

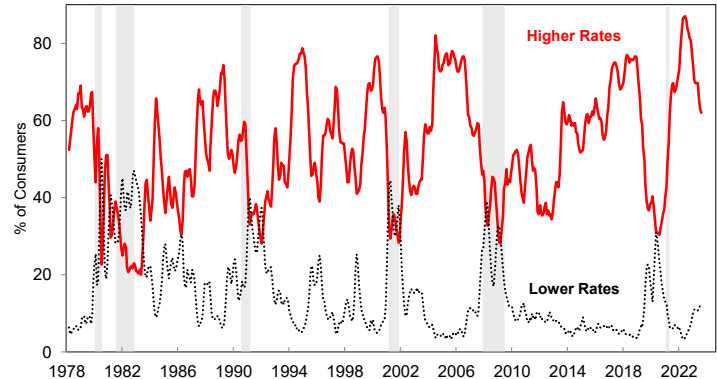
## Interest Rate and Price Pressures on Consumers

September 8, 2023

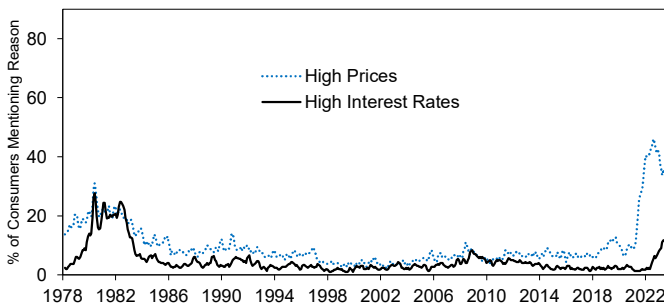
Joanne Hsu, PhD, Director

About a year and a half has passed since the Federal Reserve began raising interest rates in order to tame high inflation. Through today, these hikes have totaled over five percentage points after a long period of extremely low interest rates. As highlighted in past reports, while consumers have welcomed the slowdown in inflation in 2023, concerns over interest rates have emerged. Over the past year, current and expected labor market strength have supported consumer spending in spite of high costs, allowing interest rates to increase without sharp and sustained declines in sales. However, the effects of interest rate policy can take some time to pass through to macroeconomy, particularly from financial markets onto consumers whose spending ultimately drives aggregate demand. Furthermore, while consumers may not pay close attention to FOMC announcements, high levels of borrowing means that interest rates are salient to them. The chart to the right shows consumers' expectations of interest rate changes in the year ahead. They anticipated the rising interest rates of 2022; though consumers anticipate some of these interest rate pressures to ease, nearly two-thirds expect interest rates to continue rising over the next year.

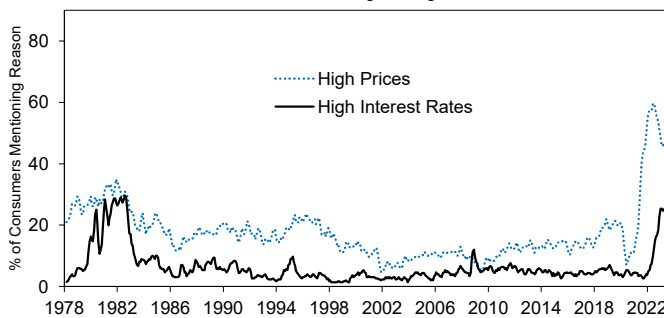
**Expected Change in Interest Rates During the Next Year**  
(% Expecting Higher and % Expecting Lower, 3MMA)



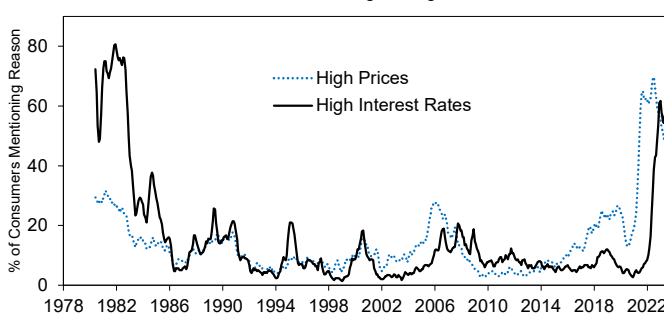
**Reasons for Poor Buying Conditions for Durables**  
3-Month Moving Average



**Reasons for Poor Buying Conditions for Vehicles**  
3-Month Moving Average



**Reasons for Poor Buying Conditions for Homes**  
3-Month Moving Average



Prices and interest rates are primary economic factors underlying the strength of demand. Data from the Surveys of Consumers record the relative importance of these two factors, among others, for consumer buying plans; these patterns shed light on the passthrough of interest rate policy to consumer behavior. The figures to the left display the share of consumers mentioning high prices (dotted blue line) and high interest rates (solid black line) as a reason for poor buying conditions for large durable goods, vehicles, and homes. For all three types of purchases, concerns over high prices began rising in 2021, peaking last summer at levels at historic highs, and have eased somewhat since then concurrently with the slowdown in headline inflation.

This recent moderation in price concerns has been offset by rising interest rate concerns, which began lifting more recently, in 2022. For homes, interest rate considerations now exceed the historically high concerns over high prices. For both autos and homes, interest rate mentions are now within the range seen in the late 1970s and early 1980s, despite the fact that the effective federal funds rate is currently lower than at any time between 1977 and 1991.

While concerns over interest rates are quite elevated from a historical standpoint, they have also been relatively flat in recent months even as the Fed continues to raise rates. This is true across the income distribution. Households with the top tercile of incomes generate more than half of all consumer spending. Notably, their views on the role of interest rates for buying conditions for these large purchases mirror that of the general population, particularly in this current inflationary episode, in spite of their greater ability to absorb higher costs, suggesting a possible pullback in spending if borrowing costs continue to escalate.