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GLOBAL ECONOMIC HIGHLIGHTS

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Stimulus Bill and Vaccine Rollout Boost the US Growth Outlook; UK in Double-Dip Recession as EU Trade Plunges

UNITED STATES: The Biden administration's huge $1.9 trillion dollar stimulus package became law on March 11, a big boost to the 2021 growth outlook. PNC upgraded its forecast for U.S. real GDP growth in 2021 to 5.2% in the February forecast from 3.4% in the January forecast, factoring in the impact of additional aid to most households, state and local governments, and the health system. The accelerating roll-out of vaccines is also extremely good news for the recovery: High-contact sectors of the economy will be able to return to normal later this year at the same time that stimulus is boosting household spending power. The faster the U.S. and world progress toward herd immunity, the better the outlook for the economy.

The overall consumer price index rose 0.4% in February from January, the largest one-month increase in prices since August 2020. Inflation in January was 0.3%. Energy prices rose 3.9% in February, pushing the overall index higher. A 6.4% increase in gasoline prices over the month accounted for one-half of overall inflation. Core inflation, excluding volatile food and energy prices, was a scant 0.1% in February; core prices have barely budged over the past few months. On a year-ago basis overall inflation was 1.7% in February, up from 1.6% in January. This was the highest inflation since February 2020, before the pandemic hit the U.S. economy. Core inflation slowed to 1.3% year-over-year from 1.4% in January, following inflation of 1.6% to 1.7% in the second half of 2020. Producer prices for final demand rose more in February, by 0.5%, with final goods prices up 1.4% and final services prices up 0.1%. Prices for core PPI (final demand less foods, energy, and trade services) rose 0.2%. From a year earlier, total PPI final demand rose 0.5%, while core PPI rose 2.2%. Although prices are rising for a limited number of goods experiencing strong demand and supply bottlenecks, such as building materials, overall inflation is tame, and core CPI inflation has slowed from the second half of last year. Businesses are finding it difficult to raise consumer prices given still-weak demand, lots of capacity, and limited wage pressures in many parts of the economy. Producer prices are rising faster, mostly due to differences in the CPI and PPI basket weights.

Both overall and core inflation will pick up on a year-ago basis over the next few months because of comparisons with 2020. Prices outright declined in the late winter and early spring of last year as the pandemic rocked the U.S. economy. But the acceleration in year-ago inflation will be transitory, and both overall and core CPI inflation will slow on a year-ago basis in the second half of 2021. Inflation will then pick up somewhat in 2022 as stimulus supports a strong economic rebound, giving businesses more pricing power.

Labor market data point to a faster jobs recovery in March. Initial claims for unemployment fell by 42,000 in the week ending March 6, to 712,000. Claims for the previous week were revised slightly higher, to 754,000 from 745,000. The four-week moving average of claims, which smooths out some of the volatility, fell by 34,000 to 759,000 in the week ending March 6. After averaging 825,000 per week between December and February, initial claims are starting to fall, but layoffs related to the pandemic remain extremely elevated. Nonfarm job openings, released at a lag to the monthly jobs report, rose to a new recovery-to-date high of 6.92 million in January from 6.75 million in December, but were still far below the 10.13 million unemployed Americans who actively looked for a job in January. Considering that there were another 3.58 million Americans who wanted a job in January but had not actively searched for one in the prior four weeks, and so were not officially considered "unemployed," there are nearly twice as many people out of work who want jobs as there are openings.

Long-term bond yields rose to the highest since the first half of February 2020 the week of March 8, in the lead-up to the Federal Reserve's March 17 monetary policy decision. The Federal Open Market Committee will likely upgrade its outlook for economic growth and inflation at the decision, but Chair Powell will probably continue to say that it is too soon to discuss when the Fed will taper its $120 billion in monthly asset purchases. In light of the latest stimulus package and encouraging vaccines news, PNC has brought forward our expectation for when the Federal Open Market Committee first raises the federal funds rate, their key short-term policy rate, to late 2023, from 2024 in our prior forecasts.

UNITED KINGDOM: Exports plunged 19.3% in January on a 40.7% collapse of exports to the EU; similarly, imports fell 21.6% with imports from the EU down 28.8%. It is too early to know how much of January's drop is temporary (businesses built up inventories in late 2020 to prepare for January's shipping delays) and how much will persist, but in the near term trade is a big drag on the British economy that is compounding the effect of the winter lockdown. The UK's monthly GDP index fell 2.9% on the month in January to 4.1% below its recovery-to-date high reached in October. This looks like as a double-dip recession, with employment and output down from October 2020 to February 2021 at least. Despite this, the Bank of England will almost certainly leave its monetary stance unchanged at its March 18 Monetary Policy Committee decision, since the rollout of vaccines will soon allow the UK's services sector to reopen and its recovery to resume.

EUROZONE: Matching PNC's forecast, the European Central Bank eased monetary policy by announcing "significantly higher" asset purchases under their Pandemic Emergency Purchase Programme (PEPP, or emergency quantitative easing) at their March 11 Governing Council decision. The ECB's guidance was ambiguous. They did not announce a specific target for purchases, and President Lagarde said in the press conference after the decision that the ECB is explicitly not aiming to hold long-term bond yields below a specific threshold (a.k.a. "yield curve control"). Instead, the faster bond purchases are intended to "prevent a tightening of financing conditions."

The ECB's lack of specificity reflects their ambivalence about preventing Eurozone long-term bond yields from rising as fundamentals improve. The euro reached the strongest since 2018 in early January, then depreciated modestly into March as U.S. long-term interest rates jumped—the ten-year Treasury yield rose 0.6 percentage points—and markets anticipated the ECB's easing decision made in March. But these conditions holding back euro appreciation could turn if the rise of U.S. interest rates slows, or the ECB's follow-through on its forward guidance underwhelms. If so, the euro's path of least resistance is likely to be modest appreciation against the dollar over the next few months.

Industrial production rose 0.8% in January from December in seasonally-adjusted terms, and was up 0.1% from a year earlier—the first year-over-year increase since late 2018.

CHINA: China's CPI fell 0.2% from a year earlier in February, after a 0.3% decline in January. Chinese consumer prices surged in early 2020 as the pandemic disrupted supply chains and distorted consumer preferences, then slowed over the course of 2020 as manufacturers replenished supply chains, global energy prices fell, and the yuan appreciated and made imported products cheaper in yuan-denominated terms. The modest year-over-year decline of consumer prices in early 2021 reflects the end of the temporary inflationary impact of the pandemic. This is a preview of what is in store for the United States as the economy reopens further and consumers redirect spending away from goods and back toward high-contact services like hospitality and tourism, where capacity utilization is currently very low.

Credit growth was faster than in the pre-crisis period in February but slower than the second half of 2020. Aggregate financing provided to the real economy (the government, household, and nonfinancial business sectors) rose 13.3% from a year earlier in February. Its growth peaked at 13.7% was in October 2020, the fastest since 2015; prior to the pandemic, it had been growing at a 10-11% annual rate. China has loosened monetary policy to aid its economic recovery, but by less than the United States; China's stimulus policy has focused on controlling the pandemic so that the market economy can return to normal and on fiscal stimulus.

JAPAN: The Bank of Japan will almost certainly hold its monetary policy stance unchanged at its next monetary policy announcement, which will be released the night of March 18 in U.S. time zones. The yen has depreciated 6.1% against the dollar since early January as U.S. inflation expectations and long-term interest rates rose while the corresponding Japanese ones were unchanged.

CANADA: As expected, the Bank of Canada maintained its target for the overnight rate at the effective lower bound of 0.25%. The BOC maintained its forward guidance and continues to carry out its quantitative easing (QE) program which buys at least $4 billion in government bonds per week. Central bankers acknowledged that economic prospects have improved but reiterated their commitment to maintain the current monetary policy stance in order to keep interest rates low across the yield curve until the increase in economic slack caused by the pandemic is reversed; the BOC doesn't expect to lift interest rates until 2023.

Canada added a huge 259,200 jobs in February, well above the consensus forecast for a net increase of 75,000, and reversing the prior two months' job losses. Recent swings in Canadian employment have been enormous; before the crisis, a normal good month saw around 15,000 jobs added. The unemployment rate dropped to 8.2% in February, the lowest since the beginning of the pandemic, from 9.4% in the prior month. 98.7% of February's jobs added were in the service sector, and 66.0% of jobs gained were part-time. Canada's economy has recovered 83% of the 2.9 million jobs lost in March and April; employment as measured by the household survey is still 599,000 (3.1%) below the pre-pandemic level.

INDIA: CPI inflation accelerated 5.0% in year-over-year terms in February, up from 4.1% in January but still within the Reserve Bank of India's 2% to 6% target range. Industrial production fell 1.6% in January from a year earlier, worse than consensus expectations for a 1.0% gain, and following a 1.0% rise in December. After plunging 57.3% in April in year-over-year terms, industrial production has increased in those terms in three of the past five months and is currently above the February 2020 pre-pandemic level.

BRAZIL: Consumer prices as measured by Brazil's IPCA index increased 0.9% in February from the prior month, following a 0.3% increase in January. Prices increased 5.2% in February from a year earlier, above consensus expectations for an increase of 5.0% and the highest since 2017. Retail sales fell 0.2% in January from December, the third straight monthly decline, following a downwardly revised 6.2% drop in December. With rising commodity prices, above-target inflation and a crumbling exchange rate, PNC Economics expects the Central Bank of Brazil (BCB) to raise the Selic rate by half a percentage point to 2.5% from 2.0% when central bankers meet on Wednesday March 17. Financial markets are pricing a 2.5 percentage point increase in the Selic rate by September, while the BCB's survey of professional forecasters conducted in the week of March 5th showed the median estimate for the Selic rate at year-end 2021 is 4.0%.

MEXICO: Industrial production rose 0.2% in January from December, with mining output up 0.2% and construction up 1.5%, while utilities output fell 1.7% and manufacturing 0.5%. The semiconductor shortage holding back auto manufacturing in the United States is likewise a drag on the Mexican auto industry; the Texas power outages in February likely caused manufacturing output to fall in that month too. From a year earlier industrial production fell 3.7% in January, with mining down 3.5%, utilities down 4.8%, construction down 10.5%, and manufacturing down 1.0%. Mexico's recovery continues, but at a very modest pace, held back by tight monetary and fiscal policies and by energy policies that favor state-owned enterprises at the expense of economic growth.

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