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Weekly Commentary

MAY 22, 2023

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Have money, will spend

We focus on the core inflation indexes because they exclude elements such as food and gasoline, whose prices fluctuate too much in the short term. It's helpful to take the same approach to retail sales. While the headline number in the Commerce Department's April report released last week rose 0.4% month-over-month, stripping out auto and gasoline sales revealed a gain of 0.6%. Similarly, general merchandise store sales (companies like Sears or Kmart) grew 0.9%. A difference less than a percentage point might not seem like much, but it is for a monthly change. So, retail sales are much higher than it would seem. Housing sales have also risen despite still high mortgage rates.

How can this happen when everyone thinks the U.S. probably is heading into a recession? Most likely it is due to having a job. Americans have always tended to spend what they have (our collective savings rate is low), so the more money that comes in, the more that is spent. With the continued strength of the labor market, that might continue for some time.

This trend is great for consumers and businesses, but the Federal Reserve sees it as a major impediment in its drive to chase down still speeding inflation. That is why it is likely to keep the pedal to the metal for monetary policy tightening. It's possible the upcoming Federal Open Market Committee meeting in June will result in another hike of the target federal funds range. But even if it does not, expect Fed officials to hold rates at the current 5-5.25% range for most, if not all of 2023.

G40461-19 (5/23)