

Dutta's Economic Daily

Retail employment strength can't last

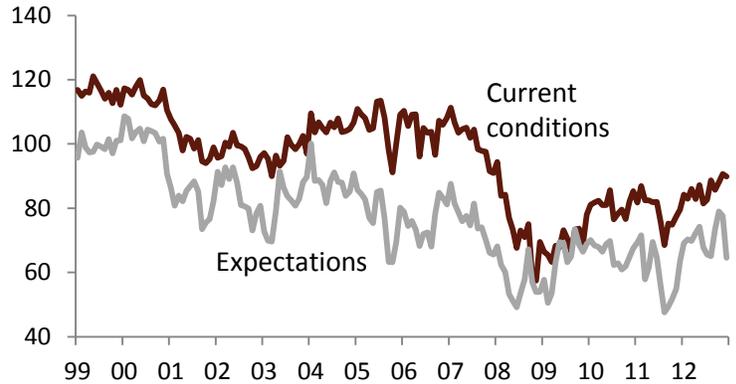
Monday, December 10, 2012

Consumer sentiment plunges

- The UofM Index of Consumer Sentiment declined 8.2pts to 74.5 in December from 82.7 in November, the sharpest one-month decline since March 2011 and the lowest level since August 2012.
- The drop was almost entirely in consumer expectations, which plunged 13.0pts or 16.8%. Current economic conditions fell 0.8pts or just under 1%.
- Normally, the equity market, gasoline prices, and jobless claims drive consumer sentiment. These metrics are trending in a favorable direction. We suspect the budget battle in Washington along with the threat of higher taxes next year is weighing on sentiment.

Expectations plunge, current conditions hold steady

UofM Consumer Sentiment

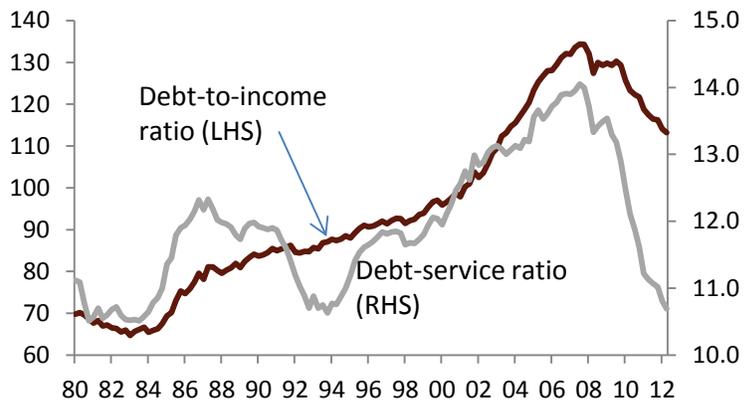


Source: Haver Analytics, Renaissance Macro Research

Household balance sheets healing

- Many pundits exclusively focus on debt reduction as a way for household to improve their balance sheets. One popular dictum, “Households must extinguish trillions more in debt to bring leverage ratios back to their pre-bubble averages.” In our view, the focus must be on a household's desire to be levered.
- The debt-to-income ratio takes a backseat to the primary decision, building net worth. Consumers do not target debt-to-income. Instead, they target a level of net worth to income needed to support future spending plans. Once they determine a path for future spending, they pivot to the second decision: how much leverage to take on.
- Consumers have made significant progress in repairing their balance sheets. Sure, there is some more work to be done, but we are nearing a point where can see the end of the upward adjustment in the personal saving rate. In the recent Flow of Funds report we learned that the household net worth to income ratio jumped to a cycle high of 543.2%, the best since mid-2008. The improvement was driven by an increase in real estate assets and equity prices.
- Higher wealth ratios tend to drive the saving rate lower and vice versa. The net worth to income ratio is (1) approaching its long run average and (2) consistent with a saving rate closer to 5%, implying another 1ppt increase in the household saving rate. This will help blaze the trail for a pick-up in consumption late next year.

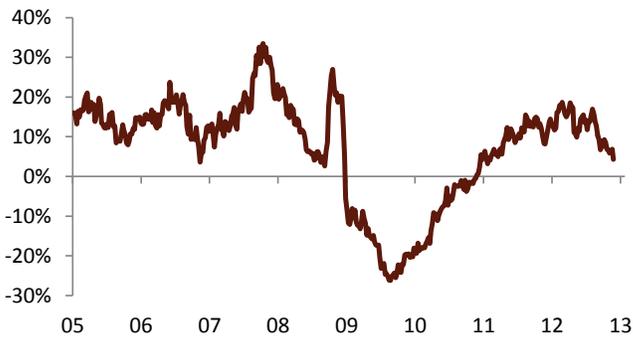
Household balance sheets improving (percent)



Source: Federal Reserve, Renaissance Macro Research

C&I lending slowing down

Commercial and industrial loans (13-week % change, annualized)



Source: Federal Reserve, Renaissance Macro Research

C&I loan growth slowing

- Commercial and Industrial loans contracted \$9.9bn for the week ending November 28th, the sharpest one-month drop since early 2010. On a three-month basis, C&I loan growth has slowed to 4.3% annualized, compared to roughly 15% in the first half. Something to keep an eye on – perhaps a sign of the Q4 inventory correction.

China export growth slowing

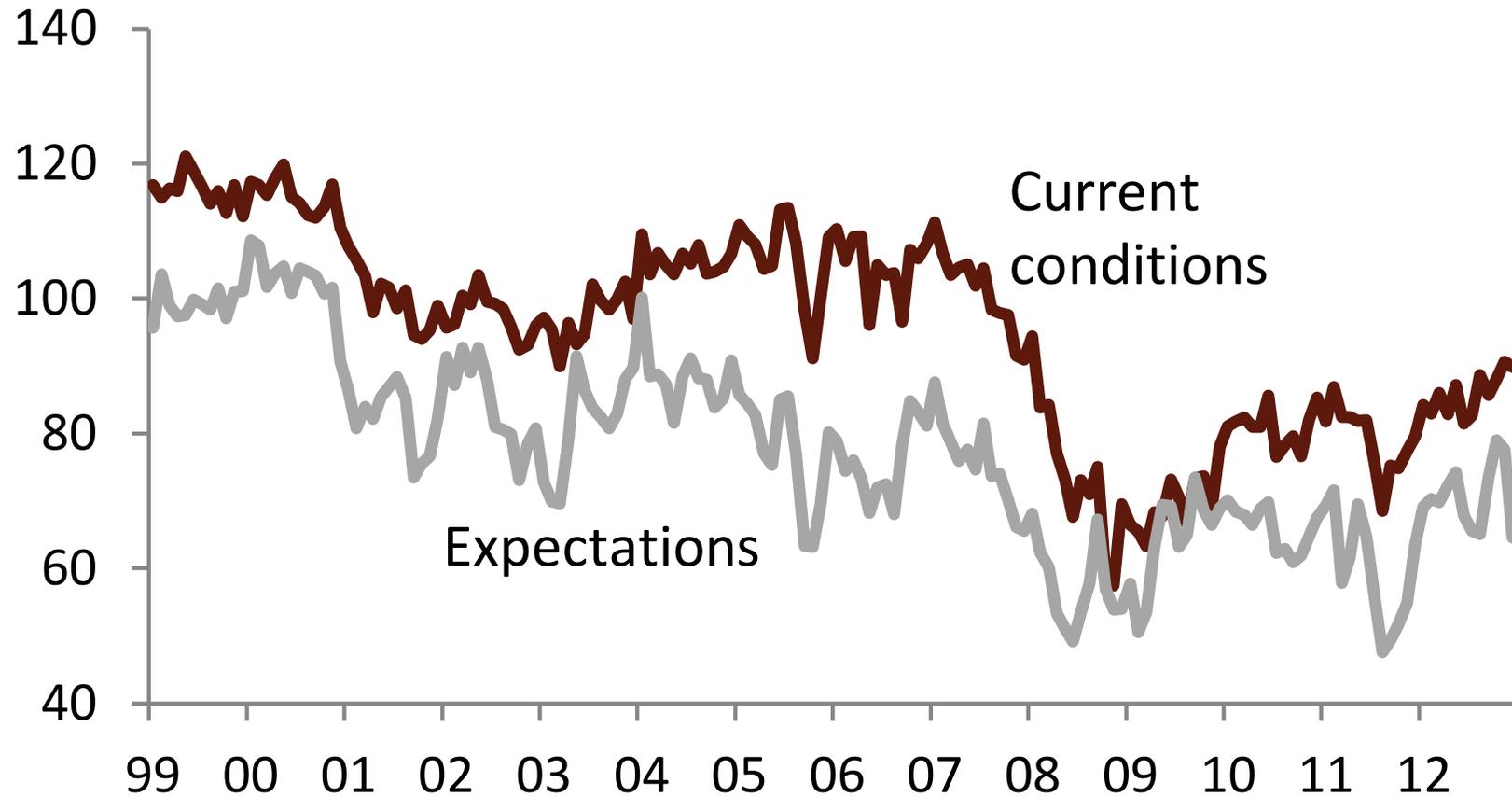
- China’s export growth slowed to +2.9% YoY in November from +11.6% in October, weaker than the market consensus of +9.0%. Exports to the US fell substantially to -2.6% YoY from +9%, the weakest since November 2009 – consistent with a weakening domestic demand backdrop.

Employment: Stable trend remains intact

- Nonfarm employment advanced 146,000 in November with downward revisions of 49,000 the prior two months. Because expectations were scaled back due to Sandy, last Friday’s employment data simply continues the slow and steady nature of the labor market recovery. Two follow up points that give us pause, suggesting a soft December.
- First, aggregate hours worked are running 1.7% at an annual rate from October-November. However, Q4 GDP is tracking just 1.0%, implying that output per hour – productivity – is declining. That is not good news for corporate profit margins. Companies are having a tough time re-establishing stronger productivity.
- Second, the timing of Thanksgiving likely introduced an upward bias in retail trade jobs last month. Retail trade employment rose 52,600 in November and is up nearly 475,000 over the last four months – this is not sustainable. Generally, what seasonal adjustment factors give in one-month, they take away in the next.

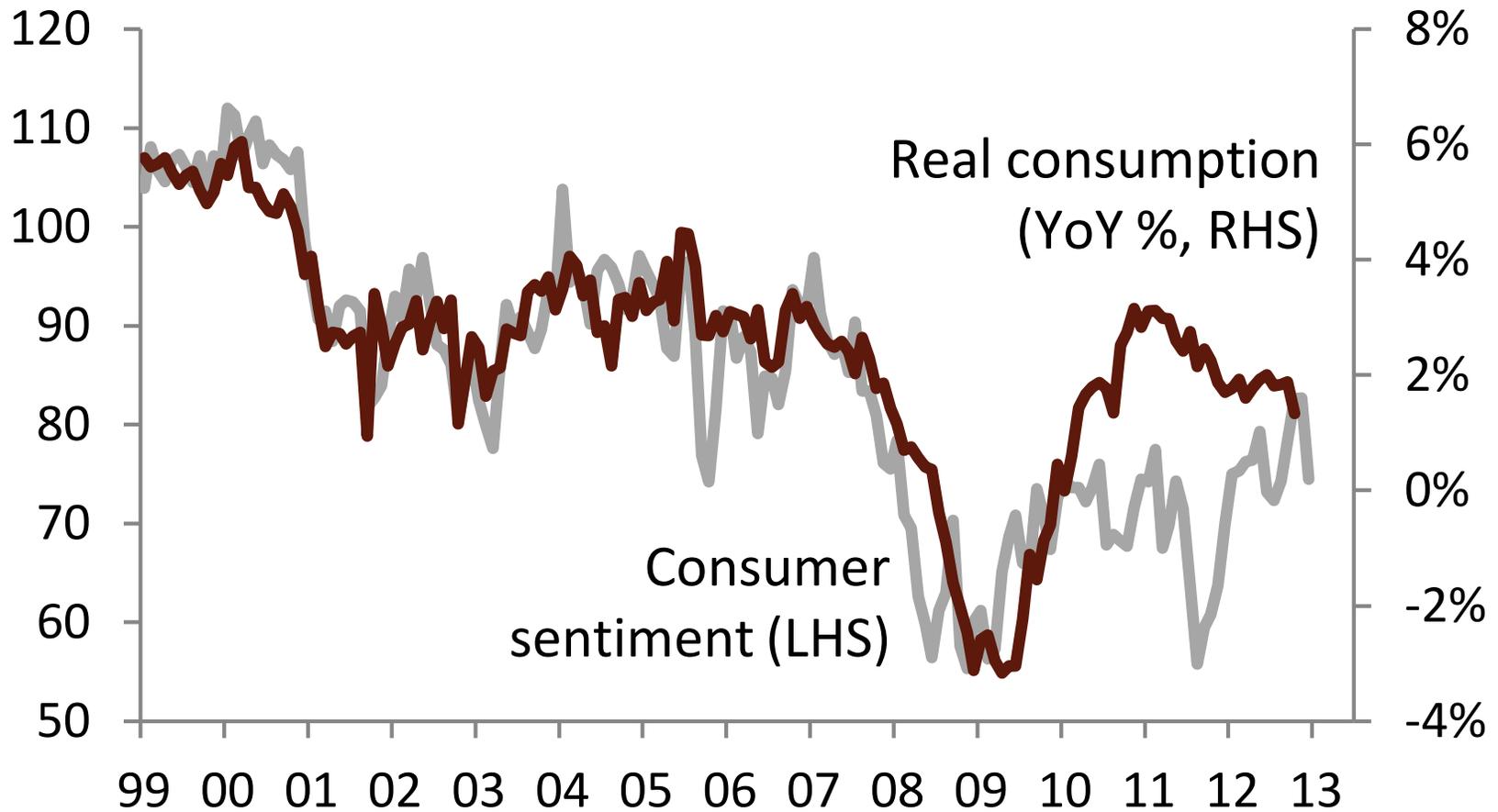
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UofM Consumer Sentiment



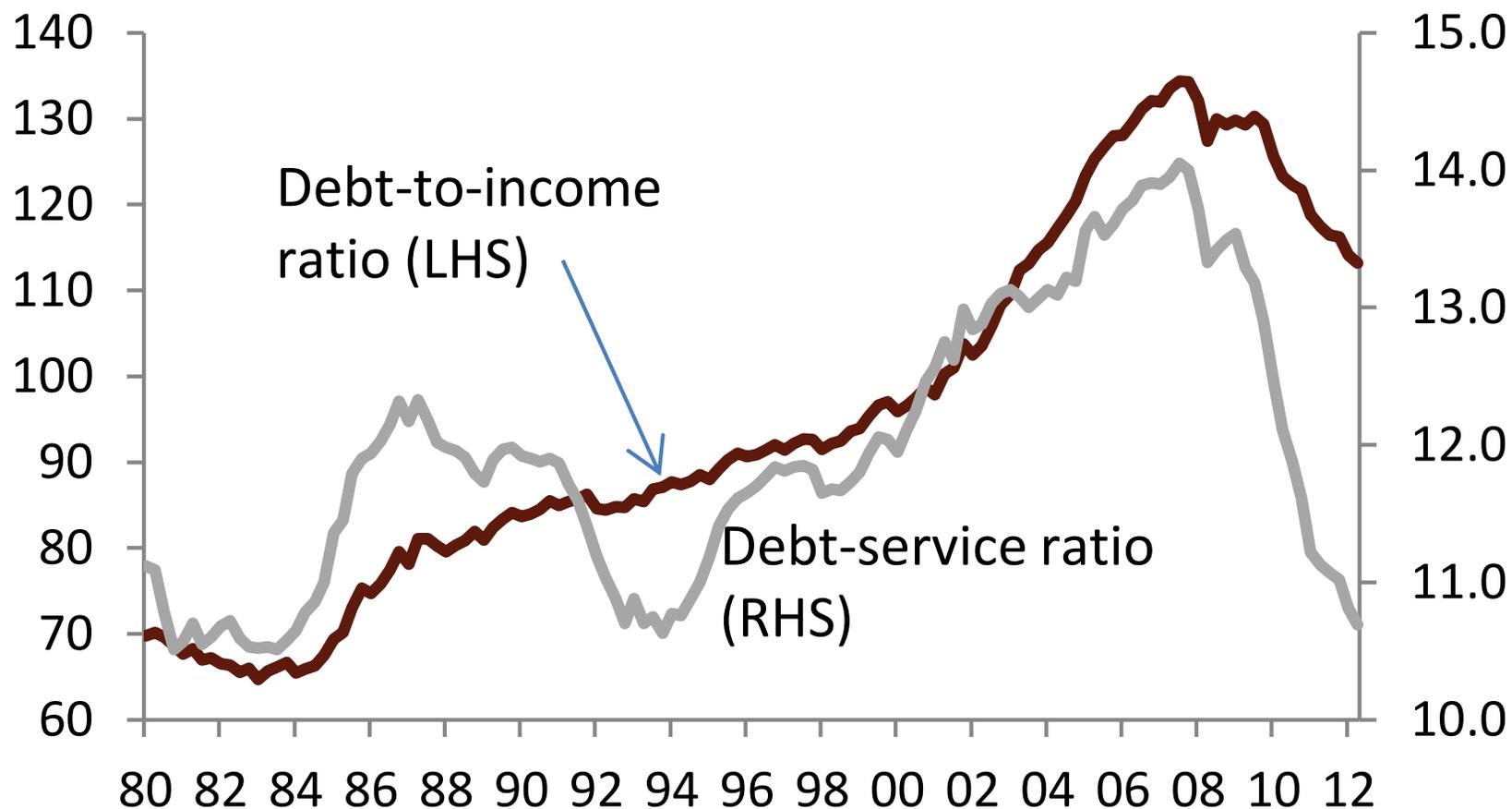
Source: Haver Analytics, Renaissance Macro Research

Sentiment vs. spending: An imperfect relationship



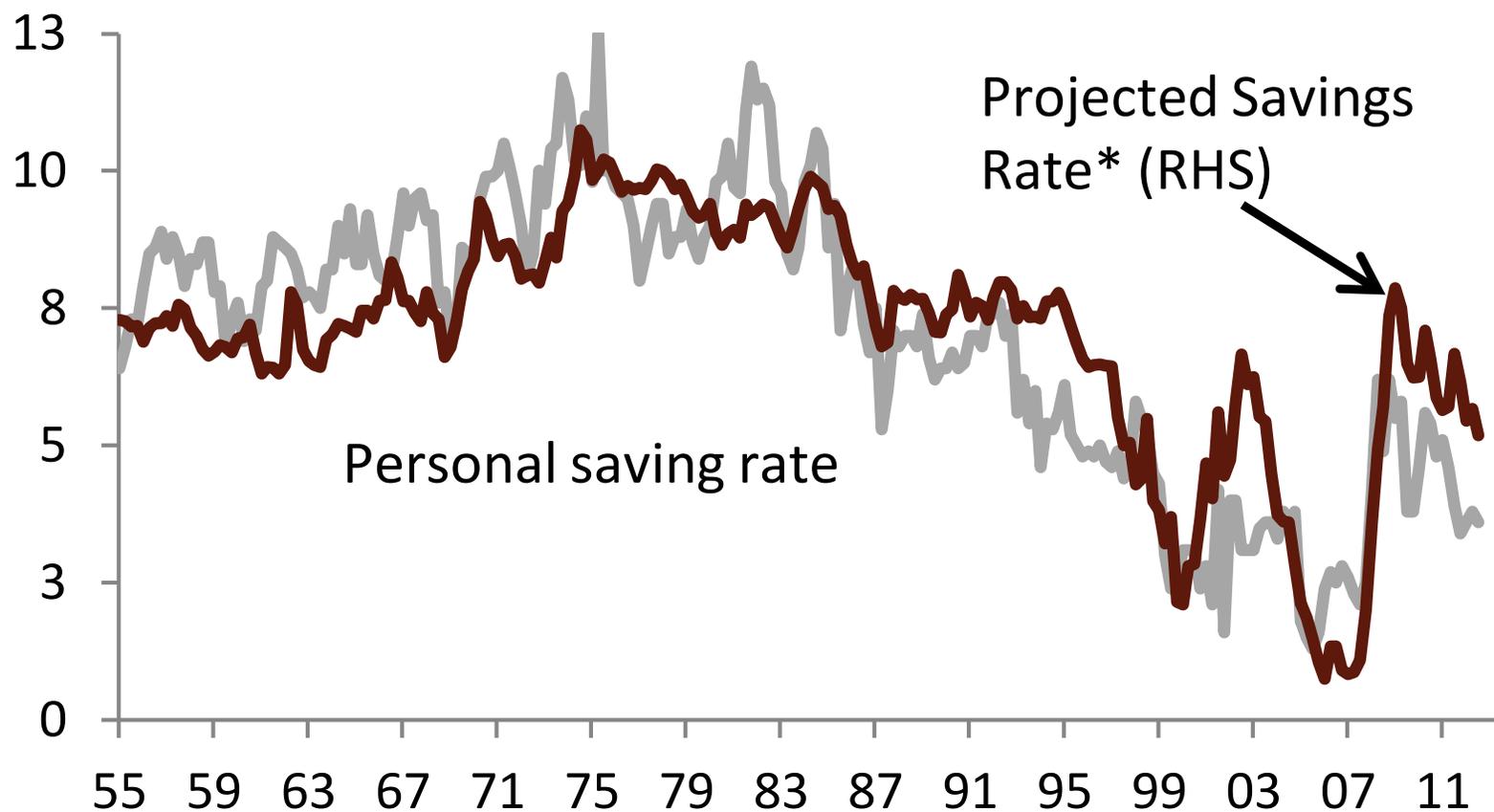
Source: Haver Analytics, Renaissance Macro Research

Household balance sheets improving (percent)



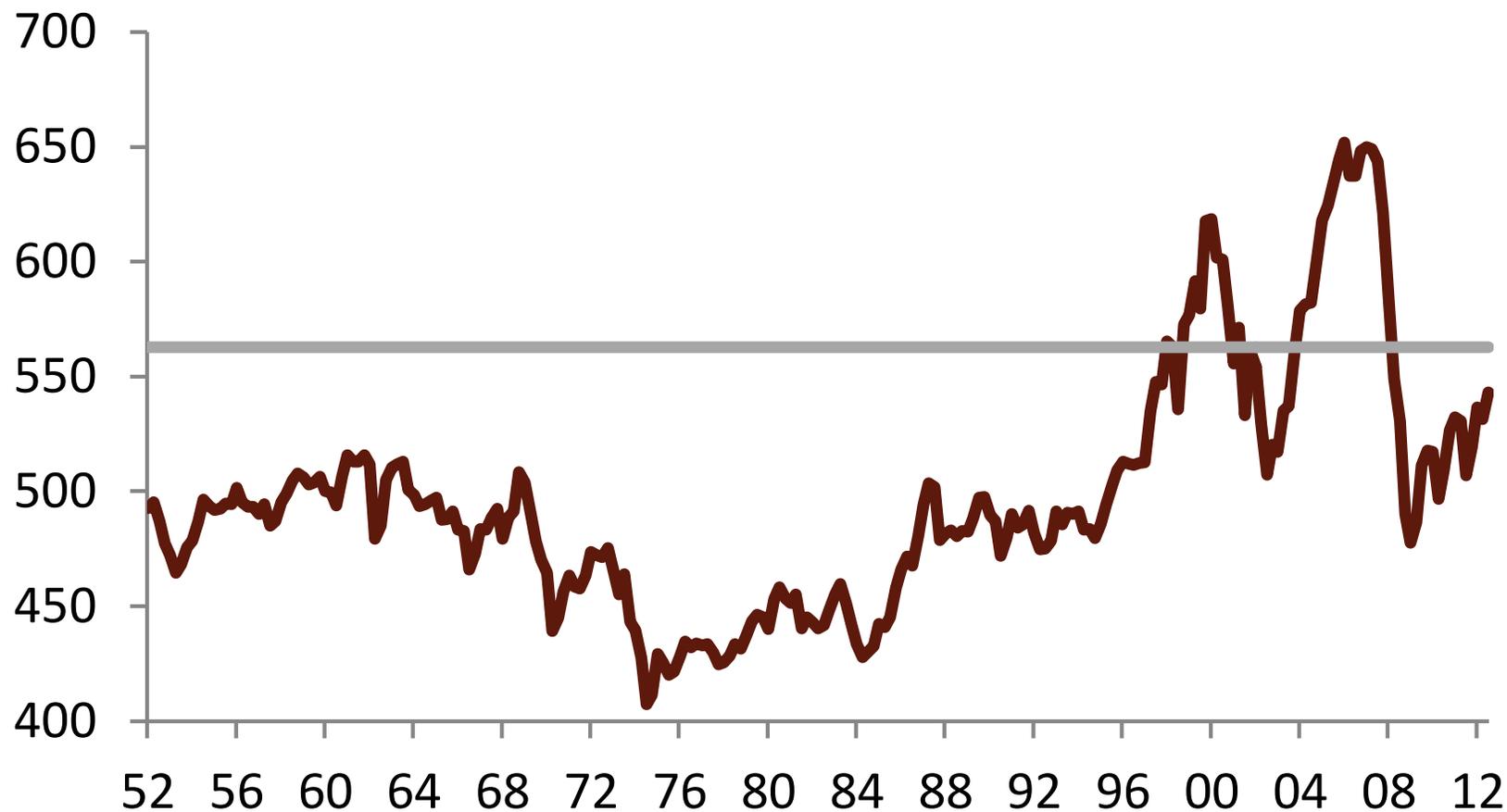
Source: Federal Reserve, Renaissance Macro Research

Consumers still need to save



*Projected saving rate using net-worth to income ratio
 Source: Federal Reserve, Renaissance Macro Research

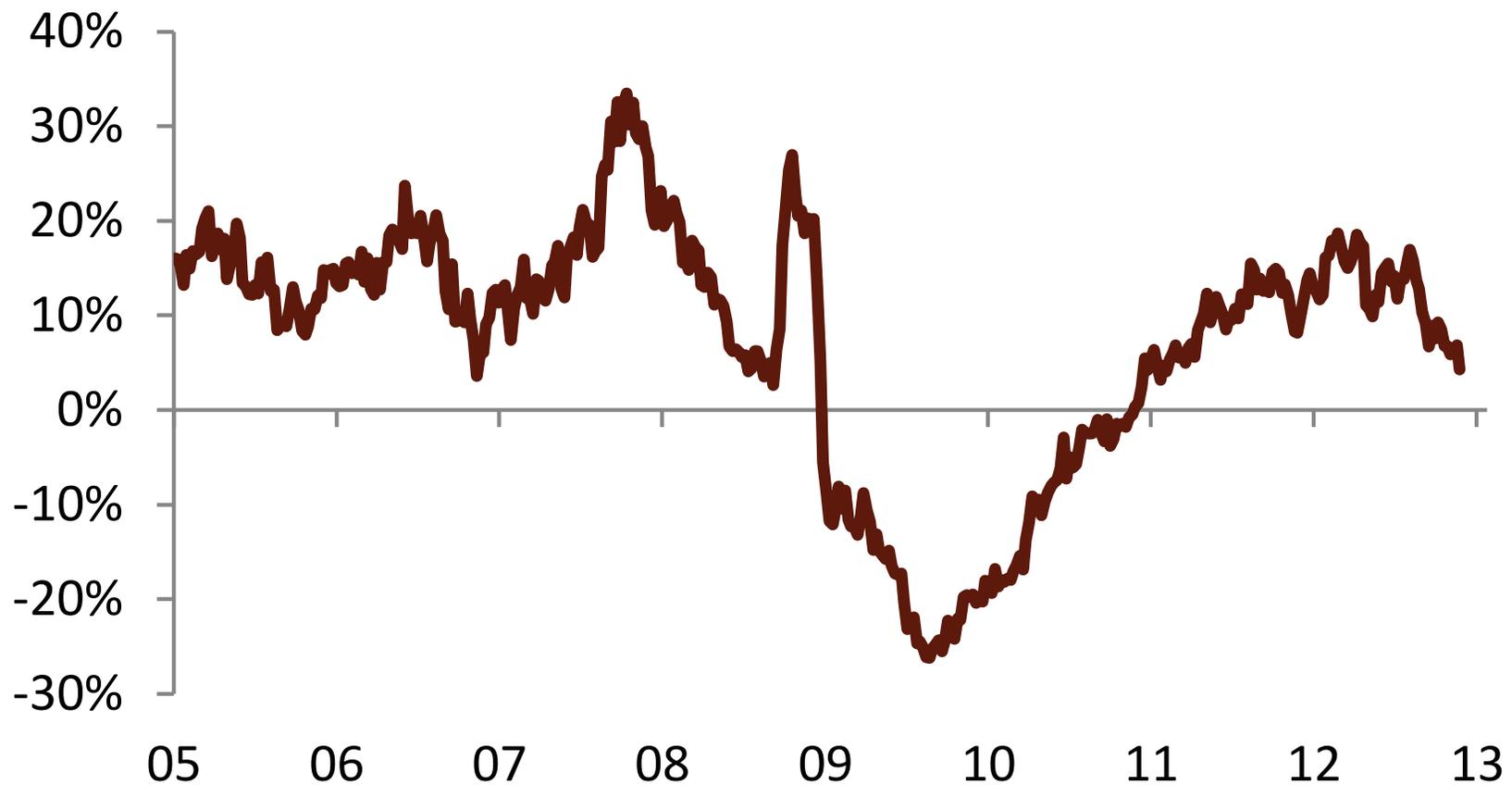
Wealth ratio slowly returning to normal (percent)



Source: Federal Reserve, Renaissance Macro Research

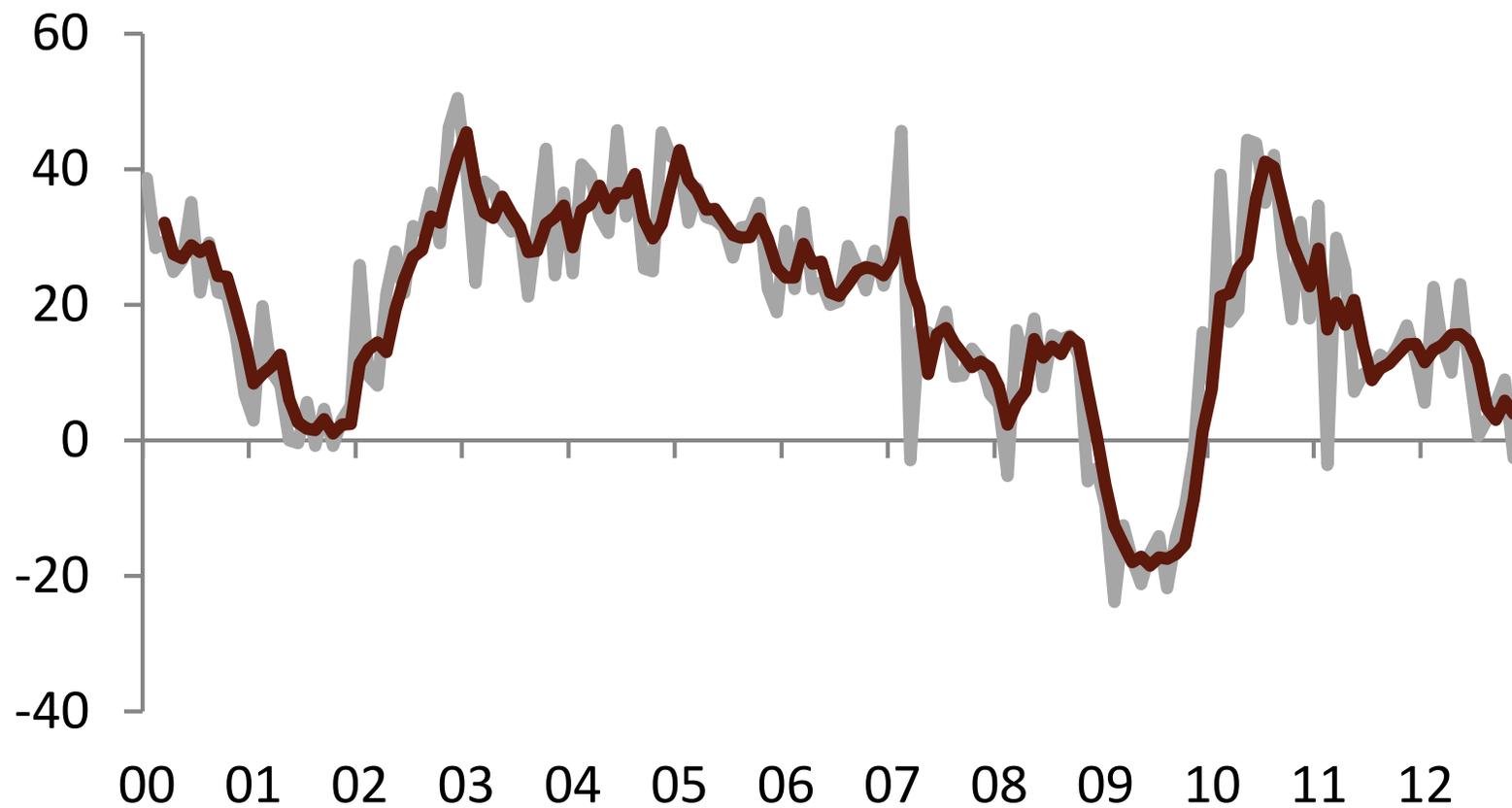
C&I lending slowing down

Commercial and industrial loans (13-week % change, annualized)



Source: Federal Reserve, Renaissance Macro Research

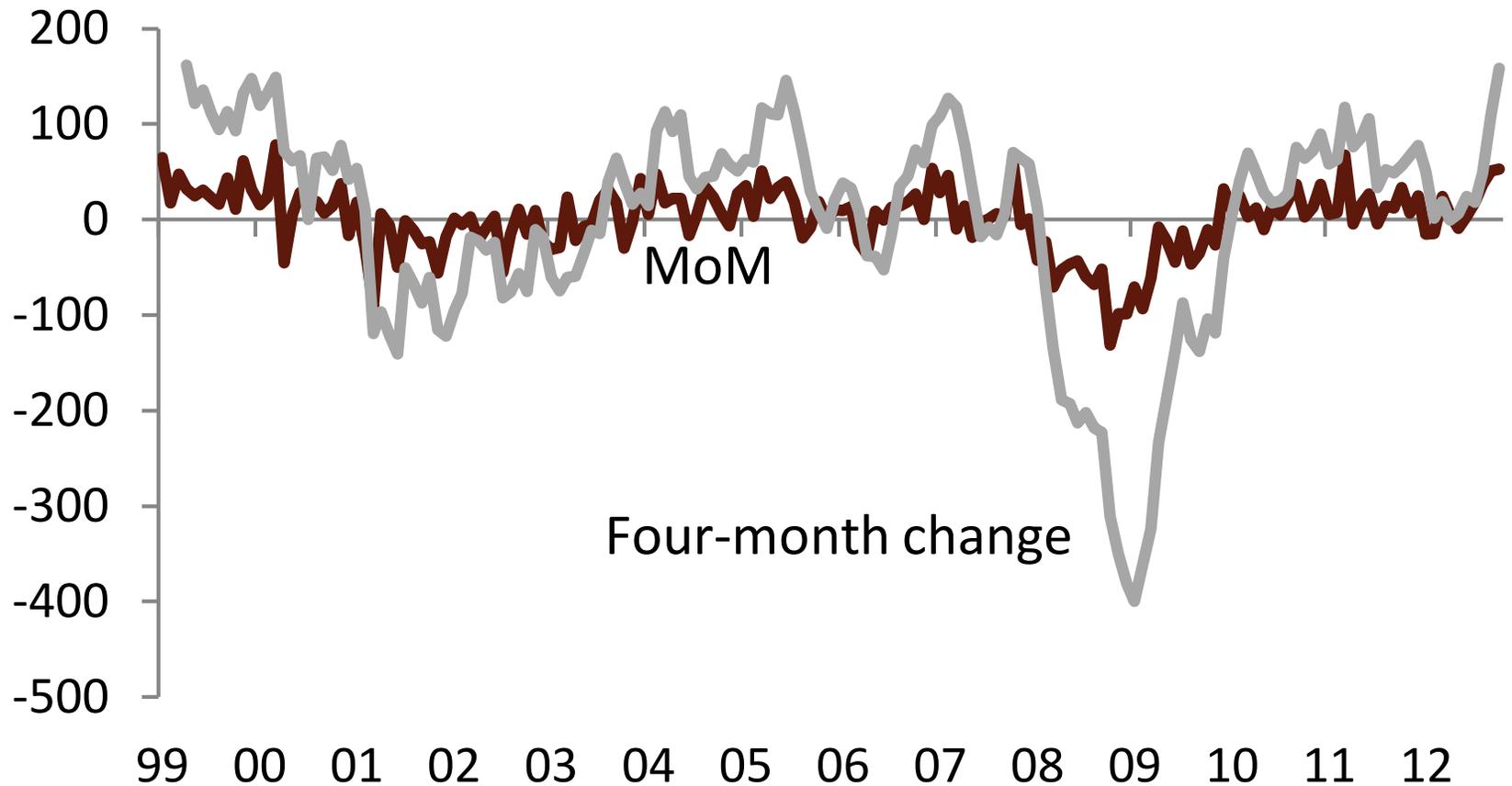
Weakening US demand backdrop China exports to US (YoY % Change)



Source: Bloomberg, Renaissance Macro Research

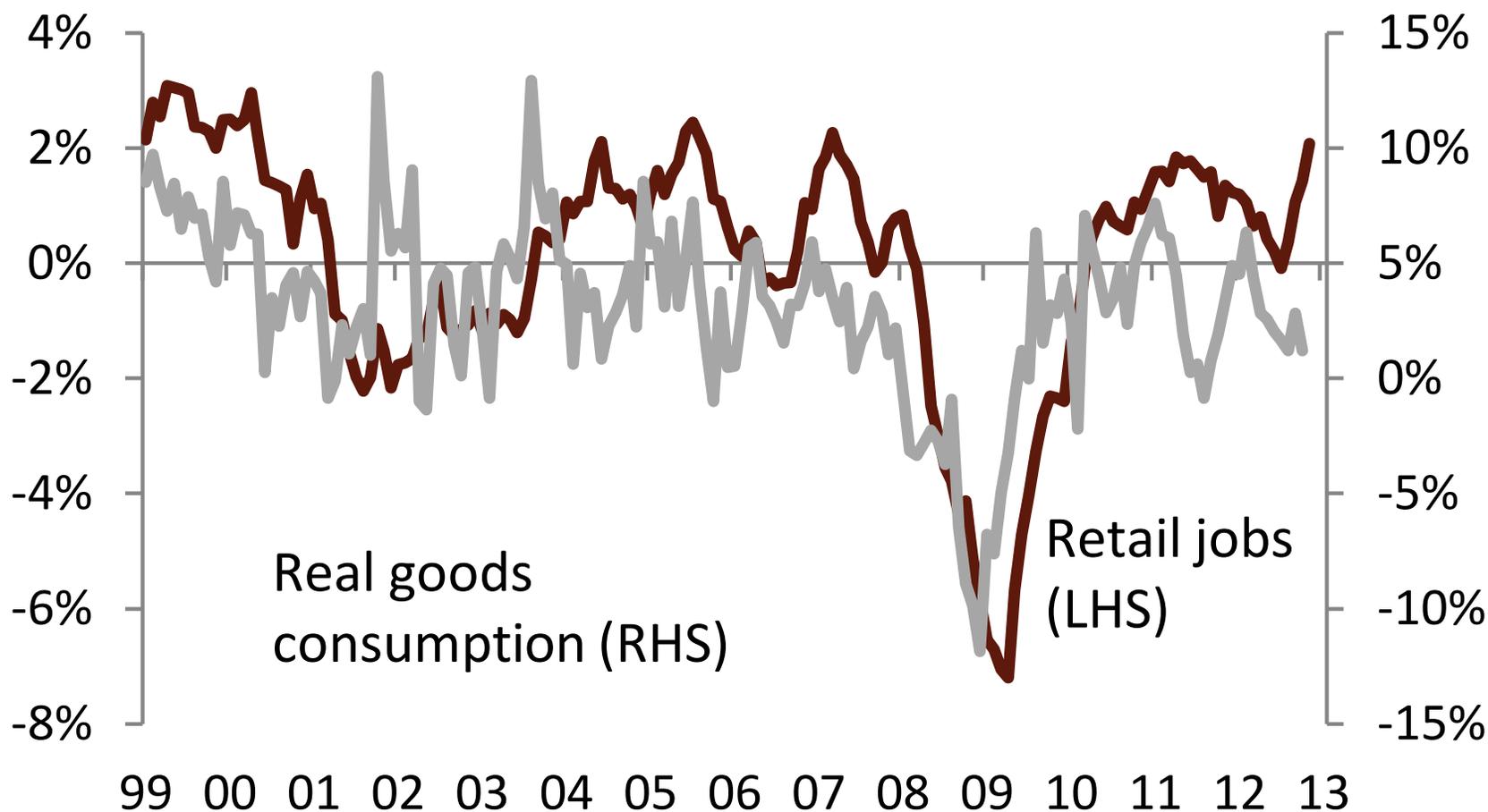
Retail employment looks too strong

Retail trade employment



Source: BLS, Renaissance Macro Research

Retail jobs versus actual consumption (six-month % change, annualized)



Source: Haver Analytics, Renaissance Macro Research

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