

US: DECENT END TO Q3 PERSONAL SPENDING SETS FAVORABLE Q4 STARTING POINT

** US real personal spending advanced 0.3% m/m in September, making up for the downwardly revised 0.2% decline in August*

** With job growth and aggregate income gains expected to slow, personal spending will not be able to boost GDP as much as before*

***The Fed's preferred measure of consumer inflation, the core PCE deflator rose 0.1%, maintaining the 1.7% yr/yr rise**

The 0.3% rise in real consumption in September implies a pick-up in momentum at the end of Q3 and sets a decent starting point for private consumption in Q4 (see Chart 1). Expect real consumption to grow near 2.0% again in Q4.

The risks to Q4 GDP are tilted to the downside. With job growth and aggregate income gains expected to slow, personal spending is vulnerable. Moreover, the net trade deficit receded in Q3 and boosted Q3 GDP by 0.8pp, but this involved an unsustainable spike in agricultural goods exports (see Chart 2) that will be reversed in Q4. Similarly, inventory investment is unlikely to repeat its sizable contribution of 0.6pp to GDP growth. Taken together, GDP growth is likely to slow from 2.9% to around 2% in Q4.

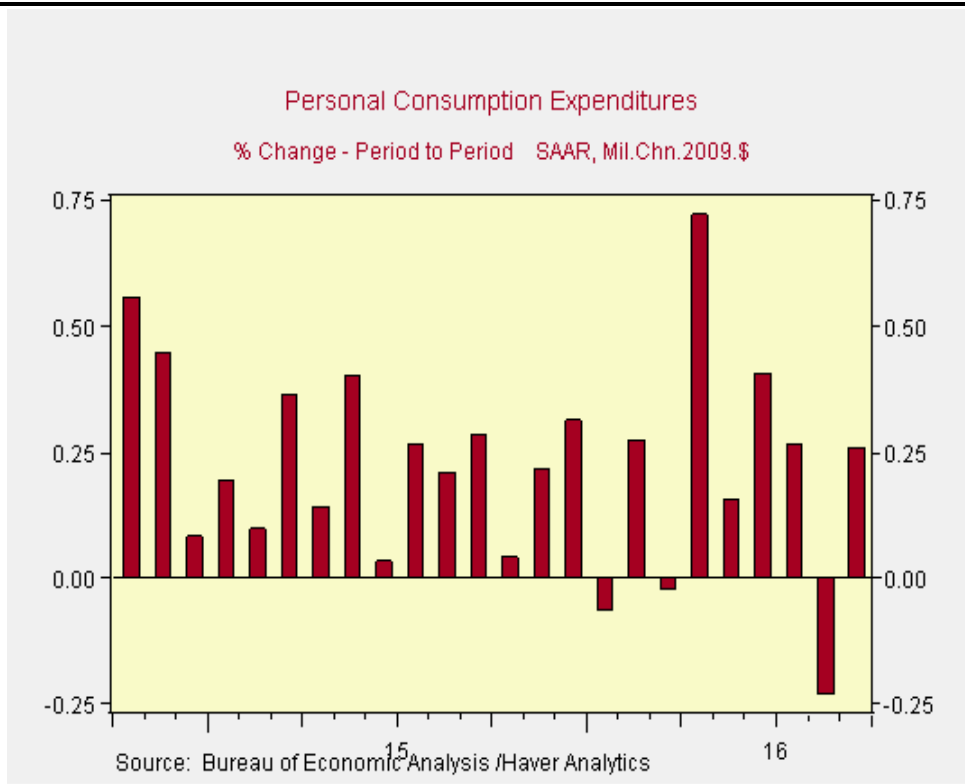
Real disposable personal income rose by only 0.05% m/m (+2.1% yr/yr) in September (see Chart 3), bringing the personal saving rate down slightly to 5.7%, which is still elevated, providing a decent cushion. Consumer confidence – although still high – started off Q4 on a subdued note, declining in October (see Chart 4).

On prices, the Fed's preferred measure of consumer inflation, the core PCE deflator, rose 0.1% m/m September (compared to 0.2% in August), but maintaining its yr/yr rise at 1.7%, very close to the Fed's 2% target.

Even though it looks like real GDP growth will decelerate decidedly in Q4, expect the Fed to increase interest rates at its December meeting. As Fed Vice Chairman Stanley Fischer has stated, the Fed has achieved its employment mandate and inflation is very close to the Fed's 2% longer-run target.

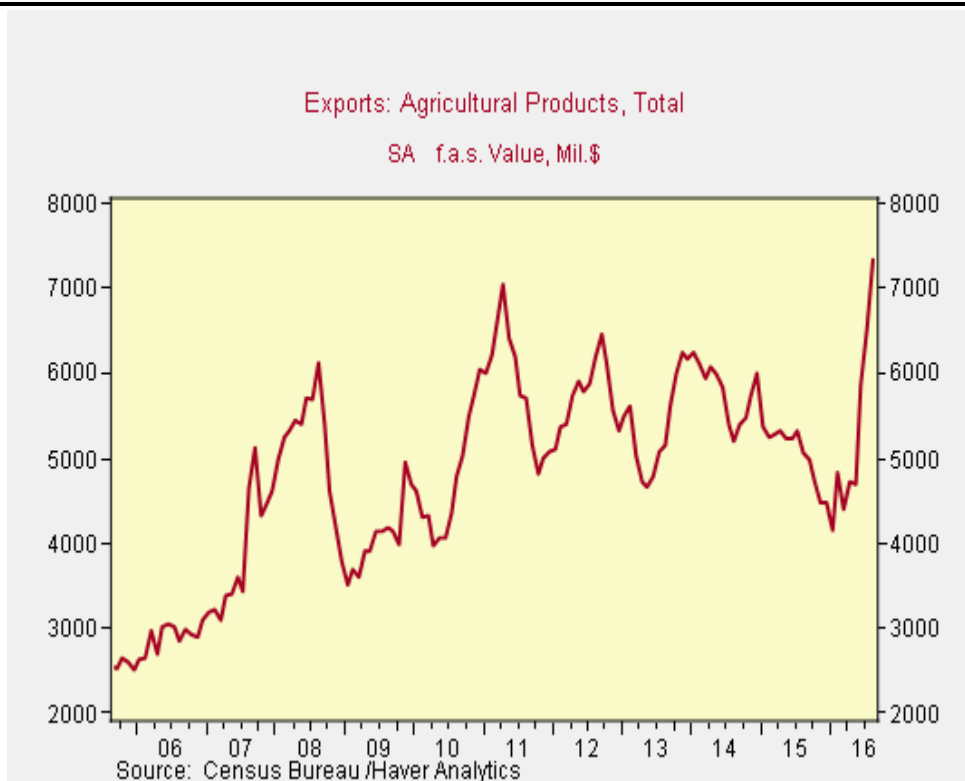
31 October 2016

Chart 1: Real personal consumption expenditures



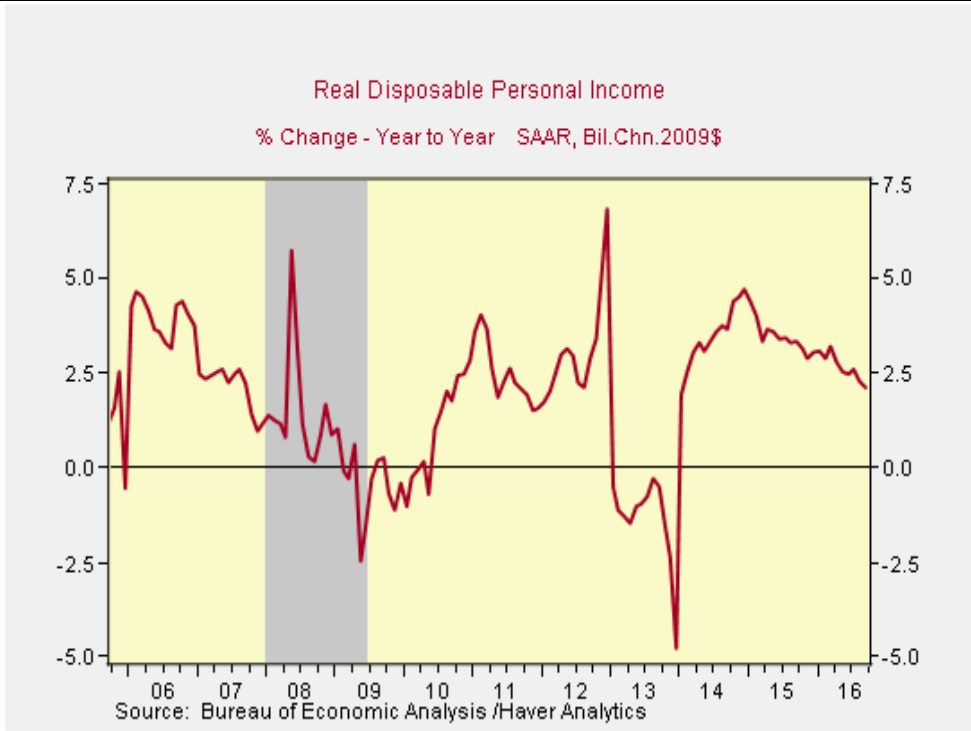
Source: Monthly data. Source: Bureau of Economic Analysis and Haver Analytics

Chart 2: Exports of agricultural products



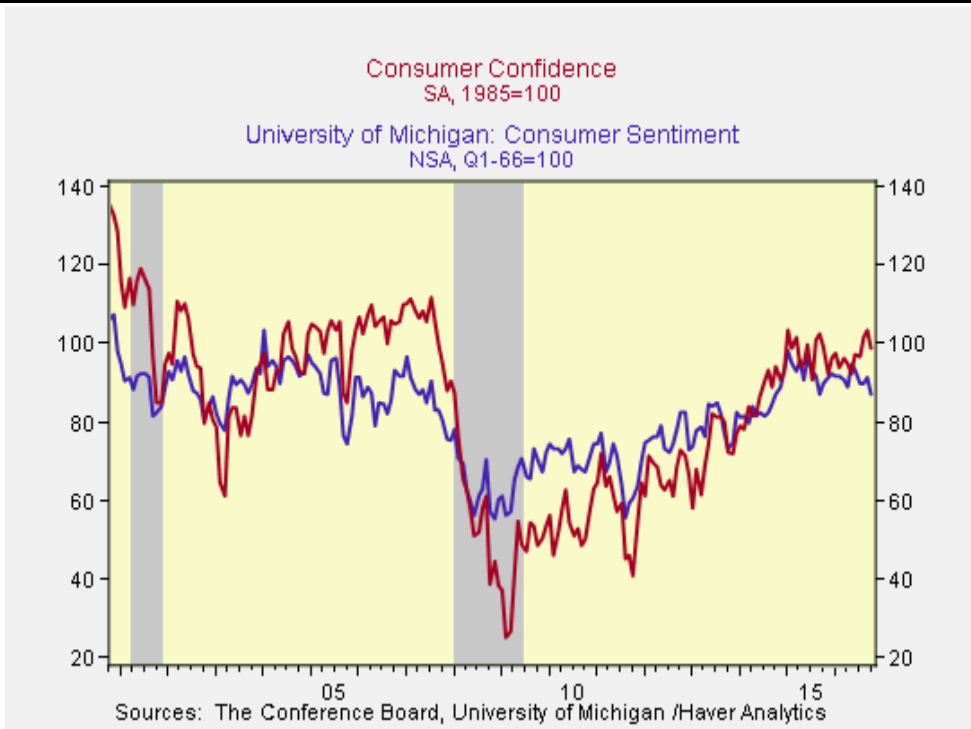
Source: Monthly data. Source: Census Bureau and Haver Analytics

Chart 3: Real disposable personal income (yoy)



Source: Monthly data. Source: Bureau of Economic Analysis and Haver Analytics

Chart 4: University of Michigan's and the Conference Board's consumer confidence indexes



Source: Monthly data. Source: University of Michigan, the Conference Board and Haver Analytics

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