



Understanding the Consumer Confidence Index
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Imagine that you are talking with your neighbor in your backyard, and you mention that you and your wife are shopping for a new car, you are getting ready to [refinance](#) your house and your wife's brother recently lost his job. Your neighbor tells you he was recently promoted, his wife is starting a business and his daughter just bought a new computer. What kind of analysis about the health of the U.S. economy could an economist make based on your backyard conversation? Well, that depends on what the conversation suggests about consumer confidence.

The mention of recent or upcoming purchases of a computer and a car suggests strong consumer demand. Your plan to refinance your home is a positive sign for the future, implying that you are confident in your ability to meet future mortgage payments. The refinancing suggests also the possibility of lower mortgage payments, which could mean an increase in your [discretionary income](#). Your neighbor's promotion and the start of his wife's new business are also positive economic signs.

The only negative reference during the conversation was the mention of one person who recently lost a job. But, from the other information exchanged between you and your neighbor, the economist might conclude that consumer confidence is high, which is good news for the economy because, on average, consumers are responsible for two-thirds of the nation's economic activity, or the [gross domestic product](#) (GDP).

Consumer Confidence

Consumer confidence, measured by the [Consumer Confidence Index](#) (CCI), is defined as the degree of optimism on the state of the economy that consumers (like you and me) are expressing through their activities of savings and spending.

The CCI is prepared by [The Conference Board](#), and was first calculated in 1985. In that year the result of the index was arbitrarily set to 100, representing the index's benchmark. This value is adjusted monthly on the basis of a household survey of consumers' opinions on current conditions and future expectations of the economy. Opinions on current conditions make up 40% of the index, with expectations of future conditions comprising the remaining 60%. In the glossary on its [website](#), The Conference Board defines the Consumer Confidence Survey as "a monthly report detailing consumer attitudes and buying intentions, with data available by age, income and region".

In the most simplistic terms, when their confidence is trending up, consumers spend money, indicating a healthy economy. When confidence is trending down, consumers are saving more than they are spending, indicating the economy is in trouble. The idea is that the more confident people feel about the stability of their incomes, the more likely they are to make purchases.

The Survey

Each month The Conference Board surveys 5,000 U.S. households. The survey consists of five questions that ask the respondents' opinions about the following:

1. Current business conditions.
2. Business conditions for the next six months.
3. Current employment conditions.
4. Employment conditions for the next six months.
5. Total family income for the next six months.

Survey participants are asked to answer each question as "positive", "negative" or "neutral". The results from the Consumer Confidence Survey are released on the last Tuesday of each month at 10am EST.

The Calculations

Once the data has been gathered, a proportion known as the 'relative value' is calculated for each question separately: each question's positive responses are divided by the sum of its positive and negative responses. The relative value for each question is then compared against each relative value from 1985, which is set as the benchmark because 1985 is the first year the index was calculated. This comparison of the relative values results in an 'index value' for each question.

The index values for all five questions are then averaged together to form the Consumer Confidence Index; the average of index values for questions one and three form the [Present Situation Index](#), and the average of index values for questions two, four and five form the [Expectations Index](#). The data is calculated for the United States as a whole and for each of the country's nine census regions.

How the Data Is Used

Manufacturers, retailers, banks and the government monitor changes in the CCI in order to factor in the data in their decision-making processes. While index changes of less than 5% are often dismissed as inconsequential, moves of 5% or more often indicate a change in the direction of the economy.

A month-on-month decreasing trend suggests consumers have a negative outlook on their ability to secure and retain good jobs. Thus, manufacturers may expect consumers to avoid retail purchases, particularly large-ticket items that require financing. Manufacturers may pare down inventories to reduce overhead and/or delay investing in new projects and facilities. Likewise, banks can anticipate a decrease in lending activity, mortgage applications and credit card use. When faced with a down-trending index, the government has a variety of options, such as issuing a tax rebate or taking other [fiscal](#) or [monetary](#) action to stimulate the economy.

Conversely, a rising trend in consumer confidence indicates improvements in consumer buying patterns. Manufacturers can increase production and hiring. Banks can expect increased demand for credit. Builders can prepare for a rise in home construction and government can anticipate improved tax revenues based on the increase in consumer spending.

Lagging Perspective

The next time you hear the results from the latest Consumer Confidence Survey, keep in mind that economists view consumer confidence as a [lagging indicator](#), which responds only after the overall economy has already changed. The explanation for this delayed reaction of the CCI is that it takes time for consumers to recover from and respond to economic events. The importance of a lagging indicator is that it confirms that a pattern is occurring. So, an increase in spending today may reflect the results of an economy that recovered a few months ago. Conversely, a decrease in spending today may confirm an ongoing recession.

Conclusion

Since consumer spending is so important to the nation's financial health, the Consumer Confidence Index is one of the most accurate and closely watched economic indicators. The index is based on a survey of five questions posed to 5,000 households, measuring their optimism on the health of the economy. The CCI, however, is a lagging indicator, so, whatever the survey says, remember that it doesn't tell us what is going to happen but what has happened and if it can be expected to continue.

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