Basis Points – August 23, 2018

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Above the Fold

Retail: The death of brick and mortar stores may have been greatly exaggerated. There have been a number of retail reports in the past week that show strong consumer spending, especially when walking in to actual stores. Target reported earnings on Tuesday, and reported same store sales growth of 6.5 percent, which is their strongest number in 13 years. The Target CEO noted on the earnings conference call that “this is the best consumer environment I have seen in my career.” Walmart also showed strong store traffic numbers last week, with sales in stores up 5.0 percent, the strongest gain in 10 years. Walmart’s online business is also showing strong growth, with revenue up 40 percent over last year. Home Depot, Lowe’s and Kohl’s also reported strong numbers recently. The restaurant sector has shown strong traffic and sales this year as well.

Why are we seeing such strong consumer spending this late in a business cycle? First, the tax reform bill has cut the payroll tax rate for workers, so the average consumer has more cash to spend, and as good Americans do, they are clearly spending it. Second, consumer confidence is at a 40-year high, as the unemployment rate is very low at 3.9 percent. In this environment, everyone who wants a job can get one, and wages for the average worker are finally rising. Lastly, the retail store chain tree has been pruned. We have seen many unprofitable retail chains declare bankruptcy in the past year, including Toys R Us, Brookstone, Claire's and Nine West. The weak sisters in retail have gone out of business, while store chains continue to thrive which offer a differentiated product offering, such as TJ Maxx, or a compelling store experience like Target, or great discounts such as Walmart.

Three Things

- The S&P 500 has risen 8 percent so far in 2018, which seems like a fairly normal return to expect from the equity market, as equity returns have averaged around 9 percent a year for the last 100 years. However, looking at yearly returns by themselves, the S&P 500 has only shown performance between 0 percent and 10 percent in 15 percent of the last 100 years. The index rose between 10 and 20 percent in 22 percent of calendar years, and has shown gains of more than 20 percent a year in 37 percent of years. So while it may seem logical to predict a market return of 0 to 10 percent in any given year, it is not very likely given historical performance results.
- For most of DFW, gone are the clumps of yellow and green rental bikes that were strewn on streets, parks and running trails. This business model has failed due to lack of demand. However, popping up in Dallas this month are rental electric scooters that seem to have attracted more demand. If you have ever wondered who charges the electric scooters, there is a good answer: A workforce of contract workers who sign up with companies like Bird and Lime to recharge their scooters at night. High school students and young professionals are making extra money by fanning out across the city and loading scooters into their car, taking them home and charging them all night, then returning them to the street early in the morning. Some workers charge 15 scooters a night, and make up to $200 a day.
- Although some parts of the retail store landscape may be struggling to attract spenders into their stores, the retail apocalypse has apparently not touched the discount sector. TJX Corp., which owns the TJ Maxx and Marshall's chains reported July same store sales on Tuesday of up 6 percent, which was far higher than the 2 percent gain expected by analysts. The CEO said that the chains are attracting new customers to all of their divisions, and a significant share of the new buyers are younger customers. Consumers like the treasure-hunt experience and liquidation prices they find at the stores. TJX only has a small online presence, as the assortment of goods rapidly change, so customers must visit one of their now 4,194 stores to purchase items.

Did You Know

Dallas-Fort Worth is missing some homes, as the market has underbuilt our housing stock by more than a million since the bottom of the last recession. A lack of construction during the Great Recession and slow recovery of the North Texas homebuilding market has left the area with a deficit of housing. D-FW should have built almost 1.2 million more houses than were actually produced since 2008, according to a new report by Zillow. In the U.S. as a whole, 6 million homes are missing from the U.S. market. In the past, population growth has been met with new construction, but construction has not kept up with demand. Between 1985 and 2000, the D-FW area was adding about five new housing units for every 1,000 residents. But since 2008, the local housing supply has only been growing by about 3.4 units per resident. The slowdown in home production has come at a time when D-FW is leading the country in population growth with thousands of people relocating to the area every month. Annual single-family home construction in the area is about a third below where it was before the recession.