

DOMESTIC CONSUMPTION AND HOUSEHOLD ECONOMIES

Tae-Yol Lee
(tylee@hri.co.kr)

The severe depression known as the IMF era has shaken the economic base of Korean families. Economic indicators related to households such as wages, unemployment, and inflation have terribly deteriorated. In 1998, the unemployment rate reached 6.8%, the highest level since 1966. The nominal wage growth rate dropped to a negative number for the first time ever. In addition, the inflation rate of 7.5%, the highest since 1991, put a heavy burden on consumers' tight budgets. The recently released 「The Family Income and Expenditure Survey」 of the National Statistical Office confirmed how serious the slump of the average household economy has been since the currency crisis broke out.

Income and Consumption Depressed

The average monthly income of salary and wage earners' households was 2.1 million won, which is lower than that of 1997 by 6.7%. Considering the inflation rate of 7.5%, the growth rate of real income was a more painful -14.2%. The decrease of income mainly comes from the drop in earnings of secondary family members (-10.7%), rather than that of the family head (-3.2%). The average number of earners per family also decreased to 1.48 from 1.57 in 1997.

The decrease of consumption was even more profound than that of income, with consumption

Table 1. Monthly Expenditures In "Salary and Wage Earners' Households" 1998

	Amount (thousand won)	% of total	Increase rate(%) (nominal)	Increase rate(%) (real)
Consumption Expenditure	1,297.9	100.0	-10.7	-17.4
Food and beverages	357.9	27.6	-14.3	-21.8
(dining out)	122.5	9.4	-23.0	-26.8
Housing	45.8	3.5	-8.0	-10.0
Fuel, light and water charges	70.6	5.4	8.2	-18.9
Furniture and utensils	50.6	3.9	-17.3	-23.2
Clothing and footwear	70.5	5.4	-26.4	-29.4
Medical care	57.7	4.4	-11.2	-15.8
Education	139.3	10.7	-6.8	-10.1
Culture and recreation	58.7	4.5	-22.6	-25.2
Transportation and communication	188.9	14.6	-0.9	-13.6
(Personal Transportation)	103.4	8.0	-4.8	-17.9
Other	257.9	19.9	-9.0	N/A

Source: National Statistical Office

expenditures falling by 10.7%. This decrease was most prominent in expenditures for clothing and footwear (-26.4), culture and recreation(-22.6%), and dining out (-23.0). The extent of decrease in expenditures for education, housing, and transportation & communication were relatively mild, being -6.8%, -8.0% and -0.9%, respectively. Most likely, these items were considered as being more of a necessity than the former ones. Despite the sharp overall decrease of consumption, the expenditures on fuel, light & water charges increased by 8.2%. However, this increase stems from price hikes, which averaged 25.1% for 1998. Real consumption expenditures on these items actually decreased by about 13%. In real terms, most of the consumption items show double-digit decreases. Clothing & footwear yielded the steepest drop, being almost 30%.

Weak Confidence in Future

According to consumption theory, consumption tends to be inelastic to transitory income change. This means that the savings rate gets higher in booming periods and lower in slumps. As mentioned above, however, consumption shrank more than income did such that the saving rate moved up to 31.5%, the highest level ever and up from 29.6% a year ago. This is a very exceptional phenomenon. Current consumption is generally decided by attitudes on the current and future economic conditions of a household. The only possible way to explain the recent movement of the savings rate is to assume that households have lost confidence about not only the current economic situation but also future expectations.

Recovery by Whom and from Where

Recently domestic consumption has been showing signs of recovery, in spite of the severe depression of households' economy last year. The question is, who is going to increase which part of consumption? Most likely, the upper income class will lead the increase in consumption. Given the expectation of no significant wage increases, this is the only group who can afford more consumption. The upper 20% income households experienced just a 0.3% income decrease. In contrast, the lower 20% income household registered a 17.2% drop. Notwithstanding the deeper income inequality, the consumption decrease rates are relatively flat across the different income levels. This means that the upper income class saved more last year so that it can increase its consumption as soon as it recovers confidence about future.

The recovery of consumption will probably come in areas which were hit the hardest by the economic depression. Clothing & footwear, culture & recreation, furniture & utensil and dining out will be major candidates for rebounds. They experienced growth rates of -20.0% or worse last year. These huge drops were probably caused by the sudden shock rather than a structural change in preferences.

Given the above-mentioned factors, the ongoing recovery of domestic retail market will be led by the upper income class and temporary rebounds of a few categories of consumption. However, long-term consumption recovery depends on how much better off the economic foundation of the middle and low income households will be. **VIP**

Table 2. Cross-Sectional Income and Consumption of Households

	Average	Bottom 20%	20-40%	40-60%	60-80%	Top 20%
Income (growth rate)	-6.7	-17.2	-11.8	-9.9	-8.0	-0.3
Consumption (growth rate)	-10.7	-11.5	-12.5	-11.1	-9.5	-10.2