



Economics Group

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Personal Income Growth Amid Modest Spending

Personal income rose 0.2 percent in March after increasing 1.1 percent in February. Personal spending rose 0.2 percent, signaling a downshift in underlying consumer spending that will likely continue in Q2.

Real Disposable Personal Income Continued to Fall

Personal income growth downshifted in March but remained positive, rising 0.2 percent for the month. Total compensation also rose 0.2 percent with wage and salary growth increasing 0.2 percent for the month. Dividend income, which had been a source of strength in income growth in February, rose a more modest 0.6 percent. In the wake of higher taxes from the fiscal cliff deal enacted in January, real disposable income growth declined 5.3 percent in the first quarter. When transfer payments, such as social security and unemployment benefits are excluded, real personal income rose 0.4 percent in March. Consumers' saving rate downshifted in the first quarter as consumers chose to reduce their pace of saving in order to adjust to slower income growth and higher taxes.

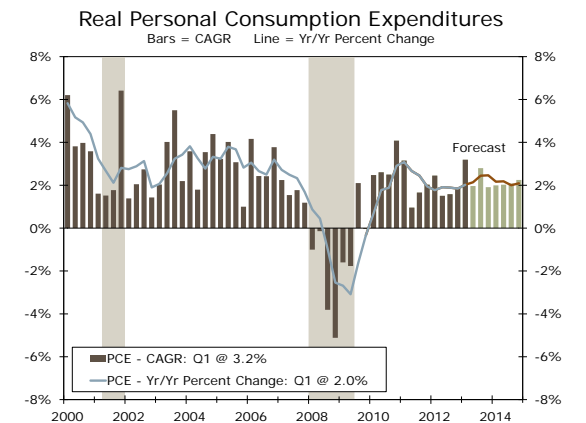
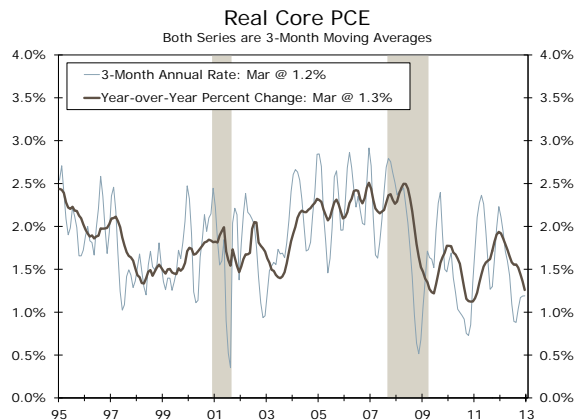
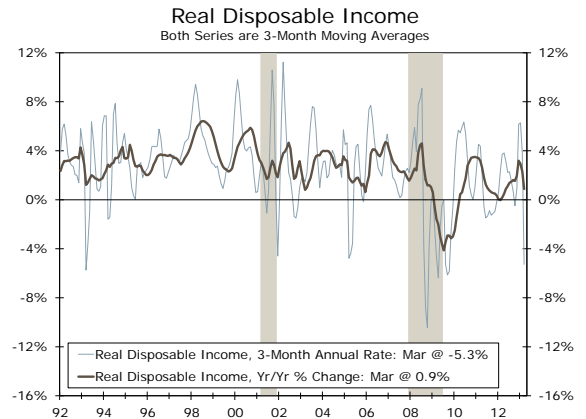
Core Spending Activity Remains Sluggish

In last Friday's GDP release we learned that one of the key reasons for the stronger first quarter personal consumption expenditure print was due to higher services spending on utilities as a result of prolonged below-average temperatures. Real core consumer spending, which excludes food and energy, rose 1.2 percent on a three-month annualized basis in March. Spending for durable goods was flat for the month while nondurable goods spending declined 0.4 percent. Spending on services rose 0.6 percent on the month as the unseasonably cool weather continued in March. Given the slow pace of core consumer spending, we continue to believe that consumers are struggling to cope with slow income growth and higher taxes this year even as inflation pressures have eased.

Consumer prices remained modest as the PCE deflator fell 0.1 percent for the month and is now up a slight 1.0 percent on a year-over-year basis. The core PCE deflator rose a slight 0.06 percent in March. Given the continued reports of softening price pressures, we expect the FOMC to maintain their current accommodative monetary policy stance for the time being.

Q2 Personal Spending Outlook

Given that core consumer spending activity remains weak and real disposable incomes are declining, we are not overly optimistic about consumer spending in the second quarter. Our expectation is that real consumer spending will downshift to a 2.0 percent pace of growth in the second quarter after the more robust 3.2 percent observed in the first quarter. Spending activity should begin to pick up again in the third quarter as aggregate income growth slowly returns. Given the expected softer pace of consumer spending, GDP growth will likely be held around 1.0 percent in the second quarter. Going forward, we expect personal consumption to rise 2.3 percent this year and downshift slightly in 2014.



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