ECONOMIC UPDATE

REGIONS

October 29, 2021

September Personal Income/Spending: Labor Earnings Remain Strong

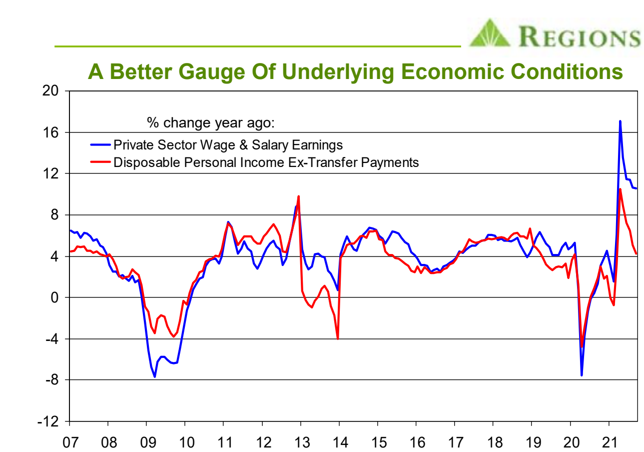
- Personal income fell by 1.0 percent in September, personal spending rose by 0.6 percent, and the saving rate fell to 7.5 percent
- The PCE Deflator rose by 0.3 percent and the core PCE Deflator rose by 0.2 percent in September; on an over-the-year basis, the PCE Deflator is up 4.4 percent and the core PCE Deflator is up 3.6 percent

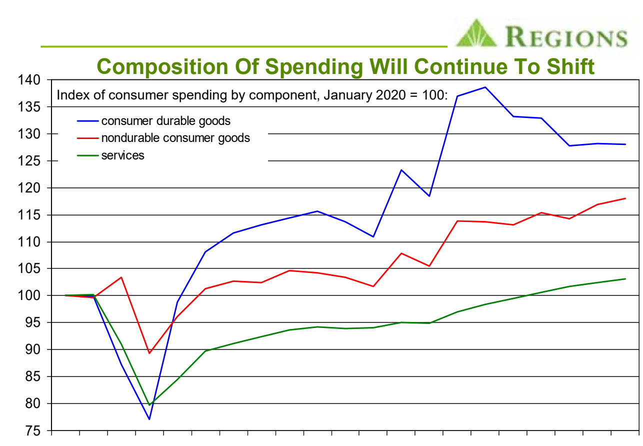
Total personal income fell by 1.0 percent in September, a steeper drop than our forecast of a 0.7 percent decline and the consensus forecast of aa 0.2 percent decline. Total personal spending rose by 0.6 percent, bettering our forecast of a 0.5 percent increase. At the same time, the prior estimate of personal spending in August was revised higher, now showing a 1.0 percent increase rather than the 0.8 percent gain initially reported. With personal income having fallen and spending having risen in September, the personal saving rate fell to 7.5 percent from 9.2 percent in August. At 7.5 percent, the personal saving rate is now not too far above the pre-pandemic norm, though we think the decline in September is somewhat exaggerated. The PCE Deflator rose by 0.3 percent in September, with the core PCE Deflator up by 0.2 percent, yielding year-on-year increases of 4.4 percent and 3.6 percent, respectively. Adjusted for inflation, total consumer spending rose by 0.3 percent in September.

While the September data on personal income and spending were built into yesterday's release of the initial estimate of Q3 GDP, they still merit examination, as the September data set the jumping off point for the Q4 data. On that basis, the stage is set for another quarter of middling growth in inflation-adjusted consumer spending. Spending on consumer durable goods such as motor vehicles, appliances, and home furnishings fell by 0.2 percent on a nominal basis in September and by 0.6 percent on an inflation-adjusted basis. This comes as no surprise as consumer durables are where inventory constraints are more pressing and, as such, are acting as a more meaningful drag on spending. September's decline means the level of real spending on consumer durable goods ended Q3 below the quarterly average, setting the stage for a further decline in Q4. At the same time, growth in consumer spending on services slowed sharply in August and September, which mainly reflects changes in consumer spending patterns amid the spike in COVID cases. The level of real spending on services ended Q3 marginally ahead of the quarterly average, which suggests a much smaller annualized increase in Q4 than the 7.9 percent increase logged in Q3. But, unlike spending on consumer durable goods, we see more upside for Q4 growth in services spending. With the worst of the spike in COVID cases behind us, the higher frequency indicators of consumer spending show services spending picked up considerably in October and we think that momentum will carry into the final two months of the year, particularly to the extent that lean supplies of goods lead consumers to alter holiday season spending patterns, i.e., spend less on goods and more on services than they otherwise would.

As we noted in our weekly *Economic Preview*, the personal income data are likely to be somewhat noisy in the near term as transfer payments continue to normalize, but changes in labor earnings will be a much more revealing indicator of the underlying trends in personal income. That is apparent in the September data. Private sector wage and salary earnings, the largest single component of personal income, posted another healthy advance in September, rising by 0.9 percent, which leaves them up 10.6 percent year-on-year. That increase, however, was swamped by a 7.0 percent decline in transfer payments and a sharp decline in farm income. The larger than expected declines in these two components account for our miss on our forecast of personal income. The end of the supplemental unemployment insurance benefits on September 5 was the primary culprit behind the steep decline in transfer payments; total unemployment insurance benefit payouts fell by $254.6 billion on an annualized basis. Natural runoff from the rolls of unemployment insurance benefits and the winding down of Economic Impact Payments will act as drags on transfer payments over coming months, and January will see a sizable decline after the monthly Child Care Tax Credit installments come to an end in December. So, it will be more important to focus on patterns in labor earnings as a better gauge of the trends in personal income.

While the monthly changes in the PCE Deflator have moderated, the year-on-year changes remain stout. Nothing we've heard on earnings calls leads us to expect much relief in the months ahead, particularly with the largest-ever increase in the Employment Cost Index in Q3.





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