# Economic Update

August 30, 2024

## Consumers Continued to Spend in July as Incomes Rose; Slowing Inflation Supports September Fed Rate Cut

- **Consumer spending rose a strong 0.5% in July from June.**
- **After-tax income rose 0.2% over the month.**
- **Inflation continues to ease, with both the overall and core PCE price indices up a moderate 0.2% for the month.**
- **Slowing inflation supports a cut in the fed funds rate at the FOMC's mid-September rate cuts, with additional rate cuts into 2025.**
- **Consumer spending growth will slow in the near term but remain positive, supported continued economic expansion.**

Consumer spending increased 0.5% in July before adjustment for inflation (nominal), according to the Personal Income and Outlays report from the Bureau of Economic Analysis. Both nominal personal income and nominal after-tax income rose 0.3% for the month.

Both the overall and core personal consumption expenditures price indices rose 0.2% over the month. On a year-ago basis overall inflation was 2.5% in July, the same pace as in June. Core PCE inflation, excluding volatile food and energy prices, was 2.6% in July, the same rate of inflation as in May and June. Inflation continues to gradually ease, headed toward the Federal Reserve's 2% objective.

With moderate inflation real (inflation-adjusted) after-tax income rose 0.1% in July, with real consumer spending up a strong 0.4%.

Consumers continue to spend in mid-2024, pushing the U.S. economy forward. Household incomes are rising with the solid labor market, including moderate job growth and wages that are increasing more quickly than inflation. Additional support to consumer spending, particularly for higher-income households, is coming from the strong stock market and rising home values.

Some households are under stress, however. Interest rates are elevated and there are rising consumer delinquency rates, particularly for lower- and middle-income households that have borrowed in response to high inflation. Consumers should get some relief, however, with the Federal Reserve set to cut the federal funds rate in a few weeks. PNC expects slower consumer spending growth in the second half of this year, but not an outright contraction. Spending growth will then pick up in mid-2025 as lower interest rates support purchasing. The U.S. economy should avoid recession as long as the labor market remains good and consumers continue to spend.

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Inflation continues to ease. Core PCE inflation, the Federal Reserve's preferred inflation measure, peaked at 5.6% year-over-year in early 2022 and has been gradually slowing since then. And over the past three months core PCE inflation was 1.7% on an annualized basis, below the central bank's 2% objective. With modest monthly price increases inflation should slow further in the near term. At the same time the labor market, although good, is not as good as it was a year ago. Given slowing inflation and an easing job market, the Federal Open Market Committee is set to cut the federal funds rate, its key short-term policy rate, by 25 basis points at its next meeting on September 18. The fed funds rate is currently in a range between 5.25% and 5.50%, the highest it has been in more than two decades, and has been in that range for more than a year. PNC expects additional rate cuts at the FOMC's two remaining meetings this year, which would bring the funds rate to a range of 4.50% to 4.75% at the end of 2024. The FOMC will cut the fed funds rate further in 2025, down to around 3.5% by the middle of next year.

Nominal (not inflation-adjusted) wages and salaries rose 0.3% in July as job and wage gains continue. There was a large 1.4% nominal increase in consumer spending on durable goods as auto sales rebounded in July after the CDK Global cyberattack weighed on auto sales in June. Nominal spending on nondurable goods rose 0.4%, as did nominal spending on services.

With spending up more than incomes the personal saving rate fell to 2.9% in July from 3.1% in June, and 4.0% in January. At some point the saving rate will need to rise, which means that consumer spending will need to increase more slowly than incomes. That need to raise savings will be a drag on near-term consumer spending growth.

There were upward revisions to nominal consumer spending growth in May, June, and July. That, in turn, contributed to the upward revision in real GDP growth for the second quarter to 3.0% annualized, from 2.8%, reported yesterday by the BEA.

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