ECONOMIC UPDATE
REGIONS
April 30, 2021

March Personal Income/Spending: Transfers Push Income And Spending Sharply Higher

- Personal income rose by 21.1 percent in February, personal spending rose by 4.2 percent, and the saving rate rose to 27.6 percent
- The PCE Deflator rose by 0.5 percent and the core PCE Deflator rose by 0.4 percent in March; on an over-the-year basis, the PCE Deflator is up 2.3 percent and the core PCE Deflator is up 1.8 percent

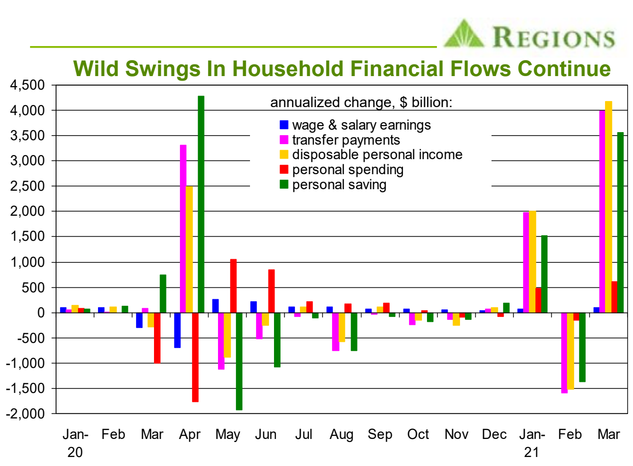
Total personal income rose by 21.1 percent in March, just shy of our above-consensus forecast of 21.2 percent, propelled higher by the third round of Economic Impact Payments. Total personal spending rose by 4.2 percent, between the consensus forecast of 4.1 percent and our forecast of 4.3 percent. With the surge in personal income, the personal saving rate vaulted up to 27.6 percent in March, adding to an already deep pool of excess savings in the household sector which we and many others expect will spark a considerable burst of consumer spending, particularly on services, in the months ahead. The PCE Deflator, the FOMC's preferred gauge of inflation, rose by 0.5 percent in March, matching what we and the consensus expected, while the core PCE Deflator rose by 0.4 percent, one-tenth more than we and the consensus expected. On an over-the-year basis, the PCE Deflator is up 2.3 percent and the core PCE Deflator is up 1.8 percent.

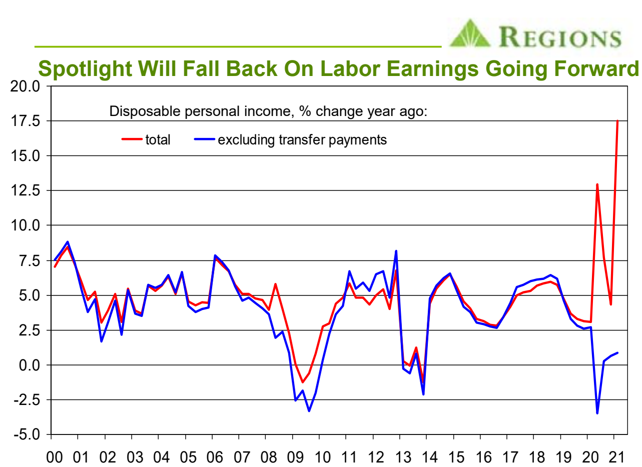
Total personal income rose by $4.213 trillion in March, largely driven by transfer payments rising by $3.986 trillion (note that these are annualized rates, which is the basis on which the data are reported). The bulk of the third round of Economic Impact Payments (EIP) was distributed in March, which accounted for $3.948 trillion of the increase in total transfer payments. A small portion of the third round of EIP fell into April, but on net transfer payments, and in turn total personal income, will fall sharply in the April data. The April data will, at least for a time, cap what have been wild swings in household financial flows over the past year, reflecting the initial hit to labor earnings and subsequent rebound and the magnitude of the fiscal transfers to the household sector during the pandemic.

The net result of these swings as of the March data is reflected in the personal saving rate of 27.6 percent. Our estimate puts the level of "excess saving" in the household sector at $2.2 trillion as of March, which is the difference between the actual level of saving and what saving would be had the trends in place prior to the pandemic remained in place. While fiscal transfers account for a sizable portion of excess saving, part of it also comes from spending on services having been held down by restrictions on economic activity and changes in consumer behavior during the pandemic, so, in a sense this portion of excess saving can be thought of as "forced" saving. Also, keep in mind that many households have freed up cash by paring down debt and/or refinancing mortgages, thus lowering monthly debt service burdens. As such, conditions are in place for there to be a significant burst in spending as more and more people are vaccinated and the economy more fully reopens in the months ahead. Obviously there are many open questions about how consumer behavior may have changed due to the experiences of the pandemic, and we do believe the saving rate will settle at a higher rate than was in place (around 7.5 percent) prior to the pandemic, but even so it is hard to argue that coming months won't see a significant burst of spending, most of which will be on services such as travel, dining out, recreation, and entertainment. With consumer spending on goods 18.2 percent above the pre-pandemic level as of March, there is likely very little pent-up demand for spending on goods. This isn't to say spending on goods won't rise further, but instead that the bulk of any increase in spending in the months ahead will likely fall on services. As of March, the level of spending on services was still 3.0 percent below the pre-pandemic level.

Assuming fiscal transfers, at least in the form of Economic Impact Payments, have run their course, attention will turn back to labor earnings as they resume their traditional role as the main driver of growth in personal income. Under the heading of "oh, by the way," private sector wage and salary earnings rose by 1.1 percent in March, and if job growth is as robust as we expect will be the case over Q2, we should see like-sized increases in wage and salary earnings.

The sizable March increases in the total and core PCE Deflators played a role in what in Q1 was fastest quarterly growth in the GDP Price Index since 1990. Though the FOMC continues to see inflation pressures as transitory, we're not quite convinced. While base effects will distort the inflation readings for a few more months, what happens after that is, at least to us, still an open question.





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