Consumer sentiment remained largely unchanged in late February at its second highest level since 2004. Consumers based their optimism on favorable assessments of jobs, wages, and higher after-tax pay. The highest proportion of households since 1998 reported that their finances had improved compared with a year ago and anticipated continued gains during the year ahead. Economic news heard by consumers continued to be dominated by the tax reform legislation and net job gains, which was untarnished by the consensus view that interest rates would increase and stock prices would remain volatile. Although rising interest rates was seen as a reason to temper their longer term outlook for the overall economy, only a modest moderation in the pace of economic growth was anticipated. Although consumers expected the unemployment rate to dip below 4% in 2018, only modest wage growth was anticipated, and inflation expectations have remained unchanged. Interest rates, even when pushed higher in the weeks and months ahead, will not cause postponement of discretionary purchases as long as income continues to rise near its present pace. Personal tax cuts are crucial to spur additional spending, but unlike prior cuts that had an immediate positive impact, this tax cut has not generated universal support. Partisanship has greatly influenced consumers’ perceptions of the tax cut legislation: when asked to identify recent economic changes, net positive references to the tax cuts were made by 37% of Republicans and by 22% of Independents, but among Democrats, net negative references were made by 4%. Presumably the partisan division will last even after the cuts add to take-home pay and boost spending. Overall, the data signal an expected gain of 2.9% in real personal consumption expenditures during 2018.

More consumers reported that they had recently heard favorable news about recent economic developments in February than at any other time since 1984. Two-thirds of consumers reported changes in tax policies and employment gains. In the past two months, more consumers mentioned favorable change in economic policies than recorded in more than a half century. In contrast, the stock market was rarely mentioned, and remarkably, it was more likely to be mentioned as a favorable development (largely due to its rebound, and annual gains) than unfavorably (7% versus 6%). The national unemployment rate was more often expected to decline even further from its current low than to increase in the year ahead (35% versus 23%). When asked to assess their financial situation, 54% reported improved finances, the highest proportion since January 2000. When asked about their financial prospects for the year ahead, 42% expected their finances to improve, up from last February’s 35%. Improved finances during the past year as well as expected gains during the year ahead were reported by 30% of all households, the largest proportion since February 1998. Income gains of 2.2% were anticipated across all households, just below the 2017 peak of 2.3%, which was the highest since 2008. Among those under age 45, a median income increase of 4.2% was expected during the year ahead. Among households in the top third of the income distribution, 51% expected improvement in their finances, the highest level since 2002. Among those with top-third incomes, 28% reported gains in net household wealth, barely below last month’s 29% or the all-time peak of 32% set in July of 2007.

A year-ahead inflation rate of 2.7% was expected in February, unchanged from the readings in the past two months as well as from last February. While it is above the 2017 low of 2.4% in October, most readings in the past year have varied in the narrow range of 2.5% to 2.7%. The longer term annual inflation rate of 2.5% was expected in February, unchanged from last month and last year’s figure. Consumers do not expect a sudden surge in the inflation rate anytime soon, and when asked to explain their finances, the fewest consumers in decades cited rising prices as a cause for declining living standards.

The impact of discounted prices on purchase plans for durables, vehicles, and homes have fallen to the lowest levels recorded in a decade. Instead, consumers base their discretionary purchases on a renewed sense of income and job security. The ongoing shift has made more homeowners think it is a good time to sell, rising to its highest level in a decade. The expected increase in home values during the year ahead rose to 1.8% in February, equal to the April 2017 peak. This improvement will act to increase the supply of existing homes for sale, and thus allow the overall sales rate of existing homes to improve.