Global Central Banks Double Down on Taming Inflation; PNC Revises Fed September Forecast to 75bps from 50bps

**EUROZONE:** The Governing Council of the European Central Bank (ECB) raised its three key policy rates by 75 basis points when central bankers met on September 8. With the ECB’s decision, the interest rates on main refinancing operations, the marginal lending facility and the deposit facility will be increased to 1.25%, 1.5%, and 0.75% respectively, with effect from September 14. Despite weak growth prospects in the Euro area, the ECB maintained its hawkish stance and signaled further interest-rate hikes in the near term. In the accompanying press release, the Governing Council stated that it expects to “raise interest rates further to dampen demand and guard against the risk of a persistent upward shift in inflation expectations.” The increase in policy rates on September 8 followed a 50-basis point increase on July 21.

With annual inflation at 9.1% in August, an energy crisis, deteriorating conditions in the manufacturing sectors in France and Germany, and a weakening global economy, the ECB’s outsized hike could imply that it will have a shorter hiking cycle, with interest rates staying higher for longer.

The ECB also upwardly revised its inflation projections. It now expects annual inflation to average 8.1% in 2022, 5.5% in 2023 and 2.3% in 2024, up from 3.3% in 2022, 2.8% in 2023 and 2.3% in 2024 in its June forecast. PNC Economics expects the ECB to raise its policy rates further by 50 basis points on October 27 and 25 basis points on December 15, taking the interest rates on main refinancing operations, the marginal lending facility, and the deposit facility to 2.0%, 2.25% and 1.5% respectively.

PNC Economics forecasts for the euro to depreciate against the dollar into 2023, given expected aggressive Fed hikes in the near term, and better economic prospects in the U.S.

**CANADA:** Matching PNC’s forecast, the Bank of Canada (BOC) raised the target for its overnight rate by 75 basis points to 3.25% from 2.5%, when central bankers met on September 7. In the accompanying statement, the BOC signaled further interest-rate hikes as central bankers try to moderate growth and tame inflation. Economic conditions remain strong in Canada even with elevated inflation. Headline CPI inflation eased in July to 7.6% from 8.1% in June. However, the BOC’s core measures of inflation moved up in July, ranging from 5% to 5.5%. GDP grew 3.3% on an annualized basis in the second quarter of 2022 as consumption and business investment grew 9.7% and 12.0% respectively.

PNC Economics forecasts a hike of 50 basis points when the BOC meets on October 26 and 25 basis points on December 7.

**UNITED STATES:** With Fed officials striking a more hawkish tone in recent public appearances, the Wall Street Journal reporting that the FOMC “appears to be on a path to raise interest rates by another 0.75 percentage point this month,” and major central banks aggressively raising interest rates this week, PNC Economics now expects the Fed to raise the fed funds rate by 75 basis points (versus 50 basis points previously) at its meeting on September 21. PNC Economics then expects further increases in the fed funds rate through the rest of this year, to a range of 3.5% to 3.75% at the end of 2022. The fed funds rate is expected to peak between 3.75% and 4.0% in early 2023.
According to the latest Beige Book, “economic activity was unchanged, on balance,” from early July to late August. There was modest growth in the Boston, Atlanta, Kansas City, Dallas, and San Francisco districts, and modest contraction in the New York, Richmond, Chicago, St. Louis, and Minneapolis districts. The economy was flat in the Philadelphia and Cleveland districts. Consumer spending was steady, with households trading down to lower-quality goods and services, and shifting toward essentials and away from discretionary goods. Labor markets remained tight, although labor availability increased somewhat, particularly in manufacturing, construction, and financial services. Wages increased across all districts, but the pace of growth slowed.

Although inflation remained high, nine districts reported a slowing in inflation in July and August. Price increases were largest for food, rent, utilities, and travel. Cost pressures, especially shipping rates fell with lower energy prices. Commodity prices fell in some districts.

The latest Beige Book provides anecdotal evidence that economic growth is slowing, and inflationary pressures are easing. Higher interest rates are weighing on the US economy, particularly on the housing market, but the economy continues to expand at a below-trend pace.

CHINA: Consumer price growth, as measured by the consumer price index (CPI), eased in August as China’s economy struggles with lockdowns, a real estate sector in crisis, and a weakening global economy. Headline CPI rose 2.5% in August from a year ago, down from 2.7% in July. On a month-over-month basis, prices fell 0.1% in August following a 0.5% increase in July. Core inflation (excluding food and energy prices) rose 0.8% in August from a year ago, unchanged from July. Annual core inflation has been below 1.4% for over a year.

Annual producer price inflation (PPI) eased in August to 2.3% from 4.2% in July. This was better than consensus expectations for 3.2%. The PPI fell 1.2% in August from July following a 1.3% decline in July.

U.S. dollar-denominated exports grew 7.1% in August in year-over-year terms, undershooting the 13.0% consensus forecast, and following an 18.0% increase in July. Imports grew 0.3% in August, the slowest pace since April, following a 2.3% increase in July. Exports will remain a headwind to China’s growth in the near term as the global economy weakens and global demand shifts from goods to services.

UNITED KINGDOM: The S&P Global/CIPS composite PMI fell to a seventeen-month low 49.6 in August from 52.1 in July. The flash S&P Global/CIPS services PMI declined to 50.9 in August from 52.5 in July. PMI readings over 50 indicate growth while readings below 50 imply contraction.

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