Datanote: US Personal Income & Spending, September / ECI, Q3

In one line: Subdued core PCE inflation and slowing ECI growth green light further material Fed easing.

- The core PCE deflator rose 0.3% in September, matching the consensus. Net revisions were 0.04%.
- Real consumption rose by 0.4%, slightly above the consensus, 0.3%. Net revisions were +0.1%.
- Personal incomes increased by 0.3%,

in line with the consensus. Net revisions were +0.1%.

- The ECI rose by 0.8% in Q3, slightly below the consensus and Q2's increase, both 0.9%.

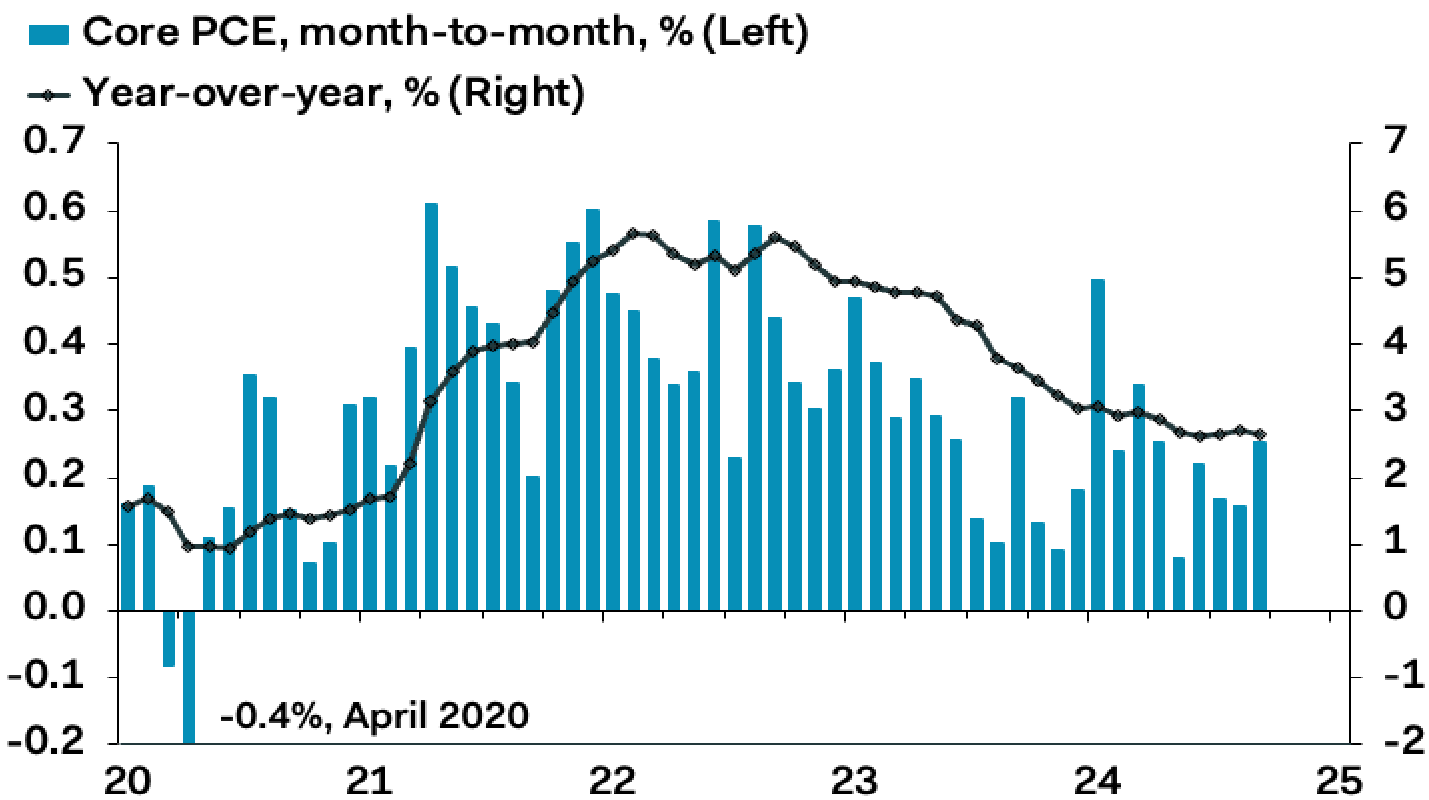
The slightly bigger quarter-on-quarter increase in the Q3 core PCE deflator than we expected manifested in small upward revisions to numbers for July and August. September's 0.25% month-to-month increase was very close to our 0.26% forecast. The Q3 data appear to have been slightly worse than the Fed expected, as it would now require month-to-month increases to average 0.10% over the next three months for the median participant's forecast of a 2.6% year-over-year increase in Q4 to be realized. We are pencilling-in a slightly faster 0.15% run rate, even though the uplift to prices for accommodation services and autos triggered by the recent hurricanes probably will be small and short-lived. Nonetheless, the low level of food and energy prices, frictionless supply chains, cooling new rent inflation and the ongoing loosening of the labor market suggest that the outlook for core PCE inflation is fundamentally benign.

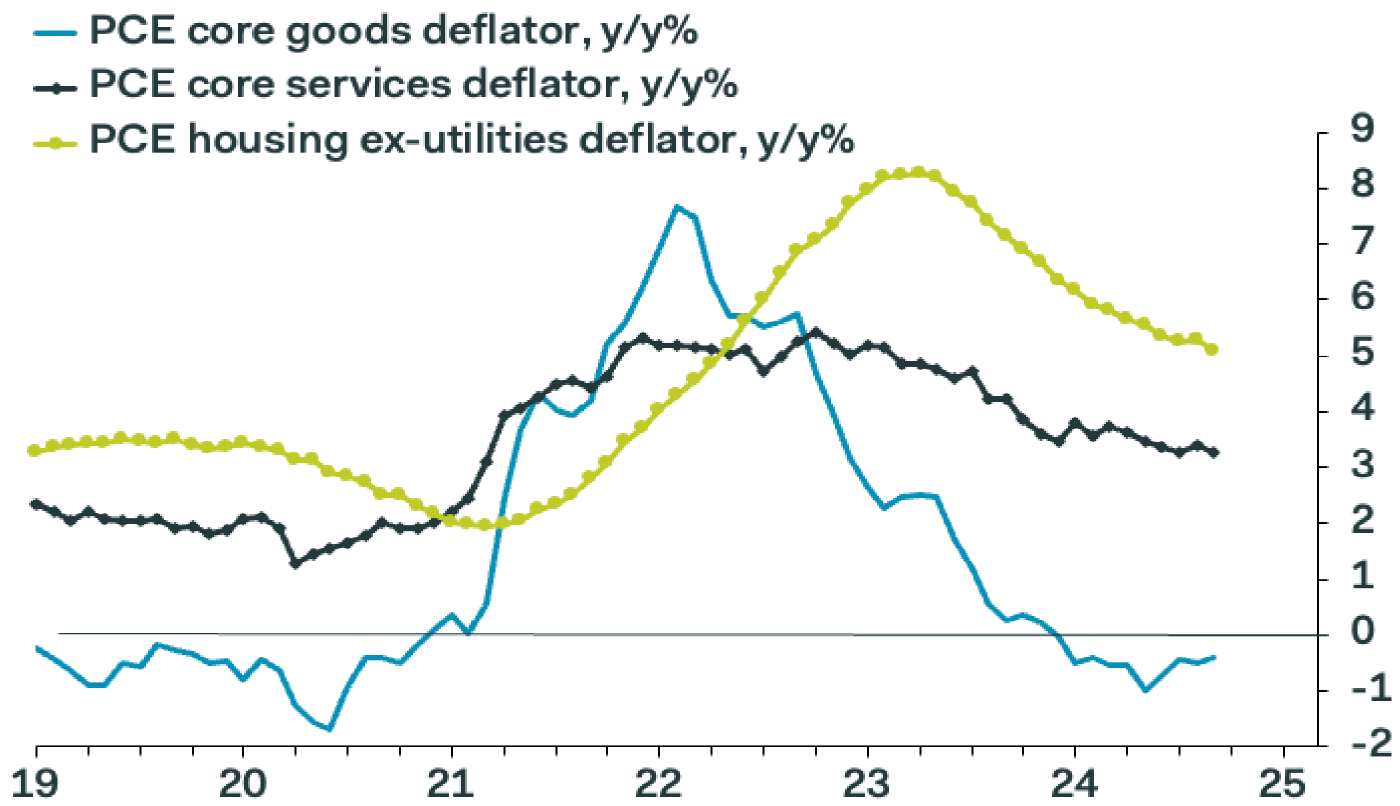
Meanwhile, September's personal income and spending data cast further doubt over the sustainability of recent rapid GDP growth. Annualized growth in real after-tax income over the last three months, compared to the previous three months, slowed to just 1.6% in September, from 2.0% in August. On this basis, nominal wages and salaries grew by a brisk 4.9% in September, but income from interest and dividends fell by 2.4%, largely in response to the Fed's easing. With most debt on fixed rates but interest rates on savings more closely linked to the funds rate, Fed easing will weigh on real after-tax income growth over the coming months.

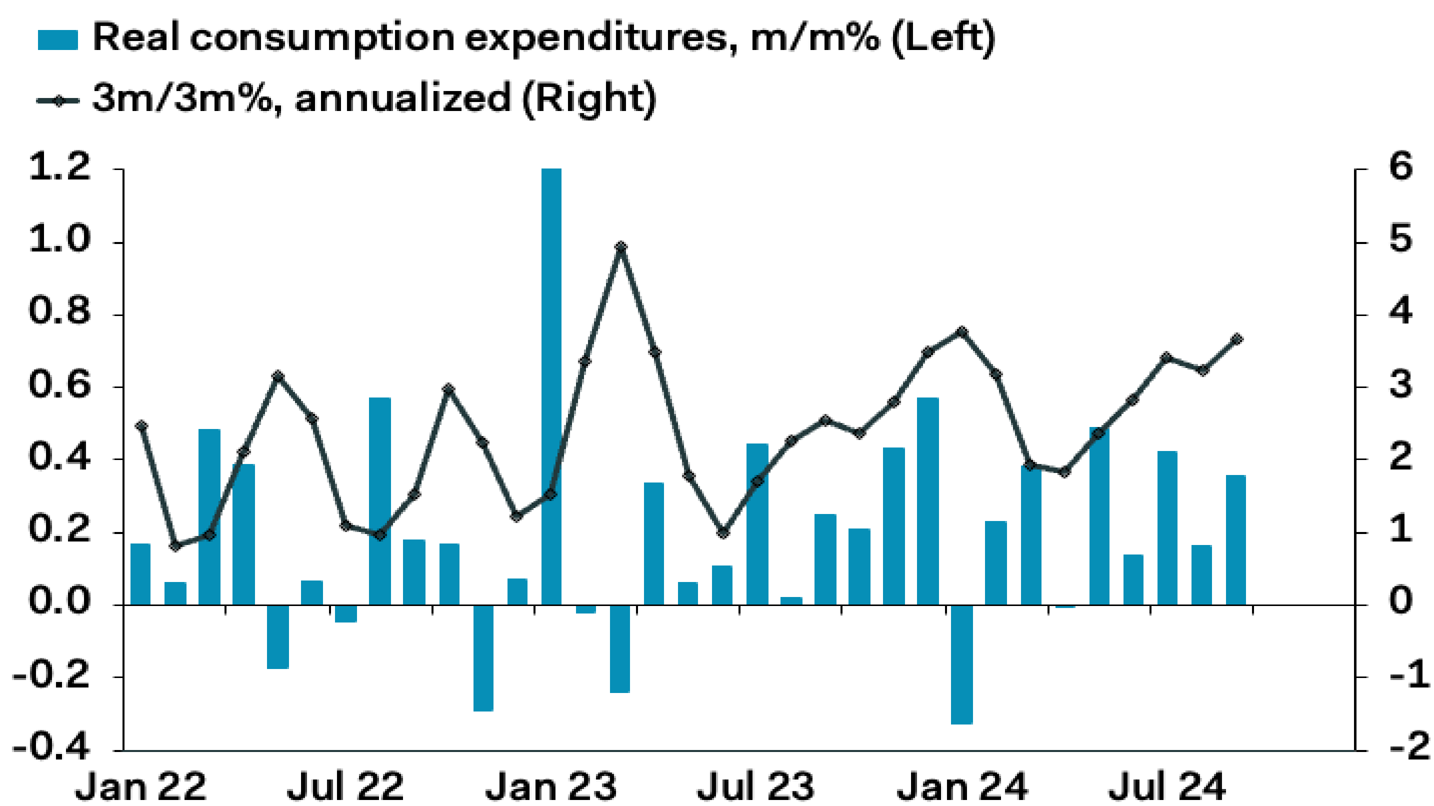
Accordingly, households have continued to fund rapid growth in real expenditure by reducing their saving rate, which dipped to 4.6% in September from 4.8% in August, and is now well below its 2015-to-19 average, 6.1%. Admittedly, a period of below-normal saving was warranted following the pandemic. But the saving rate now looks low, given that the ratio of households' liquid assets has returned to its pre-Covid trend level, and the labor market is deteriorating.

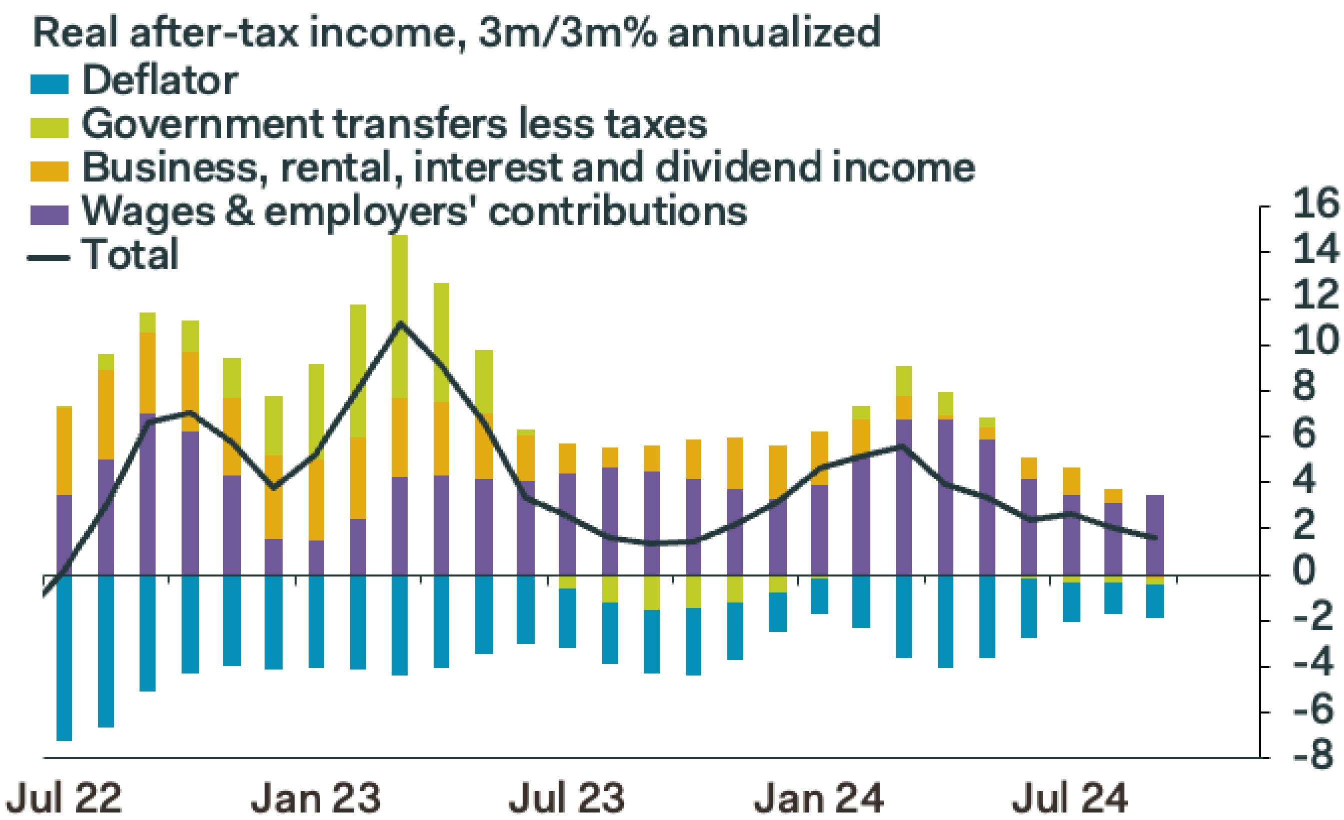
A stable saving rate next year is a solid bet, with the risks skewed towards an increase.

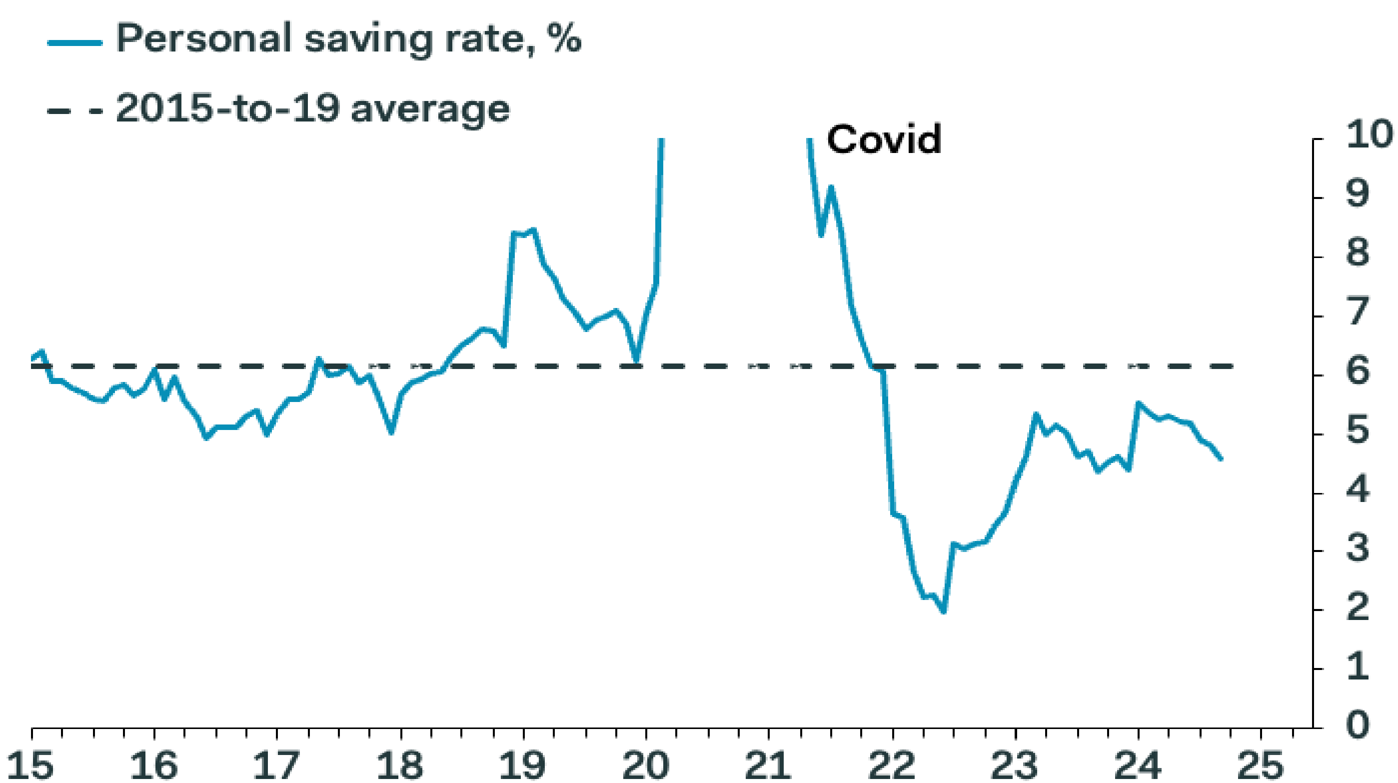
Finally, the ECI report brought good news for the Fed, which focuses on this measure of labor costs because it is mix-adjusted. The 0.8% quarter-on-quarter increase in workers' total compensation in Q3 reduced the year-over-year rate to 3.9%—the first sub-4% figure for three years—from 4.1% in Q2. Recent solid growth in productivity means that labor costs already are rising slowly enough for core PCE inflation to fully return to the Fed's 2% target. The low level of the quits rate and the job postings-to-unemployment ratio suggest that growth in ECI private wages and salaries will continue to slow, increasing the risks of a period of below 2% core PCE inflation next year.

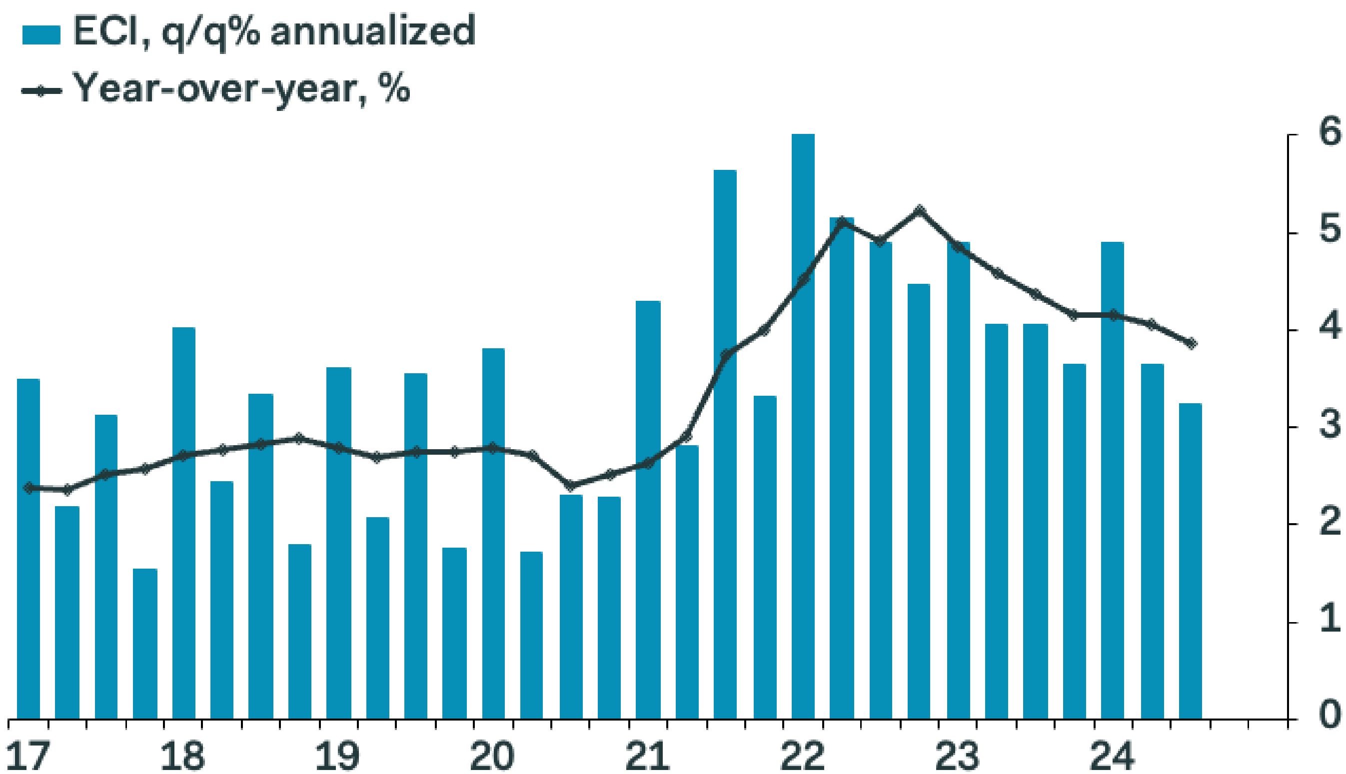


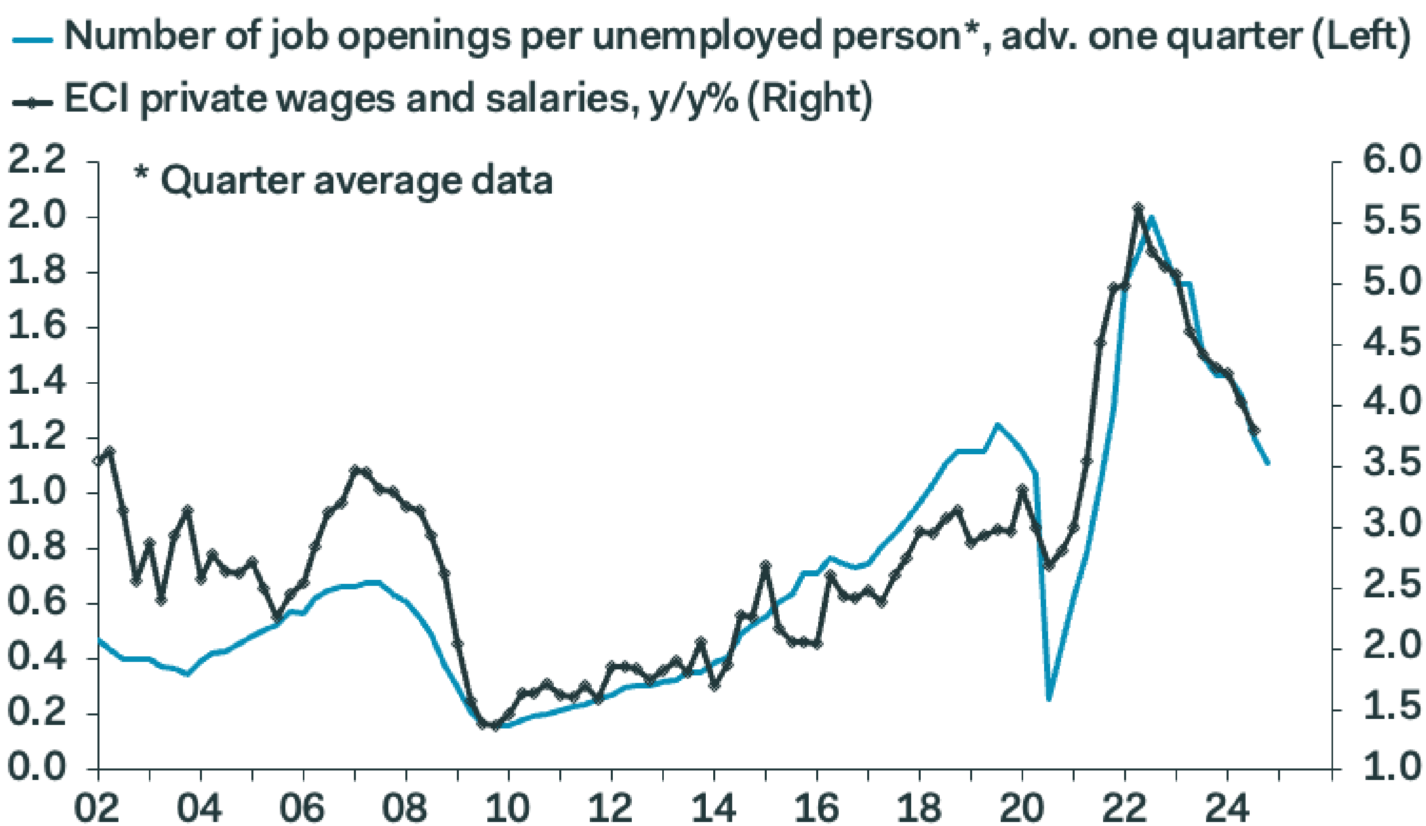

PCE core goods deflator, y/y%
PCE core services deflator, y/y%
PCE housing ex-utilities deflator, y/y%
9
8
7
6
5
4
3
2
1
0
-1
-2
19
20
21
22
23
24
25


Real consumption expenditures, m/m% (Left)
3m/3m%, annualized (Right)
1.2
1.0
0.8
0.6
0.4
0.2
0.0
-0.2
-0.4
6
5
4
3
2
1
0
-1
-2
Jan 22
Jul 22
Jan 23
Jul 23
Jan 24
Jul 24


Real after-tax income, 3m/3m% annualized
Deflator
Government transfers less taxes
Business, rental, interest and dividend income
Wages & employers' contributions
Total
16
14
12
10
8
6
4
2
0
-2
-4
-6
-8
Jul 22
Jan 23
Jul 23
Jan 24
Jul 24


Personal saving rate, %
2015-to-19 average
Covid
10
9
8
7
6
5
4
3
2
1
0
15
16
17
18
19
20
21
22
23
24
25


ECI, q/q% annualized
Year-over-year, %
6
5
4
3
2
1
0
17
18
19
20
21
22
23
24


Number of job openings per unemployed person*, adv. one quarter (Left)
ECI private wages and salaries, y/y% (Right)
* Quarter average data
2.2
2.0
1.8
1.6
1.4
1.2
1.0
0.8
0.6
0.4
0.2
0.0
6.0
5.5
5.0
4.5
4.0
3.5
3.0
2.5
2.0
1.5
1.0
02
04
06
08
10
12
14
16
18
20
22
24