



## U.S. Consumer Spending Below Expectations in September – What Does This Mean for Canada?

### Description

A reported weak back to school period for U.S. retailers has spurred the question: Will this be the Canadian experience as well?

Let's try to answer this question by taking a look at the experience of the American consumer. Back in 2008, people in the U.S. felt the sting of being caught with unsustainably high debt levels, and they have since focused on deleveraging. Their deleveraging efforts are consistent with what we would expect after going through such a crisis.

Canadians, on the other hand, have not been through such a devastating period, and continue to spend unsustainably. However, we cannot and should not rely on the consumer to fuel an economic recovery in Canada, because there is not much room left for their debt to grow.

Household debt and its potential impact on the economy has been identified as a key concern by the Canadian Central Bank. The U.S. consumer has been deleveraging ever since the crisis, but judging by the continued growth in debt levels in Canada, Canadians seem not to be overly concerned with their debt levels, which are still at record high levels, with a debt-to-income ratio of 163.4% as of the end of the second quarter.

To sum it up, I think that the Canadian consumer will follow the U.S. consumers' lead for the remainder of the year, and for some time, as they get to the business of deleveraging. This means lower spending on "discretionary" or non-essential goods. And it does not bode well for retailers of non-essential goods.

Back to retail spending, in the second quarter of this year, we were already seeing some retailers struggling with lackluster growth. Let's review some company specific names.

### Retailers that are Struggling

Against this backdrop, many retailers are struggling to find sales growth and profitability. And it seems like consumers may be redirecting their spending on what would be more “essential” expenditures.

**Sears Canada** (TSX: SCC) continues to struggle, and announced that it is cutting 245 jobs in order to streamline and cut costs. Same store sales at Sears decreased 2.5% in the second quarter.

**Rona** (TSX: RON) also continues to struggle, with declining same store sales and continued market share losses. As we have seen in the retail sales numbers, shoppers are not spending as much at the home improvement retailers such as Rona.

At **Reitmans** (TSX: RET), same store sales declined 3.5% in the second quarter. Reitmans is a very well-run company that is facing headwinds from the macro environment. The stock currently has an 8% dividend yield.

### Which Retailers are Doing Better than the Rest?

**Costco** ([NASDAQ: COST](#)) same store sales growth for the 5 weeks ended July 7, 2013 increased 6% in the U.S. and 8% in the International division (of which Canada is almost half). It will be interesting to see if they can maintain this momentum.

**Canadian Tire** ([TSX: CTC.A](#)) is also seeing increases in sales. In the second quarter, sales increased 2.1%, while same store sales increased across all banners. Canadian Tire's same store sales increased 2%, FGL Sports increased 7.2%, and Mark's Work Warehouse same store sales increased 6.4%.

While **Dollarama** ([TSX: DOL](#)) is still seeing same store sales increases, results have been below expectations. In the latest quarter, traffic declined 0.9% and same-store sales rose 3.7%, which was below expectations.

### Bottom Line

It will be interesting to see how retailers perform when third quarter results are released. My bet is that they will be struggling to find growth as the Canadian consumer pares down spending due to high debt levels.

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*Fool contributor Karen Thomas does not own shares in any of the companies mentioned. The Motley Fool owns shares of Costco.*

### CATEGORY

1. Investing

### TICKERS GLOBAL

1. TSX:CTC.A (Canadian Tire Corporation, Limited)
2. TSX:DOL (Dollarama Inc.)

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