

China's Economy Beats Expectations in the First Quarter; U.K. Inflation Remains in Double Digits

CHINA: China's economy beat expectations in the first quarter of this year after the relaxation of strict COVID measures. Real GDP grew 4.5% in the first quarter from a year ago, beating consensus expectations of 4.0%, and up from 2.9% in the fourth quarter of 2022. Real GDP growth accelerated to a 2.2% quarterly rate in the first quarter, up from 0.6% in the prior quarter. Growth in the primary (agriculture) sector fell to 3.7% in the first quarter from 4.0% in the prior quarter, growth in the secondary (industrial) sector slowed to 3.3% from 3.4% and growth in the tertiary (services) sector jumped to 5.4% from 2.3%.

Nominal retail sales jumped 10.6% in March in year-over-year terms following a 3.5% increase in the first two months of the year, as the country reopened its borders and celebrated the Lunar New Year holiday.

Industrial production rose 3.9% in March on a year-over-year basis following a 2.4% increase in the first two months of the year.

The better-than-expected pace of growth in the first quarter keeps China's government on track to meet its GDP growth target of "around 5%" this year. China's economy should gain growth momentum in the second half of the year as the real estate sector stabilizes and the PBOC maintains monetary policy support.

UNITED STATES: U.S. housing starts fell 0.8% in March to 1.420 million annualized units from 1.432 million in February (revised lower from 1.450 million). This was better than consensus expectations for a 3.5% decline. Single-family starts rose 2.7% in March to 861,000 from 838,000 in February while multifamily starts fell 5.9% to 559,000 from 594,000. The number of residential construction permits, a leading economic indicator, fell 8.8% on the month. Single-family permits rose 4.1% while multifamily permits fell by a big 22.1%. The backlog of new construction reduced slightly in March but remains near the highest level since 1974. Building completions fell slightly in March but they are over 11% above the December 2022 level. Completions should increase through 2023 as labor shortages decline and supply-chain issues improve. Starts and permits fell in March after surprise increases in February. Starts and permits were up in the first quarter of 2023. In a separate report released last week, homebuilder confidence as measured by the NAHB Market Index rose for the fourth straight month in April although the index remains below the break-even measure of 50.

Sales of existing homes fell 2.4% in March to 4.44 million annualized units after a surprise increase in February, according to the National Association of Realtors. This means 4.44 million units would be sold in 2023 if sales were at the same pace as they were in March. Sales fell on the month in the Midwest, South and West while sales were flat in the Northeast. Sales were down on a year-over-year basis in each of the four major regions for the thirteenth straight month. The median existing-home price for all housing types fell 0.9% in March from the previous year to \$375,700. Economic activity will likely slow significantly this year as interest rates increase and financial conditions tighten further. PNC forecasts a recession in the second half of 2023 as the drag from higher interest rates weighs on economic activity, with further deterioration in the housing market.

According to the latest Federal Reserve Beige Book, the U.S. economy was flat in the six weeks through mid-April. Conditions were unchanged in five districts (Boston, New York, Cleveland, Chicago, and St. Louis), down slightly in three (Philadelphia, Richmond, and Kansas City), and up slightly in four (Atlanta, Minneapolis, Dallas, and San Francisco).

The Beige Book is consistent with a slowing in growth as the U.S. economy continues to respond to Federal Reserve tightening. Conditions were mixed nationally, with activity flat in some districts, up slightly in some, and down slightly in others. Higher interest rates are weighing on industries like housing and manufacturing. The Beige Book is consistent with PNC's forecast for a mild U.S. recession starting sometime in the second half of 2023 and lasting into the spring of 2024. The Beige Book also supports PNC's call for a 25-basis point increase in the fed funds rate when the Federal Open Market Committee meets on May 3, to a range of 5.00% to 5.25%, but then no further rate hikes through the rest of 2023.

Both consumer and business banking activity were weaker in early spring. Banks tightened credit in the wake of bank failures in early March, and lending and credit demand were lower. There were also increased concerns about bank liquidity. Several districts reported a slowing in job growth, and there were reports of mass layoffs at a small number of firms. Respondents generally reported more labor market slack, and some reported an increase in labor supply. Quits were generally lower. Wage growth slowed with fewer off-cycle pay hikes but remained above its pre-pandemic pace.

Prices were higher, but the rate of increase was slowing. Costs for non-labor inputs and transportation fell, in some cases dramatically. Manufacturers reported higher prices charged for finished goods, but at a slower pace. Consumer prices continued to increase with solid demand, but rents and house prices leveled off.

Initial claims for unemployment insurance (UI) rose by 5,000 to 245,000 in the week ending April 15 from 240,000 (unrevised) in the week ending April 8. The four-week moving average of claims, which smooths out some of the weekly volatility, was unchanged at 240,000 in the week ending April 15 from the previous week. Continuing claims for unemployment insurance jumped by 61,000 to 1.865 million in the week ending April 8 from 1.804 million in the week ending April 8. The four-week moving average of continuing claims rose by 15,000 to 1.828 million in the week ending April 8. The insured unemployment edged up to 1.3% in the week ending April 8 from 1.2% in the previous week.

CANADA: Canada's CPI index rose 0.1% in March on a seasonally-adjusted basis, and was up 4.3% from a year earlier, down from 5.2% in February. March's inflation reading was the lowest headline number since August 2021. The Bank of Canada's two measures of core inflation slowed in March, with CPI-trim falling to 4.4% from 4.8% and CPI-median falling to 4.6% from 4.9%.

Retail sales fell 1.4% in March, according to a preliminary estimate by Statistics Canada. This followed a 0.2% decline in February and a 1.6% (revised from 1.4%) increase in January. With the increase in March, retail sales were up 2.8% in the first quarter of this year.

With inflation decelerating and consumer spending moderating, the Bank of Canada will likely continue its wait-and-see approach and keep its policy rate the current rate of 4.50% until early 2024.

EUROZONE: Business activity expanded at a better-than-expected pace in April as the preliminary HCOB Eurozone Composite PMI rose to 54.4 from 53.7 in March. The manufacturing PMI fell to 45.5 in April from 47.3 in March; the manufacturing PMI has remained below the key break-even measure of 50 for ten straight months. The services PMI rose slightly to 56.6 from 55.0 in March. The services PMI has remained above 50 for four straight months. A reading above 50 indicates expansionary conditions while a reading below 50 indicates contractionary conditions.

UNITED KINGDOM: CPI inflation surprised to the upside in March as consumer prices rose 0.8% from February, overshooting expectations for a 0.5% increase, and following a 1.1% reading in February. On a year-over-year basis, CPI inflation decelerated to 10.1% in March from 10.4% in February. Prices of goods rose 12.8% in March from a year earlier while prices of services rose 6.6%, the same pace as February. Headline inflation has accelerated at a double-digit pace for seven straight months. Annual core inflation (excluding food, energy, alcohol, and tobacco prices) remained unchanged in March at 6.2%. Looking ahead, inflation should moderate to around 3.0% by the end of the year as the Bank of England increases its policy rate further and economic activity cools in the U.K.

Retail sales fell 1.1% in March following a 1.1% increase in February, according to data from the Office for National Statistics.

Payroll growth decelerated to 31,000 in March from 39,000 (revised from 98,000) in February. The unemployment rate rose to 3.8% in the three months to February from 3.7% in the preceding three-month period. Yearly wage growth (average weekly earnings) was unchanged at 5.9% in the three months to February. Sticky core inflation and strong wage growth would put more pressure on the Bank of England (BoE) to continue its hiking cycle when central bankers meet on May 11. PNC Economics expects the Bank of England to raise its Bank Rate by a quarter of a percentage point to 4.50% when the Monetary Policy Council (MPC) meets on May 11.

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