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US Economics | North America

US Retail Sales Tracker: A Mild February

We forecast headline retail sales rose by 0.3% m/m in February and control-group sales rose 0.1%. Our forecasts are consistent with real consumption slowing to 1.1% growth (a.r.) in 1Q—slow but exaggerated by wintertime seasonal factors. Smoothing through 4Q and 1Q, spending still looks solid.

MORGAN STANLEY & CO. LLC

Michael T Gapen
Chief US Economist
Michael.Gapen@morganstanley.com +1 212 761-0571

Sam D Coffin
Economist
Sam.Coffin@morganstanley.com +1 212 761-4630

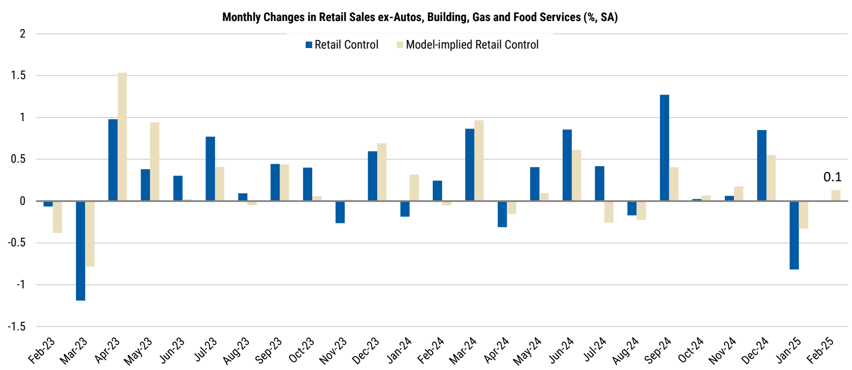
Arunima Sinha
Global Economist
Arunima.Sinha@morganstanley.com +1 212 761-4125

Heather Berger
Economist
Heather.Berger@morganstanley.com +1 212 761-2296

Diego Anzoategui
Economist
Diego.Anzoategui@morganstanley.com +1 212 761-8573

Lenoy Dujon
US/Canada Economist
Lenoy.Dujon@morganstanley.com +1 212 761-2779

Exhibit 1: Monthly changes in Retail Control sales



Source: Census Bureau, Morgan Stanley Research

Retail sales remain moderate

We forecast retail control (total-ex autos, buildings, gas and restaurants) rose 0.1% m/m and headline rose 0.3% m/m. Among the inputs to our retail control forecast, wage income remains solid. We think seasonal factors exaggerated weakness in January, as we describe in the next section, but seasonals should not factor this month. Most pockets of credit card spending data weakened in February.

We expect restaurant spending fell in February after a strong January and booming 4Q. Weaker transaction data and worse sentiment lead to our forecast of -0.2% m/m. For building materials, transaction data weakened in February. However, the correlation with spending has not been strong, and we expect warmer weather and the need to rebuild after fires/hurricanes raise sales somewhat. We expect +0.3% m/m after four consecutive negative prints.

Data in line with our forecast would bring our tracking for 1Q real consumer spending growth to 1.1% versus our current expectation of 1.2%. Some of the slowing from 4Q reflects changed spending patterns and seasonal distortion post-pandemic (more below). Averaging through 4Q and 1Q suggests a healthy 2 ¾% spending pace. 1Q growth is also held back by about 0.3 pct pt (a.r.) by residual seasonality in prices. We expect GDP and consumer spending growth to slow over the course of the year because of changes in fiscal, tariff, regulatory, and immigration policies, but that's not the source of the slowdown we see in 1Q.

So far, labor market income has remained solid and supportive of consumption. While consumer sentiment showed some weakness, it does not have clear read through for overall spending after other economic variables are accounted for. There has been significant market volatility, but we think that the changes in household wealth would need to be considered more "permanent" to have any perceptible implications for consumer spending. For now, slower immigration and firmer inflation because of tariffs lead to our expectations for consumer spending growth to slow this year compared to last.

Exhibit 2: Retail Sales Dashboard

	Jul	Aug	Sept	Oct	Nov	Dec	Jan	Feb	
								MS	Consensus
Retail & food services	1.2	-0.1	0.9	0.6	0.7	0.7	-0.9	0.3	0.8
ex autos	0.5	-0.1	1.0	0.2	0.1	0.7	-0.4	0.1	0.4
Control-group	0.4	-0.2	1.3	0.0	0.1	0.8	-0.8	0.1	0.5
Autos	4.4	-0.3	0.6	2.2	3.1	0.9	-2.8	1.5	
Gasoline	0.5	-0.9	-1.4	0.2	0.2	2.1	0.9	0.3	
Building Materials	0.9	0.3	1.1	-0.3	-0.7	-1.6	-1.3	0.3	
Restaurants	0.6	0.6	0.8	0.9	0.5	0.1	0.9	-0.2	

Source: Census Bureau, Morgan Stanley Research forecasts

"Control" Retail Sales & GDP Tracking

Control-group retail sales, which is retail sales excluding food services, autos, gas, and building materials, includes all of the retail sales components that feed through into the spending estimates for goods consumption in GDP. Also, food services affects our services consumption tracking. Revisions to retail sales data also feed through into our current-quarter tracking of consumption.

Seasonal factors mean high noise, low signal

The signal from retail sales continues to be muted by post-Covid seasonal factors. We should largely ignore misses in both directions in assessing the retail sales and real consumer spending data. Even with the month-to-month decline in retail sales, January real spending on goods was little changed on a 12-month basis from H2 2024, emphasizing continued momentum. It rose 3.1% y/y in January, about in-line with 3.3% in 4Q and 2.7% in 3Q. The month-to-month retail print looked weak only because seasonal factors had distorted the month-to-month signal for January. We do not expect seasonal distortion for February.

Household spending follows repeated patterns: ramping up a bit in summertime, slowing somewhat in the fall, increasing sharply from Thanksgiving to Christmas; falling sharply at the turn of the year and through the rest of the winter. It's not just the time of year that can have repeated effects: moving holidays like Easter or Thanksgiving, or something as simple as the number of weekend days in a month can also have an effect.

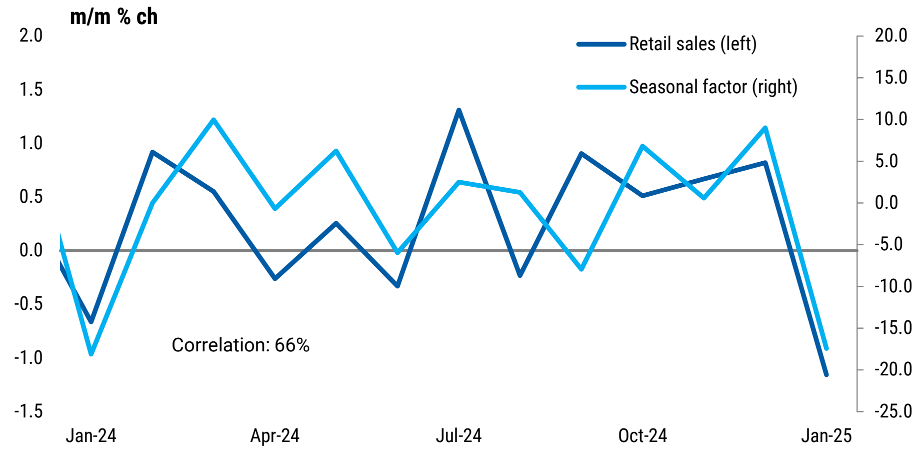
The repeated swings can make raw retail sales data hard to read. This year, unadjusted retail spending rose 7% in October, 1% in November, and 9% in December before falling 18% in January. Last year, it rose 3% in October, 2% in November, and 8% in December before a 17% decline in January. There are obvious seasonal influences, but interpreting the unadjusted data is nevertheless difficult.

Seasonal factors adjust for repeated deviations from trend. When the adjustments work well, the seasonally adjusted data give a better sense of both the trend in spending and in nearer-term accelerations or decelerations. However, they don't always work well.

Over the past year, seasonal factors were underadjusting for seasonality. Months where seasonal factors expected increases in NSA retail sales tended to be months in which retail sales were strong even after seasonal adjustment; and months where the seasonal factors allowed for decreases in NSA spending tended to be soft, even after seasonal adjustment. Exhibit 3 below shows the pattern.

In the last thirteen months, there was a correlation of 66% between the monthly percent change in the seasonal factor and the monthly percent change in the seasonally adjusted data. The SA data showed the same seasonal pattern the adjustment factors were trying to adjust for, suggesting that the seasonal factors were underadjusting for seasonality. There hadn't been high correlations in the past: over the past two years, there was correlation of -27%, and over a longer period, no correlation at all.

Exhibit 3: Seasonal factors have been under-adjusting for seasonality over the past year: Even after seasonal adjustment, retail sales have tended to accelerate in seasonally strong months and to decelerate in seasonally weak months.

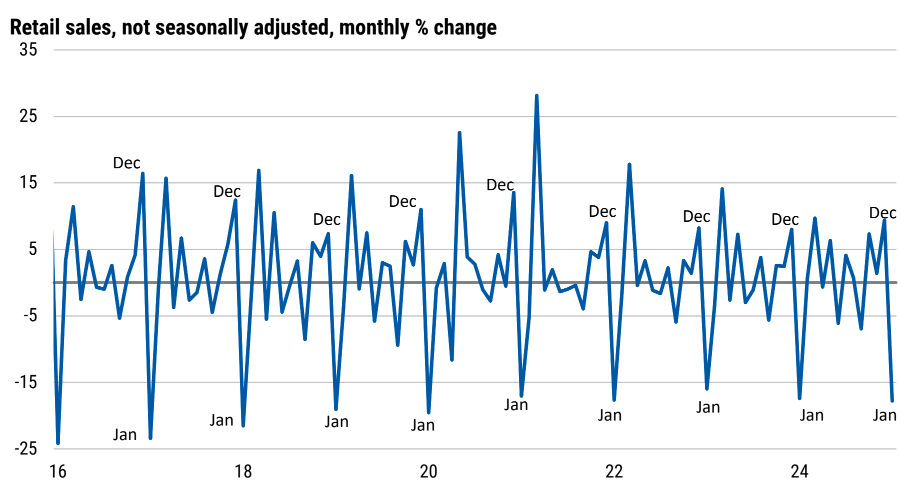


Source: Census Bureaau, Morgan Stanley Research

This year's January seasonal factor exacerbated that problem. It allowed for less decline in NSA sales this January than last January. The prior year's seasonal factor expected 20% decline, while this year's seasonal built in just a 17% decline.

Estimation of seasonal factors is still being disturbed by the pandemic. Spending patterns changed particularly sharply during the pandemic, because of changed preferences, work closures, transfer payments, and wealth. In the five years before the pandemic, spending in the first nine months of the year ranged from 73.1% to 73.5% of full-year spending—a fairly steady share. But in 2020, the first nine months' share was 72.3%—about a point below where it had been running; and in 2022 and 2023, it was 73.9% and 73.7%—about a half point above. In turn, the swing from elevated 4Q holiday spending to more basic spending in January has varied in size in recent years. The common pattern of January declines is less repeated than it had been, adding noise to the estimations of seasonality.

Exhibit 4: Holiday swings in NSA retail spending



Source: Census Bureau, Morgan Stanley Research

Effects on real goods consumption

With the changed patterns in spending (and in prices), the swings in real goods consumption from 4Q to 1Q have been large. Real goods consumption swung from +3% at an annual rate in 4Q2020 to +18% in 1Q21. Stronger spending in 4Q 2021 (5%) was followed by a weaker looking 1Q 2022 (-1.7%) Similarly, decent holiday spending in 4Q 2023 (3.4%) was followed by a -1.2% decline in 1Q 2024. We expect a similar pattern this year: 6.6% in 4Q, and slowing to a 1.2% pace in 1Q. The strength and then slowdown also distorts measures of auto sales, where increased inventory now again allows faster end of year sales; and prices, where the upward bias to 1Q prices puts downward bias on real growth.

To get a better sense of the trend in spending, smooth through these exaggerated monthly and quarterly growth rates.

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