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STATE OF FREIGHT INSIGHTS

With Expert Commentary From

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Is consumption finally back to normal?

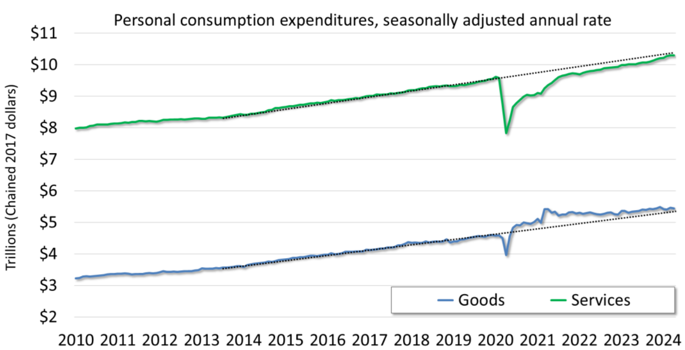
Consumer spending is sluggish, but it has held up despite hurdles.

Backed by a financial windfall and disruptions in spending opportunities during the pandemic, consumers fueled a surging freight market. Adjusted for inflation, spending has largely returned to trend for both goods and services.

Given the big swings in 2020 and 2021, the stability in consumer spending over the past couple of years is a bit surprising. We addressed consumer spending a year ago, and in broad strokes little has changed, at least when we look at spending without the distortion of inflation (labeled as “real spending”).

One apparent – but not yet certain – shift over the past year is that real spending on goods and real spending on services are moving toward their respective pre-pandemic trend lines. A year ago, it looked as if services spending might have reset slightly below the pre-pandemic trend while goods spending might have reset slightly above trend.

Real consumer spending



Source: Bureau of Economic Analysis, FTR

The moves back toward trend in goods and services spending are rather recent, so we are not quite ready to declare that the pandemic-era distortions in consumer spending are over. However, a reversion to trend does seem more logical than a permanent shift, even the relatively small one we had been seeing.

What we are not seeing – at least not yet – is a downturn in consumption. Nor have we forecast a drop in spending, in large part because payroll employment growth has remained solid. Still, the stability in consumption has been remarkable given the effects of inflation and high interest rates on consumers’ buying power.

That resilience is reassuring, but it also might indicate that consumer spending is still distorted by extraordinary conditions that eventually will no longer be around to prop up the consumer sector. Moreover, even if overall spending holds up, we might continue to see a diversion of spending from goods to services.

How durable goods spending is changing

As already noted, consumer spending in both goods and services recently has moved closer to their pre-pandemic trend lines after holding steady for two years. Again, these moves are both small and recent, but it is useful to see what is happening.

Spending on both durable and non-durable goods has flattened out a bit recently, so the pre-pandemic trend is catching up with actual spending.

In 2023, real spending on durable goods averaged a 0.7% m/m increase on a seasonally adjusted basis. Through April of this year, durable goods spending is averaging a decrease of 0.5% m/m, largely due to a 2.8% drop in January. The culprit that month was a plunge in spending on new motor vehicles. Durable goods spending recovered a bit in February from the January drop but since then has been sluggish.

Aside from motor vehicles, other broad categories have experienced softer spending. Real spending on recreational goods and vehicles – a larger category than motor vehicles and parts since the beginning of the post-lockdown recovery – was strong in 2023,

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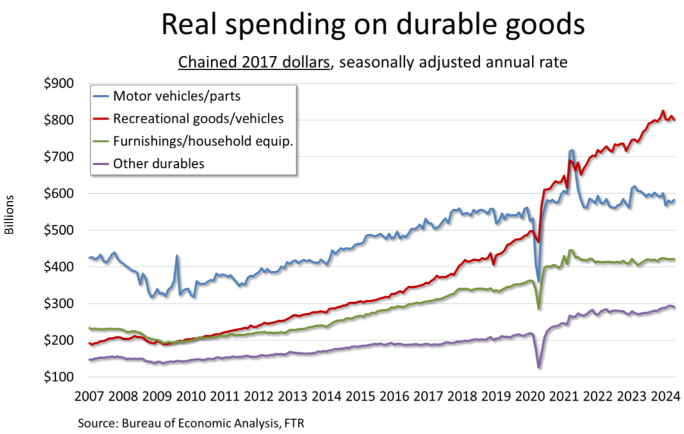

averaging 1.0% m/m growth. Through April, that spending is averaging a 0.8% decline in 2024. Recreational goods include consumer electronics, which has been the main driver of spending growth.

Furnishings and household equipment spending averaged 0.3% m/m growth in 2023. The 2024 average so far is a 0.1% decline.

How non-durable goods spending is changing

Real spending on non-durable goods averaged 0.2% m/m growth in 2023. Through the first four months of this year, spending has averaged a 0.1% decline m/m.

A big factor in the weaker results this year is gasoline and energy products. Spending in that category averaged 0.4% m/m growth in 2023 but is down 0.7% m/m on average so far in 2024.

Another broad category of non-durables that has softened recently is clothing and footwear, which averaged 0.2% monthly growth last year but is down 0.6% on average in 2024.

The broadest category of all – other non-durable goods – also is contributing to the softness. Real spending on other non-durables has been flat so far in 2024, down from 0.3% average growth last year.

The single largest group within "other" is pharmaceuticals, which is seeing weakness so far in 2024. Average monthly growth in 2023 was 0.5%. Real spending so far this year is nearly flat at down 0.1% on average each month.

A broad weakening in non-durables spending has one notable offset, though. Real spending on food and beverages purchased for off-premises consumption – i.e., at stores rather than restaurants – averaged 0.1% m/m growth in 2023 but is averaging 0.2% growth in 2024.

The difference between 2023 and 2024 growth might sound insignificant, but food and beverages represent by far the largest category of non-durables spending aside from "other" at more than double the spending on clothing and footwear.

A caveat is in order here. As discussed in the services spending section below, the uptick in spending on food and beverages for off-premises consumption does not necessarily mean that overall food consumption is growing.

The second largest category of food spending in dollar value is "food products not classified elsewhere." This category was flat on average in 2023 but is averaging 0.4% m/m growth in 2024.

Meats and poultry – the third largest food category in value – also has been a factor in increased spending on food and beverages for off-premises consumption this year. Overall real spending on meats and poultry has averaged 0.3% monthly growth this year, up from a 0.1% decline last year.

The weakness in 2023 was due to beef and veal, which averaged a drop of 0.7% m/m. Beef and veal spending has averaged a 0.2% monthly gain this year. Growth in real spending on pork and poultry also is stronger through the first four months of 2024 than in 2023.

One major category is adding to food spending growth but just barely. Real spending on cereals and bakery products – the fourth largest food category in dollar value – is averaging 0.1% growth this year after no growth on average during 2023.

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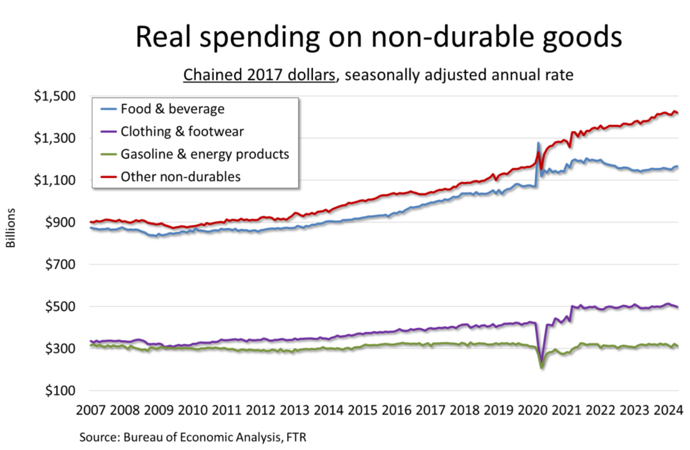

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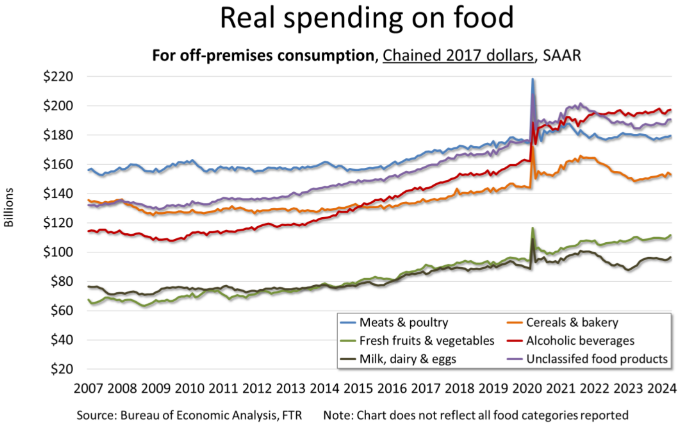


Smaller food categories in dollar value also are contributing to growth this year. Real spending on fresh fruits and vegetables is rising 0.4% monthly on average, up from 0.2% in 2023. Real spending on fish and seafood ticked up 0.1% monthly on average in 2023, but spending is averaging 0.7% growth in 2024 so far.

One exception to stronger growth is the milk, dairy, and eggs category. Real spending is up 0.3% monthly on average this year. Average growth in 2023 was 0.6% monthly, although that growth was strongly concentrated in the first half of the year.

Another large food and beverages category that has slowed so far in 2024 is alcoholic beverages. Monthly average growth last year was 0.2%. The average so far this year is -0.1%.

Given the unit costs involved, alcohol beverages now account for the single largest portion of the food and beverage category in dollar value, although that was not true before the pandemic. Real spending on meats and poultry consistently was greater than spending on alcoholic beverages for off-premises consumption prior to May 2020.

How spending on services is changing

We will focus less on details of services sector spending than on goods because the freight implications are mostly related to the direction of services spending rather than the details. There's one obvious exception that we will address below.

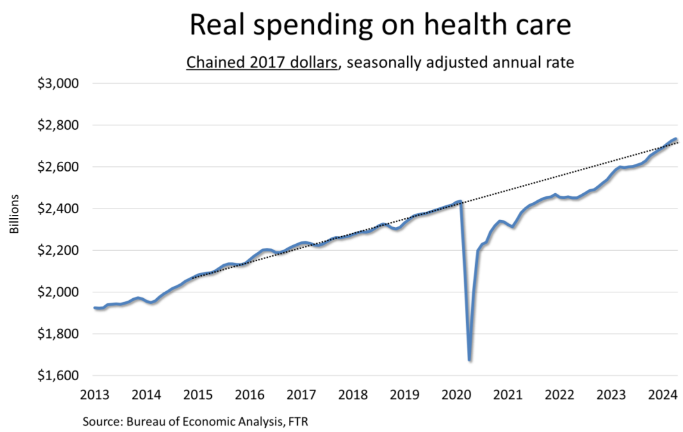
The move toward the pre-pandemic trend for real spending on services occurred mostly during the second half of last year with a big gain as well in February 2024, which saw the largest m/m increase since the beginning of last year.

A big drag on services spending has been recreation services, which were hit hard by the pandemic, of course. Real spending on recreation services did recover to its pre-pandemic level by the end of 2022, but it remains far below the spending trend in place before lockdowns.

On the other hand, some categories of services clearly benefitted from the pandemic disruptions, one of the biggest being communications. That category never really saw a decline and, instead, experienced strong growth for about two years before settling to a more normal pattern.

Categories related to travel, such as air transportation and foreign travel, took longer to recover but are now ahead of their pre-pandemic trend lines.

The recent strength in real spending on services has much to do with health care, which is the largest broad category of services expenditures. Health care spending has recovered in fits and starts since the plunge in April 2020. One growth period was from mid-2022 through early 2023, but then spending slowed for about six months.



Real spending on health care is now growing strongly again and quite recently exceeded its pre-pandemic trend slightly.

Another spending grouping that had been performing strongly until recently is food services, which is by far the largest portion of the broader category of food services and accommodations.

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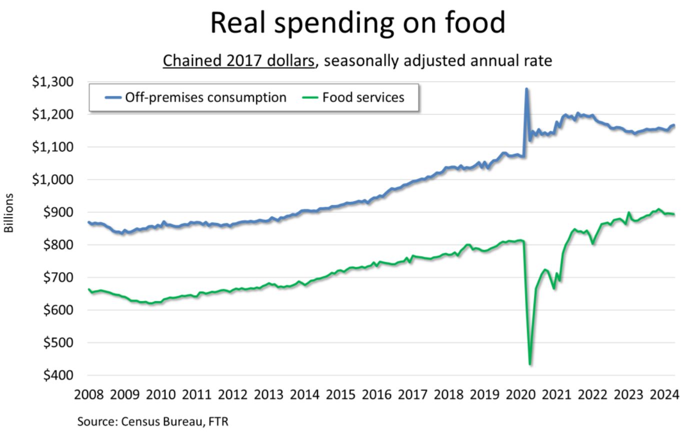

Real spending on food services had recovered to pre-pandemic levels by mid-2021 as limited-service facilities gained share, full-service restaurants pivoted to carry out and delivery, and third-party delivery services took off.

That spending basically offset food spending lost due to reduced business and personal travel. Food services spending continued to be volatile in conjunction with ongoing waves of COVID inflections that finally abated in early 2022.

Spending growth averaged 0.4% monthly in both 2022 and 2023, but the sector has been weak since December, declining in all but one month at an average of 0.3% monthly. However, it is important to recognize that the biggest hits in seasonally adjusted spending during this period occurred in December and January.

Food services is an important category because more so than any other service category it comes with an inherent goods component, namely food and beverages. Hence our admonition earlier that just because food and beverage spending for off-premises consumption is rising does not necessarily mean that overall real spending on food is rising.

A look back and ahead

The combination of lockdowns and stimulus resulted in a whipsaw for consumption as consumer spending dropped 2.5% in 2020 but spiked 8.4% in 2021. Not surprisingly, both moves were the largest ever in either direction.

Since 2022, however, consumer spending has moved roughly in line with what it was doing in the back half of the 2010s. Annual increases from 2016 through 2019 averaged 2.5%. Consumption rose 2.5% y/y in 2022 and 2.2% in 2023.

FTR is forecasting basically more of the same with a 2.5% increase this year and gains of 2.2% and 2.4% in 2025 and 2026, respectively.

With many services options shut down or sharply curtailed for much of 2020, the performance for goods spending did not experience the whiplash seen in overall spending, which is dominated by the services sector.

Spending on goods rose 4.9% y/y in 2020, which was on the high end of the normal range. Then, goods spending jumped 11.4% in 2021 and was essentially flat in 2022. Aside from 2022, the 2.1% increase in 2023 and forecasts of 1.8%, 2.1%, and 2.2% growth in 2024-2026 would be the weakest y/y gains in goods spending since 2011 and 2012.

Spending on non-durable goods always exceeds spending on durable goods, but that split has narrowed a bit over time.

In the 2000s, non-durables consistently accounted for more than 70% of spending on goods. By the late 2010s, non-durables represented slightly less than two-thirds of goods expenditures, and spending on durables has picked up a couple more share points since the beginning of the pandemic.

Except for 2022, which saw a dip in consumer durable goods spending, spending on durable goods has outpaced spending on non-durables every year since the end of the Great Recession. That delta was especially pronounced early in the pandemic as durable goods spending rose 8.0% in 2020 and

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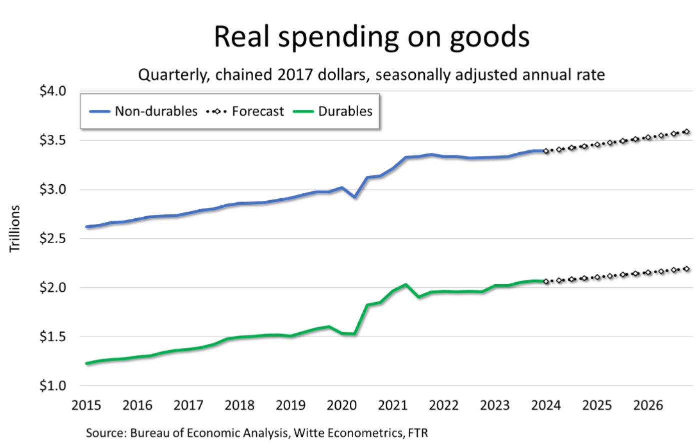

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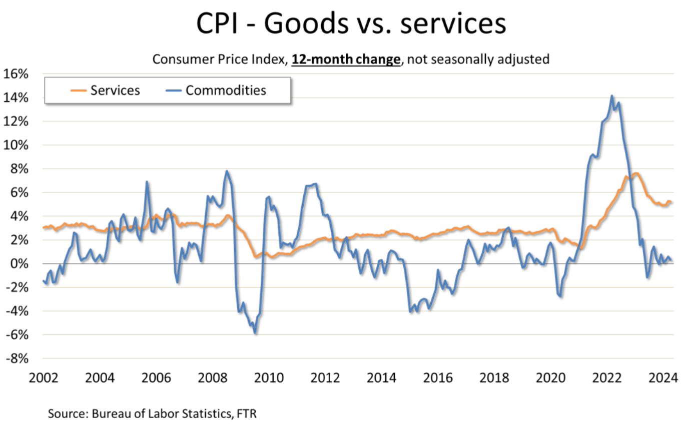
16.7% in 2021. Non-durables spending was up 3.3% in 2020 and 8.5% in 2021.

FTR's forecast for 2024 through 2026 is continued growth for both durables and non-durables. We are projecting both to be up 1.8% y/y this year. The durables forecast is +2.2% and +2.3% in 2025 and 2026 while the non-durables forecast is +2.0% and +2.1% during that period.

Risk factors

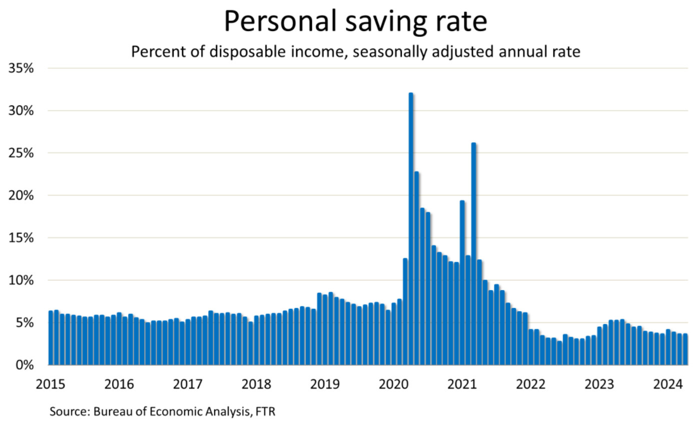
The growth rate in consumer spending was destined to subside over time once it recouped the losses during lockdown, but real spending has held up well considering inflation and the Federal Reserve's interest rate increases to combat it.

Overall inflation has diminished from 2021 and 2022 when it was soaring, but it is still running more than 3% y/y – significantly above the Fed's target rate of 2%. Moreover, while goods inflation has largely ended, inflation in the services sector not only is still elevated but the most recent data suggests that it will stay elevated for longer.



The Fed began raising the target funds rate in the middle of 2022 to combat inflation, ending the increases in August 2023 at 5.33%, which is where the funds rate stands today. With inflation sticky due especially to services, it is unclear when interest rate cuts will begin. The conventional wisdom is that we will see at least one cut before 2025, but that is far from certain.

The question everyone is asking is how long consumer spending can hold up in this climate. One warning sign is the personal saving rate. From 2015



through 2019, saving as a percentage of disposable income averaged 6.2%. Due to stimulus and severe limitations on spending for services, the saving rate skyrocketed early in the pandemic but was volatile because stimulus payments were doled out in three rounds over about a year while robust consumer spending during this period was constant.

The saving rate began to fall after the third round of stimulus in March 2021 and started running below pre-pandemic levels by the end of 2021. In real terms, consumers continued to spend nearly as much as they spent when they were receiving government support – even in the face of inflation and financing costs.

Since the beginning of 2022, the personal saving rate has averaged 3.9%, but that figure is bolstered by a slightly stronger saving rate during the first three quarters of 2023.

Based on preliminary data from the Bureau of Economic Analysis, the personal saving rate in March and April of this year was 3.6% – not quite as low as it was during most of 2022 but still sharply lower than what was the norm prior to the pandemic.

The saving rate does not consider what financial resources consumers might already have, however. It just considers *current* disposable income and how much of that income consumers set aside and don't spend. In the aggregate at least, consumers could still afford to spend a greater share of their income because they still had money left over from stimulus during 2020 and 2021.

According to an analysis of BEA data by staff at the San Francisco Federal Reserve, excess savings beyond what consumers would have saved based

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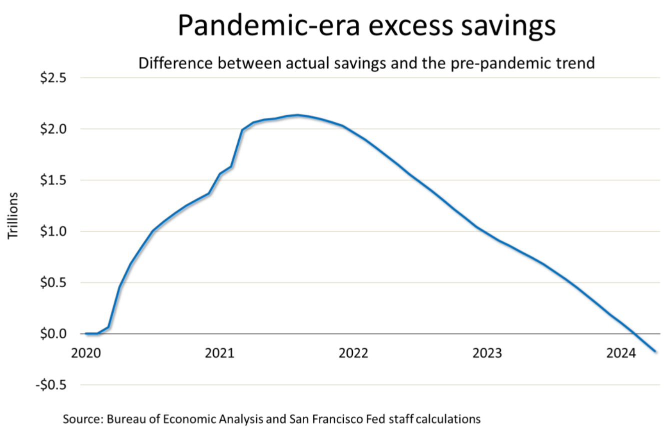


on pre-pandemic trends peaked at $2.1 trillion in August 2021. Since then, excess savings have fallen steadily. As of March 2024, consumers have fully exhausted excess savings during the pandemic and now are starting to tap into their “regular” savings, according to the analysis.

Again, it is important to recognize that this analysis is just looking at excess savings, meaning that consumers still have four years of “normal” savings on top of whatever savings they had going into the pandemic. In other words, in the aggregate at least, the situation is hardly dire.

Moreover, other data implies that consumers still have elevated resources even after prolonged spending during a time of inflation and relatively high interest rates.

For example, Federal Reserve estimates of currency and short-term deposits (including certificates of deposit) show that households throughout the wealth spectrum as of 2023Q4 still had substantially more cash available to them than they would have had absent the pandemic. Due to inflation and higher financing costs, that cash does not have the same buying power that it had before the pandemic, but the data implies that consumers still have runway to continue spending if they want.

So far we have considered only assets, but obviously the scope of debt obligations factors into future consumption. Here, the data is somewhat muddled.

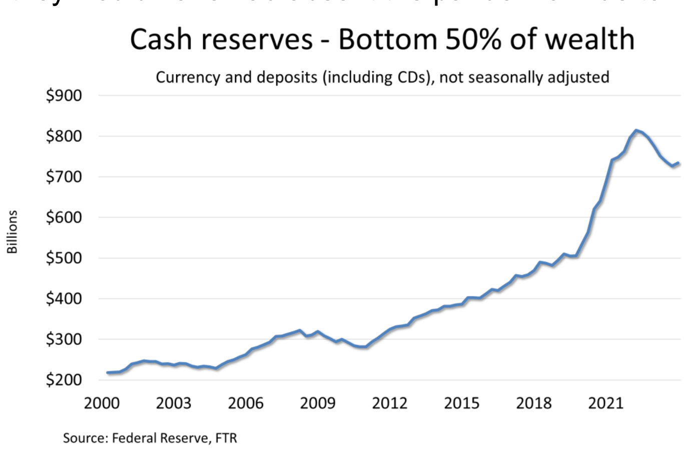
The New York Fed recently reported that total household debt in 2024Q1 was a record $17.7 trillion with high levels both in secured debt – mortgages, home equity loans, and auto loans – and in unsecured obligations, such as credit cards and student loans.

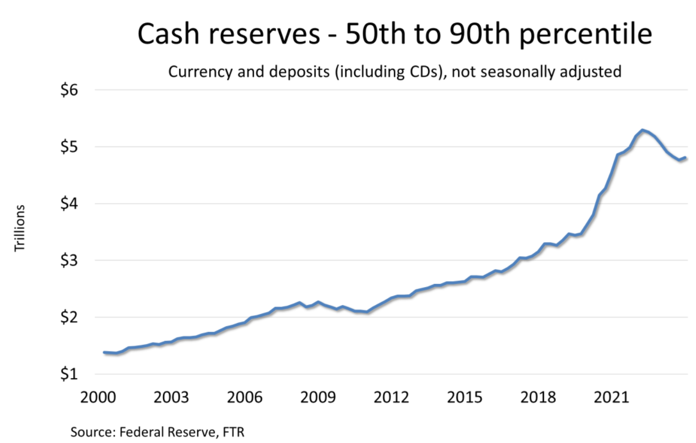
The level of debt certainly is a worry, but arguably more important for purposes of future spending levels is the ability of consumers to service that debt.

Federal Reserve data indicates that household debt service payments as a percentage of disposable personal income plunged during 2020 and 2022 as many Americans used their stimulus payments to pay down debt. The debt service percentage started rising in 2021Q2, but since the beginning of 2022 it has basically held at a level comparable to the level prior to the pandemic.

The Fed data currently is available only through the fourth quarter of 2023, but it is highly unlikely that the first quarter of this year produced a dramatic change in the situation.

Perhaps the greatest trend that offers confidence in continued spending is job growth. Payroll employment continues to rise at healthy levels, which should help offset any negative effects on spending that might result from depleted savings or higher debt levels.



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