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While luxury sales soar, economic headwinds begin to take their toll

Article

The trend: There's a growing split among the consumer behaviors exhibited among lower- and higher-income consumers.

- Rising prices are causing a growing number of consumers, particularly those who are lower-income, to **trade down to less expensive brands, forgo discretionary purchases, and cut back on saving.**

- Meanwhile, **higher-income consumers continue to spend**, with sales soaring among luxury brands.

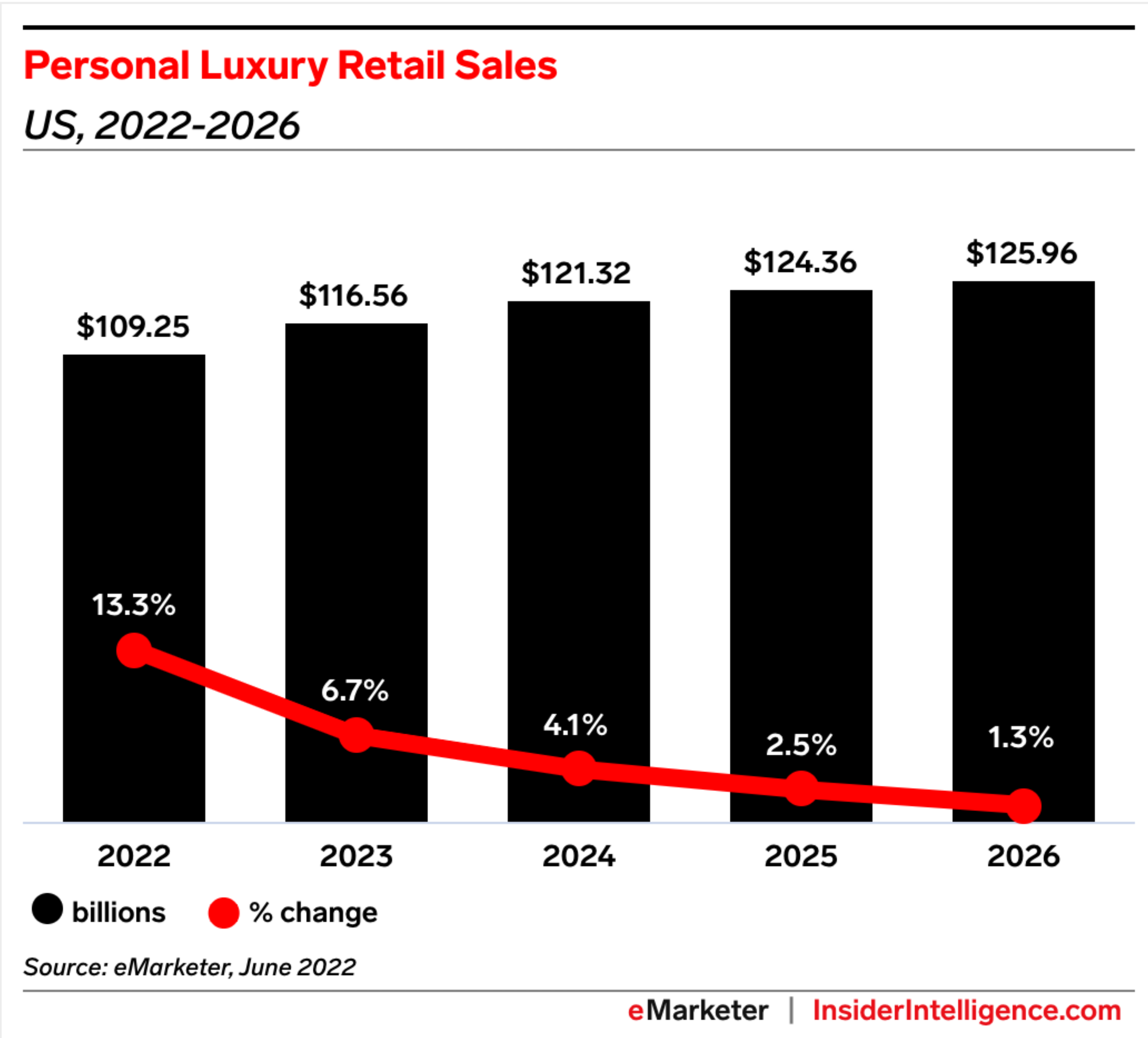
A difficult landscape: There are a host of indicators that suggest a challenging economic picture:

- **Prices continue to rise.** The personal consumption expenditures index, the US Federal Reserve's preferred inflation measure, grew 6.8% year-over-year (YoY) in June, or 4.8% when food and energy are excluded. Month-over-month prices jumped 1.0% from May (or 0.6% without food and fuel), the fastest increase in 17 years.
- **Consumers don't feel good about the economy**. Consumer sentiment is up just a tick from the historic low it hit in June, per the University of Michigan. And the Conference Board's consumer confidence index hit its lowest level since February 2021.
- **As a result, they're trading down to lower-priced options.** Store-branded food and beverages have a 21.6% share of overall spending in the category, which is up one percentage point in terms of sales dollars over the four weeks that ended July 10, per IRI as reported by The Wall Street Journal. That's higher than 2019 levels, and is helping drive growth at retailers such as **Albertson's** where store brands make up nearly 26% of the company's sales.
- **Spending is slowing.** Real spending adjusted for inflation grew just 0.1% in June as consumers barely kept pace with inflation, according to the US Bureau of Economic Analysis (BEA).
- **The overall US economy is shrinking.** US gross domestic product fell 0.9% at an annualized pace in Q2, per BEA. That followed a 1.6% decline in Q1 and was worse than Dow Jones' projected 0.3% gain.

But luxury sales continue to soar: While mass merchants such as **Target** and **Walmart** have warned investors that inflation is hurting their near-term outlook, wealthy consumers appear unfazed by the negative news.

- For example, **Hermès**' revenues rose 23% year-over-year in the first half of the year and its operating margin hit a record-high 42%.
- Similarly, **Kering Group**'s revenues grew 16% YoY, **LVMH Moët Hennessy Louis Vuitton**'s revenues grew 27% YoY, **Armani Group**'s sales grew 20% YoY, and **Richemont**'s revenues rose 42% YoY.
- We expect **US personal luxury retail sales to grow 13.3% to $109.25 billion** this year, thanks in part to **luxury retail ecommerce sales rising 39.7%**.

- There's also a **broader shift in spending** as a sizable segment of consumers are eager to eat out and travel: Spending on food services and accommodations rose 13.5% in Q2—a marked increase from 5.2% in Q1, per BEA.



Why it matters: While merchants that serve high-income consumers continue to be immune to the challenging economic climate, inflation is starting to have a significant impact on consumer spending. That's particularly true among lower-income consumers who are also likely to be hit hard by rising interest rates that make it harder to pay off credit-card loans and buy big-ticket purchases such as cars. That could stymie retail sales in the latter half of the year.

Go further: *For more on The Era of Uncertainty, read the report here.*