ECONOMIC UPDATE
REGIONS
March 17, 2020

February Retail Sales/February Industrial Production

- Total retail sales fell by 0.5 percent in February, with ex-auto sales down by 0.4 percent, while control retail sales were unchanged
- Total industrial production rose by 0.6 percent in February, with manufacturing output up by 0.1 percent

Retail Sales: Total retail sales were down by 0.5 percent in February, with ex-auto sales down by 0.4 percent while control retail sales were unchanged. Our below-consensus forecast anticipated that both total and ex-auto retail sales would be down by 0.1 percent with control sales up by 0.4 percent. It should be noted, however, that there were strong upward revisions to the initial estimate of January retail sales and, even with the soft February print, consumer spending on goods was running ahead of the pace seen in Q4 2019. We don't see much, if any, evidence that concerns over the coronavirus played a hand in the February retail sales data, though that will clearly change with the March data.

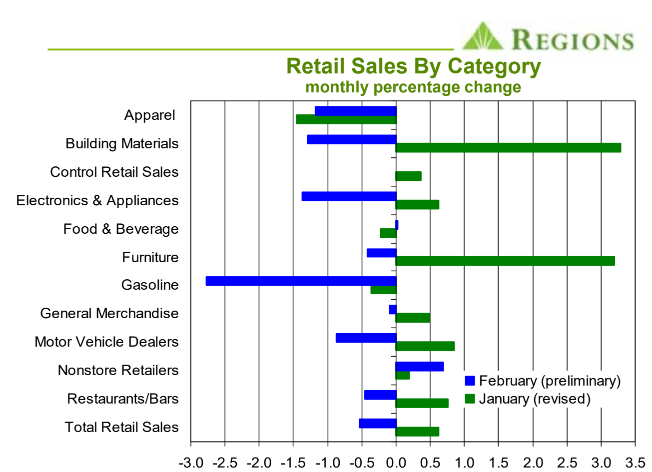
Our forecast anticipated gasoline and building materials would be sizable drags on headline retail sales, with restaurants and motor vehicles also being drags, though to a lesser degree. This proved the case, with gasoline station sales down by 2.8 percent due to sharply lower prices (the retail sales data are not adjusted for price changes), sales at building materials stores down by 1.3 percent, sales by motor vehicle dealers down by 0.9 percent, and restaurant sales down by 0.5 percent. But, as sales in these categories are excluded from the control group, we anticipated a better outcome there. Instead, control sales were weak almost across the board, with sales declining at apparel stores, furniture stores, electronics and appliance stores, and general merchandise stores. While the temptation may be to attribute these declines to increasingly anxious consumers, we think it more a case of the usual noise in the retail sales data, data not exactly known for their reliability. Each of these categories saw large upward revisions to the initial estimate for January, thus setting a higher bar for February comparisons. As we anticipated, sales by nonstore retailers rose smartly in February, though there were downward revisions to prior estimates for January and December. We continue to argue that online sales remain badly underestimated in the retail sales data.

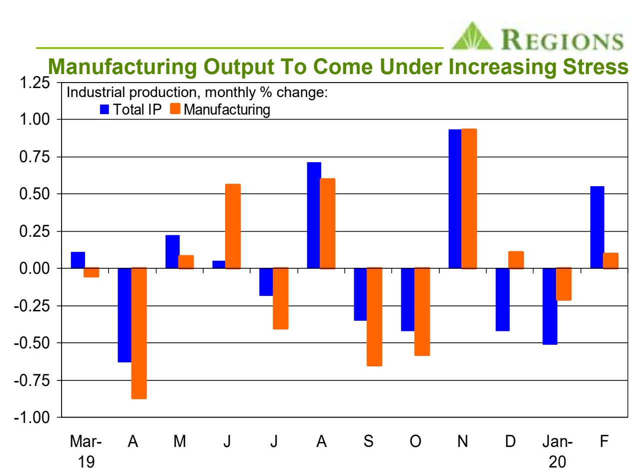
With fading consumer confidence, sharp declines in equity prices, increased social distancing, and uncertainty about jobs and incomes, the March retail sales data will be rocked by the fallout from the coronavirus. That is not, however, the explanation for the soft February data.

Industrial Production: Total output amongst the nation's factories, mines, and utilities rose by 0.6 percent in February, besting the 0.4 percent we and the consensus expected. Manufacturing output was up by just 0.1 percent, but only due to a jump in motor vehicle production, as output excluding motor vehicles and parts fell by 0.2 percent. Mining output was down by 1.5 percent while utilities output spiked by 7.1 percent, a much larger increase than our forecast anticipated. The overall capacity utilization rate rose to 77.0 percent in February, with the utilization rate in the manufacturing sector holding steady at 75.0 percent. On an over-the-year basis, total industrial production was flat while manufacturing output was down 0.4 percent in February.

Assemblies of autos and light trucks (which includes SUVs) rose to an annualized rate of 10.997 million units in February, a 5.6 percent increase from January. Assemblies of heavy trucks were basically flat. Going forward, one concern is that shortages of parts will lead to disruptions in motor vehicle production. Production of aerospace equipment fell further in February, following up on the steep decline seen in January, with these declines reflecting Boeing winding down production of the 737 Max. Computer & electronic equipment and electrical equipment remained pockets of strength in manufacturing output in February. Mining output fell sharply in February, and given the recent sharp declines in energy prices, further declines are likely in the months ahead for as long as global demand remains weakened.

Even prior to it beginning to spread within the U.S., the coronavirus was disrupting activity in the manufacturing sector. With global supply chains being impaired by widespread factory shutdowns across Asia, U.S. manufacturers were faced with growing shortages of imported inputs. What had been elevated inventory levels offered somewhat of a buffer, but that was only a transitory buffer. Now, with what will surely be a sizable hit to GDP, at home and abroad, in Q2 and perhaps beyond, capital spending is being sharply scaled back. The alarmingly steep decline in the New York Fed's index is a glimpse of what lies ahead for the factory sector in the months ahead.





Regions Financial Corporation, 1900 5th Avenue North, 17th Floor, Birmingham, Alabama 35203
Richard F. Moody, Chief Economist • 205.264.7545 • richard.moody@regions.com