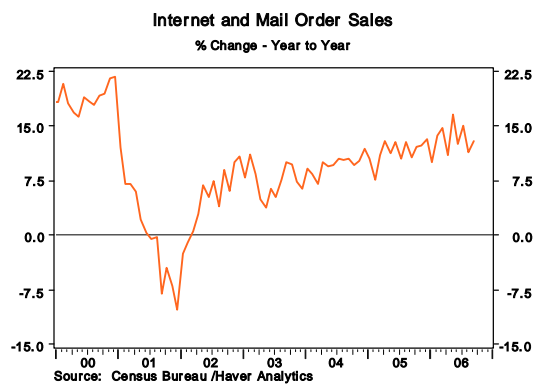
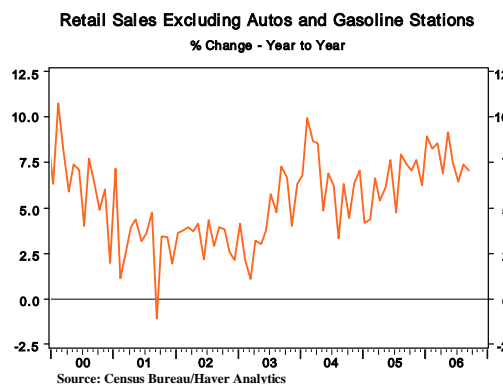
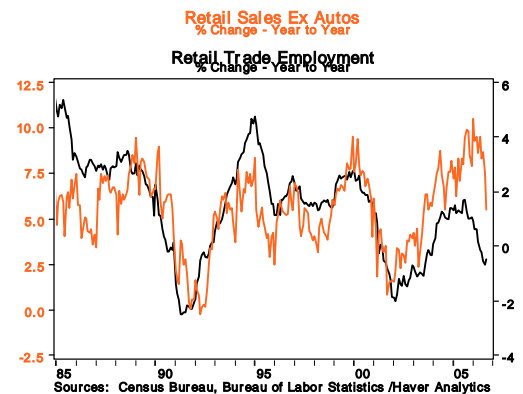
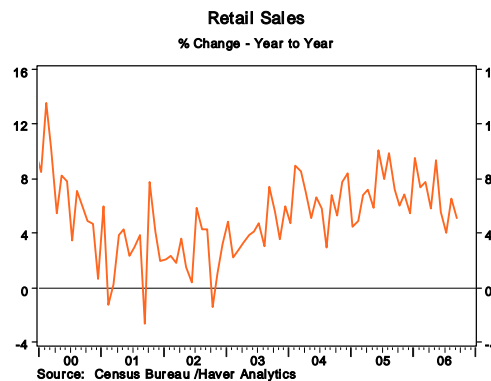


SEPTEMBER RETAIL SALES

Brian S. Wesbury
Chief Economist
Bill Mulvihill
Senior Economist
 (630) 322-7756

- Retail sales unexpectedly fell 0.4% in September, versus consensus estimates of a 0.2% gain. Sales are up 5.5% from year-ago levels.
- Despite reports from manufacturers of an increase in auto and truck sales during September, motor vehicle and parts dealers' reported sales were unchanged in September. Excluding autos, retail sales fell 0.5% in September but are up 5.5% in the past year.
- Gasoline service station sales plunged 9.3% in September, the largest decline on record (data goes back to 1992). Excluding autos and gas, sales rose 0.7% last month and 7.3% in the past year.



Implications: At first blush, the unexpected decline in retail sales appears worrisome. But, you shouldn't read a book by its cover. Upon further review, the weakness in the headline data is entirely due to falling gasoline prices. Excluding autos and gas, retail sales jumped 0.7% last month and are up a strong 7.3% in the past year – a very strong showing for nominal spending patterns. Even the news about falling gas station sales isn't as bad as it first appears. The Department of Energy reported that gasoline prices fell 13.0% (while sales fell just 9.3%). As a result, real (or inflation-adjusted) gas station sales were actually positive. This suggests that Q3 real GDP will not be adversely impacted by this report. We continue to expect real consumption of near 3.0% in Q3. The biggest wildcard remains a widening trade deficit that could pull back reported Q3 real GDP into the 2%-2½% range despite a very resilient consumer. Nonetheless, with unemployment at a cyclical low, wages rising faster than inflation, and business investment strong, we expect the economy to snap out of its recent lull and regain strong forward momentum in the fourth quarter.

| Retail Sales <i>All data seasonally adjusted</i> | Sep-06 | Aug-06 | Jul-06 | 3-mo % Ch. <i>annualized</i> | 6-mo % Ch. <i>annualized</i> | Yr over Yr % Ch |
|--|--------|--------|--------|---------------------------------|---------------------------------|--------------------|
| Retail Sales and Food Services | -0.4% | 0.1% | 1.4% | 4.2% | 2.8% | 5.5% |
| Ex Autos | -0.5% | 0.2% | 0.7% | 1.4% | 3.8% | 5.5% |
| Ex Autos and Gasoline | 0.7% | 0.4% | 0.6% | 7.2% | 4.8% | 7.3% |
| Motor Vehicle and Parts Dealers | 0.0% | -0.4% | 4.1% | 16.0% | -0.9% | 5.6% |
| Building Materials and Supply | 0.6% | 0.6% | 0.6% | 7.3% | -5.4% | 8.3% |
| Furniture, Home Furnishings, and Electronics | 0.2% | 0.0% | 0.3% | 2.0% | 3.7% | 4.5% |
| General Merchandise | 1.1% | 0.5% | 0.5% | 8.3% | 5.9% | 6.3% |
| Food and Beverage | 1.0% | 1.2% | 0.6% | 11.7% | 5.8% | 8.3% |
| Gas Service Stations | -9.3% | -1.3% | 1.5% | -32.0% | -3.9% | -6.3% |
| Health and Personal Care | 0.2% | 1.1% | 0.2% | 6.2% | 8.2% | 7.3% |
| Clothing and Accessories | 3.0% | -0.2% | 1.2% | 17.1% | 11.9% | 10.7% |
| Internet and Mail Order | 1.1% | -0.2% | 2.0% | 11.8% | 11.2% | 12.9% |

Source: Bureau of Census