



Retail sales are rising but not busting out

By Paul Davidson *July 16, 2014*

Don't expect American consumers to power substantially stronger economic growth until they start getting bigger raises, economists say.

Overall retail sales increased 0.2% in June, far less than economists expected. But sales excluding autos, gasoline, building materials and food services jumped a better-than-expected 0.6%. Economists say that closely watched measure feeds more directly into economic growth.

Sales of general merchandise, clothing, sporting goods and non-store retail items all rose solidly. Also encouraging: retail sales for April and May were revised upward.

Still, sales so far this year are up 3.8% at an annual pace vs. 4.2% in all of 2013.

"It's just modest growth," Greg Daco, chief U.S. economist of Oxford Economics says of Tuesday's data. "It's not the breakout report."

Many economists expected consumers to spend more freely this year, driving a stronger recovery. Consumer spending makes up nearly 70% of the economy. Higher household wealth — a result of a roaring stock market and rising home prices — and sharply reduced consumer debt were expected to fuel the increased outlays.

But despite stronger job growth and a rapidly falling unemployment rate, average annual wage increases remain stuck at about 2%. "You're not seeing wage growth that can support consumer spending," Daco says.

Increased household wealth is boosting spending for higher-income households that are heavily invested in stocks, says Dean Maki, chief U.S. economist of Barclays Capital. But average Americans are still spending cautiously.

The dichotomy is illustrated in the contrasting fortunes of retailers. Family Dollar Stores and Wal-Mart are among those that cater to low- and middle-income households and have struggled with falling sales. Chains such as Nordstrom's that serve higher-end consumers are seeing rising sales.

Meanwhile, low- to moderate-income shoppers have sharply increased credit card purchases recently for the first time in the 5-year-old recovery. Yet **Bernard Baumohl, chief global economist at the Economic Outlook Group**, says the pickup in borrowing is not sustainable without stronger wage increases.

Consumers "are very cautious about taking on debt" following the mid-2000s credit bubble, he says.

Noting that consumers are starting to face higher inflation that's reducing their purchasing power, **Baumohl** says, "It does raise serious concerns about the outlook for consumer spending in the second half of this year."

Daco is more sanguine. He says there are already signs of pay increases picking up in some sectors. He expects broader gains this year to drive higher consumer spending as the 6.1% unemployment rate falls further, increasing competition for available workers.

Maki doesn't expect significantly stronger wage growth until next year. Still, he expects better retail sales growth in the second half of the year as the stock market rally fuels further spending increases among higher-income households.

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