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GLOBAL ECONOMIC HIGHLIGHTS

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Powell Tees Up Fed to Begin Tapering the QE Program by Year-End; Global PMIs Turned Lower in August

UNITED STATES: Chair Powell provided negligible new information about the outlook for monetary policy in his long-awaited speech August 27 at the Kansas City Fed's annual Jackson Hole monetary policy conference, held virtually this year. The key phrase on monetary policy was, "At the FOMC's recent July meeting, I was of the view, as were most participants, that if the economy evolved broadly as anticipated, *it could be appropriate to start reducing the pace of asset purchases this year* [emphasis added]." The minutes of the Fed's July Open Market Committee meeting released August 18 already made clear that most participants shared that view. It was essentially a given that Chair Powell was part of that majority.

The speech was most noteworthy for what it did not contain— Chair Powell has not changed his assessment of the surge in inflation in the first half of 2021. He holds steadfast to the view that it is mostly transitory, which is to say, caused by one-off factors and so unlikely to cause much higher trend inflation over time. Powell described in depth how demand for durable goods surged as Americans hunkered down during the pandemic and spent their stimulus dollars; supply chains went haywire due to restrictions on travel and activity, quarantine measures, labor shortages, and unprecedented durable goods demand; and prices rose as a result.

The Fed is closely monitoring the prices of the "relatively narrow group of goods and services" that fueled the historic surge in inflation in the first half of 2021, and also is watching many other alternative measures of inflation's intensity and breadth in the U.S. economy. But Chair Powell is unpersuaded that the spike in inflation in the first half of 2021 provides much information about the course of inflation down the road, and in fact expects prices of that "relatively narrow group" to "soon" push inflation down.

Chair Powell closed his speech with a reiteration of the Fed's maximum employment goal: "Before the pandemic, we all saw the extraordinary benefits that a strong labor market can deliver to our society. Despite today's challenges, the economy is on a path to just such a labor market, with high levels of employment and participation, broadly shared wage gains, and inflation running close to our price stability goal." In 2022, if durable goods inflation slows as the Fed (and PNC's economists) forecast, Chair Powell will ambitiously target labor market conditions that are as tight *or even tighter* than those that prevailed before the pandemic struck.

The Markit manufacturing PMI for the U.S. pulled back to 61.2 in August from 63.4 in July; output growth was the slowest since March, and employment growth was the slowest since December 2020. The services PMI fell to 55.2 from 59.9; survey respondents cited labor shortages, Delta, and supply chain issues as drags on activity during the month. This retrenchment of growth looks to be a global phenomenon, since the flash estimates of PMIs for the other economies for which Markit publishes advance releases—the Eurozone, Japan, and the United Kingdom—also turned lower on the month.

EUROZONE: The Markit manufacturing PMI for the Eurozone dipped to 61.5 in the August flash estimate from 62.8 in July, and the services PMI was a hair lower at 59.7 after 59.8. The manufacturing PMI was the lowest in six months; manufacturers blamed supply chain difficulties for slower growth in the month.

The Account (a.k.a. minutes) of the ECB Governing Council's July 21 to 22 meeting showed a "few" of the 25 members—19 national central bank governors plus six Executive Board members—dissented with the decision to strengthen the Bank's forward guidance. Those overruled members preferred a more watered-down commitment to realizing the Bank's symmetric 2% inflation target. While the "large majority" of the 25 supported the revised guidance, there is some hesitancy among ECB members about the new policy, even though it commits the ECB to a dovish stance than the Fed's forward guidance does (and inflation is considerably lower in the euro area than in the U.S.).

JAPAN: The Jibun au Bank manufacturing PMI for Japan dipped to 52.4 in the August flash release from 53.0 in July, while the Japan services PMI fell sharply to 43.5 from 47.4. The services PMI was the weakest since May 2020, held back by the emergency restrictions passed in response to the Delta outbreak; Japan's coronavirus cases have reached the highest since the pandemic began in August. In the manufacturing survey, purchasing managers blamed the month's slowdown on the same supply chain disruptions that held back manufacturing in the U.S., Eurozone, and UK.

UNITED KINGDOM: The Markit/CIPS flash manufacturing PMI for the UK pulled back to 60.1 in the August flash estimate from 60.4 in July, and the services PMI fell to a six-month low of 55.5 from 59.6. British businesses are reporting labor shortages but for slightly different reasons than their American counterparts—the U.K.'s contact tracing system caused large numbers of Britons to self-isolate and miss work during the Delta outbreak, causing a labor shortage that the British press nicknamed a "pingdemic." While the specifics are changing, the big picture remains that the pandemic continues to set the pace of the economic recovery.

CANADA: PNC forecasts for Canada's real GDP to have increased 0.5% in June from May at Statistics Canada's next release on August 31. Economic output declined in April and May as Canada faced lockdowns, and the economy likely rebounded as restrictions were lifted.

MEXICO: Mexico's recovery continues to advance in fits and starts. Real GDP rose an unrevised 1.5% in the second quarter (not annualized) by the second estimate from Mexico's statistical agency. Monthly GDP fell 0.9% in June after a 0.6% increase in May, with agricultural output down 4.4% after a 7.9% surge in June, industrial output down 0.5%, and services output down 0.7%. Real GDP likely returned to growth in July judging from the month's jobs report: The labor force participation rate rose to a seasonally-adjusted 59.6% from 58.3% in June and reached a new recovery-to-date high. The unemployment rate edged up to 4.1% from 4.0% with more workers entering the labor market and actively searching for work.

BRAZIL: Brazil's economy added 316,580 jobs in July from June, better than expectations for a 300,000 gain. July marked Brazil's seventh straight month of net job gains. The IPCA-15 index rose 9.3% in the twelve months to mid-August, the highest reading since 2016. Inflation as measured by the IPCA-15 index has increased in every month this year and is well above the 5.25% upper threshold of the central bank's target range. PNC forecasts for Brazil's real GDP to marginally increase 0.2% in the second quarter, on a quarter-over-quarter basis, as the economy faced lockdowns in many big cities.

INDIA: PNC forecasts for India's economy to have grown 15.0% in the second quarter of 2021 (the first quarter of the 2022 fiscal year) from a year earlier when the GDP report is released by the Central Statistics Office on August 31. The economy is recovering rapidly due to a comparison against a very weak period in 2020 and rising exports. India's exports are around 5% above the pre-pandemic level thanks to a recovering global economy and should continue to support economic growth into 2022.