

ECONOMIC UPDATE



REGIONS

January 15, 2013

This Economic Update may include opinions, forecasts, projections, estimates, assumptions and speculations (the "Contents") based on currently available information which is believed to be reliable and on past, current and projected economic, political and other conditions. There is no guarantee as to the accuracy or completeness of the Contents of this Economic Update. The Contents of this Economic Update reflect judgments made at this time and are subject to change without notice, and the information and opinions herein are for general information use only. Regions specifically disclaims all warranties, express or implied, with respect to the use of or reliance on the Contents of this Economic Update or with respect to any results arising therefrom. The Contents of this Economic Update shall in no way be construed as a recommendation or advice with respect to the taking of any action or the making of any economic, financial or other plan or decision.

December Retail Sales: 2012 Ends On Solid Footing, But The Tax Man Cometh In January

- Retail sales rose by 0.5 percent in December after a revised 0.4 percent increase in November (initially reported as a 0.3 percent increase).
- Retail sales excluding autos rose by 0.3 percent after a revised 0.1 percent decline in November (previously reported as unchanged).
- Core retail sales (excluding vehicles, gasoline and building materials) rose by 0.6 percent, matching November's increase.

December saw consumers put aside their worries, to the extent they actually had any, about the partisan wrangling in Washington and the higher taxes on the horizon to do what they do best – shop. Total retail sales rose by 0.5 percent in December following an upwardly revised gain of 0.4 percent in November. Ex-auto sales were up by 0.3 percent but, more significantly, core retail sales rose by 0.6 percent in December matching November's gain. Lower gasoline prices helped hold down the gains in total and ex-auto sales, with sales at gasoline stations falling by 1.6 percent after a 4.5 percent decline in November.

On a nominal basis, core retail sales rose at an annualized rate of 4.0 percent during Q4, slightly ahead of the pace set in Q3. This gain will be enhanced by a slower pace of inflation during Q4, leaving us on track for annualized growth in real consumer spending of around 2.0 percent for Q4. What will remain to be seen, of course, is how consumers respond to the increase in payroll tax rates that took effect on January 1, with Social Security withholding rates rising from 4.2 percent (where they had been for two years) back to their normal 6.2 percent. It is either a nice touch of timing or a slightly cruel irony that today's release of the December retail sales data coincides with the day that many workers see their first 2013 paycheck with the higher payroll tax withholding. With a sudden hit to disposable income, many households will be forced to cut back on discretionary spending while other households will have to decide between spending less or saving less. We do expect to see slower growth in real consumer spending in 2013's first quarter as a result of the higher payroll taxes.

Rising vehicle sales have underpinned growth in overall consumer spending. During 2012's fourth quarter, unit vehicle sales topped 15 million on an annualized basis, the strongest quarter since Q1 2008. November saw auto dealers post a 3.1 percent in the dollar volume of sales and this was followed up by a 1.6 percent increase in December. To some extent, vehicle sales during Q4 2012 were aided by replacement sales in the aftermath of Hurricane Sandy, and there could

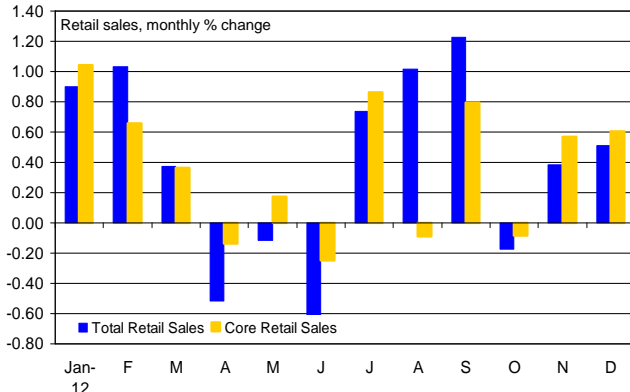
be at least some pullback during the current quarter in response to the higher payroll taxes. Beyond that, however, we expect 2013 to be an even better year for vehicle sales with over 15 million unit sales for the year as a whole.

Sales at apparel stores rose by 1.0 percent in December, while sales at restaurants rose by 1.2 percent after a like-sized gain in November. Furniture stores also saw sales jump in December, with a 1.4 percent increase coming on the heels of a 1.0 percent gain in November. Department stores ended a string of four consecutive monthly declines with a 0.3 percent increase in sales in December.

There were a few surprises in the December retail sales data. Sales at electronics stores fell by 0.6 percent, and sales at nonstore retailers, which includes but is not limited to, online retailers, rose by just 0.5 percent. In each case, lower December sales than we had anticipated came after strong gains in November, with gains of 2.3 percent and 3.4 percent, respectively. An earlier than normal Thanksgiving likely pushed sales forward into November at the expense of December, but nonetheless we had expected slightly better sales for the two-month period in both of these categories.

Consumers ended 2012 on reasonably firm footing and, to the extent they were following the ongoing fiscal policy battles in Washington, don't appear to have pulled back on spending in anticipation of higher taxes in 2013. Now that they actually see lower disposable income, however, there will likely be an impact on discretionary spending, at least in the near term. A better pace of growth in wage and salary earnings, building on the gains seen in Q4 2012, along with rising household net worth – significantly rising house prices are now contributing to rising net worth – will be supportive of consumer spending going forward. After a slow start in Q1, the pace of growth of consumer spending should gradually rise over the remainder of 2013.

 **REGIONS**
Spend In December, For The Tax Man Cometh In January



 **REGIONS**
Vehicle Sales On The Long Road Back

