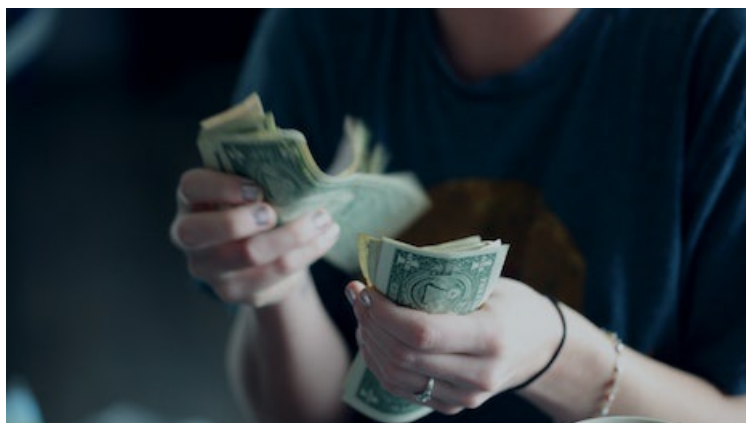


RETAIL

How consumer spending fared so far through 2020

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The biggest decline this quarter was in consumer spending on services, down 13.3 percent, led by steep drops in expenditures on health care, transportation services, recreation, travel and dining out

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By now, you have heard the news that the **United States GDP contracted 32.9 percent in the second quarter** on an annualized seasonally and inflation-adjusted basis, following a 5 percent decline in first quarter.

Personal consumption makes up over two-thirds of the U.S. GDP and it dropped even more precipitously, down 34.6 percent on an annualized basis. This quarter marks the economy's worst since the government started calculating GDP over 70-odd years ago.

However, in real terms, the decline in personal consumption was not as bad as the headlines suggest. That is because the Bureau of Economic Analysis reports data on an annualized basis, which essentially shows the results projected for the rest of the year if the quarter's current rate of change was to continue.

Economists favor annualized and inflation-adjusted rates because it allows them to compare data over different time periods, but for the rest of us, it is merely confusing.

In the second quarter, there was an actual 10.5 percent drop in personal consumption, or what people were spending their money on. That is bad, but not nearly as bad as the annualized number, which is driven by the dramatic short-term changes caused by the COVID-19 pandemic.

The biggest decline this quarter was in consumer spending on services, down 13.3 percent, led by steep drops in expenditures on health care, transportation services, recreation, travel and dining out.

But purchases of consumer goods typically bought at retail were also down by 4.5 percent, with durable goods, defined as items expected to last three or more years, dropping 1.5 percent and nondurables down 5.9 percent.

With the economy now in recession, recovery will require American consumers to do their part and get back to spending. But that is a big ask, with **unemployment rates rising** again for the first two weeks of July after showing improvement since mid-March.

Not only must more Americans get back to work, so they have money to spend, but they also have to recover their confidence to spend. That may take longer.

Consumers need confidence in order to spend

Data intelligence company Morning Consult, which takes the pulse of American consumer confidence weekly, most recently found its **Index of Consumer Sentiment** dropped beginning in July, as unemployment and the number of COVID-19 cases started to rise.

Renewed fears of contagion are keeping more Americans on the sidelines when it comes to spending, even as retail shops, malls and restaurants are starting to reopen.

In another Morning Consult survey conducted with **Bloomberg** at the end of June, it found "waning interest in public events and material things, like appliances and clothes, and a new austerity, expressed through pantry stockpiling and delayed big-ticket purchases."

Based on these findings, the researchers conclude: "This foreshadows an era of fear and frugality that could push a full economic rebound one that Washington and Wall Street are banking on out of reach. The data also raises doubts about how much rising consumer confidence will translate into spending, on which the economy heavily relies."

Trends in what people are and are not buying

Retailers large and small depend upon consumers' willingness to spend for their livelihood.

With the Bureau of Economic Analysis (BEA) providing the most authoritative source of data about what consumers are spending their money on, as opposed to the monthly retail trade report by the Census Department which only tells about where consumers are shopping, I dug into BEA's underlying NIPA tables.

The BEA cautions users that its underlying tables, specifically Table 2.3.5U, are not as reliable as the "higher level aggregates" it publishes more widely. That said, it still is an excellent source for trends in spending for nearly 150 categories of consumer goods.

And since trends in consumer spending at the detail level are important for retailers to understand, here is what people are and are not buying now and what it indicates for the rest of the year. This analysis compares spending from first half of 2019 to that of first half 2020.

Motor vehicle spending was off 6 percent, but SUVs and light truck spending held firm

Consumers have put car buying on hold. New car spending, which is nearly twice as large as used cars, was down 6 percent and used cars off 20 percent.

The only bright spot in new car purchasing, if you can call it that, was SUVs and light trucks with spending flat year-over-year, but this is also by far the largest category in new cars, so its strength bolstered the entire new car category. Foreign car spending was off more, 34 percent, than that on domestic cars, down 24 percent.

Notably, the second half of 2019 was stronger for motor vehicle spending than the first, so if current trends continue, this year will do serious damage to motor vehicle retail, even more so if consumer confidence continues to chill. In the short term, few will feel confident enough to commit to years of car payments.

Home furnishings stayed steady, with outdoor living furnishings and equipment leading

Home furnishings durable spending held even in the first half of the year, compared with last year. The most notable trend here was a shift from decorative furnishings toward the more practical.

For example, lamps and lighting, rugs and tabletop spending declined, while spending on tools and equipment for home repairs rose 8 percent, especially outdoor living furnishings and gardening equipment up 9 percent.

Furniture, the largest segment within the home furnishings category, rose less than 1 percent. And these purchases can be motivated by both decorative and practical needs.

In household appliances, spending on major appliances was even with last year, while consumers invested more on new countertop small electric appliances, up 6 percent, reflecting more time spent preparing food at home.

This category tends to rise and fall with trends in the overall housing market. **Realtor.com reports** that homebuyers started to return to the market in June, but limited housing supply was the biggest drag on growth.

Both trends will favor growth in the home furnishings durable category. People buying homes will need new home furnishings and people staying put will continue to invest in improvements that will enhance living in their homes.

Recreational goods and vehicles posted strong growth, with sporting goods spending especially strong. This is a broad reporting category, including spending on products ranging from computers to motorcycles, guns to pianos, and televisions to books.

With people spending more time at home and few places to go, they were bringing entertainment and recreational activities into their homes, giving an 8 percent boost in spending in this category. This made it the second-fastest growing category overall behind food and beverage.

The largest segment in this category was video, audio and computing equipment and it got a 6 percent bump in spending, led by personal computers, tablets, and peripherals, up 9 percent.

Notable shifts in this segment were reduced spending on records, audio discs and audio downloads, and more on video discs and downloads.

On the other hand, trends in spending on equipment to play these media were reversed. Television spending was down 1 percent, while spending on audio equipment rose 10 percent.

Sporting equipment, including balls and bats, home exercise equipment and guns, rose 13 percent, and recreational vehicles such as boats, bicycles and motorcycles advanced 10 percent. Books were flat and musical instrument spending declined 4 percent.

This should remain a strong category through the rest of the year as well as into next year. The shift toward working at home will propel computer sales and people will continue to be more self-reliant when it comes to entertainment and recreation, favoring spending in this category as well.

Other durable goods spending down sharply, comprising luxury goods such as jewelry, watches and luggage. The other durable goods category is a hodge-podge of items, including luxuries such as jewelry, watches and luggage, and practical items such as eyeglasses and therapeutic medical supplies.

Overall, this category dropped 14 percent from previous year with luggage off the most, down 20 percent, which is not surprising given nobody is going anywhere now.

Luxuries such as jewelry and watch spending dropped 15 percent, but even practical spending for therapeutic medical equipment and eyeglasses dropped 13 percent.

Food and beverage spending boomed in the shutdown, up 10 percent.

This category across the board was strong during the first half of the year, with most reported grocery segments, such as cereals and bakery products, meats and poultry, fish and seafood, milk and dairy, fresh fruits and vegetables all showing double-digits gains.

Rising more slowly were sugar and sweets, up 6 percent, and nonalcoholic beverages, up 7 percent. On the other hand, alcoholic beverages led the category in growth, rising 12 percent.

Prospects for this category depend on when restaurants reopen but even more importantly, on when consumers feel secure to dine out.

The latest [Morning Consult survey](#) from the end of July finds just over one-third of Americans feel comfortable now to go out to eat, though about half expect to feel comfortable three months from now or less. But this sentiment is fluid, depending on the rise and fall of COVID cases locally.

Clothing and apparel spending took a dive.

With consumers staying home, there is no need to buy clothes or shoes. Spending in this category dropped 19 percent, with spending on children's and infant clothing falling less, off 13 percent, than that of women's and men's.

Prospects for this category will depend on when people can return to work and children to school. Until then, they will have little need to update their wardrobes, and spending in this category will continue to lag.

Spending on gasoline down the most, giving people more money to spend elsewhere.

With people driving less and gasoline prices lower, overall spending on gasoline and fuel oil dropped the most, down 25 percent.

This has benefited consumers greatly, giving them more money to spend on other things, though it has hurt convenience stores and gasoline stations, which saw their [retail sales drop](#) nearly 20 percent year-over-year through June.

Other nondurables stayed strong with more pharmaceutical, game and toy, and household cleaning product spending

Rounding out this look at consumer spending is another hodge-podge "other" category.

Overall, other nondurable spending rose 6 percent, with growth strong in magazines and newspapers (19 percent), games, toys, and hobbies (11 percent), pharmaceuticals (7 percent), and household cleaning (7 percent) and paper products (7 percent).

Notable exceptions in this category were a 4 percent decline in household linens and 5 percent reduced spending on cosmetics, perfumes and other beauty products.

On the other hand, people spent 2 percent more on practical, necessity products for personal care, like hair care, dental and shaving products, and 6 percent more for electric personal care appliances, like shavers.

As with apparel purchases, future trends in this category will depend on when people can finally escape the confines of their homes. However, they may continue activities necessitated by the stay-at-home orders afterward, such as more attention to home cleaning, new hobbies, and more magazine and newspaper reading.

Newly established personal care routines also may continue, with women reducing their pre-pandemic beauty regimes and men spending more on their personal grooming. And all are likely to put more emphasis on essential personal care (teeth, hair and skin), which directly impacts personal health.

What this means for retailers

Many analysts are pushing back against the "new normal" narrative after the pandemic's extended disruption of everyday life in America, which includes shopping. I am with them.

Americans have "woke" to the fragility of their health in the face of an unseen enemy virus. Anxiety has risen to an all-time high, and people want nothing more than to take constructive actions to reduce it.

Americans have been forced to radically change their lives. In the process, they have adopted new habits and behaviors that ultimately will enhance their wellbeing across three interconnected dimensions: physical wellbeing (health), emotional wellbeing, and financial wellbeing.

They will continue to focus on health and safety, even as the pandemic threat subsides. So, they will lean into healthier food choices, continued home and personal care cleansing practices, and more active lifestyles that do not require going to the gym. Getting more physical activity will directly enhance their emotional wellbeing.

Restoring emotional wellbeing will hinge on feeling safe and secure. So when they return to restaurants, stores, and shopping malls, they will be vigilant to observe health and safety practices in these enclosed spaces. These places will have to be pristine, and service providers, even when they can remove their face masks, must be trained to maintain social distance.

And finally, Americans are going to pursue money-saving measures that will ensure continued financial wellbeing. As the recession takes hold, people will hang on tightly to what they have. Purchase decisions will be made favoring necessity as opposed to discretionary spending in order to reduce financial exposure in case the other shoe drops on their personal finances.

Of course, the affluent consumers at the top 25 percent of U.S. households will have more financial immunity than middle-and-lower income consumers. But they are likely to continue to be cautious into 2021 and refrain from unnecessary spending just like everyone else.

Since these high-income consumers account for nearly 50 percent of all U.S. consumer expenditures, their continued restraint will impact retailers in every sector, not just luxury.

My advice for retailers is not to look for a "new normal," rather expect more of the same through the rest of this year and into next. And with consumers' tilt toward more practical purchasing, gift selections this holiday season are likely to tilt this way as well, even as holiday spending is expected to be more constrained.

Retail is in for a long, hard slog, and retail success, even survival, will depend on caring for the wellbeing of their customers with products, prices, shopping environments and customer service that builds and maintains that.



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