



Scattered Sunshine

Experts give retail sales a cloudy forecast for the rest of 2009, but some bright spots exist

By Richard H. Gamble

Having watched the number and value of their business transactions drop off instead of grow over the past eight months, ISOs, acquirers, and merchant processors anxiously await the months ahead. But while those who predict future economic activity say the worst is probably over, they hesitate to forecast much improvement this year.

The most likely prognosis for the remainder of 2009 is that the economy will stall at a depressed level, says Richard Hoey, chief economist at Bank of New York Mellon. Middle-class spending will depend largely on job prospects; upper-class spending will depend largely on wealth, principally stock portfolios.

"We're forecasting a negative 0.5 percent growth for 2009, with modest gains in the second half, but those are compared to weak 2008 numbers," reports Scott Krugman, vice president of the National Retail Federation in Washington, D.C. "Everyone is afraid to declare a bottom to this recession."



"We don't expect a strong recovery in 2009, but we expect to start seeing signs of stabilization toward the end of the year," offers Robert Dye, vice president and senior economist for the PNC Financial Services Group in Pittsburgh. Spending is being dragged down by diminished wealth in investment portfolios and home equity, and by the growing threat of unemployment. While the stock market could bounce back quickly, it will take time for housing and employment to turn around, he suggests.

Look for a slight bounce in the fourth quarter, after sharp declines during the first half of the year and a small decline in the third quarter, suggests Dana Johnson, senior vice president and chief economist at Comerica Bank in Detroit. The culprit will be job losses.

"Income is the big driver," he says, noting the net savings rate, which at press time was about 5 percent. "I expect the savings to hold steady at 5-6 percent, in which case spending should track changes in income." But if consumers are more upset and sock away more than that amount, spending will suffer, he says.

But all forecasts are tentative. "There's unusual uncertainty in this economy," Johnson notes. "We're dealing with circumstances we've never seen before." People are reacting to the "huge destruction in household net worth" due to the halving of stock portfolios, many of them retirement accounts, and the rapid fall of home prices in some regions. "We really don't know how much consumers will throttle back spending" in response, he explains.

The second half of 2009 is "a wild card," says economist Scott Hoyt, senior director of consumer economics at Moody's Economy.com. "Our baseline forecast is for things to get better in the first half of 2009 and for those gains to carry over into the second half of the year. It may not be as strong as the first half, but it won't be bad."

A number of factors, however, could throw off that forecast: "If we don't get the financial markets closer to normal, if the stimulus doesn't work as intended, if the global downturn is worse than it looks now," Hoyt cautions. "It's not hard to construct a credible scenario where 2009 looks a lot like 2008—pretty decent in the first half and then really going downhill in the second half."

Stimulus' impact on consumers

The economy comes into spring "off good growth in January and no give-back in February," Hoyt says. Consumer spending is boosted by a reduction in tax withholding and increases in transfer payments, especially to lower-income households, which necessarily spend most of their income, he points out.

That's good news in the short run, and more encouragement should come via the stimulus bill, which increases funds for food stamps and unemployment benefits and lowers tax withholding. Unlike the tax rebate, which was a one-time check in the mail, this will be a steady stream of larger paychecks that, barring layoffs, should sustain modest growth in spending throughout the year. Even if there is no growth, Hoyt says it shouldn't be as terrible as the 4 percent decrease in real consumer spending that torpedoed the economy in the third and fourth quarters of 2008.

How much of a larger paycheck will go into spending and how much into saving depends on consumer confidence, Hoyt explains, and confidence is tied to home values. "Both disposable cash and home values are important to confidence and spending," he says. "The ability to spend is tied to income. The willingness to spend is tied to wealth, which is strongly linked to home values." If consumers have the cash, they probably won't wait for home values to start rising before they start spending; just a real slowdown in the rate of decline in value should give them a feeling that they can see light at the end of the tunnel and that the worst is over, he reasons.

The higher spending numbers from January and February aren't a significant sign of hope, warns Mark Vitner, senior economist for Wachovia Corp., based in Charlotte, North Carolina, which is now owned by Wells Fargo Corp. "It's an illusion due to seasonal factors. There's normally a dip in January and February following a peak in holiday spending. This year, the holidays were so bad that there wasn't much of a peak, so the usual dip was mild and seasonally adjusted numbers showed some apparent gains. I don't think we'll see the usual spring pick-up in April and May this year. People won't be buying those new golf clubs."

Wal-Mart economy

The gloom is pervasive but not equally distributed. For example, a typical merchant portfolio in Texas is still holding value better than a typical merchant portfolio in southern California. But that gap is closing.

While the recession hit with a vengeance in areas where a big, speculative housing bubble burst dramatically, this recession is now remarkably widespread. "Virtually every state is in recession now or will be shortly," Hoyt reports. The only exception is the District of Columbia, which has too much government activity to be sinking, he adds. "There's no port in this storm." The hot housing markets got hit first, and that's still where foreclosures are at the highest levels. The industrial Midwest is suffering from the long-term decline in manufacturing, on top of the current recession. Areas that depended on energy and commodities held up better for a while, but are getting hit hard now, too, he explains.

Based on the type of merchants, some portfolios are doing better than others. "It's a Wal-Mart and McDonalds economy," Dye says. Business is migrating to the low-end retailers, the discount outlets, and fast-food restaurants as people economize. Some high-end retailers are holding up pretty well if their customers are insulated from the problems, but the middle-market is really getting squeezed, he observes.

The merchants doing the best are the places people go to save money for the things they have to buy—Wal-Mart, Costco, Family Dollar—Vitner says. Things are starting to improve a little for auto sales, where kinks in the availability of credit are being worked out. He calls the lack of credit there until recently "bizarre."

The big-ticket vendors generally are suffering the most. Because of the credit squeeze, items that people would buy on credit—automobiles, furniture, appliances, and anything tied to housing—are gathering dust because people either don't have the credit or are reluctant to use it, Hoyt says.

Education and health services are relative bright spots. "Jobs are holding up better there than in other industries," Hoyt says. Towns or cities with major universities or regional hospitals are faring better than average, he notes. And while drugstores are seeing business decline, prescription drugs are keeping them afloat more than some retailers, he adds.

Much of what happens during the rest of 2009 depends on whether consumers gain or lose confidence. When consumer confidence gets this weak, people respond by paying down their debts. From nothing at all in April 2008, the savings rate

rose to 5 percent in February 2009. "Some increase in savings is a good thing, but this big an increase is really hurting businesses that depend on consumer spending," Dye observes. "Consumer confidence is at its lowest level since the Bubonic Plague," he jokes.

Employment worries are now the biggest damper on consumer confidence, Vitner says. The first sign that things will improve will be a drop in first-time unemployment claims, he suggests.

When spending starts to rise, discounters will feel it first, Krugman predicts. Watch how much consumers are spending but also what they are buying, he says. Wal-Mart had seen grocery sales, among the most essential purchases, doing best last fall but now has reported some gains in home goods, he reports.

When consumer spending revives, cards should see a lot of the action. For many years, credit card growth has been relatively slow as consumers tapped the equity in their homes for spending money, refinancing, or using home equity lines at lower cost than credit cards, Hoyt points out. When consumer confidence revives and consumers resume spending, cards should look attractive again. **TT**

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