Wealth Management

Consumer comeback

Return to form could reshape the spending landscape

U.S. consumers experienced a challenging 2020, but we believe consumer spending is positioned for a strong recovery this year and into 2022. Furthermore, a recovery would likely reshape the consumer spending landscape away from stay-at-home spending and towards out-of-home spending. We believe the reshaping of the U.S. consumer spending landscape is a compelling investment theme, with the travel-related and restaurant industries as well as certain segments of brick-and-mortar retail positioned to outperform during a consumer comeback.

Consumer comeback

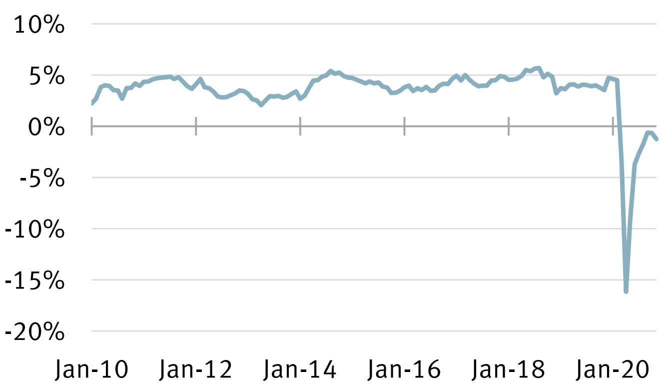
Consumer spending tracked by the U.S. Bureau of Economic Analysis declined 2.7% in 2020, compared to the 2010–2019 average annual growth rate of 4.0%, as the pandemic health crisis and economic lockdowns drove both the unemployment rate and the savings rate significantly higher. Those consumer spending headwinds were partially offset by fiscal stimulus payments and extended unemployment benefits under the CARES Act.

We believe the U.S. consumer is poised to make a strong comeback in 2021, as the rollout of COVID-19 vaccines should enable consumer mobility and spending to recover. In addition, U.S. consumers hold a strong financial position and excess savings, so spending could ramp up quickly as consumers reengage.

Lower interest rates and declining consumer debt levels have strengthened consumers' financial position. The metric of U.S. household financial obligations (debt) as a percentage of disposable personal income continued its multiyear trend lower in 2020 despite the pandemic. In Q3 2020, U.S. households spent 14.3% of their disposable income repaying their debts, compared to 15.2% at the end of 2019 and the historical high point of 18.1% in 2007, according to data from the St. Louis Fed.

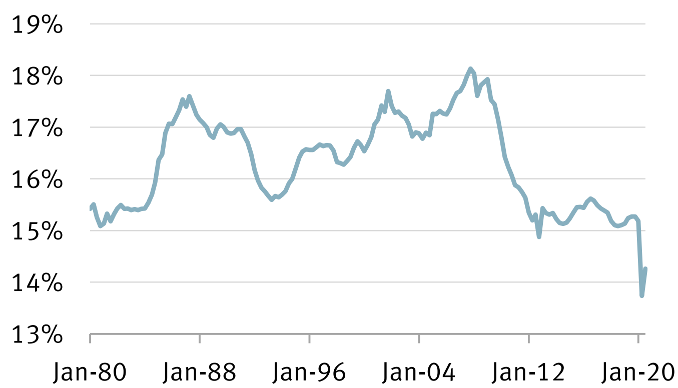
Separately, the U.S. personal savings rate jumped from 7.2% at the end of 2019 to an average of approximately 16% during 2020, based on St. Louis Fed data. RBC Capital Markets, LLC Chief U.S. Economist Tom Porcelli has

U.S. personal consumption expenditures (PCE), year-over-year growth



Source - U.S. Bureau of Economic Analysis, Federal Reserve Bank of St. Louis; monthly data through November 2020

U.S. household debt as % of disposable personal income



Source - Federal Reserve Bank of St. Louis; monthly data through November 2020

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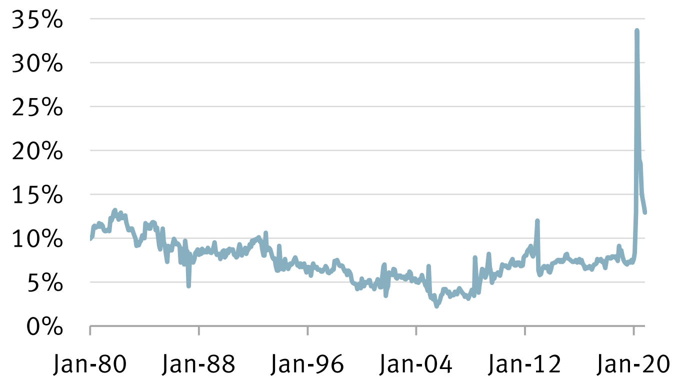
estimated the volume of excess savings during 2020 on an eight-month moving total basis is about $1.4 trillion over the pre-pandemic level. That level of excess savings represents approximately 6% of U.S. annual GDP and 30% of U.S. retail sales excluding autos. We believe that excess savings represents pent-up demand that can drive strong consumer spending during an economic reopening.

Consumers have been further armed for spending by the fiscal stimulus payments issued to eligible households in early January 2021. In addition, Congress is set to begin negotiating another fiscal stimulus package that will likely include additional payments to eligible households.

U.S. personal savings rate



Source - Federal Reserve Bank of St. Louis; monthly data through November 2020

Reshaping the consumer landscape…again

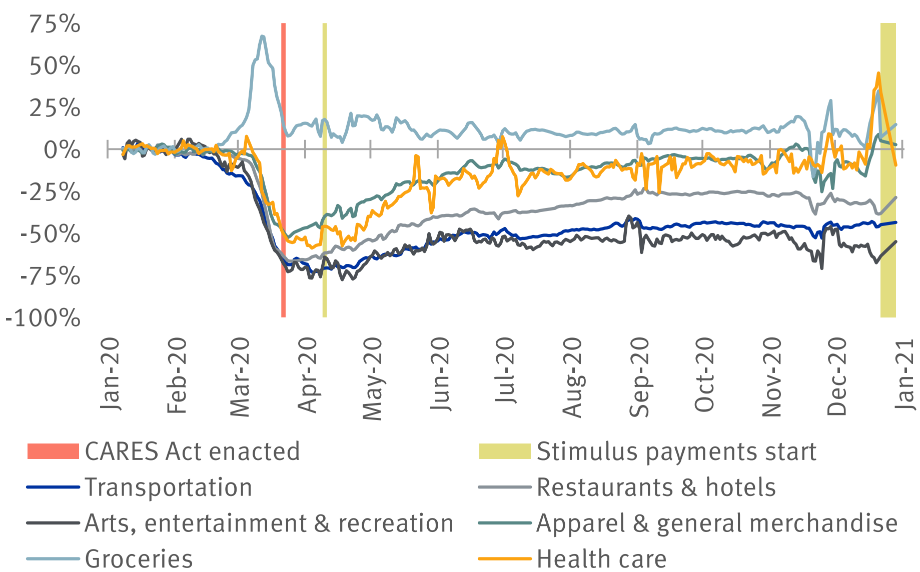
The COVID-19 pandemic significantly altered U.S. consumer spending patterns. Stay-at-home spending surged in 2020 as consumers rushed to purchase basic household goods like toilet paper and food items for home cooking. Consumers also significantly increased their home improvement spending, which received an added boost from increased home sales activity in 2020. Consumer purchases through digital channels surged, to the benefit of e-commerce retailers and delivery companies.

In contrast, out-of-home spending plunged in 2020 as consumer mobility was voluntarily and involuntarily limited by pandemic health concerns and economic activity restrictions. Travel and entertainment businesses and restaurants were hit especially hard, but other less-obvious spending categories—including elective medical procedures, apparel, and cosmetics—were also negatively impacted.

As the rollout of COVID-19 vaccines gains steam, we expect a strengthening economic recovery and increased consumer mobility to reshape the consumer spending landscape once again.

RBC Capital Markets Inc. Head of U.S. Equity Strategy Lori Calvasina has highlighted the importance of the CARES Act's fiscal stimulus measures in stabilizing overall consumer spending trends during the worst of the economic lockdowns in 2020 and helping drive a recovery. As the chart of consumer spending by industry shows, out-of-home spending categories remain well below their pre-pandemic levels. Based on our expectation of a consumer comeback, we believe certain consumer-focused companies operating in those categories could provide investment opportunities.

U.S. consumer spending by industry



Source - RBC Capital Markets, tracktherecovery.org, Affinity Solutions; data through 1/3/21

On the sector level, we tend to favor the Consumer Discretionary sector over Consumer Staples as discretionary spending has been most crimped by the pandemic. However, we would note that certain Consumer Staples businesses also saw their operations negatively impacted by the pandemic, and

Sectors positioned to benefit from a post-pandemic consumer recovery

Consumer Discretionary	Consumer Staples	Communication Services	Financials & Info. Technology	Industrials
Restaurants Online travel services Apparel & accessories Hotels & casinos Cruise lines	Soft drinks Personal products	Movies & entertainment Telecom carriers	Card payments	Airlines Mobility app platforms

Source - RBC Wealth Management

also that we believe there are stocks linked to travel and consumer spending across other sectors that stand to benefit from a consumer comeback.

In conclusion, we believe COVID-19 vaccines will enable a consumer comeback that will reshape the U.S. consumer spending landscape away from stay-at-home spending towards out-of-home spending. In our view, investors should begin to think about positioning into sectors that would benefit from such a shift.

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