

ABOVE THE FRAY

How to Feel About Consumer Feelings

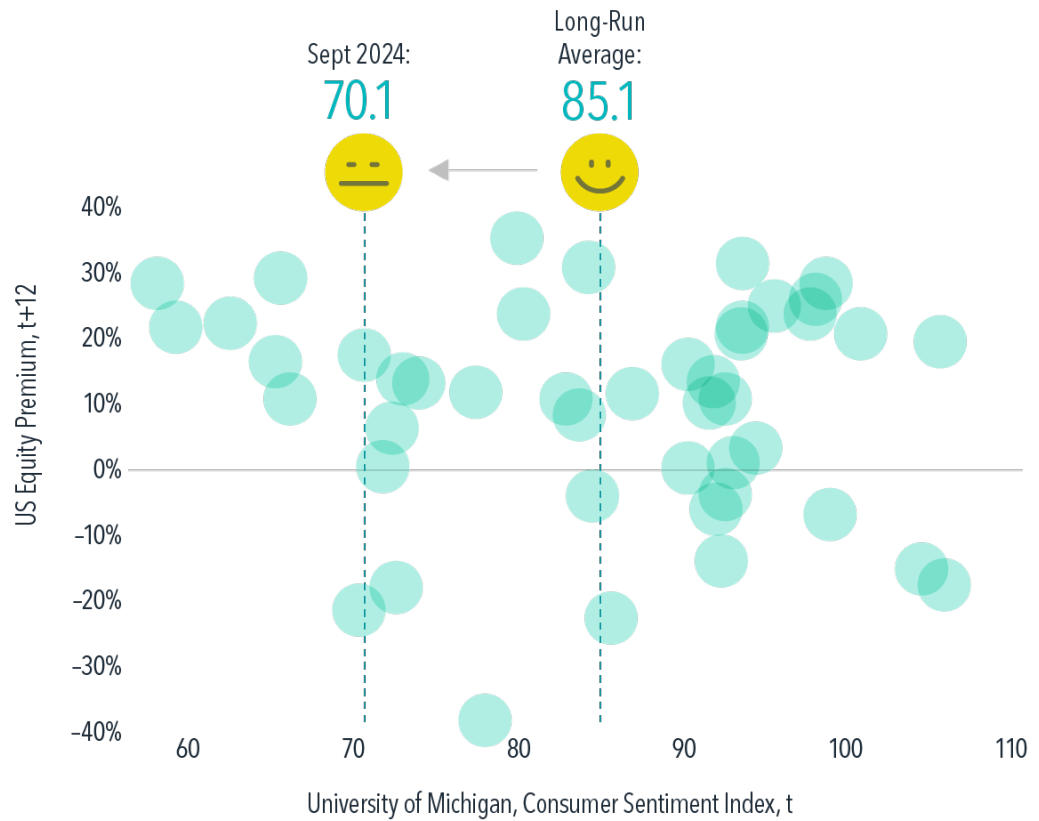
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Does your neighbor know where the economy is headed in the next 12 months? Since the 1960s, the University of Michigan has published the popular Consumer Sentiment Index, which asks everyday folk questions like: “Are you better off or worse off financially than you were a year ago?” or “Do you think that a year from now you will be better off financially, worse off financially, or just about the same as now?”¹ This index is sometimes viewed as a beacon of how investors feel about the direction of the economy.

As of September 30, 2024, the index sat at 70.1, pessimistic relative to its long-run average of 85.1.² Investors interpreting this as an ominous sign for markets may not have anything to fear though, as the data show this index has not been great at predicting future returns. Plotting the level of the Consumer Sentiment Index against subsequent 12-month stock market returns shows no discernible pattern, except that stocks tend to go up more often than they go down. Out of the 226 months where the sentiment index was below the long-run average, the average equity premium over the next year was 10.6%.

If your neighbor is feeling sour, that doesn't necessarily mean you should be changing your outlook or your investment portfolio. Markets tend to price in the latest views on the economy, including consumer optimism.

Exhibit 1**Next 12-Month US
Equity Premium
Against University of
Michigan Consumer
Sentiment Index**December 1978–December
2023**Past performance is not a guarantee of future results.**

In USD. Source: "Surveys of Consumers," University of Michigan, University of Michigan: Consumer Sentiment ©, retrieved from FRED, Federal Reserve Bank of St. Louis, October 28, 2024. US Equity Premium represented by returns to the Fama/French Total US Market Research Index minus the returns to one-month US Treasury bills. Data provided by Fama/French. Eugene Fama and Ken French are members of the Board of Directors of the general partner of, and provide consulting services to, Dimensional Fund Advisors LP. The Fama/French indices represent academic concepts that may be used in portfolio construction and are not available for direct investment or for use as a benchmark. See "Index Descriptions" for descriptions of Fama/French index data. Index returns are not representative of actual portfolios and do not reflect costs and fees associated with an actual investment.

This article originally appeared in Above the Fray, a weekly newsletter for Dimensional clients.

INDEX DESCRIPTIONS

Fama/French Total US Market Research Index: July 1926–present: Fama/French Total US Market Research Factor + One-Month US Treasury Bills. Source: [Ken French website](#).

Results shown during periods prior to each index's inception date do not represent actual returns of the respective index. Other periods selected may have different results, including losses. Backtested index performance is hypothetical and is provided for informational purposes only to indicate historical performance had the index been calculated over the relevant time periods. Backtested performance results assume the reinvestment of dividends and capital gains.

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2. Current index level as of September 30, 2024. The date range for the long-run monthly average is December 1978–December 2023.

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