June 4, 2020

ECONOMIC REPORT

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CONSUMER SPENDING PLUNGES IN APRIL, BUT INCOME WAY UP; MAY ADP JOB LOSSES NOT AS BAD AS FEARED

SUMMARY

- Household spending fell 14 percent in April as pandemic-related restrictions on movement kept consumers inside.
- After-tax income jumped 12 percent in April thanks to stimulus efforts.
- Consumer spending should rebound in May as restrictions on economic activity are gradually lifted.
- The U.S. lost a net 2.76 million jobs in May, according to data from ADP.
- PNC expects the official BLS employment report for May to show job losses of more than 9 million and an unemployment rate of about 19 percent.

Consumer spending fell 13.6 percent in April from March before adjusting for inflation, as the coronavirus pandemic and restrictions on economic activity led households to cut back on their purchases. This was by far the biggest one-month drop in spending in the history of the series, going back to 1959. Spending on durable goods fell 17.3 percent over the month, spending on nondurable goods fell 16.2 percent, and spending on services fell 12.2 percent.

While spending declined in April, personal income rose 10.5 percent, and disposable (after-tax) income jumped 12.4 percent. Both of these were the biggest one-month gains in their respective histories, also going back to 1959. Labor market income fell 7.7 percent in April (another record) due to enormous job losses and pay cuts. But there was an enormous 90 percent increase in transfer payments; this included the one-time stimulus payments sent to most households. In addition, millions applied for unemployment insurance; bonus unemployment payments and an expansion in coverage provided an extra boost. Tax payments fell 7.4 percent in April as reduced labor income led to less withholding and smaller payroll tax payments.

With spending down and income up, the saving rate jumped to 33.0 percent, from 12.7 percent in March and 8.2 percent in February. This is by far the highest saving rate on record.

Both overall and core (excluding food and energy) prices fell sharply in April. The overall personal consumer expenditures price index dropped 0.5 percent in April, with the core PCE price index down 0.4 percent. While very large, these one-month price declines were not the biggest on record. On a year-ago basis PCE prices were up 0.5 percent, with core inflation at 1.0 percent.

With prices down in April, real (inflation-adjusted) personal disposable income rose 13.4 percent over the month, while consumer spending fell 13.2 percent. Both of these were records.

On a year-ago basis real personal disposable income was up 13.8 percent, with real consumer spending down 17.3 percent. Both of these were records (see Chart 1).

The April report on personal income and outlays set lots of records, both bad and good. The bad news is that consumer spending plunged by the largest amount on record, across a variety of measures: nominal and real, one-month and year-ago. Households were unable to spend because of restrictions on movement and, to a lesser extent, were cautious with their spending because of job losses. But the good news is that the various stimulus efforts—one-time checks and expanded unemployment insurance benefits—more than made up for the loss in income from the pandemic. This means households do have money, and spending should improve as restrictions on movement are gradually lifted. High-

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frequency measures of consumer activity, such as restaurant bookings and credit card data, show that spending is picking up as consumers venture out of their homes. May consumer spending should move higher, albeit from very low levels.

Inflation is not a concern for the Federal Reserve. With prices falling in March and April, the central bank should be more worried about deflation, when prices are declining broadly. Deflation can wreak havoc on an economy, causing consumers and businesses to put off purchases in expectations of a better deal in the future; this can exacerbate and extend a recession. Prices are likely to start increasing again later this year as the economy picks up, but the potential for extended deflation must be taken seriously.

Net private-sector employment fell by 2.76 million in May, according to the ADP National Employment Report, based on data from the payroll-processing firm (see Chart 2). Although still an enormous number of job losses, it was much less than the 19.557 million jobs lost in April, and the 9 million consensus for May; PNC expected job losses of 8 million in the ADP report. April job losses were revised lower, with fewer job losses than the initially reported 20.236 million.

The industrial mix of job losses changed dramatically from April to May. In April more than 40 percent of job losses were in leisure/hospitality services, as hotels and restaurants closed due to the coronavirus pandemic and restrictions on economic activity. There were also large numbers of job losses in trade/transportation/utilities (17 percent of job losses) as many retail stores closed, and construction (12 percent) as job sites were shuttered. But in May, trade/ transportation/utilities had the greater number of job losses (30 percent), and manufacturing was second (26 percent). This suggests that the secondary effects of the pandemic are rippling through the economy due to lower demand, and not just restrictions on movement.

Employment losses in goods-producing industries were 794,000, with the bulk of those in manufacturing (719,000). Construction employment losses were just 22,000 as building resumed in many parts of the country. Private services-providing industries lost 1.967 million jobs in May, including 826,000 in trade/transportation/utilities. There were job losses of more than 300,000 in health care/social

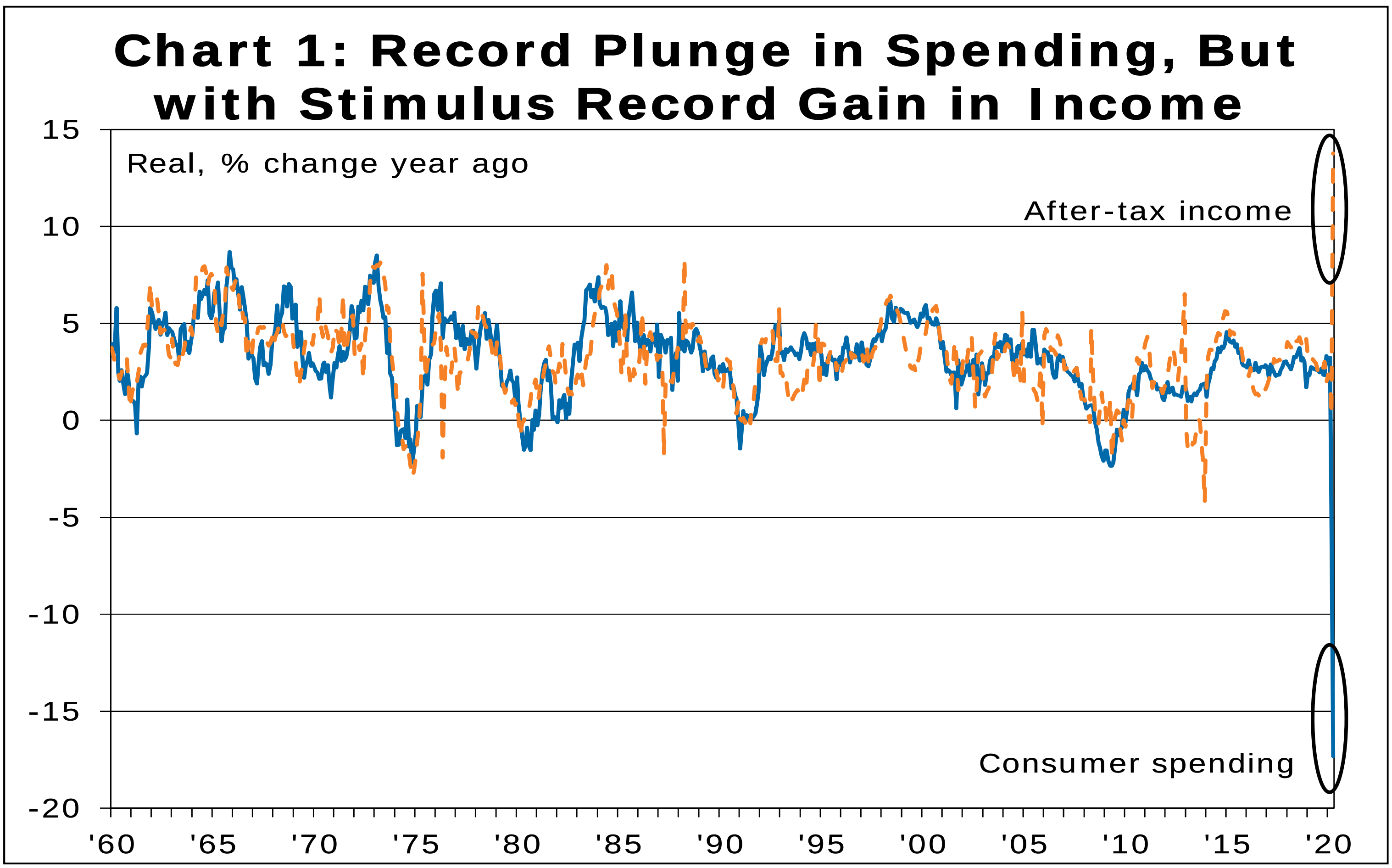

Chart source: BEA

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assistance and other services; 250,000 in professional/business services; and between 100,000 and 200,000 in financial activities, information, and leisure/hospitality services. Private education actually added 166,000 jobs in May.

The May ADP employment report was bad, but not nearly as bad as it could have been. While job losses were enormous, with employment falling 2.5 percent over the month, that was much smaller than the 15.1 percent plunge in April. Job losses were also well below the consensus of 9 million, based on unemployment insurance data.

There are two big questions about the job market over the next few months. First, will job losses turn to job gains as businesses reopen? If businesses quickly restart and most workers are quickly rehired, the structural damage to the economy would be limited and stimulus programs would bridge the gap until the labor market turns around. Second, if job growth does resume soon, will it be fast enough to bring back millions of jobs in the second half of 2020, rapidly replacing those jobs lost during the Viral Recession? Or will it be a much slower process? There are a number of factors that will drive the labor market in the second half of 2020: the success of efforts to control the spread of the coronavirus, the effectiveness of programs designed to help businesses stay open through the immediate crisis, and the willingness of consumers to spend and businesses to invest as firms gradually reopen.

The Bureau of Labor Statistics releases the government's official jobs report for May on Friday, June 5, at 8:30 AM. PNC expects job losses of about 8.5 million for May, but that was prepared before the better-than-expected May ADP report. PNC expects the unemployment rate to increase to 19.3 percent in May, from 14.7 percent in April. These are the highest unemployment rates since the Great Depression in the 1930s.

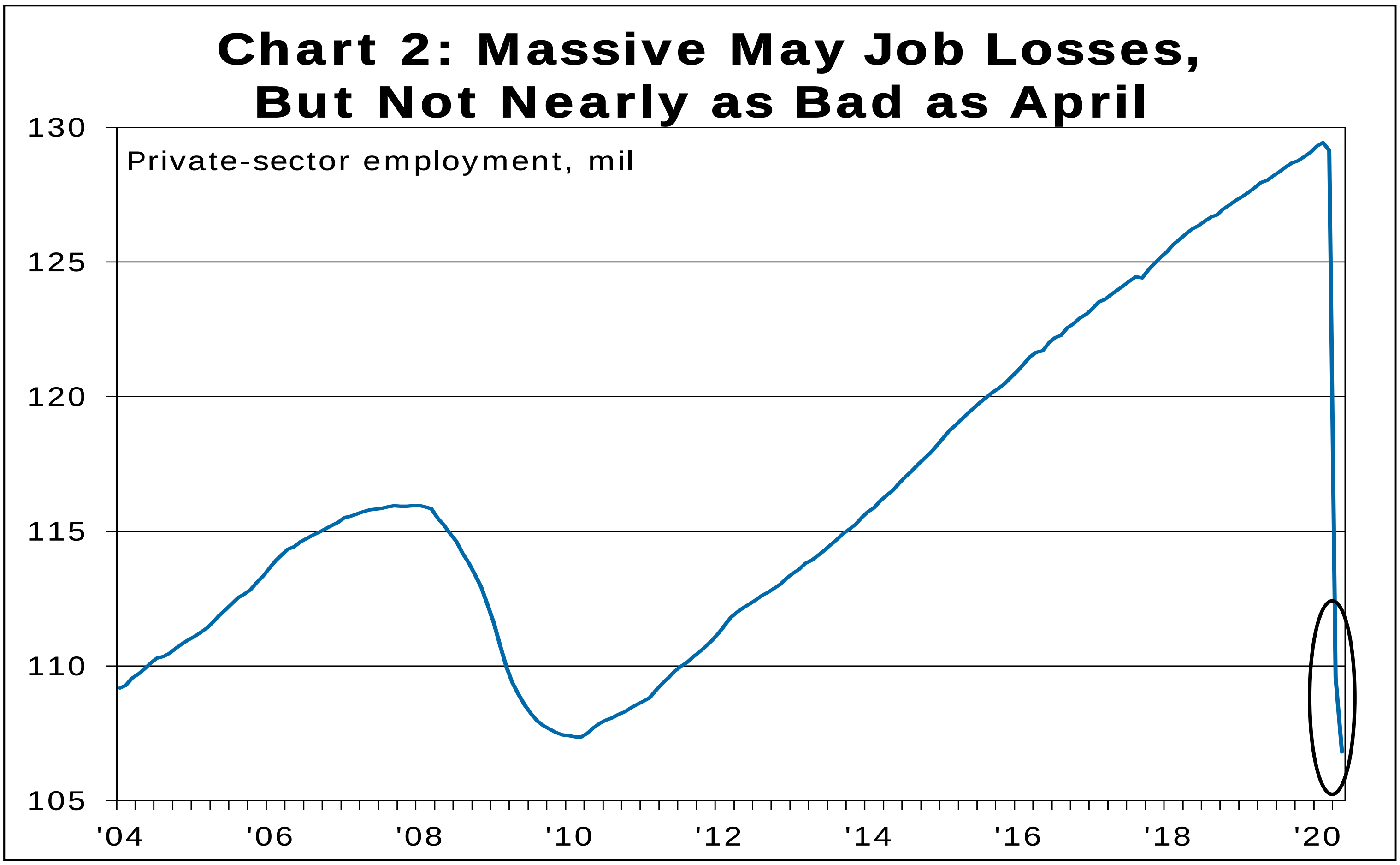

Chart source: ADP

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