yet of a deterioration in people's expectations for the economy in their local area among the middle-income group. In April, the share of those expecting things to deteriorate in the next six months actually declined among the middle-income group.

Windbreaker

The Bank of America survey provides some 'good news' and may suggest that the catch-up in middle-income spending can last for a while.

But many economic forecasters are projecting a sharp slowdown or recession in the US economy this year. BofA Global Research expects the economy to shrink starting from the third quarter of 2023. These forecasts are accompanied by a rise in unemployment, though the upturn is fairly moderate compared to previous recessions.

It seems unlikely that the middle-income group can avoid some headwinds to their spending if these forecasts materialize. With that, will the positive sentiment seen in these surveys erode when consumers are faced with these economic realities?

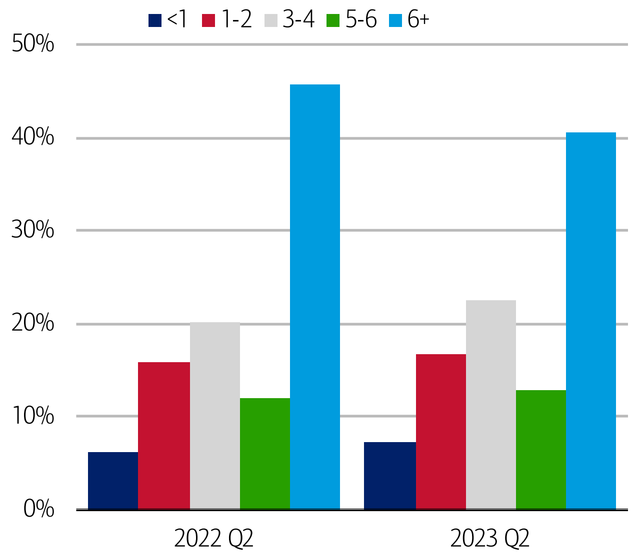
Possibly not. One source of cautious optimism remains the amount of deposit buffers in consumer accounts accumulated over the pandemic. These buffers do not appear to be falling fast – the Insights Survey asks people who have a 'rainy day' fund how long this would last if they used it to cover their 'living expenses.' Exhibit 12 shows that there has been only a modest decline in middle-income consumers saying this fund would last over 6 months. In the latest survey, around 36% said their fund would last 3 to 6 months.

And when we look at Bank of America internal data on customer deposits, we find that relative to before the pandemic, customers in two middle-income groups ($50-$100K and $100K-$150K) continue to see their savings levels around 60% higher. While there has been some drawdown in these buffers from their peaks, they have been fairly stable recently (Exhibit 13).

So there remain buffers available to cushion any economic headwinds. And the middle-income group may be able to use these to lean into any economic gusts to support their spending.

Exhibit 12: Survey response to question, 'How long would the funds in your "rainy day" or emergency fund last to cover your living expenses?' (%, months))

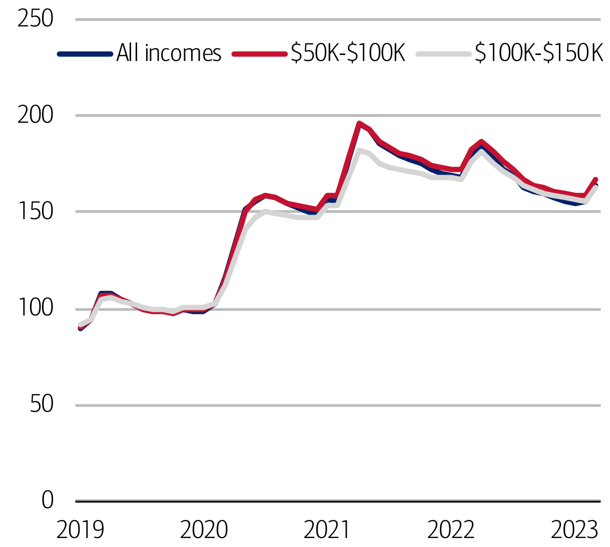
There has been only a modest decline in middle-income consumers saying this fund would last over 6 months



Source: Bank of America Proprietary Insights Study

Exhibit 13: Monthly median household savings and checking balances by income (2019=100) for a fixed group of households

Middle-income savings remain well up on pre-pandemic levels



Source: Bank of America internal data. Monthly data includes those households that had a consumer deposit account (checking and/or savings account) for all months from January 2019 through March 2023.

Methodology

Selected Bank of America transaction data is used to inform the macroeconomic views expressed in this report and should be considered in the context of other economic indicators and publicly available information. In certain instances, the data may provide directional and/or predictive value. The data used is not comprehensive; it is based on **aggregated and anonymized** selections of Bank of America data and may reflect a degree of selection bias and limitations on the data available.

Any payments data represents aggregated spend from US Retail, Preferred, Small Business and Wealth Management clients with a deposit account or credit card. Aggregated spend include total credit card, debit card, ACH, wires, bill pay, business/peer-to-peer, cash and checks.

Any **Small Business** payments data represents aggregate spend from Small Business clients with a deposit account or a Small Business credit card. Payroll payments data include channels such as ACH (automated clearing house), bill pay, checks and wire. Bank of America per Small Business client data represents activity spending from active Small Business clients with a deposit account or a Small Business credit card and at least one transaction in each month. Small businesses in this report include business clients within Bank of America and generally defined as under $5mm in annual sales revenue.

Unless otherwise stated, data is not adjusted for seasonality, processing days or portfolio changes, and may be subject to periodic revisions.

The differences between the total and per household card spending growth rate can be explained by the following reasons:

1. Overall total card spending growth is partially boosted by the growth in the number of active cardholders in our sample. This could be due to an increasing customer base or inactive customers using their cards more frequently.

2. Per household card spending growth only looks at households that complete at least five transactions with Bank of America cards in the month. Per household spending growth isolates impacts from a changing sample size, which could be unrelated to underlying economic momentum, and potential spending volatility from less active users.

3. Overall total card spending includes small business card spending while per household card spending does not.

4. Differences due to using processing dates (total card spending) versus transaction date (per household card spending).

5. Other differences including household formations due to young adults moving in and out of their parent's houses during COVID.

Any household consumer deposit data based on Bank of America internal data is derived by anonymizing and aggregating data from Bank of America consumer deposit accounts in the US and analyzing that data at a highly aggregated level. Whenever median household savings and checking balances are quoted, the data is based on a fixed cohort of households that had a consumer deposit account (checking and/or savings account) for all months from January 2019 through the most current month of data shown.

Bank of America credit/debit card spending per household includes spending from active US households only. Only consumer card holders making a minimum of five transactions a month are included in the dataset. Spending from corporate cards are excluded. Data regarding merchants who receive payments are identified and classified by the Merchant Categorization Code (MCC) defined by financial services companies. The data are mapped using proprietary methods from the MCCs to the North American Industry Classification System (NAICS), which is also used by the Census Bureau, in order to classify spending data by subsector. Spending data may also be classified by other proprietary methods not using MCCs.

Generations, if discussed, are defined as follows:

1. Gen Z, born after 1996

2. Younger Millennials: born between 1989-1995

3. Older Millennials: born between 1978-1988

4. Gen Xers: born between 1965-1977

5. Baby Boomer: 1946-1964

Any reference to card spending per household on gasoline include all purchases at gasoline stations and might include purchases of non-gas items.

Bank of America conducts a Proprietary Market Landscape Insights Study in order to provide an ongoing pulse on consumer attitudes, insights, and trends to help understand consumer responses to an ever-changing external landscape. The bank's Culture and Trends team manages quarterly and monthly online quantitative surveys conducted among customers and non-customers that provide a representative view of the U.S. adult population. Insights are based on aggregated and anonymized responses to surveys.

Additional information about the methodology used to aggregate the data is available upon request.

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Disclosures

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