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Confidence Tumbles: Surging Prices & Falling Jobs

ANN ARBOR. Consumer confidence fell to near its fifty year low due to soaring prices and mounting job losses. “Surging gas prices, high food prices, disappearing jobs, declining home values, and record foreclosures were cited by consumers as the basis for their pessimism, and most consumers expected each of these problems to continue to worsen in the months ahead,” according to Richard Curtin, the Director of the Reuters/University of Michigan Surveys of Consumers. Steep declines in the Expectations Index, which has been recorded since the start of 2007, has always been associated with subsequent recessions. The extent of the decline in consumer spending is likely to be relatively small. In the eleven recessions since 1945, consumption has declined in just two years, by -0.8% in 1974 and by -0.3% in 1980. “The data indicate that growth in consumption spending will be under 1.0% in 2008, with the pace weakening until the Spring of 2009. The risks of a deeper and longer downturn, however, can no longer be easily dismissed,” Curtin said.

The Index of Consumer Sentiment was 56.4 in the June 2008 survey, just below the 59.8 in May, and significantly below the 85.3 recorded last June and the peak of 96.9 recorded in January of 2007. There have only been two prior surveys since 1952 than recorded a lower level—in April 1980 (52.7) and May 1980 (51.7). The Index of Consumer Expectations, a closely watched component of the Index of Leading Economic Indicators that is noted for its ability to foreshadow recessions, was 49.2 in the June 2008 survey, down from 51.1 in May, and well below the 74.7 recorded in June 2007 and the peak of 87.6 in January 2007. Overall, the Expectations Index has declined by 38% from its peak, at the top end of the range of losses that has varied between 25% and 35% prior to past recessions.

More consumers than any time since the first survey was conducted in 1946 reported that their financial situation had worsened (57%). When asked to explain the changes in their finances, the highest number of consumers cited higher prices for fuel and food, and the smallest number of consumers reported income gains than at any other time in the history of the surveys. “Consumers held the bleakest inflation-adjusted income expectations since the question was first asked nearly a half century ago,” noted Curtin.

Nine-in-ten consumers thought that the economy was in recession in June, with record numbers citing unfavorable news about rising prices, lost jobs, slowing economic growth, and the continuing fallout from the credit and housing crises. “Perhaps the most significant development in the past few months is that two-thirds of all consumers now expect the economic slump to extend into the next several years,” said Curtin.

Buying plans for vehicles and household durables, such as furniture, appliances, and home electronics, were the least favorable since the early 1980's. “When asked to explain their views, consumers said that they favored the postponement of purchases given their uncertainty about their future income and job prospects as well as concerns about the future course of gas and food prices,” Curtin said.

Inflation expectations rose in June to their highest levels in more than two decades. Although much lower, long term inflation expectations also reached a decade peak in the June survey. Gas prices were expected to rise to \$4.50 in the months ahead and average \$5.00 over the next five years. “The expected permanent increase in energy prices will act to transform demand for many products and services, most notably those connected with transportation,” Curtin added.

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