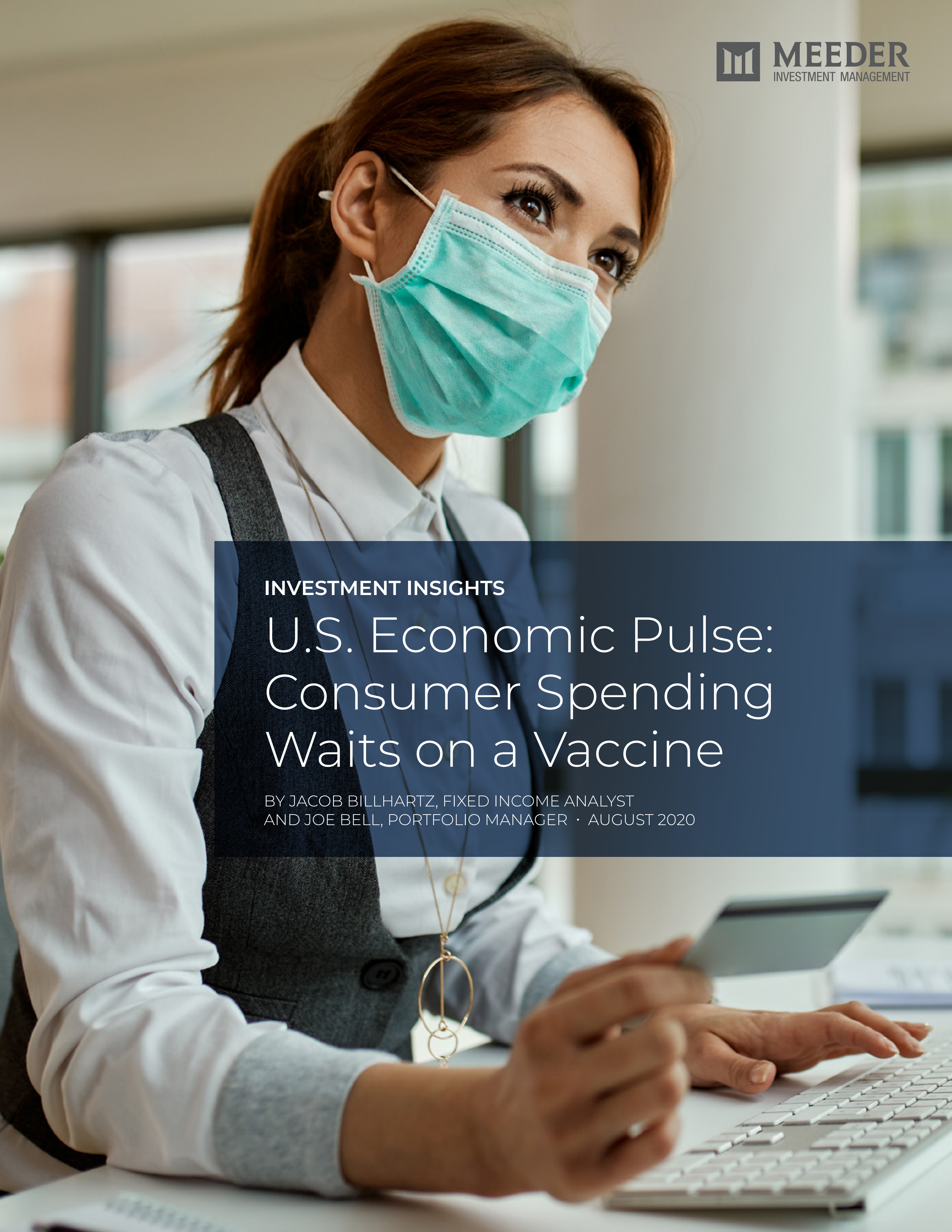

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INVESTMENT INSIGHTS

U.S. Economic Pulse: Consumer Spending Waits on a Vaccine

BY JACOB BILLHARTZ, FIXED INCOME ANALYST
AND JOE BELL, PORTFOLIO MANAGER · AUGUST 2020

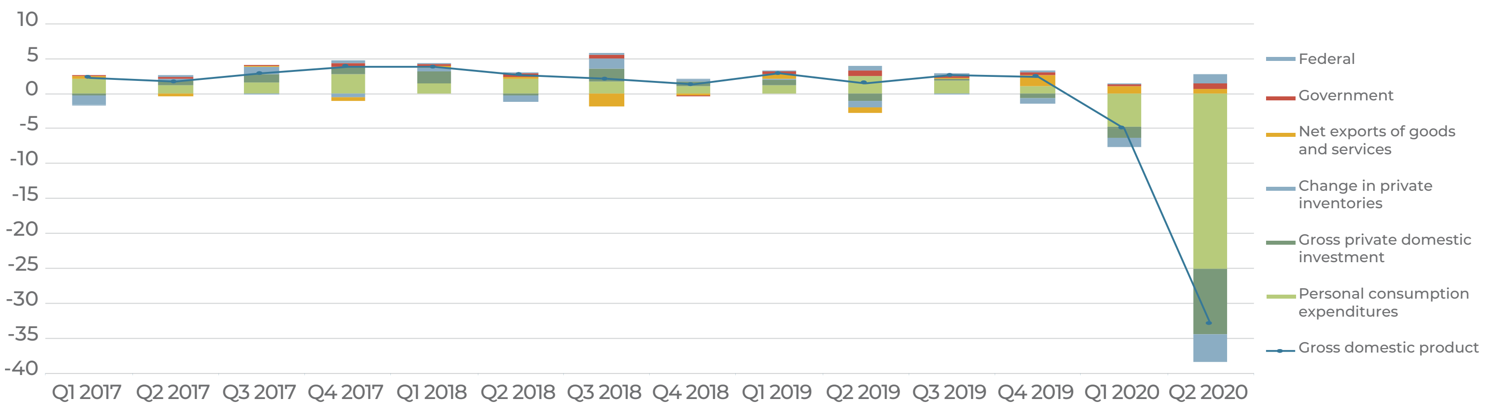
KEY TAKEAWAYS:

- Consumer spending is by far the largest part of the U.S. economy and its decline has been the biggest reason for the economy shrinking in Q2 2020.
- Enhanced unemployment benefits, which expired at the end of July, led to an increase in consumer compensation to above pre-COVID levels.
- While spending by lower-income workers is now close to its pre-COVID level, spending by higher-income Americans still significantly lags. The sharp spending decline by this group, who are largely still employed, has had the biggest impact on the reduction in total consumer spending.
- We believe consumer spending will improve once there is a vaccine, drug, or improved confidence around public health.

1. THE CONSUMER IS KING

As Exhibit 1 shows, consumer spending is by far the largest contributor to U.S. Gross Domestic Product (GDP), and therefore, has the largest impact on whether the economy is growing or not. From 2017 to 2019, personal consumption expenditures, as a portion of GDP, ranged from 62% to 78%. While private domestic investment slowed in 2019, the consumer was resilient. But as COVID-19 changed consumer spending behavior, the decline in spending led GDP lower. While GDP declined at a seasonally adjusted annualized rate of 32.9% in Q2 2020, personal consumption expenditures declined by 34.6%.

EXHIBIT 1: CONSUMER SPENDING IS THE LARGEST CONTRIBUTOR TO U.S. GDP

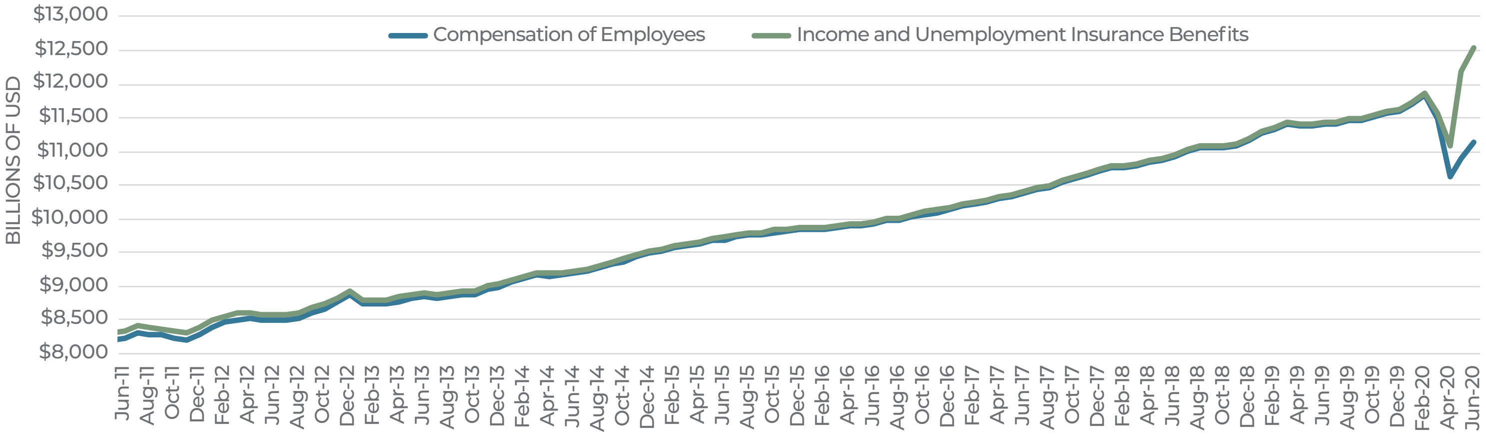


Source: BEA

2. CONSUMER COMPENSATION SURPASSES PRE-COVID LEVELS

The CARES Act included several provisions designed to bridge the economic gap created by COVID-19 and the resulting shutdown of the U.S. economy. One of the most impactful provisions was an additional $600 a week for unemployment insurance recipients. Data from the Bureau of Economic Analysis shows that the combination of traditional compensation and unemployment benefits are well above where they were pre-COVID, even though GDP still fell by a record rate in the second quarter and unemployment remains above 10%. While these benefits expired at the end of July, it is widely expected that Congress will pass a new stimulus bill soon.

EXHIBIT 2: CONSUMER COMPENSATION HAS SURPASSED PRE-COVID LEVELS



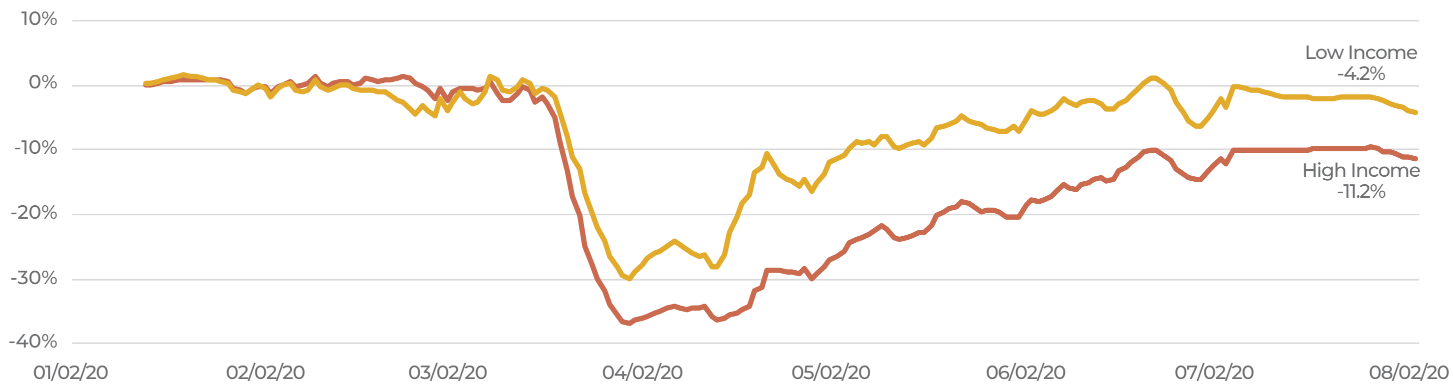
Source: BEA

3. HIGH-INCOME CONSUMERS LEAD THE DECLINE IN SPENDING

The highest-earning quartile of Americans has been responsible for about half of the decline in consumption during this recession, according to economists at the Harvard-based research group Opportunity Insights. This reduction in spending has negatively affected employment in the lower-wage service industries but has also had an outsized effect on the U.S. economic slowdown.

Data shows that, at the lowest point, the highest-earning quartile reduced household spending by 36% and is still nearly 12% below their January 2020 spending level. In contrast, spending by the lowest-earning quartile has recovered faster and is just 4% below its January 2020 level. Even though a cut in unemployment benefits may reduce spending from this group, those who are still employed have had the largest impact on the GDP decline. Note that these benefits have had an outsized effect on the lives of those receiving them, so any reduction in benefits will severely affect unemployed individuals.

EXHIBIT 3: HIGH INCOME CONSUMERS HAVE LED THE DECLINE IN SPENDING IN 2020 SO FAR



Source: Opportunity Insights, Harvard, Data is based on a 7-day moving average of consumer spending, as represented by a composite of spending data tracked at www.tracktherecovery.org.

4. SPENDING WILL LIKELY FOLLOW AN IMPROVEMENT IN PUBLIC HEALTH

We expect consumer spending to improve once a vaccine is publicly available and confidence in public health improves. The COVID-19 pandemic has changed consumer spending behavior, and these changes are unlikely to reverse until consumers can return to their "normal" lives. For example, most of the reduction in spending has been on goods and services that rely on personal interaction, including hotels, transportation, and foodservice. According to JP Morgan's proprietary data, debit and credit card transactions on Chase-branded cards were down less than 1% year over year on August 7. In stark contrast, in-person card transactions were down nearly 20% over the same period.

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6125 Memorial Drive, Dublin, OH 43017 | 1.866.633.3371 | meederinvestment.com

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