ECONOMIC UPDATE

REGIONS

May 31, 2018

April Personal Income/Spending: Consumer Spending Off To Solid Start In Q2

- Personal income rose by 0.3 percent in April, personal spending rose by 0.6 percent, and the saving rate fell to 2.8 percent.
- The PCE deflator rose by 0.2 percent and the core PCE deflator rose by 0.1 percent in April. Year-on-year, the PCE deflator was up by 2.0 percent and the core deflator was up by 1.8 percent.

Total personal income rose by 0.3 percent in April, shy of our forecast of 0.4 percent, as total personal spending surprised to the upside with the 0.6 percent increase topping the 0.4 percent increase we and the consensus expected. With spending growth topping income growth, the personal saving dipped to 2.8 percent in April. The PCE deflator, the FOMC's preferred gauge of inflation, rose by 0.2 percent with the core PCE deflator up 0.1 percent, for year-on-year changes of 2.0 percent and 1.8 percent, respectively, in each case matching our forecast.

As we expected, the April personal income data show a larger gain in aggregate wage and salary earnings than was implied by the April employment report. Private sector labor earnings were up 0.4 percent and government sector earnings were up 0.2 percent, good for year-on-year increases of 4.9 and 2.6 percent, respectively. Investment income was up by 0.3 percent in April, an increase driven entirely by a 0.4 percent increase in interest income while dividend income was flat. Rental income and transfer payments both logged 0.3 percent increases. Nominal disposable personal income was up 0.4 percent in April, leaving it up 3.9 percent year-on-year; after adjusting for inflation, disposable personal income was up 0.2 percent in April and is up 1.9 percent year-on-year. Growth in disposable personal income thus far in 2018 is easily running ahead of the pace set in 2016 and 2017, which reflects an acceleration in the growth of wage and salary earnings, by far the largest single component of personal income, and also the cut in individual income tax rates incorporated into the 2017 tax bill.

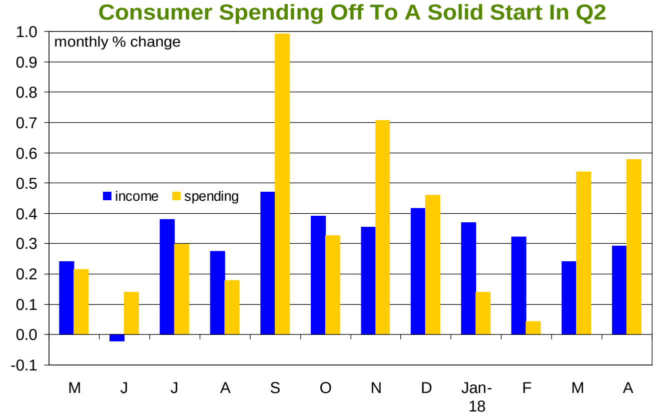
Nominal personal spending rose by 0.6 percent in April, with spending on consumer durables up 0.3 percent, spending on nondurable consumer goods up 0.9 percent, and spending on household services, which account for roughly two-thirds of total consumer spending as measured in the GDP data, up 0.5 percent. Higher gasoline prices account for some of the growth in spending on nondurable goods, while sharply higher utilities outlays, thanks to April's bout of "winter" weather, helped drive the growth in spending on services. Real, or, inflation adjusted, personal spending was up 0.4 percent in April, with the 0.9 percent increase in nominal spending on nondurable goods turning into a 0.4 percent increase after accounting for inflation. In other words, there was more than higher prices behind the solid gain in consumer spending on goods in April, with Q2 growth in real consumer spending on a much firmer trajectory than that seen in Q1. As we have noted, trend growth in consumer spending is neither as strong as implied by the Q4 2017 data nor as weak as implied by the Q1 2018 data.

One element of the April data that stands out is the personal saving rate falling to 2.8 percent. What this says, however, is open to interpretation. One interpretation is that consumers are pressed to fund necessities such as food, clothing, shelter, and utilities – one can point to higher gasoline prices and atypically high utilities outlays to back this take on the decline in the saving rate. An alternative explanation is that with solid gains in disposable income, elevated household net worth, and consumer confidence at a nearly two-decade high, consumers feel more comfortable spending more and saving less, particularly those letting rising asset prices substitute for traditional saving, a trade that has been apparent in the data to varying degrees since the mid-1980s. We'll go with "somewhere in between" as the more likely explanation, as lower income households with little, if any, in the way of net worth are more prone to dissaving due to spikes in energy prices and utilities outlays.

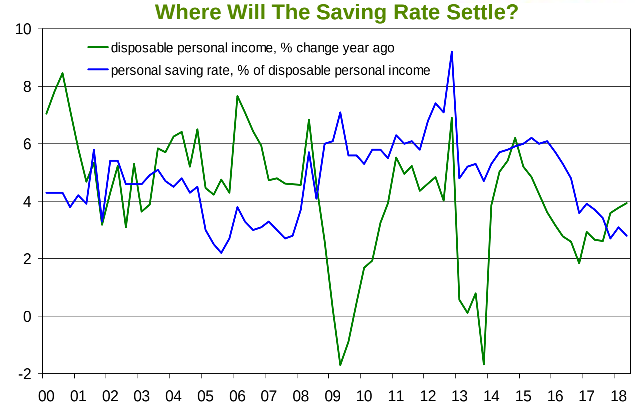
Aside from energy, there is little in the PCE deflator data that suggest inflation is poised to accelerate sharply in the months ahead. In keeping with the patterns seen in the CPI data, core goods prices were up mildly in April but were nonetheless down year-on-year, the 65th consecutive year-on-year decline in the PCE deflator's measure of core goods prices. The recent appreciation of the U.S. dollar, if sustained, will blunt any upward pressure on core goods prices over coming months.

The April data show consumer spending off to a solid start in Q2, healthy growth in disposable personal income, and core inflation still seeking traction. Nothing here is out of line with our expectations and, more importantly, with the expectations of the FOMC.

Consumer Spending Off To A Solid Start In Q2



Where Will The Saving Rate Settle?



Regions Financial Corporation, 1900 5th Avenue North, 17th Floor, Birmingham, Alabama 35203
Richard F. Moody, Chief Economist • 205.264.7545 • richard.moody@regions.com