ECONOMIC UPDATE
REGIONS
April 29, 2022

March Personal Income/Spending: Solid Growth In Labor Earnings A Critical Support

- Personal income rose by 0.5 percent in March, personal spending rose by 1.1 percent, and the saving rate fell to 6.2 percent
- The PCE Deflator rose by 0.9 percent and the core PCE Deflator rose by 0.3 percent in March; on an over-the-year basis, the PCE Deflator is up 6.6 percent and the core PCE Deflator is up 5.2 percent

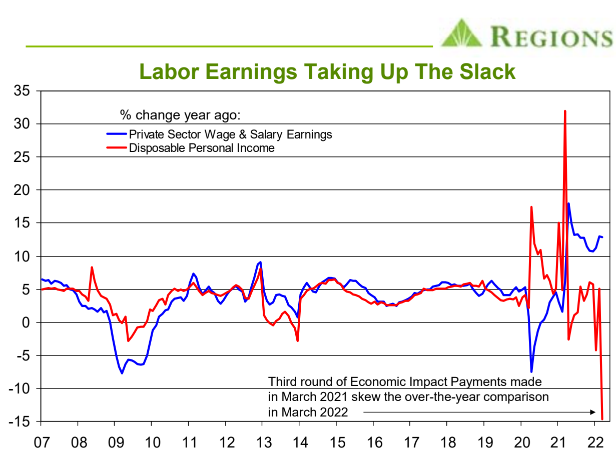
Total personal income rose by 0.5 percent in March, matching our above-consensus forecast, while total personal spending rose by 1.1 percent, topping our above-consensus forecast. With income growth lagging spending growth, the personal saving rate declined, falling to 6.2 percent in March from 6.8 percent in February. The PCE Deflator, the FOMC's preferred gauge of inflation, rose by 0.9 percent while the Core PCE Deflator rose by 0.3 percent, each matching what we and the consensus expected. On an over-the-year basis, the PCE Deflator is up 6.6 percent as of March, the largest such increase since January 1982, while the Core PCE Deflator is up 5.2 percent. While the March data on personal income and spending were incorporated into yesterday's release of the BEA's initial estimate of Q1 GDP, today's release shows the monthly patterns, with the initial estimate of personal income growth in February revised up from 0.5 percent to 0.7 percent and growth in January revised up from 0.1 percent to 0.2 percent.

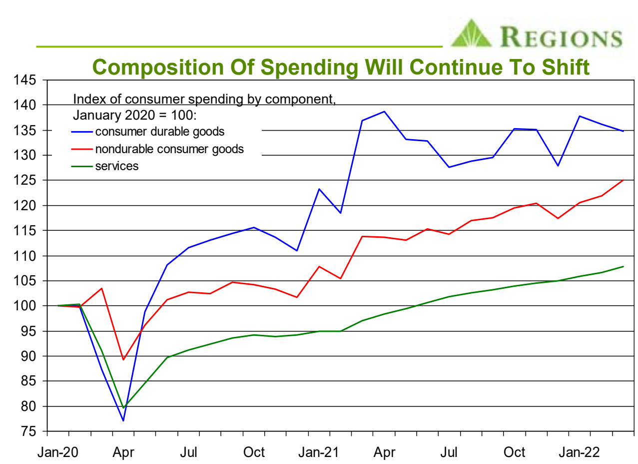
Aggregate wage and salary earnings rose by 0.6 percent in March, matching our forecast. That private sector earnings growth fell short of the 1.1 percent increase in February (revised up from 0.9) reflects the impact of the drop in average weekly hours worked, but March's increase nonetheless leaves them up 12.8 percent year-on-year. As we often note, while most zero in on average hourly earnings as a guide to patterns in personal income and spending, it is aggregate wage and salary earnings – the product of the number of people working and the number of hours they work – that are the driving force, as this is far and away the largest single component of total personal income. With pandemic-related transfer payments having run their course, healthy growth in labor earnings is putting a floor under income growth and acting as a support for spending. Transfer payments did rise by 0.3 percent in March, though this is mainly a function of growth in Medicare and Medicaid payments, which are made to service providers as opposed to reflecting cash in consumers' pockets. Rental income was up 0.7 percent in March, continuing a run of solid advances which we expect to persist over coming months, and interest income was up 0.5 percent. Nonfarm proprietors' income, a proxy for small business profits, was flat in March after rising by 0.8 percent in February. Looking over the past several months, however, it is the February reading that is the outlier in a string of weak readings. This could reflect small businesses having less capacity to pass along higher costs for labor and other inputs along to customers in the form of higher prices than is the case with larger corporations.

Our above-consensus forecast for personal spending was premised on higher prices, particularly gasoline prices, pumping up spending on nondurable goods which, along with stronger growth in spending on services, would offset a decline in spending on consumer durable goods. These things played out, though spending on both services and nondurable consumer goods grew by more than we anticipated. After accounting for price changes, however, total consumer spending rose by just 0.2 percent in March, with services more than accounting for the increase. On an inflation-adjusted basis, spending on consumer durable goods fell by 0.9 percent in March, spending on nondurable consumer goods fell by 0.3 percent, and services spending rose by 0.6 percent.

We look for further shifts in consumer patterns in the months ahead, favoring services at the expense of goods. With the exception of motor vehicles, we think there to be little pent-up demand for consumer durable goods left to be unleashed, and lean inventories will continue to weigh on vehicle sales. At the same time, higher interest rates raise the effective cost of consumer durable goods. Softer spending on consumer durables will hold down overall spending on goods at the same time we are seeing the release of considerable pent-up demand for services, such as travel, dining out, recreation, and entertainment. While not immune to higher prices, services spending has picked up markedly, which we think has further to run.

Elevated inflation will keep the FOMC on a faster track in raising the Fed funds rate, with the Committee looking past the contraction in real GDP in Q1. Renewed global supply chain impediments stemming from shutdowns in China could sustain inflation pressures for longer than would have otherwise been the case.





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