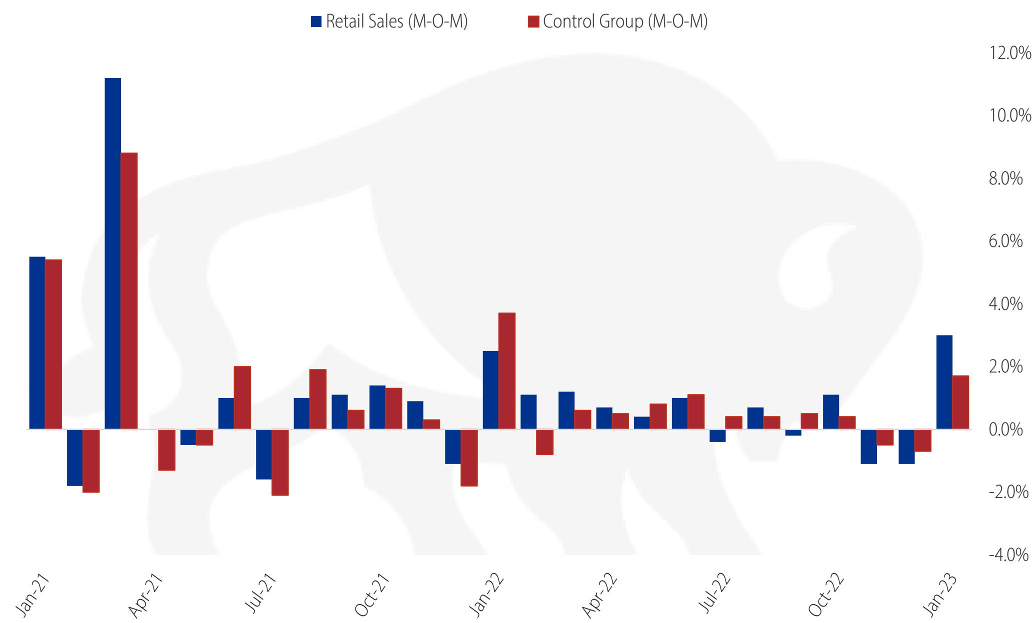
Warm Weather Boosts January Spending

Scott McIntyre, CFA
HilltopSecurities Asset Management
Senior Portfolio Manager
Managing Director
512.481.2009
scott.mcintyre@hilltopsecurities.com

Greg Warner, CTP
HilltopSecurities Asset Management
Senior Portfolio Manager
Managing Director
512.481.2012
greg.warner@hilltopsecurities.com

After two months of soft headlines, U.S. retail sales were generally expected to rebound in January. As it turned out, (seasonally-adjusted) consumer spending rose *at the strongest pace in nearly two years*. Total sales unexpectedly jumped +3.0% last month, well above the +2.0% forecast and an abrupt turn following declines of -1.1% in both November and December.

Retail Sales (Month-over-Month Percent Change)



Source: US Census Bureau

Restaurant and bar sales surged +7.2%, also a two-year high, while vehicles sales rose +5.9%. These were easily the biggest contributors last month.

Last month's increase was widespread, with all 13 categories advancing. On a year-over-year basis, retail sales were up +6.7% in January after increasing at a +5.1% annual pace in December.

Restaurant and bar sales surged +7.2%, also a two-year high, while vehicles sales rose +5.9%. These were easily the biggest contributors last month. By contrast, vehicle sales were down -1.8% in December, while sales at eating and drinking establishment were *flat*.

The retail sales "control group," which excludes sales at auto dealers, gas stations, building materials stores and food service establishments, rose +1.7%, reversing the -0.7% December decline with *the highest monthly gain in 12 months*. Since the control group data is used to calculate GDP, the notion of near-term recession suddenly seems far-fetched. *The first quarter is off to a surprisingly strong start.*

Since the control group data is used to calculate GDP, the notion of near-term recession suddenly seems far-fetched.

The counter-argument to today's unexpectedly strong report is *historically warm January weather throughout the nation*, which has likely boosted spending at dining and drinking establishments. At the same time, a rise in vehicle inventories provided buying opportunities that haven't existed for many months. And finally, retail sales represent total dollar spending, and are not adjusted for inflation. When prices are high, total receipts naturally rise. That being said, consumer spending capacity was clearly intact last month. The savings rate may be down and borrowing may be up, but none of this has discouraged Americans from spending. Not yet.

The savings rate may be down and borrowing may be up, but none of this has discouraged Americans from spending. Not yet.

Yesterday, several Fed officials responded to yesterday's unexpected CPI surge with appropriately hawkish comments. Richmond Fed President Thomas Barkin told Bloomberg TV that the FOMC would be forced to raise rates further if inflation persists at levels well above target, while Philly Fed President Patrick Harker believes policy-makers will have to raise rates above 5% and possibly higher. *Today's retail sales data will add to that chatter.*

Market Indications as of 9:03 A.M. Central Time

DOW	Down -181 to 33,908 (HIGH: 36,800)
NASDAQ	Down -58 to 11,902 (HIGH: 16,057)
S&P 500	Down -15 to 4,121 (HIGH: 4,797)
1-Yr T-bill	current yield 4.97%; opening yield 4.91%
2-Yr T-note	current yield 4.61%; opening yield 4.62%
3-Yr T-note	current yield 4.27%; opening yield 4.20%
5-Yr T-note	current yield 3.32%; opening yield 3.32%
10-Yr T-note	current yield 3.77%; opening yield 3.74%
30-Yr T-bond	current yield 3.81%; opening yield 3.77%