Economics Center

Holiday Forecast of Ohio Retail Spending

Prepared for

Focus on Ohio's Future

by the

Economics Center

November 2013

University of Cincinnati

REPORT HIGHLIGHTS

- Compared to last year, the Economics Center projects a **3.5 percent increase** in Ohio retail spending for November and December of this year.
- The Economics Center forecast for the State of Ohio is slightly lower than the National Retail Federation's national forecast of 3.9 percent. Recent declines in consumer confidence have contributed to this lower forecast.
- Internet shopping continues to be a strong component of retail sales. Among consumers, 47 percent expect to purchase items online this holiday season while 44 percent expect to shop at discount/value department stores.
- The Columbus MSA not only represents the largest share of retail spending in Ohio, the Economics Center also forecasts the Columbus MSA to see the biggest increase in holiday spending of 4.4 percent.

INTRODUCTION TO HOLIDAY SPENDING

During the majority of the year, a household's purchasing decisions center primarily around fulfilling basic needs (e.g. housing, clothing, food, general transportation, etc.). The extent to which households purchase more discretionary goods, including gifts, is smaller compared to their spending on necessities. In the holiday season, however, the level of spending on these discretionary goods increases and this spending plays a significant role in the overall health of the U.S. economy. Not only can a healthy holiday season create a boost in short-term seasonal employment, but it also serves as a strong indicator of the health of the economy going forward. Among other things, strong spending during the holiday season will lead to higher earnings. When earnings are strong, optimism regarding future investment generally rises. With additional investments in the economy, higher employment levels and higher wages are likely to soon follow and further strengthen the economy.

HOLIDAY SPENDING FORECAST

Data

Retail sales data was compiled from the Ohio Department of Taxation's website and also by direct communication between the Economics Center and the Ohio Department of Taxation.[1] The Ohio Department of Taxation administers permissive sales and use taxes for 88 counties and eight transit authorities. The revenue from the monthly collections is distributed to the counties and regional transit authorities. Because monthly tax revenue data is only provided in the aggregate at the county level, the Economics Center asked the Department to break out the monthly sales data by individual sector. The Economics Center then applied this retail sector ratio to the county-level data.

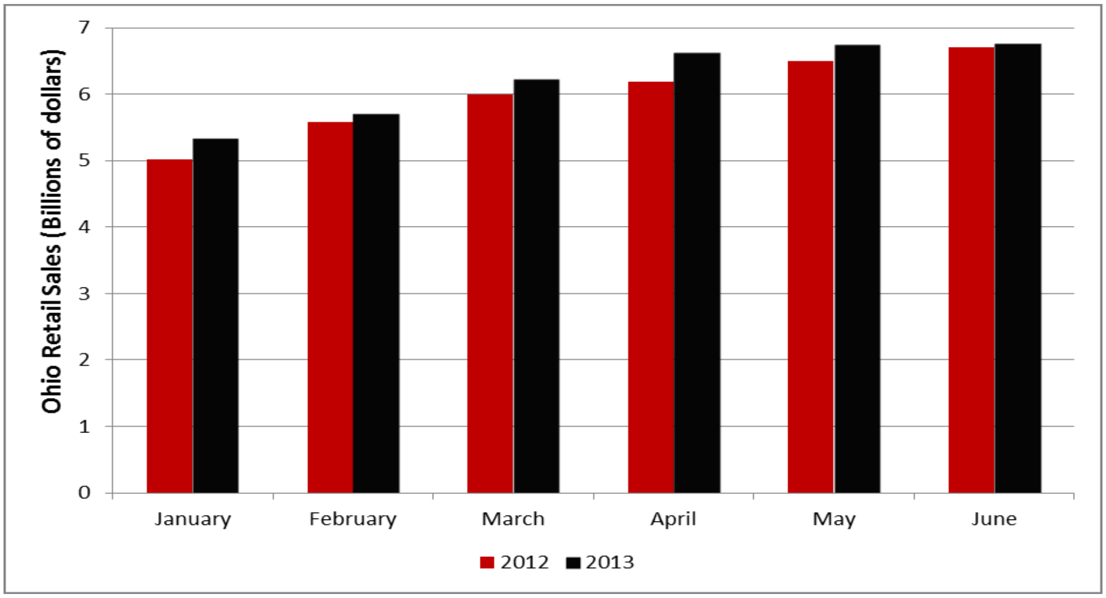
The Economics Center defined retail spending as including all retail sales except those by motor vehicle and parts dealers, gasoline stations, and non-store retailers (catalog and Internet). This definition, which is consistent with the approach used by the National Retail Federation, also excludes spending on accommodations and food services, as well as entertainment and recreation. On average, this modified retail spending definition represents approximately half of all sales and use taxes collected by the state of Ohio.

[1] http://tax.ohio.gov/divisions/tax_analysis/tax_data_series/sales_and_use/publications_tds_sales.stm

Current Spending

During the preparation of this report, sales tax revenue data through June 2013 was made available by the Ohio Department of Taxation. From January to June 2013, retail sales were 4.0% higher relative to the same period in 2012.

Figure 1: Monthly Ohio Retail Sales Comparison



Forecast

The Economics Center projects a 3.5% increase in retail spending in November and December 2013 in Ohio, compared to 2012.

The Economics Center projects that the total retail spending for November and December 2013 will be $14.90 billion, an increase of $503.50 million from 2012. At the beginning of October, the National Retail Federation is predicting a national increase of 3.9 percent in holiday sales.[2] Since that forecast however, consumer confidence has declined and private payroll gains have slowed. Based on a recent survey of consumers, the NRF also found that consumers expect to spend less this year on gift giving compared to last year.

More than half of the State's retail spending is expected to take place in Ohio's three largest Metropolitan Statistical Areas (MSAs) – the Columbus MSA, the Cleveland MSA and the Ohio portion of the Cincinnati MSA. The Economics Center forecasts that spending in Columbus will be the highest

[2] http://www.nrf.com/modules.php?name=News&op=viewlive&sp_id=1682

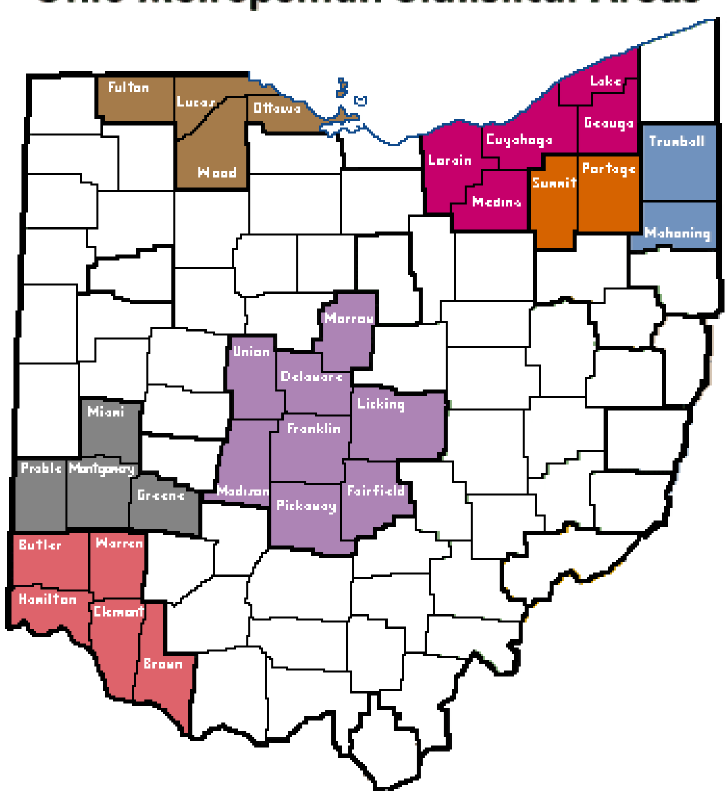
among all MSAs. Spending there is projected to be 4.36% higher than in 2012 - the largest projected increase for any MSA. Cleveland is projected to have the second-highest amount of retail spending, and the second highest growth when compared to 2012.

Table 1: 2013 Holiday Sales by Ohio Region

Major Metros	Nov-Dec Sales ($millions)	Share	Percent Increase (2013 vs. 2012)
Akron MSA	939	6%	0.4%
Cincinnati MSA (Ohio region)	2421	16%	3.4%
Cleveland MSA	2839	19%	3.8%
Columbus MSA	2972	19%	4.4%
Dayton MSA	1069	7%	0.1%
Toledo MSA	873	6%	3.8%
Youngstown MSA	535	4%	1.4%

The map below shows the counties included in these regional sales forecasts.

Ohio Metropolitan Statistical Areas



Online Retail Spending

According to Deloitte's 2013 Annual Holiday Survey, the Internet will surpass any other type of shopping destination for the first time in history. Overall, 47 percent of consumers expect to purchase items online this holiday season, while 44 percent of consumers expect to shop at discount/value department stores. In addition, 36 percent of consumers will make purchases online for pick-up in the store. The proportion of consumers who expect to make the majority of their holiday purchases online is expected to show a significant increase, from 23 percent in 2012 to 38 percent this year.

Based on previous research by the Economics Center, Ohio consumers will spend nearly $1.0 billion during the holiday period at Internet retailers' websites where sales tax is not collected. As a result, the State of Ohio and its local governments will lose almost $70 million in sales tax revenue because of online purchases on which sales tax is not paid. In addition, the Economics Center estimates that about 19 percent of this Internet spending will come at the expense of Ohio retailers, who will lose $188 million in holiday sales this year as a result of consumers choosing Internet retailers over traditional brick and mortar retailers. The Economics Center attributes some of the increase in the number of Ohio consumers buying online to the recent change in sales tax, from 5.5 percent to 5.75 percent.

FACTORS INFLUENCING HOLIDAY SPENDING

Employment

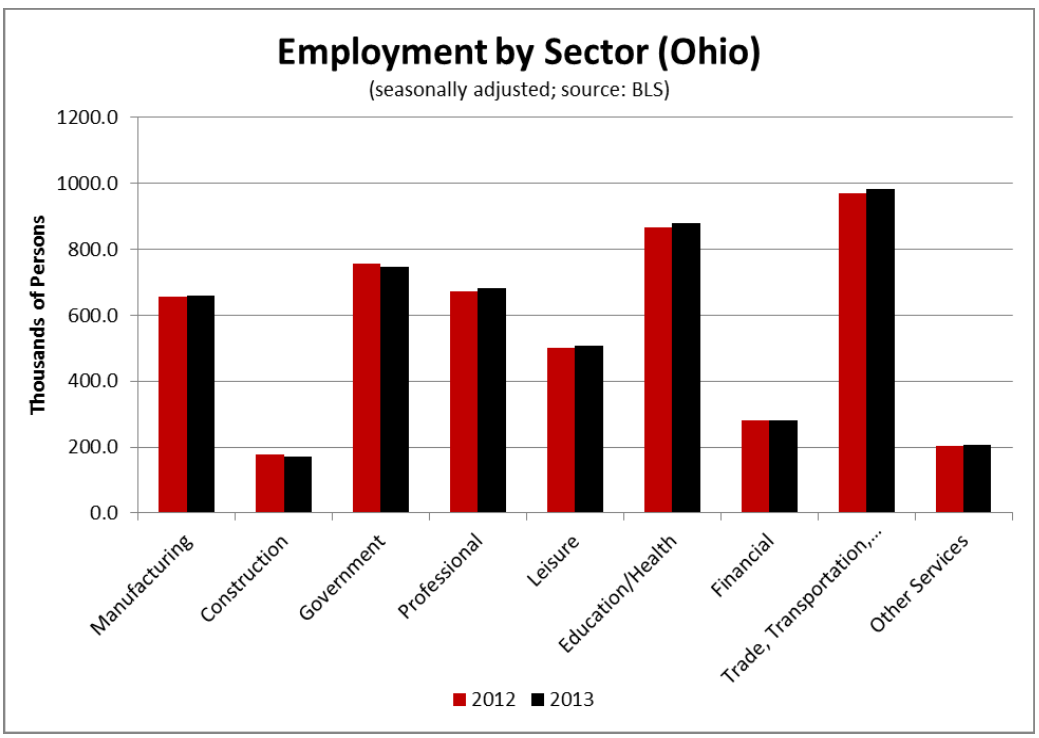
The employment picture in Ohio has been relatively flat over the past year. While the unemployment rate has only increased 0.1 percentage point over the same time last year, it is 0.6 percentage points higher than the 12-month low (6.7% Dec. 2012). *Nonfarm payrolls* have also declined slightly.

Table 2: August Measures of Ohio Employment

	Last Year	Current Year	Change
Civilian Labor Force (thousands)	5,733.6	5,732.1	-1.5
Unemployment	7.2%	7.3%	0.1%
Nonfarm Payroll (thousands)	5,323.0	5,313.0	-10.0

However, with the exception of construction and government sectors, all other sectors in Ohio have experienced employment growth.

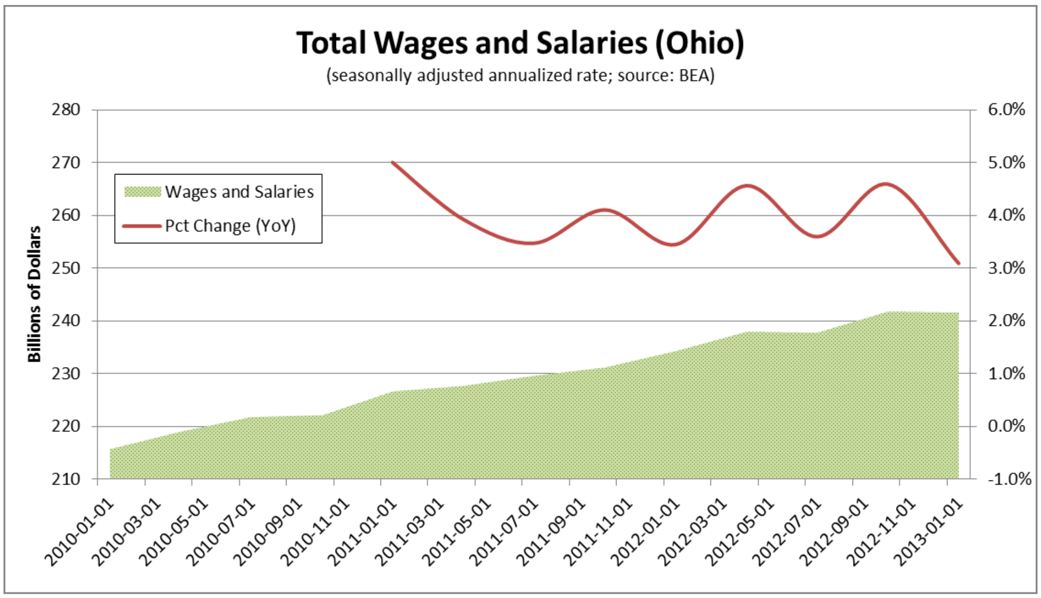
Figure 2: August Employment by Sector



Wages and Salaries

As of January 2013, *wages and salaries* in Ohio increased by 3.1% relative to the previous year and *total personal income* increased by 2.9%. During the same period, the Bureau of Labor Statistics (BLS) reported that inflation in the Midwest region increased by 1.3%. However, this improvement in income has largely been offset by an increase in payroll taxes. Effective January 1, 2013, the 2% federal payroll tax cut expired effectively reducing workers paycheck income by 2% (for all those making less than $110,000). When coupled with the 1.3% inflation rate, the gain in Ohio workers' wages is minimal.

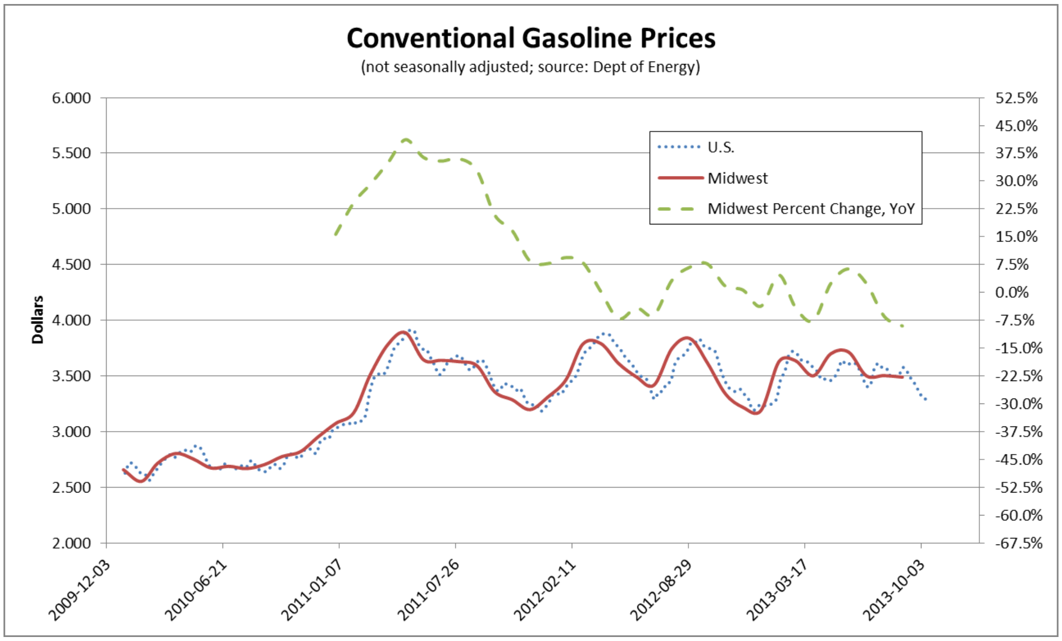
Figure 3: Wages and Salaries



Energy Prices

Disposable income should get a slight boost from a reduction in gasoline prices. According to data from the Department of Energy, conventional gasoline prices in the Midwest are 9.0% lower, year-over-year, as of September 1st. While gasoline prices are lower, utility prices for the home are mixed. Based on data from the Public Utilities Commission of Ohio, electric bills are 5.0% higher, year-over-year (October data), while natural gas bills are 4.4% lower.

Figure 4: Gasoline Prices



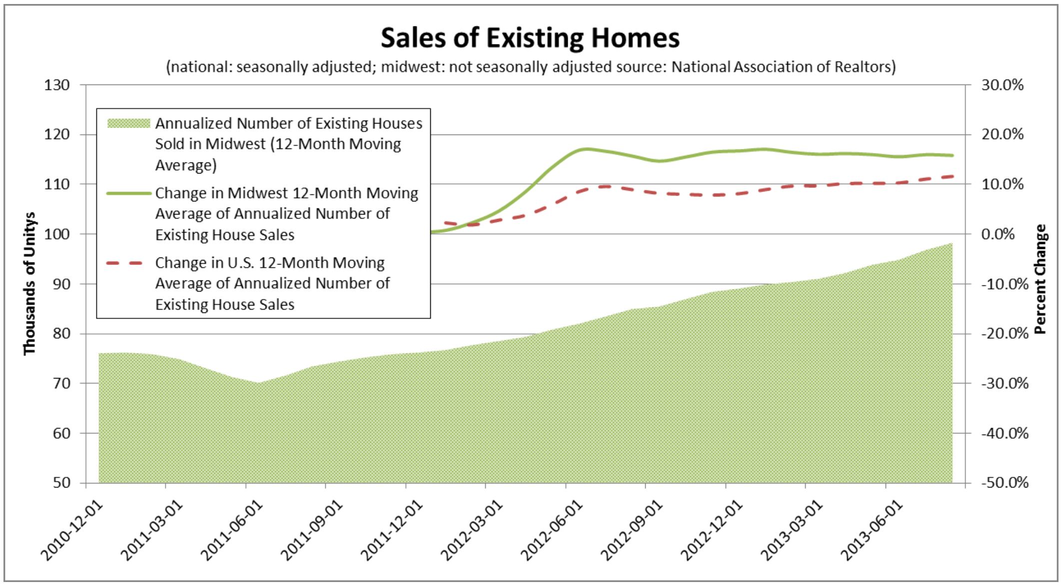
Sales Taxes

While the reduction in gasoline prices might help to offset the expiration of the payroll tax cut, holiday spending in Ohio might be slightly hampered by an increase in the base sales tax rate. In September 2013, the State of Ohio increased the sales tax rate from a base rate of 5.5% to 5.75%. While public data does not yet exist to measure the impact of this change, when comparing retail sales tax receipts for the first half of calendar 2013 to the same period in 2012, sales tax receipts in Ohio increase by 4.0% - a strong sign that Ohio consumers are increasing their spending.

Increases in Wealth

The first half increase in spending might be driven by an increase in wealth and/or borrowing. In particular, it would appear that the wealth of Ohioans has increased based on several indicators. Over the past year, the stock market has risen by 37.5% (as measured by the Russell 2000 Index - October 2013), Ohio home sales have increased by more than 10% (based on a 12-month moving average), and the prices of those home sales have increased somewhere between 3.9% and 9.0% (depending on the measurement used).

Figure 5: Existing Home Sales



The credit picture for households has steadily improved over the past few years. Compared to January 2010, *credit card charge-off rates* have fallen to 3.53% from 10.55% (as of April 2013), *credit card delinquency rates* have fallen from 5.83% to 2.52% (as of April 2013), and *household financial obligations as a percent of disposable income* have fallen from 17.54% to 15.69% (as of January 2013). While these improvements in the credit profile of households paint a picture of improving financial health for households, they do not inherently indicate that households are willing to increase borrowing for holiday spending.

Nonetheless, *household financial obligations as a percent of disposable income* may offer a small clue into household's willingness to borrow during the holiday season. From January 2009 through October 2012, this ratio was regularly declining. However, between October 2012 and January 2013, this ratio increased from 15.40% to 15.69%. While this is only one indicator, it may signal that households are again willing to assume some debt to finance holiday spending. While there is no guarantee consumers will be willing to undertake new debt, the fact that they have improved their credit profile will at least allow that opportunity.

Consumer Confidence

There is a strong relationship between the confidence of consumers in the economy and the decision by consumers to spend. Despite the University of Michigan's index of consumer sentiment falling last December to 72.9 (from 82.7 in November), consumer sentiment quickly recovered in the first three months of this year to 78.6. However, the index recently fell to 73.2 in October from 77.5 in September.

The index has fallen for three straight months after reaching a six-year high of 85.1 in July. This continual decline in consumer confidence will likely depress holiday sales.

US Retail Sales

Perhaps the best indicator of holiday spending is historical spending within the retail sector. Based on a 12-month moving average of the U.S. retail sector, retail sales continue to grow at a pace of approximately 4.6%, year-over-year. Since the Great Recession, overall retail spending has continued on an upward trend. In its forecasting model, the Economics Center included US retail sales to reflect the overall economic strength of consumer retail spending. The improving retail environment should drive increased holiday spending in the state of Ohio.

ECONOMIC UNCERTAINTY AND HOLIDAY SPENDING

The impact on holiday spending due to the U.S. Government shutdown of October 2013 is difficult to predict. While it should have a minimal impact on government workers since they will be paid for the time in which the government was shutdown, those businesses that regularly provide goods and services to government workers on a daily basis have been harmed. That is, the loss of income to these businesses and the loss of wages to their employees will not be replaced. The extent to which this loss of income will translate into potentially dampened holiday sales is unknown.

What might be a more significant impact on the holiday season is the unknown state of the U.S. budget going into January. Since the bill that the U.S. Congress passed to reopen the government only funds the government through mid-January, there exists a high degree of uncertainty as to whether another government shutdown is on the horizon. Given this uncertainty, there is a chance that government workers and businesses that derive significant portions of their income from the government (e.g. restaurants near government office buildings) might decide to reduce their holiday consumption and save more given the possibility their income could potentially disappear early into the new year.

Approach to the Development of the Forecast

The Economics Center used a Vector Autoregression (VAR) model to generate its forecast for Ohio holiday retail spending. A VAR model is used to analyze the interdependence among multiple time series variables. For example, retail sales spending is a function of consumer confidence, which in turn depends on the amount of retail sales spending. Details of the specification can be provided upon request.

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About the Economics Center

The Research and Consulting division of the Economics Center provides the knowledge building blocks that help clients make better policy and economic development decisions. Our dynamic approach and critical data analysis empower leaders to respond to changing economic conditions, strengthen local economies and improve the quality of life for their communities.