Why it Matters: Consumer Confidence

Lesson Overview

This lesson looks at consumer confidence, a closely watched indicator of the health of the U.S. economy. To begin, students complete a “consumer confidence survey.” Students then read about two well-known surveys of consumer confidence, the “Consumer Confidence Index” (CCI), a monthly index produced by the Conference Board, an independent economic research organization, and the University of Michigan Consumer Sentiment Index, published by the University of Michigan’s Institute for Social Research.

Students will consider how their and others’ view of the future health of the economy may impact people’s spending and saving decisions. Students examine the concept of the “self-fulfilling prophesy” as a potential result of trends in consumer confidence. Finally, as an extension activity, students survey their friends or adults to create their own consumer confidence index.

Lesson Introduction

In the 1940s, George Katona, a Professor of Psychology at the University of Michigan, began to apply psychological principles to macroeconomics and economic behaviors. His early work was a study of people’s responses to war-time inflation. Professor Katona’s work led to what is now the “Surveys of Consumers” published by Thompson Reuters/University of Michigan Institute for Social Research.

This and other measures of consumer confidence have become key tools for those attempting to predict the dynamics of the economy and how people respond to their future expectations. The current Survey of Consumers consists of the responses of 500 consumers in three key areas: how consumers view their personal financial situation, how they view the current health of the economy, and their view of economic conditions over the long term.

The U.S. Consumer Confidence Index (CCI) was designed in 1967 to measure “the degree of optimism on the state of the economy that consumers are expressing through their activities of savings and spending.” The index is determined monthly by The Conference Board, an
independent economic research organization. The CCI is based on five-question surveys of 5,000 households.

Consumer confidence, by these two and similar measures, attempts to quantify the impact on consumer choices and behaviors economic conditions and events, both real and perceived. If consumers are more “confident,” that is, they feel good about their economic opportunities and future, they will act in certain ways – spending and future planning will be more positive. If consumers feel negative about their current and future opportunities, they may spend less and be less likely to invest in their futures. Attitudes about the future direction of the economy may impact decisions about major purchases, saving, investment, employment, etc.

**Key terms from this lesson:**

**Consumer confidence.** (The Conference Board): The degree of optimism on the state of the economy that consumers are expressing through their activities of savings and spending.

**Consumer confidence.** (University of Michigan Institute for Social Research): Consumer attitudes toward the overall business climate, state of their personal finances, and consumer spending.

**Leading economic indicator.** Economic data or an index that tends to start declining prior to a recession and becomes positive prior to the end of the recession, signaling a recovery. These indicators provide a preview of the economy's future direction and health.

**Self-fulfilling prophesy.** An expectation (positive or negative) about some person, circumstance, or event that influences a person's behavior toward the person, circumstance or event in a way that may cause the expectation to result. Example: If people expect inflation, they may accelerate their purchasing to the degree that it has an inflationary effect.

*NOTE: Unless otherwise cited, the definitions of terms used in this lesson are from with the glossary of the Council for Economic Education’s Virtual Economics program. They are consistent with the National Voluntary Content Standards in Economics and the Ohio Academic Content Standards for Social Studies.*
Read more about leading economic indicators:

What Are Leading Economic Indicators?| eHow.com
http://www.ehow.com/about_5434079_leading-economic-indicators.html#ixzz1z0Gy4470

Economics and Statistics Administration, U.S. Department of Commerce,
http://www.esa.doc.gov/esa-mission-statement

Leading Economic Indicators, TheStreet.Com
http://www.thestreet.com/tsc/basics/tscglossary/leadingeconomicindicators.html

Leading Economic Indicators, AmosWeb, Encyclonomic Web•Pedia
http://www.amosweb.com/cgi-bin/awb_nav.pl?s=wpd&c=dsp&k=leading+economic+indicators

The Bureau of Economic Analysis (BEA) – http://www.BEA.gov

The BEA, an agency of the U.S. Department of Commerce Economics and Statistics Administration, promotes a better understanding of the U.S. economy by providing the timely, relevant, and accurate economic accounts data in an objective and cost-effective manner.

The U.S. Census Bureau - http://www.census.gov/

The Census Bureau, an agency of the U.S. Department of Commerce Economics and Statistics Administration, collects and reports the basic data used throughout the United States to measure the changing economic and demographic situation of American businesses, households, and governments.


The Bureau of Labor Statistics of the U.S. Department of Labor is the principal Federal agency responsible for measuring labor market activity, working conditions, and price changes in the economy. Its mission is to collect, analyze, and disseminate essential economic information to support public and private decision-making.
Lesson Objectives

The student will:

1. Identify indicators of economic trends and future conditions.
2. Explain the concept of the consumer confidence index.
3. Suggest how expectations may impact economic choices.
4. Interpret economic data to identify its potential impact on consumer decision making.

Lesson Materials

Handout/Visual 1: Why It Matters: Consumer Confidence
Handout/Visual 2: Consumer Confidence Survey
Handout/Visual 4: Survey of Consumers, Thompson Reuters/ University of Michigan
Handout/Visual 5: Self-Fulfilling Prophesy

Lesson Preparation

Prepare visuals to project or print copies of the Handout/Visuals for each student:

Handout/Visuals, 1-6

If using the extension activity, “Consumer Confidence Survey,” print copies for students to use surveying friends or adults.
Procedures

1. **Ask the following questions:**

   **Ask:** What does it mean to be confident? Elicit student responses to the words confident or confidence.

   *Merriam-Webster Online Dictionary: 1.* a: a feeling or consciousness of one's powers or of reliance on one's circumstances *<had perfect confidence in her ability to succeed>*; b: faith or belief that one will act in a right, proper, or effective way *<have confidence in a leader>* 2. the quality or state of being certain.*]

   **Ask:** What results when someone is confident or has confidence in something or someone?

   *Responses will vary, but should focus on a more optimistic view, being surer that something positive (or negative) will happen, or being surer of knowing the result of an action or decision.*

   **Ask:** What do you think it means to “have confidence in the economy”?

   *Suggest that confidence, in this case, means a positive view of the future of one's personal situation or that the overall economy is in good health or improving. Confidence may include stable prices, more jobs, or growth.*

2. **Distribute copies of Handout/Visual 1: Why It Matters: Consumer Confidence.**

   Students should read the article by Dr. Julie Heath.

   Briefly discuss the main points of the article. Focus some discussion on the ideas of the “self-fulfilling” prophesy and how our expectations can sometimes alter our behavior so that we get what we expect. This idea will be further discussed at the end of the lesson.

3. **Distribute copies of Handout/Visual 2: Consumer Confidence Survey.**

   Explain that this is a survey of the students’ confidence or outlook toward their financial future and the economy. Students should complete the survey, indicating for each question their personal view of each question topic. Assure that the surveys are intended to foster discussion and not for any research use. After the discussion, the students should keep or destroy their individual surveys.

   Allow time for the students to complete Handout/Visual 2: Consumer Confidence Survey.
4. **Debrief the survey results, focusing more on the intent of the questions than the students’ individual answers.** Ask the students to suggest what positive or negative responses to each question may indicate about how consumers will decide or act, primarily about their future spending.

1. **Do you feel business conditions are good or bad?**
   
   **Good:** Businesses will invest more and consumer may be willing to make large purchases.
   
   **Bad:** Businesses will invest less and consumers will be less willing to make large purchases.

2. **Do you feel jobs are hard to get or plentiful?**
   
   **Plentiful:** People may be more willing to seek to change jobs and/or have more confidence in their future income. They will spend more.
   
   **Hard to get:** People may be less willing to seek to change jobs and/or have less confidence in their future income. They will spend less.

3. **Do you think business conditions will improve or worsen over the next six months?**
   
   **Improve:** There will be more job growth and greater future income. Consumers will spend more.
   
   **Decrease:** There will be fewer jobs and less future income. Consumers will spend less.

4. **Do you think jobs will increase or decrease over the next six months?**
   
   **Increase:** More jobs means more income and consumer spending.
   
   **Decrease:** Fewer jobs means less income and less consumer spending.

5. **Do you expect your household income to increase or decrease over the next six months?**
   
   **Increase:** More income means more spending and investment in the future, such as home purchases.
   
   **Decrease:** Less income means less spending and less investment in housing.

Summarize by asking the students to suggest how their views of the future may generally impact their decisions and the economy as a whole.
5. Explain that several organizations publish estimates or indexes of consumer confidence, based on surveys of the attitudes and expectations of consumers. Handout/Visual 3 is a recent report of Consumer Confidence Survey, produced monthly by The Conference Board. Project or distribute copies of Handout/Visual 3.

6. Students should read and identify The Conference Board’s index determination conclusions about consumer confidence in June, 2012. Ask: What were the index results of The Conference Board’s Consumer Confidence Survey for June, 2012?
   • The Consumer Confidence Index®, declined in June to 62.0 from 64.4 in May.
   • The Expectations Index declined to 72.3 from 77.3.
   • The Present Situation Index increased to 46.6 from 44.

7. Ask: What were the general conclusions about the survey results in June, 2012?
   • “Consumers were somewhat more positive about current conditions, but slightly more pessimistic about the short-term outlook.”
   • “Income expectations, which had improved last month, declined in June. If this trend continues, spending may be restrained in the short-term.”
   • “Consumers’ assessment of current conditions improved slightly in June.”
   • “Consumers have grown less upbeat about the short-term outlook.”


9. Students should read and identify Thompson Reuters/University of Michigan survey’s conclusions about consumer confidence in June, 2012. Ask: What were the index results of this survey for June, 2012?
   • The Sentiment Index was 73.2 in June 2012, down from 79.3 in May.
10. **Ask: What were the general conclusions about the survey results in June, 2012?**

   - Consumer confidence posted a sizable loss in June, with most of the overall decline in how consumers viewed future prospects for the national economy."
   - “a somewhat slower spending growth rate.”
   - “The sharp declines among upper income households, however, may have a greater impact on the economy since their spending accounts for a large share of the total.”
   - “a large drop in favorable ratings of economic policies and a growing recognition that federal policies to bridge the fiscal cliff will not even be discussed until the very last minute.”
   - “more cautious spending plans now to protect their finances from potentially adverse developments.”

11. **Ask: How do the conclusions of the two surveys compare?**

    [The results of these two surveys are generally consistent. Both indexes decreased in June, 2012. Both suggested negative future expectations.]

12. **Ask: What happens when people expect something bad or something good to happen, such as change economic conditions? Further ask students how their behavior may change when they expect something bad like inflation or higher unemployment?**

    [Student responses will vary. Generally, they may suggest that people will be more conservative when they expect bad times, delaying big purchases and saving more. The may suggest that when people expect good times, they will take more risks and invest more.]

13. **Introduce the concept of the “self-fulfilling prophesy.”**

    Ask students what “self-fulfilling prophesy” means.

    [A self-fulfilling prophesy is an expectation (positive or negative) about some person, circumstance, or event that influences a person’s behavior toward the person, circumstance or event in a way that may cause the expectation to result. Example: If people expect inflation, they may accelerate their purchasing to the degree that it has an inflationary effect.]
14. **Ask students if they can think of how they have experienced self-fulfilling prophesies.**

[Student responses will vary. One good example is if a student thinks that no matter how much he studies, he will not improve his grade on a test. If he doesn’t study, the chance of a higher grade is less likely. A team that thinks they cannot win will probably not work as hard and, thus, may be less likely to win.]

15. **Ask: How might the self-fulfilling prophesy concept apply to consumer confidence?**

*If people expect bad times (fewer jobs or higher prices) in the future:*

- They will take fewer risks, spend less, and save more
- These behaviors will slow the economy and may result in less growth and higher unemployment.
- If people expect inflation, they may accelerate their purchasing to buy goods at lower prices.
- If people suddenly increase demand and spending, it may result in inflationary pressure.

*If people expect good times (more jobs or lower prices) in the future:*

- They will take more risks, spend more, and save less
- These behaviors will stimulate the economy, creating jobs and growth.
- If people expect lower prices in the future, they may delay their purchasing to buy goods at lower prices.
- If people suddenly decrease demand and spending, it may result in lower future prices.]
16. Distribute copies of Handout/Visual 4, Self-Fulfilling Prophesy. Students should consider the five “news reports,” suggesting which of the three consumer behaviors will most-likely result.

Suggested Answers:

1. **a** (If people expect higher prices in the future, they will probably purchase more at the currently lower prices.)

2. **b** (If people expect lower prices in the future, they will probably delay purchases to pay lower prices in the future.)

3. **b** (If people anticipate less income in the future, they will probably reduce their demand for higher priced items.)

4. **a** (If people feel better about the future, they will be more likely to purchase higher priced items.)

5. **a** (If people anticipate higher prices in the future, they will more likely increase current home purchases.)

17. Ask students if there are any other situations where what people expect changes their behavior?

[Students may suggest interpersonal or family relationships, taking an exam, competing in a sporting event or other situations where positive or negative expectations will impact behaviors.]

**Conclusion**

Students should be able to articulate the “consumer confidence index” assumption about impact of future expectations on current behaviors and decisions.

[People tend to respond to economic expectations and act in ways that may cause (contribute to) the result they expect. If people feel negative about the future of the economy, they may choose to spend less. Reduced consumer spending will slow economic growth.]
Extension Activities

1. Leading Economic Indicators

Students may be interested in other economic indicators, especially the most commonly cited, The Conference Board’s Index of Leading Economic Indicators. Use Handout/Visual 6: Global Business Cycle Indicators, to introduce the index of “leading indicators.”

Review The Conference Board’s ten “leading indicators.” Students should be able to suggest how each is an indicator of future economic growth. For more information about this index, go to: www.conference-board.org/data/bci.cfm

2. Create a Consumer Confidence Index

Students can use Handout/Visual 2, Consumer Confidence Survey, to survey the attitudes of friends or adults about the economy. Print some number of survey forms for forms for each student to use. After collecting the surveys and determining the results, students can generally discuss how their survey group may respond to their level of confidence.

A Note about Creating an Index

To create an index, each item on the survey can be considered as equally important or they can be ranked according to importance, and each item given a value, with the total value of 100. The initial value of all positive responses (100) can be used as the “base” figure.

Future survey results, reflecting more positive or more negative responses, can be compared to the base figure of 100. In reality, the base year is determined as some period of little change, and succeeding surveys increase or decreases from that figure. For example, The Conference Board Consumer Confidence Index® In the base year of 1985 was 100. It declined in May and June, 2012, to a level of 62.0. In 1999, a period of very high consumer confidence, the index reached over 140.

For this student survey, establish the base figure of 100 as a total of all positive responses (100 percent of the responses.). The survey responses of friends or adults can be compared to the base of 100. If the survey reflects less consumer confidence, the index will be less than 100.

Why It Matters: Your Confidence

By Dr. Julie Heath, Director, Economics Center

How confident are you? It might surprise you to learn that your level of confidence has a great deal to do with how healthy the economy is. However, in this context confidence doesn’t refer to your ability to deliver a presentation without feeling nervous, or feeling prepared for an exam. Rather, it means your confidence in how well you think the economy is doing. But wait—does your level of confidence affect the economy, or is it the other way around? Actually, it’s both.

You may have heard news reports saying that consumer confidence is up, or is down, or has stayed the same. These reports are based on measures of consumers’ perceptions of the economy and their own personal financial situation. The measure most widely reported in the media is the Consumer Confidence Index (CCI), developed by an organization called the Conference Board (the less widely-reported measure is the Surveys of Consumers, conducted by the University of Michigan). The CCI is generated by asking five questions of a sample of individuals: two about the present economic situation; i.e. what they think about the current business and employment conditions. The other three questions have to do about their expectations about what the future holds in six months (business, employment and their own family income). Each question has only three possible responses—consumers can report feeling positive, negative or neutral. Three measures, or indices, are then generated—one that reflects the overall level of consumer confidence, one that is tied to current conditions, and one that reflects expectations about how the economy will do in the future.

In June, the overall CCI fell for the fourth consecutive month. Consumers’ expectations about the future were more pessimistic in June than they had been in May, particularly
concerning when it came to the question of families’ own incomes. However, their assessment of the current situation was slightly improved in June, compared to the month before.

Why is the CCI important? Does it reflect economic conditions or does it cause economic conditions? This chicken-and-egg puzzle is an important one for our economy. When the economy is relatively weak, as ours has been, we would expect the CCI to be fairly low, as consumers look at the current and future conditions and perceive them to be rather bleak. In this case, the actual state of the economy is causing the CCI to be low. But, consumer spending is the main force behind the economy, making up about two-thirds of economic activity. If you and I perceive the economy to be weak, we delay making major purchases, and tend to save more, which means that economic activity slows down even more. In this case, consumers’ perceptions of the economy—as reflected in the CCI—can cause a worsening of economic conditions.

This self-fulfilling prophesy—consumer confidence falls, leading to an actual decline in consumer spending and a worsening economy, leading to a further reduction in the CCI, and so on—is a problem for policy makers. Consumer perception can quickly become reality, and this is something that the government and the Federal Reserve have to consider when they implement policies to stimulate economic growth. Your level of confidence has everything to do with how healthy the economy is, whether it is based on reality or not; chances are, your perceptions will become reality soon.
Consumer Confidence Survey

For each of the questions below, indicate if your personal feeling is generally positive (good, increase, plentiful) or generally negative (bad, decrease, hard to get). If you do not feel positive or negative about any of the questions, mark the “neutral” response.

1. Do you feel business conditions are good or bad?
   _____ Good  _____ Bad  _____ Neutral

2. Do you feel jobs are hard to get or plentiful?
   _____ Plentiful  _____ Hard to get  _____ Neutral

3. Do you think business conditions will improve or worsen over the next six months?
   _____ Improve  _____ Decrease  _____ Neutral

4. Do you think jobs will increase or decrease over the next six months?
   _____ Increase  _____ Decrease  _____ Neutral

5. Do you expect your household income to increase or decrease over the next six months?
   _____ Increase  _____ Decrease  _____ Neutral

Note: These questions are similar to those used for The Conference Board’s “Consumer Confidence Survey.”
**Consumer Confidence Survey®**
*The Conference Board*
*Released: June 26, 2012*

**The Conference Board Consumer Confidence Index® Declines Again**

The Conference Board Consumer Confidence Index®, which had declined in May, fell further in June. The Index now stands at 62.0 (1985=100), down from 64.4 in May. The Expectations Index declined to 72.3 from 77.3. The Present Situation Index, however, increased to 46.6 from 44.9 last month.

The monthly Consumer Confidence Survey®, based on a probability-design random sample, is conducted for The Conference Board by Nielsen, a leading global provider of information and analytics around what consumers buy and watch. The cutoff date for the preliminary results was June 14.

Says Lynn Franco, Director of Economic Indicators at The Conference Board: "Consumer Confidence declined in June, the fourth consecutive moderate decline. Consumers were somewhat more positive about current conditions, but slightly more pessimistic about the short-term outlook. Income expectations, which had improved last month, declined in June. If this trend continues, spending may be restrained in the short-term. The improvement in the Present Situation Index, coupled with a moderate softening in consumer expectations, suggests there will be little change in the pace of economic activity in the near-term."

Consumers' assessment of current conditions improved slightly in June. Those claiming business conditions are "good" increased to 14.9 percent from 13.6 percent, however, those saying business conditions are "bad" increased to 35.1 percent from 34.7 percent. Consumers' appraisal of the job market was mixed. Those stating jobs are "hard to get" increased to 41.5 percent from 40.9 percent, while those claiming jobs are "plentiful" increased to 7.8 percent from 7.5 percent.

Consumers have grown less upbeat about the short-term outlook. The percentage of consumers anticipating business conditions to improve over the next six months declined to 15.5 percent from 16.6 percent, while those expecting business conditions will worsen increased to 16.2 percent from 12.9 percent. Consumers' outlook for the labor market was mixed. Those anticipating more jobs in the months ahead declined to 14.1 percent from 15.4 percent, while those expecting fewer jobs also declined to 20.6 percent from 21.5 percent. The proportion of consumers expecting an increase in their incomes declined to 14.8 percent from 15.7 percent.

Source: [http://www.conference-board.org/data/consumerconfidence.cfm](http://www.conference-board.org/data/consumerconfidence.cfm)
Survey of Consumers
Thompson Reuters/ University of Michigan
Released: June 29, 2012

Consumer confidence posted a sizable loss in June, with most of the overall decline in how consumers viewed future prospects for the national economy. Perhaps of greater importance was that the entire June decline was among households with incomes above $75,000. Higher income households were not only less optimistic about economic prospects but viewed their own financial prospects much less favorably. The percent of upper income households that expected improve finances in the year ahead fell to 24% in June from 37% in May. Lower income households, in contrast, benefitted to a greater degree from the recent declines in gas prices, which completely offset their less favorable outlook for the economy.

Job Growth Stalls

News reports about recent economic developments reaching consumers have become increasingly negative. Reports of job losses for the first time in six months have outnumbered job gains. For the first time this year, consumers were more likely to expect increases in the unemployment rate than additional declines. Confidence in economic policies remained near record lows, as just 10% of all consumers judged current policies favorable.

Buying Plans Decline among Upper Incomes

Buying plans were unchanged among lower income households but were much less favorable among those with incomes above $75,000. Favorable vehicle buying attitudes declined by 10% among upper income households but were unchanged among lower income households. Favorable buying plans for large household durables fell by 14% among higher income households compared with a loss of just 1% among lower income households.

Consumer Sentiment Index

The Sentiment Index was 73.2 in June 2012, down from 79.3 in May, but remaining slightly ahead of the 71.5 in last June’s survey. The June loss was nearly evenly split between the current and expected components of the Sentiment Index. The monthly loss in the Expectations Index was a bit larger, falling to 67.8 in June from 74.3.

Comments by Surveys of Consumers chief economist, Richard Curtin.

The overall June decline would normally be consistent with a somewhat slower spending growth rate. The sharp declines among upper income households, however, may have a greater impact on the economy since their spending accounts for a large share of the total. The June loss among higher income households was associated with a large drop in favorable ratings of economic policies and a growing recognition that federal policies to bridge the fiscal cliff will not even be discussed until the very last minute. This meant that they wanted to adopt more cautious spending plans now to protect their finances from potentially adverse developments.
About the Survey
The Surveys of Consumers has been conducted by the Survey Research Center at the University of Michigan since 1946. Founded by George Katona, the surveys have been under the direction of Richard Curtin since 1976. The Surveys of Consumers pioneered the development of measures of consumer confidence, and remains the pacesetter in the use of the data for understanding the important influence of consumer spending and saving decisions on the course of the national economy.

The surveys have proven to be an accurate indicator of the future of the national economy. The data is widely used by a broad range of business firms, financial institutions, and federal agencies. The Index of Consumer Expectations is an official component of the Index of Leading Indicators developed by the U.S. Department of Commerce.

Each month, 500 individuals are randomly selected from the contiguous United States (48 states plus the District of Columbia) to participate in the Surveys of Consumers. In order for the results to accurately represent the opinions of the population of the United States, it is important that each person selected participates. The questions asked cover three broad areas of consumer confidence: personal finances, business conditions, and future buying plans.

The importance of consumer confidence in shaping the course of the economy has been recognized in many countries. Other countries that now regularly monitor consumer sentiment through studies patterned after this survey include: Austria, Australia, Belgium, Canada, China, Denmark, Finland, France, Germany, Great Britain, Greece, Hungary, Ireland, Italy, Jamaica, Japan, Luxembourg, Mexico, Norway, Russia, Spain, Sweden, Switzerland, and Taiwan.

Source: http://press.sca.isr.umich.edu/press/get_release/41