How to keep your customers spending when inflation bites

Overwhelmed by everyday expenses, consumers cut back on large purchases. How can manufacturers and retailers capture the money they do spend?

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From prioritizing premium and budget products to controlling upstream costs, there are concrete ways for companies to face the reduced spending associated with sustained inflation.

IESE's José Luis Nueno lays out several recommendations in a new book (available in Spanish), whose title aptly translates as "everything is terrible, but I'm fine." The book homes in on Spain, where prices have risen almost 9% since the pandemic, and considers data from almost 200 million purchases made between January 2022 and March 2023. It examines how consumers are reducing their spending and what steps companies can take to regain control.

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In June 2022, 21% of Europeans expected they would be able to maintain their current lifestyle for another 10 months or more, and by January 2023 this number had risen to 34%. Even so, the numbers on the ground are somewhat different. In Spain, Nueno points out that "the average salary of the consumers we studied was €19,817 and the average expenditure €22,598." People are spending more than they earn and paying the difference from savings, on credit or through family support systems. Unsurprisingly in the circumstances, half of consumers have tried to cut back across all categories except housing, clothing and restaurants.

Faced with rising costs for essentials such as housing, water and electricity, as well as for clothing and restaurants, consumers have reduced expenditure on high-ticket discretionary purchases, including cars, electronics, furniture and home repairs.

Additionally, over half of the people studied had made cuts to spending on healthcare, education and food. Unsurprisingly, poorer consumers have cut back the most. Likewise, older consumers, who have more fixed costs and incomes, have had to cut back on discretionary spending more than younger ones.

Tips for the retail sector

For retailers, manufacturers and regulators faced with inflation and reduced consumer spending, Nueno presents a series of recommendations and best practices, including:

- **Focus on premium and budget ranges.** Superior quality gets attention and can justify price increases, while low-price ranges, which could include smaller units (even single-serving), will attract those who are struggling. Think twice about mid-range products, particularly those with low turnover.
- **Hold on to the customers you have.** Not everyone has had to cut back yet. Do you know who your customers are? This is the last year you can afford to ignore them.
- **Entice former customers back.** Create a retention management team to track consumer behavior, set recovery goals, share data internally, identify operational changes and adopt appropriate technologies.
- **Keep nominal and real accounts.** Financial reporting can hide even as it enlightens, and many companies doing well on the surface wouldn't present so well if accounts were adjusted for inflation. It may not be customary, but it's better to keep double sets of accounts and know the true state of things.
- **Consider acquiring a DTC store.** Direct-to-consumer (DTC) e-commerce stores

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have been going through a rough patch, as investors grow skittish about their lack of profitability. But acquiring one can bring all their knowledge on board, from mastery of social networks and shorter time to market, to intensive use of customer information, which boosts product-market fit and personalization.

- **Rethink operational costs.** Primark, for example, directly controls 350,000 cotton farmers, allowing it to ensure quality, sustainability and costs upstream. Meanwhile, the upscale furniture supplier, Kave, has prioritized bringing production back to near the consumer, relocating its upholstery cluster from overseas to Spain.

What does the future hold?

Consumer aspirations continue for 2023, though the cost-of-living crisis has taken its toll on expectations. Energy prices have stabilized, but food inflation persists, exacerbated by a nationwide drought and the price of fertilizers.

Household discretionary spending (which fell from 12% in 2021 to 2% in the winter of 2022) could return to 6%-8% by the end of 2023 due to improvements in energy costs and inflation.

But Nueno warns of the need to keep an eye on the risk of recession in the U.S. or China, a probability he describes as a toss-up. If one of these economies tips into recession, the new shock will be felt by all.

About the research

The research draws on fintech data from the IESE Intent HQ Chair on Changing Consumer Behavior, which contains information on almost 200 million purchases carried out in Spain between January 1, 2022, and March 31, 2023.

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