ECONOMIC UPDATE

REGIONS

June 14, 2018

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May Retail Sales: Enjoy The Headline Number, Just Don't Get Too Attached To It

- Retail sales rose by 0.8 percent in May after rising by 0.4 percent in April (initially reported up 0.3 percent)
- Retail sales excluding autos rose by 0.9 percent after rising by 0.4 percent in April (initially reported up 0.3 percent)
- Control retail sales (sales excluding motor vehicles, gasoline, restaurants, and building materials) rose by 0.5 percent in May

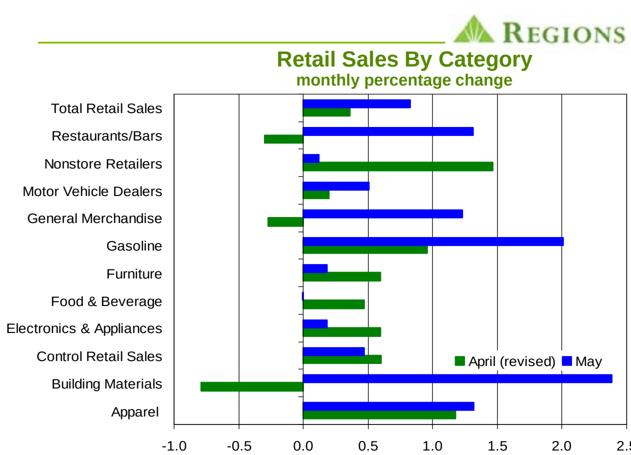
Total retail sales rose by 0.8 percent in May, easily besting the 0.4 percent increase we and the consensus expected. Ex-auto retail sales were up 0.9 percent and control retail sales, a direct input into the GDP data on consumer spending, rose by 0.5 percent, just ahead of the 0.4 percent our forecast anticipated. As our regular readers know, we put little stock into the initial estimate of retail sales in any given month, as those initial estimates are prone to significant revision. The initial estimate of May retail sales is no different, as several categories stand out as prime candidates for revision – mainly lower. To be sure, we have been and remain constructive on the state of U.S. consumers, and even ahead of today's release growth in Q2 consumer spending was tracking well ahead of the middling growth seen in Q1; we simply see the headline print on the May retail sales report as overstating the case.

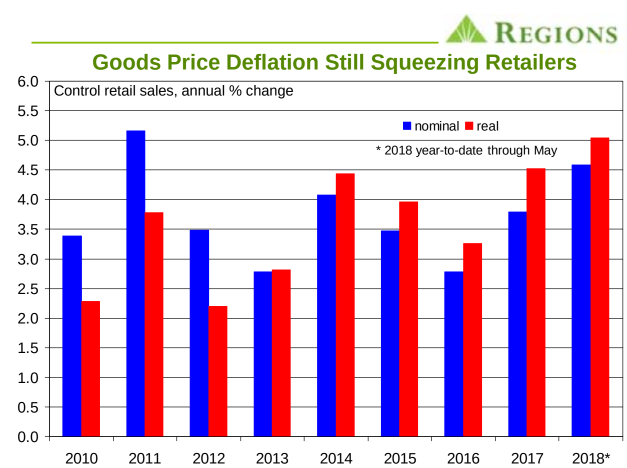
Retail sales in May were higher in 10 of the 13 broad categories for which data are reported. Sales at building materials stores jumped by 2.4 percent, the largest monthly increase since post-hurricane rebuilding and repair sparked a 2.9 percent increase last September. Gasoline station sales were up by 2.0 percent in May and are up 17.7 percent year-on-year, reflecting higher gasoline prices. Department store sales were up 1.5 percent, while apparel stores and restaurants each posted a 1.3 percent gains. Despite lower unit sales, revenue at motor vehicle dealers rose by 0.5 percent in May while sales at auto parts stores rose by 1.0 percent. On the flip side, furniture store sales are reported to have fallen by 2.4 percent in May (the largest decline since December 2013), but this follows the reported 2.7 percent increase in April though, quite frankly, neither of these numbers makes sense to us.

To our earlier point about the sizeable revisions to the initial estimates of retail sales in any given month, that 2.7 percent increase in sales at furniture stores in April was initially reported as a 0.7 percent decline, while what was originally reported as a 1.2 percent increase in sales at building materials stores is now shown to be a 0.8 percent decline. These are not the only such instances, nor is April the only month in which these patterns turn up in the retail sales data. And, while today's report incorporates an updated sample, new seasonal adjustment factors, and definitional changes in some of the component categories, Census released those revisions in late-May and we had the revised data when we prepared our forecast of May sales. So, in essence the estimates released today incorporate revisions to the revised data, and the numbers will look different upon the release of the estimates of June sales. The reported May increases in sales at apparel stores and restaurants stand out as suspect.

Again, though, this is not to cast aspersions on U.S. consumers, who we think are on increasingly solid footing given ongoing improvement in labor market conditions, the boost to disposable personal income due to the 2017 tax bill, and solid increases in household net worth, all of which are keeping consumer confidence elevated. Then again, consumer spending is leaving consumers feeling better than retailers. One trend we have been pointing to for quite some time, literally years now, is that falling prices for "core" consumer goods, i.e., excluding food and energy, have been putting a squeeze on retail profit margins. This is seen in our second chart below, which shows annual percentage changes in control sales on both a nominal and real (i.e., adjusted for price changes) basis. Goods prices are still struggling to gain traction, which is evident in the monthly CPI and PCE deflator data. But, given higher costs for inputs, labor, and shipping, the path of core goods prices in the months ahead bears watching, both in terms of the impact on consumer spending and the impact on inflation in the broader economy. Amazon or not, goods prices seem likely to head higher, even if only modestly, though we'll feel more confident in that call when (if?) goods prices actually stop falling.

In addition to goods prices, another factor that will help set the course of consumer spending over coming months will be rising interest rates. Still, unless and until the labor market begins to roll over, we will retain a constructive view on U.S. consumers.





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