ECONOMIC UPDATE
REGIONS
August 30, 2019

July Personal Income/Spending: Labor Earnings Underpin Growth In Consumer Spending

- Personal income rose by 0.1 percent in July, personal spending rose by 0.6 percent, and the saving rate fell to 7.7 percent
- The PCE deflator rose by 0.2 percent and the core PCE deflator was up by 0.2 percent in July; year-on-year, the PCE deflator was up by 1.4 percent and the core deflator was up by 1.6 percent

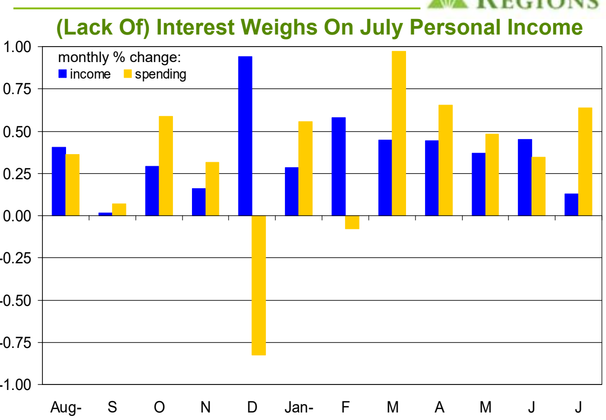
Total personal income rose by 0.1 percent in July, below the 0.3 percent increase we and the consensus expected, while total personal spending rose by 0.6 percent, matching our above-consensus forecast. A sharp decline in interest income took two-tenths of a point off of July income growth, accounting for the miss on our forecast, and revisions show income growth was stronger in June than previously estimated. The PCE Deflator, the FOMC's preferred gauge of inflation, rose by 0.2 percent in July, as did the core PCE Deflator, both matching what we and the consensus expected. On an over-the-year basis, the PCE Deflator is up 1.4 percent and the core PCE Deflator is up 1.6 percent. Real, or, inflation adjusted, personal spending rose by 0.4 percent in July, getting Q3 growth off to a solid start, though it is unreasonable to expect Q3 growth to match the heady pace seen in Q2.

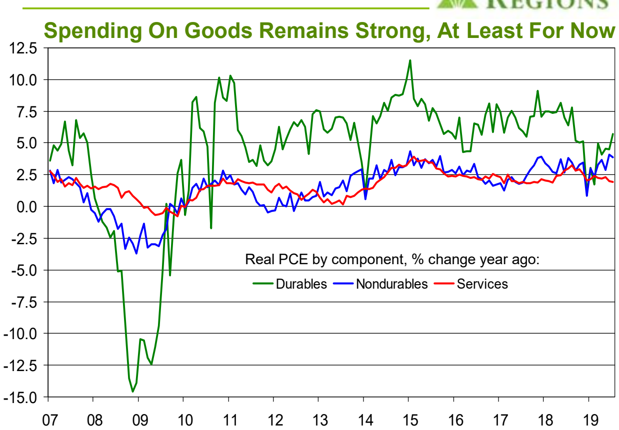
As we anticipated based on the earnings details in the July employment report, the personal income data show only a middling increase in total labor earnings in July. Private sector wage and salary earnings logged a below-trend increase of 0.2 percent, which mainly reflects a one-tenth of an hour decline in the average length of the workweek. As we routinely note, seemingly small one-tenth of an hour changes in the length of the workweek have profound impacts on productive capacity and total labor earnings. Nonetheless, aggregate private sector wage and salary earnings, easily the largest single component of total personal income, are up 5.6 percent year-on-year.

Nonfarm proprietors' income (up 0.6 percent), dividend income (up 0.6 percent), and rental income (up 0.5 percent) lent support to growth in total personal income in July. After having been notably weak in late-2018 and early-2019, growth in nonfarm proprietors' income, a proxy for small business profits, has rebounded smartly in recent months, though small businesses are still vulnerable to faster growth in labor costs amidst what remains a fairly weak pricing environment. The support for growth in total personal income from these sources, however, was largely undone by a 1.8 percent decline in interest income which, even if the declines are not as severe, we suspect will carry into the data for August and September.

Clearly, weakness in interest income punishes savers and those who are more dependent on interest income. In general, however, it is labor income that underpins growth in consumer spending, which helps account for why consumer spending has remained fairly robust. Total personal spending was up by 0.6 percent in July, with spending on consumer durables up by 0.6 percent, spending on nondurable goods up by 1.1 percent, and spending on services (which accounts for roughly two-thirds of total consumer spending as measured in the GDP data) up by 0.5 percent. Growth in spending on consumer durables has been broad based, with spending on household furnishings and appliances having been strong over recent months. Abnormally high temperatures across much of the U.S. in July led to sharply higher spending on household utilities, which added one-tenth of a point to growth in top—line consumer spending. Higher retail gasoline prices and Amazon Prime Day, which was two days this year, supported growth in spending on nondurable consumer goods in July. Even after accounting for price changes, however, spending was strong in July. What will be worth watching over coming months will be the extent to which tariffs are applied to imported consumer goods and how much of the tariffs will be passed along to consumers in the form of higher prices. It could be that spending shifts away from goods and more toward services, thus mitigating any effects on total consumer spending.

Inflation pressures remain muted as measured by the PCE Deflator. As of yet, core goods prices remain weak, with July marking the 81st consecutive month in which core goods prices as measured in the PCE Deflator were down on an over-the-year basis. That could, and likely will, change due to tariffs which, don't forget, offer producers outside of China the chance to raise their prices. Still, the effects will be more pronounced in the CPI data than in the PCE Deflator, as the CPI measures the cost of a fixed basket of goods. This goes to our earlier point about shifts in consumption patterns. More broadly, however, inflation is unlikely to be a concern for the FOMC any time soon.





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