Research Insights

Changes in spending during the COVID-19 pandemic

What can the government do to sustain spending?

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COVID-19 has shifted the way we spend

COVID-19 and the subsequent lockdown measures that started on 24 March have widely affected consumer spending, a key indicator of material wellbeing and a major component of Gross Domestic Product (GDP). In March 2020 household consumption expenditure accounted for 56% of Australia's GDP (ABS, National Accounts). High consumer spending boosts business revenue and creates more employment opportunities but in this first quarter of 2020, which included one week of lockdowns, household consumption expenditure fell by 1.1%[1]

COVID-19 has changed Australians' spending behaviour in many ways. Firstly, Australians are spending less in sectors curbed by lockdown restrictions, such as hospitality, tourism, transportation, recreation and entertainment. On the other hand, Australians have increased spending on groceries, food delivery, bills, cleaning appliances, and furniture and office equipment. Australians have also changed the way they spend. Mandated to stay at home in some states, Australians have increased the frequency of online purchases at the expense of shopping in stores. Debit and credit card usage has dominated, to help limit potential exposure to virus on surfaces in shops, reducing spending in cash.

Secondly, the current economic situation has also depressed consumption expenditure. Many Australians have lost income due to higher unemployment, reduced working hours and businesses putting employees on JobKeeper. In response to the fall in income, Australians may decide to draw on their savings, increase their debt, and/or reduce spending. For those with healthy finances, a reduction in spending is not too worrying if it relates to purchases of non-essential goods. Our worry, however, is for individuals whose expenses are dominated by necessities (such as food, rent, mortgage payments, bills etc.). If these individuals are facing income shortfalls or need to reduce savings and increase debt, it will be challenging to cut spending on non-essential goods.

The third related point is that Australians may decide to reduce spending and purposely increase savings even if current incomes have not fallen substantially. The uncertainty surrounding the future health of the economy and the strength of government support payments may induce people to save what they can, in response to uncertain future income.

Finally, the spread of COVID-19 varies by State. As the economy is reopening in many States, a second wave of community-driven infections in Victoria has induced further lockdowns. As a consequence, it is likely that consumer spending in Victoria will plunge during lockdowns, while other States may see an upward trend in spending, although at lower levels than the pre-COVID-19 period.

As consumption expenditure accounts for more than half of the Australian GDP, it is one of the key drivers of an economic recovery. In this Research Insight we study how COVID-19 is affecting spending in Australia now and in the future. It is important for the Government to learn which groups of Australians need more support, to help enact measures that put household spending on track to recover pre COVID-19 levels. As card usage has substantially increased, looking only at card spending may overestimate overall spending. To capture the impact of COVID-19 on current and expected spending accounting for changes in spending patterns and methods of payment, the Melbourne Institute's *Taking the Pulse of the Nation* survey asks two questions:

1. "Compared to the beginning of 2020, is your total spending today..."
2. "Compared to the beginning of 2020, and thinking about your spending six months from now, will your total spending at the end of 2020 be"

Respondents may answer "a lot more" , "a little more", "same as at the beginning of 2020", "a little less" or "a lot less".

Key Insights

1 Spending of many Australians has decreased and will not recover by the end of 2020.

COVID-19 has affected the spending of many Australians. 45.5% of respondents report they are spending less than what they were at the beginning of 2020 (Figure 1). Although the proportion is expected to decrease, one third of Australians will not have recovered pre COVID-19 spending levels in six months.

Australians who are already spending less than in early 2020 will be of interest to the Government. As shown in Figure 2, 55% of those people think their spending will not recover to pre COVID-19 levels by the end of the year.

Figure 1: Spending today and expected spending in 6 months compared to early 2020

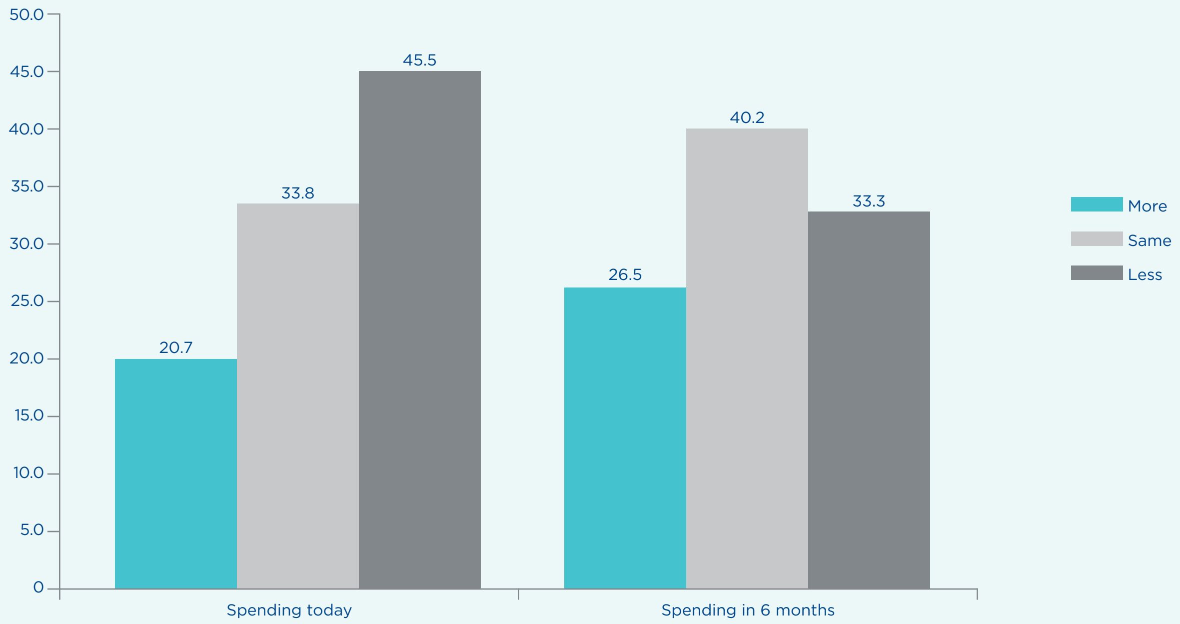
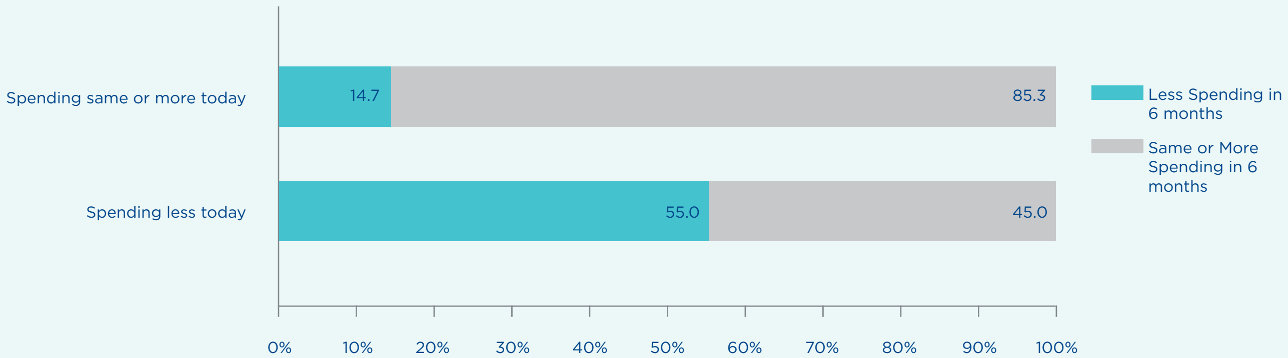


Figure 2: Expected spending in 6 months compared to early 2020 by current spending

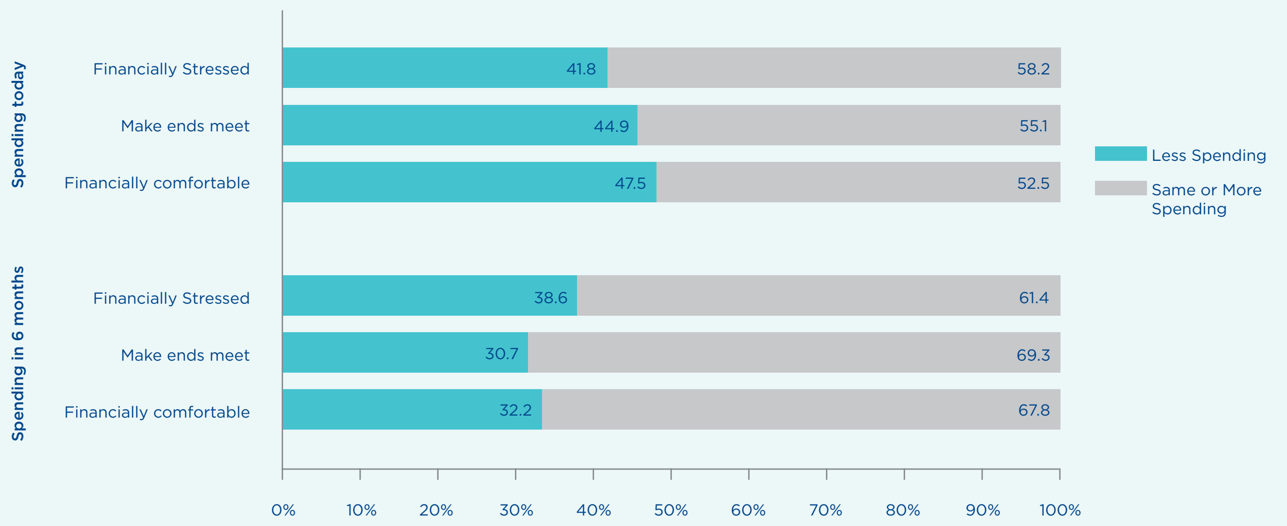


2 Spending reduction is spread regardless of financial circumstances, also among Australians who are financially comfortable.

COVID-19 has affected spending levels regardless of financial circumstances. The restrictions for travelling and the limitations in the hospitality, recreation and entertainment sectors have reduced current and expected spending among Australians who are financially comfortable. Among Australians who are in comfortable financial circumstances, 47.5% report lower spending compared to the beginning of the year and 32.2% do not expect to recover pre COVID-19 spending levels in six months. This fact may suggest the need for policies that boost spending of Australians who can afford to spend more.
Income uncertainty has an impact on consumption expenditure of Australians who are financially stressed and report they make ends meet.

Among Australians who make ends meet, the prevalence of people who are spending less (44.9%) and expect to spend less (30.7%) is not significantly different to the group of financially comfortable Australians. The group of financially stressed Australians has the lowest prevalence of people who currently spend less than in early 2020 (41.8%). This is worrisome as it suggests that financially stressed people spend most of their income on necessities and are not able to reduce spending. The small drop in the proportion who expect to spend less in six months suggests that many financially stressed Australians do not believe their situation will improve in the future. This may support calls for extended income support to financially stressed people.

Figure 3: Spending today and expected spending in 6 months by financial circumstances

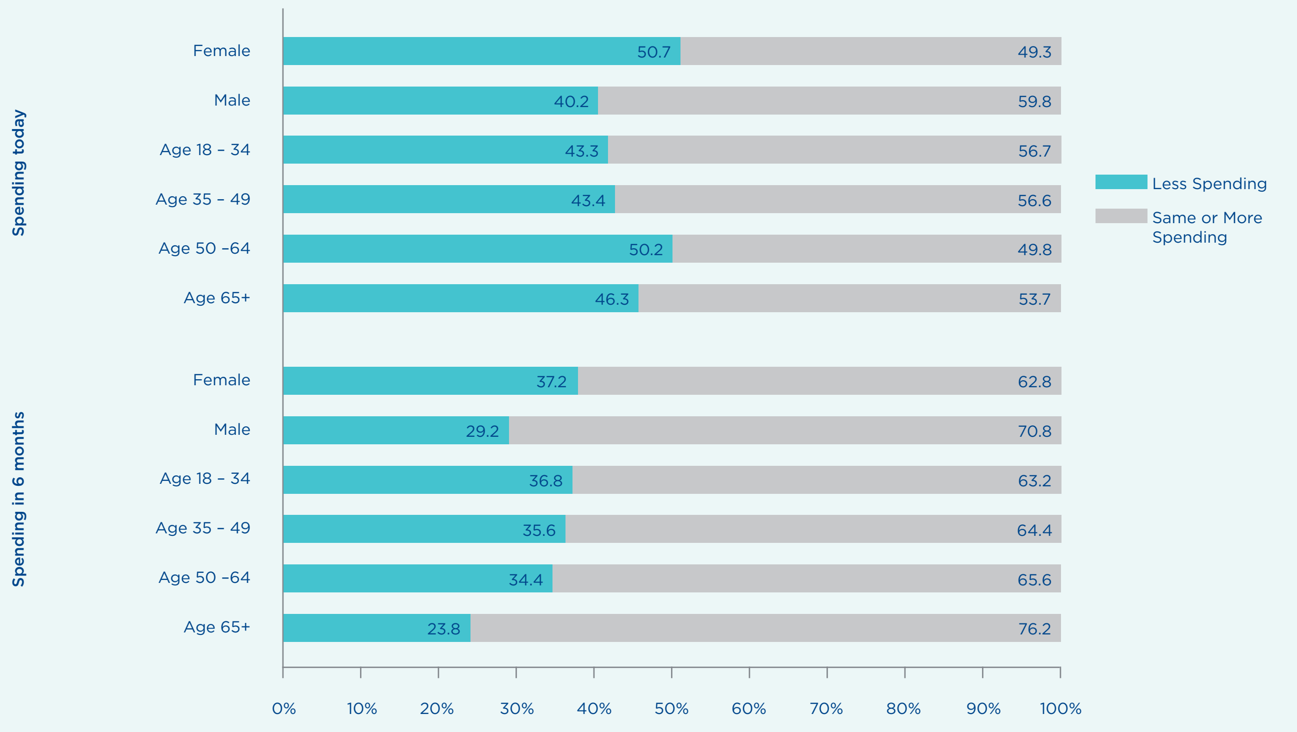


3 Women are more likely to reduce spending in six months. Young and middle aged people are more likely than older people to spend less in six months.

Women are more likely to have lower current and expected spending than in early 2020. 50.7% of women spend less and 37.2% expect to spend less than the pre-pandemic levels. The proportions for men are respectively 40.2% and 29.2%. This is consistent with the fact that women are more likely to work in sectors more affected by the COVID-19 crisis (hospitality, arts and recreation services). Older Australians are more likely to spend less than in early 2020. Notwithstanding, a higher proportion of elderly people expect to recover pre COVID-19 spending levels in the near future.

Australians aged 65 and above have the lowest share (23.8%) of people who expect to spend less in six months than at the beginning of the year. The fact that young and middle aged people are more likely to spend less in six months can be due to the uncertain conditions of the labour market. People aged above 65 mostly derive their income from superannuation annuities and pensions.

Figure 4: Spending today and expected spending in 6 months by sex and age

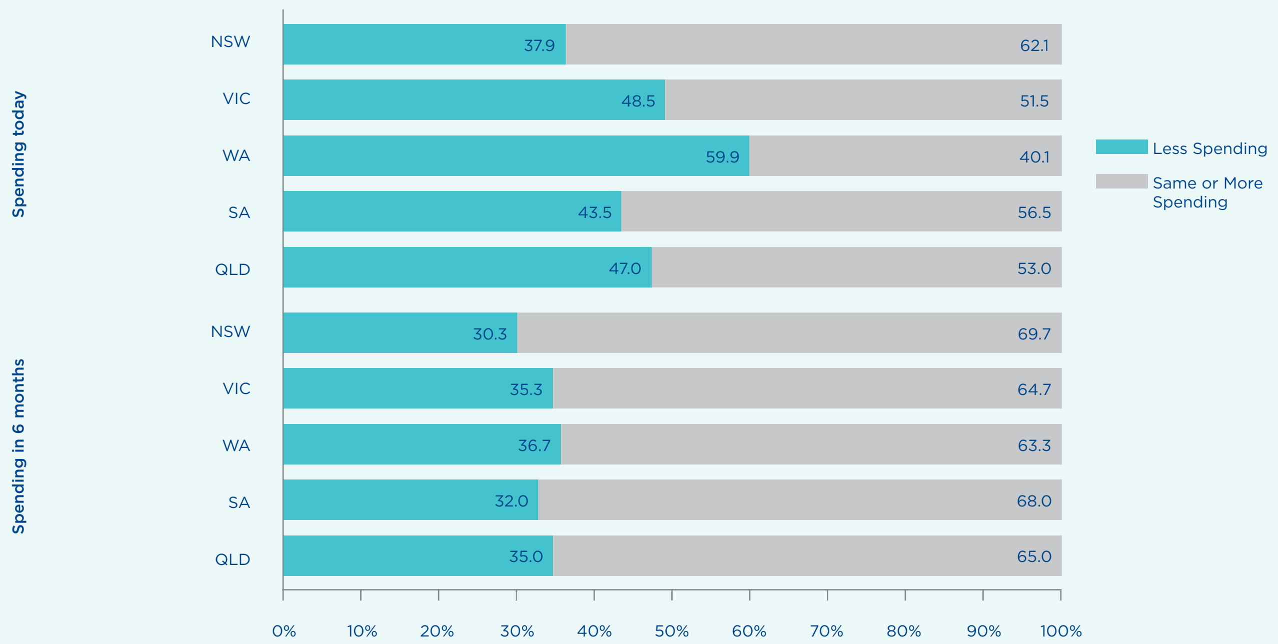


4 People who cut spending and expect to further reduce spending are spread across all States.

COVID-19 has affected spending of many Australians across all States. The proportion of residents spending less than the beginning of the year ranges from 37.9% in New South Wales to 59.9% in Western Australia. The proportion of residents expecting to spend less than pre COVID decreases but remains substantial across all States. It ranges from 30.3% in New South Wales to 36.7% in Western Australia. COVID-19 is not affecting all States in the same way.

Victoria is experiencing a second COVID-19 wave and announced a new lockdown on 8 July. As economic activities in the hospitality, tourism, recreational and entertainment sectors have been restricted further for six weeks, it is likely that spending in Victoria will drop. Spending in other States will be dependent on the local evolution of COVID-19. If they are not hit by a second wave and the economy re-opens as planned, spending will slowly recover.

Figure 5: Spending today and expected spending in 6 months by State



Policy Conclusions

Policies to sustain spending

Household consumption expenditure is the main component of the Australian GDP and a key driver of an economic recovery. High consumer spending creates opportunities for businesses generating more employment. Since the lockdowns in March, the Government has implemented policies that protect income and sustain spending. The JobSeeker Coronavirus supplement and the JobKeeper payment were thought to offer additional income support to people on low incomes and employees who would otherwise have been unemployed. The two measures have prevented consumption expenditure dropping to even lower levels than they are now.

Governments are facing challenging times. To boost spending and support the economic recovery, they may be tempted to reopen the economy and lift restrictions quickly. However, If the loosening of restrictions is not managed carefully, the COVID-19 virus could spread further and the healthcare system placed under pressure.

Getting COVID-19 under control

Experience has shown that the number of infections grew exponentially in countries that did not impose tight restrictions. They are also struggling to control the spread of COVID-19. If many economic activities are restricted, Australians have fewer opportunities to spend, resulting in consumption expenditure remaining lower than pre-pandemic levels. However, Australia may be better off in the longer term if the Government succeeds in controlling the spread of COVID-19 sooner than other countries. If Australia manages to keep the infection rate low, restrictions can be gradually lifted sooner and people may return to spending on goods and services which are currently restricted. In the meantime, it is pertinent that the Government look at implementing policies to protect income and support spending, particularly for those Australians experiencing financial distress.

Managing the JobSeeker Coronavirus supplement and the JobKeeper payment

The Government has announced an extension of the JobSeeker Coronavirus supplement and the JobKeeper payment from September 2020 to March 2021. The JobSeeker Coronavirus supplement will be reduced from $550 to $250 a fortnight, while the JobKeeper payment will fall from $1,500 to $1,200 a fortnight for people working 20 hours or more and to $750 for people working fewer than 20 hours. From January to March 2021, the JobKeeper payment will be further reduced to $1000 a fortnight for people working 20 hours or more and to $650 for people working fewer than 20 hours. The extension of the two measures will be important to protect income of unemployed people and those who would otherwise risk losing their job. Reducing the payments, the Government will also avoid incurring excessive debt and encourage people into employment over reliance on Government payments. However, people remaining on JobSeeker and JobKeeper will likely reduce spending after September. The literature has shown that spending is more sensitive to income changes for individuals who cannot draw on savings and find borrowing difficult (Crossley and Low, 2014). To sustain spending of these people, the Government could offer payments that vary according to individuals' circumstances. For example, higher JobSeeker and JobKeeper payments could be offered to individuals on low- and middle-incomes who have children and need to pay a rent or a mortgage.

Could a temporary GST cut stimulus work in Australia?

Australia imposes a 10% value-added tax – the Goods and Services Tax (GST) – on most goods. Some food, medicines, medical services, education courses and childcare services are exempt. Some governments internationally have implemented a temporary cut of the value-added tax to boost consumer spending through price reduction. The United Kingdom cut the value-added tax in 2008 at the time of the Great Recession from 17.5% to 15% for a period of 13 months, generating an increase in the volume of retail sales by around 1% (Chirakijja et al., 2009, Crossley et al. 2014). However, the volume of sales fell when the cut ended. A value-added tax cut from 19% to 16% (and from 7% to 5% for essential goods) has also been announced in Germany as part of the COVID-19 stimulus package from July to December 2020.

Implementing a temporary GST cut in Australia would be more complicated than in other OECD countries. The GST revenues are redistributed by the Federal Government to each State and Territory. The effects of any GST cut would need to take into account what mechanisms could be put into place to ensure that State revenues do not suffer. The 10% GST in Australia is also at a lower rate compared to the 19.3% average rate in the OECD countries (OECD, 2018). This means that the potential boost to spending that might be generated by a cut would be more muted than what has been observed in other countries.

The advantage of a GST cut is that it can be implemented in many ways. The Government may decide the amount of the cut, the period of time in which the cut is implemented and the specific goods and services to target. This flexibility would enable the Government to strategically focus on the factors that are most likely to boost spending via a GST cut. There are, however, other caveats to consider:

- Prices for consumers may not change if retailers choose not to pass through the savings
- A GST cut could be considered regressive given some essential goods are already exempt from the GST
- A GST cut benefits all consumers of the goods affected by the cut. This includes those who would be purchasing the goods regardless of any tax cuts. We assume that because these consumer types would be benefiting from the cut through a lower price, they might use these savings to purchase other goods.
- The measure could be ineffective if it is implemented when many activities are restricted or attached to goods and services that are not available (e.g. travel, eating out).

Although it could stimulate consumer spending, cutting the GST should be considered as part of a package of relief measures. For example, a reduction in GST is not a substitute for income support to people on low- and middle-incomes who experience temporary income shocks.

Further Information

Datasets

This analysis has been drawn from *Taking the Pulse of the Nation* – Melbourne Institute's survey of the impact of COVID-19. The aim of the weekly survey is to track changes in the economic and social wellbeing of Australians living through the effects of the coronavirus pandemic whilst adapting to various changes in Federal and State government policies. The survey contains responses from 1200 persons, aged 18 years and over surveyed each week. The sample is stratified by gender, age and location to be representative of the Australian population.

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1 It should be noted that household expenditure of the first quarter of 2020 could have also been affected by the bushfires.