

Economic Indicator — May 12, 2023

# Consumer Sentiment Slumps in Early May

## Summary

Consumers continue to signal they are downbeat about the economy, and that they expect inflation to remain higher for longer. The consumer sentiment index dropped to a six-month low and medium-to-long term inflation expectations notched a 12-year high.

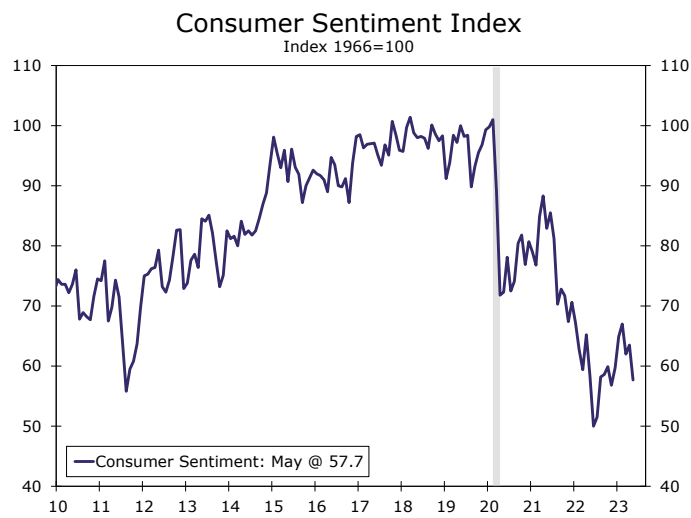
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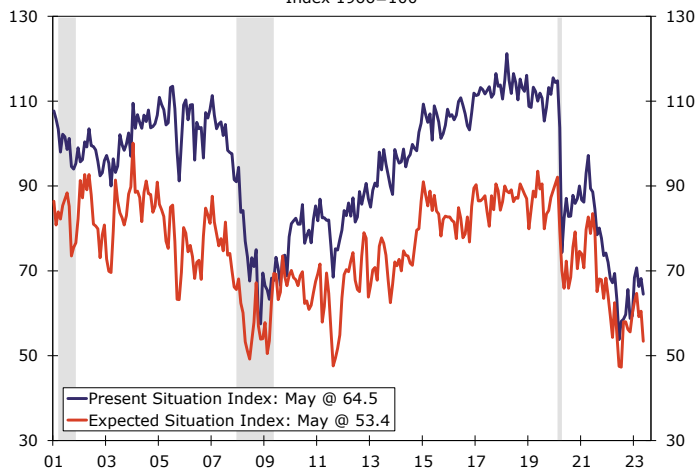
Source: University of Michigan and Wells Fargo Economics

## Not in the Mood

Consumers are downbeat on the economy. The preliminary read of the Consumer Sentiment Index for May showed the index slid to 57.7, the lowest reading in six months ([chart](#)). Consumers noted less optimistic views on both current conditions and expectations for the future, but the 7.1 drop in the expectations index is the largest in nearly a year ([chart](#)). Measures of consumer optimism have remained under pressure since the start of the pandemic amid a lingering uncertainty. We suspect there are multiple things currently weighing on the mood, such as higher interest rates, still-high inflation and growing concern over the debt ceiling.

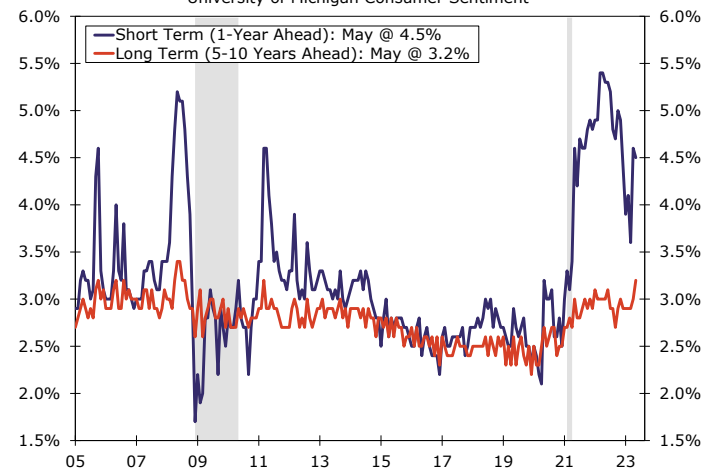
But if you look at measures of consumption, households continue to spend. Consumer spending has proved remarkably resilient in the face of high inflation and the most rapid pace of monetary tightening in forty years. Large amounts of excess savings have offset the burden of higher prices. But, while households may be somewhat looking past inflation, it doesn't mean they're not taking note of it. The real key to the inflation outlook rests on consumers' continued willingness to stomach price gains, or firms' ease in raising prices.

**Present vs. Expected Situation Index**  
Index 1966=100



Source: University of Michigan and Wells Fargo Economics

**Consumer Inflation Expectations**  
University of Michigan Consumer Sentiment



Source: University of Michigan and Wells Fargo Economics

## Inflation Expectations Heat Up

Consumers' inflation expectations have perked back up recently ([chart](#)). Short-term inflation expectations fell slightly to 4.5% in early May, but expectations have now been above 4% for 23 of the last 25 months, after reaching a high of 5.4% in March 2022. A sustained elevation in short-term expectations appears to be the lesser of two evils in this report, however, as long-term expectations continued a worrying trend of elevation. Expectations for inflation 5-10 years ahead broke out of their recent range rising to 3.2%, up from 3.0% a month ago. Today's long-term expectations are now at their highest level since 2011.

Gas prices may take part of the blame here, as consumers have had to pay up at the pump in recent weeks. Average prices at the pump rose nationally to nearly \$3.70 in late April, coinciding with the beginning of the survey period and up from gas prices near \$3.40 a month prior. While this recent uptick may explain some of the lousy print in May, it may do little to comfort Federal Reserve policymakers, who up through this point have reiterated that expectations have remained well anchored. That position may come under increasing fire specifically in the face of the highest long-term expectations in over a decade.

## Debt Ceiling on Consumers' Radar

In regard to the debt ceiling, we expect the longer a resolution is unmet the more it will start to weigh on consumer mindsets. Looking back to the debt ceiling impasse of 2011, consumers became increasingly concerned as the "X date" grew closer, and the consumer sentiment index fell 18.5 points between May and August 2011. We don't believe the debt ceiling was the main culprit behind lower sentiment in early May, but it could be in coming months.

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