

## Households' economic well-being: the OECD dashboard

### Methodological note

Gross domestic product (GDP) is the standard measure of the value added created through the production of goods and services in a country during a certain period. Equivalently it measures the income earned from that production, or the total amount spent on final goods and services (less imports). While GDP is the single most important indicator to capture these economic activities, it falls short of providing a suitable measure of people's material well-being. There is however a wealth of information available within the System of National Accounts (SNA) to help determine households' economic well-being in a more appropriate way.

The indicators selected for the OECD Household Dashboard represent a macro perspective on households using data produced within the framework of the SNA, supplemented with indicators such as the unemployment rate and consumer confidence. The first two household related indicators concern their income as a way to assess living standards (*real household disposable income* and *net transfers to households*). Another option in assessing living standards is to look at the consumption of households. In fact, a [recent study](#) conducted by the UK Office for National Statistics found that household expenditure appears to have a stronger relationship with personal well-being than household income. As stated in the [Stiglitz-Sen-Fitoussi report](#), consumption tends to be driven by permanent, long-term income more than by short-term changes in income. In this respect, it is also important to consider people's own perceptions of their economic situation, whether or not they feel confident enough to make major purchases. For the above reasons, the next two indicators look at *real household consumption expenditures* and *consumer confidence*.

Household disposable income may either be used for final consumption or saved. Disposable income thus represents the maximum amount households can consume without reducing their net wealth (without taking into account holding gains or losses on assets). As many households compensate short-term income fluctuations by increased saving or by borrowing, looking at *households' saving rates* and *households' indebtedness* can provide yet another perspective on how households are doing. Additional indicators to show how vulnerable households are to shocks to their income are presented by *financial net worth of households*, i.e. total financial assets minus total liabilities, the *unemployment rate*, and the broader *labour underutilisation rate*.

Taken together this set of indicators highlights material well-being from the household perspective, and thus provides more detailed information than simply looking at economic growth. Because many countries cannot separate data on households from data on non-profit institutions serving households, NPISHs, (such as churches and religious societies, sports and other clubs, trade unions) these data are included for each 'household' indicator, with the exception of the consumer confidence index, unemployment rate, and labour underutilisation rate. Each indicator is described in more detail below.

#### GDP per capita

This indicator shows GDP, adjusted for price changes, per member of the population, indexed to 2007 Q1=100. Because GDP growth can merely reflect a larger population, it is important to account for this when analysing people's material well-being. This indicator shows how much GDP per capita has grown or shrunk since the beginning of 2007 (right before the start of the financial crisis of 2007-2008).

## **Real household disposable income per capita**

Not all income generated by production (GDP) is available to residents of a country – some of the income is paid to non-residents. On the other hand, residents may receive income from other countries as well. In addition, not all income available to the residents of a country is available to households – some of it is retained by corporations and government.

The indicator shows the real household (and NPISHs) gross disposable income per member of the population, indexed to 2007 Q1 = 100. As such, it shows how much households' income has grown or shrunk after adjusting for how much purchasing power the money has from the beginning of 2007. For example, if money income increases more than consumer prices, real income increases. If money income increases less than consumer prices, real income declines.

Household disposable income equals the total income received, after deduction of taxes on income and wealth and social contributions, and includes monetary social benefits (such as unemployment benefits). It does not include in-kind transfers, such as those related to health and education provided free or at economically insignificant prices by government and non-profit institutions serving households (NPISHs).

## **Net cash transfers to households**

This ratio shows the impact of the redistribution of income, mainly through government intervention, on the income levels of households. The indicator is calculated as the ratio of gross disposable income to gross primary income. Since these numbers are only available at the level of the main sectors of the economy, the indicator only provides information for the sector of households (and NPISHs) as a whole. It does not give an indication of how income is distributed among groups of households (e.g. between households at the lower end of the income distribution and households at the higher end).

Household gross primary income is the income that accrues to households as a consequence of their involvement in the production process (such as compensation of employees, income from self-employment) or as a consequence of ownership of assets that may be needed for purposes of production (net of any payments on liabilities).

Household gross disposable income is derived from primary income by taking into account net current transfers; for example, the payment of taxes on income and wealth and social contributions, and the receipts of social benefits from government. Net transfers to the household sector also include other current transfers such as contributions to and benefits from pension funds, settlements of non-life insurance claims by households, and money sent by and received from relatives living abroad. It does not include, however, in-kind transfers, such as those related to health and education provided free or at economically insignificant prices by government. Also note that taxes deducted from income do not take into account the payment of consumption taxes (such as value added taxes). This type of tax is included in consumption expenditures.

A ratio above 100% indicates that households' disposable income is higher than primary income. However, since this indicator does not take into account in-kind transfers, the indicator is usually less than 100%. If in-kind transfers were included (showing the full impact of government intervention), all OECD countries would show an indicator above 100% for the most recent time periods, based on the available annual data.

For a given country, an increase in the ratio between time periods may explain a positive difference between the growth of disposable income and GDP growth, and vice versa. However, as an increase in the ratio over time reflects a higher rise (lower decrease) in the numerator as compared to the denominator, an increase in the ratio does not necessarily reflect an increase in the level of disposable income or one of its components. It merely indicates that the redistribution process is having a higher impact over time, given the level of primary income received by households. The same applies for the comparison across countries. A higher ratio in country A compared to country B indicates that the redistribution process has a higher impact in country A than in country B, given the level of primary income received by households. It does not provide any information on the income levels in country A as compared to country B.

### **Real household final consumption expenditure per capita**

Household final consumption expenditure covers all expenditure made by resident households to meet their everyday needs, such as food, clothing, housing (rent), energy, transport, durable goods (notably, cars), health costs, leisure, and miscellaneous services. It is typically around 60% of gross domestic product (GDP) and is therefore an essential variable for economic analysis of demand for goods and services.

The indicator shows the household (and NPISHs) final consumption expenditure, adjusted for price changes, per member of the population, indexed to 2007 Q1 = 100. It shows how much household consumption expenditures have grown or shrunk since the beginning of 2007.

### **Consumer confidence**

Consumer confidence is a qualitative measure based on surveys of people's own perceptions of their economic situation, whether or not they feel confident enough to make major purchases. The survey results are normally compiled as 'balances' by subtracting the number answering 'no' (or 'worse') from the number answering 'yes' (or 'improve'). Thus, a negative balance means there are more negative responses than positive responses. The indicator presented here converts the balances into an index in order to facilitate cross country comparisons. Looking at the index across time provides an indication of whether consumer confidence is trending up implying that they are more likely to spend money, or trending down implying that they are more likely to cut spending. The idea is that the more likely people feel about the stability of their incomes the more likely they are to make purchases thus indicating general trust in their personal economic situation.

### **Households' savings rate**

The households' savings rate compares the consumption and saving activities of households. From the perspective of households (at the micro-economic level), it shows how much households are saving out of current income, to provide families with financial security in the event of job loss and also how much income they have added to their net wealth, e.g. to fund part of their future retirement pension.

From a macro-economic perspective, household savings is the main domestic source of funds to finance investment in fixed assets (including investment of households themselves in, for example, housing), financial assets, or decrease liabilities.

Saving can be calculated on a gross or a net basis depending on the definition of household disposable income that is used. Gross disposable income is calculated before the deduction of depreciation (consumption of fixed capital in national accounts terms), while net disposable income is calculated by deducting depreciation from gross disposable income. Also note that the change in

net equity of households in pension funds is included in the savings of households, as a consequence of which (funded) pension entitlements are considered as a financial asset of households. All in all, gross household saving is defined as household gross disposable income plus the change in net equity of households in pension funds less household final consumption expenditure.

The household (and NPISHs) gross savings rate is calculated as the ratio of household (and NPISHs) gross savings to household (and NPISHs) gross disposable income plus the change in net equity of households in pension funds. The rates vary considerably across countries because of institutional, demographic, and socio-economic differences. For example, the government provision of old-age pensions or demographic age structure of the population will influence the rate at which populations save.

### **Households' indebtedness**

The household (and NPISHs) indebtedness ratio presents the total outstanding debt of households (and NPISHs) as a percentage of gross disposable income of households (and NPISHs). The debt of households largely consists of loans, primarily home mortgage loans, but also other types of liabilities such as consumer debt (e.g. credit card, automobile loans).

An indebtedness ratio above (below) 100 percent indicates that the household debt outstanding is larger (smaller) than the annual flow of disposable income. It is clear that high household indebtedness ratios, as is true for high government debt ratios, may create a certain risk or vulnerability for households, especially when it is unevenly distributed across different groups of households. On the other hand however, one should also take into account the availability of assets, e.g. dwellings, for which the borrowing has been made.

Furthermore, the indebtedness ratio may be affected by different levels of owner-occupied housing, house prices relative to disposable income, differences in taxation regimes for mortgage loans, and differences in pension schemes. The favourable tax regime for mortgage loans and the high level of pension wealth may be important reasons for the relatively high levels of indebtedness in some countries (such as the Netherlands and Denmark).

### **Financial net worth of households**

Financial net worth, or net financial wealth, of households corresponds to the excess of financial assets over liabilities and can provide an important source of revenue on its own. When net financial wealth increases due to, for example, a rise in share (stock) prices, households feel richer and are more inclined to save less and spend more. It is wealth in the form of securities and shares that are most sensitive to these capital gains, or "holding gains". Net financial wealth of households plays an important role in economic analyses, such as studies of asset bubbles and analyses of welfare.

The indicator is calculated as the ratio of financial net worth of households (and NPISHs) as a percentage of household (and NPISHs) gross disposable income. The higher (lower) net worth as a percentage of disposable income, the higher (lower) is the capacity of households in terms of consumption and savings and the stronger (weaker) the financial position of households.

From the above, it is clear that changes in financial net worth between two time periods are not only due to financial transactions (such as increases in savings deposits held by households because they are saving more or using the savings to pay down liabilities), but also due to other types of changes such as price changes (i.e., holding gains or losses) in financial assets or other changes in liabilities such as debt write-offs for loans.

## **Unemployment rate**

Unemployment rate is the number of unemployed people as a percentage of the labour force, where the latter consists of the unemployed plus those in paid or self-employment. Unemployed people are those who report that they are without work, that they are available for work and that they have taken active steps to find work in the last four weeks. When unemployment is high, some people become discouraged and stop looking for work; they are then excluded from unemployment and the labour force. This implies that the unemployment rate may fall, or stop rising, even though there has been no underlying improvement in the labour market. The unemployment rate is an important indicator of economic and social well-being.

## **Labour underutilisation rate**

The unemployment rate is the ratio between those who are unemployed and the labour force (the sum of the employed and the unemployed) based on International Labour Office (ILO) definition. Unemployed people are those who did not do any work for pay in the reference week of the survey, are available for work, and took active steps to look for work in the last four weeks, and those who have found a job but have not yet started. The broader labour underutilisation rate includes in the numerator the unemployed, the marginally attached (i.e. persons not in the labour force who did not look for work during the past four weeks but who wish and are available to work) and the underemployed (full-time workers working less than usual during the survey reference week for economic reasons and part-time workers who wanted but could not find full-time work), expressed as a ratio of the labour force.