US: Subdued start to 2025

Cold weather and the Los Angeles fires certainly played a role in the poor start to the year for consumer spending and manufacturing, but it may be that confusion over tariff timing is also having an impact

US retail sales dropped more than expected in January

-0.9 % MoM drop in US retail sales in January

Worse than expected

Retail sales dragged down by weather and LA fires

We thought a soft January retail sales report was likely given the cold weather and the Los Angeles fires, but it is worse than even our pessimistic forecasts. Headline sales were down 0.9% month-on-month in nominal terms (consensus -0.2%) while the control group that excludes the volatile autos, food service, building materials and gasoline and supposedly better tracks broader consumer trends fell 0.8% (consensus +0.3%). As these are nominal value changes and we know prices rose 0.5% MoM according to the CPI report, this implies very weak volume sales growth. It is the volume measure that feeds through into GDP growth. There were some slight upward revisions to the history, but even so the market is going to be disappointed with 10Y yields down 6bp on the back of this.

Auto sales fell 2.8% MoM, largely because of a big unit volume drop, which we already knew about, while furniture dropped 1.7%, electronics fell 0.7%, health spending fell 0.3%, clothing down 1.2%, sporting goods dropped 4.6% and internet sales fell 1.9%. Surprisingly, eating and drinking out actually rose 0.9% – we had expected this to drop because of very cold weather and there was a sense that the Los Angeles fires would also have a depressing effect, but somehow this was one of the very few sources of strength.

Could tariff worries also have played a role?

In trying to rationalise this outcome, we know that consumer confidence did fall quite a lot in January, largely on a sense that prices were going to rise on tariffs (big rise in price expectations and the responses showing it was going to be a worse buying environment for big ticket items – which are often imported). My sense has been that we could see consumer durable purchases actually be very strong in the early part of the year as people buy their foreign made fridge freezers and washer/dryers etc ahead of tariff-related price hikes, but maybe people are getting confused on the tariff story. Perhaps they think tariffs are happening immediately and are therefore not even considering a purchase. Alternatively, many housheolds may feel under pressure – the Philly Fed reported a record 11% of credit card holdings are only making the minimum monthly repayment and the NY Fed reported a pick-up in credit card delinquencies in the fourth quarter of 2024 – with the threat of tariffs pushing up their food and energy bills some households may be considering cutbacks on other items ahead of time.

We will need to wait until the February data to see if this is the start of a more cautious consumer trend or indeed whether it was simply a weather-related pull back and we get a subsequent big gain.

Manufacturing output held back by the weather while utilities demand surged

Rounding out the week's US numbers, industrial production rose 0.5% MoM, above the 0.3% consensus prediction, but manufacturing output fell 0.1% rather than rise 0.1% as the market predicted. As with the retail sales report, weather-related factors probably weighed on the manufacturing sector and mining, which fell 1.2%, while the cold weather prompted a jump of 7.2% MoM in utility output as we tried to keep warm. Overall though today's US retail sales and manufacturing numbers suggests a very subdued start to 2025.

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