ECONOMIC UPDATE

REGIONS

March 26, 2021

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February Personal Income/Spending: February's Declines Will Be Easily Reversed In March

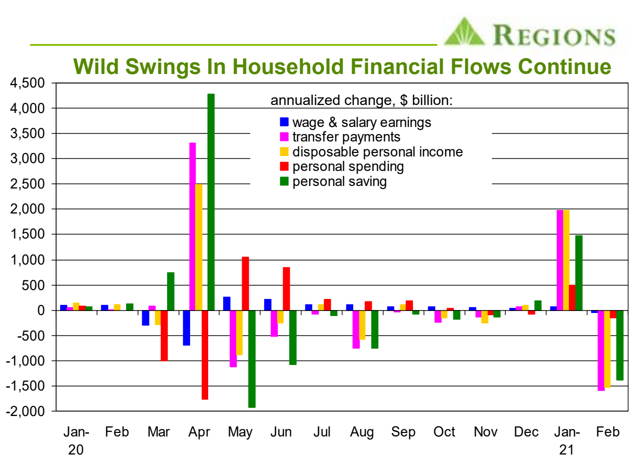
- Personal income <u>fell</u> by 7.1 percent in February, personal spending <u>fell</u> by 1.0 percent, and the saving rate <u>fell</u> to 13.6 percent
- The PCE Deflator <u>rose</u> by 0.2 percent and the core PCE Deflator <u>rose</u> by 0.1 percent in February; on an over-the-year basis, the PCE Deflator was <u>up</u> by 1.6 percent and the core PCE Deflator was <u>up</u> by 1.4 percent

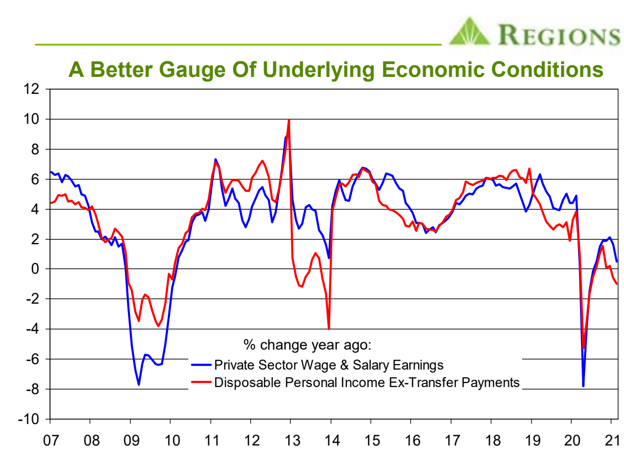
Total personal income declined by 7.1 percent in February, matching our forecast and slightly smaller than the consensus forecast of a 7.2 percent decline. Total personal spending fell by 1.0 percent, slightly larger than the 0.9 percent decline we anticipated and the consensus forecast of a 0.8 percent decline. With the steep decline in income more than offsetting the decline in spending, the personal saving rate fell from 19.8 percent in January to 13.6 percent in February. Recall that personal income rose by 10.1 percent in January, reflecting the second round of Economic Impact Payments being largely distributed during the month, so February's decline in income simply reflects the reversal in transfer payments. The decline in spending partly reflects the extent to which spending was curtailed by the unusually harsh winter weather that pummeled much of the nation during February, though for a second straight month services spending underperformed our forecast. In a sense, the February declines in income and spending seem like old news, in that by all accounts spending has rebounded smartly in March while personal income will be bolstered by the distribution of the third round of Economic Impact Payments. As such, the March saving rate will likely top January's 19.8 percent rate, setting the stage for a significant burst of spending in the months ahead as a greater share of the population is vaccinated and the economy more fully reopens.

The \$1.517 trillion decline in personal income was more than accounted for by a \$1.584 trillion decline in transfer payments (recall the personal income data are reported on an annualized basis). In January, the second round of Economic Impact Payments (EIP) added \$1.661 trillion (again, annualized) to transfer payments; the remaining \$95.9 billion of second round EIP funds was distributed in February, leaving the net change in EIP for February at -\$1.565 trillion. As noted above, the distribution of the third round of EIP, reflecting payments of up to \$1,200 for each qualified recipient, will lead to a much larger increase in transfer payments than that seen in January, and our back of the envelope calculation shows total personal income rising by better than 20 percent in March on the third round of EIP alone. The first chart below shows the pronounced swings in household financial flows over the course of the pandemic, with even bigger swings in personal income and personal saving in the March data.

One can argue that the sharp swings in top-line personal income are deflecting attention away from the underlying health of the economy, particularly the recovery in the labor market. For instance, private sector wage and salary earnings were flat in February. While this may seem at odds with private sector nonfarm payrolls having risen by 465,000 jobs, the bulk of that increase came in leisure and hospitality services, the private sector industry group with the lowest average hourly earnings and the shortest average workweek. To the extent that this industry group sees the most significant increases in employment over coming months as the economy more fully reopens, that could act as somewhat of a drag on growth in private sector wage and salary earnings, the largest single component of personal income. Still, as of January private sector labor earnings had surpassed their pre-pandemic peak and will continue to solidify in the months ahead, setting a firmer foundation for growth in total personal income. That said, disposable (after-tax) personal income excluding transfer payments remains 1.0 percent below its pre-pandemic peak, with many households still reliant on transfer payments such as EIP funds and unemployment insurance benefits.

February's decline in personal spending would have been more severe had the personal saving rate not been so elevated. Total consumer spending on goods fell by 3.0 percent in February, with spending on consumer durable goods down by 4.7 percent and spending on nondurable consumer goods down by 2.7 percent. Spending on services, which accounts for the bulk of total consumer spending, was up just 0.1 percent and it took a jump in utilities outlays to notch that paltry gain. Just as leisure and hospitality services is the biggest remaining gap in the labor market, it is also the largest remaining gap in consumer spending. The third round of EIP and more widespread vaccinations should combine to close much of that gap in the months ahead.





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