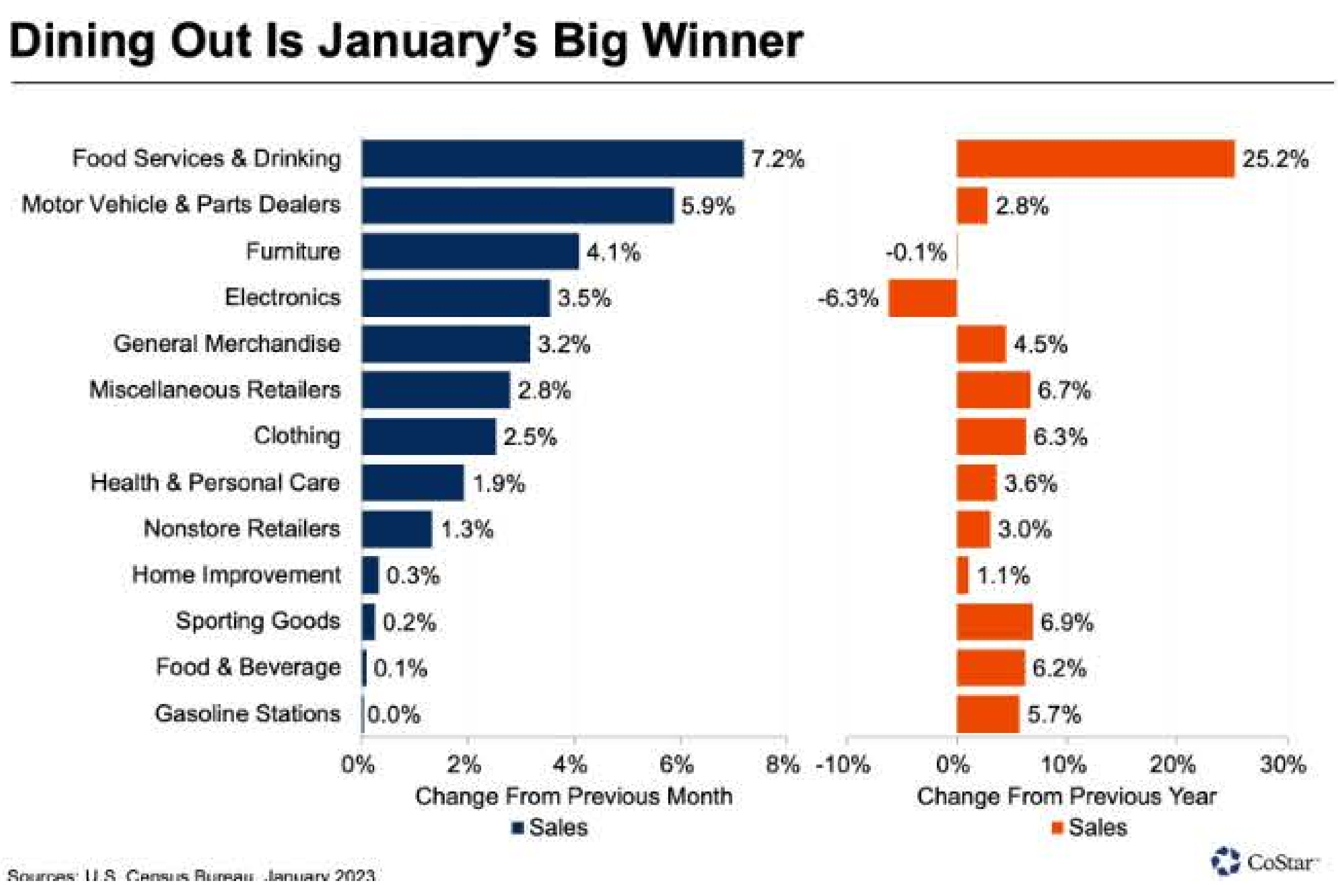
Retail Sales Grow Again, but So Did Inflation and Household Debt
Are We Better or Worse After Week of Outperformances?

By Christine Cooper and Rafael De Anda

About three months ago, we “thanked shoppers for shouldering the economy.” That trend has continued so far into 2023, as witnessed in various economic indicators released last week.

Among the most notable, retail and food services sales posted a gain of 3% in January, crushing expectations and reversing the declines seen in November and December.

All retail categories saw increases in the month. These are seasonally adjusted figures, which take into account for the sharp pullback that is typical of December's holiday-fueled spending. Non-seasonally adjusted retail and food services sales fell by 16.2% over the month, whereas pullbacks from December to January averaged a decline of 18% in the previous five years.



Consumers are continuing to lean towards spending on services, after the pandemic created pent-up demand for experiences, social events and entertainment. Bars and restaurants in particular were big winners in January, with sales surging by 7.2% in January and they are now 25.2% higher than a year ago, leading all major categories by both measures.

At the opposite side of the scale were inflation-sensitive categories, such as purchases at grocery stores and gasoline stations, which saw sales grow much more slowly in January. Demand for sporting goods and home improvement projects are now mostly squelched, with sales up by only 0.2% and 0.3%, respectively.

Along with the bounce back in retail spending, though, the consumer price index jumped by 0.5% in January, the largest increase in three months, and earlier figures for November and December were revised higher — suggesting that the Federal Reserve still has work to do to get inflation to cool. However, despite January’s hot reading on inflation, even retail sales adjusted for price changes were still quite strong.

Sales at motor vehicles and parts dealers accounted for almost 20% of overall retail sales, the largest share of any category, and grew by 5.9% over the month.

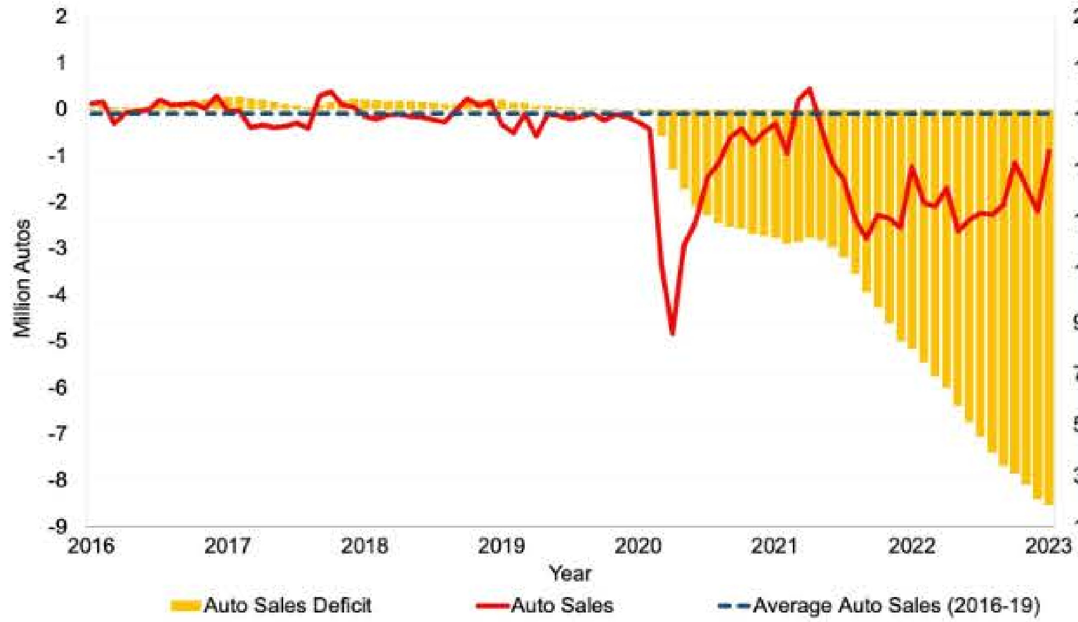
Auto sales have been significantly slower than before the onset of the pandemic given supply chain disruptions and a global shortage of semiconductors, which are critical components in today’s vehicles. These glitches are now easing, and we could see higher auto sales in 2023 simply to replace older, non-functioning vehicles.

To illustrate the amount of pent-up potential demand for automobiles, pre-pandemic auto sales averaged 17.2 million units annually rate between 2016 and 2019 but tumbled as the economy was shut down. The rebound was quick but was soon stymied by production and delivery delays. For a brief period in early 2021, auto sales topped the mark, but sales have been much slower since then. In total, the deficit between actual auto sales and the pre-pandemic average, should that return, has grown to 8.4 million autos.

If sales at motor vehicle and parts dealers do continue to grow at elevated levels, they may impact the financial well-being of consumers at large. More than any other retail sales category, auto sales are typically financed and paid over several years, which means that sales can increase as households assume more debt, rather than paying for purchases with higher incomes. The New York Federal Reserve reported that auto loan debt grew by 6.4% year-over-year in the fourth quarter of 2022, the largest increase since the third quarter of 2017.

Of course, households are accumulating debt from other categories as well, including mortgages and credit cards, where year-over-year growth is 9.1% and 15.2%, respectively. Total household debt grew by 8.5% year-over-year in the fourth quarter, reaching $16.9 trillion. The pandemic-fueled stimulus spending that padded household bank balances over the last few years and supported stronger spending is now evidently waning as consumers turn to credit cards and loans to finance purchases.

Automobiles Will Soon Need To Be Replaced



Source: Bureau of Economic Analysis, January 2023

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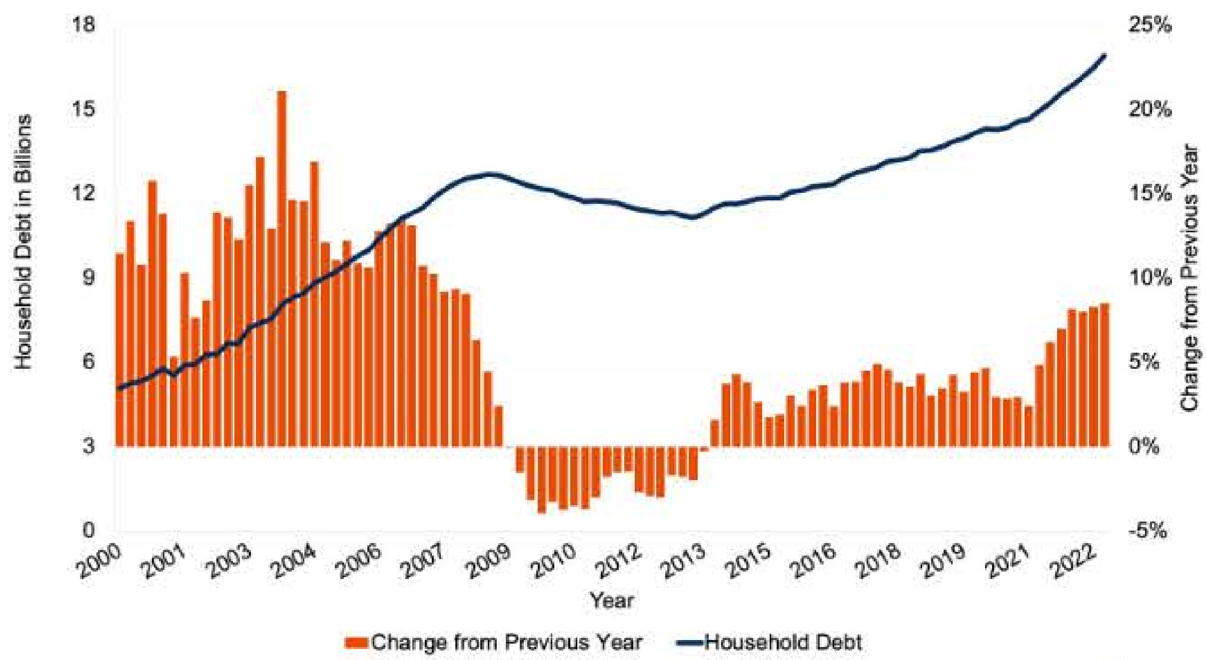
Households Are Taking On Additional Debt



Source: Federal Reserve Bank of New York, Fourth Quarter of 2022

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