European Commission

ISSN 2443-8049 (online)

European Business Cycle Indicators

How is inflation affecting consumer sentiment & behaviour?

3rd Quarter 2023

TECHNICAL PAPER 068 | OCTOBER 2023

EUROPEAN ECONOMY

Economic and Financial Affairs

European Economy Technical Papers are reports and data compiled by the staff of the European Commission's Directorate-General for Economic and Financial Affairs.

Authorised for publication by Reinhard Felke, Director for Policy Coordination, Economic Forecasts and Communication.

The Report is released every quarter of the year.

Luxembourg: Publications Office of the European Union, 2023

PDF ISBN 978-92-76-61683-2 ISSN 2443-8049 doi:10.2765/90327 KC-BF-23-008-EN-N

CREDIT
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European Commission
Directorate-General for Economic and Financial Affairs

European Business Cycle Indicators

3rd Quarter 2023

Special topic

- How is inflation affecting consumer sentiment and behaviour?

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- After a marked decrease over the second quarter, the EU and euro-area **Economic Sentiment Indicators (ESI)** slipped further, albeit at a slower pace, finishing the third quarter of this year 1.3 (EU) / 2.0 (EA) points lower compared to June. The indicator dipped further below its long-term average of 100 in both the EU (92.8 points) and the euro area (93.3 points).
- The EU/EA **Employment Expectations Indicator (EEI)** weakened in July and August before picking up slightly in September. The indicator's level in September was 1.9 (EU) / 2.2 (EA) points lower than in June, while remaining above long-term average.
- **Confidence** worsened over the third quarter in construction and among consumers. Industry and services confidence weakened to a lesser extent thanks to some signs of stabilisation in September. Confidence remained broadly stable in retail trade.
- **Economic sentiment worsened further in two of the six largest EU economies**, namely in Germany (-4.2) and Italy (-3.1). Sentiment in France (-0.8), Spain (-0.5) and the Netherlands (-0.5) was broadly stable, while improving again in Poland (+2.1). Compared to the indicators' long-term averages, confidence is now below average in all six largest Member States.
- The EU/EA **Economic Uncertainty Indicator (EUI)** picked up slightly, driven by higher perceived uncertainty in services. In industry, retail trade and among consumers the indicator remained broadly stable at June levels, while uncertainty decreased in construction.
- In July, **capacity utilisation** in industry decreased by 1.0 point compared to April and is now slightly below its long-term average. Capacity utilisation in services increased fractionally, rising above its long-term average.
- In July, the shares of industry managers pointing to **shortages of material and/or equipment** and/or to **shortages of labour force** as factors limiting their production declined, but remained high by historical standards. The share of managers reporting **insufficient demand** increased further, to above its long-term average level.
- As **consumers' quarterly quantitative perceptions of price developments** over the past 12 months edged down for the first time since 2020-Q4, **quantitative price expectations** for the next 12 months decreased slightly further. However, consumers' qualitative price expectations, which are published on a monthly basis, picked up in August and September (see special topic).

Special topic: How is inflation affecting consumer sentiment and behaviour?

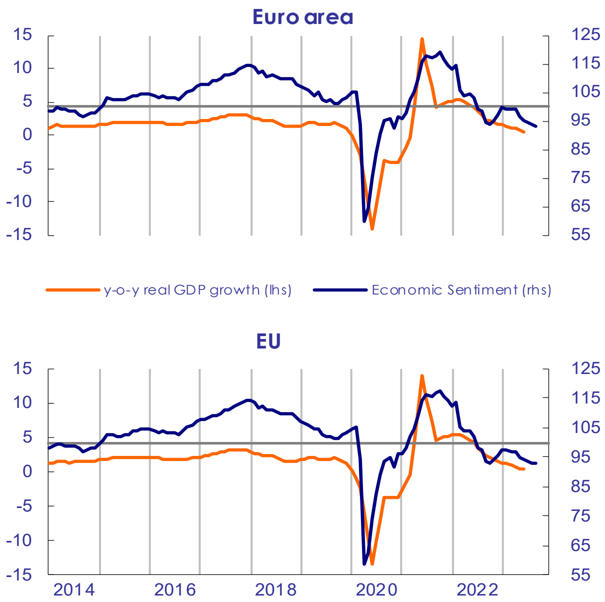
How do consumers perceive prices and expect them to develop over the next 12 months? How do their expectations and actual HICP inflation affect consumer confidence, their savings and spending intentions? To throw light on these and some related questions, the analysis presented in this special takes a close look at the results of the harmonised EU-wide consumer survey up to September 2023. Overall, the partial recovery in consumer confidence since inflation started to come down has not yet translated into clear improvements in the assessments of households' balance sheet positions. This, compounded by increasing intentions to save by the most affluent consumers, suggests subdued growth in private consumption ahead. The recent deterioration in consumer confidence in August and September - if confirmed in the months ahead - could further dampen the prospects for household spending.

1. RECENT DEVELOPMENTS IN SURVEY INDICATORS

1.1. EU and euro area

After a marked decrease over the second quarter, the EU and euro-area **Economic Sentiment Indicators (ESI)** slipped further, albeit at a slower pace (see Graph 1.1.1), finishing the third quarter of this year 1.3 (EU) / 2.0 (EA) points lower compared to June. The indicator dipped further below its long-term average of 100 in both the EU (92.8 points) and the euro area (93.3 points).

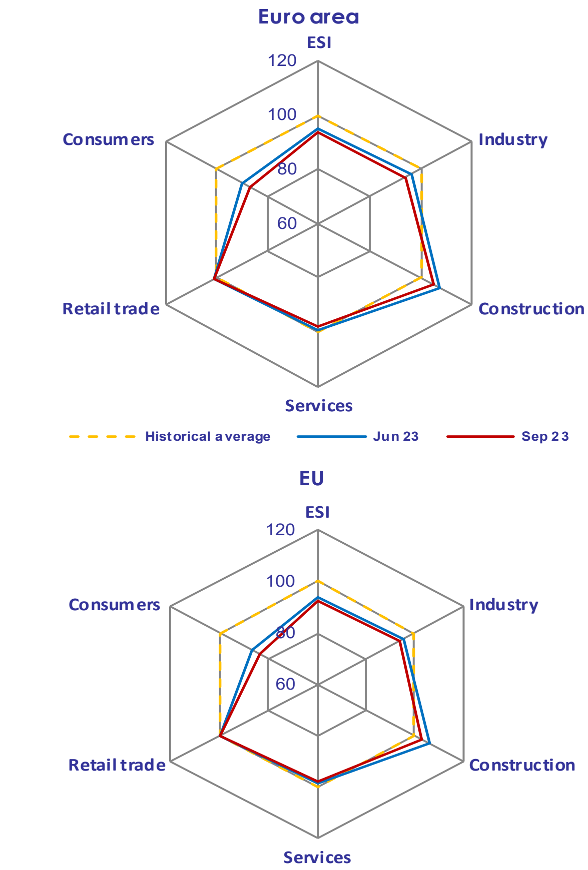
Graph 1.1.1: Economic Sentiment Indicator



Note: The horizontal line (rhs) marks the long-term average of the survey indicators. Confidence indicators are expressed in balances of opinion and hard data in y-o-y changes. If necessary, monthly frequency is obtained by linear interpolation of quarterly data.

From a sectoral perspective, EU confidence (see lower panel of Graph 1.1.2) worsened over the third quarter in construction and among consumers. Industry and services confidence weakened to a lesser extent thanks to some signs of stabilisation in September. Confidence remained broadly stable in retail trade. Developments in the EA were broadly in line with those in the EU, with decreases being slightly more marked.

Graph 1.1.2: Radar Charts



Note: A development away from the centre reflects an improvement of a given indicator. The ESI is computed with the following sector weights: industry 40%, services 30%, consumers 20%, construction 5%, retail trade 5%. Series are normalised to a mean of 100 and a standard deviation of 10. Historical averages are generally calculated from 2000q1. For more information on the radar charts see the Special Topic in the 2016q1 EBCI.

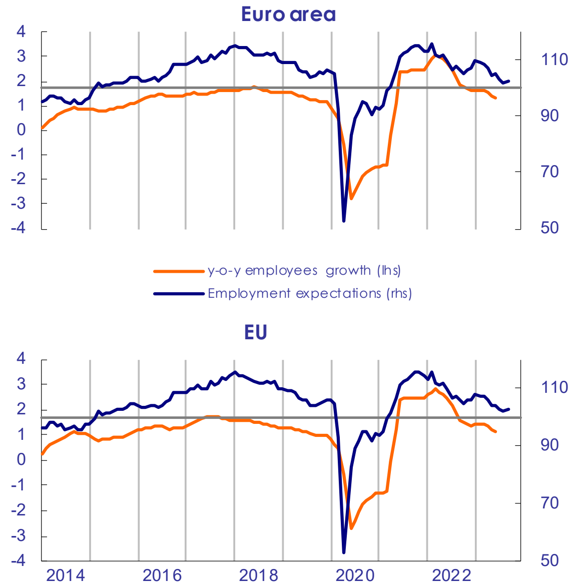
In September, in both the EU and the EA, the level of confidence remained above long-term average in construction only, while falling slightly below/remaining around it in services and retail trade. Confidence fell slightly further below long-term average in industry and among consumers.

In the third quarter, economic sentiment worsened further in two of the six largest EU economies, namely in Germany (-4.2) and Italy (-3.1). Sentiment in France (-0.8), Spain (-0.5) and the Netherlands (-0.5) was broadly unchanged, while it improved again in Poland

(+2.1). Confidence is currently below its long-term average in all six largest Member States.

The signal of a slowdown in the economy emanating from the ESI is consistent with the evolution of HCOB Flash Eurozone Composite PMI Output Index[1], which also decreased during the third quarter. Losing 2.7 points compared to June, the PMI fell to 47.2, further below its threshold of 50.0, and thus signalling a contraction of the euro area economy.

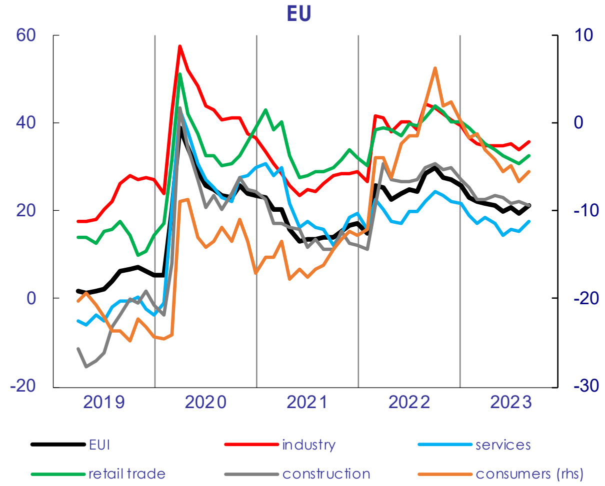
Graph 1.1.3: Employment expectations indicator



The EU/EA **Employment Expectations Indicator (EEI)** in September was 1.9 (EU) / 2.2 (EA) points lower than in June. Unlike the ESI, the indicator remained above long-term average. Employment expectations worsened marginally in all business sectors but remained above their respective long-term averages.

The EU/EA **Economic Uncertainty Indicator (EUI)**[2] picked up slightly over the quarter, driven by higher perceived uncertainty in services. In industry, retail trade and among consumers the indicator remained broadly stable at June levels, while it decreased in construction. In September, the EUI was 1.1 (EU) / 1.2 (EA) points above its June reading (see Graph 1.1.4).

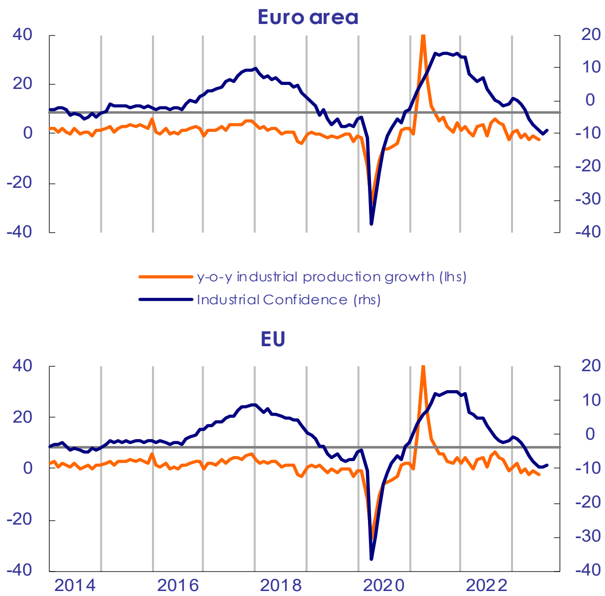
Graph 1.1.4: Uncertainty



Sector developments

Industry confidence decreased during the third quarter of 2023. Despite an uptick in September, the indicator's readings in September were slightly lower than in June (-1.1 points in the EU, -1.9 points in the EA). As shown in Graph 1.1.5., industry confidence remains below its long-term average in both the EU and the EA.

Graph 1.1.5: Industry Confidence indicator



[1] Contradictory signals from the EA ESI and the eurozone PMI can occur due to differences in their geographic and/or sectoral coverage, as well as the survey questions used for their construction. For a systematic comparison of the two indicators, see the special topic in the 2017-Q2 EBCI.

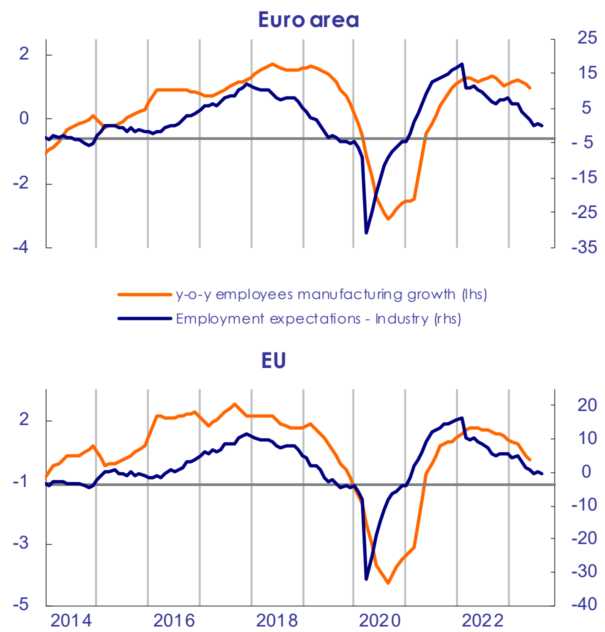
[2] See the special topic of the 2021-Q3 EBCI for background, and section 3.6 of the BCS User Guide for methodological details.

Zooming into the components of industrial confidence, the slight decrease resulted from a marked deterioration in managers' assessments of their **order books**. By contrast, their **production expectations** improved, while their assessment of **stocks** remained broadly stable. Of the components not included in the confidence indicator, managers' appraisals of **past production** and of the current **export order books** worsened markedly.

Industry managers' **employment expectations** (see Graph 1.1.6) decreased compared to June (-1.4 in the EU and -2.0 in the EA). Following the sharp fall observed since May last year, their **selling price expectations** remained virtually unchanged, ending the third quarter 0.1 (EU) / 0.8 (EA) points below their level in June. Selling price expectations in industry are, since last quarter, below their long-term average.

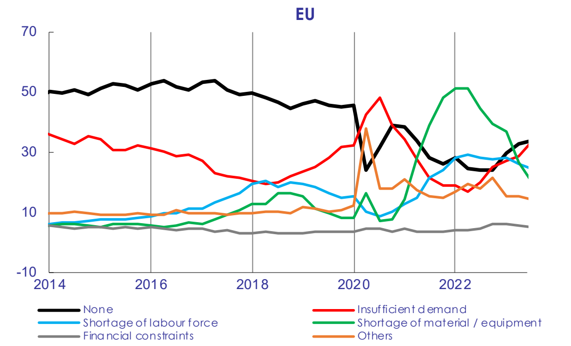
Industry confidence worsened further in three of the largest EU economies. It fell sharply for the third consecutive quarter in Germany (-5.0), and, to a lesser extent, in Italy (-2.8) and the Netherlands (-2.8). The indicator remained broadly stable in Spain (-0.1) and in France (-0.6), while improving somewhat in Poland (+1.6). The level of industry confidence in September is below long-term average in all six largest EU economies.

Graph 1.1.6: Employment expectations in Industry



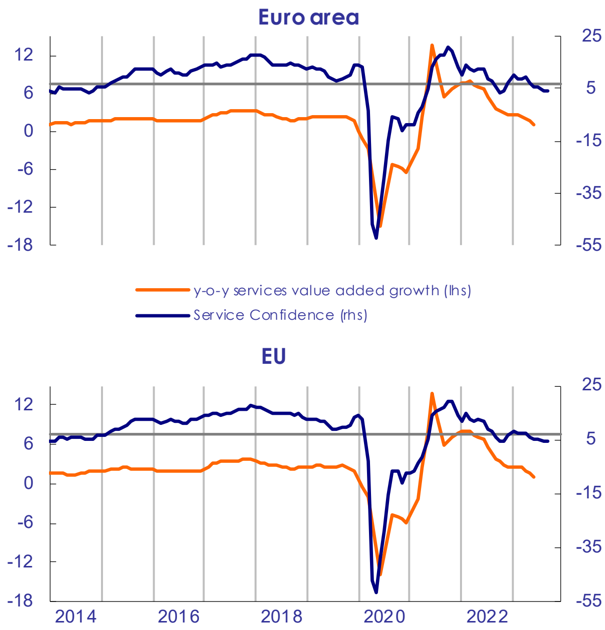
According to the quarterly manufacturing survey (carried out in July), **capacity utilisation** decreased by 1.0 point compared to April in both the EU and the EA. At 80.0% (EU) / 80.2% (EA), the indicator is now slightly below its long-term average of 80.6% (EU) / 80.7% (EA).

Graph 1.1.7: Industry – Factors limiting production (in %)

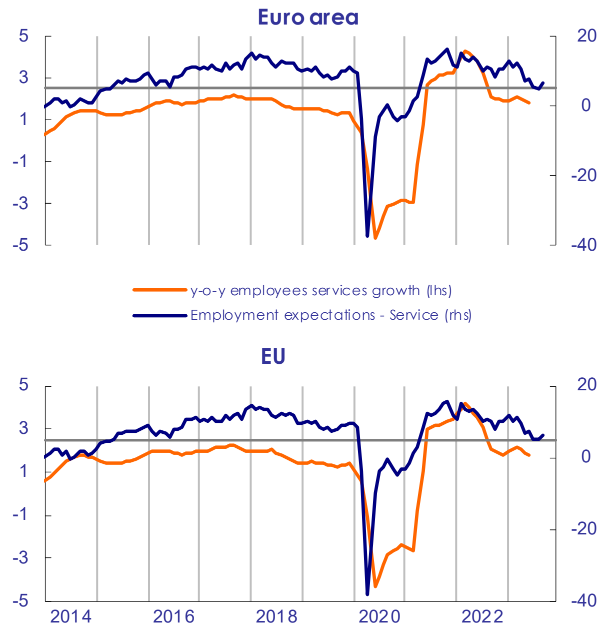


In July, the share of industry managers pointing to a shortage of material and/or equipment as a **factor limiting production** declined further in both the EU (-5.9 percentage points compared to April) and the EA (-6.4 pps). At 20.7% (EU) / 21.1% (EA), the share remains above historical averages (see Graph 1.1.7). The percentage of managers indicating shortages of labour force as a factor limiting their production edged down in both the EU (-1.7 percentage points) and the EA (-2.1 pps). At 24.5% (EU) / 22.9% (EA), the share remains high by historical standards. The share of managers reporting insufficient demand increased further in July (+4.7 in the EU, +5.7 in the EA). At 33.2% (EU) / 33.1% (EA), the percentage of managers stating insufficient demand as a limiting factor is now above its long-term average.

Graph 1.1.8: Services Confidence indicator



Graph 1.1.9: Employment expectations in services



In the EU, **services confidence** decreased slightly over the quarter. Compared to June, the EU indicator finished the third quarter 0.9 (EU) and 1.7 (EA) points down. In both areas, confidence is slightly below long-term average (see Graph 1.1.8).

Looking into the components of services confidence, managers' assessment of **past demand** worsened markedly, while views on the **past business situation** worsened in the EA but remained virtually unchanged in the EU. On the positive side, managers' **demand expectations** improved.

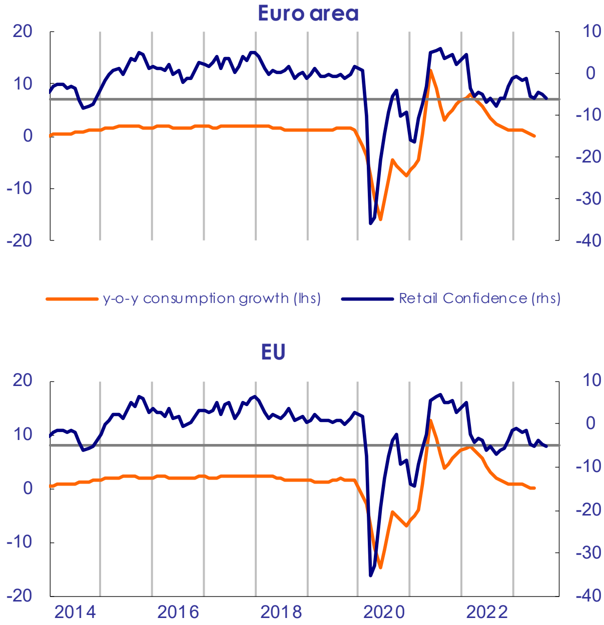
Despite a pick-up in September, **employment expectations in services** finished the quarter 1.0 (EU) / 1.2 (EA) points below their June level (see Graph 1.1.9). Managers' **selling price expectations** at the end of the third quarter were 0.7 points down compared to June in both the EU and the EA, falling to their lowest level since September 2021. Nevertheless, selling price expectations in services remain clearly above long-term average.

Among the six largest EU economies, services confidence shrank again in Germany (-4.6) and, to a lesser extent, in France (-1.8), while it stayed broadly unchanged in Italy (-0.8), Spain (-0.7) and Poland (+0.6). By contrast, services confidence improved in the Netherlands (+2.0).

In July compared to April, **capacity utilisation in services** increased fractionally in both the EU (+0.5) and the euro area (+0.7) to 90.7% and 90.6%, respectively. In both areas, the rate is above its long-term average of 89.1% (EU) and 88.8% (EA).

Retail trade confidence ended the third quarter of 2023 broadly unchanged compared to its June level (+0.3 points in the EU and +0.2 points in the EA). In the EU, confidence is at its long-term average (see Graph 1.1.10).

Graph 1.1.10: Retail Trade Confidence indicator



While retailers' assessment of the **volume of stocks** worsened, their expectations on the **future business situation** brightened. Their assessment of the **past business situation** remained stable.

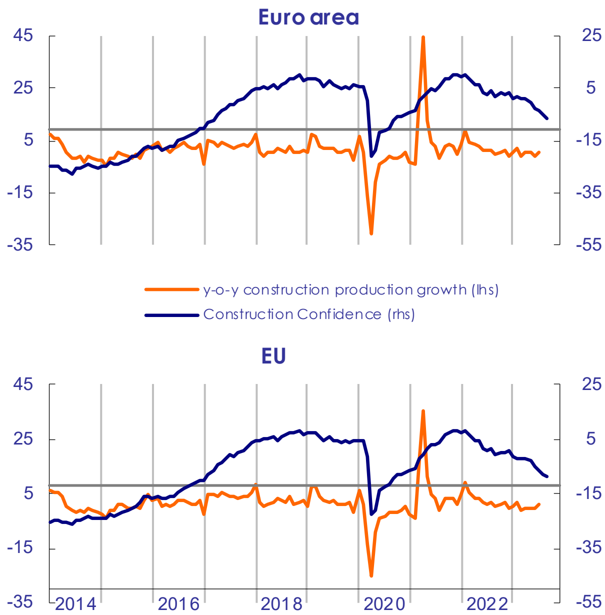
At the level of the six largest EU economies, retailers' confidence improved in France (+3.8), Spain (+1.9) and Poland (+1.0), while it worsened sharply in the Netherlands (-8.7), and to a lesser extent in Germany (-3.0) and in Italy (-1.5).

Construction confidence weakened over the third quarter (-3.4 in the EU, -3.5 in the EA), but remained above its long-term average (see Graph 1.1.11).

In both the EU and the EA, builders' **employment** expectations, and especially their appraisals of **order books** worsened. Assessments of order books have been on a downward trend since March last year.

By the end of the third quarter, the share of construction managers pointing to a **shortage of labour as factor limiting production** stayed almost unchanged at a high level in the EU (+0.5 points compared to June, to 28.6%), while picking up marginally again in the EA (+1.1 points compared to June, to 26.6%). Scarcities remained virtually unchanged in respect of the availability of **material and/or equipment**. The share of builders identifying them as factors limiting production came down by 0.2 (EU) / 0.1 (EA) percentage points to 9.9 (EU) / 7.3% (EA). The share of builders indicating financial constraints as a factor limiting their production remained virtually unchanged compared to June (+0.7 in the EU, +0.5 in the EA). At 9.9% (EU) / 9.3% (EA), the occurrence of financial constraints remains above long-term average. The share of managers reporting insufficient demand increased compared to June in both the EU (+2.6) and the EA (+2.9). At 28.7% (EU) / 27.8% (EA), the share of builders stating insufficient demand as a limiting factor reached its highest level since July 2020.

Graph 1.1.11: Construction Confidence indicator



Among the largest EU economies, construction confidence declined most in Spain (-9.9)[3] and

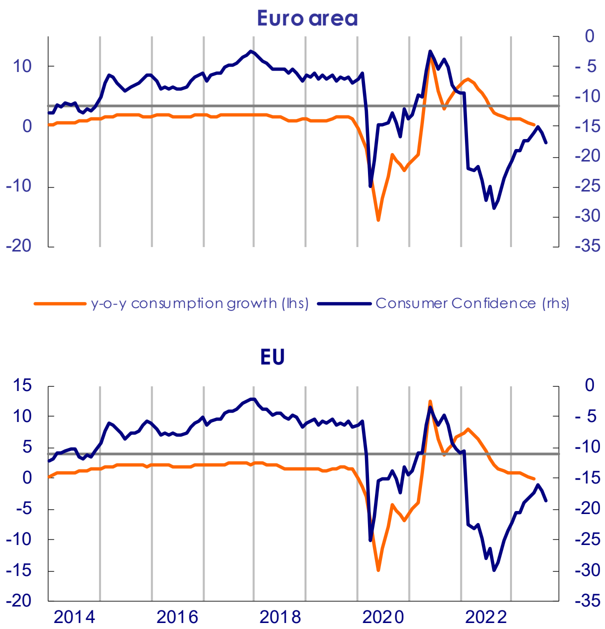
[3] The Spanish construction confidence indicator has a comparatively high month-to-month volatility.

Germany (-5.4), and less so in the Netherlands (-1.4) and France (-1.2), while it remained broadly stable in Italy (-0.9) and improved in Poland (+1.4).

Consumer confidence halted the rebound that started in autumn 2022. Compared to June, EU/EA consumer confidence was, respectively, 1.5 and 1.7 points lower at the end of the third quarter, further below its long-term average (see Graph 1.1.12).

Weaker confidence was mainly driven by downbeat expectations regarding the **country's general economic situation**, and **households' future financial situation**, while views on their past financial situation and their **intentions to make major purchases** remained broadly stable.

Graph 1.1.12: Consumer Confidence indicator

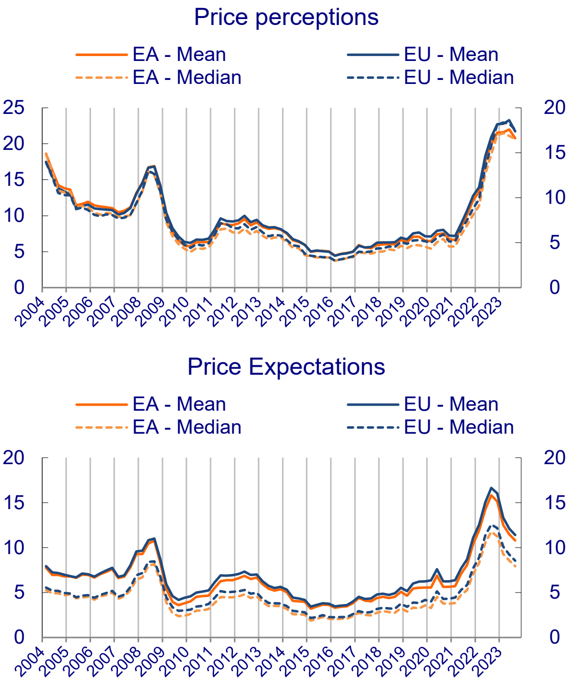


Consumer confidence decreased in Spain (-3.8), and more moderately so in Germany (-2.1), Italy (-1.7) and France (-1.1), while it recorded moderate increases in Poland (+2.0) and the Netherlands (+1.5).

In the EU and the EA, **consumers' quarterly quantitative perceptions of price developments** (change over the past 12 months, in % change) edged down for the first time since 2020-Q4. The arithmetic mean of price perceptions edged down over the third quarter, remaining at an exceptionally high level. The median of price perceptions, which is less sensitive to the presence of extreme values, remained broadly stable in both the EU and the EA, also suggesting that the peak has passed. **Quantitative price expectations** (change over the next 12 months, in %) decreased slightly, both in terms of mean and median, remaining at very high levels by historical standards (see Graph 1.1.13).[4] The results at total level were mirrored across almost all income, education and age groups, as well as among both men and women. However, consumers' qualitative price expectations, which are published on a monthly basis, picked up in August and September (see special topic).

The detailed results among the different socio-economic breakdowns can be downloaded from the European Commission's website.

Graph 1.1.13: Euro area and EU quantitative consumer price perceptions and expectations

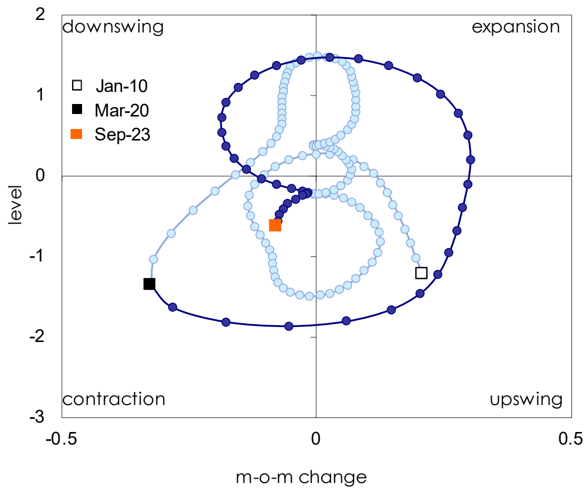


The slight worsening of economic sentiment in 2023-Q3, as captured by the ESI, also shows in the EU/EA **climate tracers** (see Annex for details). Both have moved further in the contraction zone (see Graphs 1.1.15 and 1.1.16).

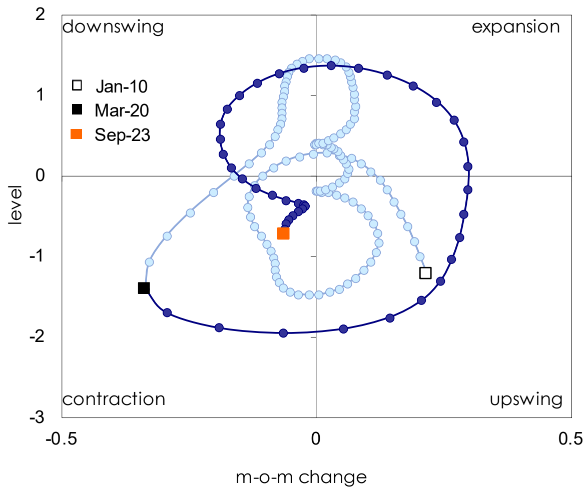
4 For more information on the quantitative inflation perceptions and expectations, see the special topic in the EBCI 2019Q1.

The developments in the sectoral EU/EA confidence indicators reverberated in the sectoral climate tracers (see Graph 1.1.17), both in terms of their intensity, as well as the direction of change: the industry and services tracers moved deeper into the contraction area. The retail trade tracers moved from the expansion quadrant into the downswing area, while the consumer tracers remained in the upswing area, but point to the contraction quadrant. The construction tracers remained in the downswing quadrant, pointing to the contraction area.

Graph 1.1.15: Euro area Climate Tracer

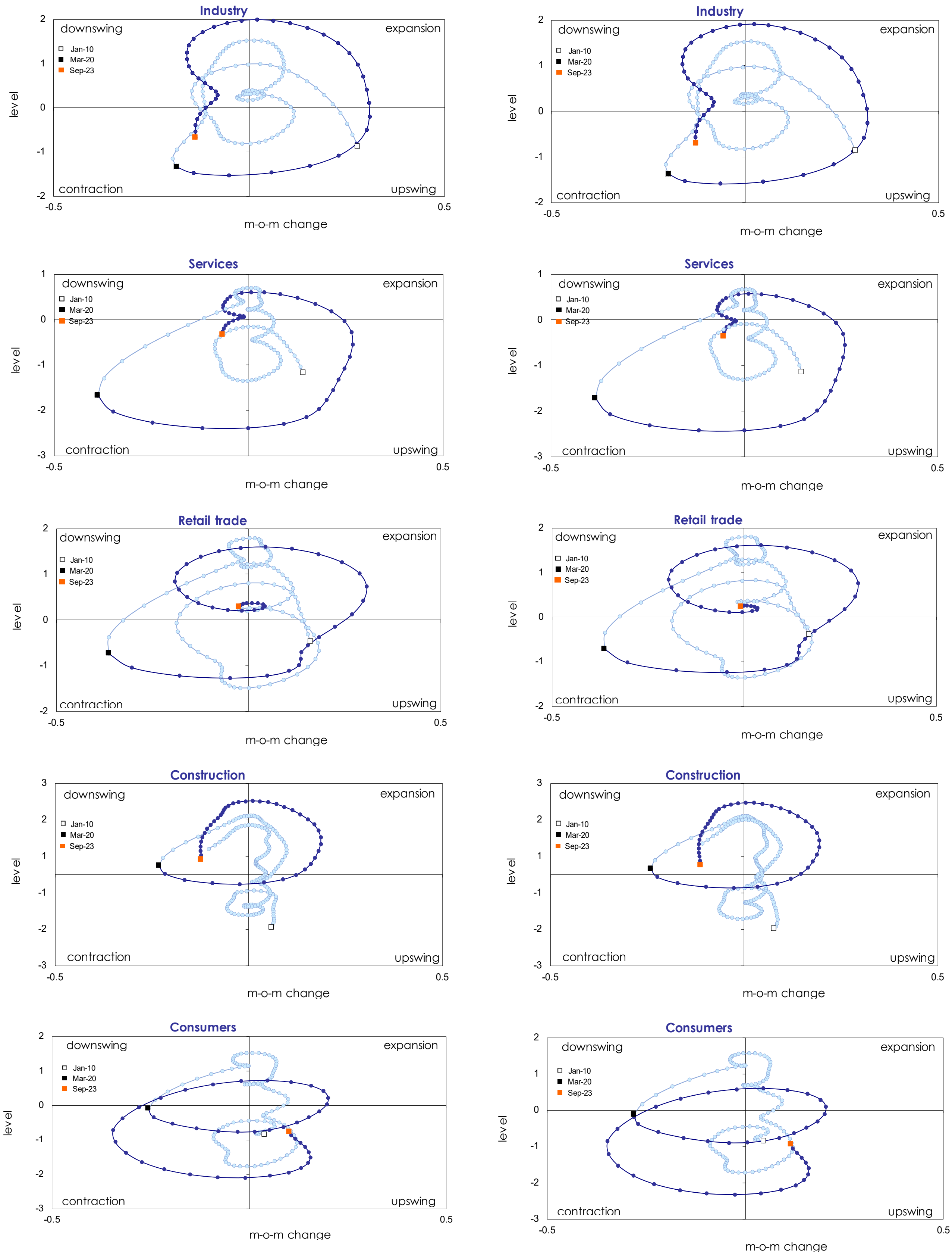


Graph 1.1.16: EU Climate Tracer



Graph 1.1.17: Economic climate tracers across sectors

Euro area **EU**

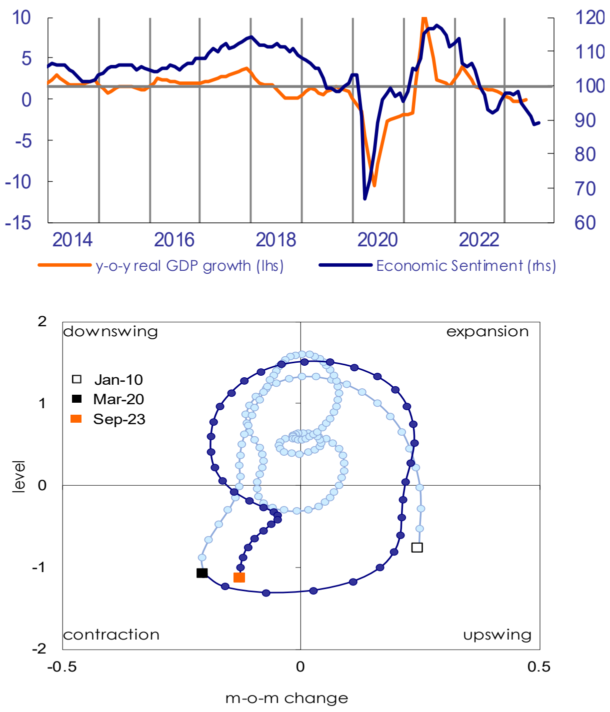


1.2. Selected Member States

After a substantial decrease in the second quarter of 2023, the **German** ESI declined further in July and August and remained broadly stable in September, finishing the third quarter 4.2 points below the June readings (see Graph 1.2.1). At 89.0 points, the indicator is well below its long-term average of 100. Consistently, the German climate tracer moved deeper into the contraction quadrant.

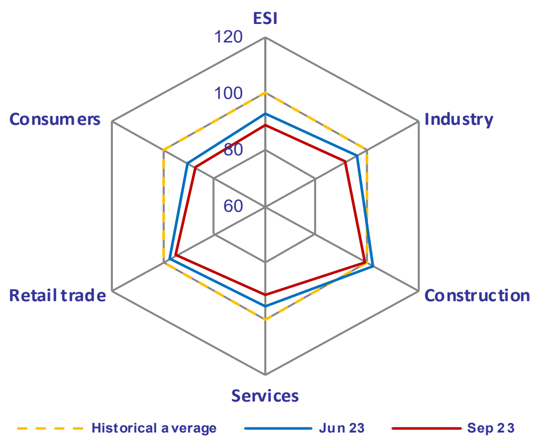
The Employment Expectations Indicator (EEI) worsened markedly over the quarter (-4.7 points compared to June) due to much more pessimistic employment plans in industry and services and, though to a lesser extent, in construction. In retail trade, employment plans remained essentially unchanged. The EEI is now below its long-term average.

Graph 1.2.1: Economic Sentiment Indicator and Climate Tracer for Germany



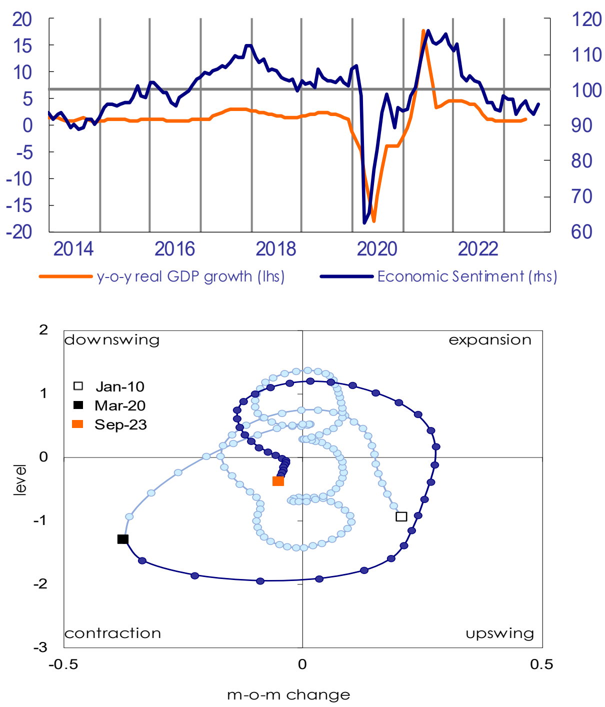
As shown in the radar chart (see Graph 1.2.2), the worsening of confidence was broad-based across all business sectors and among consumers. The deterioration was particularly strong in industry, services, and construction. In retail trade and among consumers, the decline was milder but still marked. Confidence slipped slightly below historical average in the construction sector, while falling further below it in industry, services, retail trade and among consumers.

Graph 1.2.2: Radar Chart for Germany



The **French** ESI declined markedly in July and August and rebounded strongly in September. Overall, at the end of the third quarter, the indicator was still 0.8 points lower than in June. At 95.9 points, the indicator was below its long-term average. The French climate tracer moved further down in the contraction area (see Graph 1.2.3).

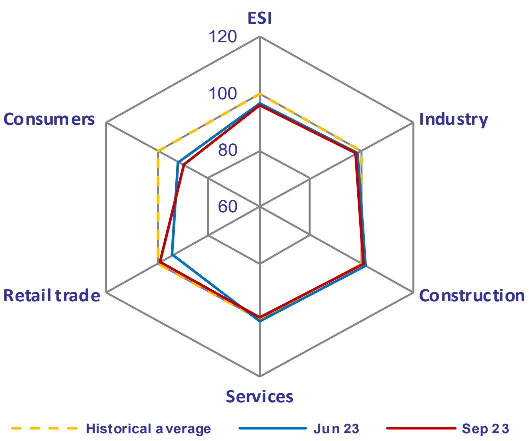
Graph 1.2.3: Economic Sentiment Indicator and Climate Tracer for France



The Employment Expectations Indicator (EEI) decreased slightly (-0.8 points compared to June) due to worsened employment plans among services, retail trade and especially industry managers, only partially offset by an increase in construction.

As evidenced by the radar chart (see Graph 1.2.4), confidence worsened in services, construction and among consumers, while sentiment remained broadly stable in industry and improved markedly in retail trade. Confidence is now below historical average among consumers and in all business sectors, except for construction.

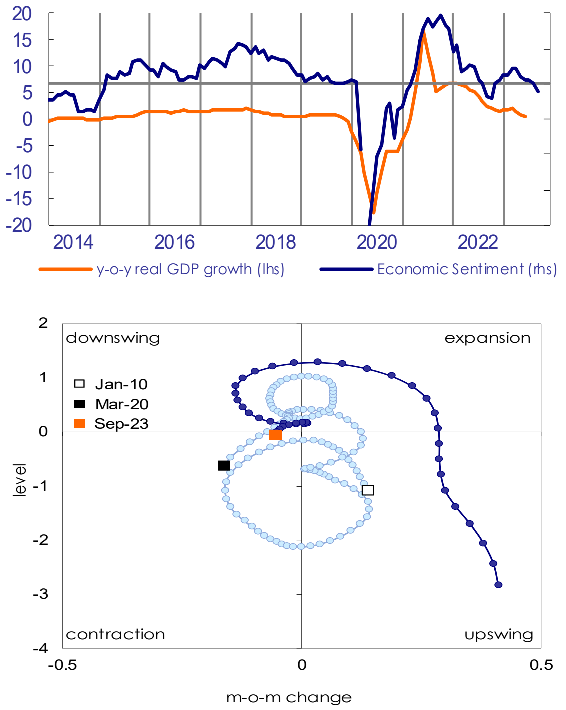
Graph 1.2.4: Radar Chart for France



The **Italian** ESI declined markedly over the quarter, losing 3.1 points compared to June. At a level of 97.9 points, the indicator is now below its long-term average. The Italian climate tracer moved from the downswing quadrant towards the contraction area and now stands at the border between the two areas (see Graph 1.2.5).

The Italian EEI decreased strongly in July, picked up in August, and improved markedly in September, ending the quarter 1.6 points higher than in June. More optimistic employment plans in services offset less optimistic ones in retail trade and construction. Employment expectations in the industry sector stayed broadly stable.

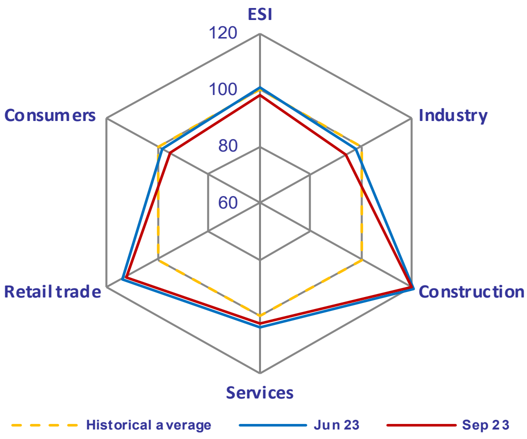
Graph 1.2.5: Economic Sentiment Indicator and Climate Tracer for Italy[5]



As shown in the Italian radar chart (see Graph 1.2.6), confidence decreased strongly in industry and among consumers, while in retail trade, services, and construction, the decline was milder. Confidence is now below its long-term average in industry and among consumers, while remaining well above it in the other surveyed business sectors.

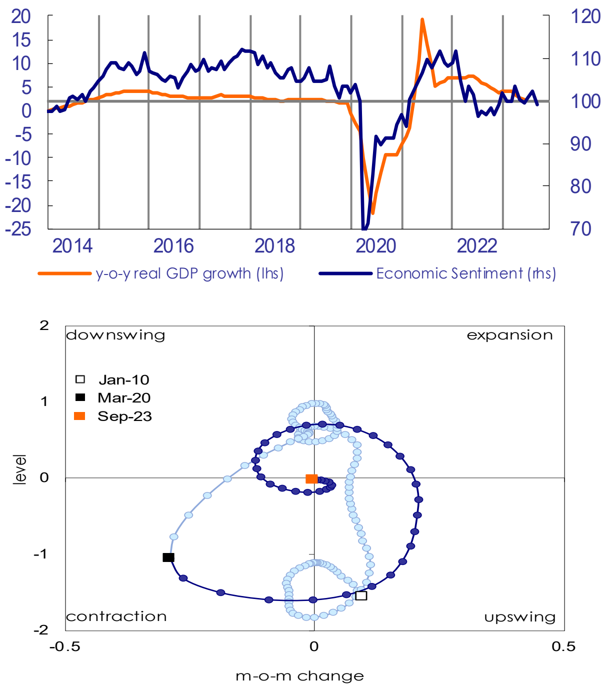
5 Due to a missing value for April 2020, the climate tracer for Italy is interrupted between March and May 2020.

Graph 1.2.6: Radar Chart for Italy



The **Spanish** ESI rose markedly in July and August and fell strongly in September, finishing the third quarter virtually at the same level as at the end of the previous quarter (-0.5 points compared to June). The indicator in September fell just below its long-term average (see Graph 1.2.7). The Spanish climate tracer moved from the upswing area to the neutral intersection between all the quadrants (see Graph 1.2.7).

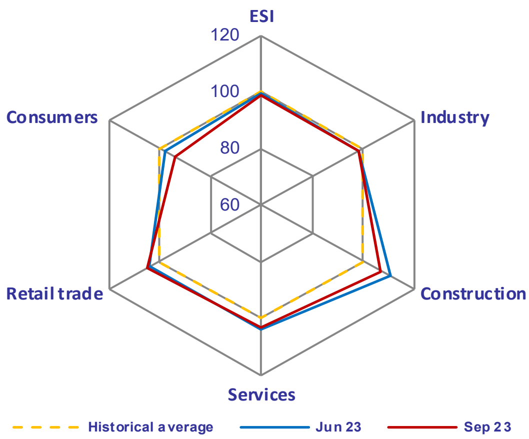
Graph 1.2.7: Economic Sentiment Indicator and Climate Tracer for Spain



At the end of the third quarter, the Spanish EEI was 1.4 points lower than in June, mainly because of much less optimistic employment plans among construction managers.[6] Managers in services were also less optimistic, while employment plans improved over the quarter in industry and remained broadly stable in retail trade.

As shown in the radar chart (see Graph 1.2.8), confidence worsened strongly in construction and among consumers, while it was up in retail trade and remained broadly stable in industry and services. Confidence remained above its long-term average in services, retail trade and construction, while falling just below it in industry, and more so among consumers.

Graph 1.2.8: Radar Chart for Spain

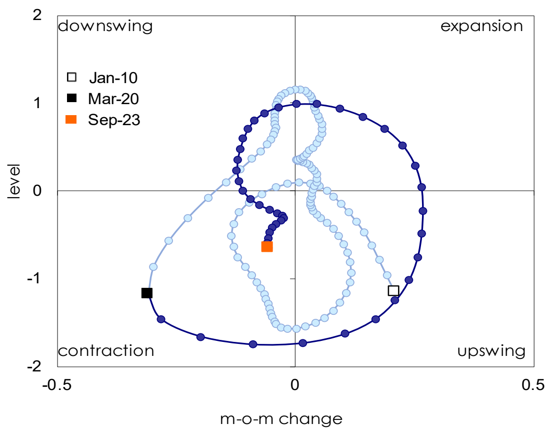


The ESI for the **Netherlands** remained broadly stable over the quarter, coming in 0.5 points lower in September than in June. At 93.3 points, the ESI is well below its long-term average of 100.

The climate tracer for the Dutch economy moved deeper in the contraction area (see Graph 1.2.9).

6 The Spanish employment expectations indicator has a comparatively high month-to-month volatility.

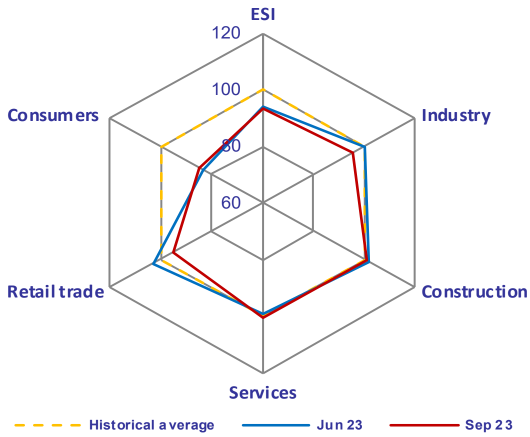
Graph 1.2.9: Economic Sentiment Indicator and Climate Tracer for the Netherlands



The EEI for the Netherlands zigzagged during the last quarter and ended the third quarter 0.3 points lower than in June. Employment plans worsened markedly in construction and, though to a lesser extent, in retail trade. By contrast, they stayed broadly stable in industry and improved somewhat in services.

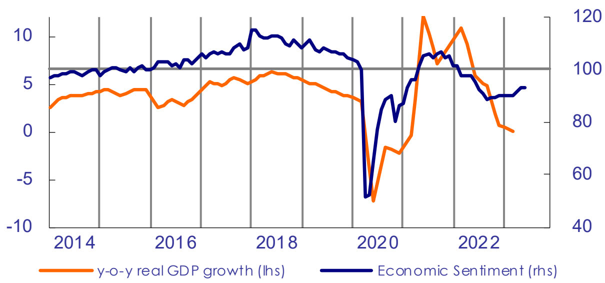
As shown in the radar chart (see Graph 1.2.10), confidence worsened significantly in retail trade and less so in industry and construction. In services and among consumers, confidence improved. The confidence level is well below long-term average in industry, retail trade and particularly among consumers. By contrast, it is just above long-term average in services and construction.

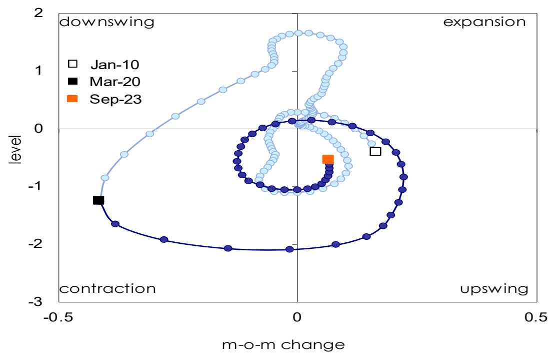
Graph 1.2.10: Radar Chart for the Netherlands



The ESI for **Poland** completed the third quarter of 2023 slightly above its June readings (+2.1 points). At 95.5 points, the indicator remained well below its long-term average. The Polish climate tracer remained in the upswing quadrant, now pointing to the expansion area (see Graph 1.2.11).

Graph 1.2.11: Economic Sentiment Indicator and Climate Tracer for Poland

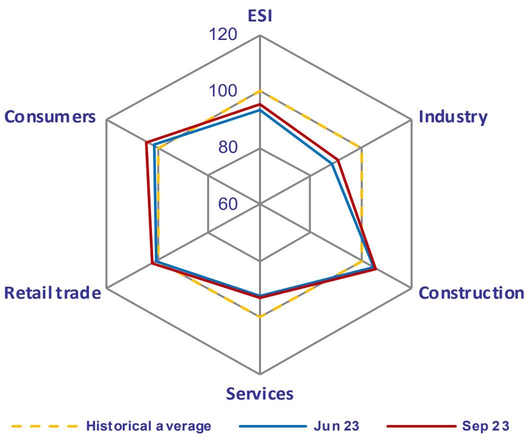




The Polish EEI moved up and down over the quarter and finished 2.8 points above its June level. The improvement reflected much more optimistic employment plans in services, construction and particularly in industry, while retailers' employment expectations remained broadly flat compared to June.

As shown in the radar chart (see Graph 1.2.12), confidence improved in industry, retail trade, construction and among consumers, while it remained broadly stable in services. Sentiment remained well below historical averages in industry and services, while remaining above among consumers, in retail trade and in construction.

Graph 1.2.12: Radar Chart for Poland



2. HOW IS INFLATION AFFECTING CONSUMER SENTIMENT AND BEHAVIOUR?

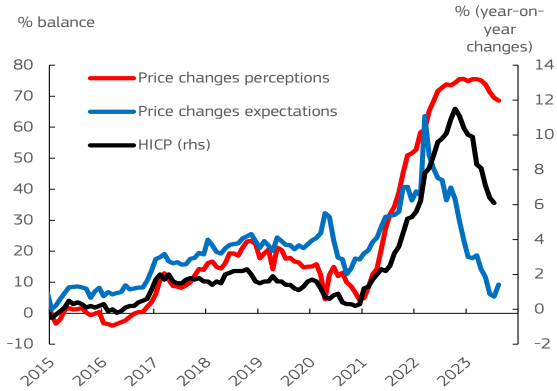
Introduction

How do consumers perceive past price developments and expect them to develop over the next 12 months? How do their expectations and actual HICP inflation affect consumer confidence, their savings and spending intentions? To throw light on these and some related questions, the analysis presented in this special takes a close look at the results of the harmonised EU-wide consumer survey up to September 2023.

Price developments and consumer confidence

Reflecting developments in HICP inflation, an increasing share of consumers in the EU reported rising prices from early 2021 until autumn 2022. After a period of stabilisation at record-high level,[7] the balance of replies reporting (fast/moderately/slightly) increasing prices over those reporting stable or falling prices started to decline in April 2023, while remaining at exceptionally high levels (see Graph 2.1).

Graph 2.1: Consumers' qualitative perceptions of price developments over the past (Q5) and next (Q6) 12 months, and HICP inflation - EU



From October 2020 to March 2022, consumers' expectations of future prices soared as well. Thereafter, the indicator of consumers' qualitative expectations started to decrease despite the continued increase in their price perceptions. It is important to note, however, that consumers were still expecting prices to increase, albeit at a slower pace (see Graph 2.2). Consumers' expectations in quantitative terms (see Graph 1.1.13 in section 1.1) actually continued to increase up to 2022-Q3, i.e. peaked broadly in line with HICP.

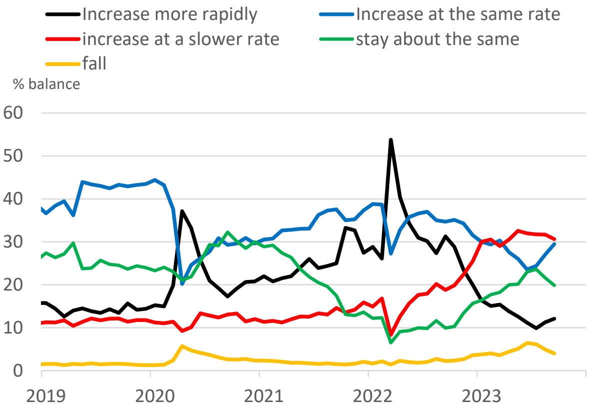
Looking at recent developments, notwithstanding the continued fall in HICP inflation, the latest available data for August and September 2023 show that consumers revised their expectations back up again, driven by a larger share of consumers expecting prices to increase more rapidly again or increase at the same rate (see Graph 2.2).[8]

---

7 The survey asks consumers: "How do you think consumer prices have developed over the last 12 months? They have risen a lot/risen moderately/risen slightly/stayed about the same/fallen/don't know". They are also asked about their inflation expectations: "By comparison with the past 12 months, how do you expect consumer prices will develop in the next 12 months? They will increase more rapidly/increase at the same rate/increase at a slower rate/stay about the same/fall/don't know."

8 Consumers are also asked by how much (in % changes) they expect prices to change over the next 12 months. These "quantitative" inflation expectations – which are only published at a quarterly frequency – continued to increase up to October 2022, reaching an all-time high of 17.5%.

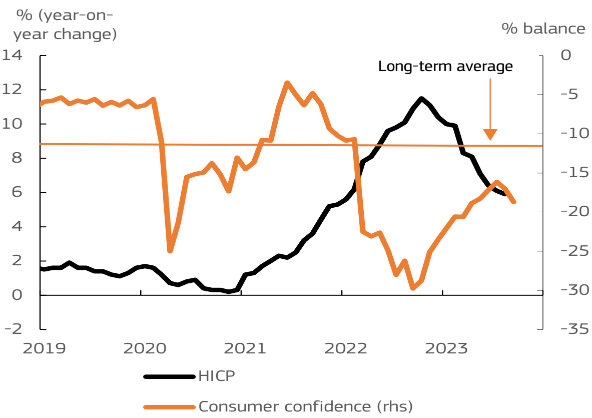
Graph 2.2: Consumers' qualitative expectations of price developments over the next 12 months, EU.



Consumer confidence in the EU reached an all-time low in September 2022, as HICP inflation was about to peak at 11.5% the following month. Since then and up to July 2023, consumer confidence has steadily increased towards its long-term average (see Graph 2.3), while inflation has gradually eased. This suggests that moderating inflation has had a positive influence on consumer confidence.

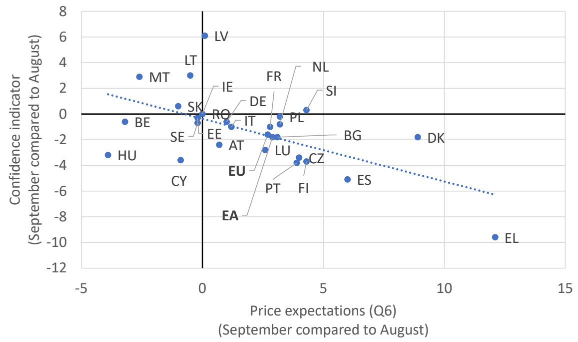
As inflation (and prices) has remained high, consumer sentiment has remained well below its long-term average. Moreover, in August and September, consumer confidence decreased once again. This coincided with the above-mentioned renewed up-tick in consumers' inflation expectations after several months of decline.

Graph 2.3: Consumer confidence and HICP inflation, EU



The strong influence of consumers' inflation expectations on their confidence is visible also at Member State level. Graph 2.4 points to a negative correlation between changes in consumer price expectations and consumer confidence in the latest survey wave of September: the more consumers revised their price expectations upwards, the more they reported lower confidence.

Graph 2.4: Consumer confidence and HICP inflation, EU, EA and EU Member States



Developments at the level of components of confidence

A large proportion of consumers have yet to recover from the negative shocks to confidence suffered over the last three years. The consumer confidence indicator is composed of four variables: views on the past and expected financial situation of the household [9], intentions to make major purchases[10] and views on the general economic situation in their country[11]. Graph 2.5 shows that all components improved as inflation eased between autumn 2022 and July 2023, though all remaining well below both their pre-COVID levels and their long-term averages.

Since then, expectations decreased but remain at a rather high level of around 12%.

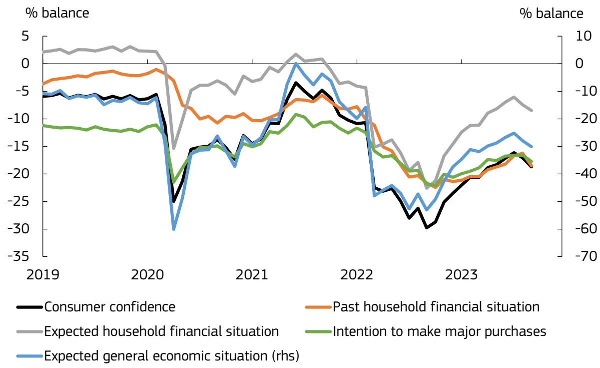
9 The question on the past financial situation reads "How has the financial situation of your household changed over the last 12 months? It has got a lot better/got a little better/stayed the same/got a little worse/got a lot worse/don't know". The question on the expected financial situation reads "How do you expect the financial position of your household to change over the next 12 months? It will get a lot better/get a little better/stay the same/get a little worse/get a lot worse/don't know".

10 "Compared to the past 12 months, do you expect to spend more or less money on major purchases (furniture, electrical/electronic devices, etc.) over the next 12 months? I will spend much more/a little more/about the same/a little less/muss less".

11 "How do you expect the general economic situation in this country to develop over the next 12 months? It will get a lot better/get a little better/stay the same/get a little worse/get a lot worse/don't know".

This suggests that an important share of consumers have not yet recovered from the negative confidence shocks incurred over the past three years (COVID, war in Ukraine, steep increase in energy costs and high inflation).

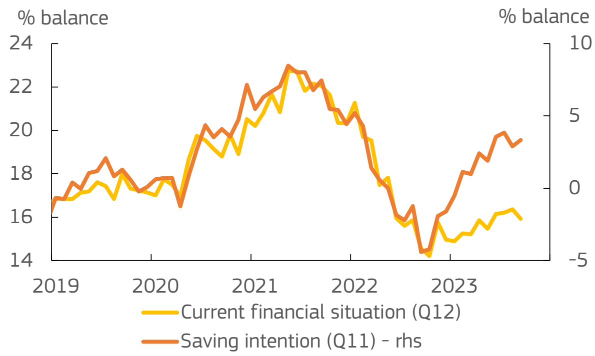
Graph 2.5: Consumer confidence and its components, EU



The survey results show that a gap opened between consumers' forward-looking and backward-looking assessments of their household's financial situation, with the forward-looking assessments rebounding more strongly. The results further show that the recovery in consumers' intentions to make major purchases was also slow compared to the expectations of an improved financial situation. In August and September 2023, however, the gap shrank as consumers' expectations concerning their household's future financial situation slipped back down again.

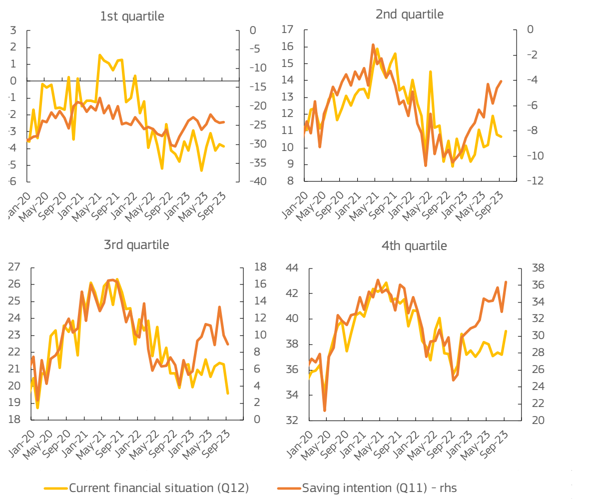
Household's current financial situation and their saving intentions

Graph 2.6: Saving intentions vs current saving and dissaving, EU



An opening gap is also apparent between the balance of currently saving or dissaving households[12] and their savings intentions over the 12 months following the survey[13]. Between early 2020 and autumn 2022, developments in the two variables had been very similar: after increasing steeply until the summer of 2021, they both fell rapidly to a trough in October 2022, when inflation peaked. When inflation started to decline, consumers' intentions to save started soaring, beyond their pre-COVID19 level (see Graph 2.6). By contrast, the balance of currently saving or dissaving households improved much more slowly. The discrepancy between changes in the assessment of the current savings/dissaving situation and savings intentions mainly results from developments among consumers with the highest incomes, the group with the largest saving potential (see Graph 2.7).

Graph 2.7: Saving intentions vs Current saving and dissaving by income quartile, EU



It is worth noting that the share of respondents reporting to be drawing on their savings or running into debt – an indicator of financial distress - increased rapidly between August 2021 and October 2022, when it reached an all-time high. The percentage of respondents reporting to be saving (a lot or a little) decreased to a similar extent (see Graph 2.8). Since inflation started to ease, both series have been showing some

12 "Which of these statements best describes the current financial situation of your household? We are saving a lot/a little /just managing to make ends meet on our income/having to draw on our savings/running into debt/don't know".

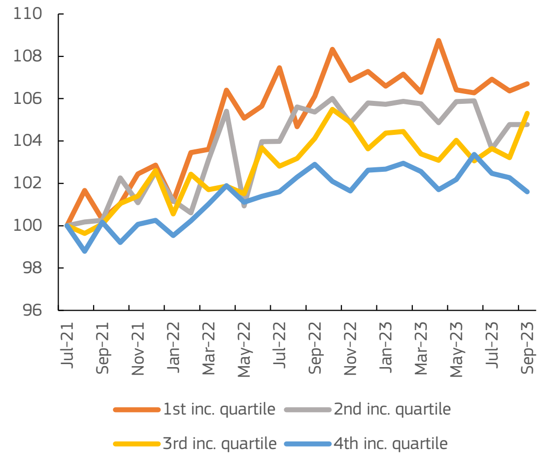
13 "Over the next 12 months, how likely is it that you save any money? Very likely/fairly likely/not likely/not at all likely/don't know".

improvement, but the share of consumers reporting to be in financial distress remains very high.

Graph 2.8: Percentage of respondent replying they are currently saving versus those who are dissaving

When looking at the financial distress indicator by income quartiles, it becomes apparent that the gap between low-income and high-income groups has widened markedly. In July 2021, 21.5% of households from the 1st income quartile reported being in financial distress, against around 5.9% of respondents from the 4th quartile. In September 2023, the share of households from the 1st income quartile in financial distress increased by 6.7 percentage points to 28.2%, while the increase has remained contained for the fourth income quartile (+1.6 percentage points to 7.5%) (see Graph 2.9).

Graph 2.9: Financial distress indicator by household income quartile – EU - Jul. 2021 = 100



Conclusions

Overall, the partial recovery in consumer confidence since inflation started to come down has not yet translated into clear improvements in the assessments of households' balance sheet positions. This, compounded by increasing intentions to save by the most affluent consumers, suggests subdued growth in private consumption ahead. The recent deterioration in many of the above-discussed consumer variables in August and September - if confirmed in the months ahead - could further dampen the prospects for household spending.

ANNEX

Reference series

Confidence indicators	**Reference series from Eurostat (volume/year-on-year growth rates)**
Total economy (ESI)	GDP, seasonally- and calendar-adjusted
Industry	Industrial production, working day-adjusted
Services	Gross value added for the private services sector, seasonally- and calendar-adjusted
Consumption	Household and NPISH final consumption expenditure, seasonally- and calendar-adjusted
Retail	Household and NPISH final consumption expenditure, seasonally- and calendar-adjusted
Building	Production index for building and civil engineering, trend-cycle component

Economic Sentiment Indicator

The economic sentiment indicator (ESI) is a weighted average of the balances of replies to selected questions addressed to firms and consumers in five sectors covered by the EU Business and Consumer Surveys Programme. The sectors covered are industry (weight 40 %), services (30 %), consumers (20 %), retail (5 %) and construction (5 %).
Balances are constructed as the difference between the percentages of respondents giving positive and negative replies. EU and euro-area aggregates are calculated on the basis of the national results and seasonally adjusted. The ESI is scaled to a long-term mean of 100 and a standard deviation of 10. Thus, values above 100 indicate above-average economic sentiment and vice versa. Further details on the construction of the ESI can be found here.
Long time series (ESI and confidence indices) are available here.

Economic Climate Tracer

The economic climate tracer is a two-stage procedure. The first stage consists of building economic climate indicators, based on principal component analyses of balance series (s.a.) from five surveys. The input series are as follows: industry: five of the monthly survey questions (employment and selling-price expectations are excluded); services: all five monthly questions except prices; consumers: nine questions (price-related questions and the question about the current financial situation are excluded); retail: all five monthly questions; building: all four monthly questions. The economic climate indicator (ECI) is a weighted average of the five sector climate indicators. The sector weights are equal to those underlying the Economic Sentiment Indicator (ESI, see above).
In the second stage, all climate indicators are smoothed using the HP filter in order to eliminate short-term fluctuations of a period of less than 18 months. The smoothed series are then normalised (zero mean and unit standard deviation). The resulting series are plotted against their first differences. The four quadrants of the graph, corresponding to the four business cycle phases, are crossed in an anti-clockwise movement and can be described as: above average and increasing (top right, ‘expansion’), above average but decreasing (top left, ‘downswing’), below average and decreasing (bottom left, ‘contraction’) and below average but increasing (bottom right, ‘upswing’). Cyclical peaks are positioned in the top centre of the graph and troughs in the bottom centre.

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