



# How the Stimulus Could Affect Stocks

## Wall Street warily eyes government rebates

By Kirk Shinkle

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American consumers are in a pretty foul mood, and the debate is on as to whether they'll cheer up when \$117 billion in stimulus-plan tax rebates land in mailboxes across the nation.

On May 2, the first round of checks is set to go out, starting at \$600 for most singles and rising into four figures for many families. (Some low-income workers and recipients of federal benefits will get \$300 payments.)

Retailers are already taking notice. Big chains like Sears and grocers like Kroger have announced they'll offer gift cards above and beyond the face value of the checks to entice wary shoppers willing to trade cash for store credit.

Expect rivals to follow as the retail sector, already reeling from dismal March sales, positions itself for what could be a fierce competition.

Investors are worried because the American shopper's litany of troubles is long: Rising prices for food and gasoline, mounting debt, resetting mortgage rates, and rising unemployment have created an anxious undercurrent among large swaths of formerly upbeat consumers.

The worry for Wall Street is that they'll spend accordingly. "My sense is most consumers will use this tax rebate for survival," says Roxanne Meyer, a specialty retail analyst at Oppenheimer.

Consumer surveys and expectations of spending seem to back that view. The latest ABC News/*Washington Post* Consumer Comfort Index this month hit its lowest level since October 1993. Gasoline prices are climbing, home prices are falling, and unsettled credit markets are tightening lending on everything from credit cards to corporate debt.

Also, after last week's April 15 tax filing deadline, a survey by Discover U.S. Spending Monitor showed consumers are cash-strapped heading into rebate season. Nearly two thirds of those surveyed who expect a tax refund plan to spend it on household expenses

like gas, groceries, or mortgage or credit card debt. Just 16 percent plan to save their refunds.

"The windfall has already been spent," according to Dick Outcalt, a longtime retail watcher and consultant at Seattle-based Outcalt & Johnson: Retail Strategists. "Household liabilities are \$1.40 compared to their \$1 of disposable income."

Such belt-tightening has already shaken retail stocks in this downturn. The S&P Retail Index has lost nearly a third of its value compared with a year ago.

Still, cash in hand plus low interest rates could help keep the consumer from capitulating totally. Morgan Stanley economists estimate consumers will probably spend 20 cents of every tax rebate dollar—not a negligible amount but not enough to lift all boats. They predict that consumers will "narrowly skirt" a spending downturn despite a recession but that the recovery will be slower than many would like.

So who gets the cash? If a boost comes, it will be during the third quarter. The likely beneficiaries would be the sorts of stores that offer necessities rather than luxuries. Nimble department stores and big discounters might be among those best positioned to benefit.

Citigroup's Deborah Weinswig, who covers multiline and food retailers, predicts a small pickup from rebate spending. "People are going to feel a little more wealthy, but there's still a big push to be frugal right now," she says.

Weinswig likes **Wal-Mart**, which won a 25 percent share of the rebate checks cashed during 2001 and could see a strong repeat performance this time around. Another favorite is **J.C. Penney**, which sent shivers through the retail sector after it cut first-quarter guidance but could reap an extra \$150 million in sales from the stimulus checks alone.

More broadly, the second half of the year could see improved results as problems that plagued retailers through late 2007 and early 2008—poor holiday sales, high inventories—offer some breathing room for better-than-expected earnings late in the year. Also, the timing of the checks matters. They will go out during some crucial months for back-to-school shopping.

Other analysts discount the impact of the checks but maintain that fundamental strength in a few choice retail names makes some stocks attractive.

**Brian Hamilton, who runs researcher Sageworks.com and screens stocks for underlying fundamental strength, likes Men's Warehouse, where sales are rising with strong cash flow and positive net income.** Last week, the company saw shares rise after the firm expressed confidence in its first-quarter guidance.

Specialty retailers as a whole might not be so lucky. Oppenheimer's Meyer remains generally downbeat, noting that in the last recession, a weighted average of her group underperformed the S&P 500 by 25 to 35 percent. It's off just 10 to 15 percent in this

downturn. She predicts any rebate-inspired rally will simply be a "head fake" before the next leg down.

One short-term exception, she says, could be urban fashion retailer **Citi Trends**. The company saw notable one-time gains during both the last tax rebate and after government checks were cut following Hurricane Katrina, when same-store sales jump above 20 percent from single digits in earlier months. "Citi's customers are used to spending their disposable income on clothing," she says.

Better bets remain the fastest growers that have managed to buck much of the sector slowdown already. There, **Urban Outfitters** and **J. Crew** top Meyer's list of picks. "They are absolutely on top of their game and poised to have a terrific year," she said of J. Crew, while at Urban, "you would never know we're in a recessionary environment based on traffic in their stores."