ECONOMIC UPDATE

REGIONS

December 1, 2022

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October Personal Income/Spending: Strong Start To Q4 Spending, Inflation Pressures Ease

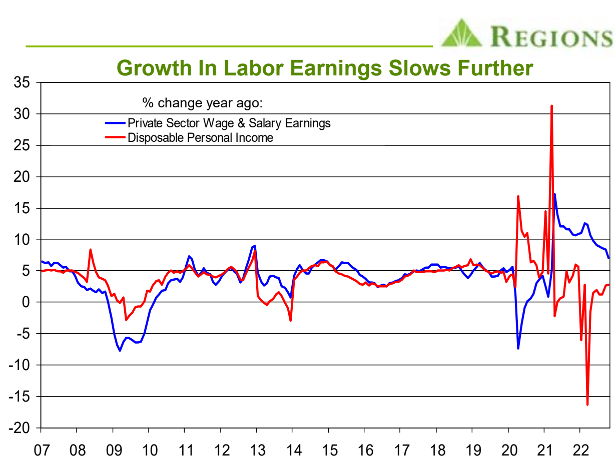
- Personal income rose by 0.7 percent in October, personal spending rose by 0.8 percent, and the saving rate fell to 2.3 percent
- The PCE Deflator rose by 0.3 percent and the core PCE Deflator rose by 0.2 percent in October; on an over-the-year basis, the PCE Deflator is up 6.0 percent and the Core PCE Deflator is up 5.0 percent

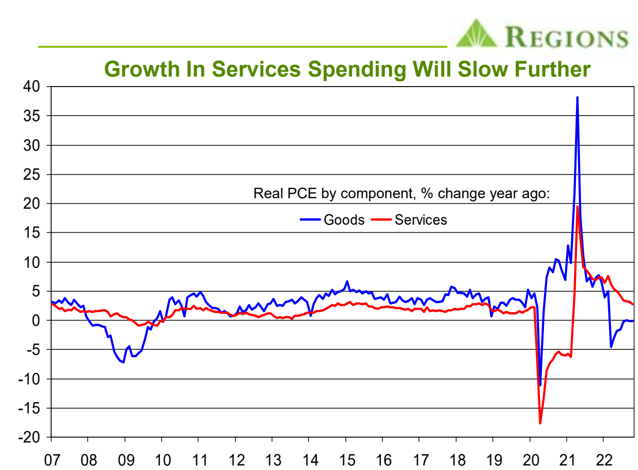
Total personal income rose by 0.7 percent in October, between what we (0.9 percent) and the consensus forecast (0.4 percent) expected, while total personal spending was up by 0.8 percent, matching the consensus forecast but a touch lighter than the 1.0 percent increase we anticipated. With income growth lagging spending growth, the personal saving rate fell to 2.3 percent, though we don't find this a very useful gauge of the state of household finances. A surge in transfer payments, largely reflecting several state governments transferring surplus funds tied to various pandemic relief programs to residents, was the main driver of growth in top-line personal income, though keep in mind that when these payments run their course that will act as a drag on top-line income growth. On the spending side of the ledger, a surprisingly large increase in unit motor vehicle sales contributed to higher spending on consumer durable goods, while higher gasoline prices helped push nominal spending higher. The PCE Deflator, the FOMC's preferred gauge of inflation, rose by 0.3 percent in October, with the core PCE Deflator up by 0.2 percent, both smaller than expected, leaving headline PCE inflation at 6.0 percent and core PCE inflation at 5.0 percent. That inflation is moderating gives the FOMC grounds to wind down its course of Fed funds rate hikes; that inflation remains far above the FOMC's 2.0 percent target, and will for some time to come, means that whatever the terminal funds rate in this cycle proves to be, the funds rate will remain there for some time to come.

Aggregate private sector wage and salary earnings rose by 0.5 percent in October, a smaller increase than we anticipated and the primary culprit in our forecast miss on growth in total personal income. Though to some extent base effects are contributing to decelerating year-on-year growth in aggregate private sector earnings, the slowing pace of job growth is also playing a role. As we routinely note, it is aggregate wage and salary earnings, the product of the number of people working, the number of hours they work, and what they earn for each hour worked, that is the relevant measure of labor costs, despite all of the attention lavished on average hourly earnings. After all, firms manage to total wage bills, not average hourly wages. That growth in total labor earnings is slowing should alleviate the concerns of those who see labor costs as a primary driver of broader inflation pressures. As noted above, the 1.6 percent increase in transfer payments was the primary factor in growth in total personal income in October, and transfers from state governments to their residents should also prop up November personal income. Asset-based income was up a strong 1.0 percent in October, mainly reflecting a jump in dividend income, which was up 1.5 percent.

Nominal spending on goods was up 1.4 percent in October, led primarily by higher spending on motor vehicles and gasoline. At the same time, nominal spending on appliances and apparel fell, which in part reflects lower prices. Total services spending was up by 0.5 percent, falling short of our forecast and easily below the run rate seen over the prior several months. One drag on services spending came in the form of lower prices for utilities, thus holding down nominal outlays. Discretionary services spending, such as travel and dining out, notched a healthy increase in October. This is the segment of services spending that we've been expecting to soften, and while that has not yet been the case, it is nonetheless something to watch in the months ahead.

The PCE Deflator shows that core (consumer goods excluding food and energy) goods prices fell by 0.3 percent in October, the first monthly decline since February 2021. This reflects a steep decline in prices for used motor vehicles and smaller declines in other categories such as appliances & furnishings and apparel. The 4.6 percent year-on-year increase in core goods prices is the smallest such increase in over a year. At the same time, core services prices were up by 0.4 percent in October, smaller than the increases seen in the prior two months, with slower rent growth contributing to the deceleration. Still, core services prices were up 5.1 percent year-on-year, the largest such increase since October 1990. Core services price inflation has been accelerating, thus acting as a counter to decelerating core goods price inflation. But, if we are correct to expect growth in discretionary services spending to slow, that should take some of the steam out of services inflation, which is when we'd expect overall inflation to slow more sharply.





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