Recession Risks Rise as Consumers Turn Cautious

Consumer spending has powered the economic recovery from the pandemic shock. Now wallets are thinner, and some businesses are feeling the difference.

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The economy's resurgence from the pandemic shock has had a singular driving force: the consumer. Flush with savings and buoyed by a sizzling labor market, Americans have spent exuberantly, on goods such as furniture and electronics and then on services including air travel and restaurant meals.

How long this spending will hold up has become a crucial question.

Despite contortions in world markets, many economists are cautioning that there is no reason to panic — at least not yet. In July, there was a notable slowdown in hiring and a jump in the unemployment rate to its highest level since October 2021, but consumer spending has remained relatively robust. Wages are rising, though at a slower rate, and job cuts are still low.

"Overall, there isn't evidence of a retrenchment in consumer spending," said Gregory Daco, chief economist at the consulting firm EY-Parthenon. The strength of spending helped power greater-than-expected economic growth in the spring.

That could change if the labor market's slowdown accelerates.

Already, some consumers, especially those with lower incomes, are feeling the dual pinch of higher prices and elevated interest rates that are weighing on their finances. Credit card delinquencies are rising, and household debt has swelled. Pandemic-era savings have dwindled. In June, Americans saved just 3.4 percent of their after-tax income, compared with 4.8 percent a year earlier.

On calls with investors and in boardrooms around the country, corporate executives are acknowledging that customers are no longer spending as freely as they used to. And they are bracing themselves for the slide to continue.

On Wednesday, Disney cited a “moderation of consumer demand” that “exceeded our previous expectations” for a newly challenging outlook at its theme parks, a key to its profitability. “The lower-income consumer is feeling a bit of stress,” with less to spend on amusements, Hugh F. Johnston, Disney’s chief financial officer, told analysts.

There is also apprehension among retailers, fast-food chains and packaged-goods makers.

“We are seeing cautious consumers,” Brian Olsavsky, Amazon’s chief financial officer, said on a call with reporters last week. “They’re looking for deals.”

Chris Kempczinski, the chief executive of McDonald’s, likewise noted last week that some lower-income consumers were “dropping out of the market, eating at home and finding other ways to economize.”

McDonald’s, which reported a 1 percent decline in global same-store sales, a measure of year-over-year retail sales for companies, in the quarter that ended in June, has been trying to lure back consumers with a $5 value meal. Other fast-food brands are introducing similar deals. Taco Bell is offering a variety of tacos and burritos priced at less than $3. Burger King is selling a “Your Way Meal” for $5.

Many food manufacturers, which are seeing volumes decline as consumers buy less or trade down to less expensive store-brand options, also say they plan to reduce prices on some foods, increase portions on others and offer more sales.

After reporting a 0.5 percent decline in revenues in the second quarter in its Frito-Lay snack business from year-ago levels, a result of a 4 percent drop in volumes, executives at PepsiCo noted that some consumers had become more price-sensitive about some of its salty snacks, like Tostitos tortilla chips and Ruffles potato chips. As a result, the company said, it plans to cut prices or offer more sales on certain snacks.

“You see different behaviors happening everywhere,” Ramon Laguarta, PepsiCo’s chief executive, said on an earnings call last month. “The connecting line would be: The consumer is more cautious, but the consumer is willing to spend in areas where they see value.”

Retail sales have not buckled. In June, the most recent month for which data is available, they were unchanged from the month before, according to the Commerce Department, defying expectations of a decline. But retailers are also observing changes in consumer spending.

Mr. Olsavsky of Amazon said shoppers were generally shifting to lower-cost items. And he noted that purchases of higher-ticket items had declined from levels that a thriving economy would indicate.

Many food manufacturers say they plan to reduce prices on some foods, increase portions on others and offer more sales. Jessica Attie for The New York Times

Tony Spring, Macy's chief executive, described consumers as "under pressure, discerning, very choiceful," in an earnings call in May. Gap, the struggling apparel retailer, said in its most recent earnings call that it was taking a "measured view of the consumer environment."

Retailers that sell big-ticket items like electronics and furniture have also noted more consumer reluctance. Big Lots said in June that a shortfall in its sales goals was "due largely to a continued pullback in consumer spending by our core customers, particularly in high-ticket discretionary items." Williams-Sonoma, a higher-end retailer that owns Pottery Barn, said consumers were buying fewer large furniture pieces, while sales of textiles and easy decorating updates were still healthy.

Even higher-income consumers, who have generally been less affected by high interest rates, appear to be making some adjustments.

Walmart has repeatedly said higher-income shoppers started spending with it during the height of inflation and now hopes to retain them with a revamped private-label food line that includes gluten-free crackers and coconut-lime sparkling water. (Executives also still take pains to emphasize that 70 percent of the products in that line are priced under $5.)

"Life is about balance, and retail is about balance," Doug McMillon, Walmart's chief executive, told reporters in June. "We're not letting go of one thing to try and reach for something else."

A clearer picture from retailers will emerge in the coming weeks, when many, including Walmart, Target and Macy's, report their most recent quarterly earnings. Analysts will be looking for signs of further belt-tightening among shoppers.

Even airlines, which enjoyed a postpandemic surge in travel, are bracing for a decline in demand beyond the typical fall lull, though they have indicated they are experiencing little pullback.

The Federal Reserve, which held its benchmark interest rate at 5.3 percent last week, is widely expected to begin cutting interest rates at its meeting in mid-September, which could begin to provide some relief to consumers.

Still, there is fear that the weak July jobs data reported on Friday could herald deeper consumer restraint in the months to come.

While the uptick in the unemployment rate was largely driven by more workers entering the work force, and not by employees losing their jobs, there are more potentially worrisome signs for consumers below the surface. The number of people working part time who would have preferred full-time employment increased, while the number of hours worked per week ticked down slightly, both signs that workers are taking home less pay.

Should that trend continue, it could set off a damaging economic cycle whose impact would be more widespread, economists say.

"The key risk at the moment is that firms begin to pull back on hiring and that we see that translate into job loss," said Michael Pearce, the deputy chief U.S. economist at Oxford Economics. That could precipitate more restricted consumer spending, which could in turn lead to revenue declines that could drive companies to cut jobs.

"It's this self-fulfilling process," he said.

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