ECONOMIC UPDATE

REGIONS

June 27, 2025

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May Personal Income/Spending: No Real Surprises Here, At Least There Shouldn't Be . . .

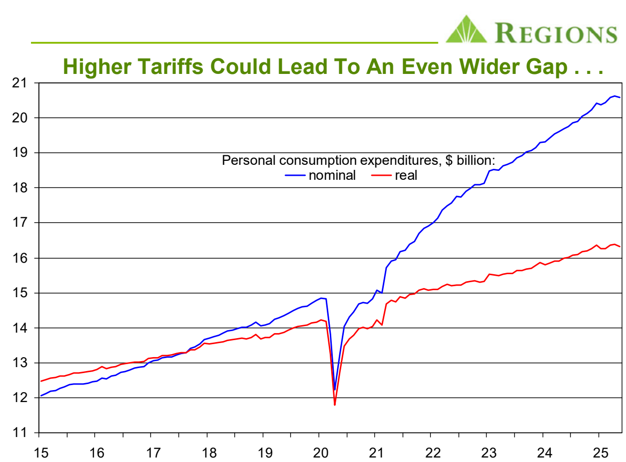
- Personal income fell by 0.4 percent in May, personal spending fell by 0.1 percent, and the saving rate fell to 4.5 percent
- The PCE Deflator was up by 0.1 percent and the core PCE Deflator was up by 0.2 percent in May; on an over-the-year basis, the PCE Deflator is up 2.3 percent and the core PCE Deflator is up 2.7 percent

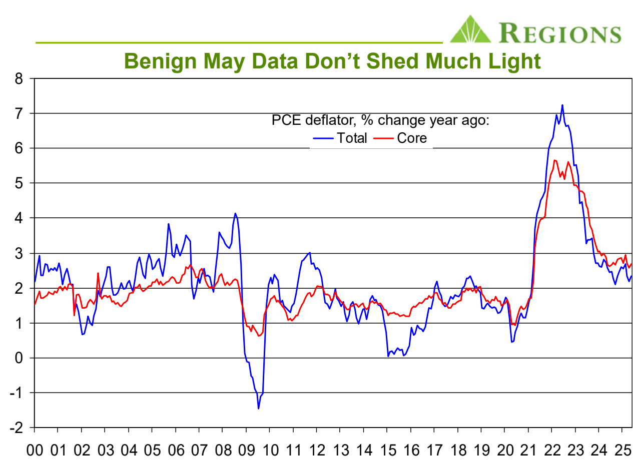
Total personal income fell by 0.4 percent in May, contrary to our forecast of a 0.2 percent increase and the consensus forecast of a 0.3 percent increase. At the same time, personal spending fell by 0.1 percent, a touch lighter than our below-consensus forecast which anticipated spending being flat. Though both income and spending fell short of our forecasts, we don't see much in the May data that is surprising, though judging from some of the reactions we've seen thus far, plenty of people seem to find plenty of surprises in the data. The shortfall in income is entirely due to a steep decline in transfer payments, which is simply the flip side of the increases seen over the prior two months reflecting retroactive payments to certain former public sector workers under the *Social Security Fairness Act*. We pointed this out in this week's *Economic Preview* and noted that, while our forecast anticipated a decline in transfer payments weighing on May income growth, we were just not sure about the magnitude of that decline, which turned out to be larger than incorporated into our forecast. We also noted that our forecast anticipated a trend-like increase in labor earnings, which is what the May data show. On the spending side, our forecast anticipated a sharp drop in goods spending offsetting a gain in services spending. Though the decline in goods spending matched our forecast, the gain in services spending was a touch lighter than we anticipated, hence our miss on our forecast of spending growth. The PCE Deflator was up by 0.1 percent in May, while the core PCE Deflator was up by 0.2 percent, each matching our forecast though the latter was above the consensus forecast. The May increases translate into year-on-year increases of 2.3 percent and 2.7 percent, respectively, with still only limited evidence of pass-through effects from higher tariffs and leaving open the question of whether we just haven't seen such increases yet or they're just not coming. We think it's the former, not the latter.

After rising by 2.5 percent in April, transfer payments fell by 2.2 percent in May. As noted above, retroactive payments under the *Social Security Fairness Act* pushed Social Security payouts up by 3.7 percent in March and 6.9 percent in April, whereas May saw payouts drop by 7.3 percent, and these swings account for the swings in total transfer payments (Social Security payments account for roughly one-third of all transfer payments) We think it worth noting the firming trend in unemployment insurance benefits over recent months, which is in keeping with the weekly data showing continuing claims for benefits, a count of the number of people drawing benefits, trending higher. At the same time, however, aggregate private sector wage and salary earnings were up by 0.4 percent in May. While trend growth has slowed along with the slowing pace of job growth, aggregate private sector wage and salary earnings are up 4.6 percent year-on-year, still comfortably outpacing inflation. Though most of the categories of personal income were in line with our forecast, we were surprised by the 0.4 percent decline in nonfarm proprietors' income, a proxy for small business profits, which ended a run of solid advances.

Spending on consumer durable goods fell by 1.8 percent in May, with steep declines in spending on motor vehicles and appliances. These declines, however, follow sharply higher outlays over prior months when consumers were pulling purchases forward to avoid tariff-related price hikes. In that sense, May's declines should be neither surprising nor concerning. Services spending rose by just 0.1 percent, with our proxy of discretionary services spending falling by 0.1 percent, continuing a trend of softness in such spending, with spending on air fares, lodging, and dining out falling in May. Recall that in the BEA's third pass of the Q1 GDP data, prior estimates of services spending were revised sharply lower, and the monthly data suggest no reversal in the weakness in discretionary services spending that we began pointing to in late-2024.

Prices for core (non-food, non-energy) consumer goods were up by 0.2 percent in May, and while that's smaller than April's 0.3 percent increase, lower prices for both new and used motor vehicles were a stiff drag on the May data. In other categories of consumer durable goods, prices have firmed considerably over the past two months. Either way, core goods prices are up 0.7 percent year-on-year, and while that may not seem like much, it is the largest such increase since July 2023. Still, slowing core services price inflation is acting as a counter in terms of the increase in the total PCE Deflator, which we think will remain the case.





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