

Subject: June 2018 survey results

June 29, 2018

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Consumer sentiment retreated in late June to just above the May reading largely due to concerns about the potential impact of tariffs on the domestic economy. The falloff in confidence was minor, as the Sentiment Index has been virtually unchanged for the past three months. Indeed, the Sentiment Index has remained largely unchanged in the first half of 2018 compared with all of 2017 (98.6 versus 96.8), with variations during the past 18 months confined to  $\pm 4.0$  index-points from its overall mean.

The persistent strength has been due to favorable assessments of jobs and incomes. While consumers anticipated rising interest rates during the year ahead, those expected increases were associated with a modest decline in longer term prospects for the national economy and not viewed as a barrier to economic growth during the year ahead. For the year ahead, consumers still anticipated that the economy would produce small additional declines in the unemployment rate as well as higher wage gains. Consumers also anticipated an uptick in inflation during the year ahead, partly due to rising energy prices and partly due to new tariffs. Importantly, longer term inflation expectations suggest the rise in inflation will be temporary.

The potential impact of tariffs on the domestic economy was spontaneously cited by one-in-four consumers, with most expecting a negative impact on the domestic economy (21% out of 26%). The primary concerns were a downshift in the future pace of economic growth and an uptick in inflation. Among those

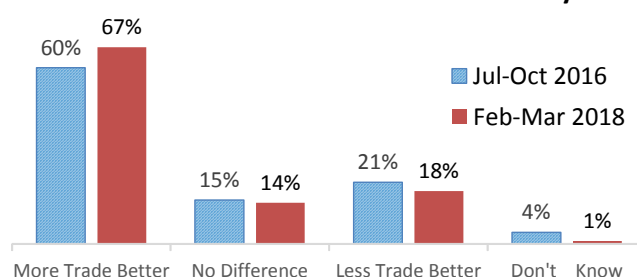
who expressed negative views of the trade policies, the Expectations Index was 22.7 points below those who made no mention of tariffs and the expected inflation rate was three-tenths of a percentage point higher. A longstanding belief of consumers is that trade with other countries results in a broader range of available goods at lower prices. When asked in a recent survey about their views on international trade, two-thirds of consumers thought that more trade with other countries would be better for the domestic economy (see the chart). To be sure, consumers' judgements about the impact of higher tariffs will not crystalize until they have experienced actual changes in product prices and heard about changes in employment. While tariffs may have a

direct impact on only a very small portion of overall GDP, the negative impact could quickly generalize and produce a widespread decline in consumer confidence and optimism. The June survey offers a glimpse into the potential reactions of consumers to rising tariffs and suggests that the timing and size of the loss in confidence could be quick and substantial.

The year-ahead expected inflation rate rose to 3.0% in June from 2.8% in May and last year's 2.6%, reaching the highest level since 2015. Year-ahead gasoline price expectations were higher in May and June, but has remained at relatively low levels. Long term inflation expectations ticked up to 2.6% in June from 2.5% in the preceding five months, returning to the top of the range it has traveled during the past year. Other data also indicate that the rise in inflation will be temporary, as just 8% complained that rising prices had reduced their living standards, unchanged from the last two months and from last June. In addition, buy-in-advance price rationales have declined for the third consecutive month for household durables (from 21% in March to 13% in June) and for vehicles (from 12% to 8%); for homes these rationales fell to 12% from last month's 17%.

June recorded the long awaited rise in wages as consumers anticipated an annual gain of 2.5% in household incomes, up from 1.6% in May, and the highest rate of increases in incomes since 2008. Moreover, when asked to describe how their current finances had changed, 47% of consumers reported income gains, the highest proportion since mid 1966. Unemployment was expected to edge downward (30%) or remain unchanged at its current low (47%), with just 22% who expected any increase.

**Would More Trade or Less Trade with Other Countries Be Better for the U.S. Economy?**



|                                | June 2017 | July 2017 | Aug 2017 | Sept 2017 | Oct 2017 | Nov 2017 | Dec 2017 | Jan 2018 | Feb 2018 | Mar 2018 | Apr 2018 | May 2018 | June 2018 |
|--------------------------------|-----------|-----------|----------|-----------|----------|----------|----------|----------|----------|----------|----------|----------|-----------|
| Index of Consumer Sentiment    | 95.0      | 93.4      | 96.8     | 95.1      | 100.7    | 98.5     | 95.9     | 95.7     | 99.7     | 101.4    | 98.8     | 98.0     | 98.2      |
| Current Economic Conditions    | 112.4     | 113.4     | 110.9    | 111.7     | 116.5    | 113.5    | 113.8    | 110.5    | 114.9    | 121.2    | 114.9    | 111.8    | 116.5     |
| Index of Consumer Expectations | 83.8      | 80.5      | 87.7     | 84.4      | 90.5     | 88.9     | 84.3     | 86.3     | 90.0     | 88.8     | 88.4     | 89.1     | 86.3      |
| Index Components               |           |           |          |           |          |          |          |          |          |          |          |          |           |
| Personal Finances—Current      | 131       | 132       | 130      | 128       | 135      | 127      | 127      | 126      | 133      | 142      | 133      | 130      | 136       |
| Personal Finances—Expected     | 132       | 122       | 134      | 133       | 132      | 132      | 127      | 131      | 133      | 132      | 131      | 129      | 128       |
| Economic Outlook—12 Months     | 110       | 111       | 119      | 110       | 123      | 123      | 119      | 121      | 124      | 120      | 113      | 122      | 117       |
| Economic Outlook—5 Years       | 95        | 89        | 100      | 97        | 110      | 103      | 93       | 95       | 105      | 105      | 111      | 108      | 102       |
| Buying Conditions—Durables     | 161       | 163       | 158      | 162       | 168      | 168      | 168      | 160      | 166      | 173      | 165      | 160      | 166       |