

Box 6

RECENT TRENDS IN HOUSEHOLD REAL DISPOSABLE INCOME

Following a protracted period of decline, real household disposable income in the euro area posted its first positive annual growth in the fourth quarter of 2013, increasing by 0.6%, compared with a fall of 0.3% in the third quarter. Among the key factors contributing to the improvement were the increases in the compensation of employees and in net property income earned.

The recent slowdown in consumer price inflation has also had a positive impact on the latest developments in real household disposable income.

Household disposable income increased recently

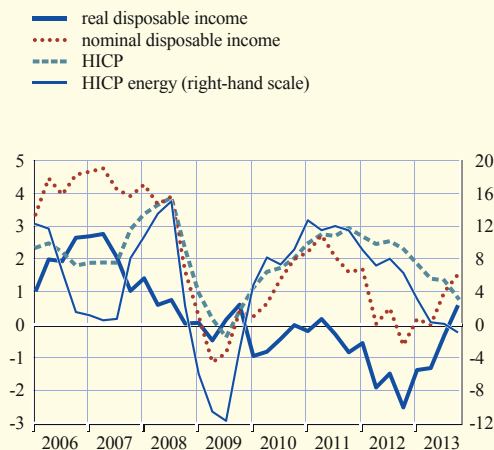
After an extended period of negative or stagnant developments in both nominal and real household disposable income, the former returned to positive growth in the course of 2013. The annual growth rate in euro area household nominal disposable income stood at 1.5% in the fourth quarter of 2013, compared with 1.0% in the third, benefiting from the recovery in real GDP (see Chart A).

Owing to the protracted fall in employment and the negative or subdued developments in real wages, real household disposable income in the euro area had been on a downward trend from the first quarter of 2010 to the third quarter of 2013, when it stood 2.5% below its value in the third quarter of 2009. However, supported by positive developments in the main components of gross income and a less negative effect from direct taxes, as well as by the slowdown in consumer price inflation, the annual growth rate of real household disposable income has recently been positive, increasing by 0.6% in the fourth quarter of 2013.

The strengthening of nominal gross disposable income growth in the fourth quarter of 2013 mostly benefited the household sector through an acceleration in the compensation of employees (with its positive contribution to the growth in disposable income increasing by 0.4 percentage point), a higher contribution stemming from the property income earned and net social benefits (with the respective contribution increasing by 0.1 percentage point). These, coupled with a less negative effect from direct taxes (by 0.2 percentage point), more than offset the smaller positive contribution from the gross operating surplus and mixed income¹ (by 0.2 percentage point) and the marginally lower net interest income in the context of overall low interest rates (see Chart B).

Chart A Euro area household disposable income, HICP and HICP energy

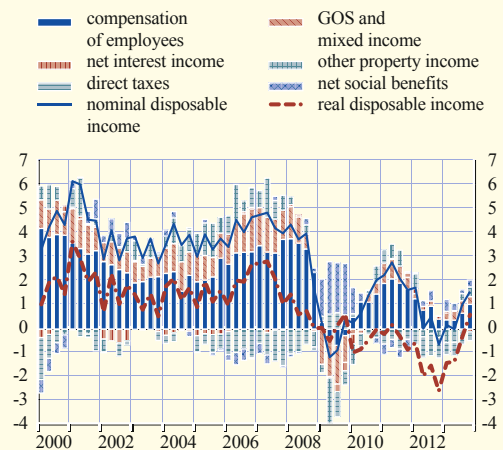
(year-on-year percentage changes)



Sources: Eurostat and ECB calculations.

Chart B Household disposable income and components

(year-on-year growth rate; percentage point contributions)



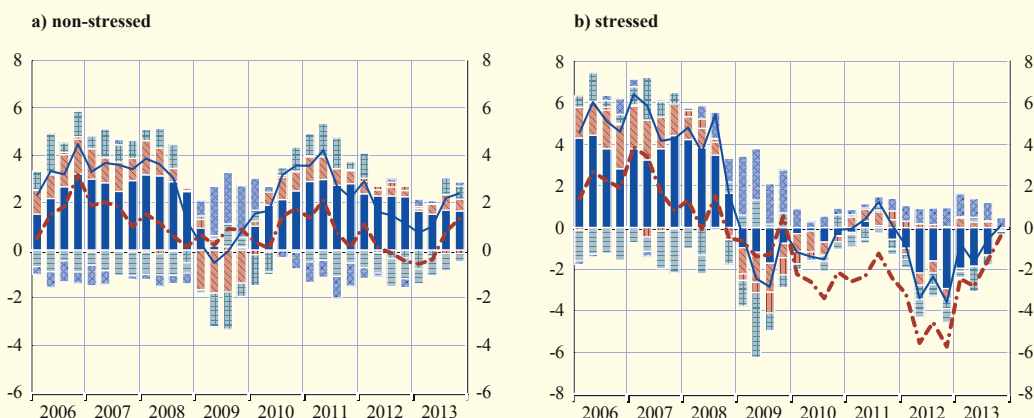
Source: Eurostat and ECB calculations.

¹ The main components of household gross operating surplus and mixed income are profits of self-employed business owners and imputed rental income from owner-occupied housing.

Chart C Household disposable income and components in stressed and non-stressed countries

(year-on-year growth rate; percentage point contributions)

■ compensation of employees
■ net interest income
■ direct taxes
■ nominal disposable income
■ GOS and mixed income
■ other property income
■ net social benefits
■ real disposable income



Sources: Eurostat and ECB calculations.

Notes: National quarterly sector accounts data are not available for all euro area countries. Thus, the aggregate for non-stressed economies refers to Germany, France, the Netherlands, Austria and Finland, and that for stressed economies to Italy, Spain, Greece, Ireland, Portugal and Slovenia.

In addition, the slowdown in consumer price inflation accounted for approximately 40% of the recovery in real household disposable income. Euro area HICP inflation has gradually fallen from the elevated levels observed in late 2011. The decline in euro area inflation has to a large extent been driven by external factors such as lower energy and commodity prices and exchange rate developments. The purchasing power of households has also been strengthened by these factors which, other things being equal, should support consumption.

Heterogeneous patterns at country level

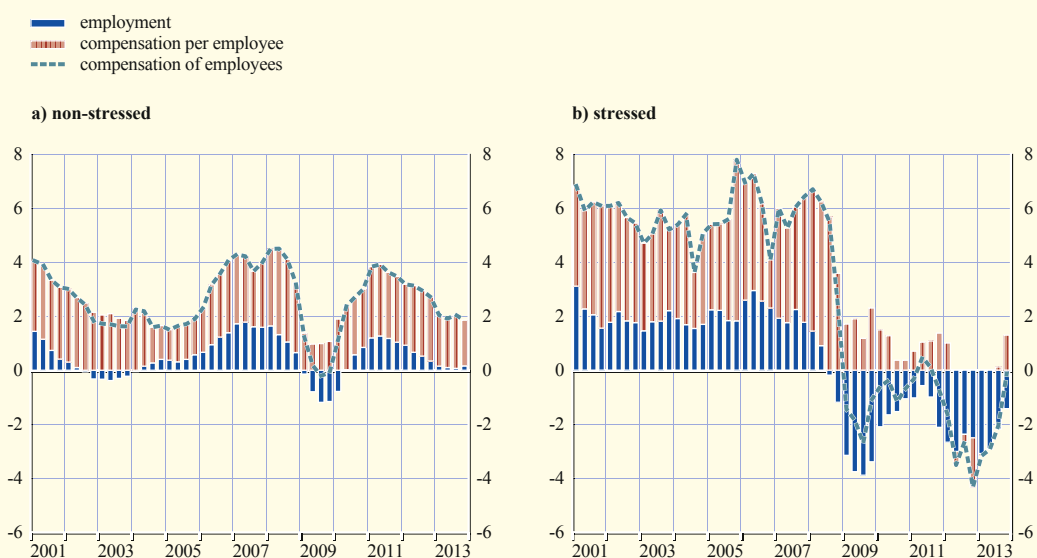
Across countries, patterns have been markedly different. Non-stressed countries (namely Germany, France, the Netherlands, Austria and Finland²) have experienced solid growth in household disposable income since 2010, while stressed countries (namely Italy, Spain, Greece, Ireland, Portugal and Slovenia) experienced a protracted decline in income from 2009 until the third quarter of 2013. This decline was only briefly interrupted by gross operating surplus and mixed income-driven increases between the second and fourth quarters of 2011 (see Chart C). In these stressed countries, nominal cost rebalancing was supported by a downward adjustment of wages in 2012 and only a moderate increase at the end of 2013.

Recently, household disposable income in stressed countries has shown signs of stabilisation, with nominal income growth turning positive in the fourth quarter of 2013 for the first time since the end of 2011, driven by the fact that the large negative contributions from the compensation of employees and property income came to an end. Although the pace of the decline in real

² Note that national quarterly sector accounts data are not available for all euro area countries.

Chart D Employment and nominal compensation in stressed and non-stressed countries

(year-on-year growth rates)



Sources: Eurostat and ECB calculations.

Notes: National quarterly sector accounts data are not available for all euro area countries. Thus, the aggregate for non-stressed economies refers to Germany, France, the Netherlands, Austria and Finland, and that for stressed economies to Italy, Spain, Greece, Ireland, Portugal and Slovenia.

household disposable income in stressed countries has slowed sharply since the middle of 2013, its growth was still slightly negative in the fourth quarter of 2013 (-0.4% on an annual basis).

Breaking down labour income developments into contributions of employment and wages (compensation per employee) shows that this stabilisation of income in stressed countries at the end of 2013 resulted from a significant slowdown in the decline in employment and an increase in nominal wages (see Chart D). Nevertheless, the increase in compensation per employee in stressed economies on an annual basis is also driven by a base effect, reflecting the unwinding of measures taken in some countries in 2012. Hence, the rebalancing within the euro area, i.e. the remaining competitiveness adjustment needs, might not be over yet. This is also suggested by recent analysis from a sectoral perspective of the ongoing current account rebalancing within the euro area³.

Labour cost adjustment in stressed countries improving competitiveness

The pattern of a protracted decline in labour costs in stressed countries from 2009 to 2013 may in fact have lent support to developments in overall income in the medium term. In spite of the direct negative impact on household income from the downward wage adjustment between the second quarters of 2012 and 2013, the decline may have helped to avoid an even stronger fall in employment. Furthermore, by helping countries to regain competitiveness, the adjustment is likely to have prevented a more prolonged decline in household disposable income. Similarly,

³ See the boxes entitled “Sectoral contributions to rebalancing within the euro area”, *Monthly Bulletin*, ECB, December 2013, and “To what extent has the current account adjustment in the stressed euro area countries been cyclical or structural?”, *Monthly Bulletin*, ECB, January 2014.

such nominal adjustment may also have supported the deleveraging process by mitigating the job losses. Available evidence shows that deleveraging in the private non-financial sector is taking place⁴. Notably, it seems to have proceeded faster in those countries where debt accumulation was greater in the run-up to the crisis and the impact of the crisis was more severe.

Conclusion

Following four years of declines, real household disposable income in the euro area increased in the fourth quarter of 2013. The weak trend in euro area household disposable income in recent years reflects heterogeneous patterns at country level. Positive developments in the main income components at the end of 2013 which benefited from the recovery in real GDP were coupled with a slowdown in consumer price inflation. In particular, low energy and commodity prices are strengthening the purchasing power of households and, other things being equal, should support consumption going forward. A continued recovery in real disposable income growth should help to strengthen household balance sheets (i.e. it would allow households to further reduce their indebtedness) and may provide an additional boost to private consumption. Signals of this may already be reflected in the recent rise in consumer confidence and retail sales.

⁴ See the boxes entitled “Integrated euro area accounts for the fourth quarter of 2013”, *Monthly Bulletin*, ECB, May 2014, and “Deleveraging patterns in the euro area corporate sector”, *Monthly Bulletin*, ECB, February 2014.