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UPDATED U.S. ECONOMIC OUTLOOK:

Mixed Signals on Consumer Spending

Plus Bonus Feature: Scenario Planning 101 for 2021

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Mixed Signals on Consumer Spending, Plus Bonus Feature: Scenario Planning 101 for 2021

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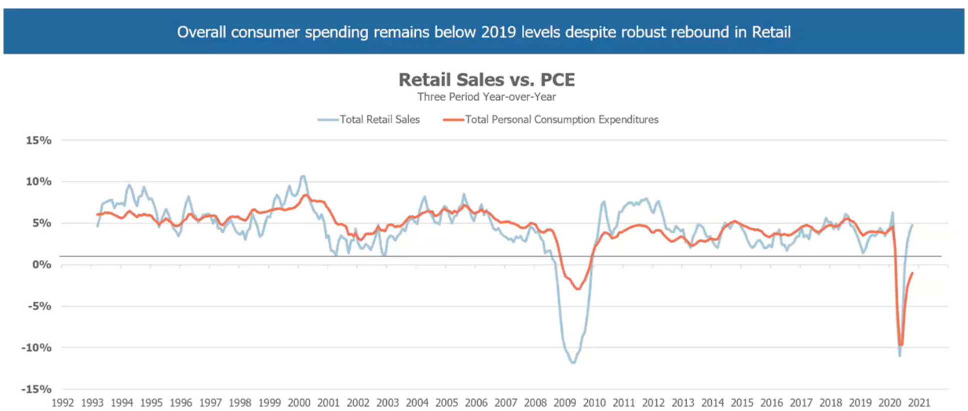
Overall, the economy is still tracking in a soft recovery as expected. There have been no significant changes over the last few weeks to our overall GDP forecast here at Prevedere, and we still expect the recovery to continue into 2021. Of course, that depends on the pandemic. But, from a total GDP standpoint, many of our key macroeconomic indicators are tracking in line with our recovery expectations.

Mixed Signals on Consumer Spending



One of the surprises of this recession is how fast of a rebound retail sales have experienced. When you look at media headlines indicating that they are back above year-ago levels, it's like the recession never happened. Total retail sales from the Census Bureau suggest that sales are growing at a 4 to 5% clip. That's pretty much where they were before the pandemic. So what's going on? Is the U.S. in a recession or not? Are consumers cutting back or not?

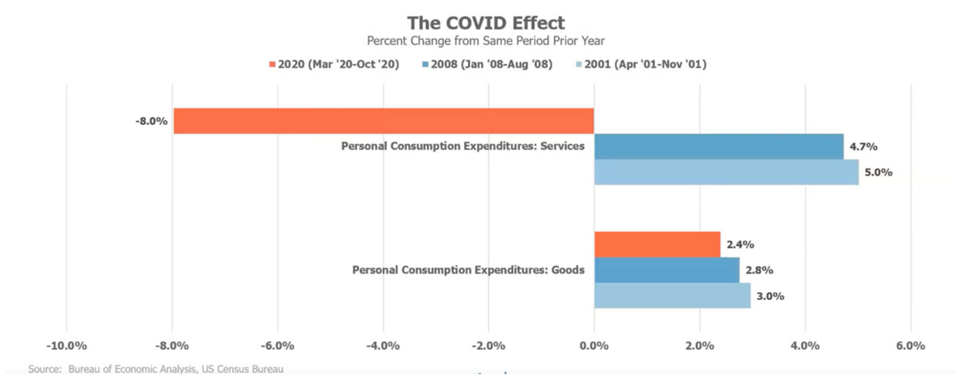
The broader perspective is that total retail sales don't cut it from fully measuring this pandemic's impact. Why? Because total retail sales aren't total. It is a measurement of actual stores and retailers. However, this isn't just the only thing that people spend on. It is heavily biased towards retailers of goods, both online and in-store. What this doesn't cover are things like going to a lawyer or hiring a babysitter.

Total personal consumption expenditures from the Bureau of Economic Analysis include things that do not require actual retail transactions. That data indicates that the recovery doesn't look as V-shaped and not back to pre-recession levels on a year-over-year basis. In fact, it's still down about 1% on a year-over-year basis. If you look historically, these two data sets tell very different stories about the nature of the economic cycle this time around.

In looking at total retail sales, it dipped down as much as the Great Recession back in 2009, but the recovery has been swifter and now back to year-over-year growth. In past recessions, such as 2000 and 2001, total retail sales didn't even go into contraction, and that's normal if you look back through a 100-year history. Often, recessions are not bad enough for consumers to pull back their spending. They merely slow it down.

However, total personal consumption expenditures, both spending at physical retail stores and online and services, went much lower than in 2009, especially in 2001, but the recovery is not entirely there. This makes sense as this pandemic has specifically hit services.

Spending Patterns Have Shifted



The chart above illustrates the difference in the COVID effect or how it is different from other recessions. In looking at personal consumption expenditures, which was the red line in the previous chart, this chart breaks it out into its two components: whether consumers are spending dollars on goods or spending dollars on services.

In this chart, the red is measuring the COVID-19 recession and comparing that to the recessions of 2008 and 2001. This shows some comparison to other times where the economy was in recession and what the consumer was doing. Consumers were always spending on goods in past recessions. They are still spending on goods in this recession, but spending is slightly weaker than the previous two recessions.

A significant difference that we are currently seeing from consumers is that they are pulling back spending on services. Their spending levels in previous recessions have been much higher. This is the big gap, an 8% reduction in spending on services year-over-year versus ongoing growth, even during recessionary conditions, on services in the past two recessions.

There are some key takeaways to be gathered from this. The first is that the Bureau of Economic Analysis total personal consumption expenditures illustrates that we are in a recession, and there is a contraction in consumer spending. However, this data is somewhat overshadowed by heavily reported retail sales numbers that do not capture the whole picture.

From a business standpoint, a key takeaway is that many businesses that have not been forced to shut down are getting some boost in 2020 from share of wallet gains. This COVID recession has created winners and losers. Either you are going out of business, or perhaps because consumers have nowhere else to spend their money, they are spending it in your industry. The wallet is shrinking overall for consumers, but because so many services are unreachable right now for consumers, they are paying relatively more on other things like groceries, home improvement, and online sales.

Conclusion

Our advice about 2021 is to watch out for the post-covid whipsaw. Suppose any significant portion of consumer spending reverts to the old distribution of services and goods that have been neglected for the past nine months. In that case, many retailers and businesses that are on a high from the share of wallet gains in 2020 could see their recession in 2021 as consumer spending moves back to more traditional ways and proportions. However, consumers have less to spend overall.

While we are in a recession and consumers are spending less, your business or your industry might not be feeling the effect of it, or on the flip side, you might be massively feeling the impact. Either way, watch out for the whipsaw effect in 2021 because that will likely happen as we start to move back to some normalcy.

Of course, this is in anticipation of a vaccine and COVID-19 not being the headline story for the entire year of 2021.

Economic Scenario Planning 101 For 2021

Prevedere's advice to our customers when thinking about 2021 is that it will be different from 2020 in several ways from a planning perspective. In 2020, the unfortunate effect of COVID on forecasting and planning is that you simply could not plan. The pandemic hit, and everything ground to a halt. Companies were left with economic indicators and historical relationships that no longer mattered. There was no data and much uncertainty about what would happen in 2020. Now, in December, there are practically nine full months of pandemic data. Businesses should be taking that valuable information and using it to understand the post-COVID effects on their business.

We recommend starting to build two sets of dashboards. The first dashboard should include pre-COVID indicators, which are the basic run of the mill leading indicators that everybody should have been monitoring well before the pandemic. These include how data such as household income or employment rate impacts your business. Those indicators might not be as relevant today. However, as we move towards a post-COVID society and start to get, hopefully, back to more normalcy, some of those key traditional lead-lag relationships and economic impact indicators are going to matter again for your business. Hence, you need to be monitoring those.

We also now have nine months of data on economic factors that have drastically increased in importance due to COVID-19. Picture a center aisle grocery manufacturer for something like chocolate chips. Your pre-COVID dashboard might include many indicators like is my product priced or promoted and marketed at the right spot in the right location to capture the steady business of selling chocolate chips. Some economic factors might also matter, like is employment going up or down.

In a post-COVID society, you might find the biggest factors for chocolate chips are things like people eating more at home, conducting Google searches for cookie recipes, or spending less out on restaurants. This is a whole different set of indicators. People might have searched for recipes at a very stable rate before the recession and COVID, but then that spiked. So what was a marginal indicator before becomes a relevant indicator now. Keep that indicator in a second dashboard alongside pre-COVID indicators to monitor how your business is aligning.

Importantly, as a vaccine becomes available, cases start to go down, and people's choices broaden, it's going to be very important to know whether people are baking less at home now that they can go out to restaurants or have they picked up a new habit that is going to be a positive tailwind to your business.

Economic Scenario Planning 101 For 2021 (cont.)

Behaviors such as these can be monitored through economic data, and companies can start to understand trends in consumer sentiment, consumer habits, and online search behavior. Much real-time data is available, and companies can track whether there is a sustained trend-shift or something that has created new patterns because of the pandemic.

This goes beyond just the grocery store example. There are home improvement trends as people have been spending more renovating their houses and their backyards. There is a significant demand for pools creating a backlog because people want to vacation in their backyard. Will that change after COVID-19 goes away, or will this start years of new habits where people are more comfortable spending more money and time near the home?

Economic data allows you to monitor trends and decipher which are near-term, COVID related trends and which are here to stay for the long term.

The big difference between 2020 and 2021 is that in 2021, we have data. There are now use cases for what a COVID-19 economy looks like versus a non-COVID economy. Yes, the future is uncertain, but at least data is available, and models can be built off of that data to track and monitor the economic recovery and the COVID-19 situation.

No matter which way COVID-19 tracks over the next couple of quarters, some relationships have been identified that can be applied to say that sales are likely to do “x” if “y” happens. However, if COVID-19 remains and we find ourselves in the same situation two quarters from now, data is available for that too.

Just some food for thought as you look out towards 2021, the planning environment is right for new analysis. Companies no longer have to guess. Some data is available and should be leveraged to make better plans, even though there is still an elevated level of uncertainty.

Navigate What's Next with Economic Scenario Planning

The COVID-19 crisis has given rise to a world of economic uncertainty, with uneven effects across regions and industries. As we head into the 2021 planning cycle, every business wants to know how the pandemic will impact next year's numbers.

Prevedere's Economic Scenario Planning solution helps companies navigate these tumultuous times. The solution projects future business outcomes for three plausible macroeconomic scenarios under COVID-19. Companies can use these insights to sharpen 2021 forecasts and plans, improve shareholder guidance, and stay on top of the pandemic's evolving impact.

Click here to learn more about Economic Scenario Planning. >>

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