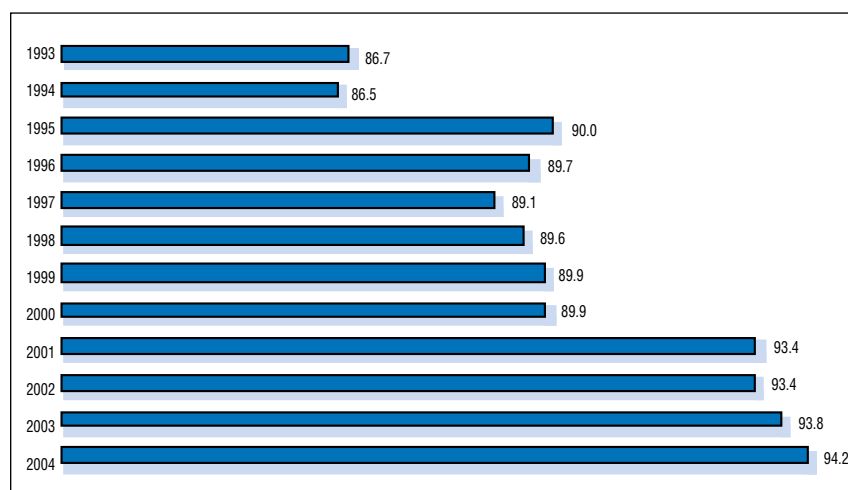


# INTERNATIONAL COMPARISON OF THE PROPENSITY TO CONSUME IN THE HOUSEHOLD SECTOR

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A general trend around the world in the past two decades has been a permanent growth in the preference for consumption, even in countries with a traditionally high rate of saving, for example, Japan. The preference for consumption over savings may be measured by the propensity to consume, which is expressed as that part of incomes available to households over a current year that is spent on purchases of consumer goods and services; the remainder becomes a part of savings. While in 1993 Slovak households spent 87% of their disposable incomes on consumption, in 2004 the figure was already 94%.

**Graph 1 Propensity of Slovak households to consume in % of disposable income**



Source: Statistics Office of the Slovak Republic, own calculations

The propensity to consume is a result of the development of both income and consumption, it is thus influenced by the definition of income and consumption in the household sector. In analysing the development of the propensity to consume among households and in its international comparison, we need to take account of at least the following descriptions applicable in Slovak statistics, which use the ESA 95 national accounting principles.

The household sector (S.14) in the national accounts terminology covers not only households as consumers, but also the households of owners of unincorporated businesses, meaning private individuals not entered in the commercial register, private individuals conducting business on a basis other than that provided by the Free Traders Act, and independent smallholders not entered in the commercial register. The household sector thus inclu-

des also free traders and small businesspersons (their definition is not unified in all countries). It does not include non-profit institutions serving households (as is the usual practice in some other countries).

By consumption we understand expenditure on the final consumption of households, i.e. on products and services used for the direct satisfaction of individual needs, housing services for homeowners, incomes in kind, materials and works connected with small repairs, objects of long-term consumption not deemed gross fixed capital, financial services and fees, payments for licences

and the purchase of production at economically insignificant prices.

(Some countries calculate the propensity to consume on the basis of actual consumption, i.e. including services provided to households free of charge).

Income is defined as gross disposable income (current incomes minus current expenditure). Gross disposable income is then that part of households' current incomes (wages, wage compensations, interest received, social benefits, etc.) remaining to households after the settlement of current expenditure (taxes, insurance contributions, etc.). Gross disposable income

is an own source for financing consumption or the accumulation of savings. Savings as the residual variable following the deduction of consumption expenditure from disposable income are a gross indicator, i.e. including the consumption of fixed capital. (Some countries record net indicators, i.e. excluding the consumption of fixed capital).

In calculating consumption and income, a national concept is used. Expenditures of Slovak households are monitored in the domestic territory and abroad; likewise the income of Slovak households is ascertained from domestic and foreign sources. The resultant share of consumption in disposable income is the propensity to consume according to the national concept.

An international comparison of the propensity to consume is made difficult by the lack of a comprehensive and consistent database for the household sector. One of



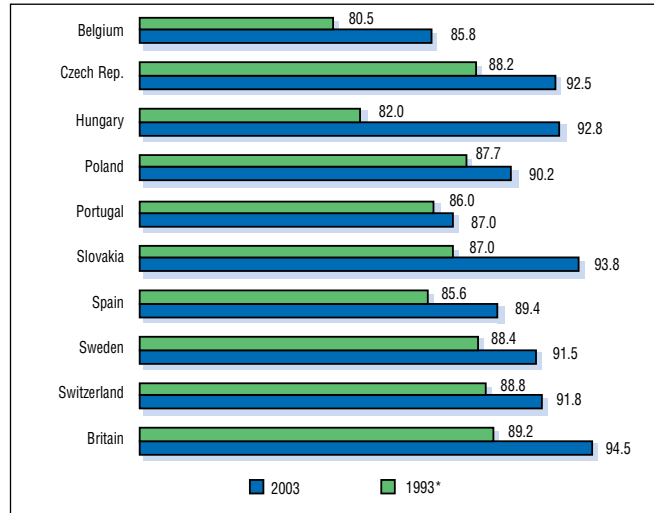
the most extensive databases available, published by the OECD, gathers data from the other side of household consumer behaviour, that of savings. The set of data on the propensity to save for the 21 statistically surveyed countries of the OECD was transformed into data on the propensity to consume (100 minus the propensity to save). The database gained was expanded to include current data from national statistics offices for four central European countries: the Czech Republic, Hungary, Poland and Slovakia.

From the database of the 25 countries compiled in this way it was found that the propensity to consume in 2003 ranged from 86% to 107%, where two countries (Australia and New Zealand) spent on consumption more than 100% of their concurrently gained disposable income. The wide spread of the interval (almost 21 percentage points) however reflects not only differences in households' behaviour, but also differences caused by the statistical approaches in individual countries. It is problematic to differentiate authentic differences from methodological ones. The national understanding of the propensity to consume in individual countries is different and thus an international comparison of the indicator has limited predicative ability. National concepts differ in terms of their non-uniform definition of income, consumption, the household sector and other characteristics. For example, in the case of France the modified approaches to calculating the propensity to consume, and thereby the propensity to consume, can change the result by up to 10 percentage points, in the case of Slovakia according to the same modified approaches, by more than 15 percentage points.

From the compiled database for the 25 countries we can select a narrow group of 10 countries having a comparable method of calculating the propensity to consume: Belgium, Britain, the Czech Republic, Hungary, Poland, Portugal, Slovakia, Spain, Sweden, Switzerland. A common methodological feature is the use of the gross disposable income for the purpose of calculating the propensity to consume and an almost identical definition of final household consumption.

Graph 2 compares the levels and changes of selected national propensities to consume for the past decade. Over the period 1993 – 2003 the selected group of the 10 countries exhibited a clearly growing trend in their propensity to consume. The distribution of countries according to the propensity level also changed. In 1993 the distribution of countries was symmetrical (the same number of countries being found below and above the arithmetic mean of national propensities). In 2003 the distribution had taken on a left skew, most of the national propensities being found above the average of national propensities. The accelerated growth in the propensity to consume was characteristic for more than half the count-

**Graph 2 Comparison of the propensity to consume in selected countries**



\* Hungary and Portugal: 1995, Poland: 1999.

Source: OECD Economic Outlook database and national statistics offices of the SR, Czech republic, Hungary and Poland.

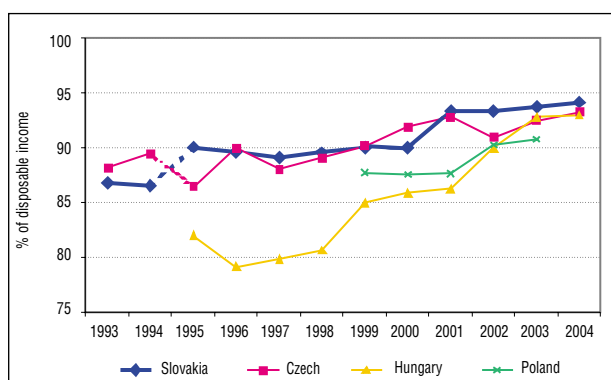
ries. Descriptive statistics in the tables below give the average values (mean, median), limit values of the national propensities to consume and Slovakia's position in comparison to the median.

At the outset of the transformation period Slovak households used 87% of their disposable incomes, which corresponded to the median for the selected countries. In 2003 however they already belonged to the more numerous group of countries, whose propensity to consume exceeded the median. In the case of Slovakia this excess represented more and 2 percentage points and the Slovak propensity to consume approached the upper limit of the interval (Table 1).

**Table 1 Descriptive statistics for a homogenous group of 10 countries with the propensity to consume (in %) from gross indicators**

	1993	2003	Change in propensity in 2003 against 1993
Mean	86.2	90.9	+ 4.7
Median	86.7	91.7	+ 5.0
Minimum	80.5 (Belgium)	85.8 (Belgium)	+ 5.3
Maximum	89.2 (Britain)	94.5 (Britain)	+ 5.3
Slovakia	86.7	93.8	+ 7.1
<i>Slovakia's position: against median</i>	<i>at median level</i>	<i>+2.1</i>	<i>+2.1</i>
Fastest growth in propensity to consume	from the level 81.9	to the level 92.8	Hungary +10.9

\*The European Countries: Austria, Belgium, Britain, Denmark, France, Germany, Holland, Ireland, Italy, Norway, Portugal, Spain, Sweden, Switzerland and the non-European countries: Australia, Canada, Japan, Korea, New Zealand, USA.


**Graph 3 Development of the propensity to consume in central Europe\***


Source: national statistics offices

\* interrupted lines indicate incomplete consistency of data in 1993 – 1994 with data in 1995 – 2004.

In the homogenous group of the 10 countries in 2003 Slovakia achieved:

- the second highest propensity to consume (after Britain) and concurrently,
- the second fastest growth in the propensity to consume (after Hungary).

If we narrow the selected group to the 4 central European transforming economies (Graph 3), Slovakia had, just ahead of the Czech Republic, over the long term the highest propensity to consume. The gap between the Slovak and other national propensities however has gradually been closing, with this being most apparent in the years 2003 – 2004.

With a high degree of simplification and with estimates of comparable data for the sector of Slovak households we can attempt to position Slovakia also in the group of the remaining 15 OECD countries. The comparison of national propensities to consume has reduced predicative ability, given the methodological non-uniformity in the calculation. The principal unifying methodological feature for the group is the calculation of the propensity to consume from net disposable income, which abstracts from the consumption of fixed capital. Likewise, data on household disposable incomes for Slovakia was cleansed of the estimated consumption of fixed capital in the house-

**Table 2 Descriptive statistics for a heterogeneous group of 16 countries with the propensity to consume (in %) from net indicators**

	1993	2003	Change in propensity in 2003 against 1993
Mean	90.0	95.5	+5.5
Median	89.4	95.6	+6.2
Minimum	79.2	88.9	+9.7
Maximum	100.2	106.5	+6.3
Slovakia (expert estimate)	90.8	98.5	+7.7
<i>Slovakia's position: against median</i>	+1.4	+2.9	+1.5

holds sector. The descriptive statistics of the heterogeneous group of 16 countries are in Table 2.

From the heterogeneous group of 16 countries it can be seen that:

- only six countries exceeded the level of the Slovak propensity to consume and concurrently,
- only in three countries did the propensity to consume grow faster than in Slovakia (Canada, Italy, Korea).

Following an overall evaluation of the individual development curves of the national propensities, without regard to the methodological approach used in calculating the propensity, it may be said that:

1. Over the past decade Slovak households have been among the fastest record holders as regards the rate of acceleration in consumer expenditure at the detriment of savings.

2. The speed of the increase in the Slovak propensity to consume was in the range of the transforming economies of the central European region.

3. Slovak households recorded a 6-year long persistence in the propensity to consume, untypical for transforming economies, where the database records only a couple of countries with a similar characteristic of conservative behaviour among households (examples are Germany and France).

4. Similar significant development breakpoints in the propensity to consume such as that in Slovakia in the years 1995 and 2001 appear in the database only exceptionally (most clearly in Hungary in 1992 and 2002, heading upwards, as in Slovakia).

From the national economic aspect the growth in the propensity to consume needs to be monitored for at least two reasons. On the one hand a high propensity to consume in a period of sufficient growth in disposable incomes increases consumption demand with possible impact in external disequilibrium (via imports of consumer goods on the current account in the balance of payments) or internal disequilibrium (via demand pressures for inflation). In a period of a significant fall in disposable incomes, persistence of a high propensity to consume can lower household wealth, should consumption be financed by an increase in liabilities and/or a reduction of assets acquired. Monitoring the propensity to consume in the household sector requires particular attention especially during a period of increasing liabilities in consequence of growing household debt. Significant asset losses in the household sector can threaten the financial stability of households as well as other sectors, such as the financial corporation sector in the case of a collapse in the repayment of insufficiently secured loans provided to households, or the general government sector by means of the necessitated increase in social expenditure.

On the other hand a high propensity to consume limits the creation of savings in the household sector. Savings



generated by the household sector are the basis of savings in the national economy. A weakening of the central position of the household sector in the creation of savings in the national economy can thus disturb the internal financial capacity of the whole economy. Savings as the unconsumed part of disposable incomes are, from the macroeconomic aspect, a synonym for investment. Investment financed from savings leads to the accumulation of capital. From the long-term aspect investment inc-

reases the potential product and creates a basis for future economic growth. Over the short term, investment increases aggregate demand, and thereby a growth in the gross domestic product. Theoretically, a country with a high rate of savings should be less sensitive to a sudden isolated slowdown in economic activity. In a small open economy this function of domestic savings while weakened, still must be monitored concurrently with the development of savings in other sectors of the economy.