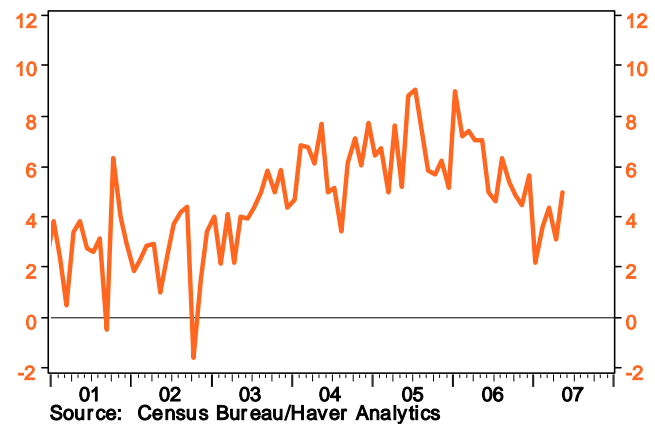


MAY RETAIL SALES

Chief Economist – Brian S. Wesbury
Senior Economist – Robert Stein, CFA
Economic Research Analyst – Trevor Scott

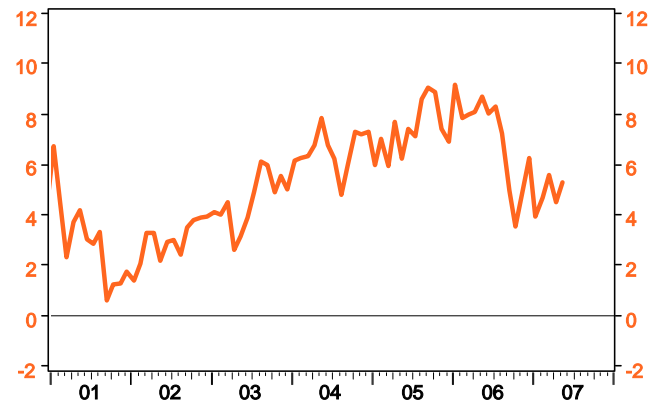
- May retail sales increased 1.4% and were up 1.3% excluding autos, both much better than consensus expectation. Also, April retail sales were revised up slightly. Retail sales are up 5.0% versus last year, 4.6% excluding autos.
- The largest dollar gains in May were in autos and gas. Sales were also strong for building materials, at general merchandise stores (including department stores), and clothing and accessory stores. No major category of sales declined in May.
- Excluding autos, building materials, and gas, retail sales were up 0.8% in May and are up 5.6% versus a year ago.

Retail Sales & Food Services
% Change - Year to Year



Implications: Stick a fork in it. The widespread belief (which we never shared) that the economy was in trouble and the Federal Reserve was going to cut rates is done. Weakness in housing and high energy prices have not undermined consumption. Retail sales excluding autos and building materials are a direct feed into GDP data (auto sales data come from another source and building materials are counted as investment) and these sales are up 10.5% at an annual rate in the past three months. Excluding gas from this metric (gas sales are usually driven by inflation) shows a gain at a 6.5% rate the past three months. Given this data, real consumption (including services) should grow at about a 3% annual rate in the second quarter and real GDP appears set to grow at a 4% annual rate in Q2. In other news this morning, import prices were reported up 0.9% for May versus a consensus expected 0.3%. Ex-petroleum, import prices were still up 0.5%. Export prices were up 0.1% (0.2% ex-agriculture). The data show strong growth and higher overall inflation. As a result we continue to believe the Fed's next move will be to hike rates, not cut them.

Retail Sales and Food Services EX: Autos and Building Materials
% Change - Year to Year



Retail Sales <i>All Data Seasonally Adjusted</i>	May-07	Apr-07	Mar-07	3-mo % Ch. annualized	6-mo % Ch. annualized	Yr to Yr % Change
Retail Sales and Food Services	1.4%	-0.1%	1.0%	9.6%	8.2%	5.0%
Ex Autos	1.3%	0.1%	1.1%	10.1%	8.8%	4.6%
Ex Autos and Building Materials	1.2%	0.3%	1.0%	10.5%	9.4%	5.3%
Ex Autos, Building Materials and Gasoline	0.8%	0.1%	0.7%	6.5%	6.4%	5.6%
Autos	1.8%	-0.5%	0.6%	7.9%	6.2%	6.6%
Building Materials	2.1%	-2.2%	1.8%	6.6%	3.5%	-1.7%
Gasoline	3.8%	1.8%	3.1%	40.6%	31.4%	3.7%

Source: Bureau of Census