Rising Income and Elevated Savings Bode Well for Future Spending

Scott McIntyre, CFA
HilltopSecurities Asset Management
Senior Portfolio Manager
Managing Director
512.481.2009
scott.mcintyre@hilltopsecurities.com

Greg Warner, CTP
HilltopSecurities Asset Management
Senior Portfolio Manager
Director
512.481.2012
greg.warner@hilltopsecurities.com

Most analysts expect continued deceleration in the pace of GDP growth in the first quarter of 2021, but recent data and encouraging vaccine progress suggest Q1 weakening could be limited. This morning, a report from the Commerce Department showed a +0.6% increase in personal income for December, well above the +0.1% forecast. December income was boosted by an increase in pandemic unemployment compensation at the federal level. However, at the same time income rose, personal spending fell for the second straight month. The -0.2% spending decline in December followed a revised -0.7% drop in November. The fact that Americans chose to curtail their consumption late in the year reflected the worsening virus outlook and uncertainty over the next round of government support. The increased income combined with the decreased spending drove the December savings rate up for the first time since April. The lofty 13.7% savings rate, roughly five-times what it had been four years ago, indicates *future capacity to spend*.

The expectation, right or wrong, is that first quarter growth will be sluggish... but growth will pick up considerably in the second half of the year as more and more Americans are vaccinated. This morning, Johnson & Johnson announced the trial results of its single shot vaccine, which prevents 66% of moderate to severe cases, but more importantly, 85% of severe infections and *100% of deaths and hospitalizations*. J&J expects to file for emergency-use authorization next week, and hopes to bring the vaccine to market by March.

The fact that Americans chose to curtail their consumption late in the year reflected the worsening virus outlook and uncertainty over the next round of government support.

Yesterday, according to Commerce Department data, GDP grew at a +4.0% annualized rate in the fourth quarter. This was down from the record +33.1% advance in the third quarter and just below the +4.2% median forecast. Following the initial Q4 reading, GDP remains down -3.5% for all of 2020. Personal consumption, which historically contributes about two-thirds of GDP growth, rose by just +2.5%, down from +41% in Q3...but still historically solid. Residential investment (housing) and business investment made substantial contributions during the quarter. Net exports were the biggest drag in Q4 as much of the global economy concentrated less on spending and more on combating the virus. Inventory accumulation also fell short of expectations. *Both net exports and business inventories are likely to take a step forward later this year as conditions improve.*

Both net exports and business inventories are likely to take a step forward later this year as conditions improve.

As it stands, the elevated savings rate, expectation of additional government support, progress on the vaccine front and relatively lean business inventories all hint at higher future spending and production, and an improving outlook for the first quarter and beyond.

Stocks are down again today. The recent short-squeezing show has untethered the equity market from reality and introduced yet another layer of uncertainty.

Please see disclosure starting on page 2.

Market Indications as of 11:45 A.M. Central Time

DOW	Down 609 to 29,995 (HIGH: 31,188)
NASDAQ	Down 316 to 13,021 (HIGH: 13,636)
S&P 500	Down 67 to 3,720 (HIGH: 3,855)
1-Yr T-bill	current yield 0.08%; opening yield 0.08%
2-Yr T-note	current yield 0.11%; opening yield 0.12%
5-Yr T-note	current yield 0.43%; opening yield 0.43%
10-Yr T-note	current yield 1.07%; opening yield 1.05%
30-Yr T-bond	current yield 1.83%; opening yield 1.81%