*econ today*SM *economics - without the hype*

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Construction and Manufacturing; Spending and Income

December's construction spending grew 0.4% from November. (Comparisons are between monthly estimates which are seasonally adjusted and then annualized.) In 2003, construction spending grew 7.0% over 2002.

The Institute for Supply Management's January estimate of manufacturing activity was essentially unchanged from December: 63.6 compared to 63.4. This means that the overall level of manufacturing activity is still expanding.

December's Personal Income rose 0.2% and Personal Spending rose 0.4% over November. Personal Savings fell to a level of 1.3% of disposable income compared to 1.5% in November.

Construction Tapers Off

Construction spending can be broken up into several categories: residential vs. non-residential is one way, and public vs. private is another. Right now, the first way of slicing the pie tells the more important story. Residential construction carried the industry during 2003, no surprise there, but I'm not sure we realize how strong it actually was.

From July to September, construction spending grew an average of 2.24% a month, around a 30% annualized rate. During the same time period, non-residential construction actually slowed down slightly. The full year numbers for 2003 reflect this: residential grew 13.5% from 2002 while non-residential did not grow at all. But since October, construction spending has tapered off; this could signal a slowing trend, particularly in residential as mortgage rates are off their lows of last summer and new home sales have also slowed somewhat.

Industrial Economy Continues to Grow

Today's Institute for Supply Management (ISM) Index was marginally higher than last month's. It was driven by a big increase in the component that measures prices paid by manufacturers for their inputs. It confirms a similar increase in the Chicago Purchasing Managers' Index of last week, leading us to suspect that pressure to raise prices is increasing at the manufacturing level.

On the other hand, the national ISM numbers do not confirm the stronger production figures from the Chicago area. Forward looking parts of the ISM report, 'new orders' and 'new export orders', declined in the month. We are carefully watching for the possibility that the economy is cycling through another inventory rebuilding phase. This fits with new factory orders were flat in December. If this turns out to be the case, then manufacturing will turn sluggish again sometime in the first half of the year.

Spending Grows Faster Than Income

The Personal Income number is an example of how statistics can mask the important data in a report. On the surface, the 0.2% increase is a ho-hum number: not remarkably good, but not bad either. But 'Personal Income' bundles together all income from different sources, including wages, farm and rental income and transfer payments, like social security, from the federal government.

For most people, wages are the biggest part of personal income. Yet the striking detail, under emphasized in the press release and follow-up commentaries, is that wages actually declined 0.3% from November. (Prior to this, wages had not declined month-over-month since April 2002.) If it were not for increases in farm and rental income, and some catch-up social security payments, the month-over-month change in income would have been close to zero.

Revisions to October and November estimates of Personal Income were also released, and they showed slower rates of growth than first announced. Declining or stagnant wages along with sluggish job growth are a bad combination. This would lead to falling consumption (which lately has been growing twice as fast as income) and a return to the no-growth, slow-growth economy of the past few years.