Daiwa Capital Markets

U.S. Data Review

- Retail sales: broad-based advance
- CPI: jumps in some volatile areas
- Industrial production: constrained by utility output; mining & manufacturing firm

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Retail Sales

The volatile components of retail sales (autos and gasoline) behaved about as expected (autos down 1.4 percent and gasoline up 2.3 percent), but other areas were stronger than generally expected, which left a surprisingly firm retail sales report. The headline increase of 0.4 percent exceeded the expected advance of 0.1 percent, while the increase of 0.7 percent ex-autos and ex-gasoline was even more impressive. Upward revisions in the prior two months added to the positive tone of the report (headline adjusted by 0.3 percent; ex-autos, ex-gasoline by 0.1 percent).

Retail Sales -- Monthly Percent Change

	Sep-16	Oct-16	Nov-16	Dec-16	Jan-17
Total	1.0	0.7	0.2	1.0	0.4
Ex.-Autos	0.8	0.6	0.3	0.4	0.8
Ex.-Autos, Ex.-Gas	0.5	0.4	0.3	0.1	0.7
Retail Control*	0.4	0.4	0.2	0.1	0.6
Autos	1.9	0.8	-0.3	3.2	-1.4
Gasoline	3.6	2.7	0.0	3.2	2.3
Clothing	0.2	-0.1	0.2	0.1	1.0
General Merchandise	-0.4	0.4	0.4	-0.4	0.9
Nonstore**	0.6	1.7	0.3	1.9	0.0
Discretionary***	0.2	0.0	0.4	-0.6	1.1

** Retail sales excluding sales from motor vehicle dealers, gasoline stations, and building materials, garden equipment, and supply dealers.*

*** Primarily online and catalog sales; also includes sales by fuel-oil dealers.*

**** Discretionary items include sales from the following types of stores: furniture and home furnishing; electronics and appliance; clothing and accessory; sporting goods, hobby, book, and music; general merchandise; and food services and drinking places. These stores deal primarily with items whose purchase could be postponed.*

Source: U.S. Census Bureau; Daiwa Capital Markets America

Several areas posted strong results. A jump of 1.0 percent at clothing stores added noticeably to the upward drift evident in prior months, and the increase of 1.4 percent at restaurants and bars more than offset a drop in December and resumed an upward trend. Activity at building supply stores continued to advance. Several areas that had been soft in recent months showed much better results in January, although the advances represented only partial offsets to earlier declines (electronics, sporting goods, general merchandise).

Nonstore retailers (primarily online and catalogue, but fuel oil dealers also are in this category) showed no change in January, but results in December were quite strong and thus the flat reading did little damage to a strong upward trend.

Two special groupings in the retail sales report are worth monitoring carefully. The so-called retail control -- a grouping that correlates well with portions of spending as measured by the GDP accounts -- rose 0.6 percent in January, a good start to the first quarter. Sales at stores that deal primarily with discretionary items jumped 1.1 percent. The increase followed a drop in the prior month, but the latest result was still encouraging in that it lifted the moderate underlying trend.

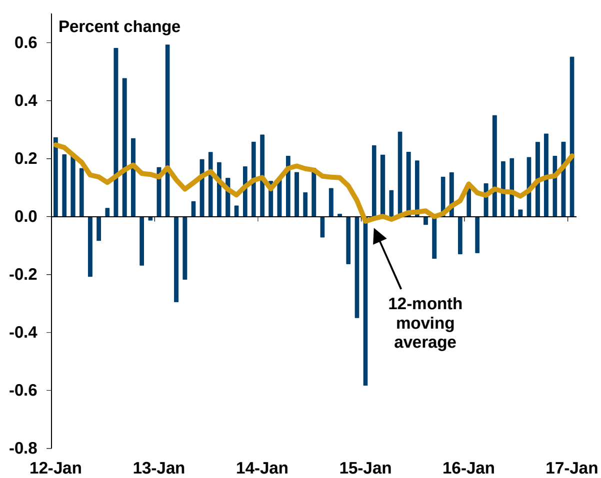
Consumer Price Index

The jump of 0.6 percent in the CPI exceeded the expected increase of 0.3 percent by a wide margin. Most of the surprise occurred in the energy category, where the increase of 4.0 percent easily exceeded our expectation of 1.5 percent. However, the core component also rose more than expected (0.3 percent versus the consensus expectation of 0.2 percent). The food component was tame (0.1 percent) but the increase represented a shift from the downward drift that has been in place since mid-2015.

The increase in the core component can perhaps be downplayed because some of the pressure occurred in volatile areas. For example, airfares rose 2.0 percent, most likely driven by recent increases in fuel prices. Apparel prices rose 1.4 percent, but the increase followed declines in several prior months, and sharp increases are common in this area and discounting often follows. Prices of new cars and trucks jumped 0.9 percent, but the increase drove the index well above the flat, tight trend and appeared to be an aberration.

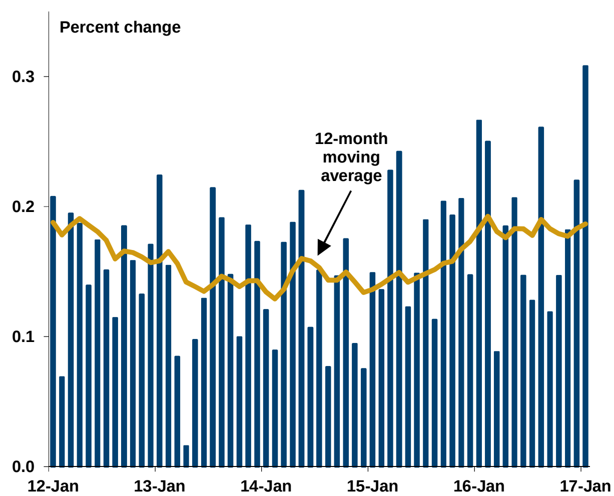
The latest changes pushed the year-over-year increase in the headline index to 2.5 percent. The annual change has now quickened for six consecutive months, with the pace moving to its highest rate since March 2012 (chart, left). The year-over-year change in the core component moved to 2.3 percent. The latest reading on annual core inflation was still within the recent range, albeit in the upper end of that range and the recent range is higher than that from 2013 through most of 2015 (chart, right).

Headline CPI



Source: Bureau of Labor Statistics

Core CPI



Source: Bureau of Labor Statistics

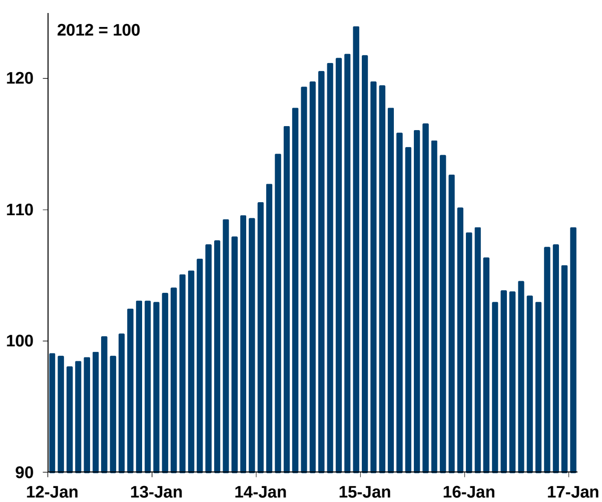
Industrial Production

The headline figure for industrial production was much softer than expected (off 0.3 percent versus a consensus expectation of no change), but the surprise occurred in the utility sector, where the drop of 5.7 percent was a reflection of warmer-than-normal temperatures rather than economic fundamentals. The other two components performed well, with mining advancing 2.8 percent and manufacturing increasing 0.2 percent.

The increase in mining activity represented the third increase in the past four months. The changes have been modest relative to the contraction in 2015 and early 2016, but nevertheless they suggest that this previously soft area has turned a corner (chart, left).

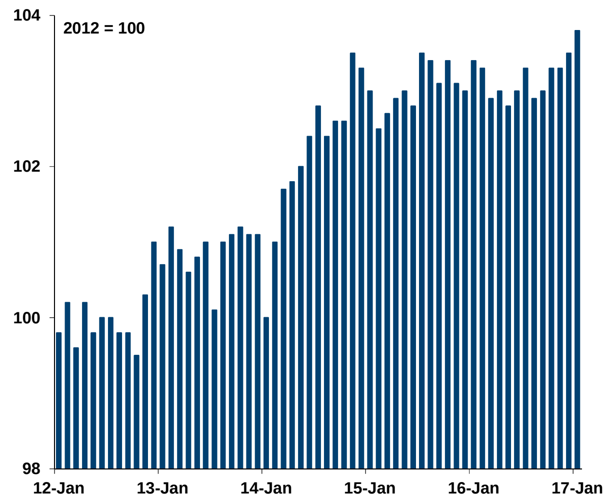
The increase in manufacturing activity represented the fourth increase in the past five months, leaving an upward tilt to what had been a flat trend (chart, right). The latest increase occurred despite a drop in the auto sector; output excluding motor vehicles and parts rose 0.5 percent, a firm performance. The increase was broadly based, with 12 of 20 industry categories showing increases and one showing steady activity.

Industrial Production -- Mining



Source: Federal Reserve Board

Industrial Production -- Manufacturing



Source: Federal Reserve Board