US: Spending hits the skids

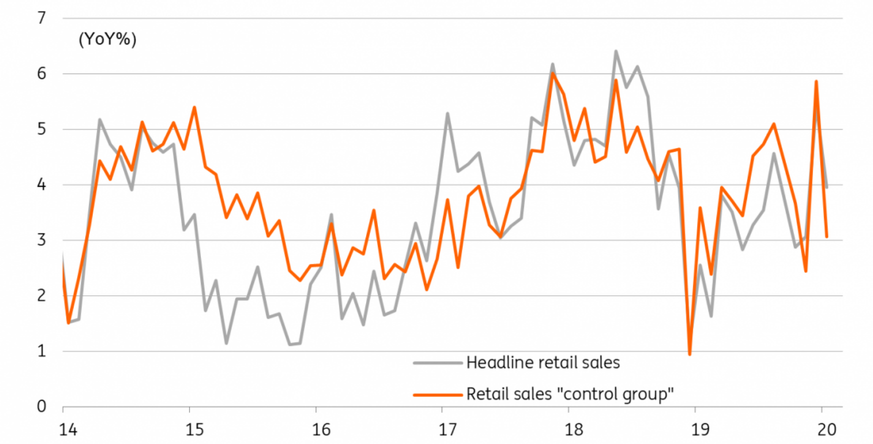
A disappointing US retail spending story for January given strong consumer fundamentals - and this is before any potential coronavirus fears hit

Headline retail sales grew 0.3% month-on-month in January, in line with expectations, but when we look at the "control" group, which excludes volatile items such as cars, gasoline and building materials (and has a better relationship with broader consumer spending) we see it was flat on the month versus expectations of a 0.3% MoM gain. Meanwhile, December's initially reported 0.5% MoM control group growth figure was revised down to just 0.2% for this key consumer spending measure.

In theory, retail sales should be supported by the fact consumer confidence is so strong. Record low unemployment and new highs for equity and real estate prices mean households have a sense of security and think their personal situation is on the up. However wage growth remains disappointing, which is perhaps limiting the scope for upside surprises in retail sales growth - barring any potential run down in household savings.

The details show building materials (+2.1%MoM) was the main growth contributor, which ties in with the improving housing market, but elsewhere the numbers were poor. Clothing fell 3.1%, health fell 0.4% and electronics fell 0.5%. There were some signs of life in furniture sales (again linked to the housing market, possibly) and miscellaneous stores. Nonetheless, given the recent weakness in the core "control" group, it doesn't suggest consumer spending will be a major driver of first quarter US GDP growth.

US retail sales



Source: Macrobond

Over the next month or so, sharp falls in gasoline prices will weaken the contribution from gas station sales, but it will free up cash to spend on other items. Looking a little further ahead, the chief concern is whether coronavirus fears become more apparent within the US. So far the number of cases are tiny and the biggest disruption is to manufacturing supply chains, but the longer it remains in the headlines, the greater the chance it starts to impact consumer behaviour.

Consumer spending accounts for nearly 70% of US GDP on an expenditure basis, which is greater than other developed markets so a shock here would have major ramifications for growth. Spending on services would be most vulnerable given it involves more human contact. Hotels & restaurants (7% of US consumer spending), transport services (3% of spending) and recreational services (4% of spending) are vulnerable, while spending by tourists would also be hit by falling visitor numbers. Internet retailers would likely receive a boost to sales from this environment.

Given the highly uncertain outlook, we continue to feel it prudent to err on the side of caution and stick with our sub-consensus US GDP growth view of 1.5% for 2020 with a further Federal Reserve rate cut and US 10Y Treasuries anchored in a 1.5-1.75% range through the first half of 2020.

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