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October Personal Income and Consumption

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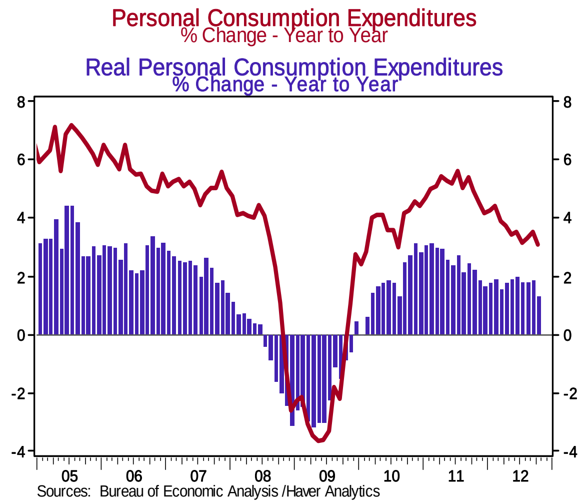
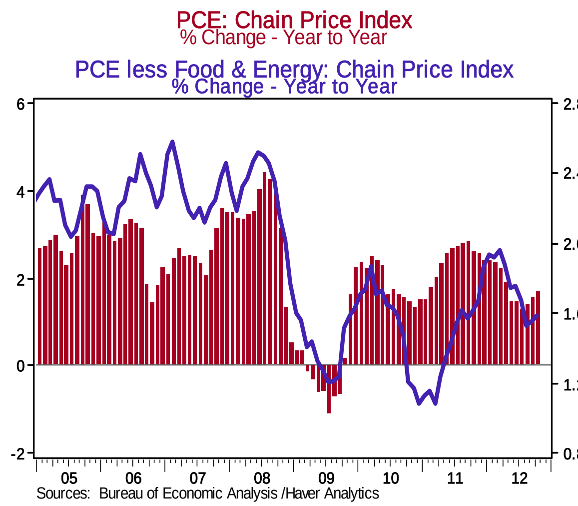
- Personal income was unchanged in October, coming in below the consensus expected gain of 0.2%. Personal consumption declined 0.2%, below the consensus expected no change. In the past year, personal income and spending are both up 3.1%.
- Disposable personal income (income after taxes) was also unchanged in October but is up 3.0% from a year ago. Gains in interest and dividend income in October offset a decline in private wages & salaries.
- The overall PCE deflator (consumer inflation) was up 0.1% in October and up 1.7% versus a year ago. The "core" PCE deflator, which excludes food and energy, rose 0.1% in October and is up 1.6% in the past year.
- After adjusting for inflation, "real" consumption fell 0.3% in October but is up 1.3% from a year ago.





Implications: Super storm Sandy struck today's data hard. Consumer spending fell 0.2% in October, the steepest drop in any month since right after the end of cash-for-clunkers in 2009. "Real" (inflation-adjusted) personal spending was down 0.3% in October (-0.5% including downward revisions for prior months) and only up 1.3% from a year ago. Incomes were unchanged in October as private-sector wages & salaries dropped 0.2%, also likely a result of Sandy. If we take all of the recent data at face value, our GDP model is tracking zero real growth in Q4. That's right, a big fat goose-egg. However, we are likely to see a rebound in the data for later in the quarter as the eastern seaboard recovers from Sandy. For example, we expect a surge in auto sales for November, which will be reported by automakers on Monday. As a result, Q4 should end up with slightly positive growth in the end. Assuming a political deal on the "fiscal cliff" sometime in late December or very early January, we expect real GDP growth of close to 3% next year. That includes boosts from farm inventory replenishment after this year's drought, as well as Sandy-rebuilding on the East Coast. Despite October's weak income number, real disposable income is still up 1.2% from a year ago, which is enough to keep pushing consumer spending higher. Meanwhile, households' financial obligations – recurring payments like mortgages, rent, car loans/leases, as well as other debt service – are now the smallest share of income since 1984. This allows consumers to stretch their income gains further. On the inflation front, overall consumption prices as well as the core PCE, which excludes food and energy, were both up 0.1% in October. Overall prices and core prices are up 1.7% and 1.6% respectively in the past year, versus the Federal Reserve's target of 2%. This is awfully close for a central bank running a very loose monetary policy. Expect higher inflation in the year ahead.

Personal Income and Spending *All Data Seasonally Adjusted*	Oct-12	Sep-12	Aug-12	3-mo % ch. annualized	6-mo % ch. annualized	Yr to Yr % change
Personal Income	**0.0%**	0.4%	0.1%	1.8%	2.0%	3.1%
Disposable (After-Tax) Income	**0.0%**	0.4%	0.1%	1.8%	1.9%	3.0%
Personal Consumption Expenditures (PCE)	**-0.2%**	0.8%	0.3%	3.6%	2.1%	3.1%
Durables	**-1.9%**	2.0%	0.9%	4.0%	2.1%	3.6%
Nondurable Goods	**-0.2%**	1.4%	1.3%	10.7%	2.9%	3.3%
Services	**0.1%**	0.3%	-0.1%	1.2%	1.9%	3.0%
PCE Prices	**0.1%**	0.3%	0.4%	3.3%	1.5%	1.7%
"Core" PCE Prices (Ex Food and Energy)	**0.1%**	0.1%	0.0%	0.9%	1.2%	1.6%
Real PCE	**-0.3%**	0.4%	0.0%	0.3%	0.6%	1.3%

Source: Bureau of Economic Analysis