

John Williams'
Shadow Government Statistics
Analysis Behind and Beyond Government Economic Reporting

COMMENTARY NUMBER 423
February Retail Sales

March 13, 2012

Rising Prices Largely Accounted for February Retail Sales Gain

PLEASE NOTE: The next regular Commentary is scheduled for Friday, March 16th, covering February CPI, PPI, real retail sales and industrial production.

Best wishes to all — John Williams

Opening Comments and Executive Summary. Inflation increasingly is the issue. Looking at February data, where the headline retail sales number put in its strongest monthly showing in six months, headline consumer inflation likely showed its strongest monthly gain in at least 11 months. Higher prices accounted for much of the February sales gain. Whatever gain was left over for the series—net of inflation—was accounted for by unseasonably mild winter weather in much of the country, in the context of ongoing concurrent seasonal factor distortions and normal monthly reporting volatility.

Along with labor data, trade balance, industrial production and housing construction, real (inflation-adjusted) retail sales—as a measure of the physical demand for consumer goods and services—is one of the key monthly economic releases. Accordingly, today's *Commentary* is relatively brief, just outlining the nominal (not-adjusted-for-inflation) retail sales detail. A more comprehensive discussion on the latest inflation and economic information will follow in Friday's (March 16th) *Commentary*, which will cover February inflation (CPI and PPI) and key economic (industrial production and real retail sales) reporting.

Hyperinflation Watch. Irrespective of any intervening economic, inflation and financial-market developments, the broad economic, inflation and hyperinflation outlooks discussed in [Hyperinflation 2012](#) of January 25th are not changed.

REPORTING DETAIL

RETAIL SALES (February 2012)

February Retail Sales Gain Was Statistically Meaningful but Largely Reflected Rising Prices. On top of the oil-induced inflation that was triggered in late-2010 as a result of the Fed's QE2 dollar-debasement policy, mounting political tensions in the Middle East recently have added fresh upside pressure to oil and gasoline prices. That more than accounted for the 3.3% monthly increase in gasoline station sales in February's retail sales reporting. With overall consumer inflation in February likely accounting for more than half of the 1.1% headline monthly sales, the residual reported sales would not be statistically significant.

Reporting quality of the series also continued to suffer from the concurrent seasonal-factor issues and broader distortions seen otherwise in seasonal-adjustment factors and sampling methodologies, as discussed in [Hyperinflation 2012](#). The stability of the seasonal-adjustment process and sampling methods have been disrupted severely by the unprecedented depth and length of the current economic downturn in the post-World War II era (the period of modern economic reporting). More-common seasonal-adjustment issues also have surfaced in the current reporting, with likely positive contributions to adjusted sales activity from unseasonably mild weather. That factor should swing into a net-negative contributor status by April reporting.

Under such circumstances, where the markets effectively are flying blind as to actual economic activity, consideration of broad underlying fundamentals is essential. Consumer income and credit remain structurally impaired (see [Commentary No. 422](#)) and continue to signal economic deterioration, not recovery, with the broad economy in serious trouble.

Nominal (Not-Adjusted-for-Inflation) Retail Sales. Today's (March 13th) report on February 2012 retail sales—issued by the Census Bureau—indicated a statistically-significant, seasonally-adjusted monthly gain of 1.06% (up by 1.60% before prior-period revisions) +/- 0.6% (95% confidence interval). February's increase followed a revised January gain of 0.62% (previously 0.38%). The numbers are heavily modeled and include generally overly optimistic underlying assumptions at this stage of reporting.

New and used automobile sales were guesstimated to have risen by 1.9% (1.2% net of prior-period revisions) for the month of February, against a revised 2.1% (previously 1.3%) decline in the month of January. Despite already existing and better quality industry reporting, the Census Bureau is unable to estimate new car sales in its “advance” report.

Showing somewhat stronger year-to-year growth in the context of prior-period revisions, February 2012 retail sales were reported up by 6.48% +/- 0.8% (95% confidence interval), where year-to-year January 2012 retail sales were up by a revised 6.26% (previously 5.84%).

The annual benchmark revisions to retail sales will be published on April 30th. As most commonly happens, the revamped data likely will show downside revisions to retail sales in recent years, as overly-optimistic underlying assumptions get replaced by actual data.

Real (Inflation-Adjusted) Retail Sales. Details on real retail sales for February 2012 will be published in the Friday, March 16th, *Commentary*, along with details from the February 2012 CPI-U release. Where February CPI-U inflation likely will be strongly positive (see *Week Ahead*), official February CPI-U inflation has the potential again to offset fully the nominal (not adjusted for inflation) sales gain.

Core Retail Sales. In February 2012 retail sales reporting, both gasoline stations and groceries stores showed increases in monthly sales. Assuming that the bulk of non-seasonal variability in food and gasoline sales is in pricing, instead of demand, “core” retail sales—consistent with the Federal Reserve’s preference for ignoring food and energy prices when “core” inflation is lower than full inflation—are estimated using two approaches:

Version I: February 2012 versus January 2012 seasonally-adjusted retail sales series—net of total grocery store and gasoline station revenues—up by 0.86%, versus an official gain of 1.06%.

Version II: February 2012 versus January 2012 seasonally-adjusted retail sales series—net of the monthly change in revenues for grocery stores and gas stations—was up by 0.67% versus an official gain of 1.06%.

Week Ahead. Recognition of an intensifying double-dip recession as well as an escalating inflation problem remains sporadic. The political system would like to see the issues disappear until after the election; the media does its best to avoid publicizing unhappy economic news; and the financial markets will do their best to avoid recognition of the problems for as long as possible, problems that have horrendous implications for the markets and for systemic stability.

Until such time as financial-market expectations move to catch up fully with underlying reality, or underlying reality catches up with the markets, reporting generally will continue to show higher-than-expected inflation and weaker-than-expected economic results in the months and year ahead. Increasingly, previously unreported economic weakness should show up in prior-period revisions.

Producer Price Index—PPI (February 2012). The February PPI is due for release on Thursday, March 15th. With higher monthly-average oil prices in place and historically minimal distortion from oil-price seasonal adjustments in February; with catch-up from January’s seasonally-adjusted understatement of

PPI inflation; and with spreading inflation outside the energy area; monthly inflation in this regularly-volatile series should be on the upside of market expectations.

Consumer Price Index—CPI (February 2012). Due for release on Friday, March 16th, the February 2012 CPI-U has a fair shot of an upside surprise to the consensus estimate (0.5% per MarketWatch.com). Gasoline prices rose 5.8% month-to-month in February 2012, versus January, per the Department of Energy, and seasonal-adjustments to gasoline prices should provide a boost to the reported inflation. In February 2011, a 2.2% increase in monthly gasoline prices was inflated to 4.7%, after seasonal adjustments. Those adjustments, however, will reverse direction in March reporting. Inflationary pressures also likely continued to spread outside the energy area.

Year-to-year total CPI-U inflation would increase or decrease in February 2012 reporting, dependent on the seasonally-adjusted monthly change, versus the 0.44% gain in the adjusted monthly level reported for February 2011. I use the adjusted change here, since that is how consensus expectations are expressed. To approximate the annual unadjusted inflation rate for February 2012, the difference in February's headline monthly change (or forecast of same) versus the year-ago monthly change should be added to or subtracted directly from January 2012's reported annual inflation rate of 2.93%. A consensus 0.5% monthly gain would leave annual CPI-U inflation for February at about 3.0%.

The real (inflation-adjusted) numbers on February 2012 retail sales activity will be published along with the March 16th release of the February CPI-U.

Industrial Production (February 2012). Due for release on Friday, March 16th, industrial production reporting easily could be surprised on the downside of expectations, net of revisions. With production being cut back in an effort to balance excess inventories, production could show an actual monthly contraction, net of prior-period revisions.
