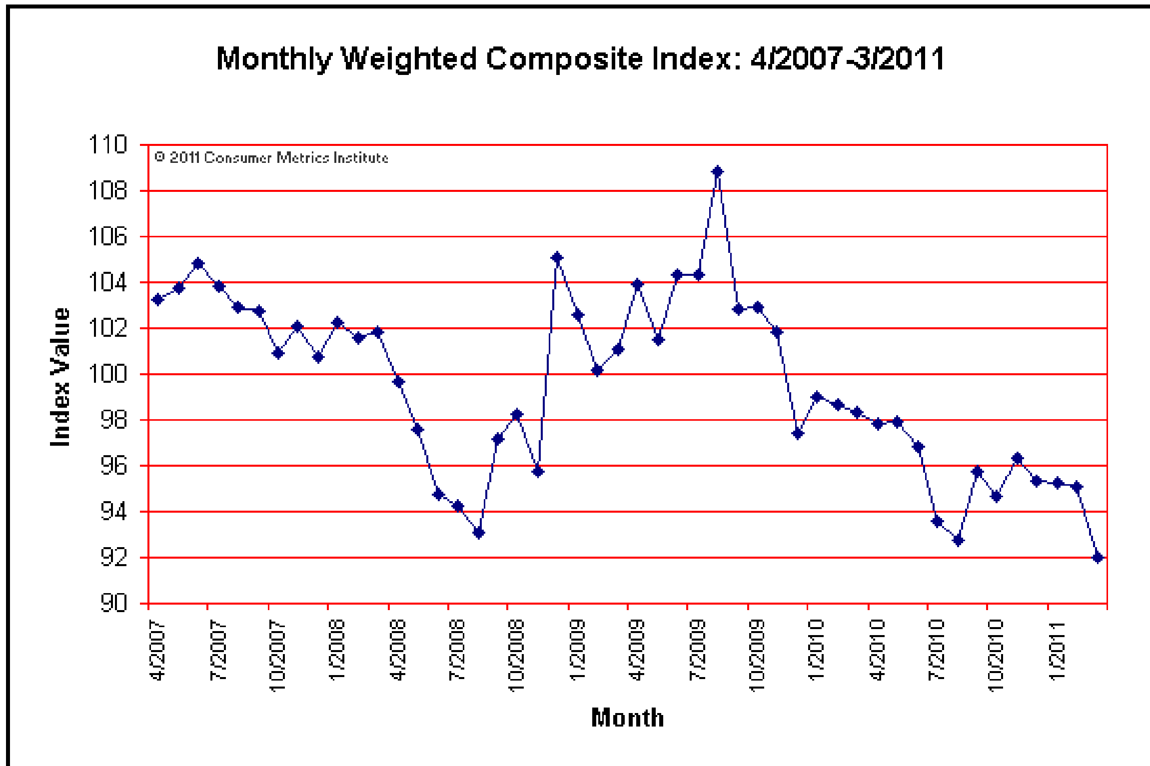
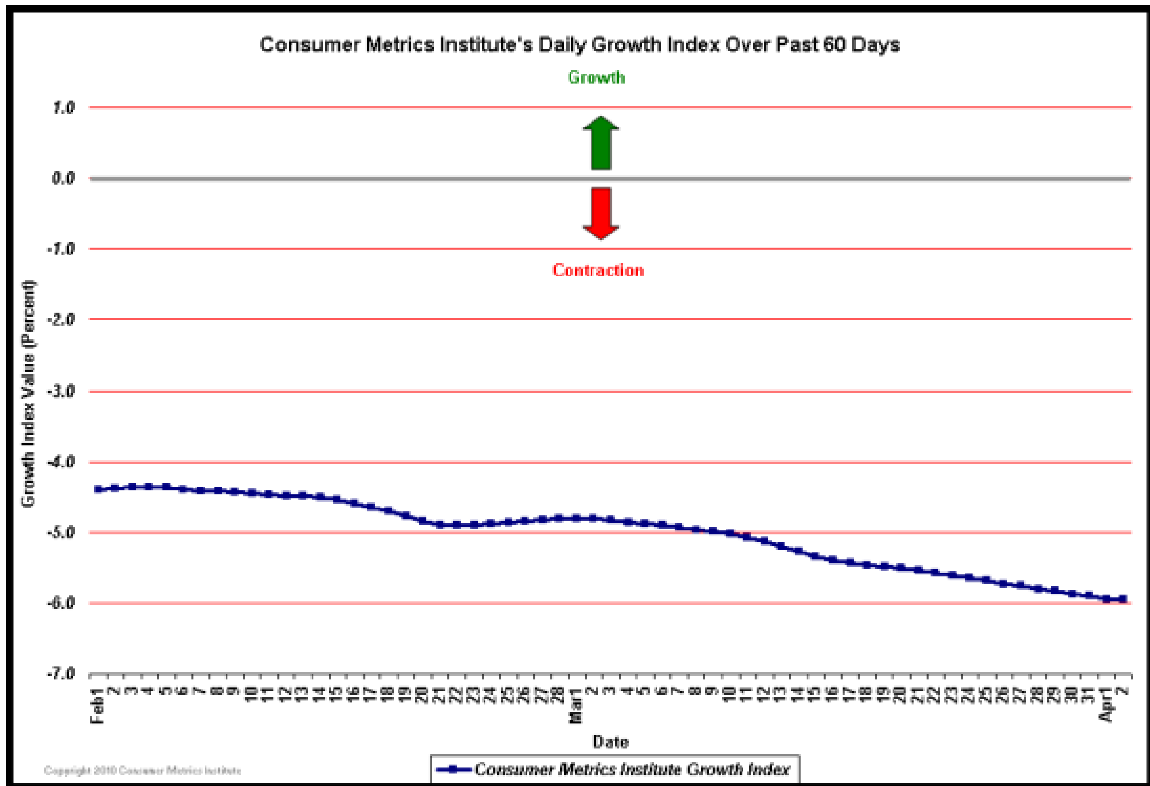
Consumer Metrics Institute Members News

March 31, 2011: Continued Weakness; Divergences Revisited

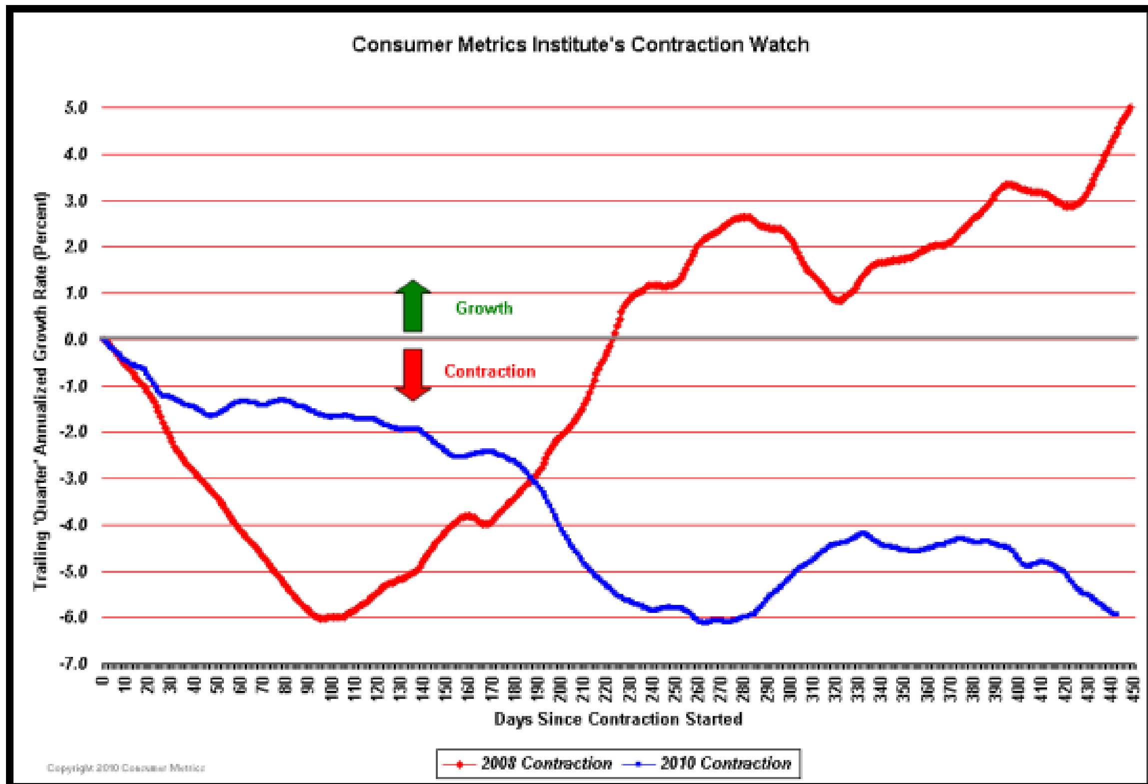
We continue to see weakness in our Weighted Composite Index, and the persistence of that weakness can be clearly seen in our monthly chart:



And at a year-over-year contraction rate of -5.83%, our 91-day trailing "quarter" Daily Growth Index is again rapidly approaching the record lows set this past fall (-6.13% on October 4, 2010):



As we have mentioned before, our "Contraction Watch" (which follows the Daily Growth Index shown above and compares it on a day-by-day basis with the same index during the dip created by the "Great Recession") is perhaps the best way to visualize what has been happening with the consumers that we monitor, and that chart is still not showing any signs of a sustainable consumer driven "recovery":



There are two critical points to remember when looking at the above charts:

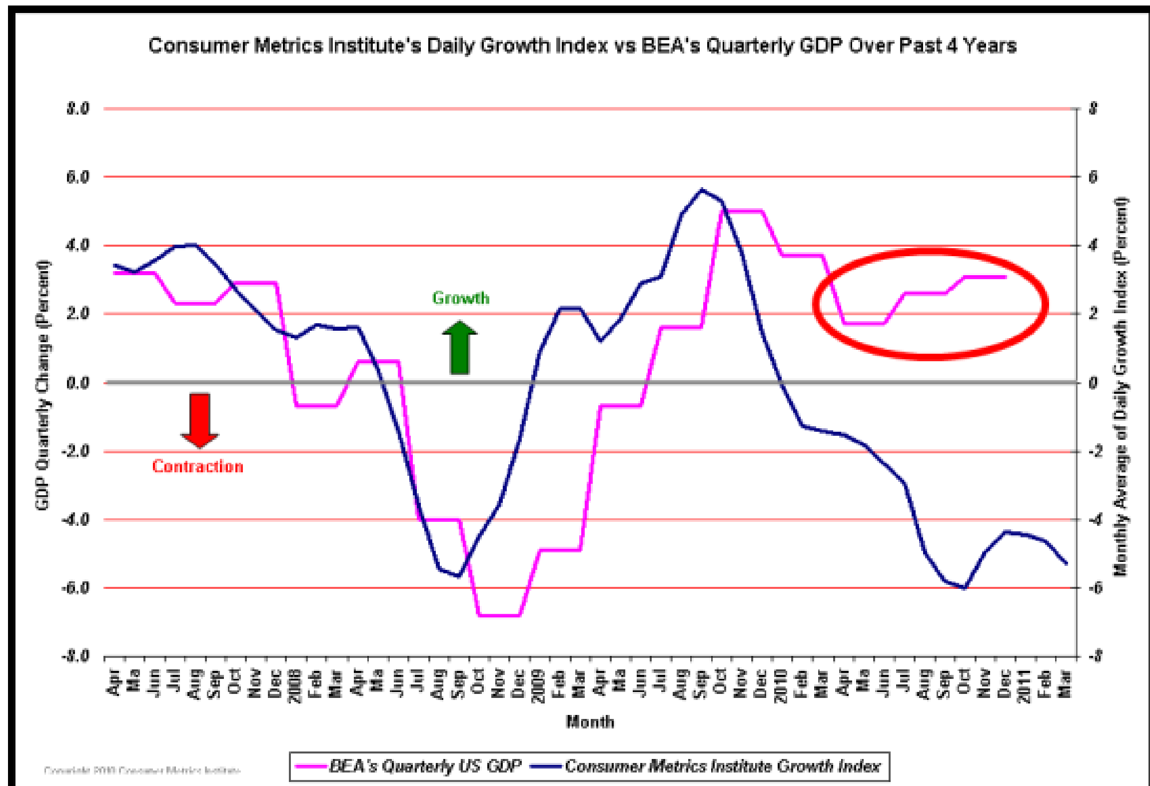
-- We have not changed our data collection or analysis methodologies at all during the past 24 months. All of our data back to 2005 uses exactly those same methodologies. As tempting as it may be to "correct" for the divergences between our data and BEA reports (or any other data currently showing a self-sustaining recovery), we have not done so. The data we report is real, consistently derived, current and unadjusted for rosier readings. What you see in our charts appears to be a material shift in the consumption patterns of the consumers that we are able to track.

-- Our year-over-year comparisons have now shown continuous contraction for over a year, and our current year-over-year contraction is against already contracting demand this time last year. This means that the contraction rates that we chart are actually having a compounded impact on total demand.

We realize that our data is not the definitive statement about the U.S. consumer economy, let alone the entire U.S. economy. However, regardless of the cause for the divergences between our data and more commonly reported macro-economic data (as discussed below), a prudent observer of the economy should be at least a little cautious about the prospects for a continued "recovery" of real commerce as we move into the second and third quarters of 2011.

Data Divergences Revisited

We have recently been asked to speculate about when our data and the BEA's GDP will begin to re-converge. To understand the issues, it is best to start with the divergence itself, as highlighted by the red oval in the below chart:



One interpretation of the above chart is that something began to impact the GDP during the second quarter of 2010 that failed to similarly benefit consumer households.

In fact, the vast majority of the $105 billion of stimulus-financed construction contained in the American Recovery and Reinvestment Act of 2009 (ARRA) began to impact real commerce during the summer of 2010. By some estimates nearly 10,700 highway projects were underway in July of 2010, compared to just 1,750 in July of 2009. Similarly, state incentives led to the "weatherizing" of 82,000 homes during the summer of 2010 - 27 times the number of homes that were weatherized the previous year. And there were 2,828 clean-water projects under construction, a twenty-fold increase over the prior year.

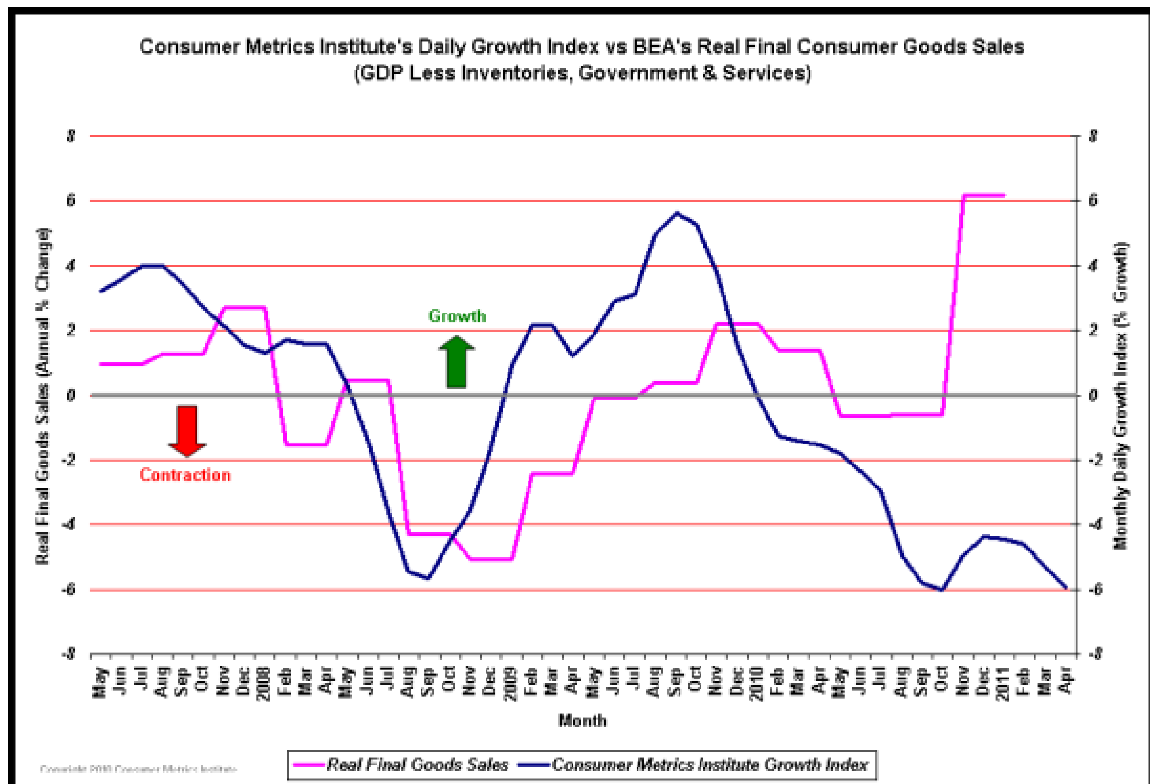
The reality is that there were very few "shovel ready" projects for ARRA to spend money on, and the lag caused a significant portion of the ARRA's impact to be felt nearly 18 months after the stimulus package's passage. And we have argued before that infrastructure construction projects are an inefficient way to stimulate a consumer driven economy. The projects themselves go to established major contractors, and a large portion of the money is spent on materials and seasonal (i.e., non-permanent) workers -- and certainly not on the kinds of innovation and productivity gains that generate real long-term economic growth. Those ARRA projects clearly did not benefit most of the consumers that we track (and arguably not the vast majority of U.S. consumers either).

If we assume a 1.7 multiplier effect for the entire $787 billion ARRA, it could generate perhaps

10% aggregate GDP additions, spread over several years -- and most likely peaking during the summer of 2010, with at least some of the spending still going on.

Although most households saw some tax breaks, there was not a material boost to their net real income -- at least not enough to trigger increased consumption of discretionary durable goods. If anything, the tax breaks simply enabled further household deleveraging.

When we look at the BEA's "Real Final Sales" (and removing Government and Services) -- and ignoring for the moment the silliness in the BEA's data for the fourth quarter of 2010 -- we can see a much weaker "recovery" that had begun to slip back into contraction during the summer of 2010:



Unfortunately it is hard to ignore the silliness of the BEA's 4Q-2010 data. Per their data, "Real Final Sales" (less Government and Services) was growing at an annualized 6.17% rate. Although we also saw a bump in our data during fourth quarter (actually a lessening of the contraction rate), the effect was far less dramatic and ultimately un-sustained. The 6.17% number is nice, but it strains credibility almost as much as the 0.4% annualized inflation rate that they used to derive it.

Recapping some of the other reasons why our data may have diverged from the BEA's reports:

-- From time to time the BEA's data seems to be taken hostage by seasonal adjustments and pricing deflaters "gone wild." Our data is inherently free of such problems.

-- We measure only consumer demand for discretionary durable goods, which is less than 10% of cash flows for most households -- and much, much less than 10% for those at the lowest income

levels.

-- Our baseline data assumes that residential housing is relevant to the economy. In the BEA's current GDP that is no longer true.

-- Our data is inherently "per capita" by virtue of our "same shopper" metrics (used to normalize for the growth of on-line shopping vis-a-vis "brick and mortar" sales).

-- There are some biases introduced into our data by our sampling process. Our demographics may have been hit harder by the recent recession than an average or "typical" consumer. On the other hand, our "per capita" consumer may actually be more typical than averages that are tilted by the spending of those benefiting disproportionately from the wealth recently generated by the equity markets.

We are also intrigued by a hypothesis offered by one of Doug Short's readers: that our on-line consumers are reasonably educated about the true state of the economy by virtue of their cyber-connectivity -- thereby causing them to become more conservative in their spending habits than the "great unwashed hoards."

So, back to the original question: when will a "re-convergence" start to happen? It will probably be either when:

-- Governments run out of stimulus monies, and the whole GDP drops down to meet the line traced by our consumers; or,

-- The "recovery" finally reaches our consumers.

Unfortunately, our guess is that the former is far more likely than the latter.

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