WEAKER US HOUSEHOLD CONFIDENCE, A SOURCE OF CONCERN?

A recent academic paper argues that, considering the significant recent decline of consumer expectations, the US could be entering recession. However, Covid-19 complicates the interpretation of household confidence data. Fluctuations in infections play a role and the recovery from last year's recession as well as other factors have caused a jump in inflation. Given the historically high quits rate, the weakening in household sentiment probably reflects mounting concern about the impact of inflation on spending power. Something similar has been observed in the latest consumer confidence data for France.

A recent NBER paper[1] has raised eyebrows. Its authors argue that, considering the recent downward movement of consumer expectations, the US economy could be entering recession. Their assessment is based on the historical experience that all recessions since the 1980s have been predicted by a significant drop in the expectations component of the Conference Board household confidence index and the University of Michigan sentiment index (chart 1). As shown in table 1, their recent decline is at the higher end of the historical range, hence the conclusion drawn by the researchers. However, the specific nature of the pandemic-related recession and the recovery that has followed creates an analytical challenge. Swings in household sentiment may reflect fluctuations in the concern about the health situation. Increases in the number of new cases have been associated with a drop in confidence although it should be noted that the Conference Board index started losing ground in spring despite lower infection rates (chart 2).

Another complicating factor is the co-existence of high inflation and a strong labour market. Concerning the latter, filling vacancies has become a top concern for US (and European) companies. Workers sense this as well and change jobs more easily. In the US, the quits rate is at a record high[2]. Interestingly, a gap has opened between this indicator and household sentiment (chart 3). Traditionally, both series are highly correlated but, as of late, the quits rate has continued moving higher whereas sentiment has dropped. Clearly, weaker sentiment does not reflect mounting fears about the job market so another factor must be at work. Rising inflation and inflation expectations are an obvious candidate. They fuel concern amongst households about their spending power, as mentioned in a report on the September University of Michigan sentiment survey: *"There was a complete rout of net favourable views of buying conditions: household durables fell to the lowest level since 1980, vehicles fell to the lowest level since 1974, and homes to the lowest level since 1982. These record drops were all due to complaints about high prices."*[3] A similar divergence is noticeable in France where consumer confidence has weakened in October. The assessment of the future savings capacity has recorded a strong decrease and the share of households considering that their standard of living will improve in the next twelve months is also down. The percentage of those who think that prices are rising is up sharply and the same holds for inflation expectations for the next 12 months. Yet, households' fears about future unemployment continue to fall sharply and are well below their long-term average[4]. To conclude, sounding the alarm bell on weaker household sentiment is premature, certainly in Europe, where confidence has hardly declined and remains elevated, but even in the US, despite its drop from recent highs. It does force us to be particularly vigilant to inflation developments and the labour market outlook and to monitor closely whether the latter remains sufficiently strong to neutralise the headwind coming from the former. Based on hiring intentions, one should expect this to remain the case in the near term.

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1. *The Economics of Walking About and Predicting US Downturns*, David G. Blanchflower and Alex Bryson, NBER Working Paper No. 29372, October 2021. The authors are respectively professor at Dartmouth College and University College London. David Blanchflower is a former member of the Bank of England's monetary policy committee.
2. The quits rate is the number of quits during the entire month as a percent of total employment (source: US Bureau of Labor Statistics).
3. Source: Preliminary results from the September 2021 survey, University of Michigan, Surveys of Consumers, 17 September 2021.
4. Source: INSEE, Monthly consumer confidence survey, October 2021.

US CONSUMER CONFIDENCE, EXPECTATIONS INDEX

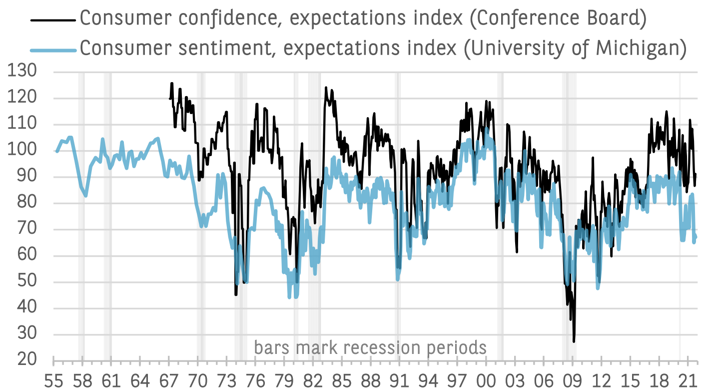

CHART 1 SOURCE: CONFERENCE BOARD, UNIVERSITY OF MICHIGAN, BNP PARIBAS

> Sounding the alarm bell on weaker household sentiment is premature, certainly in Europe –given its high level- but also in the US. It does force us to monitor closely whether the labour market outlook remains sufficiently strong to neutralise the headwind coming from higher inflation. Based on hiring intentions, one should expect this to remain the case in the near term.

US CONSUMER CONFIDENCE AND COVID NEW CASES

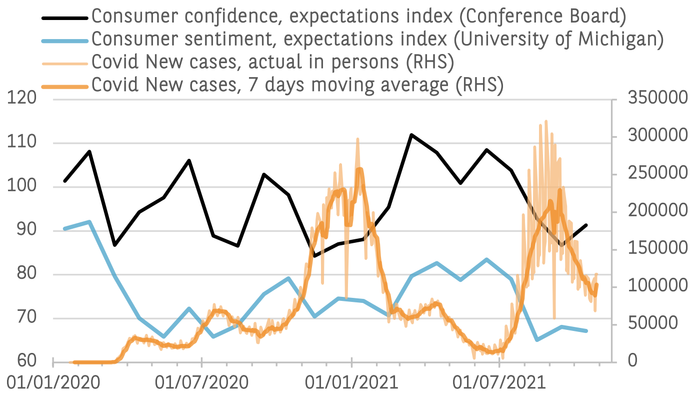

CHART 2

SOURCE: CONFERENCE BOARD, UNIVERSITY OF MICHIGAN, REUTERS, BNP PARIBAS

US CONSUMER CONFIDENCE AND EMPLOYMENT QUITS RATE

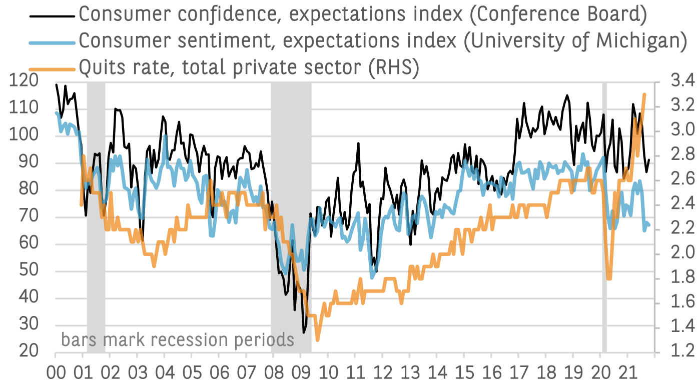

CHART 3

SOURCE: CONFERENCE BOARD, UNIVERSITY OF MICHIGAN, BLS, BNP PARIBAS

HOUSEHOLD CONFIDENCE AND RECESSIONS IN THE US

	POINTS DROP FROM MOST RECENT PEAK	
START OF RECESSION*	CONFERENCE BOARD	UNIVERSITY OF MICHIGAN
January 1980	26.3	17.6
July 1981	8.8	6.1
July 1990	16.5	13.3
March 2001	36	22
December 2007	20.5	21.4
February 2020	21.3	21.3
September 2021	25.3	18.4

*As determined by the NBER Business Cycle Dating Committee, with the exception of September 2021.

TABLE 1

SOURCE: DAVID G. BLANCHFLOWER AND ALEX BRYSON, NBER WORKING PAPER NO. 29372, OCTOBER 2021.