Economics

Special Commentary — March 16, 2022

It’s Only Phenomenal When It’s Nominal, a Look at Real Retail Sales

Summary

- Is this the real life? Is this just fantasy? Retail sales shot up 4.9% in January, the largest monthly gain in any pre-pandemic month in 20 years before posting another gain in February. Unfortunately, there is no escape from the reality that inflation is higher now as it was when Queen's “*A Night at the Opera*” album was released in November 1975.
- The retail sales figures are reported nominally, which is to say: not adjusted for inflation, and thus must be taken with a grain of salt today when considering how the highest inflation in 40-years is eating into consumers purchasing power.
- We've constructed retail sales deflators based on the Consumer Price Index for total retail sales and per retail category to get a cleaner read on the degree to which prices are driving recent sales gains.
- The real estimates demonstrate more muted sales gains. The reported figures from the BEA suggest total retail sales are a whopping 25% ahead of their pre-pandemic February 2020 level. But when adjusting for the run up in consumer prices, we estimate real retail sales "just" 8% higher than prior to the pandemic.
- Sales at auto retailers and gasoline stations are where the real versus nominal divide is the most striking. While nominal auto sales are 28% ahead of pre-pandemic levels, dealers aren't moving more cars, but rather cutting dealer incentives and price concessions with real sales *down* about 1%. Similarly, consumers are actually purchasing a comparable amount of gasoline today as they were two years ago, they're just paying more to fill up their tanks.

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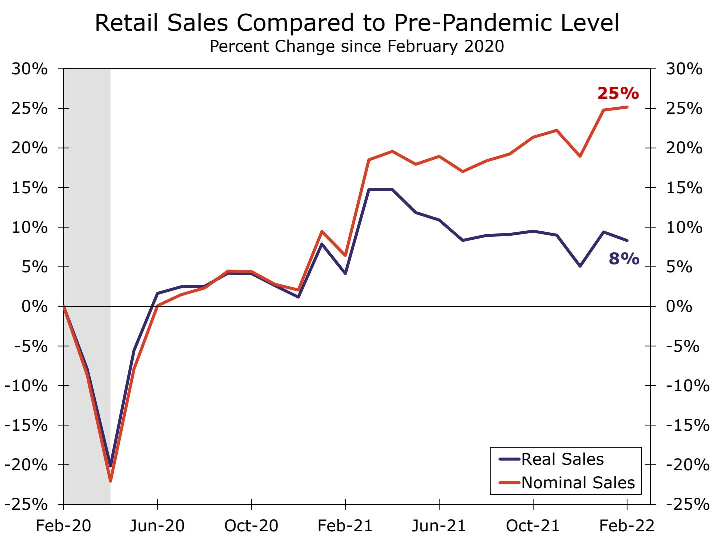


Source: U.S. Department of Commerce, U.S. Department of Labor and Wells Fargo Economics

Clean Read?

At the start of this year we encouraged readers not to worry about spending despite the surging case counts of the Omicron variant, a key concern at the time, saving our worry instead for the impact of higher inflation. At the time we offered that while "consumer activity can be sustained in the face of the Omicron variant, we are less sanguine about how households can continue to cope with ever higher prices." January ended up being the best month for retail sales since stimulus checks went out in March 2021, and we learned earlier today that retail sales notched another 0.3% gain in February. That said, since retail sales figures are reported nominally, the recent gains need to be taken with a grain of salt.

In each of the past six months the year-over-year headline rate of CPI inflation has risen higher, breaking inflation records that have stood for decades. At 7.9% in February, CPI inflation is hotter than it has been since January 1982. In the absence of an official "real" measure of retail sales, we set out to figure out a better way to factor in the highest inflation in a generation when we think about retail sales figures and its various categories. This task became more urgent with Russia's invasion of Ukraine in February because it makes price problems worse by driving energy prices higher and threatening to undo the early momentum in normalizing supply chains.

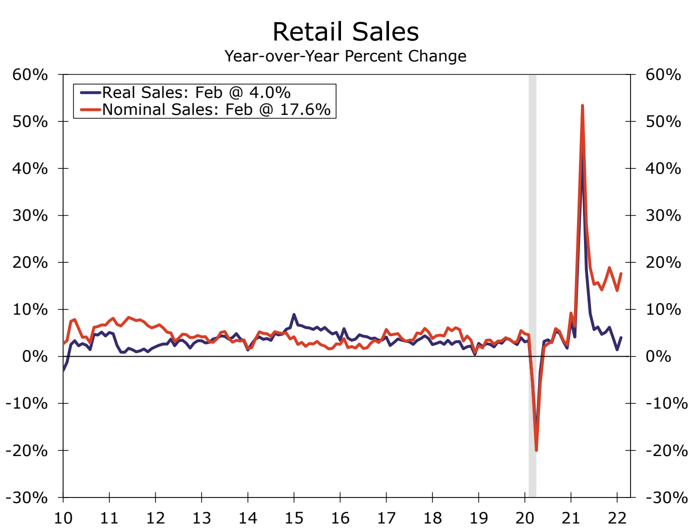
Price Fixing

To fix how much prices are driving retail sales growth, we've constructed a "real" retail sales measure. To do this we utilize Consumer Price Index data from the U.S. Department of Labor and match various sub-categories of consumer prices to the applicable retailer.[1]

The regularly reported nominal retail sales data versus our real retail sales proxy can be seen in the figures below. The immediate and unsurprising conclusion is that inflation has eaten up quite a bit of the reported gain in retail sales in recent months. The reported 0.3% gain in sales in February brought the year-ago pace of sales to 17.6%, but when adjusting for inflation that annual gain reflects a more modest 4.0% gain in sales (Figure 1).

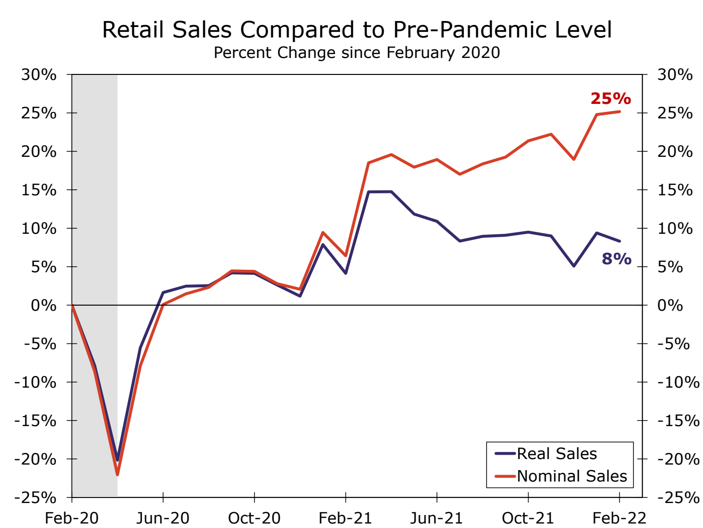
But even in real terms, we've still seen an impressive pace of retail spending. While it took just about two years to achieve the amount of growth in nominal retail sales that took nine years in the past cycle, in real terms the amount of growth achieved in a little over a year (~15%) still took eight years in the past cycle. At 8% above pre-recession levels as of February (Figure 2), real sales are currently running at a pace consistent with seven years into the past cycle.

Figure 1



Source: U.S. Department of Commerce, U.S. Department of Labor and Wells Fargo Economics

Figure 2



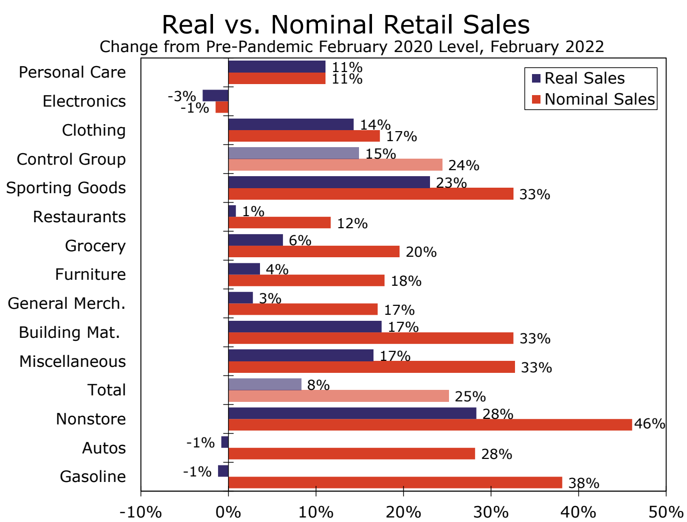
Source: U.S. Department of Commerce, U.S. Department of Labor and Wells Fargo Economics

Know Your Price

The idea of breaking out a "real" retail sales measure is not particularly novel, and while it helps put surging nominal figures in perspective, it is less helpful when price dynamics are particularly pronounced for a given store type. Yes, the rapid rise in goods prices over the past year has been interesting, but the story is so much more compelling when we break out the difference between nominal and real sales by retailer. This is where the real versus nominal divide is really striking.

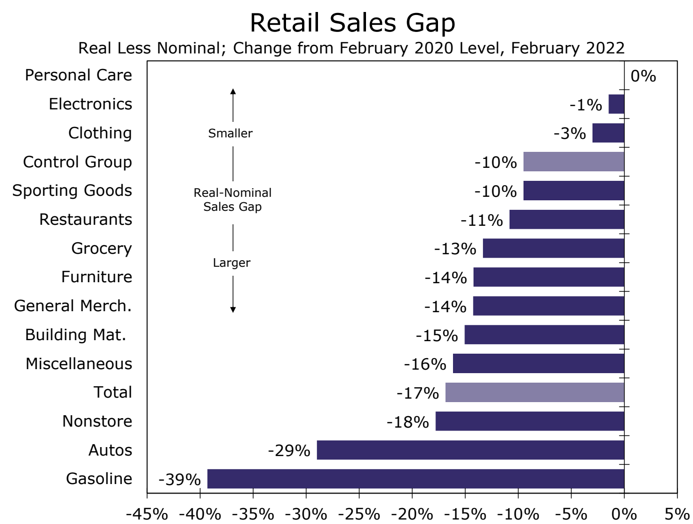
Most emblematic of this dynamic are auto sales, which are at the intersection of the surging demand and the lack of product due to supply chains. In the stories we tell about the pandemic era, the scarcity of autos and the lack of availability of rental cars will be part of the lore; it will also be used in Econ 101 to explain what happens to prices when demand is high and supply is low. On a nominal basis, auto sales are up 28% from where they were before the pandemic in February 2020 (Figure 3). But it is not as though dealers are actually moving more cars. Instead, what is driving the surge is the extinction of dealer incentives and price concessions. There is no need to offer rebates when buyers will pay over MSRP if they can just get the keys and get out of the dealership. Real auto sales are actually down nearly 1%. This is not even as bad factory level auto sales, which finished 2021 at 15 million and just over 14 million at an annualized pace in February. Both of those figures are a far cry from the 16 million or higher average sales pace in 2019 and the first two months of 2020.

Figure 3



Source: U.S. Department of Commerce, U.S. Department of Labor and Wells Fargo Economics

Figure 4



Source: U.S. Department of Commerce, U.S. Department of Labor and Wells Fargo Economics

While the gap between real and nominal auto sales takes the top spot among durable goods categories, the overall number one spot goes to the another prime example of high inflation: gasoline prices (Figure 4). The real change in spending on gas is near zero. We are not buying any more of it than we were two years ago, but the fact that the nominal figure is up 38% means that consumers either need to save less or cut back in other areas.

One area where consumers are not cutting back is online shopping. The 46% nominal increase in nonstore retailers (e-commerce) is enough to take first place with eight percentage points to spare. But e-commerce is not immune to inflation, as real gains here for the same period are up just 28%, making online shopping the number three spot in terms of the real versus nominal spending gap, right behind autos.

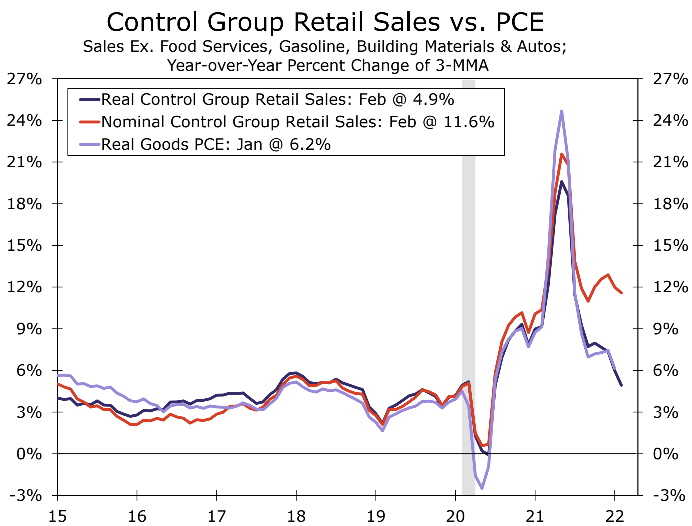
The last place most consumers want to have to cut spending is at the grocery store. While outlays there are slowing, we are still spending a lot more money at the supermarket than we were before the pandemic.The trouble is that our dollar doesn't stretch as far as it did two years ago. We are spending 20% more but only taking home 6% more groceries.

A small mercy in an otherwise relentless inflation environment is that amid a pandemic, spending on personal care (mostly pharmacies and drug stores) does not cost more than it did before the pandemic. This is the only category where real spending has kept pace with nominal outlays.

Back in Control

Finally, these real retail sales figures also give us a better read on real goods consumption for the quarter. Control group sales are typically a reliable indicator for consumer spending, but with increased volatility in prices today, the nominal estimates can be a bit misleading. For example, control group sales slipped 1.2% last month after surging 6.7% in January, but when adjusting for inflation, we estimate real control group sales declined a larger 2.1% in February after a still-strong, but more muted, gain of 5.8% in January. Figure 5 makes clear how our real control group sales measure more closely tracks real goods spending in GDP. The first two months of the quarter suggest real goods spending is tracking with our forecast for first quarter PCE to grow at a 2.5% annualized rate, though second quarter consumer spending could be even weaker than the 0.8% in our forecast if war-induced inflation worsens during that period.

Figure 5



Source: U.S. Department of Commerce, U.S. Department of Labor and Wells Fargo Economics

Endnotes

[1] We use our discretion to choose which pricing categories are applicable to each retailer. For example, we match appliances within the household furnishings & supplies pricing category with electronics & appliances retailers but readily acknowledge some of these purchases may take place at general merchandise retailers or at building material & garden retailers. For retailers that may sell a wide-array of products, such as general merchandise, miscellaneous store retailers and nonstore retailers, we use the broad pricing category of core goods less transportation as a proxy for prices. (Return)

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