ECONOMIC UPDATE

REGIONS

August 31, 2023

July Personal Income/Spending: A Last Hurrah For Consumer Spending?

- Personal income rose by 0.2 percent in July, personal spending rose by 0.8 percent, and the saving rate fell to 3.5 percent
- The PCE Deflator rose by 0.2 percent and the core PCE Deflator rose by 0.2 percent in July; on an over-the-year basis, the PCE Deflator is up 3.3 percent and the core PCE Deflator is up 4.2 percent

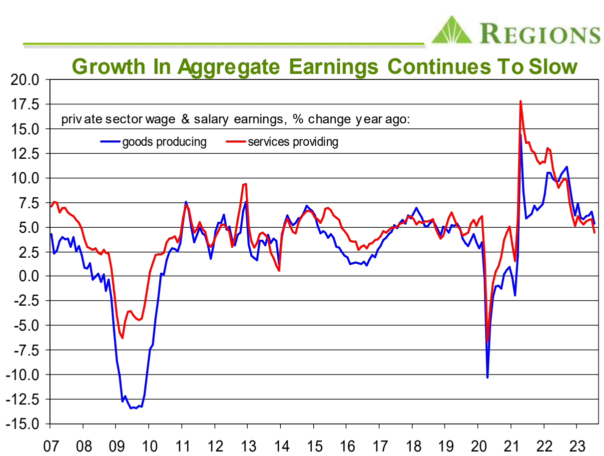
Total personal income rose by 0.2 percent in July, below what we and the consensus expected, while total personal spending rose by 0.8 percent, matching our above-consensus forecast. With spending growth outpacing income growth, the personal saving rate fell to 3.5 percent in July from 4.3 percent in June. The PCE Deflator, the FOMC's preferred gauge of inflation, rose by 0.2 percent in July, as did the core PCE Deflator, both as we and the consensus expected. This puts the total PCE Deflator up 3.3 percent year-on-year, up from the 3.0 percent increase in June, while the core PCE Deflator is up 4.2 percent year-on-year, up from the 4.1 percent increase in June. Services price inflation checked in at 5.2 percent in July, accelerating from June, while prices for both durable and nondurable consumer goods were down year-on-year. The solid increase in real consumer spending, up 0.6 percent in July, sets a base for Q3 spending growth to be significantly faster than that seen in Q2, which in turn will boost Q3 real GDP growth. That said, July's pace of spending growth is highly unlikely to be sustained, which we expect to be apparent by the end of Q3 as we expect a marked deceleration in discretionary services spending. If so, real consumer spending will be virtually flat in Q4, which in turn will set up a weak Q4 real GDP growth print.

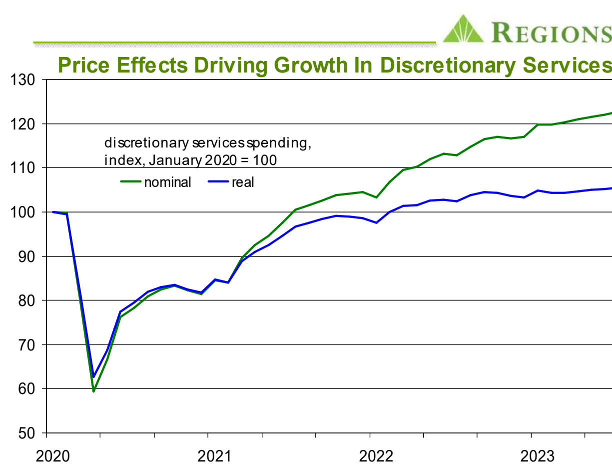
Aggregate wage and salary earnings rose by 0.4 percent in July. Across the private sector, earnings amongst goods producing industries were up by 0.5 percent, driven by construction, while earnings amongst services providing industries were up by 0.3 percent, half of June's increase. Earnings in the broad trade, transportation, and utilities industry group were up just 0.1 percent, and while that comes off a 0.9 percent increase in June, it is the June number that is the outlier. Payrolls in transportation and warehousing services have contracted over the past several months, thus weighing on earnings growth in the broader industry group. As seen in the chart below, growth in aggregate earnings across both the goods producing and the services providing industries has slowed to a pace consistent with pre-pandemic growth, though inflation was obviously much slower then than is the case at present. Either way, we expect to see further deceleration in earnings growth in the months ahead. Rental income, up 1.1 percent, and proprietors' income, up 0.5 percent, were the other main supports for July income growth. Transfer payments, however, logged the third decline in the past four months as many states continue to trim Medicaid roles.

Total consumer spending was up by 0.8 percent in July, with spending on goods up 0.7 percent and spending on services up 0.8 percent. Spending on consumer durable goods rose by 0.7 percent, outperforming the retail sales data, particularly in the appliances and home furnishings categories. Though watered down by declining gasoline sales, spending on nondurable consumer goods also notched a 0.7 percent increase in July, with healthy increases amongst grocery and personal care stores. With goods prices having fallen in July, real consumer spending on goods rose by 0.9 percent, the largest such increase since January.

As noted above, total services spending was up by 0.8 percent in July, though after accounting for higher services prices the increase is 0.4 percent. In nominal terms, spending on household utilities jumped by 2.7 percent, largely reflecting the effects of punishingly hot weather across much of the nation in July. Spending on financial services, more of an imputed than actual figure, was reported to have risen by 2.7 percent in July. Our proxy for discretionary service spending rose by 0.5 percent, which translates into a 0.3 percent increase on an inflation-adjusted basis. Spending on entertainment, driven by large-scale concert tours and a couple of box office blockbusters, was strong, though the late-July movie releases mean the August data could also be boosted on this front. Keep in mind that the concert tours also propped up spending on travel and lodging, both of which were up big in July. As we have for some time now, we continue to expect discretionary services spending to slow sharply with the end of the summer.

Higher food and energy prices will push headline inflation sharply higher in the August data, but the FOMC will be more focused on core inflation, which is proving to be frustratingly persistent. For now, discretionary services continue to contribute to robust services price inflation, but if we are correct on the spending front, this should follow though to prices.





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