

Covid resurgence weighs heavily on US households

The seventh biggest fall ever in University of Michigan sentiment must be acknowledged as a clear sign that the latest Covid spike is causing huge anxiety amongst households. Rising inflation is adding to their worries. Sentiment has given misleading signals on spending before and we think it will do again this time, but caution is warranted



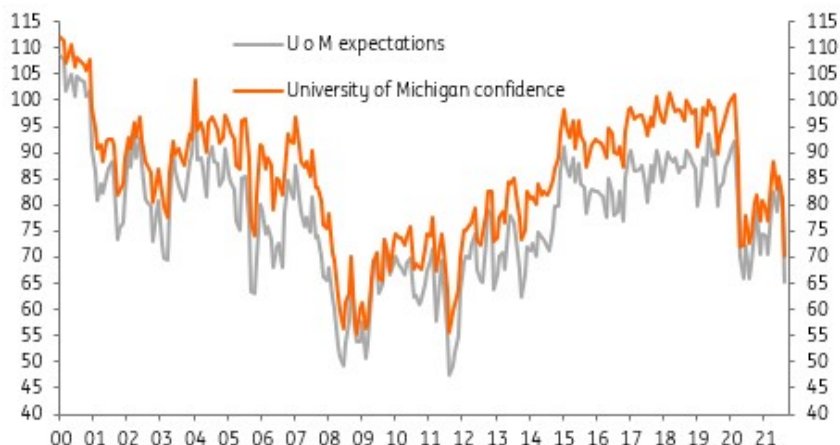
Movement of people wearing a protective mask and maintaining social distance, Domino Park, Brooklyn

Source: Shutterstock

Huge hit to sentiment

The University of Michigan consumer sentiment report has thrown up a very negative surprise with confidence plunging to its lowest level since 2011. It is an 11 point drop to 70.2. A huge fall has only been previously seen around major events, such as the pandemic start (March 2020 with an 11.9 point drop followed by a 17.3 point drop in April 2020), the Global Financial Crisis (12.7 point drop in October 2008) and Hurricane Katrina (12.2 point drop in September 2005).

University of Michigan sentiment index



Source: Macrobond, ING

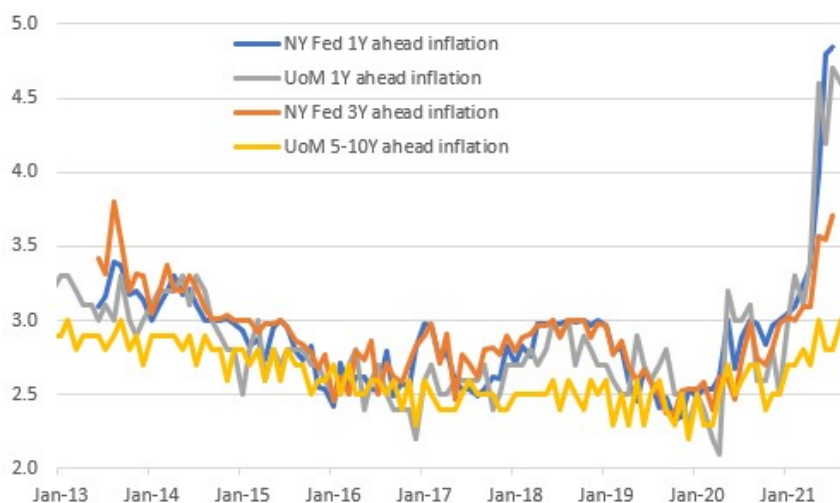
Covid worries return

It is difficult to rationalise given the strong macro performance and equity markets at all-time highs. Weakness seems driven by concerns over personal finances, which may at the margin be related to the ending of unemployment benefits, but we have to attribute the majority of the weakness to the latest spike in Covid cases. After all, there was a huge (37 point) drop in the "country will have continuous good times over next 12 months", while the survey also thinks there will be more unemployment over the next 12 months.

Inflation anxiety played its part

It could also be tied to inflation anxiety – 47% of households think inflation will exceed income growth over the next 1-2 years with just 19% thinking incomes will outpace inflation. The "good time to buy major household item" fell 11 points, which could also be tied to this. So too the readings for home purchases and vehicles.

Inflation expectations series

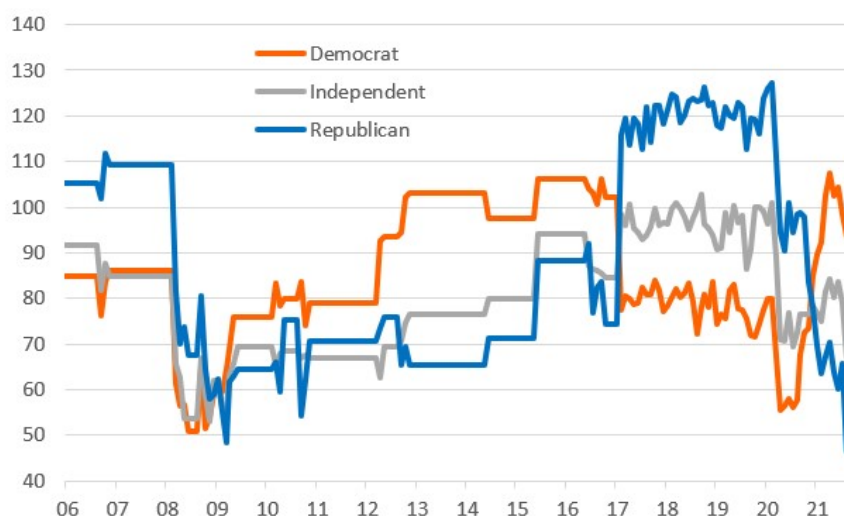


Source: Macrobond, ING

The political divide grows

There does seem to be a political angle as well. Confidence amongst Republican Party supporters plummeted from 65.7 to 46.7. That is an all-time low for a series that goes back to 1984! Sentiment amongst Democrat supporters did fall, but by less than 5 points. Independents were obviously in between – showing a drop of 11.6. The Republican Party themselves have been pushing the line that Government spending plans will only add to inflation risks while eye-balling a map shows that several of the Republican controlled states are seeing some of the biggest increases in Covid cases.

University of Michigan sentiment split by political support



Source: Macrobond, ING

Beware misleading signals...

That said, plunging confidence has given misleading signals in the past – such as Hurricane Katrina and we are hopeful that this will be repeated after this month’s release. After all, incomes are growing, jobs are being added in significant number, equities are at all-time highs so fundamentals in general are healthy and point to robust spending. We are also highly doubtful that we will see new lockdowns happen in the US given high vaccination numbers, that continue to rise.

Assuming we are correct then the Fed will likely “dial back” on its stimulus this year. The inflation expectations series shows 5-10Y ahead inflation expectations rising to 3% from 2.8%. This follows from the NY Fed survey of consumer inflation expectations that jumped to 3.7%. Given these events it looks increasingly difficult for the Fed to justify its assertion that “longer-term inflation expectations remain well anchored at 2 percent” as they still do within the FOMC statement.

Author

James Knightley

Chief International Economist, US

james.knightley@ing.com

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies)*. The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit <http://www.ing.com>.