ECONOMIC UPDATE

REGIONS

January 31, 2013

December Personal Income/Spending: Paying It Forward In December, Payback In January

- Personal income rose by 2.6 percent in December, personal spending rose by 0.2 percent, and the savings rate jumped to 6.5 percent.
- The PCE deflator was flat, with the core PCE deflator up by 0.1 percent in December. On a year-over-year basis, the PCE deflator was up by 1.3 percent and the core deflator was up by 1.4 percent.

Sure, all dividends are special, but some are more special than others. Particularly those paid out in December 2012 in order to beat higher tax rates on investment income in 2013. Thanks to a 34.3 percent increase in dividend income and accelerated bonus payments in advance of higher personal income tax rates on higher income households, total personal income surged by 2.6 percent in December. To find a like-sized monthly increase in personal income, one needs to go back to December 2004 when another special dividend payment – courtesy of Microsoft – boosted total personal income by better than three percent.

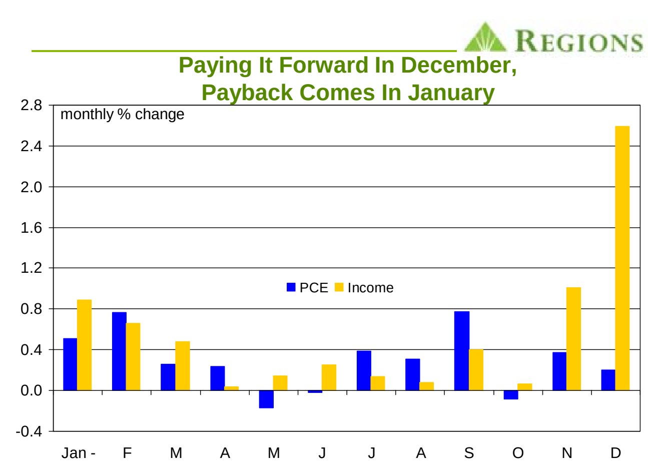
The impact of these higher dividend payments is felt throughout the December data. Real disposable personal income was up by 2.8 percent month-to-month and up 5.6 percent on an over-the-year basis, with the jump in income pushing the personal saving rate up to 6.5 percent.

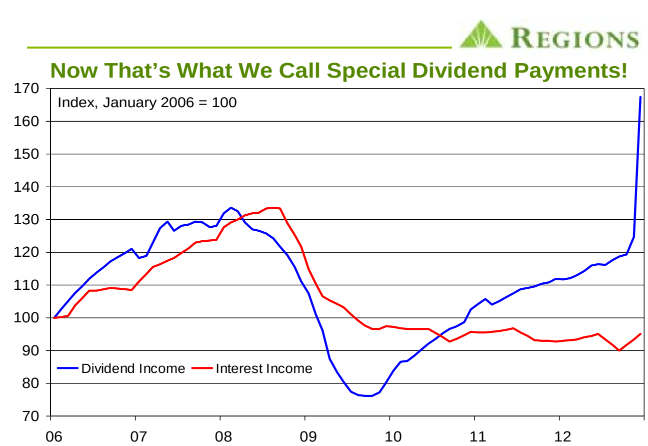
The obvious reaction may be to cast aside December's growth in personal income in December as a one-off anomaly, but in doing so one would overlook what, at least to us, is an encouraging development. Private sector wage and salary earnings followed up a 1.1 percent increase in November with a 0.8 percent increase in December, the best back-to-back growth since 2006. Earnings in the government sector continue to flat line, reflecting ongoing job losses in the public sector. A better (at least slightly) pace of job growth, increased hours worked, and growth in jobs in goods producing industries all combined to boost the pace of private sector earnings growth late in 2012. This is worth noting, as what had been slow growth in earnings, the largest single component of personal income, had been acting as a drag on overall personal income growth. While we do not anticipate monthly gains in private sector earnings to continue at the pace seen in November and December over coming months, what should be a faster pace of job growth will contribute to better earnings growth than seen over much of 2012, thus supporting better overall income growth.

Another reason to not totally dismiss the jump in dividend income seen in December is that, over the longer term, growth in dividend income has easily outpaced growth in interest income, as seen in the second chart below. December's dividend bonanza notwithstanding, dividend income has rebounded smartly from the plunge seen during the 2007-09 recession, while low interest rates have meant that interest income is still well below its precious cyclical peak. There are of course some who insist that low interest rates are not punishing savers, perhaps they prefer to see it as encouraging people to buy stocks instead.

On the spending side of the ledger, December was pretty much of a dud by comparison. Total personal consumption expenditures (PCE) managed only a 0.2 percent increase, concentrated in spending on consumer durable goods, up by 1.0 percent on the strength of motor vehicle sales. There were some price effects in play in December – mainly due to lower gasoline prices, the PCE deflator was flat (down slightly on an unrounded basis), but these effects were minor, with real PCE up by 0.244 percent, unrounded, compared to the 0.200 percent gain in nominal spending. Still, for Q4 2012 as a whole, real consumer spending grew by 2.2 percent, a faster pace than seen during Q3.

January's income data will of course not look nearly as nice as December's. Not only will there be a sharp reversal in dividend income, but the higher payroll tax rates that took effect on January 1st will take a bite out of personal income as well. Should we see a smaller gain in private sector earnings, which we do expect to be the case, then we could see a month-to-month decline in personal income on the order of three percent for January. This will, in turn, have implications for consumer spending – don't be misled by the jump in the personal saving rate in December, as that will be highly concentrated amongst those households with dividend income. Many lower-to-middle income households, lacking such a cushion, will be forced to pare back on discretionary spending. For Q1 as a whole, growth in real consumer spending will be considerably slower than that seen during Q4 2012, though growth should pick up over the remainder of 2013.





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