NRF National Retail Federation

MONTHLY

Economic Review

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The data for this report is released on a rolling schedule. The presented numbers are current as of publication and are subject to revision.

SYNOPSIS | 2023 Was Not a Smooth Run But Consumers Showed Resiliency

The 2023 U.S. economy was marked in large measure by the impressive resiliency of the consumer. A year ago, many commentators were skeptical and calling for a recession, but the recession never came. With each passing month, consumers kept spending despite inflation and higher borrowing costs, supported by a tight labor market, a wealth effect from a rise in equity and home prices, and savings built up during the pandemic. By the end of the year, inflation-adjusted gross domestic product was up a solid 2.3% year over year, and December's unemployment rate of 3.7% was one of the lowest in decades.

Consumer spending has been supported not just by low unemployment but also by wage gains, which have outpaced inflation even as employers have slowed hiring. The Personal Consumption Price Index – the Federal Reserve's preferred measure of inflation – was up 2.6% year over year in November, substantially less than the year-over-year 4.5% increase in wages measured by the quarterly Employment Cost Index.

Nonetheless, those tailwinds are not necessarily sustainable. Tighter credit conditions along with higher borrowing costs continue to be in place now that we've turned the page on the annual calendar, and employment reports confirm that the labor market expansion is slowing. According to the Bureau of Labor Statistics, nonfarm payroll employment expanded by 216,000 jobs in December – a solid figure that included a gain of 164,000 jobs on private payrolls. But there were revisions to prior months that reduced private payrolls by 96,000, leaving the net gain in private jobs at a modest 68,000. Job openings data provides some insight into the slowing of labor demand. Job openings fell to 8.79 million in November, the lowest reading since March 2021. While firms have clipped back hiring, they have largely avoided layoffs after struggling to attract workers after the pandemic. November's 1.53 million layoffs remained below the pre-pandemic average.

The slowing job market could actually be good news. While the odds of a recession are low compared with a year ago, there is no guarantee it won't happen. The Fed is hopeful that its long string of interest rate hikes will help slow the pace of growth in the economy and employment enough that inflation will decline without the economy sliding into a recession, and that appears to be working. Since the beginning of 2022, the Fed has increased the benchmark federal funds rate from near-zero to a range of 5.25-5.5%, a level not seen in two decades and one that many feared would trigger a recession. But the current inflation rate of 2.6% is down from a peak of 7% in mid-2022 and has come without a significant increase in unemployment. With breathing room to consider policy choices, the Fed has signaled that it is nearing the end of elevated interest rates, leaving the rate unchanged at its most recent meeting and projecting a federal funds rate of around 4.6% by the end of 2024. The big question is where rates will settle in the next several years if the Fed hits its target of bringing inflation down to 2%.

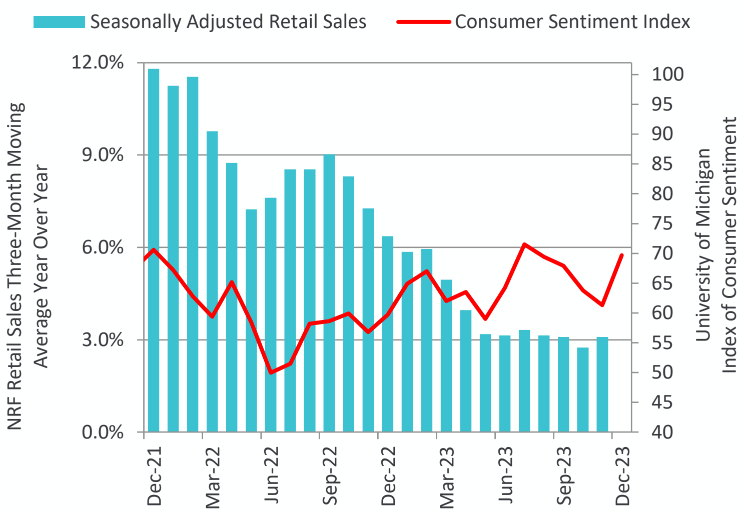
The disconnect between consumer spending and weak consumer confidence has been an important story in the past year. Recent surveys show consumers are concerned about a number of factors – the outlook for income, business and job market conditions slowing because of higher interest rates, ongoing inflation and political stress. Nevertheless, consumers have become incrementally more positive as price deceleration has unfolded. The University of Michigan's Index of Consumer Sentiment remains low but reversed four consecutive months of declines in December. Likewise, consumer confidence reported by the Conference Board improved markedly in the final month of the year, with the headline index rising to 110.7, the highest level since July. Prior low readings may have reflected the aftereffects of the pandemic as Americans contended with a one-two punch of rapid inflation and product shortages and then high interest rates.

In October and November of 2023, consumers continued to show their ability to spend, with spending on both goods and services growing 5.2% year over year unadjusted for inflation. Households have kept their foot on the pedal for services spending, which has returned to where it was prior to the pandemic at approximately 65% of consumption. Disposable personal income was up 7% year over year, much faster than earlier in the year, and helped boost consumer purchases. The holiday spirit may also have provided some extra energy. Core retail sales as defined by NRF – excluding automobile dealers, gasoline stations and restaurants – were up 3.3% unadjusted year over year on a three-month moving average as of November and up 3.7% for the first 11 months of the year. While we are waiting for December figures to be released, spending is on track to meet our projection for sound holiday shopping season growth between 3% and 4% over 2022.

In sum, 2023 was full of inconsistencies and uncertainties and not a smooth run. Consumers kept consuming when we expected they would have done the opposite. There were recession fears, regional bank failures and inflation, and the Fed continued to raise interest rates despite poor consumer confidence. Looking ahead, however, spending is elevated relative to current income and maintaining the recent pace of growth will be increasingly difficult. Household finances have been in good shape, but excess liquidity is shrinking as the savings buffer built during the pandemic has run down. While the amount of credit appears in the aggregate to be manageable as incomes have risen, consumers have ratcheted revolving debt back up to pre-pandemic levels. The labor market looks set to cool further this year, which will impact consumer expectations for employment and wage growth, and, in turn, affect spending decisions.

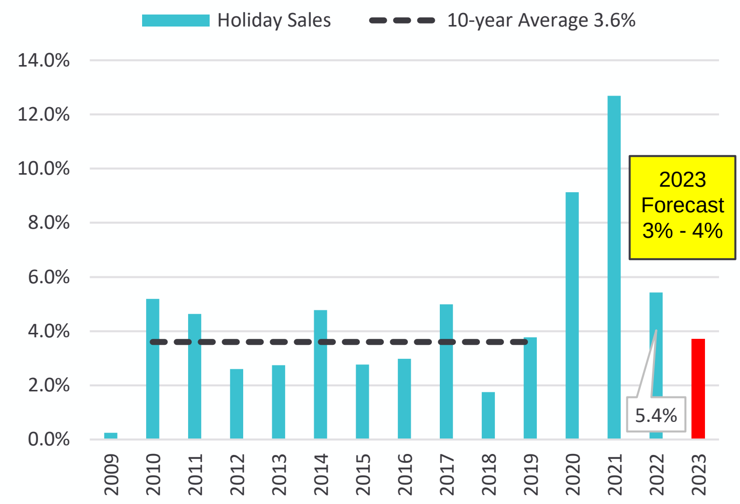
SALES AND SENTIMENT

Retail sales rose in November, but year-over-year growth stayed near the three-month moving average of 3%. Despite a jump in December, consumer confidence is consistent with a slower economy.



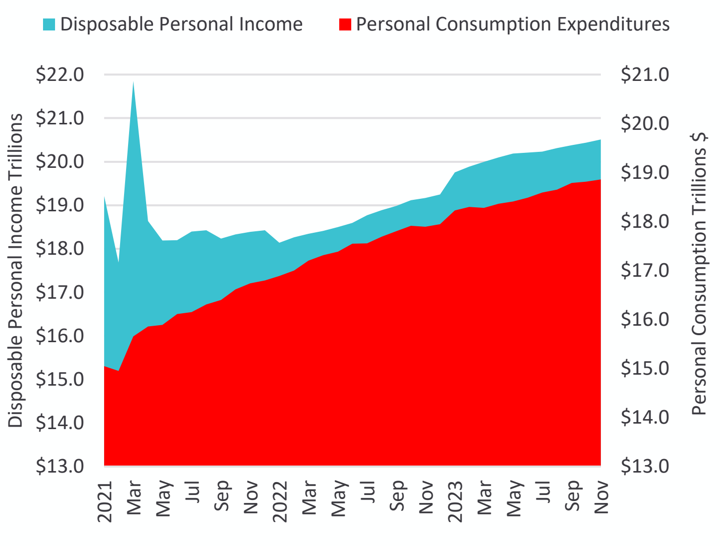
NRF HOLIDAY FORECAST

NRF forecast holiday spending would increase between 3% and 4%, which compares favorably with the 10-year average of 3.6% prior to the pandemic. Final numbers will come this month.



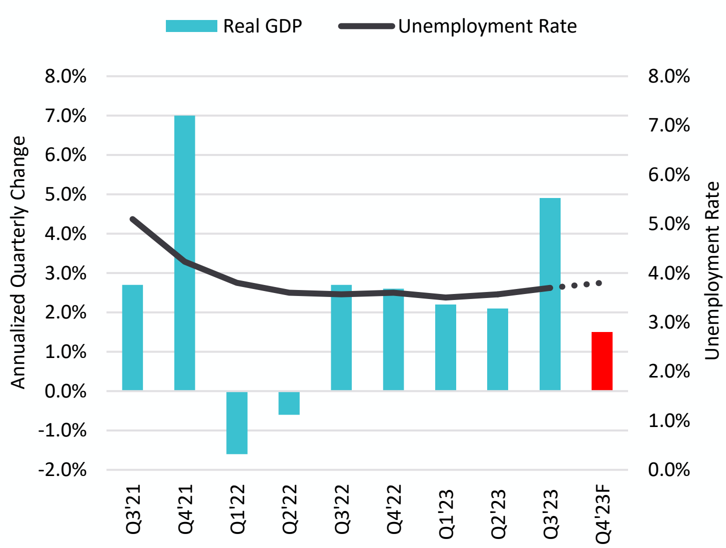
INCOME & CONSUMPTION

The trend for disposable personal income growth remains healthy. Growth has exceeded inflation for the past two months and will be a factor going into 2024.



GDP & UNEMPLOYMENT

Despite a surprise downward revision, GDP grew 4.9% in the third quarter, the fastest pace in nearly two years, according to the BEA.



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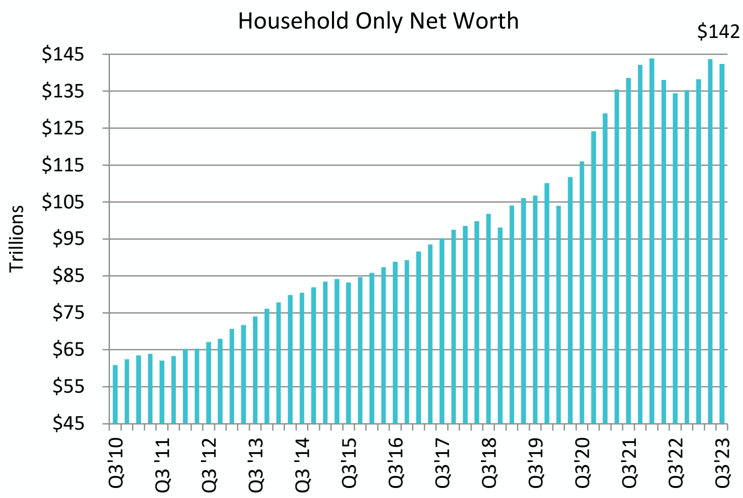
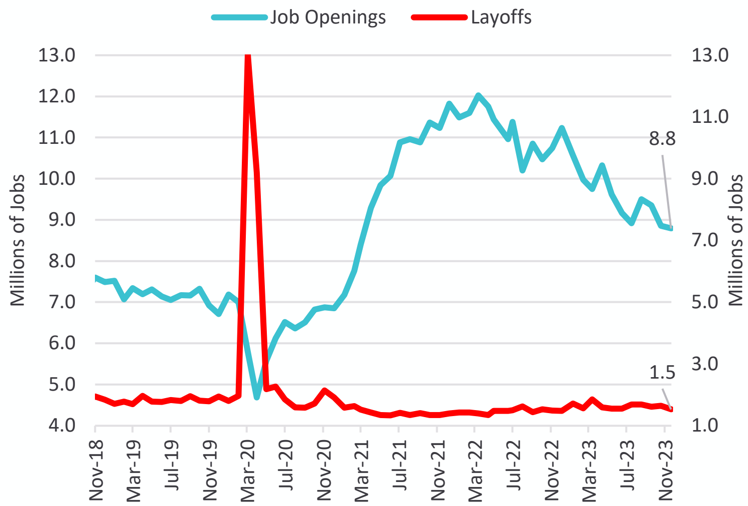
HOUSEHOLD NET WORTH

Household net worth fell $1.3 trillion in the third quarter after surging to a record $152.3 trillion in the second quarter. The decline snapped a three-quarter rise that had likely boosted consumer spending.



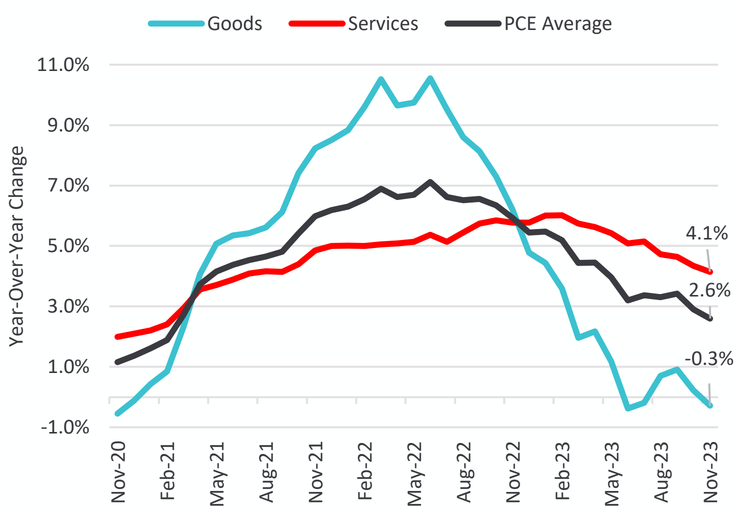
EMPLOYMENT

The demand for workers as measured by job openings fell in November to its lowest level in 2½ years. In contrast, layoffs hovered near historic lows.



CONSUMPTION EXPENDITURE

Year-over-year growth in the Personal Consumption Expenditures Price Index has drifted downward. While the price of goods has downshifted significantly, the price of services continues to drive inflation.



GOODS VS SERVICES

The 5.4% pace of overall consumer spending growth in November was driven by services. The largest contributors were housing and utilities along with restaurants and hotels.

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