Macro Vision

May 13, 2024

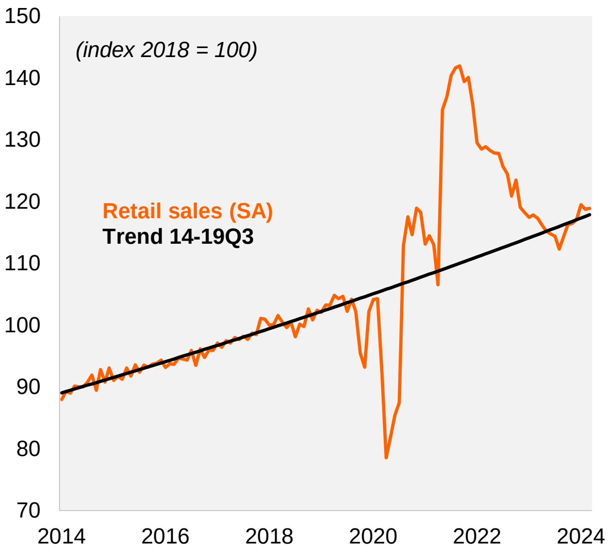
CHILE – Retail Sales: The only way is up! right?

- In January real retail sales grew in annual terms for the first time in nearly two years. This improvement suggests the post-COVID adjustment might have finally turned the corner… however, we are not necessarily back to normal. Some fundamentals for consumption locate us in a less auspicious situation than prior to the pandemic and it is unclear whether the labor market has experienced a permanent decrease in participation.
- Our analysis suggests that the fundamentals behind retail sales are at or close to their sustainable growth path. In this context, because of compositional changes in employment and the implementation of the Universal Guaranteed Pension (PGU), there will be enough support for real retail sales to grow about 2% this year in line with our view of a gradual private consumption-led recovery.

The party is long over…

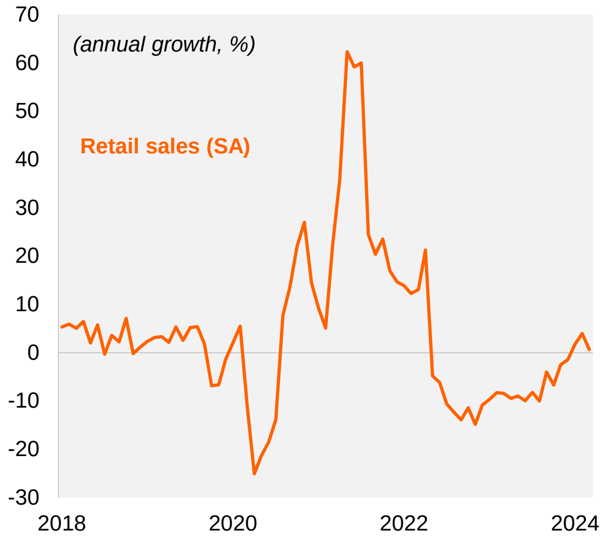
The liquidity injections that started in 2020 provided more than enough resources for families to avoid the economic hardships brought on them by the pandemic. In fact, the combination of pension fund withdrawals and universal cash transfers among others reached 25% of GDP by 4Q21, by far exceeding household support measures in any other economy. As a result, there was an evident decline in consumer loans and a catchup in late payments but also an explosive increase in consumption, particularly of durable goods. This unprecedented expansion in retail sales began in May 2021, triggered by the re-opening of the economy, following the swift vaccination process, and fueled by an unparalleled flood of cash to households from the third pension fund withdrawal and the universal cash transfers. As a result, retail sales growth in May 2021 escalated to a whopping 62% YoY peaking in 3Q21 at 28% above the pre-covid trend. The descent followed shortly, leading to annual contractions between May 2022 and December 2023.

Real Retail Sales



Source: National Statistics Institute (INE)

Real Retail Sales



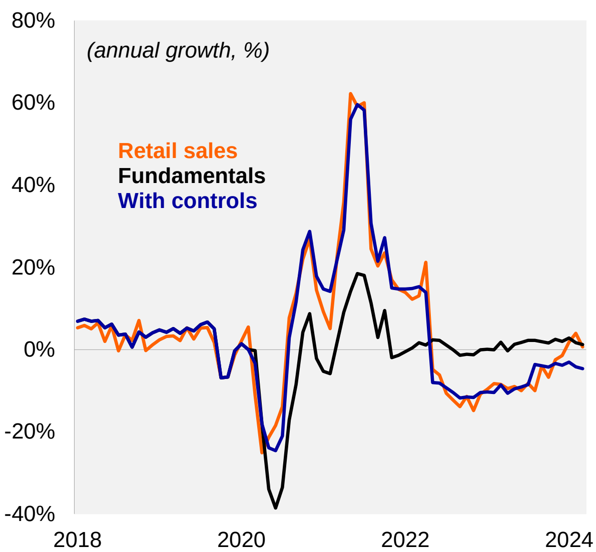
Source: INE

… maybe the hangover is over too.

As of the last three prints, January, February and March 2024, real retail sales showed positive annual prints and levels roughly in line with the pre-pandemic trend. Although this appears to be a promising start to the year, it is not obvious whether the improvement will continue. Why? Well, our analysis shows that retail sales during the last three years have been driven more by consumer preferences and available supply rather than by traditional fundamentals like earnings, employment, and credit. Currently, the level of consumption that may be supported by the latter is still unclear.

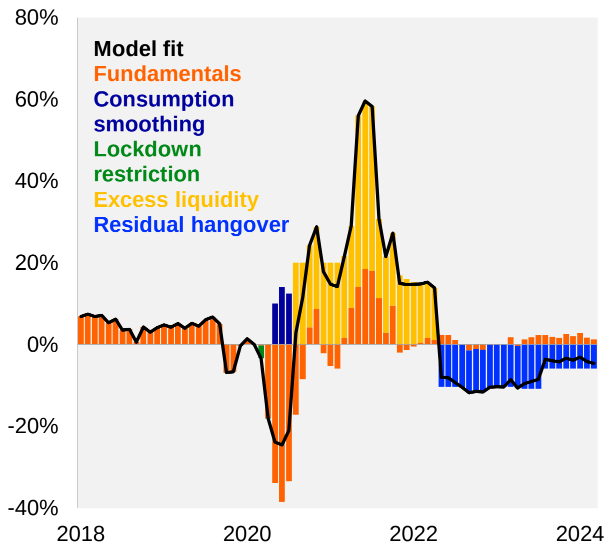
To provide some insight into this issue, we turn to a model based on fundamentals, composed by employment, real wages, consumer credit and consumer sentiment, that is estimated prior to the pandemic, and we compare the predicted values with the actual prints. We then add additional controls to derive the magnitude of the effect of the liquidity injections on this variable and back out how we expect it to be affected in the near future.

Retail sales model



Source: Own calculations based on data from INE

Contribution of main drivers



Source: Own calculations based on data from INE

Recapping the events in order, COVID hit Chile in mid-March 2020 with retail sales falling because of the mobility restrictions. Then came a sharp drop motivated primarily by a loss of employment, driving the real wage bill down. In fact, the actual prints were somewhat better than predicted by the model, which may be attributed to consumption smoothing but could also be explained by the heterogeneous loss of employment among income-groups. At the end of July of 2020, a first pension fund withdrawal was approved, increasing retail sales annual growth by approximately 20pp., that was followed by a second withdrawal in December of 2020. In May 2021, although employment was already recovering, a third withdrawal took place accompanied by state-financed universal cash transfers, and mobility restrictions in the economy eased, increasing retail sales growth by an additional 20pp. As a result of the unsustainable levels of consumption as of May 2022 subsequent contractions followed for nearly two years. Based on the model's prediction at the height of sales growth, two thirds of the 60% increase were due to the liquidity injections and around 10pp. of the subsequent contractions was a consequence of the high base of comparison.

So… is retail sales growth here to stay?

As of November 2023, the actual data prints have been stronger than predicted by the model that accounts for the carry-over of the high base of comparison. This is somewhat puzzling given that related indicators have continued to deteriorate. Credit growth is slacking and consumer non-performing loans are at their highest level in a decade. Also, real wage growth is returning to historical levels and consumer sentiment remains low. All this suggests there is little space to support a further improvement in retail sales by other means than income coming from employment which has remained stubbornly below pre-pandemic trend levels. Although this could be a source for additional contractions, given that current sales could still be above sustainable levels, we believe that there has been a permanent change in the labor market that might even provide some additional boost.

We estimate that by the end of 2023 employment was around 290 thousand jobs below the pre-pandemic trend. However, all the gap is concentrated in workers aged 55 years and over, and proportionally more for the older workers. It is likely that the foregone income from these workers was compensated by the Universal Guaranteed Pension (PGU) program that was implemented in January 2022 and will continue to be onwards. The PGU broadened the coverage of state-financed pension payments to those aged above 65, excluding the 10% highest earners, reaching up to 2.4 million people, while raising benefits. Since then, the program's coverage has increased further. Supporting this view is the fact that the gap is also present in the workforce by age-group. Also contributing to the apparently large employment gap is the reduction among young workers that is also well below its pre-pandemic levels, over 100 thousand, but this is more likely to be a consequence of a negative trend that started over a decade ago and became more pronounced with the implementation of free tertiary education for lower income families. All this suggests that aggregate household income is not as far below as its pre-pandemic trend as the aggregate gap in employment would imply.

In this context, if workforce participation and employment continue to recover at their recent pace and other fundamentals follow their recent trends, we expect real retail sales to grow around 2% in 2024. Although this number is somewhat below the recent trend of 2.8%, we believe it is consistent with our view of a gradual private consumption-led recovery which would be broadly neutral on inflation (That is, it is unlikely to be a source of demand-driven inflationary pressures or deflationary relief on the prices of tradable goods). There are, however, sources for higher prints. One is that there is still some space for a quicker increase of employment. Another is that greater retail sales growth could arise from the recent rise in tourism from Argentina (+13% YoY in 1Q24), that purposefully travel with the intention of acquiring certain goods that are not available or much more expensive back home. Finally, with municipal elections drawing nearer (October 27, 2024), there have been some voices supporting new pension fund withdrawals that, if approved would undoubtedly add fuel to consumption.

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Marcus Cobb C.

Annex

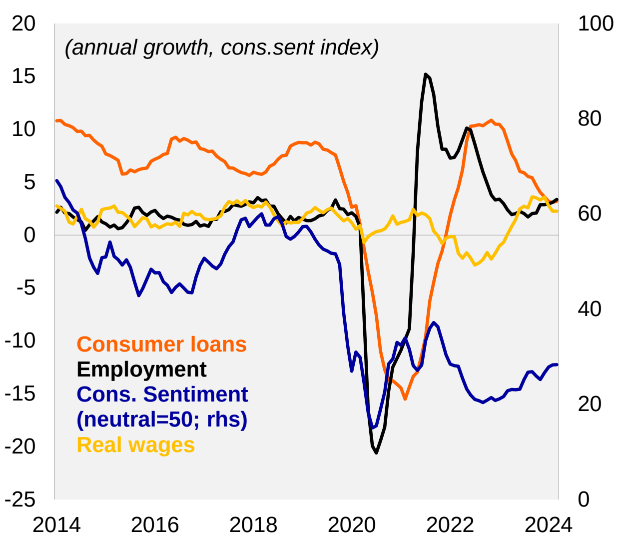
Fundamentals model: Retail Sales YoY growth

	Estimate	Std. Error	t value	Pr(>|t|)	
(Intercept)	-0.21	0.05	-4.03	0.000	***
cons.loans (-1)	0.12	0.05	2.56	0.012	*
employment	1.71	0.27	6.33	0.000	***
employ (-3)	-0.68	0.23	-3.01	0.003	**
cons. sentiment (-1)	0.00	0.00	3.63	0.000	***
realw	0.62	0.17	3.75	0.000	***
Controls:					
monthly working days	0.01	0.00	3.08	0.002	**
2010.3 (earthquake)	0.09	0.01	8.32	0.000	***
2019.10 (social unrest)	-0.12	0.03	-4.27	0.000	***
2019.11 (social unrest)	-0.10	0.03	-3.84	0.000	***

Signif. codes: 0 ‘***’ 0,001 ‘**’ 0,01 ‘*’ 0,05 ‘,’ 0,1 ‘ ’ 1

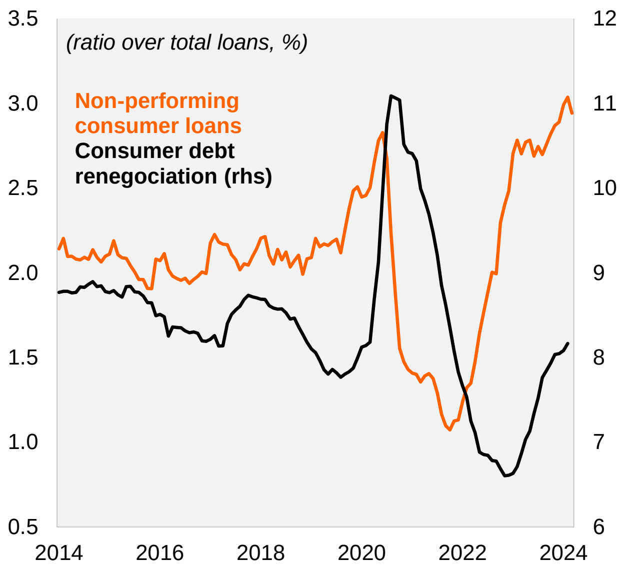
Residual standard error: 0,02701 on 155 degrees of freedom
Multiple R-squared: 0,7623, Adjusted R-squared: 0,7485
F-statistic: 55,24 on 9 and 155 DF, p-value: < 2,2e-16

Fundamentals



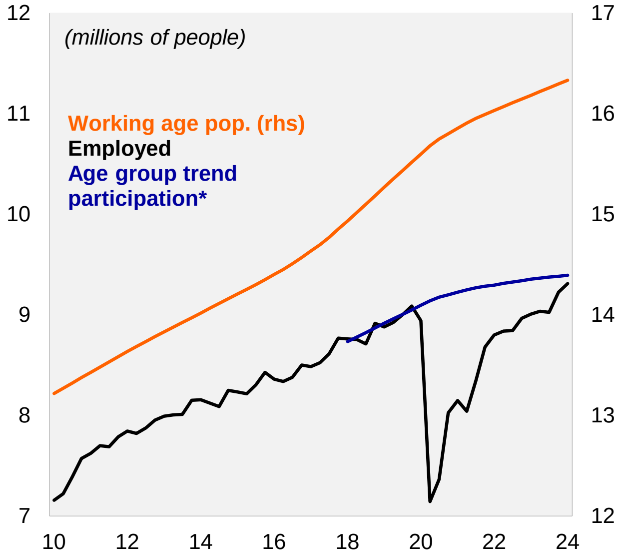
Source: CMF, INE, GfK.

Credit indicators



Source: CMF

Employment



Source: INE

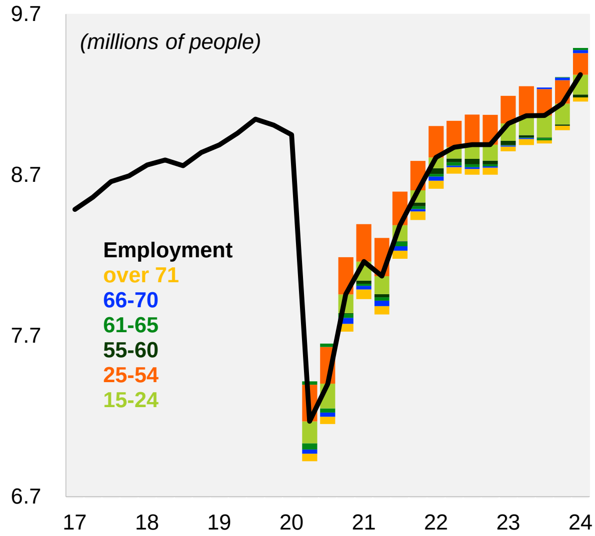
Employment gap by age group in 2023		
(with respect to age group trend)*		
Age group	n° people (thous.)	% employed
total	**297**	**3.3**
15-24 **	-1	0.0
25-54	71	1.1
55-60	77	8.2
61-65	51	9.5
66-70	38	14.5
over 71	51	34.1

*based on ratio employ./population

**only group to shows negative trend

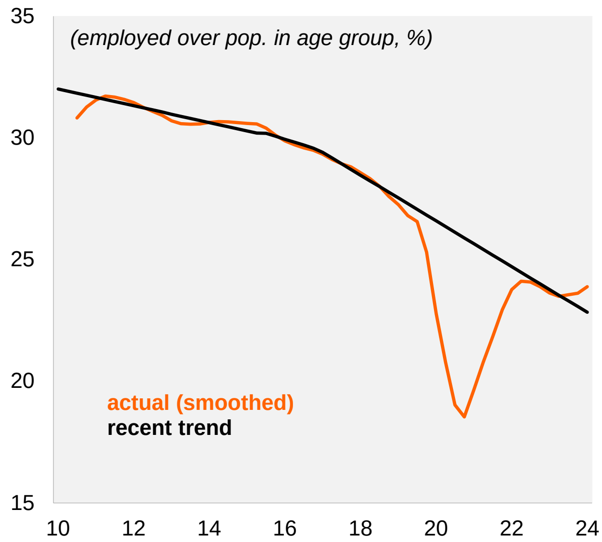
Source: INE

Composition of employment



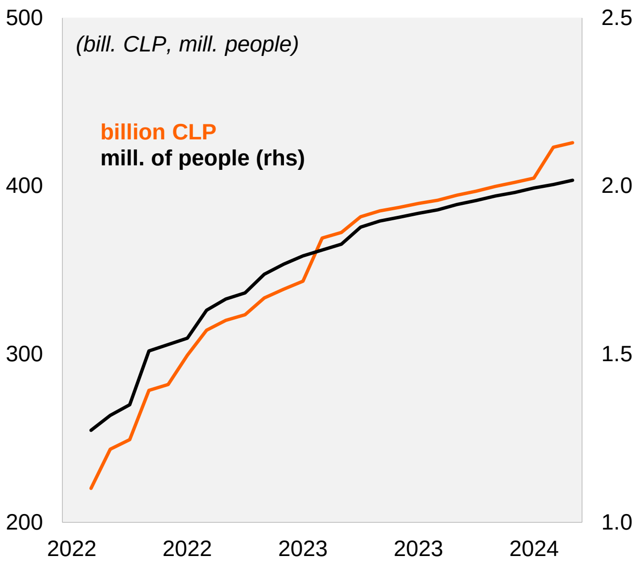
Source: INE

Employment 15-24 age group



Source: INE

Beneficiaries of PGU



Source: Pensions Superintendence

Macro Research – Itaú

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