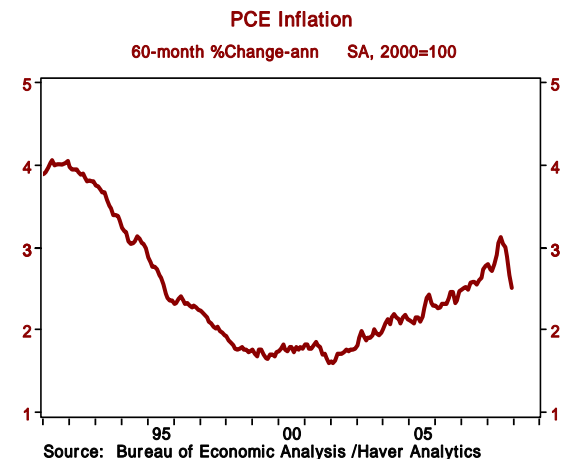
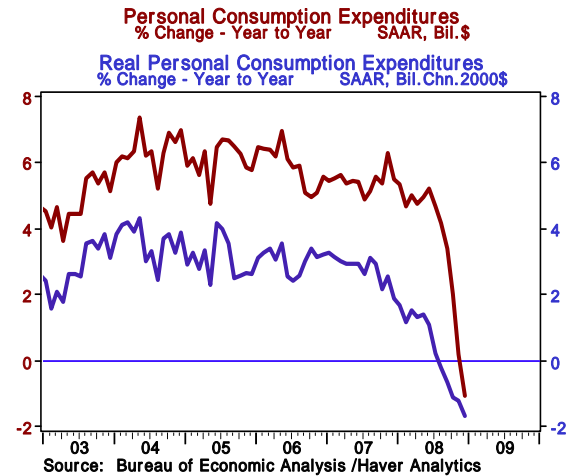


DECEMBER PERSONAL INCOME AND CONSUMPTION

Chief Economist – Brian S. Wesbury
Senior Economist – Robert Stein, CFA

- Personal income declined 0.2% in December versus consensus expectations that it would fall 0.4%. Personal consumption dropped 1.0%, versus the consensus expected 0.9% decline. Personal income is up 1.4% in the past year while personal consumption is down 1.1%.
- Disposable personal income (income after taxes) declined 0.2% in December but is up 1.9% versus last year. Pre-tax wages and salaries were down 0.3% in December, but unemployment benefits (which count as income) were up 24.0%.
- The overall PCE deflator (consumer inflation) fell 0.5% in December but is up 0.6% versus a year ago. The “core” PCE deflator, which excludes food and energy, was unchanged in December but is up 1.7% versus a year ago.
- After adjusting for inflation, real consumption was down 0.5% in December and down 1.7% versus last year.

Implications: Personal spending continued to decline in December and dropped faster than prices, meaning the “real” (inflation-adjusted) value of consumer purchases also declined. The weakness in December was concentrated in nondurable goods (such as food, clothing, and energy products like gas). Recent reductions in spending are much greater than economic conditions warrant. As we have pointed out before, autos usually sell at a rate so that it would take about 13 years to replace all the vehicles on the road. At the worst point of the recession in 1981-82, consumers postponed buying cars, lengthening the replacement rate to 16.3 years. In December 2008, the replacement rate was 23.4 years. This is simply not sustainable, which is, in part, why we believe the deepest negative months for spending are behind us. On the inflation front, energy price declines continued to suppress consumption prices in December, when overall consumption fell 0.5% but “core” prices (excluding food and energy) were unchanged.



Personal Income and Spending <i>All Data Seasonally Adjusted</i>	Dec-08	Nov-08	Oct-08	3-mo % ch. annualized	6-mo % ch. annualized	Yr to Yr % Change
Personal Income	-0.2%	-0.4%	-0.1%	-2.6%	-2.3%	1.4%
Disposal (After-Tax) Income	-0.2%	-0.3%	0.0%	-2.3%	-5.0%	1.9%
Personal Consumption Expenditures (PCE)	-1.0%	-0.8%	-1.1%	-11.2%	-6.9%	-1.1%
Durables	-1.3%	0.4%	-5.2%	-22.3%	-20.2%	-12.7%
Nondurable Goods	-3.5%	-2.7%	-3.0%	-31.3%	-19.3%	-6.2%
Services	0.2%	0.0%	0.4%	2.3%	2.1%	3.6%
PCE Prices	-0.5%	-1.1%	-0.6%	-8.4%	-3.1%	0.6%
"Core" PCE Prices (Ex Food and Energy)	0.0%	0.0%	0.0%	-0.1%	0.9%	1.7%
Real PCE	-0.5%	0.3%	-0.6%	-3.1%	-4.0%	-1.7%

Source: Bureau of Economic Analysis