Consumer Metrics Institute Members News

January 10, 2011: Lessons from 2010

2010 was a year that contained a number of disappointments. First and foremost, at a macro level the economy was not growing as quickly as we should expect after more than a year of "official" recovery. But frankly, our greatest disappointment was how the most commonly reported measures of the tepid recovery began to diverge significantly from the much weaker data that we track. The divergences started in the second quarter and widened during the third -- with early consensus expectations for the fourth quarter of 2010 pointing to divergences that likely continued through the end of the year.

We have taken from this experience a number of key lessons. These lessons have helped us understand that 2010 was a year of extraordinary distortions in the sources of economic growth in the U.S. economy. Even though it was the fourth consecutive year of unprecedented governmental intervention in the economy, this time the interventions were not targeted exclusively at rescuing financial institutions, auto makers and the housing market. By the second quarter of 2010 the full impact of both a wide range of stimulus spending and the defacto devaluation of the dollar was supplanting the consumer as the primary (and traditional) source of economic growth in the U.S. economy.

The shift to non-consumer sources of economic growth was clearly not the sole reason for the divergence between our indexes and the commonly reported measurements of the economy. By the third quarter we began to understand that the demographics of the consumers most likely to buy on-line were the same as those households most severely impacted by the recession. Unwittingly, some of the previously identified sampling biases in our data collection methodologies turned out to be much more significant than we might have suspected. Simply put, young and highly educated members of generations "X" and "Y" were particularly vulnerable to the hallmarks of this recession: entry level job losses and vanishing home equity.

That said, at the end of 2010 the data that we track had not materially improved. Our consumers still appear to be reluctant to take on new debt, and they remain cautious in their expectations for the economy in 2011. The heavily reported increases in holiday spending came primarily from reductions in personal savings rates, and they may turn out to be merely brought forward from the first quarter of 2011 -- similar to holiday dietary indulgences preceding thoroughly resolved first quarter diets. In any event, the consumers that we track are still contracting their year-over-year discretionary durable goods purchases at levels that indicate that something is still seriously amiss in this economy.

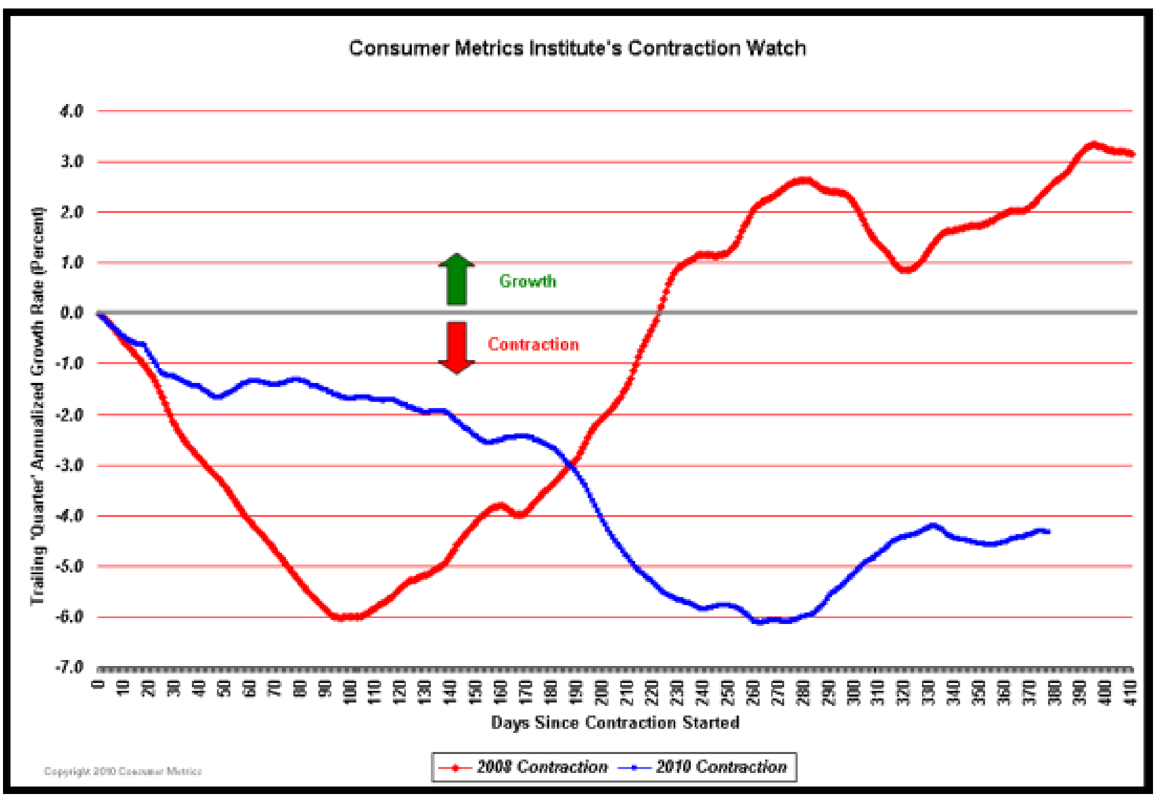
A summary of the lessons we took from 2010 might look something like this:

-- **GDP growth rates can be significantly impacted by non-consumer line items**. Manufacturers building inventory, export growth, increased governmental spending and (counter-intuitively) consumer cut-backs on imported goods have all increased the GDP during portions of 2010 even as consumer spending remained relatively flat. Despite the headline GDP growth numbers, during the second and third quarters of 2010 the annualized growth of the "real final sales of domestic product" languished at levels below 1%.

-- **This recession was not a shared experience**. Some consumers were especially hard hit by the downturn, just as they may have been the demographics that most benefited from the expansion that led up to the 2007 peak. Unfortunately, the consumers who provide the transactions that we capture appear to be disproportionately among those most severely impacted by this recession.

-- **At year-end 2010 consumers were still cautious about the long term**. In effect, the massive stimulus applied by the government during 2010 still didn't significantly improve longer term consumer confidence. Households are still deleveraging, although at a moderated pace. Consumers are still reacting to their own personal assessments of the employment and housing markets, and they see no reasons for changing their new-found conservative behaviors.

Despite the BEA's reports that "real final sales of domestic product" were growing at a (feeble) 0.9% rate during both the second and third quarters of 2010, our Daily Growth Index remained in year-over-year contraction from the middle of January through the end of the year:



In the above chart the day-by-day courses of the 2008 and 2010 contractions in our Daily Growth Index are plotted in a superimposed manner with the plots aligned on the left margin at the first day during each event that our Daily Growth Index went negative. The plots then progress day-by-day to the right, tracing out the changes in the daily rate of contraction in consumer demand for the two events. The 2010 contraction event is now very nearly a year old, dating back to January 15, 2010. Although the chart clearly bottomed at about 9 months into the contraction (at roughly 270 days), the rise since that bottom has been neither steady or substantial. In fact, there is no way to project when the contraction will end based on the recent course of the blue line.

Since the contraction has extended for nearly a full year, any continued contraction would mean that the year-over-year decline is being compounded (i.e., the current year-over-year contraction is against already contracting data points from the prior year). This is not the type of data we were tracking during most of 2009. We understand the lessons from 2010, but we also recognize when major portions of the consumer economy are still far from healthy.