

# THE ECONOMIC OUTLOOK GROUP



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## ECONOMIC TALKING POINTS

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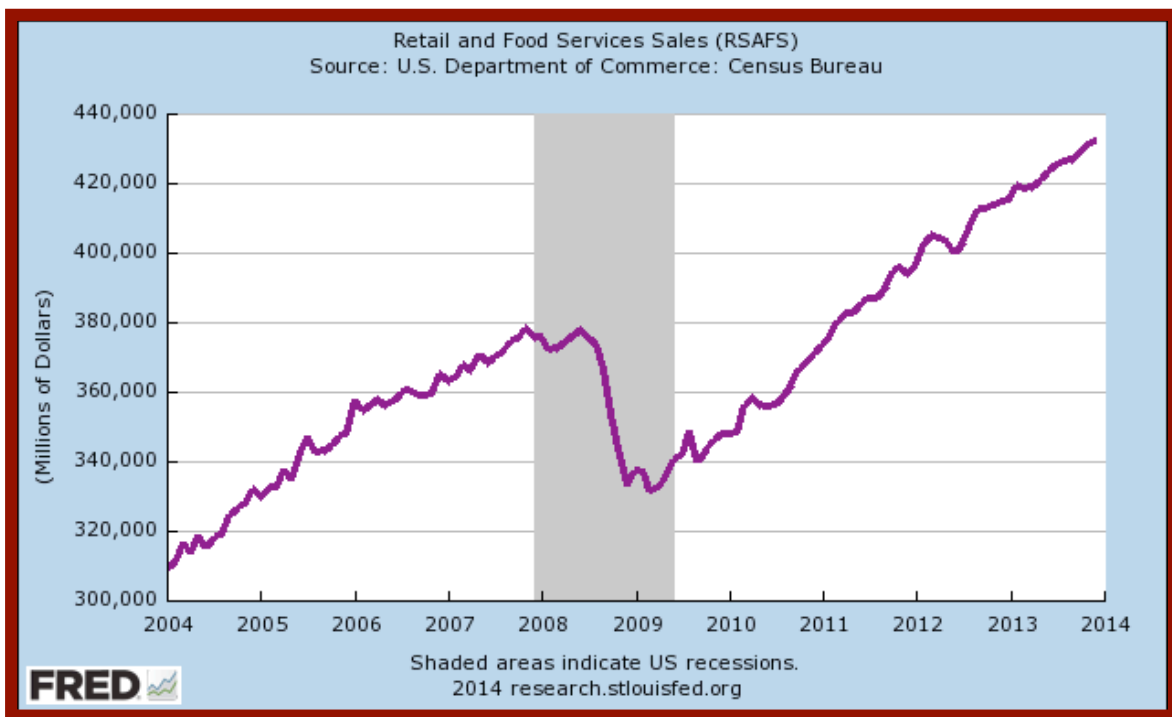
January 14, 2014

### **A Trifecta: Rising Retail Sales, Dormant Inflation and Small Business Optimism**

Anyone worried about the health of the economy after last week's dismal (and dubious) jobs report now has much less to be concerned. We got something of a Trifecta of good news this morning: December's retail sales turned out to be better than expected, import inflation remains non-existent, and small business confidence increased last month as firms expressed more optimism that sales and profits will pick up the next six months.

#### **Retail sales**

Of the three reports, the most closely studied is retail sales since it's an important barometer of consumer spending. Total retail sales rose 0.2% last month, beating out consensus forecasts. Most analysts expected either a decline or a smaller increase. If you eliminate motor vehicles and parts, December sales jumped 0.7%, which turned out to be the largest increase since last February. Overall, spending on retail products rose to \$431.9 billion in December, the most recorded for a single month. And if you take out motor vehicle sales, then sales rose to \$350.2 billion, yet another new high.



There is every indication consumers will continue this shopping trend. Both average weekly earnings and disposable personal income have been rising faster than inflation, increasing purchasing power. Other key factors that underpin spending --- such as the rise in household net worth, a decline in debt service burdens, and steadily improving confidence--- suggest consumers will take the lead in propelling the economy forward this year.

### **Import inflation**

We also expect to see wages and salaries grow at a faster pace during the year as the unemployment rate drops and companies seek to retain workers. If pay hikes accelerate and consumer prices remain quiescent, that will provide even more fuel for consumers to spend. Certainly the latest news on inflation is favorable for shoppers. The import price index was unchanged in December, after falling the previous two months. On a year-over-year basis, import inflation has been negative for four straight months! We'll get producer prices and the CPI in the next two days, but we expect both will be relatively flat.

### **NFIB's Small Business Economic Trends --- and the ADP Employment Report**

What was particularly interesting among the economic data out this morning was the National Federation of Independent Business (NFIB) report on Small Business Economic Trends. We like to compare their survey results with the latest ADP Employment release, since it tracks actual hiring in the small business sector. Are both studies about this all-important segment of the economy consistent? It certainly appears so.

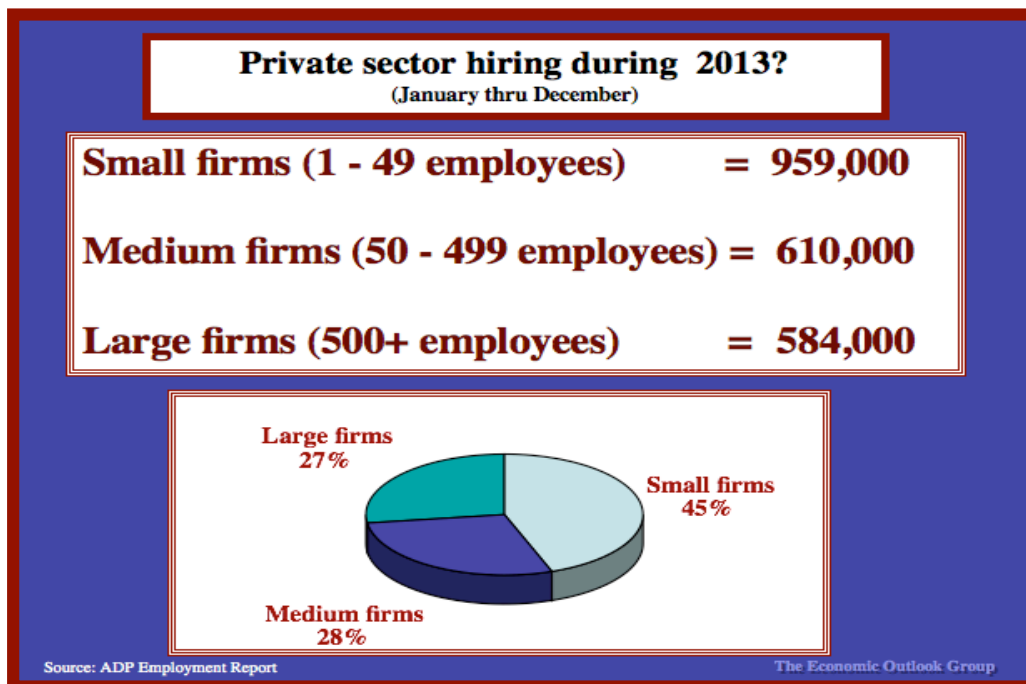
Let's focus on the NFIB release first.

- Their small business optimism index rebounded to 93.9 in December, the strongest since August. A year ago, it stood at 88.
- When small businesses were asked whether it would be a good time to expand their operations the next three months, the December number came in at the highest in two years.
- When queried on how hard it is to fill job openings, that index shot up to the highest in nearly six years!
- Firms who said they boosted capital spending in the last six months turned out to be the most in *a decade!!!*
- Those who have plans to carry out such expenditures in the next three to six months jumped to the largest since June 2008.

Pretty good numbers! But do these numbers coincide with the ADP Employment report of last week, which breaks down job gains by small, midsize, and large firms? It appears ADP is in full agreement with the pick up in activity captured by NFIB.

According to ADP, small businesses (defined as firms with 1 to 49 employees) boosted hiring by 108,000 in December, the largest of the year. Equally impressive is that small firms were responsible for hiring 959,000 people in all of 2013. That means nearly one in every two people who found employment in the private sector last year (45%) did so with small businesses. And the pace of hiring for this group accelerated most in the final three months of the year.

In contrast, midsize firms (with 50 – 499 employees) added 610,000 to payrolls in 2013, accounting for 28% of the total, while large companies (500 and above employees) added 584,000, which represents 27% of the 2.153 million total companies hired.



**Bottom line:**

There is now a preponderance of evidence that the economy has gained traction, and virtually nothing to suggest that grip is starting to slip. We believe Congress will pass an extension of unemployment benefits very soon, and that will help sustain consumer spending. It is likely the expiration of the accelerated depreciation allowance at the end of last year will slow capital outlays this month and next, but we fully expect such investments to pick up again the balance of the year. All in all, we see fundamentals in the economy improving and this will be underscored by acceleration in employment and household spending during the coming months.

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