

Trade War Weighed on Sentiments; Uncertainty Remains Elevated

UNITED STATES: The Conference Board's Leading Economic Index (LEI) declined 0.7% in March to 100.5 (2016=100) following a 0.2% dip in February (previously -0.3%). The decline was more than double PNC's forecast of -0.3% and points to slower growth in the near term. The drop was concentrated in three components: Average Consumer Expectations for Business Conditions (-0.26%), S&P 500 Stock Index (-0.25%) and ISM New Orders Index (-0.22%). The fourth successive monthly decline in the Conference Board's Leading Economic Index is consistent with PNC's outlook for slower economic growth in 2025. As a result, PNC's March baseline forecast calls for two 25 basis point cuts in the fed funds rate this year, lowering the fed funds rate to a range of 3.75%-4.00%. However, depending on the expected near-term inflation trajectory, those rate cuts could be pushed out to later this year.

Initial claims for unemployment insurance fell by 9,000 to 215,000 in the week ending April 12, the lowest level in the past eight weeks. The four-week moving average of initial claims, which irons out some of the weekly volatility, edged down by 2,500 to 221,000 for the week ending April 12, remaining near the lower end of a 213,000 to 238,000 range in the past six months. Continuing unemployment insurance claims jumped by 41,000 to 1.885 million in the week ending April 5, nearly reversing the 49,000 (revised) rise in the previous week. The four-week moving average of continuing claims edged up by 1,000 to 1.865 million. Both levels are close to 75,000 above the same period last year, suggesting it is taking unemployed workers somewhat longer to find a new job. The insured unemployment rate held steady at 1.2 percent in the week ending April 5, the same as a year ago. There is a growing but still small impact from the Department of Government Efficiency's layoffs of Federal government employees. Initial jobless claims filed by fired civilian Federal employees were 542 in the week ending April 5, up by 34 from the previous week. There were 7,192 continuing claims filed by fired civilian Federal employees in the week ending March 29, a decrease of 528 from the previous week. This is below the 14,000 decline of Federal government employees in February and March according to the BLS. We expect larger declines in April, May and June.

Total privately-owned U.S. housing starts plunged 11.4% in March to 1.324 million units at a seasonally adjusted annualized rate from a downwardly revised 1.494 million, more than erasing the 10.7% advance in the previous month. Single-family housing starts fell by more than 14%, while multifamily starts (apartment and condominium) were largely unchanged from the prior month. On a year-ago basis total housing starts were still up 1.9%, a notable improvement from the 3.4% decline in February. Total housing construction permits rose 1.2% on the month to 1.482 million units and were down 0.2% from March 2024. Single-family permits fell 2.0% while multifamily permits increased 10.1%. On a year-ago basis both single-family and multifamily permits were down marginally. PNC expects more fed funds rate easing this year, supporting a gradual recovery in housing affordability and housing demand, but risks remain with metals tariffs and possible increases on lumber tariffs.

Industrial production fell 0.3% in March from February, the first decline since November. The decline came from an almost 6% drop in utilities output, which is heavily tied to the weather. Manufacturing output rose a moderate 0.3% in March, with mining output up 0.6%. Output of motor vehicles and parts rose 1.8%, perhaps as automakers tried to boost output ahead of tariffs. On a year-ago basis total industrial production was up a modest 1.3% in March. Both overall and manufacturing output have been basically flat since 2022, after recovering to their pre-pandemic levels. But manufacturing output is still about 6% lower than it was before the Great Recession in 2007 to 2009, even as overall

Gus Faucher
Chief Economist

Stuart Hoffman
Senior Economic Advisor

Jay Hawkins
Senior Economist

Kurt Rankin
Senior Economist

Ershang Liang
Economist

industrial production is slightly higher. Higher interest rates have been a drag on the industrial sector, even as the overall economy has continued to expand. Industrial production is set to decline in the near term. Although tariffs may boost demand for some US-made goods, many domestic manufacturers will face higher prices for imported inputs. In addition, US manufacturers will raise prices to take advantage of tariffs; even though this may increase profits, the higher prices will weigh on demand and reduce volumes. Exporters will suffer from retaliatory actions by US trading partners; China cancelled orders for Boeing aircraft.

CANADA: CPI inflation came in weaker than the consensus expectation and slowed to 2.3% year-over-year in March from 2.5% in February. The slowdown in the headline inflation was broad-based except food, alcoholic beverages, and tobacco. Core inflation, total inflation excluding food and energy prices, fell sharply from 2.9% in February to 2.4% in March on a year-ago basis.

The Canadian economy finished 2024 on solid ground, with real GDP in Q4 expanding 2.6% at a seasonally adjusted annualized rate. With an escalation in the trade war between the US and Canada, the Bank of Canada pointed to rising uncertainty around growth prospects and inflation and kept the overnight target rate unchanged at 2.75% on April 16, a month after a 25-bps cut from 3%. In the quarterly Monetary Policy Report published along with the central bank's decision on interest rates, both proposed scenarios point to a slower domestic economic growth in Canada (scenario 2 shows the Canadian economy falls into a temporary recession before growing in early 2026). In scenario 1, according to this policy report, most tariffs are negotiated away under assumption, and inflation is expected to slow below 2% for a year due to the drop in the consumer carbon tax, before returning to its 2% inflation target in Q2 2026. In scenario 2, persistent and potentially additional tariffs, could create severe drags on domestic and global economic growth, and inflation rises to above 3% in mid-2026. In both scenarios exports are expected to fall and to create drags on economic growth, albeit in variant degrees depending on tariff assumptions. The BOC expects domestic demand to pull back with a buildup in precautionary savings in the current environment and under circumstances of higher unemployment rates, depending on the two scenarios. Compared to the January's Monetary Policy Report, year-over-year CPI inflation was revised up, and the average annual GDP growth was revised down, regardless of the two scenarios.

EUROZONE: Seasonally adjusted retail trade volume increased 0.3% in February according to Eurostat after being unchanged month-on-month for the past three months. With slowing inflation and the European Central Bank cutting major interest rates multiple times in 2024, the volume of retail sales marched noticeably higher in the third quarter, but lost momentum in the last quarter of 2024, indicating slower household consumption approaching the end of the year. On a year-over-year basis, retail sales grew 2.3% in February, up from 1.8% in January, 2.2% in December, and 1.8% in November.

On April 17, ECB President Christine Lagarde announced the Governing Council's decision to cut ECB's main policy rates by 25 bps as expected. The US tariff war continued to escalate since the beginning of April, to include a broader range of countries including the European Union and higher effective tariff rates from early 2025. With a great deal of uncertainty around decisions and impacts from President Trump's tariff measures, the flash consumer confidence indicator fell to -16.7, an 18-month low in April according to European Commission. The weaker consumer sentiment could translate into weaker household consumption in the near term, giving another reason, except for an on-track slowing inflation, for the ECB to further lower key interest rates in April after cutting twice in 2025 and four times in 2024. The year-over-year CPI inflation fell from 2.3% in February to 2.2% in March, moving down to the ECB's inflation objective of 2%. Slower wage growth this year should support inflation moving down to the ECB's objective, but uncertainty around tariffs and how trade fragmentation evolves create both downside and upside risks to inflation respectively.

UNITED KINGDOM: In contrast to Canada and the European Union, the UK has a trade deficit with the US, excluding itself from a list of President Trump's reciprocal tariff targets. However, the 25% tariff rate on autos that took effect on April 3 still applies to the UK, along with US's 10% baseline tariff rate effective on April 5. According to UK's Office for National Statistics (ONS), the US is the UK's largest trading partner, up to 17% of total UK trade in the four quarters ending Q3 2024, and the largest category of goods exports was machinery and transport equipment (autos). Exports will likely fall under tariffs on autos and the broad-based base tariff, creating drags to UK's real GDP growth this year (exports of goods and services were roughly 30% of UK's GDP in 2023 according to the World Bank). Proposed weaker overall global economic growth along with slower growth in the US under a permanent high tariff shock will likely create additional downside risks to UK exports, employment, and business investments in 2025. According to the ONS, the headline CPI inflation slowed to 2.6% in March from 2.8% in February. Both goods and services inflation slowed in March on a year-over-year basis, though services inflation remained much elevated above its pre-pandemic pace at 4.7%.

INDIA: The Reserve Bank of India cut its policy repo rate by 25 bps from 6.25% to 6.00% on April 9, after making the first interest rate cut since mid-2020 on February 6. India's CPI inflation continued to slow in early 2025 and came in weaker than the consensus expectation. Headline CPI inflation slowed to 3.3% in March from 3.6% in February according to the Central Statistics Office. Both months' inflation fell below the Reserve Bank of India's 4% inflation objective. Recent disinflation in topline CPI was driven by the food and beverage component, which fell to 2.9% in March, down from 3.8% in February and 5.7% in December. India's Composite PMI rose to a 7-month high in March 2025 according to S&P Global, to 59.5, driven by a noticeably faster expansion in factory activity. The Services PMI fell only slightly to 58.5 on the month, indicating a solid expansion in private business activity in March.

JAPAN: Japan's seasonally adjusted nominal merchandise trade surplus was short-lived and turned into a deficit in March 2025. According to the Ministry of Finance, nominal exports fell 3.8% and imports rose 0.6% on the month. On a year-over-year basis, exports rose 3.9%, and imports increased 2%. CPI inflation in Japan slowed to 3.6% year-over-year in March from 3.7% year-over-year in February, led by a retreat in food prices. Core inflation, headline inflation excluding volatile fresh food and energy components, increased from 2.6% in February to 2.9% in March on a year-over-year basis.

MEXICO: The Central Bank of Mexico cut the policy rate by 50 bps from 9.5% to 9.0% on March 27. The CPI increased 0.3% on the month and 3.8% over the past year in March 2025, according to Instituto Nacional de Estadística y Geografía (INEGI). The pace of inflation resides within the Banxico's inflation target range between 2% and 4%.

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