U.S. Flash

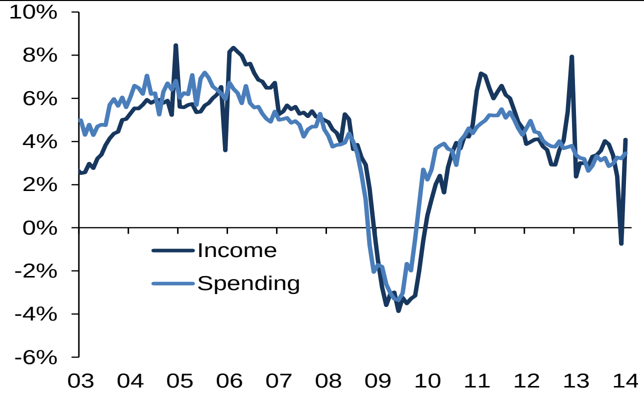
Personal Spending and Income Continue Upward Trend

- **Consumer spending up 0.4% in January due to positive bias from services sector**
- **Personal income recovers to 3.7% on a YoY basis after negative stint in December**
- **Attention shifts to PCE inflation, which remains significantly below the Fed's target**

Consumer spending in January increased 0.4% MoM, continuing its upward trend over the last year but driven mostly by services instead of the goods component. Utilities spending likely inflated the consumption figure, as people cranked up their heaters to stay warm in the presence of extreme winter weather. On the other hand, spending in the goods component dropped 0.6% on a MoM basis. Still, month-to-month readings on spending do not always tell the full story, and looking at the bigger picture, overall consumption expenditures are up a healthy 3.45% YoY, the biggest annual increase since December 2012, behind 2.3% and 4.1% gains in the goods and services sector, respectively. Meanwhile, personal income in January rose a strong 0.3%, just a touch below consumption growth, which shows that consumers are spending more and saving less. In fact, personal savings has declined for four consecutive months and remains low as a share of disposable personal income at 4.3%, yet still considerably higher than 2-3% range seen before the recession. In the short-term, this trend is positive for the economy, as spending serves as the backbone for growth, accounting for roughly two-thirds of economic activity. However, an increase in borrowing might mean slower economic growth in later months, when consumers must eventually pay back the debt used to fund short-term expenditures. On a YoY basis, however, personal income is up 3.7%, which is roughly in-line with consumption, so we do not believe consumers are spending excessively.

Looking at inflation, the personal consumption expenditures price index increased by 0.1% in January as the component continues its positive trend, albeit at a slow pace. On a YoY basis, prices are up 1.2%, and because personal income is rising at a more rapid pace, consumers are feeling more bang for their buck. The growth rate is not significantly different when looking at core PCE, so energy and food are not providing much bias on the figure, either. The goods PCE index has held in negative territory on a YoY basis throughout the past six months, which is certainly driving deflation worries within the Fed. As personal consumption and income remain healthy overall amid the economy recovery, we are turning our attention to inflation levels to ensure they do not drop to dangerous levels as the Fed continues with QE tapering.

Chart 1
Real Personal Income and Spending
YoY % Change



Source: Bureau of Economic Analysis & BBVA Research

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