

2 Consumption of durable goods in the ongoing economic expansion

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Household spending on durable goods is the part of private consumption that is most sensitive to the business cycle. Private consumption encompasses

services, non-durable goods, semi-durable goods and durable goods. Durable goods typically have an expected lifetime of more than three years, whereas semi-durables and non-durables have a shorter lifetime.¹² Households do not derive utility directly from spending on durable goods in the current period, but rather from the flow of services they provide over their lifetime. As a result, the consumption of durable goods is more sensitive to the business cycle. Households may temporarily reduce these purchases when their income falls, without any great reduction in utility in the short term. When their income recovers, they can then resume their purchases again in order to offset earlier losses in their stock of durables.¹³ In addition, durable goods also have a greater tendency to be financed using credit, owing to their high unit value and their longer lifetime. The high unit value of durable goods means that current income may not be sufficient, so households may need credit to finance them. Moreover, owing to their longer lifetime, some durable goods can be used as collateral, which makes them easier to finance using credit. However, as credit standards are usually tighter during economic downturns and looser during expansions, this also makes them more sensitive to the business cycle.¹⁴ As a result, even though durable goods only account for around 10% of total consumption, they explain up to 20% of total variation in consumption growth owing to their greater variability.

Growth in the consumption of durable goods has been very strong in recent years. During the financial crisis, durable goods consumption contracted sharply (see Chart A), although the car scrappage schemes in several euro area countries provided some relief by encouraging purchases of new cars (e.g. in 2009). Since 2013, durable goods consumption has again grown vigorously, pushing up growth in overall consumption. The recovery observed in real disposable incomes and the easing of financing conditions have both boosted households' appetite for durable goods, particularly in those euro area countries that were more affected by the financial crisis.

¹² See the box entitled "[Recent developments in the consumption of durable goods](#)", *Economic Bulletin*, Issue 3, ECB, 2015.

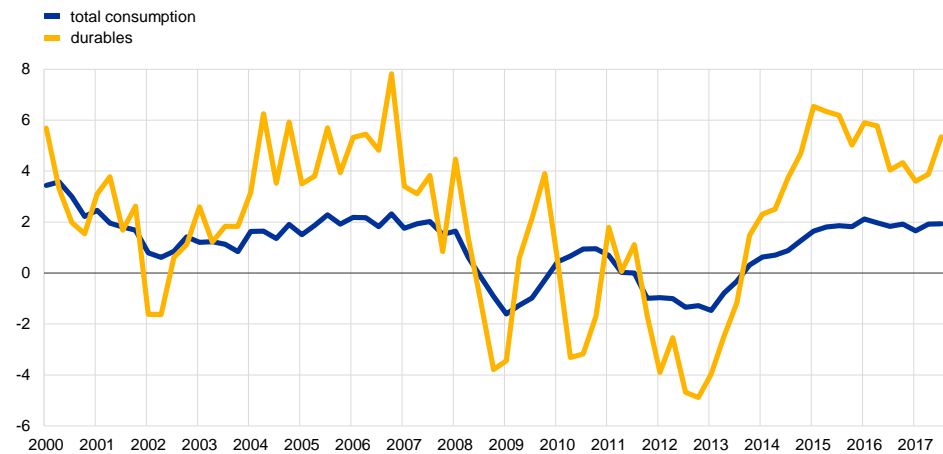
¹³ See Browning, M. and Crossley, T., "Shocks, Stocks, and Socks: Smoothing Consumption Over a Temporary Income Loss", *Journal of the European Economic Association*, Vol. 7, Issue 6, 2009, pp. 1169-1192.

¹⁴ See Chah, E., Ramey, V. and Starr, R., "Liquidity Constraints and Intertemporal Optimisation: Theory and Evidence from Durable Goods", *Journal of Money, Credit and Banking*, Vol. 27, Issue 1, 1995, pp. 272-287.

Chart A

Euro area private consumption

(annual percentage changes)



Sources: Eurostat and ECB calculations.

Notes: Total consumption relates to households and non-profit institutions serving households. Durables relate to households and are approximated using available data for all euro area countries except Belgium and Ireland. The latest observation is for the third quarter of 2017.

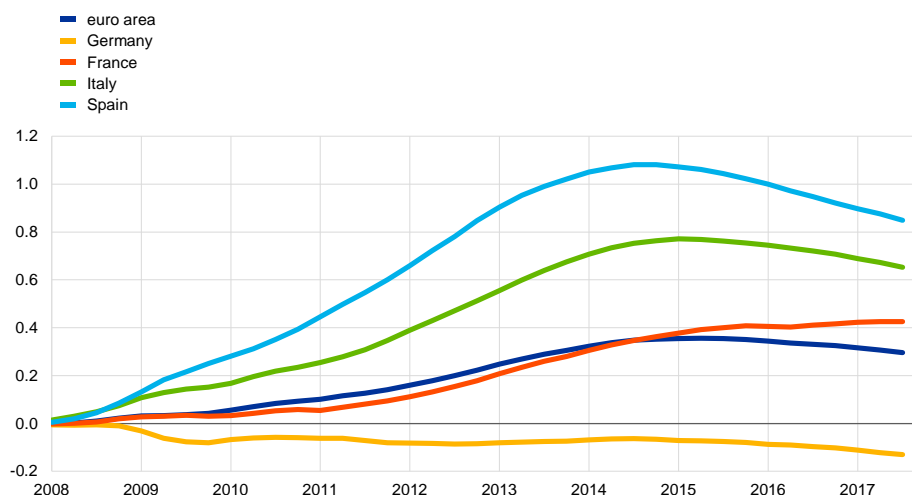
Another factor supporting durable goods consumption is pent-up demand. The sharp drop in durable goods consumption during the crisis also resulted in a decline in the effective stock of durables and a commensurate increase in its average age (see Chart B). In the countries that were more affected by the financial crisis (e.g. Italy and Spain), the increase in the average age of the stock of durable goods was much stronger, which gave rise to pent-up demand as soon as economic conditions improved. As the economic recovery has progressed, households have been able to increase spending on durable goods and offset earlier losses in their stock of durables. Consequently, the average age of the stock of durable goods has been falling since 2015 and the upward impact of pent-up demand for durables has been declining. This is also confirmed by model-based evidence from Spain.¹⁵ Following a long catch-up phase for private consumption, this can be regarded as a normalisation.

¹⁵ "Reabsorption of the pent-up demand for consumer durables", *Economic Bulletin*, Issue 4/2017, Banco de España, 2017.

Chart B

Change in the average age of the stock of durable goods

(years; cumulative change since Q4 2007)



Source: ECB calculations.

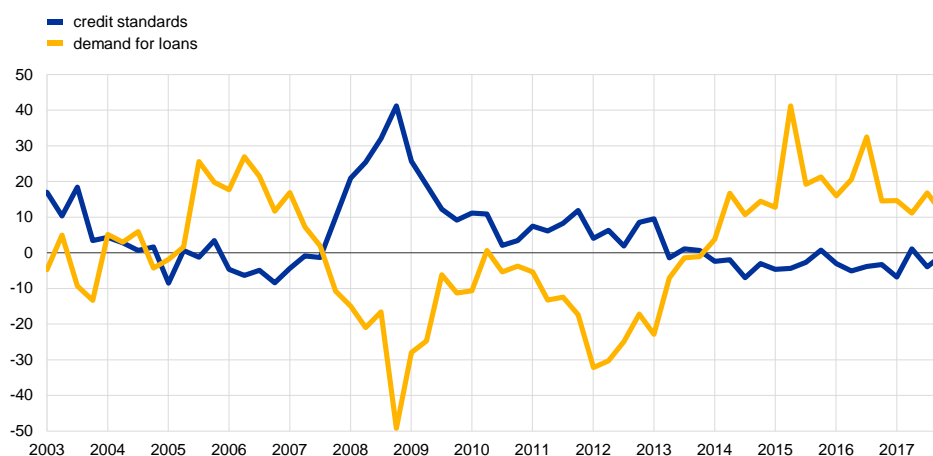
Notes: The average age of the stock of durables can be estimated using the depreciation rate and the service life of durables. A decrease in the average age implies that current spending on durable goods exceeds the depreciation of the stock. The latest observation is for the third quarter of 2017.

Favourable credit conditions are continuing to support the consumption of durable goods. According to the euro area bank lending survey, banks' credit standards for consumer credit have been easing since 2014 (see Chart C). This reflects the credit-easing measures that the ECB put in place in order to repair the monetary policy transmission mechanism. At the same time, survey respondents report that demand for consumer credit has increased in recent years, supported by very low lending rates (see also Section 5).

Chart C

Supply of and demand for consumer credit in the euro area

(weighted net percentages)



Source: ECB.

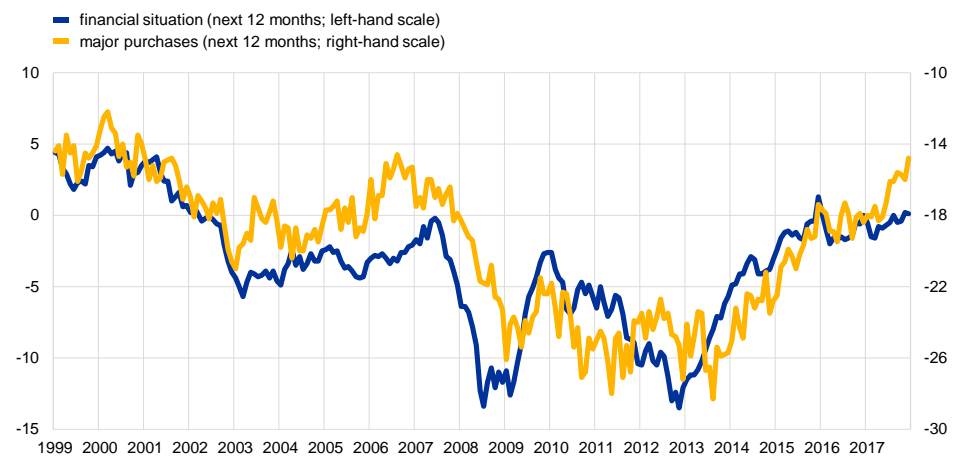
Notes: The bank lending survey asks banks how the credit standards applied to the approval of loans to households for consumer credit have changed over the past three months. Similarly, banks are also asked how demand for these loans has changed over the past three months. The latest observation is for the fourth quarter of 2017.

Going forward, household spending on durable goods should continue to grow on the back of robust income developments. The European Commission's latest consumer survey indicates an increase in the number of households that expect to spend more on major purchases over the next 12 months (see Chart D). Similarly, the number of households that expect their financial situation to improve over the coming year has also increased. This largely reflects further growth in employment and wages as the labour market improves (see also Section 3), as well as increases in net worth as asset prices rise.

Chart D

Households' financial situation and intentions to make major purchases

(percentage balances)



Source: European Commission.

Note: The latest observation is for December 2017.