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Inflation cools off US consumer spending

Article

The news: Inflation is starting to weigh on US consumers' spending as **household consumer spending rose 0.2% month-over-month (MoM) in May, a slowdown from a downwardly revised 0.6% increase in April,** per the US Commerce Department.

- But when those numbers are adjusted for inflation, that translates to a 0.4% drop. That's the first MoM decline this year—and an abrupt shift from the 0.3% gain in real spending in April.
- The balance between spending on goods and services continues to regress toward pre-pandemic levels as goods outlay fell, while spending on services grew.

- The level of inflation remained high in May, though it increased slightly less than expected. **Core personal consumption expenditure prices**—which exclude volatile food and energy prices—**rose 4.7% year-over-year** (YoY), 0.2 percentage point less than the previous month and 0.1 percentage point less than a Dow Jones estimate, per CNBC. The measure has been declining since February, when it was 5.3%.
- On a monthly basis, the measure increased 0.3%, slightly less than the 0.4% Dow Jones estimate.

Looking ahead: Consumers continue to spend, as their YoY household spending rose 8.6% in May.

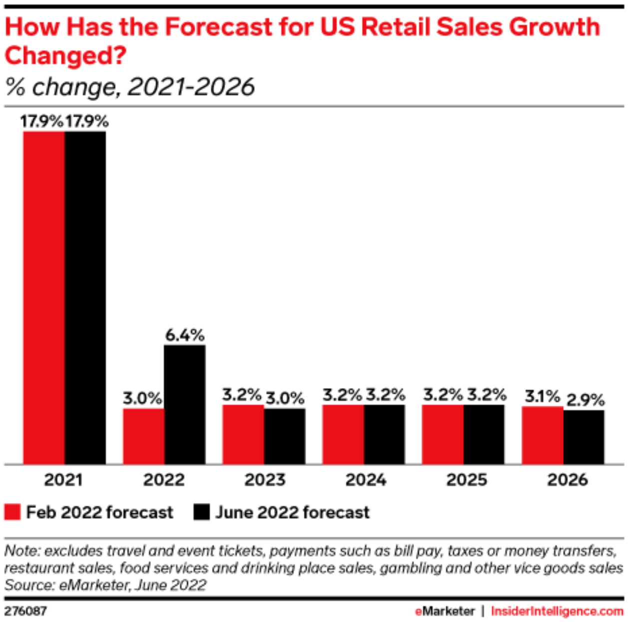
- But they are increasingly tapping into their savings. **The savings rate inched up to 5.4%**, after the rate fell to 5.2% in April, its lowest level in more than a decade in April.

A significant cooling off: Consumer spending appears to be losing steam.

- Spending on durable goods fell 3.2%, which shows that consumers are pulling back from big-ticket items, such as furniture.
- The slowdown is by design, as the US Federal Reserve is aggressively raising interest rates to combat inflation. However, it's walking a delicate line to avoid driving a more significant consumer pullback that could tip the economy into a recession.

What it means for retail: Despite the challenging environment, we expect US retail sales to grow 6.4% this year.

- That growth is largely due to inflation, as consumers have the means to keep up with the rising costs of essential items like food and household products.



The big takeaway: The good news for retailers is that consumers continue to spend. The bad news is that they've significantly shifted their spending during the first half of the year. That's left retailers such as **Bed Bath & Beyond**, **Target** and others discounting their excess inventory to keep it moving. To avoid similar mismatches between inventory with consumer demand, retailers in categories which have significantly slowed, such as home goods, may need to take a more conservative approach to merchandising.

Go further: For more on The Era of Uncertainty, read our report here.