



# Economics Group

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## Consumer Spending Drove Economic Growth in Q2

*June spending data suggest the consumer is on pretty solid footing, and a pop in the consumer confidence index for July suggests spending should remain elevated. The Fed is still set to cut rates 25 bps tomorrow.*

### The Consumer Sector Remains Healthy

Going into this morning's personal income and spending report, we already knew real personal consumption expenditures (PCE) grew at a solid 4.3% annualized pace in the second quarter, so a solid read on the consumer didn't come as a surprise.

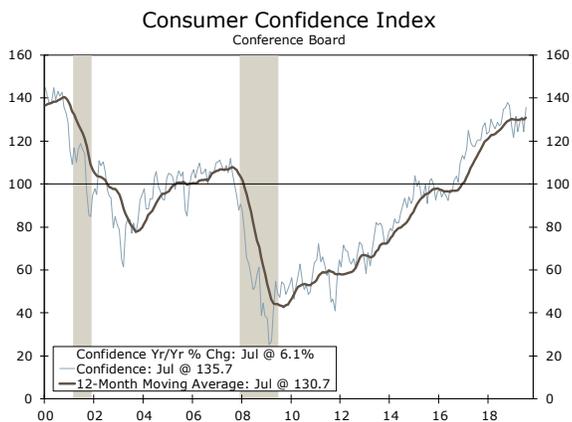
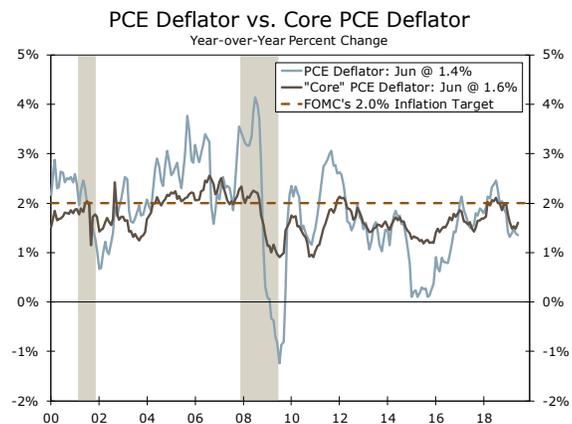
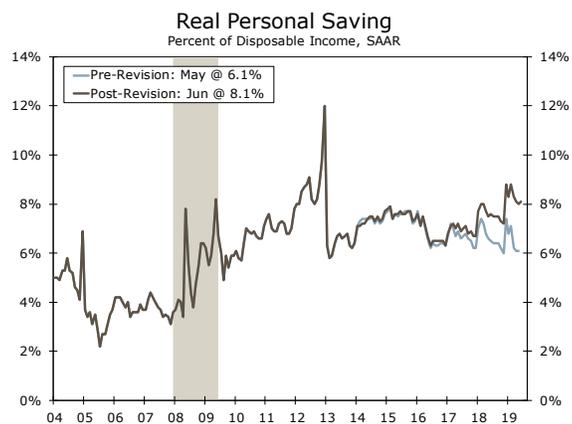
Real personal spending rose for the fourth consecutive month, up 0.2% in June following back-to-back 0.3% gains in April and May. Consumers have also seen steady income gains in recent months. Personal income rose for the fourth consecutive month, up 0.4%, led by a 0.5% jump in wages and salaries.

This morning's personal income and spending report reflected the annual update to the National Income and Product Accounts, which revised data since 2014. Perhaps most notable was the upward revision to the personal saving rate, as depicted in the top chart. The upward revision to the saving rate may help explain the weaker consumption in the first quarter, as the stock market sell-off and trade uncertainty at the end of last year weighed on consumption and confidence measures. But, at 8.1% in June, the real personal saving rate is an encouraging sign for the health of the consumer in the late stage of this expansion.

The Fed's preferred measure of inflation—the core PCE deflator—rose slightly to 1.6% in June on a year-over-year basis. But, at 1.4%, the headline PCE deflator still remains well-below the Fed's 2.0% inflation target (middle chart). Despite this uptick in core inflation and the strong report on the consumer, we still look for the FOMC to cut the fed funds rate 25 bps tomorrow, as below-target inflation and trade and other geopolitical uncertainties cloud the economic outlook.

What does a Fed rate cut mean for the consumer? As we [wrote](#) recently, we do not expect the consumer sector will get the same benefit from Fed rate cuts it did in the past. Since the last recession, U.S. household debt has grown exclusively in two categories: student and auto loans, which tend to have fixed rates that do not move in lockstep with a lower fed funds rate.

Still consumer spending looks set to rise in the second half of the year. In a separate release from the Conference Board this morning, we learned the consumer confidence index surged 11.4 points to 135.7 in July. That was the largest monthly pop since November 2011 and brought the index to its highest level this year. This gain follows a sharp drop in June, when trade uncertainty weighed on confidence. Notably, the expectations component also rose to its highest level this year, suggesting—if sustained—consumer spending should remain solid. The 4-handle for PCE notched in the second quarter, however, is unlikely to be sustained, and PCE growth will likely slow to a 2-2.5% pace in the second half of the year.



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