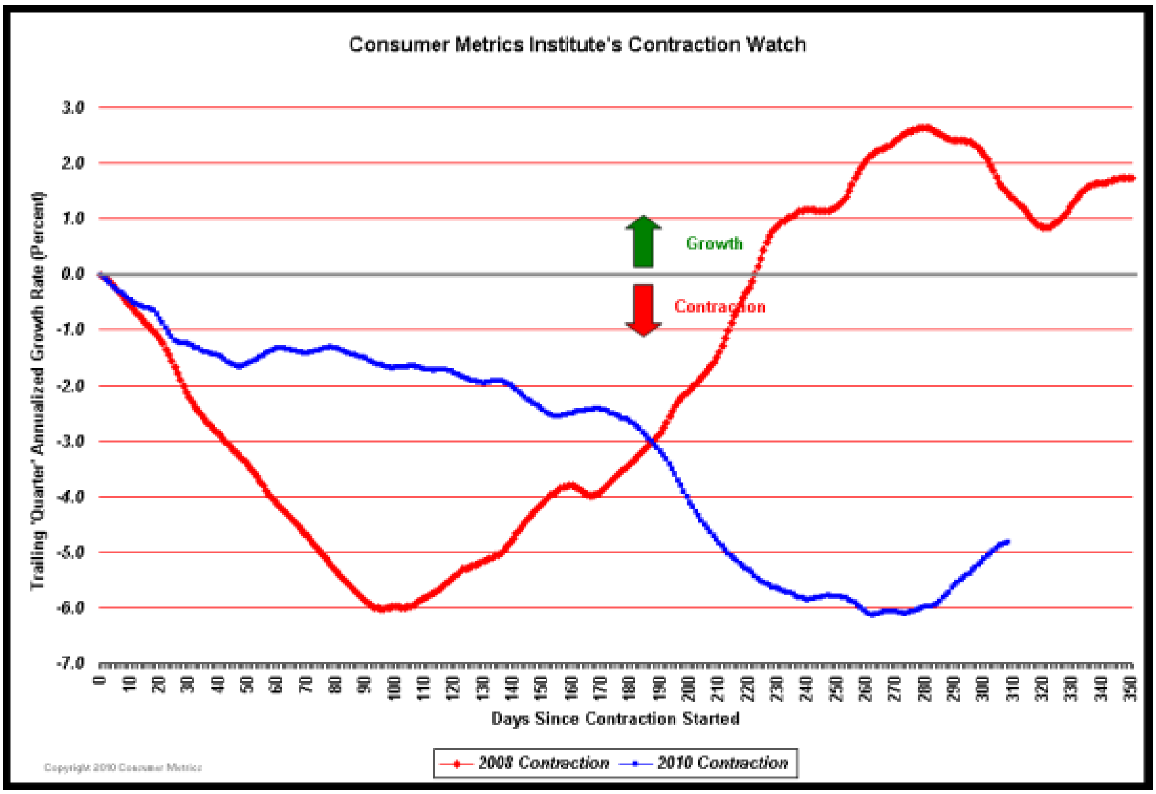
Consumer Metrics Institute Members News

November 14, 2010: What Does the Bottom in the Daily Growth Index Mean?

The good news is that a quick glance at our "Contraction Watch" chart tells you that our Daily Growth Index has formed a nice bottom. The bad news is that in order for that quick glance to even see that bottom we have had to extend the horizontal scale on our "Contraction Watch" chart once again, this time reaching out to 350 days, nearly a full year:



The three key points to understand about this chart are:

-- The dip that forms the visible "bottom" is the result of a span of poor year-over-year comparisons to the "green shoots" economy of the second half of 2009, when the Federal stimuli for "clunkers" and new housing were in full effect -- stimuli which targeted the automotive and housing industries that are so heavily weighted in the real economy. It was after the expiration of those stimuli that the "recovery" we were monitoring sputtered, dropping into contraction by January 15, 2010. As we approach the anniversary of the beginning of the 2010 contraction, our year-over-year comparisons will inevitably improve -- even if the economy continues to sputter.

-- The shear longevity of the 2010 contraction in consumer demand is both impressive and unprecedented in our data. Although our data extends back only about 6 years, it does fully cover the "Great Recession" as defined by the National Bureau of Economic Research ("NBER"). The duration of this contraction now exceeds the duration of that 2008 contraction by 50%.

-- The daily inputs into the 91-day trailing "quarter" average that makes up the Daily Growth Index are still negative -- and have been so continuously for the past 195 days. If consumer demand continues at current levels relative to the prior year the blue line will level off at about a -3% contraction rate. By way of reference, at the same point during the time span of the 2008 event we had already witnessed daily Weighted Composite Index values reflecting year-over-year growth in excess of 10%, which eventually led to the trailing average Daily Growth Index peaking at a year-over-year growth of +6% by the end of August 2009.

Given the above, we are left to wonder whether the blue line in the above chart will continue up, revert back down, or drift laterally to the right. Simple arithmetic indicates that until our Weighted Composite Index sustains growth levels (i.e., levels above 100) for the better part of a quarter, the blue line will remain below the gray "zero" line and drift to the right in a year-over-year contraction mode.

We are continually asked why our measurements of consumer demand differ so much from the headline number of 2% annualized growth in the most recent 3Q-2010 GDP report (see our October 29, 2010 commentary for a fuller exploration of that report). In actuality, the GDP measurements of consumer demand for durable goods are not nearly as positive as the headline number. If we try to reconcile our measures of the economy to the BEA's report by fully embracing the BEA's almost "Alice in Wonderland" arithmetic:

-- The headline number of 2% growth includes about 1.4% created by inventory building at factories and within product distribution channels. Taking that out of the headline number reduces the GDP to about a 0.6% annualized growth. This figure is actually cited by the BEA each quarter as their "real final sales of domestic product," and it is generally viewed as a more accurate indicator of the true growth of the economy.

-- The official BEA number also includes a 0.6% contribution from exports, which is not generated by domestic U.S. consumer demand. Backing that out of the "real final sales of domestic product" results in a zero annualized growth rate for "real final" domestic spending.

-- Governmental and commercial spending contributed another 0.8% to the headline growth. Again, this does not reflect consumer demand. Removing those factors from the above chain of calculations results in a -0.8% contraction rate for real final domestic consumer spending.

-- Consumer spending on services added roughly 1.2% to the headline number. We only capture consumer demand for discretionary durable goods, which in large part excludes purchases of services. In order to reconcile our data to the BEA's we also need to subtract that 1.2%, lowering the real final domestic consumer spending on domestic goods to a -2.0% annualized contraction rate.

-- While we are at it, if we fully embrace the BEA's Wonderland arithmetic, that -2.0% annualized contraction rate can be calculated more directly by combining the BEA's reported consumer consumption of domestically generated goods (0.6%) with the GDP figure for imports (which contributed -2.6%) -- thereby including the domestic consumption of imported foreign oil, autos and Chinese manufactured goods. This surreal math is a consequence of the BEA's focus on "domestic product," which requires them to subtract net foreign trade from the gross numbers.

In that Wonderland context, the net -2.0% GDP number for net domestic consumer demand of goods corresponds to our Daily Growth Index late in 2Q-2010, leading the mid-point of the BEA's 3Q-2010 time frame by about 10 weeks. When looking at all these comparisons it is important to remember that although our Daily Growth Index should be leading, it also measures only demand for discretionary durable goods and should therefore also be somewhat amplified. Both of these factors should be considered when comparing our data to the BEA's.

Even when ignoring the Wonderland math, the annualized growth rate in the BEA's "real final sales of domestic product" happens (this quarter at least) to be very near their calculation of the annualized growth rate in consumer consumption of domestically generated goods -- both recording a 0.6% annualized growth rate, substantially below the headline number. This 0.6% number is both statistically indistinguishable from contraction and subject to likely downward revisions.

The jobs environment has been the bottom line in this recession. Looking at the positive line items in the BEA's 3Q-2010 for news about the jobs environment raises some caution:

-- The growth in exports has primarily benefited major corporations. These same corporations have been growing margins over the past year by cutting jobs, and now appear reluctant to start major re-hiring.

-- The growth in governmental spending has probably peaked, with both the future impact of Federal ARRA spending capped and with local governments being forced to deal with looming deficits.

-- The only bright spot in the report is the growth of consumer spending on services, which largely flow to the small businesses that are most capable of growing jobs. This is a positive step, even if the annualized growth in that portion of the consumer economy is only 1.2%.

We have said before that the real consequences of the "Great Recession" on U.S. consumers were triggered by rising energy prices, dropping home values and persistent unemployment. Until something dramatically turns around in those specific areas consumer demand for discretionary durable goods is not likely to improve.

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