

Affordability Gap in a K-Shaped Economy

Key Takeaways

- **Headline economic strength masks household strain.** While real GDP growth has remained solid through 2025, rising prices, intensified by tariff-policy uncertainty, continue to pressure budgets for many middle- and lower-income households.
- **Inflation's cumulative impact is eroding purchasing power.** Price levels have risen roughly 25% since 2020, with essentials such as food, rent, insurance, and auto repairs remaining persistently high, creating a lasting affordability burden rather than a temporary spike.
- **Consumer resilience is uneven and increasingly K-shaped.** Higher-income households, buoyed by strong balance sheets and asset gains, are driving most spending growth, while middle- and lower-income consumers face stagnant real purchasing power and rising debt burdens.
- **The affordability divide is reshaping retail winners and losers.** Premium and value retailers continue gaining market share, while mid-tier players struggle, reflecting the broader bifurcation of the consumer economy.

Affordability Reality Check

The familiar adage that a rising tide lifts all boats assumes that economic growth benefits everyone. Recent years have exposed the limits of this idea, as middle- and lower-income households increasingly struggle despite solid headline economic data. Real U.S. GDP grew 2.9% in 2023 and 2.8% in 2024, with an annualized rate of roughly 3.8 % through 2Q25, fueled by consumer spending. Yet aggregate national data understates the post-pandemic strain on many U.S. households, where rising costs, intensified by recent U.S. tariff-policy, continue to pressure budgets.

A recent *Wall Street Journal* report noted that the cumulative price level for goods and services had risen roughly 25% since 2020. Tariffs pushed up headline CPI inflation to 3% in September and are expected to have a greater impact in 4Q25 and into 2026. Through September (the latest CPI data), essentials such as coffee, ground beef, rent, insurance, and car repairs remain stubbornly high. Rather than a short-lived surge, inflation is an accumulated burden that has permanently raised the cost of living.

The Illusion of Consumer Resilience in a K-Shaped Economy

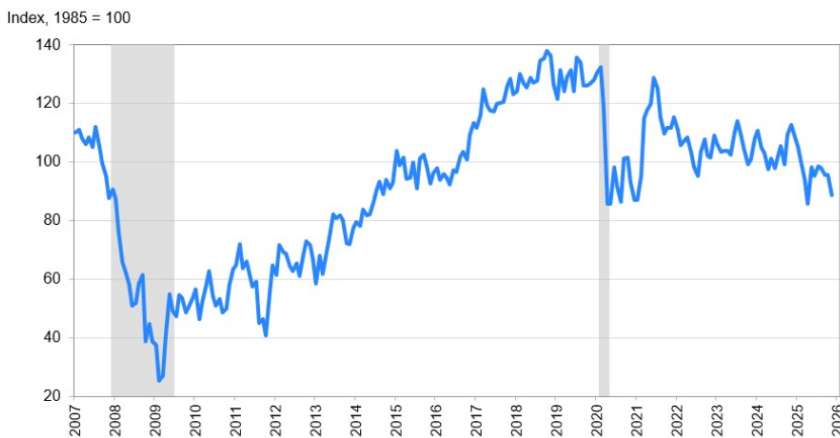
The national figures continue to show a seemingly resilient consumer. Month after month, the Bureau of Economic Analysis reports rising personal consumption expenditures. U.S. Census data also shows that retail sales continue to grow. October retail sales increased 4.5% through the first ten months of 2025 (excluding auto and gas), outpacing inflation which rose to 3% in September.

Seasonally Adjusted Retail Sales				
Source: U.S. Census, Bloomberg				
	Oct 2025	Oct 2025 (Est.**)	Sep 2025	Oct 2025
	m/o/m	m/o/m	m/o/m	y/o/y
Total Retail Sales	0.0%	0.1%	0.1%	3.5%
Retail Sales Ex Auto	0.4%	0.2%	0.1%	4.0%
Retail Sales Ex Auto and Gas	0.5%	N/A	0.0%	4.2%
Core Retail Sales*	0.8%	0.3%	-0.1%	5.1%
By Category:				
Furniture & home furnishings	2.3%		-2.4%	0.5%
Electronics & appliance	0.7%		0.0%	4.9%
Building materials & garden	-0.9%		-0.1%	-4.5%
Food & beverage stores	0.3%		-0.1%	2.2%
Grocery	0.3%		0.0%	2.7%
Health & personal care	-0.6%		1.3%	5.7%
Gasoline stations	-0.8%		1.9%	1.9%
Clothing & clothing accessories	0.9%		-0.9%	5.7%
Sporting goods, hobby, musical instrument & <u>book stores</u>	1.9%		-1.7%	4.6%
General merchandise	0.5%		0.1%	2.0%
Department stores	4.9%		-0.3%	4.6%
<u>Nonstore retailers</u>	1.8%		-0.4%	9.0%
Food services & drinking places	-0.4%		0.2%	4.1%
Miscellaneous store retailers	1.5%		2.2%	9.5%

Excludes sales from auto & motor vehicle dealers, gasoline stations, building materials, food services & drinking places
 ** Represents Bloomberg monthly sales estimates

Consumer spending has remained surprisingly resilient despite weakening confidence. Over the past year, a disconnect has emerged between declining consumer sentiment, negative outlooks, and actual spending, which continues to drive GDP growth. The Conference Board’s Consumer Confidence Index declined 6.8 points in November to 88.7, with consumers’ assessment of both their current and short-term outlook falling.

Consumer Confidence Index®



*Shaded areas represent periods of recession.
 Sources: The Conference Board; NBER
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The Conference Board said, “All five components of the overall index flagged or remained weak. The *Present Situation Index* dipped as consumers were less sanguine about current business and labor market conditions. The labor market differential—the share of consumers who say jobs are 'plentiful' minus the share saying 'hard to get'—dipped again in November after a brief respite in October from its year-to-date decline. All three components of the *Expectations Index* deteriorated in November.

Consumers were notably more pessimistic about business conditions six months from now. Mid-2026 expectations for labor market conditions remained decidedly negative, and expectations for increased household incomes shrank dramatically, after six months of strongly positive readings.”

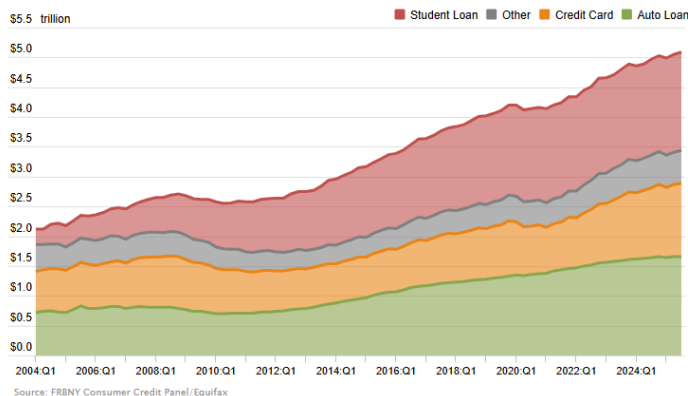
Economists have warned that the U.S. economy is becoming increasingly K-shaped, characterized by stronger spending among higher-income households while lower-income consumers struggle with affordability.

A recent Federal Reserve Bank of Boston report offers a clearer lens on what is happening beneath the surface. Its 2025 decomposition of consumer spending indicated that “real (inflation-adjusted) spending by the lowest-income consumers (< \$59k) increased sharply in 2021 and 2022” following the pandemic “and has grown only modestly since then, whereas real spending growth by the higher income groups —especially the top earners (>\$121k)—has remained robust. The middle-income quintiles are \$59k to \$121k.” These findings indicate that recent growth in aggregate spending, which sums across all income groups, has been propelled by the highest-income consumers. These households, supported by stable employment, savings, and rising asset values, have substantial financial cushions and have continued spending despite higher prices. Most have also locked in historically low mortgage rates. Mirroring this, premium discretionary categories, ranging from high-end apparel to electronics and niche accessories, have seen some of the strongest gains.

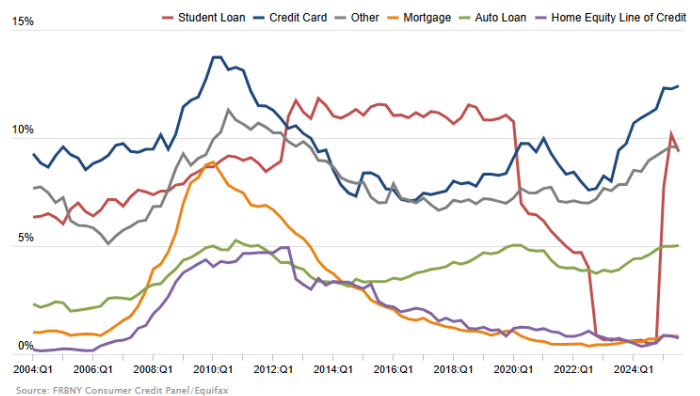
For middle-income and lower-income households, the picture is very different. After adjusting for inflation, real spending power is flat or falling, while the excess savings accumulated during the pandemic have long been spent.

At the same time, debt levels are rising, with credit card debt rising near 6% YOY in 3Q25 to \$1.23 trillion, while delinquencies are becoming a concern again.

Non-Housing Debt Balance



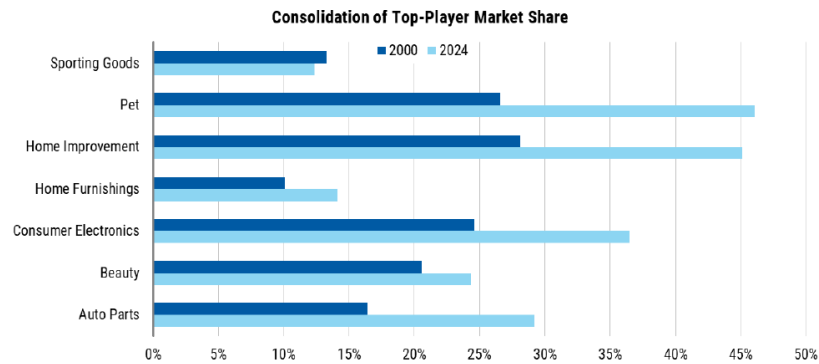
Percent of Balance 90+ Days Delinquent



These pressures are not the result of a short downturn rather longer-term challenges, including the aforementioned higher general inflation, a shortage of affordable housing, high home and rent prices, rising insurance premiums, and escalating medical costs. The widening gap between asset owners and those without homeownership and financial asset wealth has further contributed to this. America’s K-shaped economy, with one upward path for higher-income households and a flat or declining path for everyone else, is now a defining feature of the U.S. economy and consumer landscape.

Retail Winners and Losers in the K Economy

The K-shaped economy isn't limited to consumers, as there is growing evidence that retail market share is being further consolidated by the largest players. Morgan Stanley research shows this by sector:



Source: Euromonitor, Morgan Stanley Research

Note: the decline in market share among top sporting goods retailers likely reflects bankruptcies or liquidations (eg Sports Authority) and growth of smaller online competitors. Dick's Sporting Goods remains the only national sporting goods chain, with a market share now in the low teens following the acquisition of Foot Locker.

An analysis of sales growth among RetailStat's portfolio of publicly traded retailers shows that growth has been concentrated among the largest retailers, which are grabbing an increasing share of their markets. The following table shows the percentage of growth achieved by the top retailers by sector from FY19 through 1H25:

Retail Growth Leaders	
Mass Merchandise:	
Walmart	49%
Costco	35%
Grocery:	
Kroger	25%
Publix	23%
Albertsons	18%
Department Stores:	
TJX*	115%
Ross	39%
Burlington	27%
Home Improvement:	
Home Depot	64%
Lowe's	13%
Sporting Goods:	
Dick's Sporting Goods	63%

* TJX had growth represented over 100% of the sector growth due to negative growth from traditional operators including Macy's, Kohl's and JCP.


The divide in consumer finances is becoming more noticeable across the retail sector. Differentiated retailers serving affluent shoppers remain well-positioned. Lululemon, RH, Williams-Sonoma, Nordstrom, Apple, and Ulta continue to attract customers who can afford higher prices and sustain demand for premium or novelty goods. Extreme luxury brands like Richemont, Hermès, and Prada have reported strong results. In its most recent 3Q report, Macy's Bloomingdale's division posted 9% comparable sales growth, marking its fifth straight quarter of positive comparable sales. To better address this market, many brands are expanding their premium offerings, confident that the wealthiest consumers will keep spending.


Value-oriented retailers are also gaining ground, although for the opposite reason. These retailers tend to outperform when families start stretching every dollar. As inflation eats into household budgets, more middle-income consumers are trading down. Shoppers who once frequented mid-tier stores are more frequently turning to Walmart, Dollar General, Dollar Tree, and off-price chains such as TJX and Ross in search of lower prices.


Walmart's CFO John David Rainey explicitly called out that better-off customers are driving share gains: "We're seeing higher engagement across income cohorts with upper income households continuing to account for the majority of share gains." Dollar Tree's CEO, Michael Creedon share similar views: "an increasingly broad spectrum of shoppers, from core value-focused households to middle- and higher-income shoppers who are making deliberate choices about how and where they spend."

Beneath resilient GDP and macroeconomic numbers, America is experiencing an affordability crisis that is reshaping the consumer economy. Rising prices have outpaced incomes for most households, while wealthy consumers keep the spending engine running. Both ends are gaining share: premium retail, defined by exclusive or higher-end merchandise, strong customer service, and advanced omnichannel capabilities, and the value segment, which continues to deliver strong quality, particularly among off-price department stores. In the K-shaped economy, the premium and value retailers are positioned to win, while mid-tier players lose share.

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