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## February Personal Income/Spending: Solid Growth In Labor Earnings Provides Support

- › Personal income rose by 0.5 percent in February, personal spending rose by 0.2 percent, and the saving rate rose to 6.3 percent
- › The PCE Deflator rose by 0.6 percent and the core PCE Deflator rose by 0.4 percent in February; on an over-the-year basis, the PCE Deflator is up 6.4 percent and the core PCE Deflator is up 5.4 percent

Total personal income rose by 0.5 percent in February, in line with the consensus forecast and above the 0.4 percent increase we expected, while total personal spending rose by 0.2 percent, lagging our forecast of a 0.3 percent increase and the consensus forecast of a 0.5 percent increase. With income growth outpacing spending growth, the personal saving rate ticked higher, rising to 6.3 percent from January’s rate of 6.1 percent. The PCE Deflator rose by 0.6 percent and the core PCE Deflator rose by 0.4 percent, each matching our forecast, which yields year-over-year increase of 6.4 percent and 5.4 percent, respectively. With the increase in the PCE Deflator outpacing the increase in nominal consumer spending, real spending fell by 0.4 percent in February. That said, the initial estimate of January consumer spending was revised higher, now pegged at a 2.7 percent increase rather than the 2.1 percent gain first reported, with real (inflation adjusted) spending up by 2.1 percent rather than the 1.5 percent increase initially reported. This leaves annualized growth in real consumer spending at 3.9 percent thus far in Q1, a step up from 2.5 percent growth in Q4 2021.

Aggregate wage and salary earnings rose by 0.8 percent in February, matching our forecast, with private sector earnings up by 0.9 percent and public sector earnings up by 0.4 percent. On an over-the-year basis, private sector wage and salary earnings were up 12.6 percent as of February, which reflects not only stepped-up growth in average hourly earnings but also sizable increases in aggregate hours worked – the product of the number of people working and the number of hours they work. As we’ve noted over recent months, robust growth in private sector labor earnings, the largest single component of personal income, is countering the effects of pandemic-related transfers having run their course. As can be seen in our first chart below, these transfers washing from the data has left a void in disposable (i.e., after-tax) personal income, but ex—transfers income is more than holding its own thanks to a steadily improving labor market. While transfer payments were once again a drag on total personal income in February, that drag was slightly less powerful than our forecast anticipated, thanks to the level of Child Tax Credit payouts. Our miss on transfer payments accounts

for our miss on our forecast of top-line income growth.

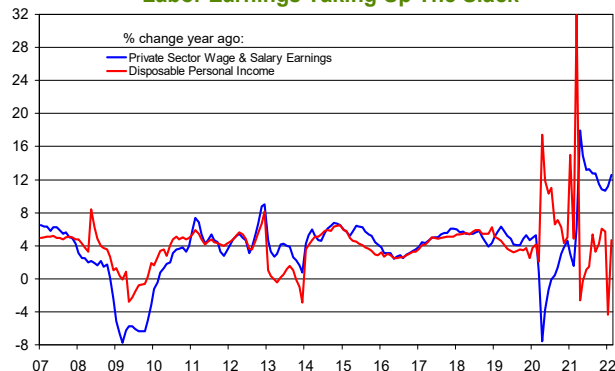
Our below-consensus forecast for total personal spending was premised on growth in services spending more than offsetting lower spending on goods. While the 0.9 percent increase in consumer spending on services in February matched our forecast, spending on goods fell a bit more than we anticipated. Spending on consumer durable goods fell by 2.5 percent in February, with steep declines in spending on motor vehicles and home furnishings/appliances. A 6.5 percent increase in spending on gasoline, a function of sharply higher prices, was not enough to salvage consumer spending on nondurable goods, as spending fell across the other main categories. The net result was a 0.1 percent decline in total spending on nondurable consumer goods. A strong increase in spending on food services and accommodations, up 3.0 percent, was a prime contributor to the 0.9 percent increase in spending on services, with increases in spending on recreation, entertainment, and health care also contributing, while lower utilities outlays acted as a modest drag.

While higher prices are contributing to growth in nominal spending, it is likely that sharply higher prices for food, energy, and shelter are holding down growth in discretionary spending. At the same time, we think that we are seeing a rotation in overall consumer spending, away from goods and toward services. As COVID case counts have subsided, consumers have gravitated back toward spending on travel, tourism, dining out, recreation, and entertainment. That said, we think it is still early in this process and, as indicated in our second chart below, there is much further to go. This rotation is likely to remain a drag on spending on goods over coming months.

Though the inflation readings in the February data did not come as a surprise, that likely won’t make them any less uncomfortable for the FOMC. At 6.4 percent, PCE inflation at its highest since January 1982, and coming months are unlikely to bring meaningful relief. Higher food and energy prices stemming from Russia’s invasion of Ukraine and renewed global supply chain impediments stemming from shutdowns in China figure to sustain inflation pressures for some time to come.



### Labor Earnings Taking Up The Slack



### Composition Of Spending Will Continue To Shift

