ECONOMIC UPDATE

REGIONS

November 29, 2018

October Personal Income/Spending: Solid Headline Numbers, Not So Inspiring Details . . .

- Personal income rose by 0.5 percent in October, personal spending rose by 0.6 percent, and the saving rate fell to 6.2 percent
- The PCE deflator rose by 0.2 percent and the core PCE deflator was up by 0.1 percent in October; 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 0.5 percent in October, matching our above-consensus forecast, while total personal spending rose by 0.6 percent, besting our above-consensus forecast. With spending growth outpacing income growth, the personal saving rate fell to 6.2 percent in October from 6.3 percent in September. The PCE deflator, the FOMC's preferred gauge of inflation, rose by 0.2 percent in in October, with the core PCE deflator up by 0.1 percent, each falling shy of our forecast. On an over-the-year basis, the PCE deflator is up 2.0 percent and the core PCE deflator is up 1.8 percent.

Growth in total personal income was helped along by an $11.6 billion increase in farm proprietors' income. To a large extent, this reflects subsidy payments associated with the Department of Agriculture's "Market Facilitation Program" which assists farmers who have been adversely impacted by tariffs imposed by foreign nations on U.S. agricultural products. This jump in farm income added one-tenth of a point to the change in total personal income in October. Transfer payments posted a second consecutive 0.6 percent increase in October, also adding one-tenth of a point to the change in total personal income.

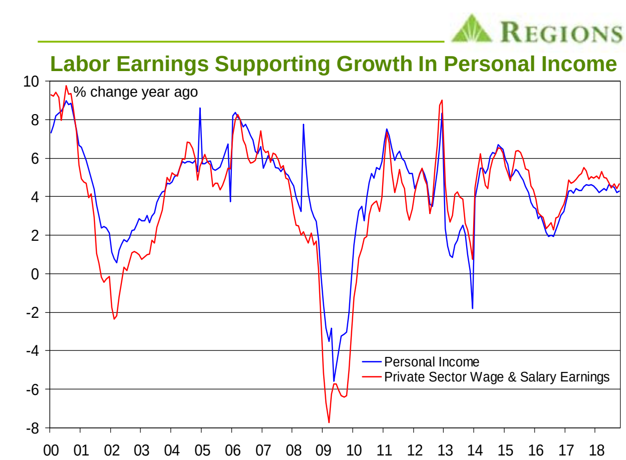
Not to be picky (who, us?) or anything, but the details beneath the 0.5 percent increase in total personal income in October aren't all that inspiring. Our forecast was predicated on a larger increase in private sector wage and salary earnings than the actual increase of 0.3 percent. Moreover, today's release incorporates revisions to wage and salary earnings over the prior six months on the basis of the latest quarterly "census" of employment and earnings, and those revisions were to the downside (and were also reflected in yesterday's GDP release). In short, while growth in private sector wage and salary earnings is still the primary driver of growth in total personal income, growth in labor earnings is now shown to be a bit less strong than had been reported.

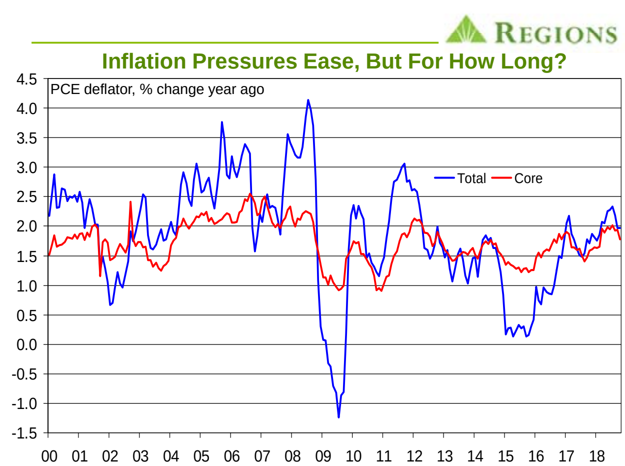
The 0.9 percent increase in nonfarm proprietors' income (which basically reflects profits of small businesses) matched our forecast but comes on the heels of a 0.6 percent decline in September. Dividend income was up 0.5 percent in October and interest income rose by 0.3 percent after having been flat over the prior three months. Total personal income was up 4.1 percent year-on-year as of October, while private sector wage and salary earnings were up 4.7 percent.

As with personal income, October's 0.6 percent increase in total personal spending is less inspiring when put into context (again, not being picky or anything). What was originally reported as a 0.4 percent increase in total spending in September is now reported to be a 0.2 percent increase (this was also reflected in yesterday's GDP release), thus setting a lower bar for spending growth in October. BEA notes that prescription drugs made the largest contribution to growth in spending on goods, while utilities outlays made the largest contribution to growth in spending on household services, neither of which is what you think of when you think of confident consumers ready and willing to spend. That said, the start of the holiday sales season is more in line with our expectations of what consumer spending will look like in November and December. Real personal spending was up 0.4 percent in October.

Inflation pressures eased further in October, which is perhaps more noteworthy in the context of core, rather than headline, inflation. The core PCE deflator was up just 0.1 percent, leaving it up 1.8 percent year-on-year. Core goods prices were flat in October, ending a string of monthly declines but nonetheless down year-on-year for a 72nd straight month. Health care costs were down 0.1 percent in October, and remain a drag on PCE inflation. While rents do not play nearly as large a role in the PCE deflator as they do in the CPI, rent growth is showing signs of softening which, if this persists, will be a drag on core PCE inflation.

Though many were quick to point to the inflation details in the October data as proof that the FOMC has latitude to hit the pause button, the FOMC is less interested in what inflation was in October than what it will be in 2019. Rising labor costs, rising shipping costs, and potentially higher, and wider reaching, tariffs all suggest the FOMC may have less latitude to pause than is implied in the October data.





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