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December Retail Sales: Pure Noise, No Signal

- › Retail sales fell by 1.9 percent in December after rising 0.2 percent in November (initially reported up 0.3 percent)
- › Retail sales excluding autos fell by 2.3 percent in December after rising 0.1 percent in November (initially reported up 0.3 percent)
- › Control retail sales (sales excluding motor vehicles, gasoline, restaurants, and building materials) fell by 3.0 percent in December

Total retail sales fell by 1.9 percent in December with ex-auto sales down 2.3 percent and control retail sales, a direct input into the GDP data on consumer spending on goods, fell by 3.0 percent. December retail sales fell well short of expectations, with the consensus forecast calling for both total and control retail sales to be unchanged from November. Our forecast had total retail sales down by 1.4 percent, ex-auto sales down by 1.8 percent, and control retail sales down by 2.3 percent. We'll offer two alternative explanations for the December retail sales data. One is that elevated inflation, the spread of the Omicron variant, and the end of financial support in the form of transfer payments have robbed consumers of their spending power, particularly when it comes to discretionary spending. The other explanation is that global supply chain and logistics bottlenecks incited consumers to get an earlier start to their holiday season spending and those who did not do so were increasingly less likely, the longer they did wait, to find the goods they wished to purchase. This will have held down spending in December, thus running afoul of what in any December are punishing seasonal adjustment factors, thus making the seasonally adjusted data look much worse than was actually the case. Our long-time readers, or even those who just happened upon this week's *Economic Preview*, know which explanation we'll go with.

To that point, on a not seasonally adjusted basis, total retail sales rose by 10.0 percent in December (our forecast had unadjusted sales up by 11.2 percent) while control retail sales rose by 14.7 percent – these are the month/month changes, not the over-the-year changes. While those are big numbers, they are not as big as the typical December increases; over the 2000-2020 period, the average December increase in total retail sales was 14.7 percent and the average December increase in control retail sales was 22.9 percent. With the December seasonal factors geared for larger increases than those we actually got, the result is that the seasonally adjusted data look much worse than was actually the case. It is hard to understand how anyone who has been paying attention over the past several months could have been taken by surprise by a weaker than normal December for retail sales. This is yet another instance of a point

we frequently make, which is that you cannot begin to understand what the data are really saying by going solely on the seasonally adjusted data without first examining the not seasonally adjusted data.

Sure, it is fair to ask why retail sales in both November and December fell short of the typical performances for those months. To start, keep in mind that going into the holiday season, consumer spending on goods was over already 25 percent higher than the pre-pandemic peak. Next, we'll point to supply-side constraints that worsened as 2021 wore on. Recall that October retail sales were stronger than normal for the month – not seasonally adjusted control retail sales rose by 5.6 percent, larger than the typical October increase. That in part reflected consumers getting a jump on holiday shopping, but to the extent consumers did so, that set the stage for smaller increases in November and December than are common for those months. Also, to the extent that limited supplies led people to give gift cards rather than actual gifts this holiday season, that will also have held down measured retail sales, as gift card purchases are not booked as retail sales until the cards are redeemed. To be sure, we are by no means dismissing the effects of inflation, particularly food, energy, and shelter prices, on discretionary consumer spending, particularly for lower-income households. That, however, cannot explain the December retail sales report. Also, recall that retail sales are reported in nominal terms, i.e., the data are not adjusted for price changes, which helps account for some portion of the 2021 increases in retail sales.

It's hardly worth bothering going through line by line December results given the extent to which the data are plagued with seasonal adjustment noise. To illustrate our point, however, consider sales by nonstore retailers, roughly 90 percent of which consist of online sales. The not seasonally adjusted data show increases of 18.1 percent in November and 11.4 percent in December, while the seasonally adjusted data show declines of 1.5 percent and 8.7 percent, respectively. Ask yourself which set of numbers makes sense. While not dismissing the effects of inflation and the Omicron variant, consumers are on firmer footing than implied by the seasonally adjusted December retail sales figures.

