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MONDAY ECONOMIC REPORT

Record Personal Income Growth Spurs Both Spending and Saving

By Chad Moutray – May 3, 2021

The Weekly Toplines

- Personal income soared 21.1% in March, buoyed largely by stimulus checks, the largest monthly increase in the history of the series, which dates to January 1959. Total wages and salaries increased 1.1% in March, or 1.9% in the first quarter overall. Aggregated manufacturing wages and salaries rose 1.4% in March but remained 1.1% lower than before the pandemic.

- Personal consumption expenditures increased 4.2% in March, bouncing back from the 1.0% decline in February and the largest monthly increase since June 2020. Durable and nondurable goods purchases jumped 10.8% and 6.5%, respectively, with service-sector spending up 2.2%.

- Despite the solid increase in personal consumption expenditures in March, the data suggest that Americans saved more of their extra dollars than they spent. As a result, the saving rate nearly doubled from 13.9% in February to 27.6% in March, the highest since April 2020 (33.7%).

- The Conference Board and the University of Michigan both reported that consumer confidence reached the best readings in at least 13 months, with Americans more upbeat about economic growth and the labor market and with increased purchasing intentions in their outlook.

- The U.S. economy grew 6.4% at the annual rate in the first quarter, building on the 4.3% gain in the fourth quarter. The data were buoyed by robust rebounds in consumer spending and sizable growth in business fixed investment and government spending, but growth would have been larger if not for weaknesses in spending on inventories and nonresidential structures and in net exports.

- More importantly, real GDP remains just 0.9% shy of the pre-pandemic levels seen at the end of 2019, and the U.S. economy should return to that pace in the next quarter, even as growth remains well below trend (of where it would have been without COVID-19).

- The current forecast is for 6.5% growth in 2021 overall, boosted by more Americans getting vaccinated, pent-up consumer and business demand and government stimulus.

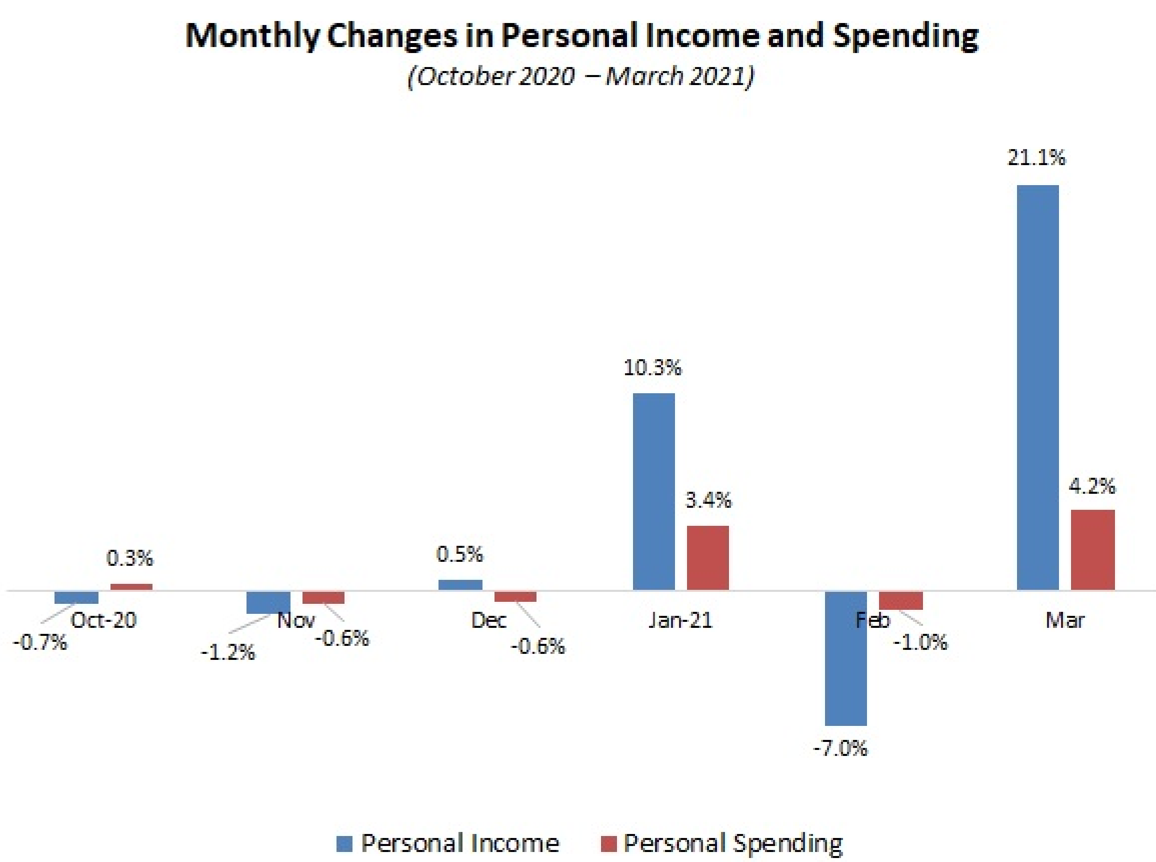
- After falling 0.9% in February, largely from poor weather and supply chain disruptions, new orders for durable goods rose 0.5% in March, or growth of 1.6% with transportation equipment excluded. Overall, the durable goods sector is growing rapidly, rising 4.1% over the past 13 months, or 10.8% with transportation equipment excluded since February 2020.

- Nondefense capital goods excluding aircraft—a proxy for capital spending in the U.S. economy—rose 0.9% to $73.2 billion in March, a new record. Core capital goods orders have soared 10.2% over the past 13 months, as firms have ramped up activity on the brighter economic outlook.

- The PCE deflator rose 0.5% in March, the fastest monthly pace since June 2020. Excluding food and energy prices, the PCE deflator rose 0.4% in March, the most since October 2009. Overall, the PCE deflator has risen 2.3% year-over-year, the most since August 2018, and core inflation has increased 1.8% since March 2020, the fastest pace since August 2019.

- Cost pressures have accelerated, but the key will be whether those price increases are transitory or more sustained. Core inflation is likely to exceed 2% year-over-year in the coming months. To the extent that the current price growth is transitory, the Federal Reserve is likely to accept inflation that runs a little hotter than we have become accustomed to, particularly if the longer-term average continues to hover around 2%, which is its stated goal.

- For its part, the Federal Open Market Committee will continue to pursue extraordinary measures until it achieves its mission of full employment and price stability and until economic growth returns to trend, but the Federal Reserve will also monitor inflationary pressures and supply chain constraints closely moving forward.



Last Week's Indicators:
(Summaries Appear Below)

Monday, April 26
Dallas Fed Manufacturing Survey
Durable Goods Orders and Shipments

Tuesday, April 27
Conference Board Consumer Confidence
Richmond Fed Manufacturing Survey

Wednesday, April 28
Business Employment Dynamics
FOMC Monetary Policy Statement
International Trade in Goods (Preliminary)

Thursday, April 29
Gross Domestic Product (First Quarter)
Weekly Initial Unemployment Claims

Friday, April 30
Employment Cost Index
Personal Consumption Expenditures Deflator
Personal Income and Spending
University of Michigan Consumer Sentiment (Revision)

This Week's Indicators:

Monday, May 3
Construction Spending
ISM® Manufacturing Purchasing Managers' Index®

Tuesday, May 4
Factory Orders and Shipments
International Trade Report

Wednesday, May 5
ADP National Employment Report

Thursday, May 6
Productivity and Costs
Weekly Initial Unemployment Claims

Friday, May 7
BLS National Employment Report

Vuforia Live: Augmented Reality That Inspires

Join this half-day virtual event devoted to all things augmented reality. Featuring sessions on the business value of AR, spotlights on real-world AR case studies and a sneak peek into what the Vuforia team is working on next.

- **Business Employment Dynamics:** Manufacturing experienced a net increase of 102,000 jobs in the third quarter of 2020, beginning the process of bouncing back after plummeting by 54,000 and 888,000 in the first and second quarters, respectively. Manufacturers had gross job gains of 578,000 in the third quarter, with 525,000 from expanding establishments and 53,000 from new establishments. At the same time, gross job losses amounted to 476,000 in the third quarter, with 426,000 from contracting establishments and 50,000 from closing establishments.

  At the same time, 16,559,276 Americans received some form of unemployment insurance benefit (including state and federal programs) for the week ending April 10. That figure declined from 17,405,150 for the week ending April 3, largely on reduced pandemic assistance and state claims.

  More importantly, the report predicts strong consumer spending moving forward. “Overall, the data indicate an exceptional outlook for consumer spending through mid-2022. The size and persistence of the spending gains depend on continued job growth as well as wages that effectively draw people back into the labor force.”

- **Weekly Initial Unemployment Claims:** Initial unemployment claims totaled 553,000 for the week ending April 24, down from 566,000 for the week ending April 17 and the lowest since the week of March 14, 2020. Meanwhile, continuing claims changed little, edging up from 3,651,000 for the week ending April 10 to 3,660,000 for the week ending April 17. That pace remains highly elevated, consistent with 2.6% of the workforce.
  As noted above, raw material costs increased from 6.15% at the annual rate in March to a robust 7.11% in April. Likewise, respondents anticipate an annualized 4.67% increase in costs six months from now, which changed little from 4.66% in the prior survey.

- **University of Michigan Consumer Sentiment (Revision):** Consumer confidence rose from 84.9 in March to 88.3 in April, a 13-month high, according to final data from the University of Michigan and Thomson Reuters. This was an improvement from the previous estimate of 86.5. Americans felt more positive about current economic conditions and in their outlook, with consumers reacting favorably to stronger economic and labor market growth. Increased vaccinations, economic stimulus payments and pent-up demand have helped lift spirits. There was some concern about rising prices in the short term, but respondents felt encouraged by expectations of further reductions in unemployment.

  Total unemployment insurance payments were $541.3 billion in March, up from $535.4 billion in February. Unemployment insurance payments in total averaged $543.3 billion in the first quarter, up from the average of $296.5 billion in the fourth quarter. At the same time, other government social benefits to persons soared to $4.75 trillion in March, a new monthly record, up from $2.36 trillion in January and $782.1 billion in February.

  Total wages and salaries increased 1.1% in March, or 1.9% in the first quarter overall. In the manufacturing sector, wages and salaries rose 1.4% from $904.5 billion in February to $917.1 billion in March. While the sector has bounced back strongly since last spring, total manufacturing wages and salaries remain 1.1% lower than 13 months ago before the pandemic.

Meanwhile, personal consumption expenditures increased 4.2% in March, bouncing back from the 1.0% decline in February and the largest monthly increase since June 2020. Durable and nondurable goods purchases jumped 10.8% and 6.5%, respectively, with service-sector spending up 2.2%. Over the past 13 months, personal spending has risen 3.5%, with durable and nondurable goods soaring 29.5% and 12.4% since February 2020, respectively, but with service-sector purchases down 3.0% over that time frame.

Despite the solid increase in personal consumption expenditures in March, the data suggest that Americans saved more of their extra dollars than they spent. As a result, the saving rate nearly doubled from 13.9% in February to 27.6% in March, the highest since April 2020 (33.7%).

- **Richmond Fed Manufacturing Survey:** Manufacturing businesses in the Richmond Federal Reserve Bank's district continued to expand solidly in April, with the composite index of general business activity unchanged at 17. New orders and capacity utilization both strengthened in April, but shipments, employment and capital expenditures slowed somewhat. The data continue to show lingering supply chain challenges, with the backlog of orders and vendor lead times (which was unchanged) each at their highest point on record and inventories for raw materials and finished goods both falling to all-time lows. Meanwhile, the forward-looking indicators remained encouraging, with manufacturers in the district expecting continued solid growth in activity over the next six months.

  Rising raw material costs continue to be a major concern for manufacturers, and these data are consistent with price growth seen in other economic indicators. While the core PCE deflator did jump in March by the most since late 2009, this likely reflected supply chain disruptions and soaring pent-up demand in the marketplace. The year-over-year data were also skewed by deflationary impacts in March 2020 figures at the beginning of the COVID-19 pandemic (or "base effects").

  As such, cost pressures have accelerated, but the key will be whether those price increases are transitory or more sustained. Core inflation is likely to exceed 2% year-over-year in the coming months. To the extent that the current price growth is transitory, the Federal Reserve is likely to accept inflation that runs a little hotter than we have become accustomed to, particularly if the longer-term average continues to hover around 2%, which is its stated goal. For its part, the Federal Open Market Committee will continue to pursue extraordinary measures until it achieves its mission of full employment and price stability and until economic growth returns to trend (see above), but the Federal Reserve will also monitor inflationary pressures and supply chain constraints closely moving forward.

- **Personal Income and Spending:** Personal income soared 21.1% in March, buoyed largely by stimulus checks, the largest monthly increase in the history of the series, which dates to January 1959. The previous record occurred in April 2020, when personal income rose 12.4%, and government transfer payments and a rebounding economy played a factor in both instances. On a year-over-year basis, personal income has jumped 29.0%.

  In March, goods exports increased across the board, led by steep gains in industrial supplies (up $4.69 billion), capital goods (up $2.84 billion), consumer goods (up $2.30

billion) and automotive vehicles (up $861 million). At the same time, sizable increases occurred in goods imports for consumer goods (up $4.26 billion), industrial supplies (up $3.55 billion), capital goods (up $3.38 billion) and automotive vehicles (up $2.05 billion). Final data will be released May 4, which will also include the service-sector trade surplus.

- **Personal Consumption Expenditures Deflator:** The PCE deflator rose 0.5% in March, up from 0.2% in February and the fastest monthly pace since June 2020. Food and energy costs increased 0.2% and 4.9% for the month, respectively. Excluding food and energy prices, the PCE deflator rose 0.4% in March, the most since October 2009. Overall, the PCE deflator has risen 2.3% year-over-year, the most since August 2018, and core inflation has increased 1.8% since March 2020, the fastest pace since August 2019.

- **International Trade in Goods (Preliminary):** In advance statistics, the goods trade deficit rose from $87.07 billion in February to $90.59 billion in March, a new record. Goods exports jumped from $130.67 billion to $142.05 billion, the strongest pace since October 2018, but those gains were more than outpaced by soaring goods imports, which rose from $217.74 billion to $232.63 billion, an all-time high. Breaking down the details in this report:

  The Federal Reserve noted strengthening output and employment in the U.S. economy, with vaccinations and pent-up demand helping to boost activity. Vaccinations have helped buoy growth and the outlook, with future progress hinging on continued progress in the battle against COVID-19. The statement noted that economic growth remains below trend, especially in those sectors hit harder by the pandemic, and inflation has accelerated. While price growth is seen as being largely “transitory,” the FOMC will continue to monitor it.

  Overall, the FOMC plans to continue its current stance on monetary policy for the foreseeable future, including keeping interest rates near zero and maintaining asset purchases at current levels. This could change with incoming data and economic progress.

  With that said, I would not be surprised if the Federal Reserve starts to taper (or slow) purchases later this year given the current strong forecasts for economic growth. I would also anticipate higher interest rates at some point in 2022.

  - **Personal consumption expenditures** increased an annualized 10.7% in the first quarter, jumping strongly from the 2.3% gain in the fourth quarter. Goods spending soared 23.6% at the annual rate in the first quarter after pulling back 1.4% in the previous report, with durable and nondurable goods purchases up 41.4% and 14.4%, respectively. Service-sector spending rose 4.6% in the first quarter, increasing for the third straight quarter. Goods consumption contributed 4.94% to headline growth in real GDP, with spending on services adding another 2.07% (for a total of 7.07% from personal consumption expenditures overall). As such, consumer spending was the largest bright spot in this release, as Americans opened their pocketbooks once again and resumed some semblance of normalcy. Government stimulus checks were also a major factor.

  - **Business investment** data provided mixed results in the first quarter. Fixed investment grew 10.1% at the annual rate in the latest data, rising for the third consecutive quarter and buoyed by strong growth in spending on equipment and intellectual property products, up 16.7% and 10.1%, respectively. Residential investment also remained encouraging, up 10.8% for the quarter. On the other hand, investment in structures fell for the sixth straight quarter, down 4.8% in the first quarter. Overall, business fixed investment added 1.77% to topline GDP growth in the first quarter, but spending on inventories plummeted, subtracting 2.64% from headline growth. As a result, gross private domestic investment subtracted 0.87% from real GDP in the quarter.

  - **Net exports of goods and services** also subtracted 0.87% from topline growth in the first quarter, dragging down real GDP for the third consecutive quarter. Imports have continued to recover faster than exports. Real goods exports were off 0.9% at the annual rate in the first quarter, but real goods imports rose 5.5%. Indeed, real goods imports have increased 6.7% since the fourth quarter of 2019 (before the pandemic), whereas real goods exports remain down 3.8% over that time frame.

  - **Government spending** contributed 1.12% to real GDP growth in the first quarter after being a drag on growth in the previous two reports. Federal government spending rose 13.9% at the annual rate in the first quarter, boosted by economic recovery spending. At the same time, state and local government spending rose 1.7%, the first positive reading in one year.

- **Gross Domestic Product:** The U.S. economy grew 6.4% at the annual rate in the first quarter, building on the 4.3% gain in the fourth quarter. The data were buoyed by robust rebounds in consumer spending and sizable growth in business fixed investment and government spending, but growth would have been larger if not for weaknesses in spending on inventories and nonresidential structures and in net exports. More importantly, real GDP remains just 0.9% shy of the pre-pandemic levels seen at the end of 2019, and the U.S. economy should return to that pace in the next quarter, even as growth remains well below trend (of where it would have been without COVID-19). The current forecast is for 6.5% growth in 2021 overall, boosted by more Americans getting vaccinated, pent-up consumer and business demand and government stimulus.

  Benefits costs for manufacturing employees increased 0.4% in the first quarter, down from 0.6% in the fourth quarter. On a year-over-year basis, benefits have risen 2.1%. Overall, total manufacturing compensation rose 0.5% for the quarter, or 2.3% year-over-year.

- **FOMC Monetary Policy Statement:** The Federal Open Market Committee continued to pursue extraordinary monetary policies as it seeks its dual mandate of full employment and price stability. The Federal Reserve will keep the target federal funds rate at 0 to 25 basis points, and it will continue purchasing at least $120 billion in Treasury securities and agency mortgage-backed securities each month. These actions have kept the federal funds rate near zero since March 15, 2020, with the Federal Reserve's balance sheet nearly doubling over that time frame, up to $7.82 trillion in the latest data.

  In addition, nondefense capital goods excluding aircraft—a proxy for capital spending in the U.S. economy—rose 0.9% from $72.5 billion in February to $73.2 billion in March, a new record. Core capital goods orders have soared 10.2% over the past 13 months, as firms have ramped up activity on the brighter economic outlook.

  In March, new orders increased for motor vehicles and parts (up 5.5%), communications equipment (up 4.3%), fabricated metal products (up 3.6%), other durable goods (up 2.3%), primary metals (up 1.2%) and machinery (up 1.0%). At the same time, activity fell for nondefense aircraft and parts (down 46.9%), defense aircraft and parts (down 20.2%), electrical equipment, appliances and components (down 1.5%) and computers and related products (down 1.4%).

Meanwhile, durable goods shipments increased 2.5% in March, rebounding after falling 3.6% in February, with a 1.5% gain with transportation equipment excluded. Over the past 13 months, durable goods shipments have risen 4.0%. Excluding transportation, shipments have increased 7.7% since February 2020. In addition, core capital goods shipments increased 1.3% from $71.2 billion to $72.1 billion, another all-time high, but with 8.9% growth over the past 13 months.

- **Employment Cost Index:** Private manufacturing wages and salaries rose 0.6% in the first quarter, the same pace as in the prior two quarters. That translated into 2.5% growth over the past 12 months, the slowest pace since the fourth quarter of 2017. For all private-sector employees, wages and salaries increased 1.1% in the first quarter, up from 0.8% in the fourth quarter, with 3.0% growth year-over-year, a four-quarter high.

  Looking ahead, manufacturers in the Texas district remained upbeat in their outlook for the next six months, with the forward-looking composite measure increasing from 33.7 in March to 36.6 in April, the best reading since October 2018. The underlying data point to robust growth anticipated over the coming months, with the expected employment measure rising at a record pace. Input prices are forecasted to continue to accelerate rapidly, albeit with the index pulling back slightly from the strongest reading since March 2012.

- **Durable Goods Orders and Shipments:** After falling 0.9% in February, largely from poor weather and supply chain disruptions, new orders for durable goods rose 0.5% in March, recovering some of the earlier decline. Yet, transportation equipment orders fell 1.7% in March on sizable reductions in defense and nondefense aircraft and parts sales. With transportation equipment excluded, new durable goods orders increased 1.6% in March, bouncing back from the 0.3% decline in February. Overall, the durable goods sector is growing rapidly, with significant gains since declining sharply last spring due to the COVID-19 pandemic. Indeed, durable goods orders have jumped 4.1% over the past 13 months, or 10.8% with transportation equipment excluded since February 2020. (Year-over-year growth for new durable goods orders was 25.0%, but that reflects plummeting activity at the beginning of the COVID-19 crisis in March 2020 as much as the gain seen in the latest data.)

  Survey respondents felt optimistic about the labor market and income prospects. The percentage of respondents suggesting that business conditions were “good” rose from 18.3% to 23.3%, while the percentage feeling that conditions were “bad” dropped from 30.1% to 24.8%. In addition, the percentage of respondents suggesting jobs were “plentiful” increased from 26.5% to 37.9%, while those saying jobs were “hard to get” fell from 18.5% to 13.2%.

  Regarding the outlook, the percentage of consumers anticipating better business conditions over the next six months edged up from 40.3% to 40.5%, while those predicting a worsening of conditions was unchanged at 11.9%. At the same time, the percentage of respondents expecting more jobs in the next six months declined from 35.9% to 34.5%, while those expecting fewer jobs rose from 14.4% to 15.5%.

- **Dallas Fed Manufacturing Survey:** Manufacturing activity continued to expand strongly, with the composite index of general business conditions rising from 28.9 in March to 37.3 in April, the best reading since June 2018. New orders and employment both strengthened at the fastest paces in the survey's history, which dates to June 2004. At the same time, shipments, production, capacity utilization and capital expenditures slowed in April, but with each measure continuing to expand solidly. With that said, supply chain disruptions pushed growth in raw material prices to the fastest pace since October 2004, or just shy of a record high. This is a trend seen in other reports as well.

In addition, there were 6,000 manufacturing start-ups in the third quarter, or a rate of 1.9% of all establishments in the sector. Those new establishments (or "births") employed 23,000 workers in the third quarter, up from 21,000 in both the first and second quarters. The pace of manufacturing start-ups has been relatively flat for about a decade, and notably, entrepreneurship in the sector (as well as economy-wide) has slowed from the rates in the 1990s and early 2000s.

- **Conference Board Consumer Confidence:** According to the Conference Board, consumer confidence moved sharply higher, up from 109.0 in March to 121.7 in April, the best reading in 14 months, or since the COVID-19 pandemic began. Americans felt more upbeat in their assessments of current and future economic conditions. More importantly, consumers expressed greater willingness to open their pocketbooks and spend more, and with increased vaccination rates, vacation intentions also rose.

Take Action

- The Manufacturing Institute and Deloitte will host a webinar, "Creating Pathways for Tomorrow's Workforce Today: Beyond Reskilling in Manufacturing," on Thursday, May 6, at 1:00 p.m. EDT in conjunction with an updated release of the skills gap study. Deloitte Human Capital Practice Managing Director Victor Reyes will join MI Executive Director Carolyn Lee for a discussion of the highlights of the report and current and future labor force conditions for manufacturers. Chad Moutray, the MI's director for the Center for Manufacturing Research, will also provide an economic overview. Click here for more information and to register.

Questions or comments? Email NAM Chief Economist Chad Moutray at cmoutray@nam.org.