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GLOBAL ECONOMIC HIGHLIGHTS

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BOC Considers a Pause in Tightening; Central Banks Meet in the U.S., U.K., Eurozone and Mexico

CANADA: Matching PNC's forecast, the Bank of Canada (BOC) raised the target for its overnight rate by 50 basis points to 4.25% from 3.75%, when central bankers met on December 7. The BOC also announced the continuation of its quantitative tightening policy. In the accompanying statement, the BOC opened the door to a pause in its hiking cycle. The statement noted that "the Governing Council will be considering whether the policy interest rate needs to rise further to bring supply and demand back into balance and return inflation to target." With the BOC's latest move, the policy rate has risen by a full four percentage points in 2022. Canada's CPI inflation registered at 6.9% in October, unchanged from September, but well above the central bank's 2% inflation target. Economic growth remains strong, and the labor market is very tight with the unemployment rate near the all-time low. Real GDP grew stronger than expected in the third quarter mostly driven by trade and business investment in inventories. PNC Economics expects the Bank of Canada to raise its target rate by 25 basis point to 4.5% when policymakers meet on January 25.

The value of building permits fell 1.4% in October from the prior month as activity in the housing sector remained subdued. Building permits were down 6.3% in October on a year-over-year basis.

UNITED STATES: The ISM nonmanufacturing composite index rose to 56.5 in November from 54.5 in October. The ISM nonmanufacturing index is a diffusion index that measures net activity among nonmanufacturing (services) industry companies; a reading above 50 implies that the service sector is in an expansion phase while a reading below 50 indicates contraction. The details of the report were good. The business activity index rose sharply in November to 64.7 from 55.7 in October. The employment index bounced back above the breakeven threshold of 50, registering at 51.5, up from 49.1 in October. Private service-providing employment has recovered fully from the Viral Recession but leisure and hospitality employment remains below the pre-pandemic level by more than 5%. The new orders index fell for the fourth straight month in November, but it remains above the neutral threshold of 50. In contrast to the services sector, the ISM manufacturing composite index fell in November to 49 from 50.2 in October.

The U.S. trade deficit widened in October to \$78.2 billion from \$73.3 billion in September, according to the U.S. Census Bureau. Exports fell 0.7% while imports rose 0.6%. Foreign demand for U.S. exports remains soft due to a weaker global economy as many countries are faced with higher interest rates and elevated inflation. Also, the U.S. dollar's strength against other currencies this year has reduced the appeal of U.S. exports to foreigners. PNC Economics expects trade to be a weight on economic growth through 2022, and in 2023.

The producer price index (PPI) for final demand increased 0.3% in November from October, slightly more than the consensus expectation for an increase of 0.2%. The PPI for final demand goods was up 0.1% in November from the prior month while the PPI for final demand services increased 0.4%. Yearly PPI inflation decelerated to 7.4% in November from 8.1% in October, and down from the peak pace of 11.7% in March 2022. On a year-over-year basis, the PPI for final demand goods increased 9.6% while the PPI for final demand services rose 5.9%. Overall, inflation should moderate further as interest rates increase and supply chains improve. The Federal Open Market Committee raised the funds rate by 75 basis points at four consecutive meetings through early November taking it from close to zero at the beginning of 2022 to a range of 3.75% to 4.00%. PNC expects a 50-basis point increase in the fed funds rate at the FOMC'S meeting this week, to a range of

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4.25% to 4.5%. PNC then expects another couple of rate hikes in early 2023, bringing the fed funds rate to 4.75% to 5.00% by the spring.

The FOMC hopes to raise the fed funds rate by enough to cool off growth and bring down inflation, but not by too much, which could cause a recession. But given the rapid increase in the fed funds rate in 2022, still-high inflation and job growth that remains well above the economy's long-run potential, further fed funds rate hikes make a recession likely next year. In particular the yield curve has inverted, with the yield on a 3-month Treasury bill above that on a 10-year Treasury note. This inversion, which has been a very reliable recession indicator, is expected to deepen and persist in the near term as the FOMC continues to increase the fed funds rate into 2023.

PNC Economics forecasts for the November Consumer Price Index report, to be released December 13, to show consumer prices up 0.4% from October; core CPI excluding food and energy likely rose 0.4% in November. On a year-over-year basis, headline CPI likely declined to 7.3% in November from 7.7% in October, driven by lower used car and energy prices. Core CPI likely decelerated to 6.2% in November from 6.3% in October.

EUROZONE: Real GDP growth in the third quarter was stronger than previously estimated, according to data from the European statistics agency Eurostat. Real GDP growth was revised up to 1.3% on an annualized basis in the final estimate from 0.8% in the preliminary estimate. The details of the final estimate were favorable as domestic demand (final consumption expenditure and gross capital formation) grew 6.1%; the strongest pace since the third quarter of 2021. Household spending added 0.5 percentage points and gross fixed capital formation added 0.8 percentage points to growth. Net exports of goods and services subtracted 1.1 percentage points from growth.

Despite the expansion of economic output in the third quarter, the euro area economy will likely tip into a mild recession at the start of 2023 due to higher interest rates, elevated inflation, and a weak global economy.

PNC Economics expects the European Central Bank's Governing Council to raise its three key policy rates by 50 basis points when central bankers meet on December 15. PNC then expects 25-basis point hikes at each of the ECB's four monetary-policy meetings in the first half of 2023 (February 3, March 10, April 14, and June 9).

UNITED KINGDOM: Real GDP grew 0.5% in October from the prior month, slightly stronger than the consensus expectation for 0.4% and following a 0.6% decline in September. The services sector led the way. Economic output in consumer-facing industries grew 1.2% in October following a decline of 1.7% in September. On a quarterly basis, GDP contracted 0.3% in the three months through October compared to the prior three-month period (July, August, and September). With the expansion in October, real GDP is 0.4% above the pre-pandemic level.

Industrial output in October was unchanged from September. On a year-over-year basis, industrial output fell 2.4% in October following a 3.1% decline in September.

With inflation at an all-time high and well above the Bank of England's 2% target, PNC Economics expects the Bank of England to raise the Bank Rate by 50 basis points to 3.5% when policymakers meet on December 15. PNC then expects four 25 basis-point hikes in 2023. The U.K. economy is likely in recession. Real GDP contracted in the third quarter, composite PMI data have registered below 50 for four straight months and consumer sentiment is near the all-time low.

MEXICO: Inflation as measured by the consumer price index (CPI) rose 7.8% in November from a year ago, down from 8.4% in October. On a month-over-month basis, CPI inflation was unchanged at 0.6%. Core CPI inflation (excluding food and energy) accelerated to 8.5% in November from 8.4% in October.



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Industrial production rose 3.1% in October from a year ago following a downwardly-revised 3.8% increase in September. Industrial output increased in the mining, utilities and manufacturing industries while output fell in the construction industry.

With a moderation in inflation in recent months, PNC Economics expects the Bank of Mexico (Banxico) to raise its benchmark interbank rate 0.5 percentage point to 10.5% at the December 15 rate decision.

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