

Subject: Preliminary results from the December 2018 survey

December 7, 2018

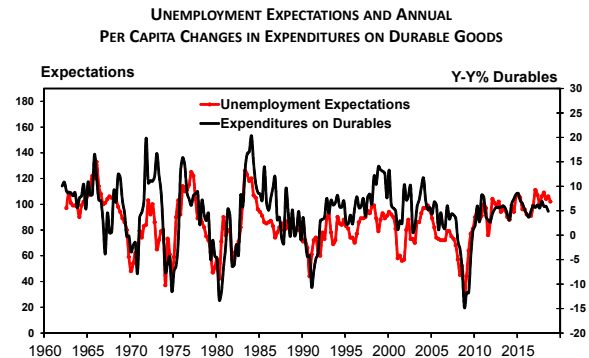
From: Richard Curtin, Director

Consumer sentiment was unchanged from last month's reading and has remained at very favorable levels since the start of 2017. In the two years from January 2017 to December 2018, the Sentiment Index was consistently above 90.0, averaging 97.5, identical to the early December reading. The last time the Sentiment Index was consistently above 90.0 for at least as long was from 1997 to 2000, recording a four-year average of 105.3. The higher average in the late 1990's was due to more optimistic economic expectations (99.5 versus 87.3), while current economic conditions were judged nearly identically in both periods (114.3 versus 113.5). There are a number of plausible causes for this difference, most of which revolve around job and wage prospects. Record lows in unemployment and a revival in income gains have been primarily responsible for the very favorable recent levels of consumer sentiment. Consumers have also noted the absence of attractive discounting on homes and vehicles as well as recent increases in interest rates. Some of the initial impact from higher

prices and interest rates has been offset by consumers buying-in-advance of further increases, facilitated by larger income gains. As noted in last month's report, rising prices and interest rates will not cause substantial cutbacks in spending as long as job and income growth remain strong. In the early December survey, however, consumers did mention hearing much more negative news about future job prospects. The chart above shows the close relationship between recent changes in per capita durable spending and trends in unemployment expectations. While income gains can keep purchases affordable despite rising interest rates, most consumers understand that the goal of those increases is to slow the pace of economic growth. In past expansions, there was plenty of room between low and high interest rates to nudge up rates without damaging consumer spending. The gap has now been squeezed to just a few percentage points and more caution is warranted. An increase in interest rates of an eighth-point, rather than a quarter-point, would enable greater flexibility and provide the necessary feedback. If a downturn did occur in late 2019 or 2020, the difference would not significantly affect the Fed's ability to counter the downturn; more sizeable rate increases may prompt consumers to make greater defensive cutbacks in spending.

When asked about what recent economic news they had heard, consumers offered fewer positive references to employment and more negative mentions of rising unemployment. Positive changes in employment were cited by 16% in early December, down from 21% to 23% in the last four months, while negative references to the employment situation rose to 20%, up from 9% to 12% in the prior four months. When specifically asked how they expected the unemployment rate to change in the year ahead, the balance of opinion turned negative for the first time in the past eighteen months. While one month's results must be treated with caution, if it is confirmed in the months ahead, it will act to diminish consumer spending in 2019.

Income expectations, in contrast, have remained favorable, although slightly below last month. When asked about how they anticipated their household incomes to change in the year ahead, a gain of 2.4% was expected across all households, barely below last month's 2.5%, and the highest two month average since 2007; the average for 2018 was the highest since 2007. Among respondents aged 18 to 44, income gains of 3.9% were anticipated in early December and in the November survey. The year-ahead expected inflation rate was 2.7% in early December, just below last month's 2.8% and equal to last year's figure. The annual long term inflation rate was expected to be 2.4% in December, down from 2.6% in November and also equal to last year's reading. Overall, the recent moderation indicates that consumers do not anticipate an acceleration in 2019.



	Dec 2017	Jan 2018	Feb 2018	Mar 2018	Apr 2018	May 2018	June 2018	July 2018	Aug 2018	Sept 2018	Oct 2018	Nov 2018	Dec Prelim
Index of Consumer Sentiment	95.9	95.7	99.7	101.4	98.8	98.0	98.2	97.9	96.2	100.1	98.6	97.5	97.5
Current Economic Conditions	113.8	110.5	114.9	121.2	114.9	111.8	116.5	114.4	110.3	115.2	113.1	112.3	115.2
Index of Consumer Expectations	84.3	86.3	90.0	88.8	88.4	89.1	86.3	87.3	87.1	90.5	89.3	88.1	86.1
Index Components													
Personal Finances—Current	127	126	133	142	133	130	136	133	133	135	130	130	132
Personal Finances—Expected	127	131	133	132	131	129	128	134	131	135	131	129	127
Economic Outlook—12 Months	119	121	124	120	113	122	117	116	118	123	123	117	118
Economic Outlook—5 Years	93	95	105	105	111	108	102	101	101	106	105	109	101
Buying Conditions—Durables	168	160	166	173	165	160	166	164	154	164	163	161	167