Consumer Spending Slows as Delta Surges and Stimulus Fades

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Analysts had anticipated consumer spending would slow as stimulus checks were gradually spent. The expectation was that Americans would quickly return to work, and regular paychecks would pick up the slack. But, workers have been slow to return and the July Delta wave injected yet another dose of uncertainty. As a result, retail sales disappointed with a -1.1% drop in July, well below the -0.3% median forecast. Eight of 13 spending categories declined last month, led by a -3.9% drop in vehicle sales and a -2.6% decrease in clothing sales. The vehicle market has been hamstrung by depleted inventory and record high prices, while the dip in clothing sales probably reflects continued stay-at-home workers with little need for new business attire.

Significant increases were found last month in gas station sales (+2.4%), reflecting high pump prices and increased summer travel, as well as restaurant and bar sales (+1.7%). Eating and drinking establishments are the only service category captured in the retail sales report. Much of the summer reopening, including air travel and lodging fall outside the scope of this report, as do housing and healthcare, two of the larger monthly household expenses.

The retail sale "control group," which excludes sales of autos, building materials, gasoline and food services fell -1.0%. *The control group is used to calculate GDP, so the July drop indicates a slow start to the third quarter.* With the Delta wave still gaining momentum, it's unlikely that spending will pick up in August.

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Headline retail sales are still up +15.9% year-over-year, but the base effect is fading after posting eye-popping annual gains of +53.6% in April, +27.4% in May and +19.1% in June.

Bond prices are generally flat this morning, while all three major U.S. stock indexes are down in early trading. In theory, the Fed would tighten monetary policy to slow economic growth and stem inflation. *This morning's report suggests that GDP is moderating without the Fed's help.* As a result, the first rate hike has probably edged further out in 2023. It's not unusual for stocks to rally when weaker economic data suggests accommodative Fed policy will continue. This morning's equity sell-off, *coming a day after the S&P 500 and Dow set new highs*, reflects rising uncertainty.

There's still plenty of pent-up demand for big-ticket housing and autos, household balance sheets are in good shape and the amount of spending capacity is historically high. This means the economic foundation is solid, but the next few months could be bumpy.

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In other news this morning, homebuilder sentiment dropped for the third straight month and is currently at the lowest level in over a year. The National Association of Home Builders (NAHB) Market Index fell from 80 to 75 in August. Demand for homes is still strong, but inventories are tight, and shortages of materials and labor are still creating bottlenecks. At 75, the current level is still well above the 20-year average of 50, but has dropped from a frothy 90 last November.

Market Indications as of 10:32 A.M. Central Time

DOW	Down 283 to 35,343 (HIGH: 35,625)
NASDAQ	Down 152 to 14,642 (HIGH: 14,895)
S&P 500	Down 30 to 4,450 (HIGH: 4,480)
1-Yr T-bill	current yield 0.07%; opening yield 0.06%
2-Yr T-note	current yield 0.21%; opening yield 0.21%
3-Yr T-note	current yield 0.42%; opening yield 0.42%
5-Yr T-note	current yield 0.76%; opening yield 0.76%
10-Yr T-note	current yield 1.27%; opening yield 1.26%
30-Yr T-bond	current yield 1.93%; opening yield 1.93%