

Spending and income through July 2019

High rates of savings could allow spending to remain strong

United States of America
Economic Report

September 5, 2019

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HR Ratings comments on the July 2019 personal expenditures and income reports which show strong rebounds in real spending from early weakness as income growth rates stabilize at around 3%.

Real personal consumer spending continued to grow strongly in July vs. immediately prior months although much of the strength is due to unusually large declines in growth at the end of 2018. The rebound, as well as the previous decline, was especially strong in the spending of goods but the same pattern existed for services spending as well. On a year-over-year basis, overall spending growth appears to be stabilizing with goods spending growth still rebounding strongly, while services spending growth continues to decline.

For its part, income growth appears to be a mirror image of what is happening to consumer spending. Growth rates for income are now weakening vs. immediately prior periods after surging in early 2019. The surge was particularly strong for employment compensation whose growth often lags slightly the growth in overall personal income before transfers and taxes. Consequently, for the quarter ending in July, employment compensation growth is once again lagging due to the strong comparisons early in the year.

Going forward we would expect a lower degree of volatility as the effects of extreme movements become less noticeable. Furthermore, we would also expect spending to remain relatively strong even if income growth begins to decelerate. This is due to the strong increase in personal savings and the rate of personal savings in the beginning of the year. The rate of savings is now declining, although declining from relatively very high levels.

Table 1: Real Personal Consumer Expenditures in Billions

	For the Quarter ending in			Change vs. Period	
	Jul-18	Apr-19	Jul-19	Prior Year	Prior Qtr.*
Goods	4,592	4,674	4,777	4.04%	9.13%
Durable Goods	1,690	1,721	1,773	4.92%	12.58%
Non-Durable Goods	2,914	2,965	3,019	3.60%	7.41%
Services	8,388	8,501	8,562	2.07%	2.88%
Total	12,952	13,144	13,299	2.68%	4.78%
Residual	-40	-44	-55	n.a.	n.a.

Source: HR Ratings with data from the BEA converted into billions of real 2012 USD (3mma).

*Annualized change vs. immediately prior quarter.

The residuals (i.e., the difference between total spending and the sum of the individual components) are due to the use of different PCE deflators to convert different categories of nominal spending into real terms.

Table 1 above shows the strong growth in consumer expenditures for the quarter ending in July vs. the quarter that ended in April. Growth was particularly strong for goods spending which typically is more volatile than spending on services. On an annual basis, consumer expenditures advanced a more moderate 2.68%, again showing greater strength for goods but with a much reduced differential.

Graph 1 shows the extreme volatility in spending, beginning roughly in the 4Q of 2018 with strong declines and the sharp increases that we are currently seeing.

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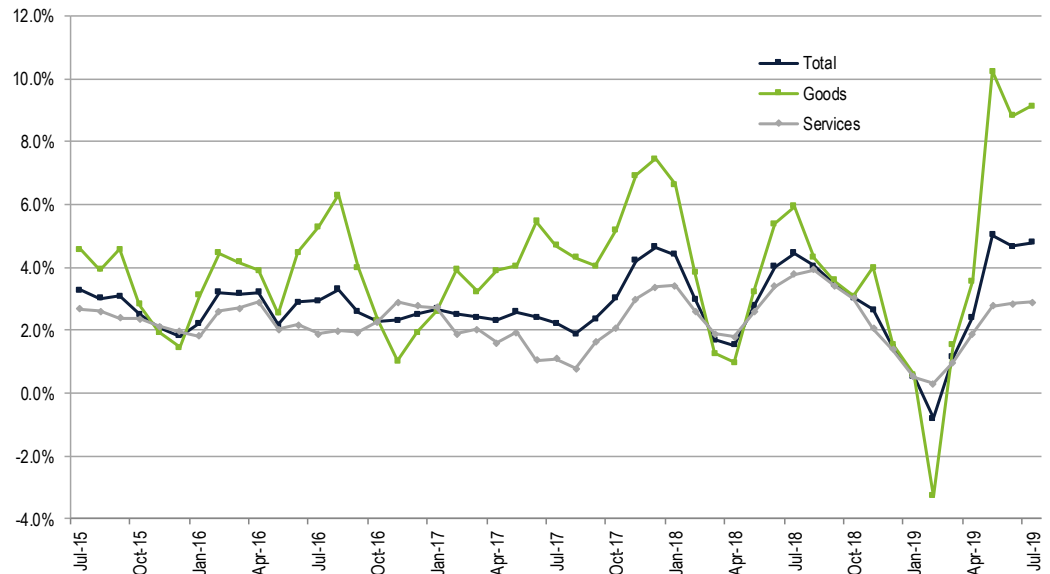
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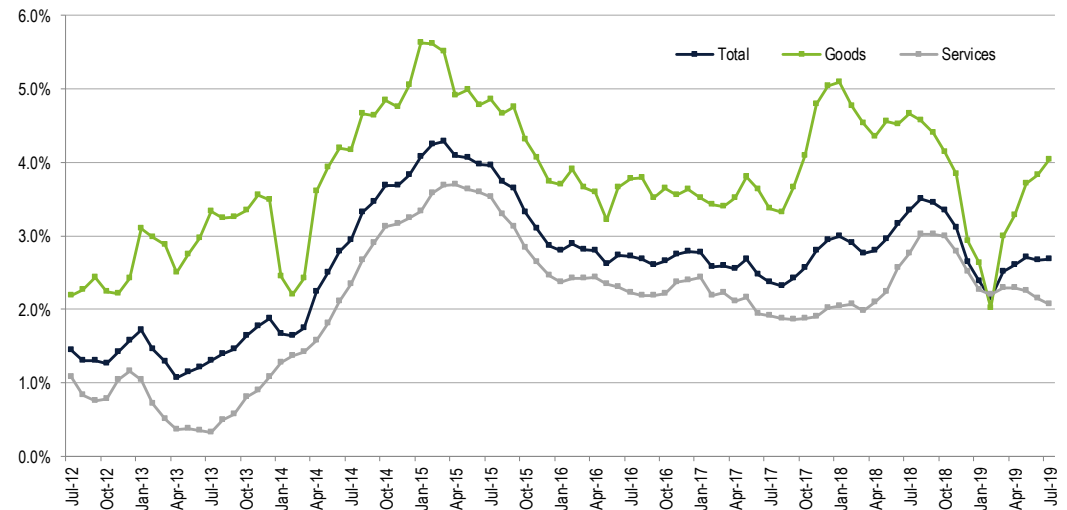
Graph 1: Annualized quarterly change in Real Personal Consumer Expenditures



Source: HR Rating, with data from the BEA, converted into real USD. Three month moving averages.

In Graph 2 we show the quarterly change in spending on a year-over-year basis with many of the same trends seen in Graph 1 although with much less volatility. The graph suggests that real spending growth is beginning to stabilize at a rough 2.7%.

Graph 2: Real Annual Growth in Personal Consumer Expenditures (3MMA)



Source: HR Ratings with data from the BEA converted into real USD based on the 3MMA.

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In Table 2 we show the quarterly evolution of personal income. For the quarter ending in July (vs. the quarter ending in April) real personal income before transfers and taxes advanced at a relatively modest annualized rate of 2.21%. For its part, employee compensation, which is the principal component of personal income, advanced at a much slower 1.43%. Still, despite this poor performance, on a year-over-year basis, it still rose a robust 3.70% vs. the same quarter during 2018. By this last measure, employee compensation growth was even stronger than the 3.10% expansion of total income before transfers and taxes.

Table 2: Real Quarterly Personal Income and its Disposition in Billions*

	Jul-18	Apr-19	Jul-19	YoY**	Change USD**	QoQ**
Wages & Salaries	8,202	8,494	8,523	3.91%	28	1.33%
Supplements to W&S	1,884	1,928	1,937	2.80%	9	1.86%
Employee Compensation	10,086	10,422	10,459	3.70%	37	1.43%
Proprietors' Income	1,462	1,486	1,497	2.40%	11	3.05%
Rental Income	700	706	714	2.03%	8	4.53%
Interest Income	1,577	1,568	1,595	1.15%	27	7.06%
Dividend Income	1,134	1,156	1,157	2.03%	1	0.32%
Personal Income on Assets	2,711	2,724	2,752	1.52%	28	4.16%
Personal Income before Taxes and Transfers	14,958	15,338	15,422	3.10%	84	2.21%
Plus Personal Current Transfers	2,746	2,867	2,896	5.45%	29	4.05%
Less: Contrib. for govt. social insurance	1,252	1,297	1,300	3.90%	3	1.02%
Personal Income before Taxes	16,453	16,908	17,017	3.43%	109	2.61%
Less: Personal current taxes	1,919	1,994	2,019	5.21%	25	5.12%
Disposable Personal Income (DPI)	14,533	14,914	14,998	3.20%	84	2.28%
Less personal savings	1,091	1,258	1,184	8.51%	-74	-21.47%
Less interest payments	308	330	333	8.11%	3	3.80%
Less personal current transfers	183	182	182	-0.14%	0	1.05%
Non pers. consumer expend. outflows	491	512	516	5.04%	4	2.81%
Personal Consumption Expenditures	12,952	13,144	13,299	2.68%	154	4.78%
Personal Savings Rate***	7.51%	8.43%	7.89%	39	n.a.	-54

Source: HR Ratings with data from the BEA (converted into real 2012 USD).

*Based on three month moving averages.

**YoY: Change vs. same quarter year earlier. USD & QoQ: Absolute change and Annualized change vs. immediately prior quarter.

***For the personal savings rate (PSR) absolute values refer to the change in basis points. PSR = Personal Savings / DPI.

On a net basis, the effect of transfer receipts, social insurance payments and personal taxes was modestly positive leading to a slightly higher rate of disposable personal income growth. Thus, on a quarter-over-quarter basis the 2.21% increase in income before taxes and transfers translated into a slightly stronger 2.28% advance on an after tax basis.

In Graph 3 we present the evolution of the quarterly annualized changes in personal income before transfers, social insurance and personal taxes, and, for comparative purposes, the changes in employee compensation, its principal component. Note the difference with Graph 1. Graph 3 shows a surge in income growth while during roughly the same months Graph 1 shows a decline in spending. In the last few months we see a sharp decline in income growth vs. the strong comps. In contrast, in Graph 1 we see strong rebounds in spending vs. the weakness in previous months.

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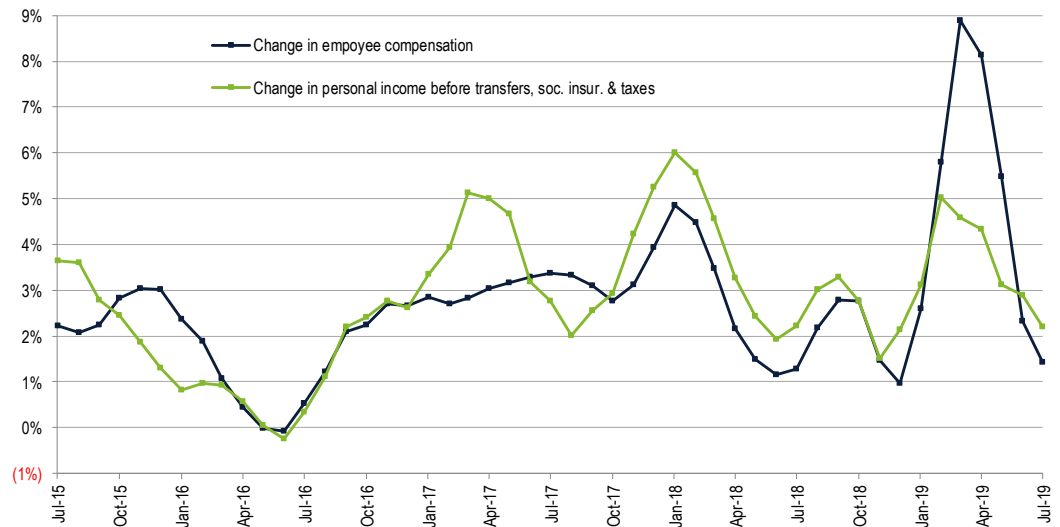
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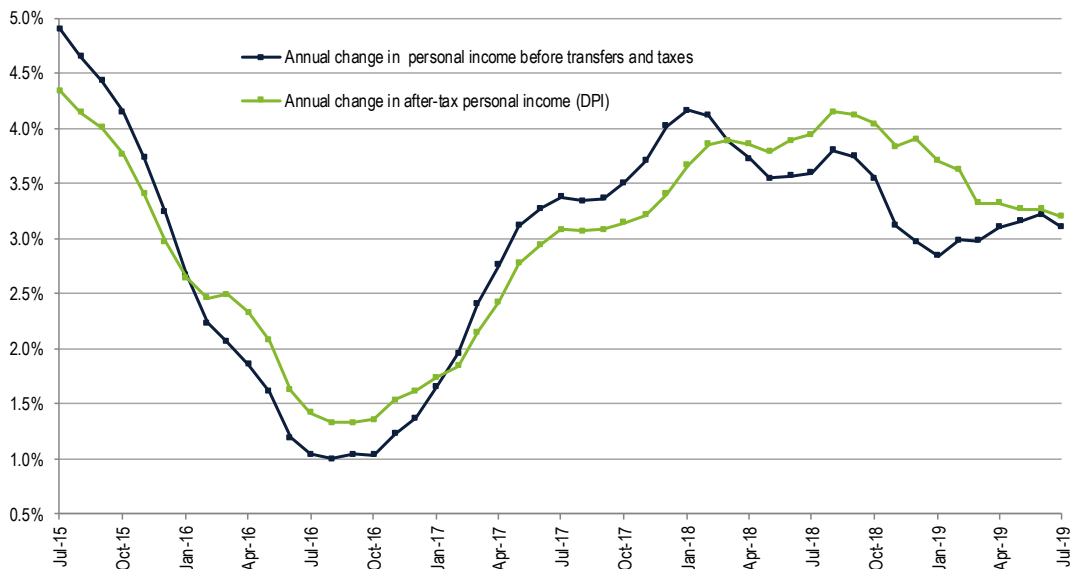
Graph 3: Annualized quarterly change in Real Personal Income



Source: HR Ratings with data from the BEA, converted into real 2012 USD. Three month moving averages.

Graph 4 below shows the annual evolution of real personal income before and after transfers, social insurance and taxes. On an after tax basis the graph shows a declining rate of growth which tended to reduce the positive impact of the surge in before tax personal income early in 2019. On an annual basis, after tax personal income appears to be stabilizing at a growth of slightly above 3%.

Graph 4: Real Annual Growth in Personal Income before and after taxes (3mma)



Source: HR Ratings with data from the BEA, converted into real USD. Three month moving averages.

It is relevant to note that during 2017 the net effect of transfers and taxes (including for social insurance) tended to reduce the net increase in personal income. During 2018, in contrast, the tax effect was positive. Currently the effect is becoming increasingly negligible.

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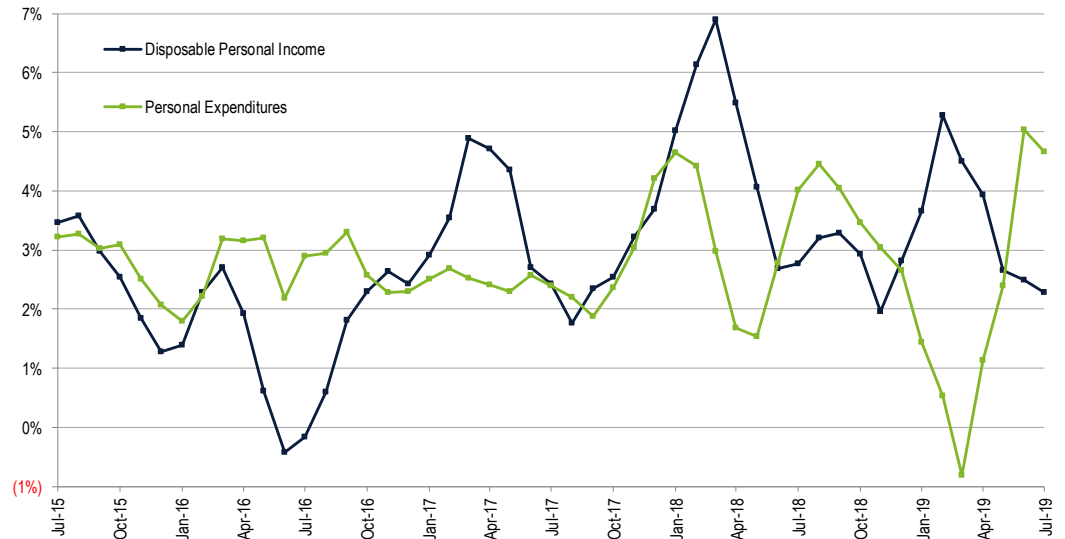
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Graph 5: Real Annualized Quarterly change in Income and Spending



Source: HR Ratings with data from the BEA, converted into real 2012 USD. Three month moving averages.

Graph 5 essentially shows more clearly the relationship that we have been noting in which over the last few months while the growth in DPI was rising, the growth in consumer spending was falling; while in the spring/summer we see a rebound in spending and a decline in income expansion.

The effect of these relationships is seen in Graph 6 below which shows the quarterly evolution of the rate of personal savings. From the relative lows in 2016 we have seen significant increases over the last few years, peaking in the first quarter of 2019 when we saw strength in income growth and some weakness in spending. Over the last three or four months, spending has been helped by the decline in the savings rate. The question is how much longer this can continue. Given the relatively high current levels of personal savings, even with the decline in the spring/summer months, savings rates might continue to fall. However, we may be in the midst of a longer-term upward trend in the savings rate and could see a rebound as we have seen on several occasions since the summer of 2017.

The continuation of the recent strength in consumer spending will depend in large part on the answer to this question.

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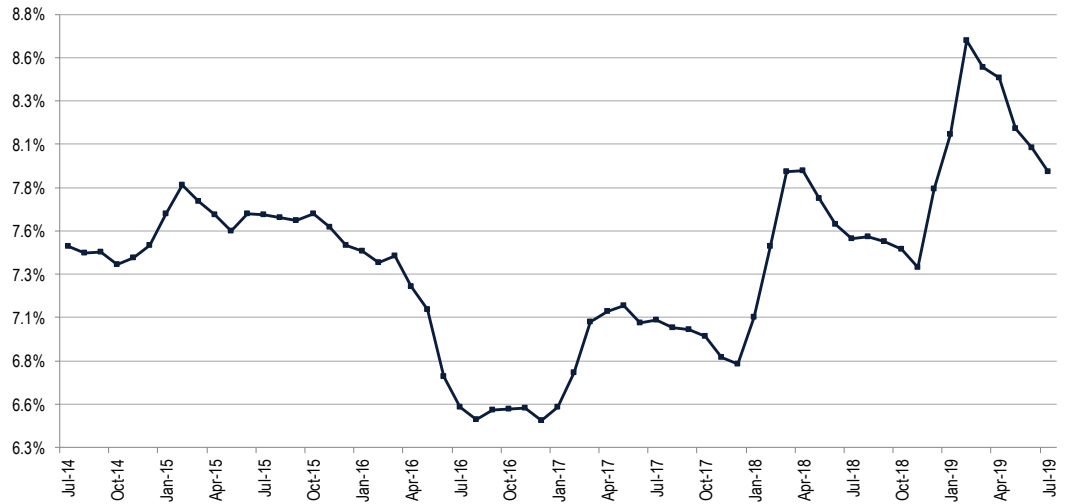
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Graph 6: Quarterly Rate of Personal Savings



Source: HR Ratings based on the U.S. BEA.



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