# PERCEPTION VS. REALITY:

## EXAMINING MIDDLE-INCOME HOUSEHOLDS' FINANCIAL OUTLOOK HEADING INTO 2024

A report on findings from the Primerica Financial Security Monitor™ survey and Household Budget Index™.

By Amy Crews Cutts, Ph.D., CBE ®

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# Executive Summary

The financial outlook of middle-income households plays a key role in the U.S. economy. But there is often a gap in perception vs. reality of the financial situation among these households, defined as those with incomes of $30,000 to $130,000. Given that this subset of the population accounts for 57% of all households in the U.S., examining the differences between their perception of their finances and the reality of what the economic data shows is critical to understanding their financial situation.

To better appreciate the impact of the economy on this core group, Primerica lauched the Financial Security Monitor™ (FSM™) in 2020. The quarterly survey measures changes in perceptions about the finances of more than 1,000 middle-income households. As inflation climbed in recent years, Primerica also wanted to better understand its impact on middle-income families. As a result, leveraging federal data the company launched the monthly Household Budget Index™ (HBI™) in August 2023 to examine how the cost of necessities — food, utilities, gas and health care — are affecting these households.

Today, the data from both show that while the pace of inflation has moderated, it continues to affect the financial outlook of middle-income households. Primerica's Household Budget Index™ (HBI™) shows that the cumulative loss from the rise in the cost of food, gas, utilities and health care since May 2021 has created an average cumulative deficit of $2,440 in family budgets. As a result, rebuilding depleted savings and paying off debt is likely to take several more months and potentially even several years for many middle-income families.

Given this mixed landscape, it's important to examine how perception vs. reality in the data align — and where the two diverge.

- **Even as inflation wanes, middle-income households are feeling increasingly less confident in their financial situation**. About 48% of survey respondents rated their personal finances as "excellent" or "good" in Q3 2023, a slight decline from 50% in the previous survey, and a marked decline from 53% the previous year.
- **Families are cutting back on spending, turning to credit cards and depleting savings to adjust to higher prices: About 72% of respondents in the Q3 2023 survey stated their incomes were not keeping up with inflation**. Among those, about 74% said they were cutting back on nonessential purchases like entertainment or restaurant meals, 84% were curtailing or stopping saving for the future or dipping into their savings to cover the deficit, and 28% said they were using their credit cards more.
- **Consumer spending has not slowed**. From January 2021 through September 2023, consumer spending has grown at an average annual rate of 4.2%, the second strongest period of growth in over 50 years. In 2021, the consumer spending growth rate set a record at 8.1%.
- **The compounding impact of inflation has left a deep mark on household finances**. According to the Q3 2023 survey, 80% of the respondents indicated rising gas and grocery prices have influenced their ability to stick to their budget.

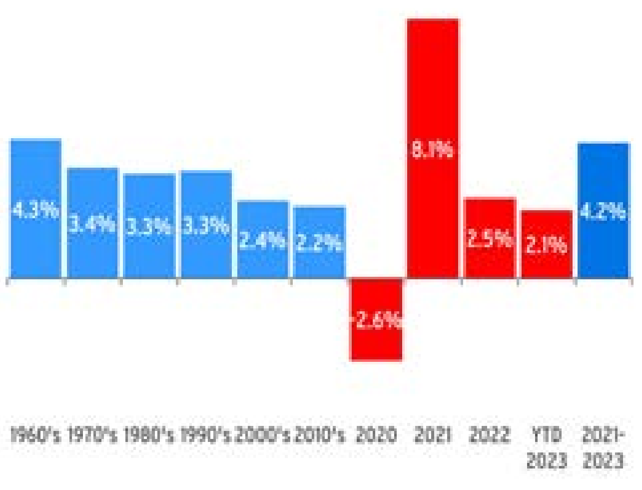
- **While wages rose faster than inflation in 2020 and 2021, respondents began indicating their income was falling behind the cost of living by the Q4 2020 survey**. Shortly after, inflation's rapid rise started to outpace income gains and the Consumer Price Index (CPI) hit a 42-year high for year-over-year growth of 9.1% in June 2022, the third highest peak in the rate of inflation since 1960.
- **Over the last few years, middle-income households have underestimated the economy's impact on their future economic activities**. For example, they have not been successful at predicting the likelihood that they would increase the use of their credit cards. Since the survey's launch in 2020, the deviation between expectations and actions has averaged almost 25 percentage points higher with them increasingly turning towards credit cards. On a more positive note, nearly 9% of respondents in Q2 2023 planned to add to their savings account and 26% of respondents in the Q3 2023 survey ended up doing so. The average difference between savings intentions and actions was over 15 percentage points.
- **Spending of retirement or personal savings has increased**. In the Q2 2023 survey, about 5% of respondents thought they would spend some of their personal or retirement savings in the months ahead, and 34% indicated that they had needed to tap this resource in the Q3 2023 survey.

> The compounding impact of inflation has left a deep mark on middle-income household finances. Over the past few years families have repeatedly underestimated the economy's impact on their finances, such as whether they would need to use their credit cards more frequently. That's why even as inflation wanes, middle-income households are feeling increasingly less confident in their financial situation.

# The Pandemic's Lingering Impact on the U.S. Economy

When COVID-19 hit the U.S., Congress rapidly stepped in to provide financial support to businesses and households beginning just two weeks after shutdowns began. In total, families received $2.4 trillion in pandemic relief payments and increased unemployment benefits. Additionally, payments on many mortgages and federal student loans were suspended. Federal student loans did not accrue interest during the suspension period, which ended in September 2023, saving student loan borrowers $115 billion in accrued interest over the three and a half years. Payments on student loans resumed in October 2023, marking an end to federal pandemic support.

**Exhibit 1: Growth in Real (Inflation-adjusted) Personal Consumption Expenditures**
Average annualized growth rate (%)




Source: AC Cutts & Associates LLC, U.S. Bureau of Economic Analysis, Federal Reserve Bank of St. Louis (FRED). 2023 data through September.

Without federal support, the economy may have looked drastically different. Instead, consumer spending, outside of the early months of the pandemic, remained extraordinarily strong. In the 1960s, inflation-adjusted consumer spending grew at an average annual rate of 4.3% over the decade [Exhibit 1].

From January 2021 through September 2023, consumer spending grew at an average annual rate of 4.2%, the second strongest period of growth in over 50 years. Moreover, 2021's remarkable 8.1% growth in consumer spending set the record since the modern measurement of the metric began in 1959.

The pandemic also exposed weaknesses in the global supply networks, resulting in shortages, production delays and logistical log jams. At the same time, governments and businesses around the world began embracing decarbonization efforts, shifting demand preferences just as supply networks began breaking. A shortage of silicon semiconductor microchips was one of the primary issues affecting global commerce, and while the amount of chips supplied rose to new records, demand rose even faster. New car lots were empty and everything from refrigerators to TVs to water heaters were on backorder starting in 2020 and continuing well into 2022.

The massive federal support for consumer pocketbooks combined with supply chain shortages provided the perfect recipe for inflation.

[1] U.S. Bureau of Economic Analysis, "Effects of Selected Federal Pandemic Response Programs on Personal Income" https://www.bea.gov/sites/default/files/2023-03/effects-of-selected-federal-pandemic-response-programs-on-personal-income-2022q4-3rd.pdf

[2] ibid

> The Consumer Price Index (CPI) eventually hit a 42-year high for year-over-year growth of 9.1% in June 2022. It marked the third highest peak in the rate of inflation since 1960.

## Inflation's Grip on the U.S. Economy

Inflation was surprisingly low throughout the worst of the pandemic into early 2021. Some prices rose quickly, such as those for new vehicles and lumber, but inflation overall stayed in line with the Federal Reserve's target of 2% or less. And then it didn't. A few months into 2021, prices of all sorts of items started to rise quickly, leading the Consumer Price Index (CPI) to eventually hit a 42-year high for year-over-year growth of 9.1% in June 2022. It marked the third highest peak in the rate of inflation since 1960 [Exhibit 2].

**Exhibit 2: Inflation periods and their causes since 1960**
Percent change in Consumer Price Index versus same period a year ago


Source: AC Cutts & Associates LLC, U.S. Bureau of Economic Analysis, Federal Reserve Bank of St. Louis (FRED)

# A Look Back to the '70s and '80s Inflation

In the 1970s, the U.S. economy experienced major paradigm shifts and shocks. Although inflation peaked in 1970, President Nixon's frustrations with high unemployment spurred him a year later to unilaterally abandon the Bretton Woods system for currency exchange, which pegged global currency values to gold, and issue an Executive Order establishing temporary wage and price controls. The end of the gold standard sent global financial markets into chaos and price controls artificially increased consumer demand, both of which ultimately lead to higher inflation. Just as Nixon ended his policies restricting wage and price growth, the Organization for Petroleum Exporting Countries (OPEC) sharply cut oil exports to the U.S. By December 1974, inflation hit 12.4%. Adding insult to injury, not only did gas prices rise sharply, but Americans also had to wait in long lines just to fill up their cars.

For a brief period in the middle 1970s, inflation subsided, and the economy grew. Then the Iranian Revolution in 1979 and the Iran-Iraq war in 1980 once again led to skyrocketing energy prices. Inflation peaked at a new high of 14.7% in April 1980, before a series of aggressive interest rate hikes by the Federal Reserve Board tamed the inflation dragon.

Following the tumultuous events of the 1970s and early 1980s, the country experienced brief periods of higher-than-normal inflation caused by global events, such as Iraq's invasion of Kuwait in 1990, which sent global oil prices up, or when companies and governments invested heavily in technology upgrades in 1999 in preparation for the turn of the millennium.

# Perceptions of Inflation's Bite

Economic studies have shown that consumers would rather deal with a recession that results in high unemployment than face high inflation. Cynically, this could stem from the view that other people lose their jobs, but inflation affects me personally. Digging a little deeper, however, it's clear that inflation has an insidious and permanent impact on individuals and families, especially those who are already economically vulnerable, whereas unemployment is a (hopefully) temporary state.

The Great Recession (2007-2009) is the only recorded period in the CPI's history when inflation dove deep into the negative digits, a period of deflation [Exhibit 2]. This was largely a result of the freefall in housing prices and record numbers of foreclosures. While it marked a terrible period of time when many families lost their homes because they could no longer afford their mortgage payments, the prices of many goods and services didn't decline much.

While an inflation rate between 0% and 2% is generally considered benign, it still means that prices for goods and services are rising overall, reflecting the many ebbs and flows in commerce and the relative scarcity of resources. As a result, taming inflation after a period of rising prices doesn't mean those prices drop back to their previously lower levels. Instead, they simply increase more slowly.

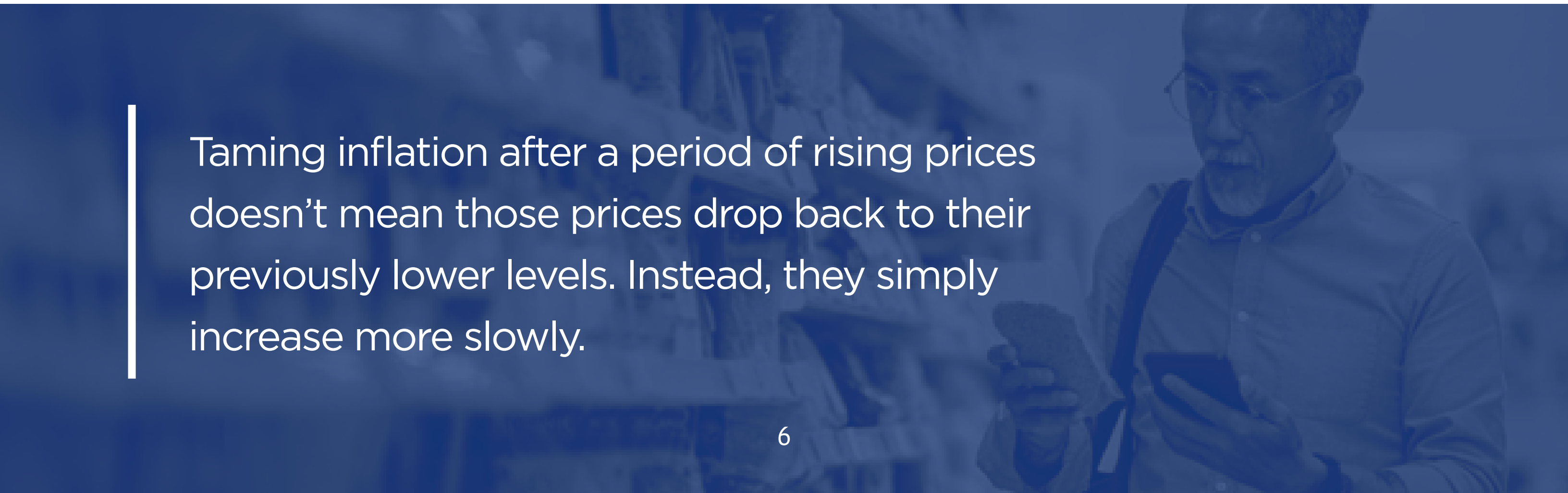
Inflation itself is not a problem when incomes are also rising by the same rate or faster. Indeed, over time this has meant that many enjoy a better standard of living. Since 1997, when the Federal Reserve Bank of Atlanta began tracking wage growth, the rise in income has exceeded the rise in prices in most years [Exhibit 3].

**Exhibit 3: Annualized wage growth and inflation since 1997**
Year-over-year percent change


Source: AC Cutts & Associates LLC, U.S. Bureau of Economic Analysis, U.S. Bureau of Labor Statistics, Federal Reserve Bank of St. Louis (FRED).
2023 data through September.

Between 1997 and 2019, wages rose an average of 3.6% per year while inflation, as measured by the CPI, rose an average of 2.2%.

More recently, inflation exceeded the growth in wages from April 2021 through February 2023. Since then, inflation has slowed and incomes are once again rising faster than prices, but consumers are still expressing concerns about their financial health and well-being in surveys such as Primerica's FSM™.



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# Findings from the Primerica Financial Security Monitor™ Survey of Middle-Income Households

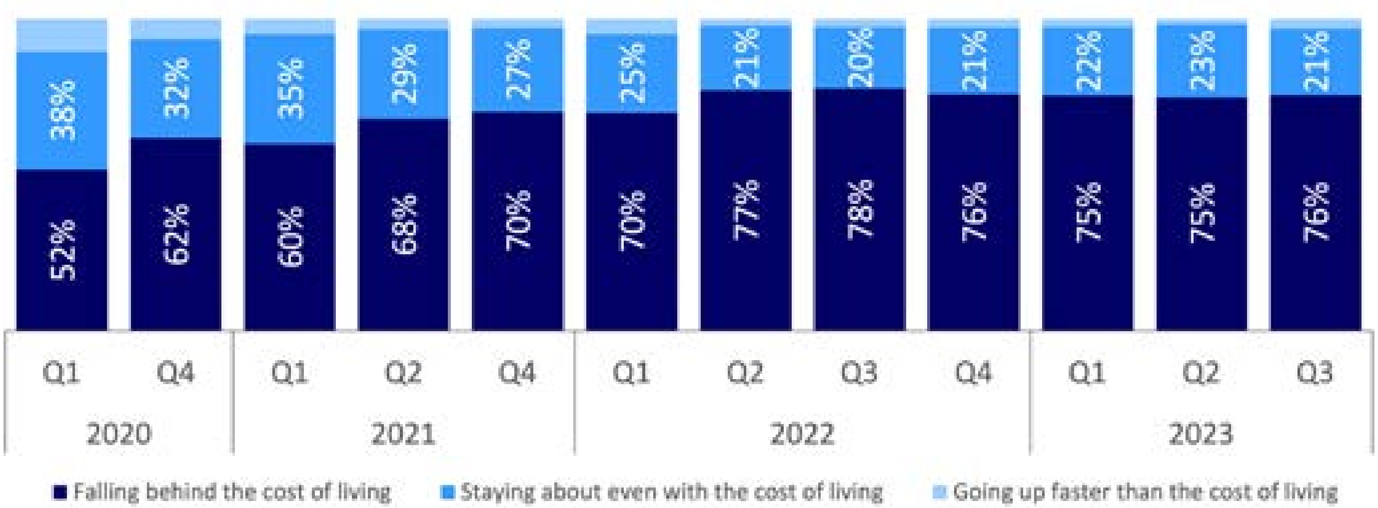
Primerica has been asking middle-income consumers about their financial outlook and perceptions about the economy since 2020. Responses to whether a respondent's income is keeping up with the cost of living show that households began feeling stressed by inflation in late 2020, well before inflation first topped 2% in March 2021.

Exhibit 4 shows the shares of respondents indicating whether their incomes were rising faster, equal to or slower than the rate of inflation. Even though Exhibit 3 indicates that wages were rising faster than inflation in 2020 and early 2021, in Q4 2020 the percentage of survey respondents who said their income was falling behind the cost of living had already increased by 10 percentage points.

This discrepancy reflects two things. One is that wage rates are only part of the earned income story, with the other being hours worked. As the pandemic spread, many workers exited the workforce to stay at home and take care of young or old family members or themselves. Many others worked fewer hours as stores or factories shut down or operated at lower capacity, resulting in reduced incomes for many. The second reason for the disparity is that while Exhibit 3 contains data for all workers represented in the Atlanta Fed's Wage Tracker and all goods and services represented in the overall CPI, these average metrics don't necessarily reflect the experiences of middle-income households.

**Exhibit 4: "Overall, would you say your income is..."**

Share of respondents in Primerica Financial Security Monitor™ Survey indicating whether their income is falling behind, staying even, or going up faster than the cost of living




Source: AC Cutts & Associates LLC, U.S. Bureau of Economic Analysis, U.S. Bureau of Labor Statistics, Federal Reserve Bank of St. Louis (FRED).
2023 data through September.

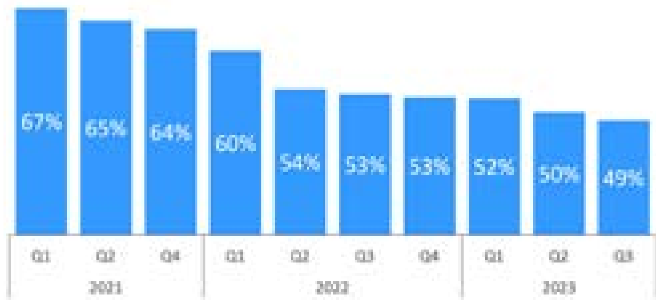
As inflation peaked in mid-2022, the percentage of respondents in the survey who indicated that their incomes were falling behind the cost of living also peaked at 78%. Since then, the share has fallen, but only by about two percentage points even though the economy has markedly improved. That begs the question: Why haven't middle-income households felt an improvement in their financial situation now that inflation has moderated to levels well below income growth?

The answer is that the compounding effect of inflation's impact has left a deep mark on household finances. When respondents to the survey were asked to rate the condition of their personal finances, the share who chose "excellent" or "good" fell steadily from around 67% in the beginning of 2021 to below 50% in the third quarter of 2023 [Exhibit 5]. When asked about the economic health of their communities, the share indicating "excellent" or "good" went from a range of 43% to 48% in 2021 to a range of 38% to 42% in 2023 [Exhibit 6]. Lastly, when asked about their ability to save for the future, about 40% of respondents provided "excellent" or "good" rating in Q1 2021 before this share steadily fell to a low of 24% in Q4 2022. Since then, the share has increased slightly to about 27% [Exhibit 7].

Why haven't middle-income households felt an improvement in their financial situation now that inflation has moderated to levels well below income growth?

**Exhibit 5: How would you rate the condition of your personal finances?**

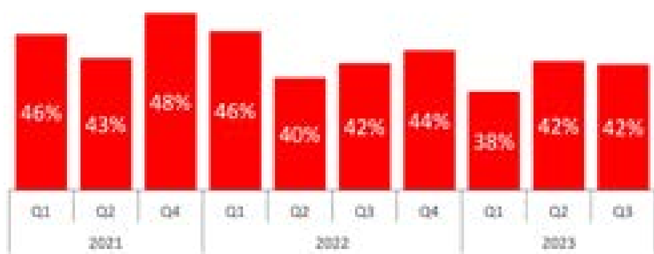
Share of respondents in Primerica Financial Security Monitor™ Survey respondents indicating "Excellent" or "Good"




Source: Primerica Financial Security Monitor™ Survey Q3 2023.

**Exhibit 6: How would you rate the condition of the economic health of your community?**

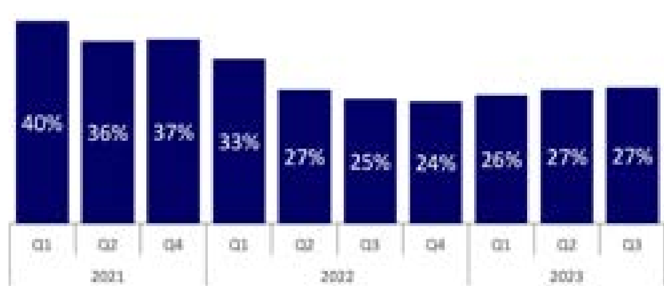
Share of respondents in Primerica Financial Security Monitor™ Survey respondents indicating "Excellent" or "Good"




Source: Primerica Financial Security Monitor™ Survey Q3 2023.

**Exhibit 7: How would you rate your ability to save for the future?**

Share of respondents in Primerica Financial Security Monitor™ Survey respondents indicating "Excellent" or "Good"




Source: Primerica Financial Security Monitor™ Survey.

# Not All Inflation Is the Same

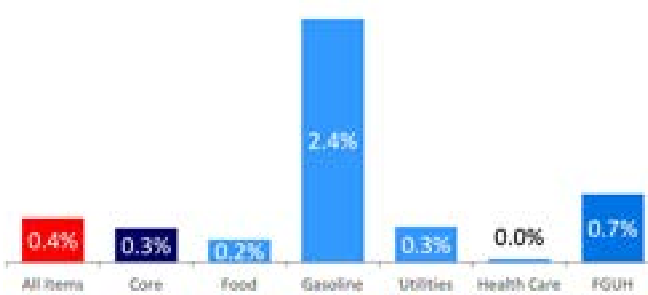
Metrics like the CPI follow the prices of a basket of goods and services over time to measure inflation. The U.S. Bureau of Labor Statistics analysts create the index by weighing the prices in that basket based on a survey of consumers about the quantities of the items they buy. However, the published CPI does not offer a clear picture of how price changes impact middle-income households. The budget of these particular consumers is disproportionately made up of necessities like food, gasoline, utilities and health care. When the prices of these goods change rapidly, families have few ways to adjust. Moreover, because these items are purchased frequently, changes in prices can have an outsized impact on both perception and reality.

Primerica created the monthly Household Budget Index™(HBI™) to fill the need for a reliable and consistent measure to track the purchasing power of middle-income families with incomes between $30,000 to $130,000. Understanding middle-income families' purchasing power is important because it directly impacts their ability to become or remain financially secure particularly when the cost of necessity items is volatile. The HBI™ measures the changes in inflation-adjusted earned income for middle-income households, with January 2019 as the reference baseline and a middle-income weighted measure of inflation in the costs of necessity items. As of October 2023, middle-income households were still worse off than they were in January 2019, but were making up ground at a quick pace [Exhibit 8]. However, the loss from the rise in the cost of food, gas, utilities and health care since May 2021 has left an average cumulative deficit of $2,440 in family budgets. Rebuilding depleted savings and paying off debt incurred as a result of inflation is likely to take several more months and potentially even several years for many middle-income families.

**Exhibit 8: Primerica Household Budget Index™**
January 2019 = 100%, NSA

Source: Primerica Household Budget Index™, October 2023.

**Exhibit 9: Average monthly percent change in consumer prices reweighted for middle income households between June and September 2023,** NSA




Source: AC Cutts & Associates LLC, U.S. Bureau of Labor Statistics, Macrobond Financial. Data are not seasonally adjusted. Rates are not annualized.

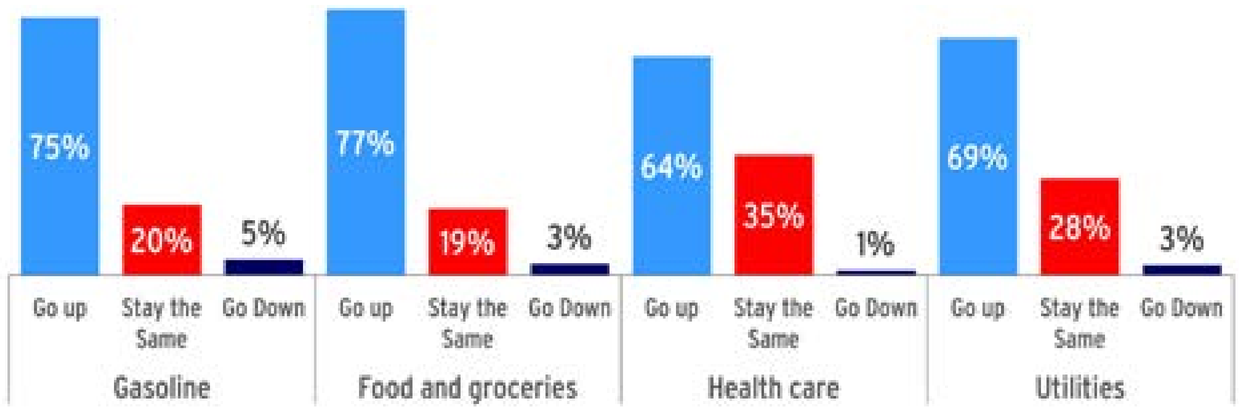
Alongside this, in the three months leading up to September 2023, the CPI for all items reweighted to reflect middle-income household purchasing patterns rose 0.4%, or about 5.2%

on an annualized basis [Exhibit 9]. The middle-income weighted core items CPI, which removes volatile food and energy prices, went up a little less, at 0.3% but the middle-income weighted CPI for combined food, gas, utilities and health care items, which is used in the calculation of the HBI™, rose by more than double that at 0.7% (8.2% annualized) led by a sharp increase in the price of gasoline of 2.4% per month (32% annualized). When prices of necessity items rise this swiftly, middle-income households are left with few options to cover the cost. As a result, many turn to credit cards and carry balances they hope will be temporary, stop adding to savings accounts or, worse, take money out of savings to cover the additional costs.

## Consumer Forecasts

In the Q3 2023 Primerica FSM™ survey, respondents were asked whether they thought the prices of necessities would rise in the next few months. Overwhelmingly, respondents indicated that they thought prices of food, gas, utilities and health care would all increase [Exhibit 10]. Overall, 75% of respondents thought gas prices would go up, 77% thought food and grocery costs would climb, and 64% of respondents believed health care costs would rise.

Exhibit 10: Over the next few months, do you expect your cost for the following to go up, go down, or stay about the same?




Source: AC Cutts & Associates LLC, Primerica Financial Security Monitor™ Survey Q3 2023.

As it turns out, respondents were overly pessimistic about energy costs, at least in the near term. In October, a month after the fielding of the Q3 2023 survey, the average price of gasoline fell by 5.3% and the cost of utilities fell by 0.8%. But survey respondents were right about food and health care costs, which both rose at a higher pace than in the months leading up to the Q3 survey.

In every survey, respondents are asked what financial activities they completed over past year and what they intend to do over the next few months. A consistent pattern has emerged showing what middle-income Americans say they plan to do and what they do are vastly different. This is true for both positive behaviors, such as adding to a savings or investment account, and negative ones such as missing debt payments or spending more overall.

Since the survey began in 2020, there has been an almost 25-percentage-point gap between respondents' plans to increase their credit card usage and the share of those who did charge more to their card [Exhibit 11]. For example, in the Q2 2023 survey, only 3% of respondents thought they would increase credit card usage. However, by the Q3 2023 survey, about 37% stated that they had done so in the past year.

Similarly, the survey has recorded a significant mismatch averaging about 23 percentage points in those who thought they would need to dip into personal or retirement savings and those who did take that action. For example, in the Q2 2023 survey, about 5% of respondents thought they would spend some of their personal or retirement savings in the months ahead, while 34% indicated that they had already needed to tap this resource.

On a more positive note, nearly 9% of respondents in Q2 2023 planned to add to their savings account and over 26% ended up doing so, with the average difference between savings intentions and actions being a net positive of 15% over the survey' history. Part of this may be driven by the mismatch in those expecting to spend less or to create and follow a budget and those that end up doing so — on average, consumers are about 7% more likely spend less than planned and 8% more likely to set up and follow a budget.

**Exhibit 11: Which activities do you expect to do in the next few months and which activities did you do over the past year?**

| Activity | Q2'23 FSM™ expectation next few months | Q3'23 FSM™ actual activities over the past year | Avg Gap All FSM™ Surveys |
|---|---|---|---|
| Add to a savings account | 8.9% | 26.5% | 14.6% |
| Add to an investment account | 3.7% | 15.8% | 10.4% |
| Create and follow a budget | 12.2% | 22.4% | 7.8% |
| Increase usage of your credit cards | 2.8% | 36.6% | 24.8% |
| Miss a mortgage, rent, car, or other debt payment | 2.8% | 17.6% | 14.4% |
| Purchase life insurance | 2.1% | 5.0% | 3.5% |
| Seek advice from a financial professional | 4.7% | 12.8% | 5.7% |
| Spend less money overall | 18.1% | 43.3% | 6.6% |
| Spend more money overall | 10.2% | 34.4% | 13.5% |
| Spend personal or retirement savings | 4.7% | 33.7% | 23.0% |
| Take out a new loan | 2.9% | 18.2% | 12.9% |

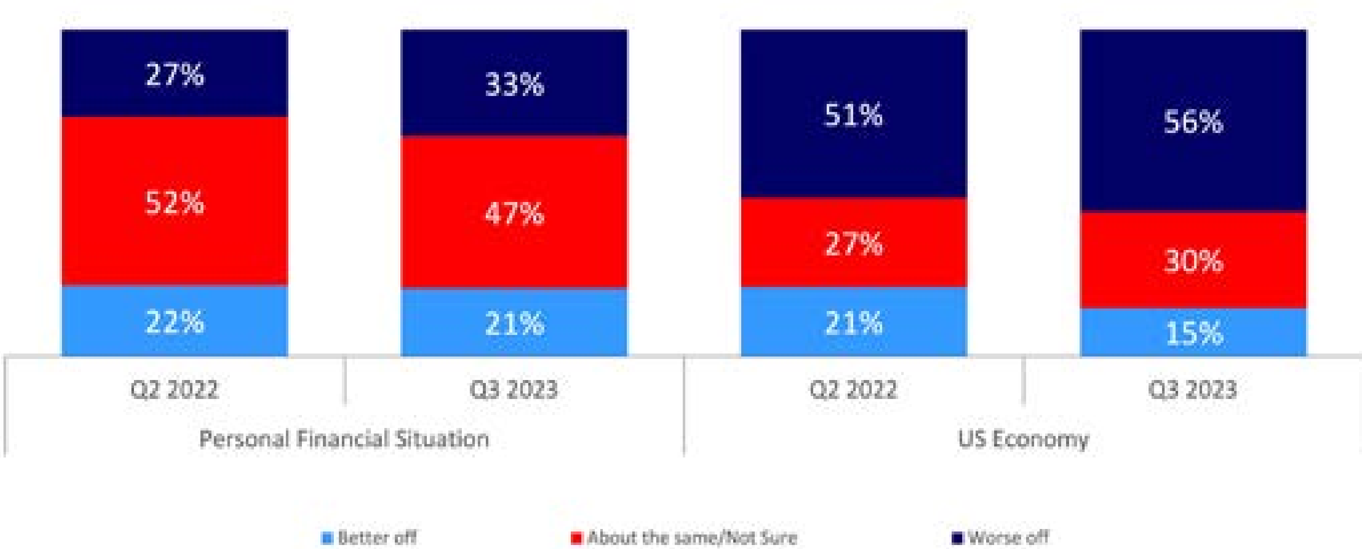
Source: Primerica Financial Security Monitor™ Survey Q3 2023.

When asked why respondents were unable to stick with their budget, most pointed to rising costs and unexpected events as the main reasons. In the Q3 2023 survey, 80% of respondents indicated that the rising cost of necessities like gasoline and groceries influenced their ability to stick to their budget. In addition, 32% cited unexpected car repairs, another 32% cited unexpected home repairs and 24% cited unexpected health problems. (Multiple answers could be selected.)

Given the sharp increase in the prices of necessities over the past two years, the burden of unexpected large expenses and the ensuing financial stress these have caused, it's no wonder that middle-income households' outlooks are increasingly cautious. When asked whether they thought their personal financial situation would be better off, about the same, or worse over the course of the next year, about 33% of respondents in the Q3 2023 survey indicated they thought they would be worse off [Exhibit 12]. A year earlier, about 27% of respondents thought they would be worse off. Similarly, when asked how they thought the U.S. economy would fare in the coming year, 56% in the Q3 2023 survey indicated they thought things would get worse, up from 51% of respondents a year earlier.

Professional forecasters aren't much more accurate than consumers. The Wall Street Journal Economic Forecasting Survey asks economists to predict the likelihood that the economy will enter a recession over the next 12 months. In the most recent survey in October, the consensus forecast puts a 48% probability of a recession occurring in the next year. A year ago, the group of economists pegged the likelihood of a recession at 63% due to the expectation that consumers would sharply curtail spending. But consumers defied expectations, and the likelihood of a recession seems distant, at least for now.

**Exhibit 12: In the next year, do you think your financial situation or the U.S. economy will be better off, the same, or worse off than it is now?**
Share of survey respondents, NSA




Source: Primerica Financial Security Monitor™ Survey Q3 2023.

# Conclusion

Looking ahead to 2024, inflation is surely waning, and wages appear to be rising steadily at a faster pace than prices. Should this continue to be the case, middle-income households should find themselves in a gradually improved financial condition. If incomes continue to grow faster than inflation as they did in 2023, especially ahead of inflation in frequently purchased necessity items, we should expect to see more respondents in future FSM™ surveys indicating that they were able to set and keep a budget or add to savings and investments, and fewer that indicate they have had to tap into savings or increase the use of their credit cards.

For middle-income households, spending is already constrained from the cumulative impacts of inflation. Thus, the enormous surge in aggregate consumer spending over the past three years came primarily from higher income households. Should they also start to worry about finances and cut back on spending before middle income households can recover, we might very well see the soft landing economists are hoping for, where we avoid a formal declaration of a recession, turn into a hard one.

# About the Author

Dr. Amy Crews Cutts is an internationally recognized thought leader and chief economist focused on providing strategic economic analysis rooted in practical business terms. Amy is the President and Chief Economist of AC Cutts & Associates LLC, an economic and policy consulting firm. She was previously Senior Vice President and Chief Economist for Equifax and Senior Director and Deputy Chief Economist at Freddie Mac before that. With over 25 years of economic analysis and policy development experience, Amy is a passionate advocate for building the financial security of families and expanding consumer and small business access to low-cost, nonpredatory credit. She is a noted expert in credit reporting, consumer and small business credit markets, loan servicing, securitization, residential real estate including home equity and price indices, and trends in employment and compensation. She is a regular panelist in the Wall Street Journal and Blue Chip Economic Indicators surveys of economists. She earned her PhD from the University of Virginia and is a Certified Business Economist®, a distinction of professional achievement from the National Association for Business Economics (NABE).