Holiday Forecast of Ohio Retail Spending

Prepared for

Focus on Ohio's Future

by the

Economics Center

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REPORT HIGHLIGHTS

- The Economics Center projects a **4.5 percent increase** in Ohio retail spending for November and December of this year, relative to last year.

- The Economics Center's forecast for the State of Ohio is slightly higher than the National Retail Federation's national forecast of 4.1 percent. Recent rallies in consumer confidence have contributed to this higher forecast, as has stronger growth in the State of Ohio.

- Internet shopping continues to be a strong component of retail sales. Among consumers, 45 percent expect to purchase items online this holiday season while 44 percent expect to shop at discount/value department stores.

- Retail sales in Ohio's three largest MSAs are all expected to increase substantially this holiday season, relative to last year, and account for more than half of the State's total retail sales.

INTRODUCTION TO HOLIDAY SPENDING

During the majority of the year, a household's purchasing decisions center primarily on 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.

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.

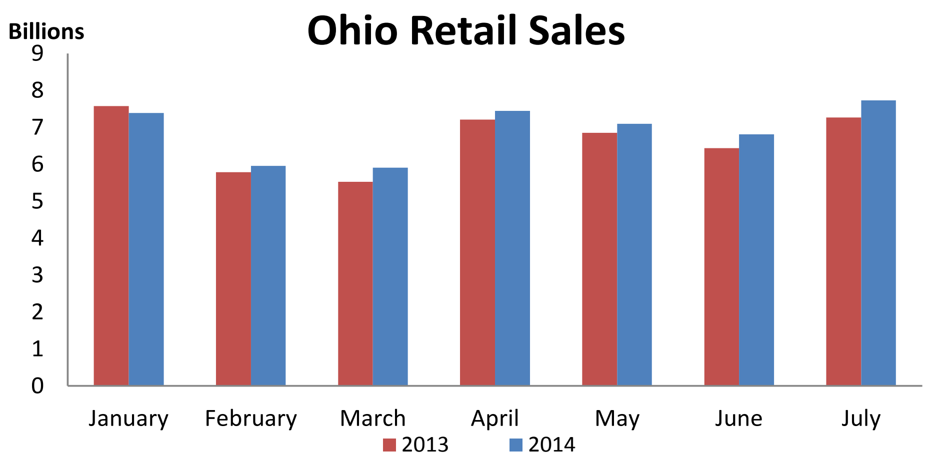
The Economics Center defined retail spending as including all retail sales except those by motor vehicle and parts dealers, gasoline stations, and non-store retailers (catalog and Internet). This definition, which is consistent with the approach used by the National Retail Federation, also excludes spending on accommodations and food services, as well as entertainment and recreation.

Current Spending

During the preparation of this report, sales tax revenue data through July 2014 was made available by the Ohio Department of Taxation. From January to July 2014, retail sales were 3.6 percent higher relative to the same period in 2013.

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

Figure 1: Monthly Ohio Retail Sales Comparison



Forecast

The Economics Center projects a 4.5 percent increase in retail spending in November and December 2014 in Ohio, compared to 2013.

The Economics Center projects that the total retail spending for November and December 2014 will be \$14.5 billion, an increase of \$630 million from 2013. At the beginning of October, the National Retail Federation predicted a national increase of 4.1 percent in holiday sales.[2] Since that forecast, however, consumer confidence has continued to rally, reaching its highest point since 2007. Based on a recent survey of consumers, Deloitte also found that consumers expect to spend more 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 among all MSAs. Spending there is projected to be 6.3 percent higher than in 2013. Cleveland and Cincinnati are also expected to have strong increases in sales, at 5.1 percent and 3.9 percent respectively.

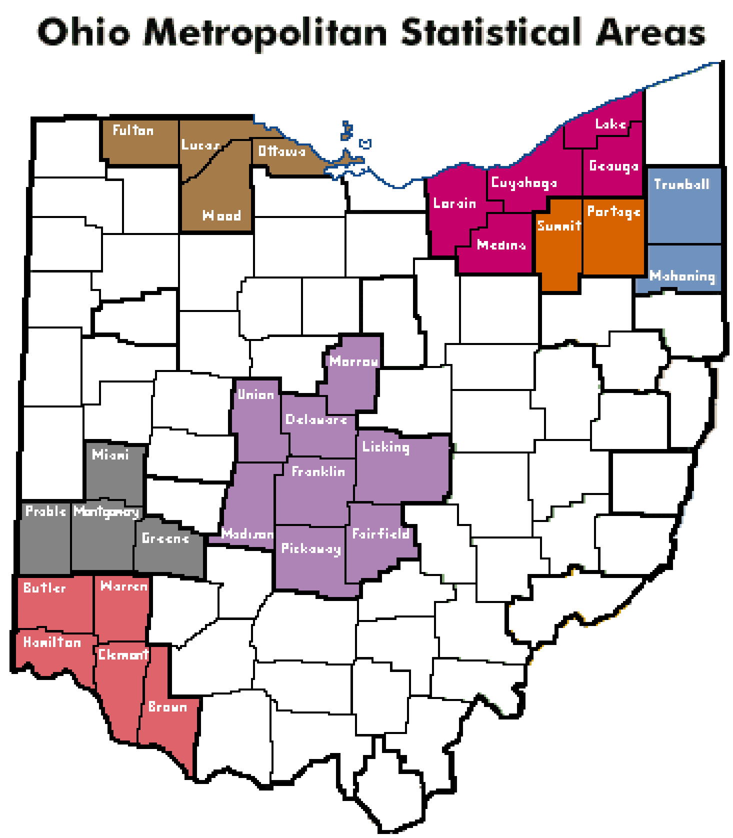
[2] https://nrf.com/media/press-releases/optimism-shines-national-retail-federation-forecasts-holiday-sales-increase-41

Table 1: 2014 Holiday Sales by Ohio Region

Major Metros	Nov-Dec Sales ($millions)	Share	Percent Increase (2014 vs. 2013)
Akron MSA	906	6.3%	1.8%
Cincinnati MSA (Ohio region)	2,260	15.6%	5.1%
Cleveland MSA	2,650	18.3%	3.9%
Columbus MSA	2,850	19.7%	6.3%
Dayton MSA	949	6.5%	-0.8%
Toledo MSA	779	5.4%	6.3%
Youngstown MSA	480	3.3%	1.3%

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

Figure 2: Map of Ohio MSA definitions



Online Retail Spending

Internet retailers continue to account for a larger portion of total retail sales. The legality and feasibility of taxation on these sales has become increasingly important as e-commerce grows. Currently, online shopping captures a greater percentage of consumer purchases than at any point in the past. Legal and practical considerations limit the ability of governments to collect taxes from online retailers, but the revenue losses to state and county governments loom large.

According to Deloitte's 2013 Annual Holiday Survey, the Internet surpassed any other shopping destination for the first time in history just last year. Results from the 2014 survey indicate that the Internet remains the favorite shopping venue for consumers (followed closely by discount/value department stores), with 45 percent of consumers indicating that they will complete at least some of their holiday shopping online.

The Economics Center determined that in the 2013 holiday period, Ohio consumers spent 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 lost almost $70 million in sales tax revenue because of online purchases on which sales tax was not paid. In addition, the Economics Center determined that Ohio retailers lost nearly $200 million in holiday sales in 2013 as a result of consumers choosing Internet retailers over traditional brick and mortar retailers.

The loss of tax revenue is not the only concern of untaxed online retail sales. Though consumers can find cheaper prices online (by at least 6.75 percent in many counties) these lower prices cost local stores and the local economy. As consumers shift their purchases to the online marketplace, brick-and-mortar stores will suffer, causing local employment and wages to decline. In 2011, the Economics Center estimated that Ohio's economy was 15,000 jobs poorer due to the magnitude of online retail sales. However, many states have begun to collect online sales taxes, and four of the five states that border Ohio collect sales taxes for online purchases.

Sales tax collections are critical to the health of Ohio's economy and institutions. Further, purchases of non-taxed goods through the Internet may harm the local economy by modifying consumer purchase behavior, discouraging businesses from making local investments, and reducing the amount of funding to local government institutions. These impacts are substantial and growing; however there are effective legal mechanisms for dealing with this issue, and the number of states employing these tactics continues to grow.

FACTORS INFLUENCING HOLIDAY SPENDING

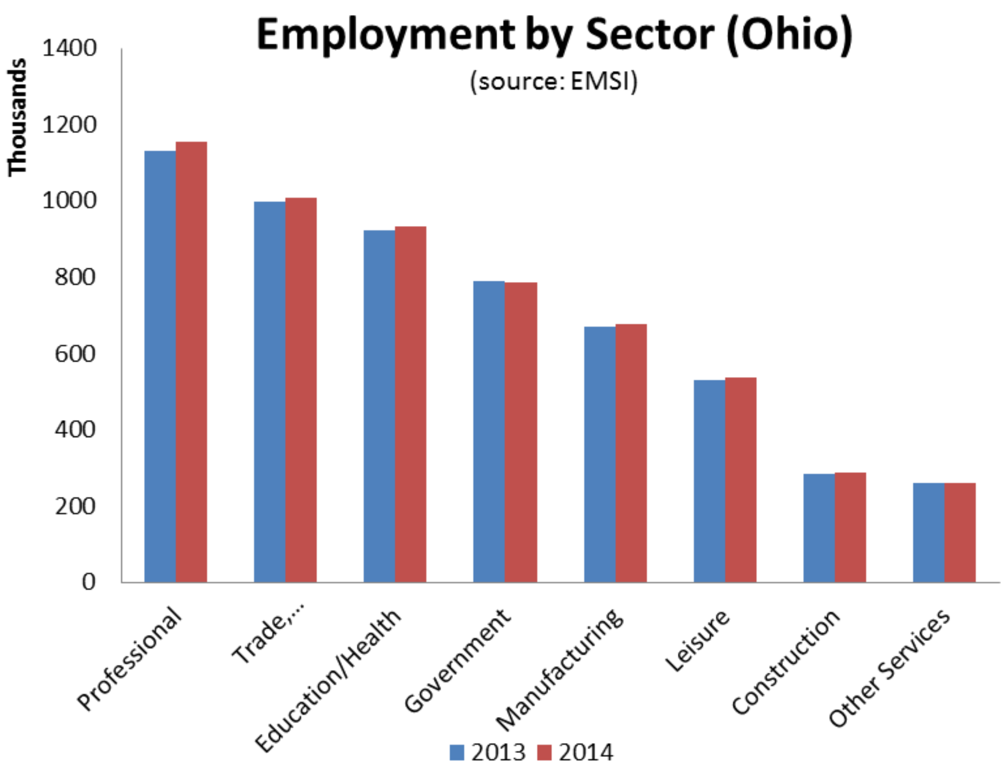
Employment

Employment in Ohio has continued to recover over the past year. The unemployment rate has declined by nearly two percentage points since the same time last year, and currently rests at its lowest point since 2006. With the exception of Government and Other Services, all major industry sectors have added jobs over the past year. In addition, the retail trade sector in Ohio has increased jobs from 562,824 in 2013 to 564,043 in 2014 (QCEW employment).

Table 2: August Measures of Ohio Employment

	Last Year	Current Year	Change
Civilian Labor Force (thousands)	5,779	5,740	-0.6%
Unemployment	7.1%	5.1%	
Employment (thousands)	5,299	5,331	0.6%

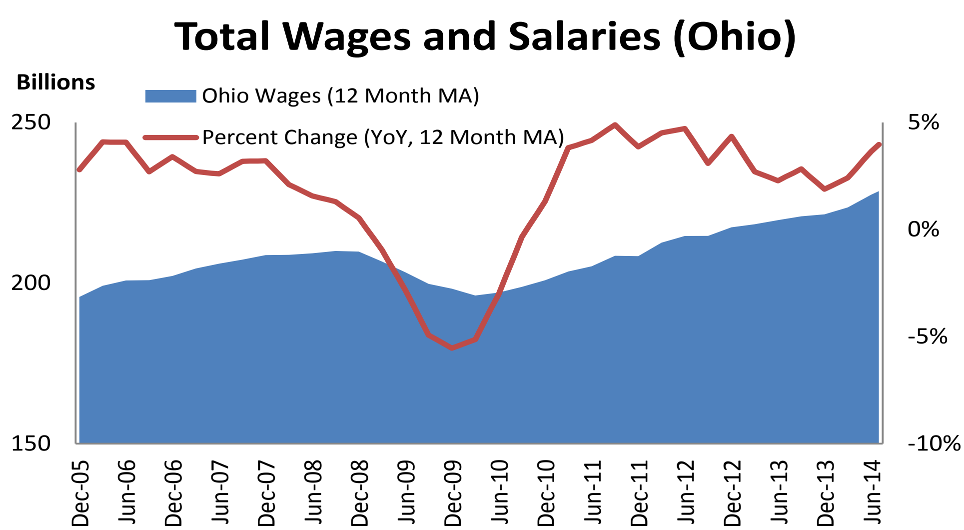
Figure 4: Annual Employment by Sector



Wages and Salaries

Total wages have continued to increase in 2014. Improving employment numbers and increased productivity among existing workers have resulted in year over year positive wage growth. A high percentage of an individual's paycheck is used to purchase goods and services. When individuals see an increase in their paycheck, an increase in retail sales usually follows.

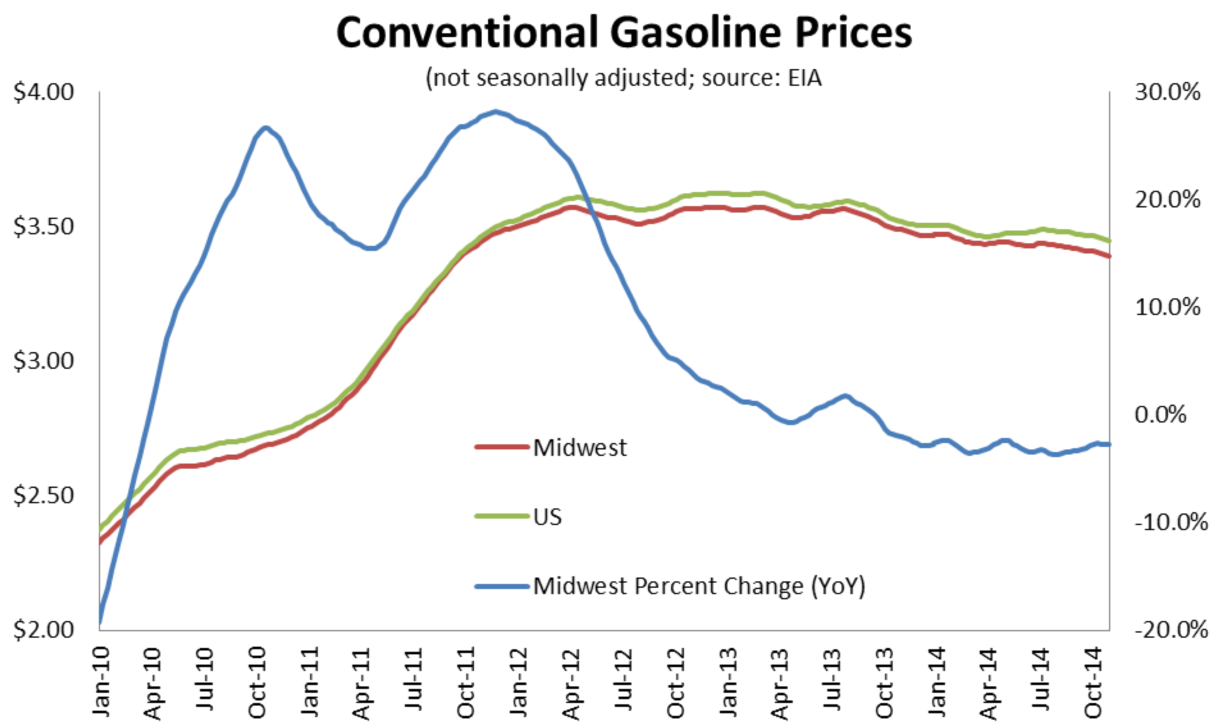
Figure 5: Wages and Salaries



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 2.8 percent lower, year-over-year (using annual averages ending the first week of November) and 7.2 percent lower relative to the first week of November 2013. While gasoline prices are lower, electricity prices for the home are up from last year. Based on data from the Public Utilities Commission of Ohio, electric bills are 7.1 percent higher, year-over-year (August data), while natural gas bills are 8.7 percent higher.

Figure 6: Gasoline Prices



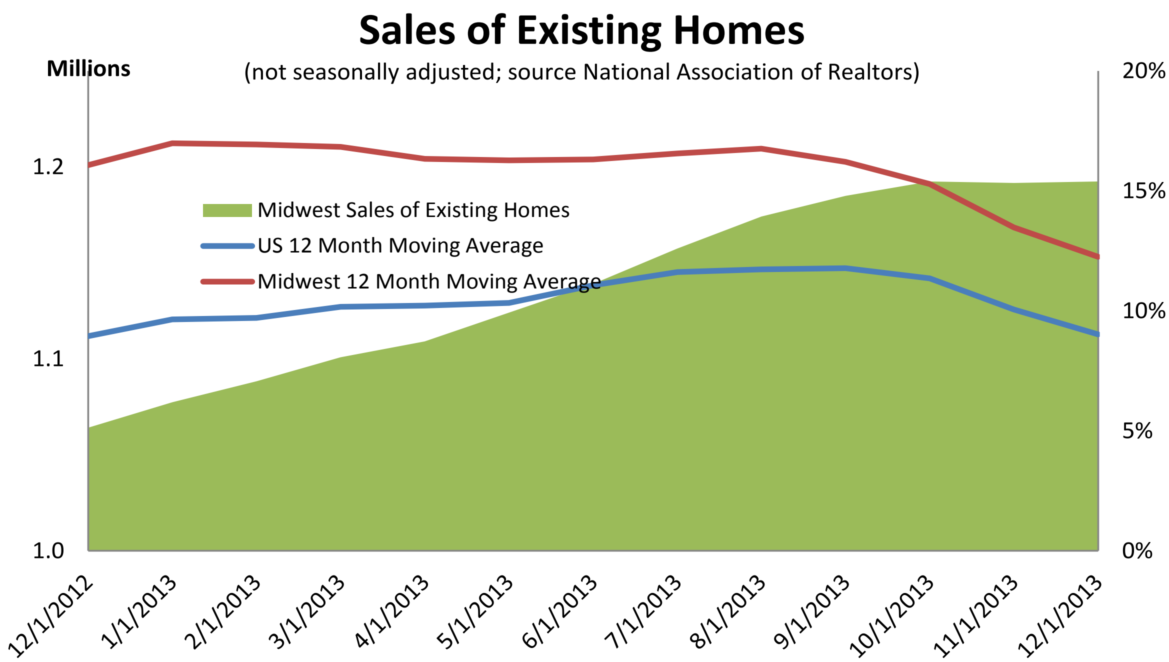
Sales Taxes

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 2014, the State of Ohio increased the sales tax rate from a base rate of 5.5 to 5.75 percent. While economic theory suggests that an increase in tax rates will cause consumers to decrease their spending, little impact of this change in tax rate has been seen on total retail sales, though sometimes such impacts are delayed. Likely, this diminished effect is due to the negligible cost increase represented by this additional tax. Nevertheless, retail sales seem to be continuing their upward trend in the State of Ohio. When comparing retail sales tax receipts for the first half of calendar year 2014 to the same period in 2013, sales tax receipts in Ohio increased by 3.6 percent.

Increases in Wealth

The recent growth in the wealth of Ohioans has stagnated from the growth seen in previous years. Over the past year, the stock market has only risen by 5.1 percent relative to the first week in November of 2013 (as measured by the Russell 2000 Index). This is distinctly lower than the growth from the first week of November in 2012 to 2013 of 39.6 percent. Midwest home sales have increased by twelve percent (based on a 12-month moving average ending in December 2013), but the prices of these Midwest home sales have increased by only 5.0 percent relative to last year.

Figure 7: Existing Home Sales



The credit picture for households has steadily improved over the past few years. *Credit card charge-off rates* have fallen to 3.3 percent in the second quarter (Q2) of 2014 from 10.8 percent in Q2 of 2010. *Credit card delinquency rates* have fallen from 6.8 percent in Q2 of 2009 to 2.3 percent in Q2 of 2014. In addition, *household financial obligations as a percent of disposable income* have fallen from 17.8 percent in 2007 to 15.3 percent in Q2 of this year. 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 households' willingness to borrow during the holiday season. From January 2009 through October 2012, this ratio was regularly declining. However, between October 2012 and January 2014, this ratio increased from 15.0 to 15.5 percent and has remained steady at this level since. 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. The University of Michigan's index of consumer sentiment rose last December to 77.5 (from 70.4 in November), and has continued this trend through 2014, reaching its highest point since 2007 of 94.5 in October. This increase in consumer optimism will undoubtedly affect consumer expenditures this holiday season.

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 slowed last year, growing at 2.4 percent year-over-year relative to 2013 (3.5 percent) and 2012 (5.5 percent). Since the Great Recession, overall retail spending has continued 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.

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.