ECONOMIC UPDATE
REGIONS
February 24, 2023

January Personal Income/Spending: Still-Solid Growth In Labor Earnings

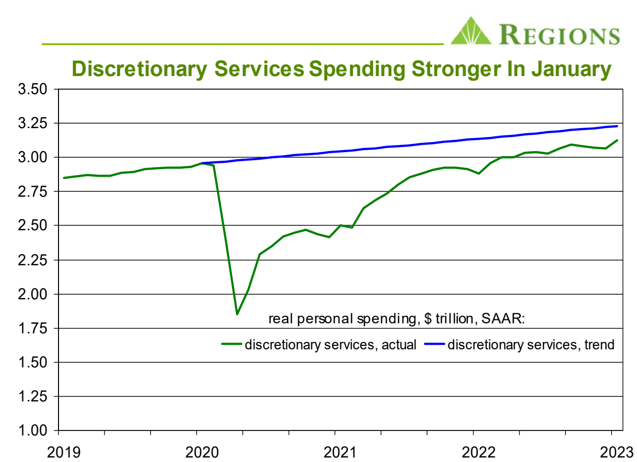
- Personal income rose by 0.6 percent in January, personal spending rose by 1.8 percent, and the saving rate rose to 4.7 percent
- The PCE Deflator rose by 0.6 percent and the core PCE Deflator rose by 0.6 percent in January; on an over-the-year basis, the PCE Deflator is up 5.4 percent and the core PCE Deflator is up 4.7 percent

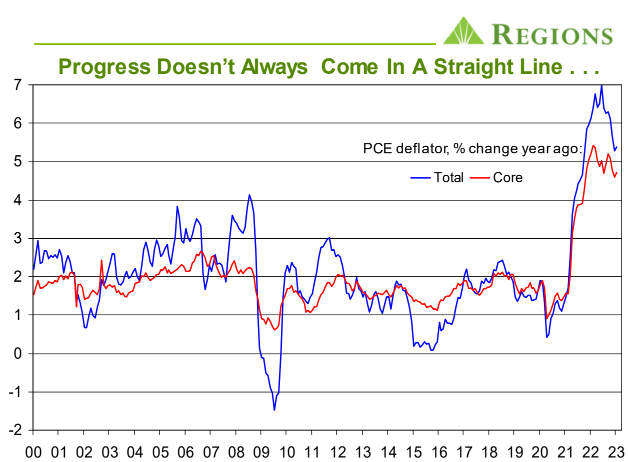
Total personal income rose by 0.6 in January, half the increase our forecast anticipated, while total personal spending rose by 1.8 percent, ahead of our above-consensus forecast of a 1.6 percent increase. Our miss on our forecast of growth in personal income reflects private sector wage earnings and transfer payments falling short of our expectations. The personal saving rate rose to 4.7 percent in January, a fourth straight monthly increase which leaves the saving rate higher than at any point in the past year. The PCE Deflator rose by 0.6 percent in January, matching our above-consensus forecast, and the core PCE Deflator also posted a 0.6 percent increase, topping our above-consensus forecast of a 0.5 percent increase. On an over-the-year basis, the PCE Deflator is up 5.4 percent and the core PCE Deflator is up 4.7 percent. Note that, as with the Consumer Price Index, inflation as measured by the PCE Deflator (headline and core) is now reported to have been faster over the final quarter of 2022 than had previously been reported.

Aggregate private sector wage and salary earnings rose by 1.0 percent in January, below the 1.5 percent increase our forecast anticipated and a considerably smaller increase than implied by the details on earnings and hours worked in the January employment report. That said, the revised Q4 GDP data contain upward revisions to private sector labor earnings over the back half of 2022. As such, even with a smaller January increase than we had banked on, aggregate private sector wage and salary earnings are still up 8.4 percent year-on-year, extending a prolonged run of growth in private sector labor earnings easily outpacing inflation. Transfer payments were flat in January despite the considerable boost from the 8.7 percent cost-of-living adjustment to Social Security benefits. That was to some extent offset by the expiration of the extended Child Tax Credit, or, should we say, the BEA's accounting treatment of the extended Child Tax Credit. At the same time, the transfers of unspent pandemic relief funds from several state governments to their residents seen over the latter months of 2022 having run their course left a sizable gap in transfer payments in the January data. All in all, however, while short-lived "rebate" payments and the BEA's accounting treatments of already-expired programs can impact the monthly change in personal income, as in January, that labor earnings continue to grow at a healthy, and above-inflation, pace is far more relevant in gauging the financial health of U.S. consumers, which is and has been stronger than implied by some of the eye-catching headlines based on the monthly twists in the data.

Nominal spending on goods was up 2.8 percent in January while nominal services spending was up 1.3 percent, a stronger increase than our forecast anticipated. A spike in unit motor vehicle sales yielded an 11.4 percent increase in outlays on motor vehicles, underpinning the 5.5 percent increase in spending on consumer durable goods. Our proxy for discretionary services spending (household spending on services excluding housing, utilities, health care, and financial services) jumped by 1.9 percent in January, but at the same time the declines over the final three months of 2022 are now shown to be larger than was first reported. We would, however, caution that the January spending data, on both goods and services, received a considerable boost from seasonal adjustment. We pointed this out in our analysis of the January data on retail sales, and it is clearly a factor in the reported January increases in categories such as air travel, dining out, lodging, and recreation.

The boost from seasonal adjustment likely carried into the January data on the PCE Deflator, as the sizable increases in the price indexes in the same categories that go into our proxy of discretionary services spending stand out. To be sure, the usual suspects, i.e., rents and energy, helped push the total PCE Deflator higher, but for those focused on core services excluding housing, we think the reported January increases overstate the degree of actual inflation pressures. With the year-on-year increases in both total and core inflation larger in January than in December, it helps to recall that the economic data never move in straight lines, and the trend in inflation is clearly down. If we are correct in arguing that seasonal adjustment has made the January data seem stronger than is actually the case, that will become increasingly apparent as the data for the spring months come in.





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