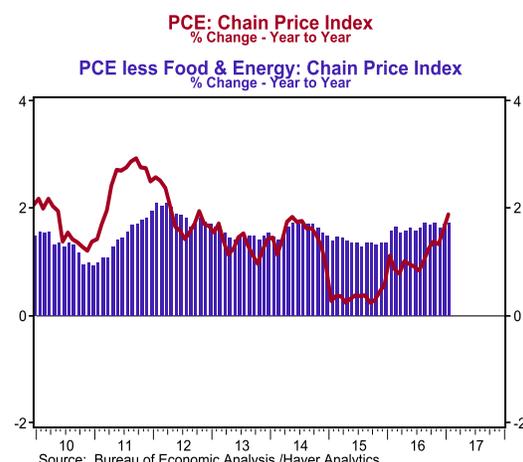
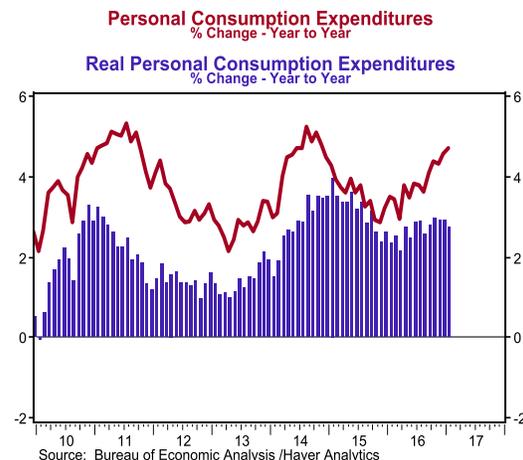


January Personal Income and Consumption

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- Personal income increased 0.4% in January, coming in above the consensus expected 0.3%. Personal consumption rose 0.2% in January, coming in below the consensus expected 0.3%. Personal income is up 4.0% in the past year, while spending is up 4.7%.
- Disposable personal income (income after taxes) increased 0.3% in January and is up 4.0% from a year ago. The gain in January was led by private-sector wages & salaries and government benefits.
- The overall PCE deflator (consumer inflation) rose 0.4% in January and is up 1.9% versus a year ago. The “core” PCE deflator, which excludes food and energy, increased 0.3% in January and is up 1.7% in the past year.
- After adjusting for inflation, “real” consumption declined 0.3% in January but is up 2.8% from a year ago.

Implications: The most important news today was on inflation. The Fed’s favorite measure, the PCE deflator, rose 0.4% in January, the most for any month since 2011, and is up 1.9% from a year ago, just a hair under its 2% target. By contrast, just 12 months ago, in January 2016, the PCE deflator was up only 1.1% and 12 months before that it was up a meager 0.3% in the year ending January 2015. And it’s not just an energy story. “Core” prices, which exclude food and energy, rose 0.3% in January, the most for any month since 2007 and is up 1.7% from a year ago. The bottom line is that inflation is accelerating and should exceed the Fed’s 2% target a month from now. No wonder the futures market is now pricing in about an 80% chance that the Fed raises rates in March. In our view, the Fed is likely to raise rates on March 15 unless the employment report on March 10 is unusually weak (right now, we think the jobs report will be at or above consensus expectations). Although some analysts are bemoaning a tepid 0.2% increase in consumer spending in January, there is no reason to be concerned. Unusually warm winter weather held down utility output in January. So while spending on goods rose 0.5%, spending on services, which includes utilities, was unchanged for the month. (This may happen again in February due to continued mild weather; don’t panic then, either.) Moreover, income gains remain healthy, increasing 0.4% to start 2017. The gains in income were led by private-sector wages & salaries and government social benefits. The bump in government benefits was, in part, caused by a jump in credits related to Obamacare. However, in the past year, while overall personal income is up 4.0%, private wages & salaries are up 4.8% while government benefits are up a slower 3.7%. If President Trump wants faster growth he needs to slow the growth of (or reduce!) government benefits. The one consistent dark cloud in the income reports has been government redistribution. Before the Panic of 2008, government transfers – Medicare, Medicaid, Social Security, disability, welfare, food stamps, and unemployment insurance – were roughly 14% of income. In early 2010, they peaked at 18.5%. Now they’re around 17%, but not falling any further. Redistribution hurts growth because it shifts resources away from productive ventures and, among those getting the transfers, weakens work incentives. That’s why, for the time being, we still have a Plow Horse economy, not a Race Horse economy.



Personal Income and Spending <i>All Data Seasonally Adjusted</i>	Jan-17	Dec-16	Nov-16	3-mo % ch. annualized	6-mo % ch. annualized	Yr to Yr % change
Personal Income	0.4%	0.3%	0.2%	3.5%	3.9%	4.0%
Disposable (After-Tax) Income	0.3%	0.3%	0.2%	3.1%	3.7%	4.0%
Personal Consumption Expenditures (PCE)	0.2%	0.5%	0.2%	3.7%	4.2%	4.7%
Durables	-0.3%	1.7%	-1.0%	1.8%	4.3%	6.2%
Nondurable Goods	1.0%	0.3%	0.2%	6.0%	6.7%	4.6%
Services	0.0%	0.4%	0.5%	3.4%	3.5%	4.5%
PCE Prices	0.4%	0.2%	0.1%	2.7%	2.5%	1.9%
"Core" PCE Prices (Ex Food and Energy)	0.3%	0.1%	0.0%	1.9%	1.8%	1.7%
Real PCE	-0.3%	0.3%	0.2%	1.0%	1.7%	2.8%

Source: Bureau of Economic Analysis