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Questionable Seasonal Adjustments and Omicron Surge Weigh on December Spending

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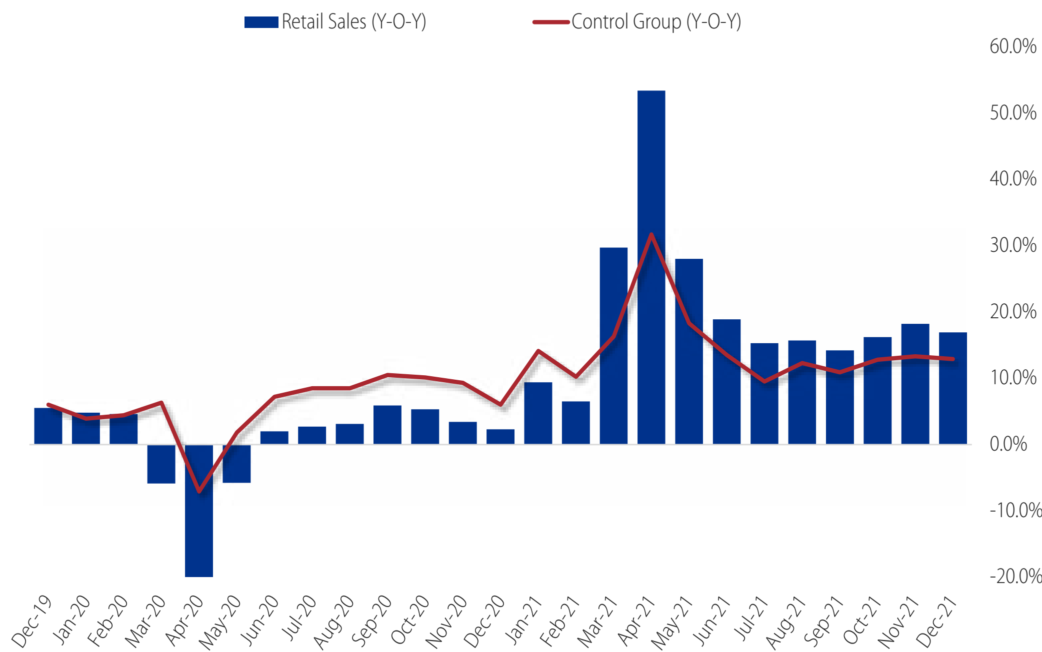
December retail sales fell well short of forecasts as the rapid spread of the Omicron variant and misplaced seasonal adjustment factors conspired to create a distorted picture of consumer health.

Headline sales fell -1.9%, a huge miss from the -0.1% median forecast. Ten of 13 spending categories were down in December with non-store (e-commerce) sales falling by -8.7%, vehicles and vehicle parts -0.4%, furniture sales -5.5%, and food and beverage sales -0.5%. Overall retail sales were still up +16.9% year-over-year despite the December shortfall.

Retail Sales (Year-over-Year Percent Change)



Source: U.S. Census Bureau

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The retail sales "control group," which excludes sales at food services, auto dealers, gas stations and building materials stores, and is used in the GDP calculation, fell -3.1% in December. The median control group forecast was for an unchanged reading. The November control group number was revised downward from -0.1% to -0.5%.

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Retail sales measure total store receipts, *and are not adjusted for inflation*. Sales would have appeared even weaker with if inflated goods prices hadn't contributed mightily to total receipts. On the flip side, seasonal adjustments, intended to smooth out sales in what is normally a huge month for holiday spending, further distorted the picture as 2021 shopping patterns were far from normal this year. The overall season was solid, with total retail sales up +8.7% for the quarter on an annualized basis, but

a much higher portion of spending occurred earlier than normal. Economists are now scrambling to adjust their fourth quarter GDP projections sharply downward. According to Bloomberg Economics, this mornings' sales numbers are more consistent with +3.0% GDP growth in Q4 21 than the +6.0% calculation made before the release.

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Fed officials could ultimately alter their policy plan, but for now, a quarter point rate hike is still queued-up for March, despite signs that growth slowed late in the quarter and will start the new year at a slower pace. As of this morning, the bond market has priced-in three rate increases over the next 11 months. Market participants have been assured of a more aggressive Fed, not by the economic data, but by an increasing number of Fed officials pledging to address persistently high inflation. Elevated year-over-year price pressure is expected to continue until late spring/ early summer. Until then, FOMC members will take a strong public stand to assure investors they're taking inflation seriously. They can pivot later if necessary.

The financial market reaction is not quite what you'd expect given the apparent weakness of the data release. Whereas signs of economic weakness would typically push market yields lower, this morning's numbers have had the opposite effect as yields are higher in early trading.

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Market Indications as of 9:53 A.M. Central Time

DOW	Down -288 to 35,825 (HIGH: 36,800)
NASDAQ	Down -36 to 14,771 (HIGH: 16,057)
S&P 500	Down -21 to 4,638 (HIGH: 4,797)
1-Yr T-bill	current yield 0.47%; opening yield 0.43%
2-Yr T-note	current yield 0.94%; opening yield 0.91%
3-Yr T-note	current yield 1.23%; opening yield 1.21%
5-Yr T-note	current yield 1.52%; opening yield 1.49%
10-Yr T-note	current yield 1.75%; opening yield 1.72%
30-Yr T-bond	current yield 2.09%; opening yield 2.05%

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