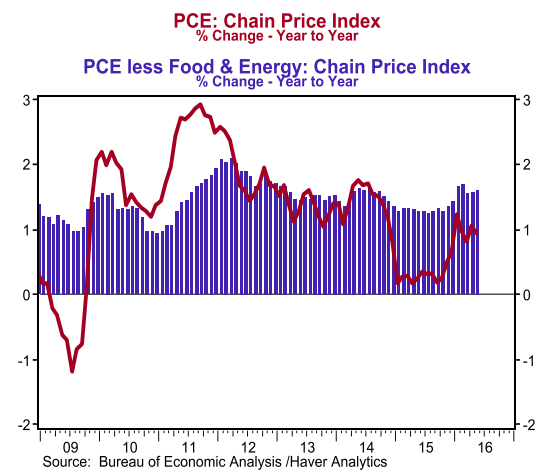
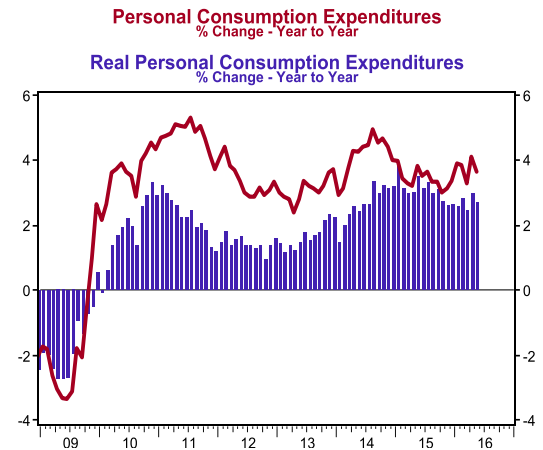


## May Personal Income and Consumption

Brian S. Wesbury – Chief Economist  
Robert Stein, CFA – Dep. Chief Economist  
Strider Elass – Economist

- Personal income increased 0.2% in May, slightly below the consensus expected rise of 0.3%. Personal consumption rose 0.4% in May, matching the consensus expectations. Personal income is up 4.0% in the past year, while spending is up 3.7%.
- Disposable personal income (income after taxes) increased 0.2% in May and is up 4.1% from a year ago. The gain in May was led by private sector wages and salaries plus dividends.
- The overall PCE deflator (consumer prices) rose 0.2% in May and is up 0.9% versus a year ago. The “core” PCE deflator, which excludes food and energy, increased 0.2% in May and is up 1.6% in the past year.
- After adjusting for inflation, “real” consumption rose 0.3% in May and is up 2.7% from a year ago.

**Implications:** In April, consumer spending grew at the fastest monthly pace since 2009, back during “cash for clunkers.” After a month like that, you might expect consumers to pull back a little if they felt nervous about the economy. Instead, consumer spending grew 0.4% in May, the second fastest pace in the past year. No signs of a recession here, not even close. “Real” (inflation-adjusted) consumer spending grew 0.3% in May and is up 2.7% in the past year. Although personal income grew a modest 0.2% in May, incomes are up 4% in the past year versus a 3.7% gain for consumer spending. In other words, the recent strength of the American consumer has not been fueled by an unsustainable credit binge. Instead, it reflects higher purchasing power by American workers; private-sector wages and salaries rose 0.2% in May and are up 4.9% from a year ago. As the labor market keeps tightening, incomes will continue on their upward trend. The one consistent dark cloud in these reports has been the data on government redistribution. While unemployment compensation is hovering around the lowest levels since 2007, overall government transfers to persons were up 0.2% in May and are up 3.8% in the past year. Before the Panic of 2008, government transfers – Medicare, Medicaid, Social Security, disability, welfare, food stamps, and unemployment comp – 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 we have a Plow Horse economy, not a Race Horse economy. On the inflation front, the PCE deflator, the Fed’s favorite measure, increased 0.2% in May. Although it’s only up 0.9% from a year ago, it was up only 0.3% in the year ending in May 2015, so inflation is accelerating. Meanwhile, the “core” PCE deflator, which excludes food and energy, is up 1.6% from a year ago. That’s also below the Fed’s 2% inflation target, but we expect continued acceleration in the year-to-year change in the months ahead. Together with continued employment gains, these data support the case for the Fed to hike rates again in 2016, in spite of fear-mongering by uber-doves. On the housing front, pending home sales, which are contracts on existing homes, declined 3.7% in May after rising 3.9% in April. Combined, the past two months suggests existing home sales, which are counted at closing should be roughly unchanged in June, staying around the highest level since 2007.



Personal Income and Spending <i>All Data Seasonally Adjusted</i>	May-16	Apr-16	Mar-16	3-mo % ch. annualized	6-mo % ch. annualized	Yr to Yr % change
<b>Personal Income</b>	0.2%	0.5%	0.3%	4.3%	3.8%	4.0%
<b>Disposable (After-Tax) Income</b>	0.2%	0.5%	0.4%	4.5%	4.2%	4.1%
<b>Personal Consumption Expenditures (PCE)</b>	0.4%	1.1%	0.0%	6.4%	4.0%	3.7%
<b>Durables</b>	0.3%	2.6%	-0.2%	11.7%	3.6%	3.0%
<b>Nondurable Goods</b>	0.6%	1.7%	0.4%	11.5%	1.4%	1.1%
<b>Services</b>	0.4%	0.7%	-0.1%	4.0%	4.8%	4.6%
<b>PCE Prices</b>	0.2%	0.3%	0.1%	2.2%	0.9%	0.9%
<b>"Core" PCE Prices (Ex Food and Energy)</b>	0.2%	0.2%	0.1%	1.6%	1.8%	1.6%
<b>Real PCE</b>	0.3%	0.8%	-0.1%	4.1%	3.0%	2.7%

Source: Bureau of Economic Analysis