

Retail Sector Market Outlook (Nov 2022): Inflation Cools as Consumers Head Into Holiday Season

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Key Takeaways

- **Sector Performance: Cooling inflation led to strong market rally.** The Federal Reserve imposed another 0.75–point rate hike in the November FOMC meeting. During his post–meeting conference, Fed Chair Jerome Powell signaled the central bank could begin dialing back the pace of its increases soon but also saw a higher terminal rate. The CPI and PPI reading for October both came in lower than expected, which led to a strong market rally after the reading.
- **Economic Data: Core inflation slows while energy prices rebound.** The consumer price index was up 7.7% from a year earlier, the smallest annual advance since the start of the year and down from 8.2% in September. Core prices, which exclude food and energy and are regarded as a better underlying indicator of inflation, advanced 6.3%, pulling back from a 40–year high. US retail sales posted the biggest increase in eight months in October, as the value of overall retail purchases climbed 1.3% last month. The University of Michigan consumer sentiment index decreased to 54.7 in November from 59.9 in October, its lowest level since July, as concerns over high inflation and an upcoming economic downturn weighed.
- **Our Perspective:** US inflation might have peaked, as core prices continued to fall. Rent prices began to fall but might remain sticky in the short term. Energy prices rebounded in the month, as tight demand in oil market might lead to rising oil prices and persistent energy inflation. Retail sales topped expectations in October, as US consumer demand remained resilient. The strong retail sales data might affect market expectations about a Fed pivot in its monetary tightening. Therefore, investors should focus on the overall economic outlook and the subsequent policies established by the Federal Reserve in the future.
- **Potential Risk:** Macroeconomic risk, Monetary policy risk. Consumer demand might remain lower than expected. Sticky inflation might impact overall consumer sentiment.

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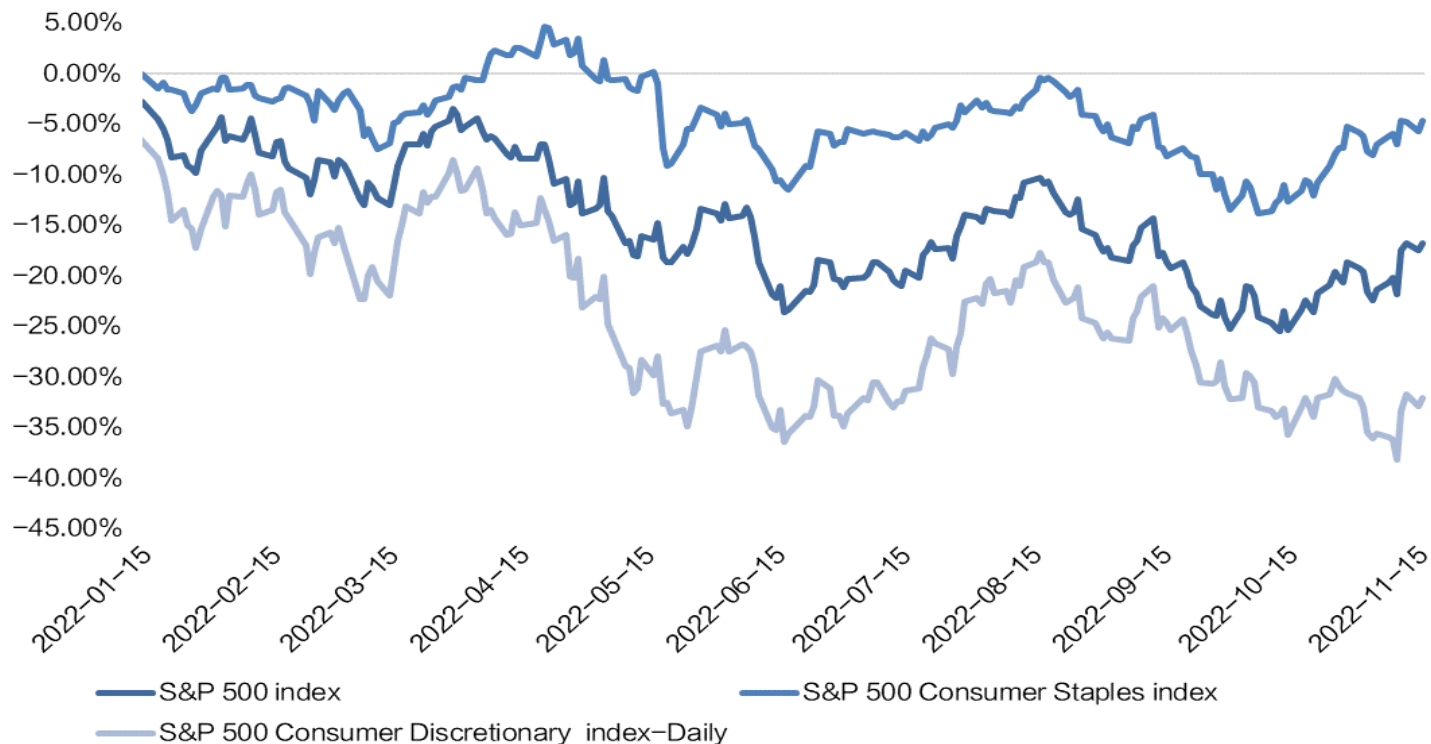
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Cooling inflation led to strong market rally

- **Cooling inflation led to strong market rally.** The Dollar Index and U.S. 2-Year Treasury both fell from record highs since late October as equity market rallied. The Federal Reserve imposed another 0.75-point rate hike in the November FOMC meeting, as Fed Chair Jerome Powell signaled the central bank could begin dialing back the pace of its increases soon but also saw a higher terminal rate. The CPI and PPI reading for October both came in lower than expected, which led to a strong market rally after the reading.
- **The S&P 500 Consumer Staples index gained 6.89%, while the S&P 500 Consumer Discretionary index lost 1.64% in October.**

Figure: The S&P 500 / S&P 500 Consumer Staples / S&P 500 Consumer Discretionary index—Daily return performance, as of Nov 15, 2022



Most S&P 500 sectors gained, while automobiles sector was the lone loser

- Most S&P 500 sectors gained in October, as energy sector rose 25.3%. Consumer staples sector gained 8.7%, while consumer discretionary sector gained 2.9%.
- Besides automobiles, major consumer-related stocks all gained in October. Media stocks gained 14.2%, while consumer service stocks gained 13.2%. Automobiles and auto parts stocks lost 8.5% for the month, as Tesla stock accounted for most of the losses.

Figure: Monthly return of S&P 500 primary sectors, as of Oct 31, 2022

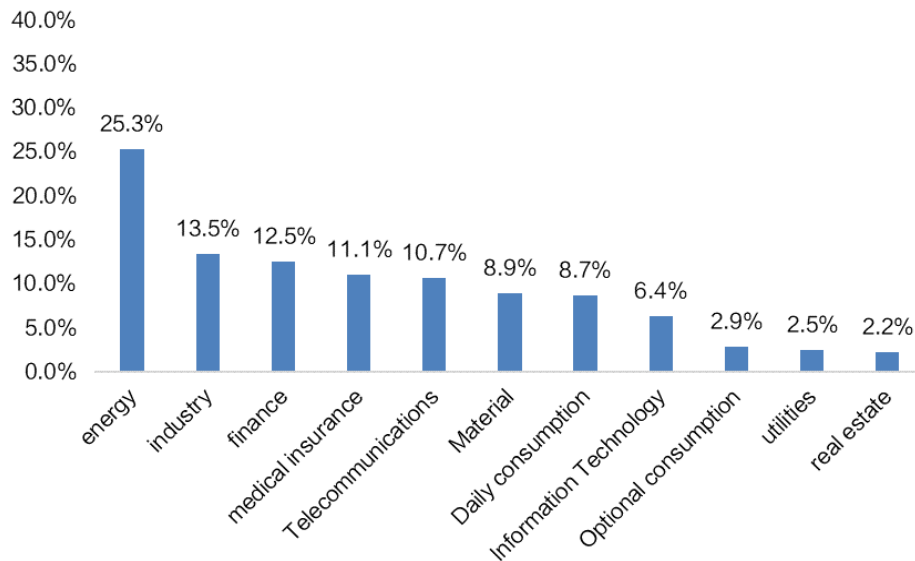
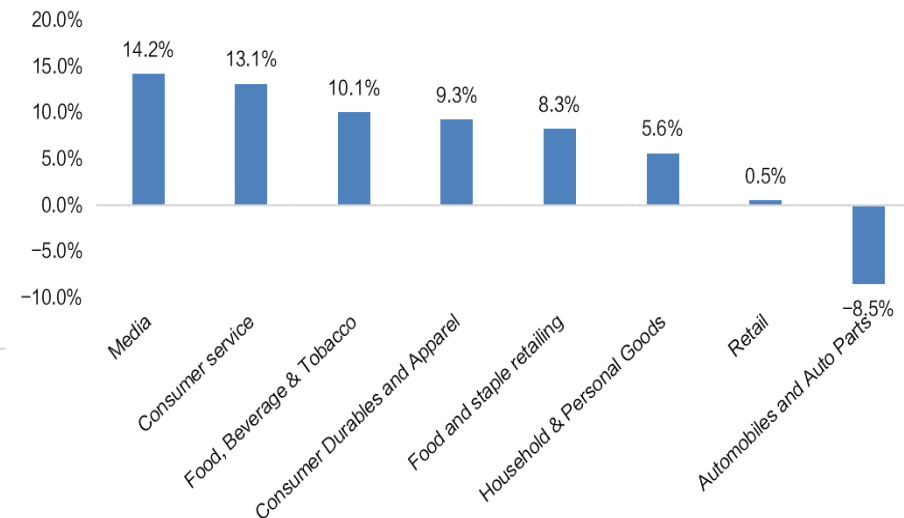


Figure: Monthly return of S&P 500 Consumer Discretionary/S&P 500 Consumer Staples, as of Oct 31, 2022



Food service stocks led consumer staples sector, while cruise stocks led consumer discretionary sector

- Food service stocks led consumer staples sector. Food distributor Sysco Corporation (SYY.N) was the top gainer for the month(+23.2%). Food processing company Archer–Daniels–Midland (ADM.N)(+20.5%), retail pharmacy owner Walgreens Boots Alliance (WBA.O)(+16.2%), food company Kraft Heinz (KHC.O)(+15.4%) were the other major gainers. Kraft Heinz saw its Organic Net Sales up by 11.6% for Q3 2022, as consumer demand remained strong.
- Norwegian Cruise Line Holdings (NCLH.N)(+48.3%) led the consumer discretionary sector in October, while Royal Caribbean Cruises (RCL.N)(+40.8%) and Caesars Entertainment (CZR.O)(35.6%) were the other gainers.

Figure: The top ten monthly gainers of S&P 500 Consumer Staples, as of Oct 31, 2022

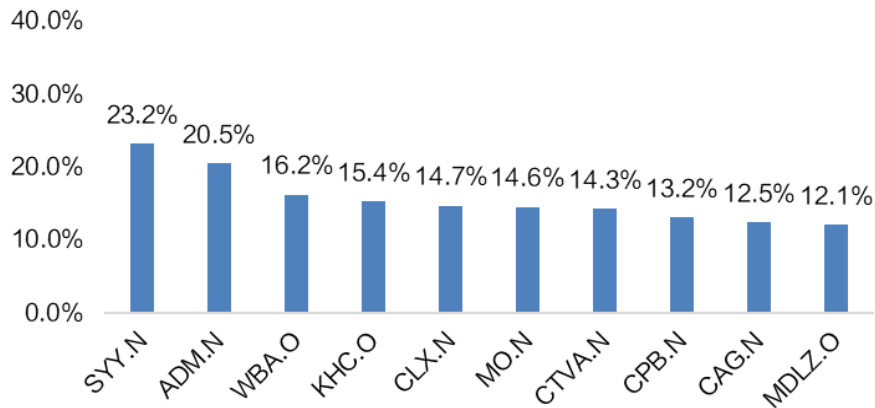


Figure: The top ten monthly gainers of S&P 500 Consumer Discretionary, as of Oct 31, 2022

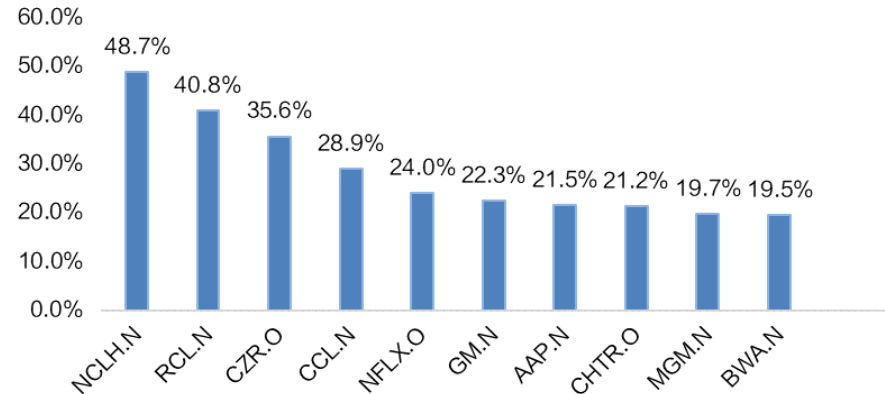


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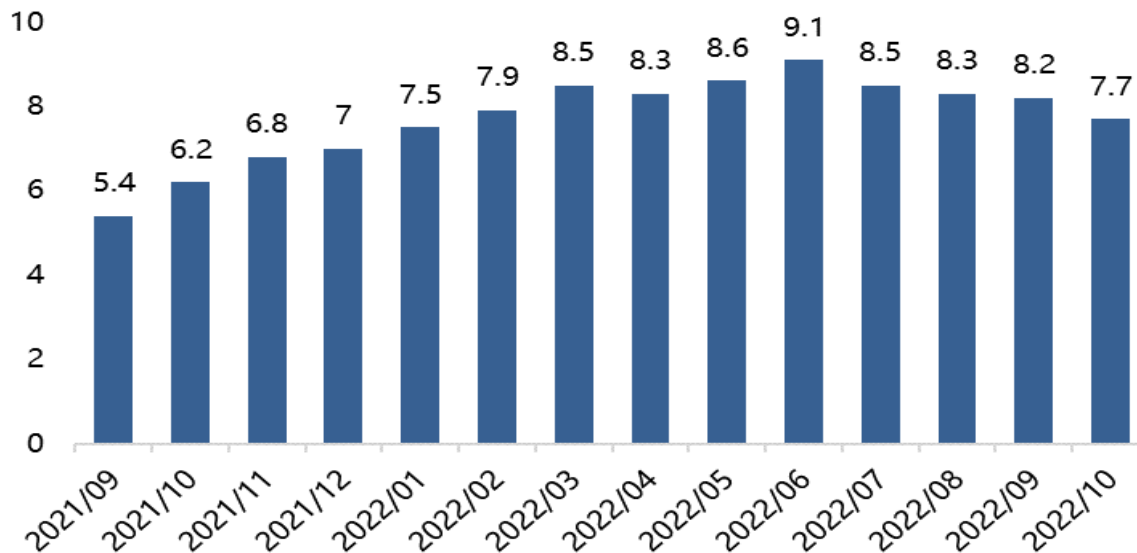
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Economic Data: Core inflation slows while energy price rebounds

- **U.S. October CPI and Core CPI came in lower than expected, which might signal a potential Fed pivot in monetary policies.** The consumer price index increased 0.4% for the month and 7.7% from a year ago, both lower than estimates. Excluding volatile food and energy costs, so-called core CPI increased 0.3% for the month and 6.3% on an annual basis, also lower than expectations.
- **Decline in core prices helped to bring down inflation, while energy prices bounced back for the month.** A 2.4% decline in used vehicle prices and a 0.7% decline in apparel prices helped to bring down the inflation figures. Import prices also dropped on lower transportation costs and a strong dollar. Energy prices increased 1.8% for the month, thanks to a 4% increase in gasoline prices. Rent prices rose 0.7% for the month compared to a 0.8% increase in September.
- **Inflation and core inflation are cooling down, yet energy prices might still be sticky.** With lower oil production levels by OPEC+ and rising demand from European countries, oil prices might still rise in the short-term, which could lead to sticky energy inflation.

Figure: U.S. CPI growth rate , yoy, %



Economic Data: Retail sales rose into holiday season while consumer sentiment weakened

- US retail sales posted the biggest increase in eight months in October, as the value of overall retail purchases climbed 1.3% last month. Nine of 13 retail categories rose last month, according to the report, including firm results at auto dealers, grocery stores and restaurants. The value of sales at gas stations climbed 4.1%, mostly reflecting higher pump prices. Sales of automobiles climbed 1.3%, while sales at restaurants rose 1.6%.
- The University of Michigan consumer sentiment index decreased to 54.7 in November from 59.9 in October, its lowest level since July, as concerns over high inflation and an upcoming economic downturn weighed.

Figure: US Consumer Confidence Index , as of November 11, 2022

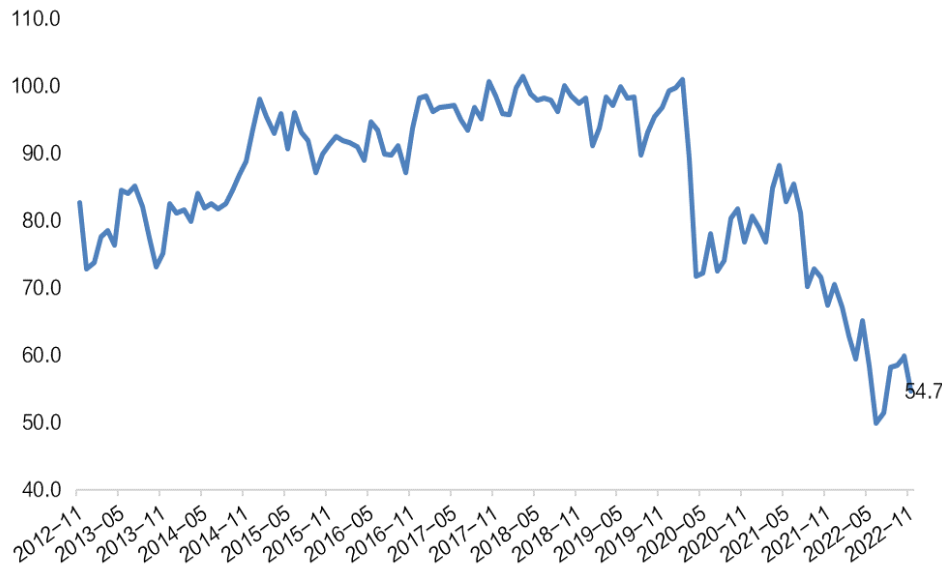


Figure: U.S. retail sales monthly rate (%) , As of October 2022

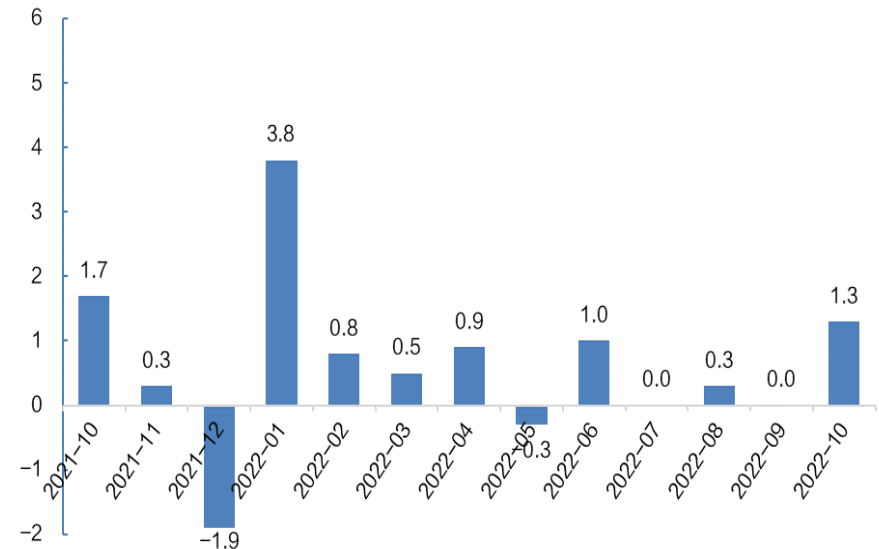


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Key Companies

- Amazon (AMZN.O): Amazon reports Q3 revenue of \$127.10 billion vs. estimated \$127.46 billion and Q3 earnings of \$0.28 per share vs. estimated \$0.21. Revenue grew 15% in the third quarter. The company expects net sales in the fourth quarter to be \$140–148 billion, corresponding to a year-on-year growth rate of 9.2%~9.7%, lower than market expectations of \$155.52 billion. The company expects an operating profit of \$0–4 billion in the fourth quarter, significantly lower than Bloomberg's consensus forecast of \$4.66 billion and \$3.46 billion in the fourth quarter of last year.
- Coca-Cola (KO.N): Coca-Cola reports Q3 revenue of \$11.06 billion vs. estimated \$10.5 billion and Q3 earnings of \$0.69 per share vs. estimated \$0.64. Total revenue rose 10%, while organic revenue climbed 16%, fueled by higher prices across its portfolio. The company won't provide its full 2023 outlook until February.
- Starbucks (SBUX): Starbucks reports quarterly revenue of \$8.41 billion vs. estimated \$8.31 billion and quarterly earnings of \$0.81 per share vs. estimated \$0.72. Global same-store sales increased 7%, fueled by increased spending in its home market. For fiscal 2023, Starbucks is projecting revenue growth of 10% to 12%, despite a 3% hit from foreign currency translation. The company also expects its global same-store sales growth on the high end of its prior range of 7% to 9%.
- Walmart (WMT): Walmart reports quarterly revenue of \$152.81 billion vs. estimated \$147.75 billion and quarterly earnings of \$1.50 per share vs. estimated \$1.32. Comparable sales for Walmart U.S. rose 8.2%, excluding fuel. That topped Bloomberg's consensus forecast of 3.46%. U.S. e-commerce sales grew 16% year over year, or 24% on a two-year basis. Walmart expects adjusted earnings per share to drop by 3% to 5% in the fourth quarter and consolidated net sales to grow by about 3%, as it is, negatively affected by approximately \$1.3 billion from currency fluctuations.

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Potential Risk

- Recovery in travel demand might be slower than expected
- Consumer demand might remain weaker than expected
- Decline in disposable income might affect consumer sentiment
- High inflation might stay longer than expected
- Geopolitical risks

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