U.S. Retail Sales Unchanged; Consumers Showing Resilience

By Lucia Mutikani

WASHINGTON (Reuters) - U.S. retail sales were unexpectedly flat in September as households cut back on purchases of motor vehicles and other big-ticket items like electronics and appliances amid stubbornly high inflation and rapidly rising interest rates.

But consumers are not rolling over yet, with the report from the Commerce Department on Friday also showing a measure of underlying retail sales rising last month, thanks to strong wage gains and savings. These so-called core retail sales were also stronger than initially thought in August.

"Consumer staying power may be waning, but it's showing few signs of breaking," said Tim Quinlan, a senior economist at Wells Fargo in Charlotte, North Carolina. "Overall spending will continue to moderate as inflation persists and tighter monetary policy begins to weigh more meaningfully on consumption."

The unchanged reading in retail sales last month followed an upwardly revised 0.4% rise in August. Sales in August were previously reported to have gained 0.3%. Retail sales increased 8.2% on a year-on-year basis in September. Economists polled by Reuters had forecast sales would climb 0.2%, with estimates ranging from as low as a 1.1% decline to as high as a 0.8% increase.

Retail sales are mostly goods and are not adjusted for inflation. Soaring costs for rents and healthcare are squeezing budgets for many Americans, leading them to reduce spending on goods. The situation has been compounded by higher borrowing costs, which are making credit more expensive.

Economists saw no impact on monetary policy from the mixed retail sales report.

A survey from the University of Michigan on Friday showed consumer sentiment improved further in October, but inflation expectations deteriorated a bit as average national gasoline prices moved back up towards $4 per gallon after falling over the summer.

"The (retail sales) data don't show the kind of overheating that would necessitate more aggressive rate hikes, nor the kind of rapidly deteriorating consumer spending that would encourage a pause," said Will Compernolle, a senior economist at FHN Financial in New York.

The Federal Reserve has raised its policy rate from the near-zero level in March to the current range of 3.00% to 3.25% as it battles inflation. A fourth straight 75-basis-point interest rate hike is expected next month after data on Thursday showed inflation increasing strongly in September.

Retail sales also are slowing as spending shifts back to services. Sales at auto dealerships slipped 0.4% last month, while receipts at service stations dropped 1.4%.

Furniture store sales fell 0.7%, while those at building material and garden equipment retailers decreased 0.4%.

Receipts at electronics and appliance stores declined 0.8%. There were also decreases in sales at hobby, musical instrument and book stores, a sign that consumers were pulling back on discretionary spending.

But sales at clothing and general merchandise stores rose as did those of online and mail-order retailers. Receipts at bars and restaurants, the only services category in the retail sales report, increased 0.5%.

"While consumers remain willing to spend, many families, especially those at the lower-to-median end of the income spectrum, are feeling increasingly constrained by elevated prices and rising interest rates," said Gregory Daco, chief economist at EY-Parthenon in New York.

Stocks on Wall Street were trading lower as the earning season started with a drop in profits for big banks. The dollar rose against a basket of currencies. U.S. Treasury prices fell.

UNDERLYING STRENGTH

According to the National Retail Federation, consumers are spending on household priorities. The NRF says removing tariffs on Chinese goods and enacting immigration reforms to address worker shortages could compliment the Fed's efforts to tame inflation.

"As we enter the holiday season, shoppers are increasingly seeking deals and discounts to make their dollars stretch, and retailers are already meeting this demand," NRF President Matthew Shay said. "However, the Biden administration must enact policy measures to relieve inflationary pressure and lower costs for American families."

Excluding automobiles, gasoline, building materials and food services, retail sales increased 0.4% last month. Data for August was revised higher to show these core retail sales rising 0.2% instead of being unchanged as previously reported.

Core retail sales correspond most closely with the consumer spending component of gross domestic product. The increase in September and upward revision to August data left economists expecting that growth in consumer spending likely topped a 1.0% annualized rate in the third quarter after increasing at a 2.0% pace in the April-June quarter.

GDP is expected to have rebounded last quarter after two straight quarterly declines, as slowing domestic demand curbs imports and leaves a stockpile of unsold merchandise in warehouses. A third report from the Commerce Department showed business inventories increased 0.8% in August.

Third-quarter GDP growth estimates are as high as a 2.9% rate. The economy contracted at a 0.6%

pace in the second quarter. The government is scheduled to publish its snapshot of third-quarter GDP at the end of this month.

There were, however, some glimmers of hope in the fight against inflation. A report from the Labor Department on Friday showed import prices dropped for a third straight month in September, pulled down by falling costs for petroleum products and a strong dollar, suggesting that imported inflation pressures were subsiding as global supply chains improve.

Import prices decreased 1.2% last month after declining 1.1% in August. In the 12 months through September, import prices increased 6.0%, the smallest rise since February 2021, after advancing 7.8% in August.

"These recent declines likely reflect effects of declines in commodity prices and dollar appreciation, and suggest some easing pressure on domestic inflation, primarily on the goods side," said Daniel Silver, an economist at JPMorgan in New York.