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Softening Labor Markets in Mid-2025 Support Fed and BoE Rate Cuts

UNITED STATES: The July jobs report came in much weaker than expected. The US only added 73,000 jobs over the month, according to a survey of employers from the Bureau of Labor Statistics. Even more worrisome, job growth in May and June was revised much lower, by a combined 258,000. May job growth was revised lower to 19,000, from 144,000, with June job growth lowered to 14,000, from 144,000. Over the past three months job growth has averaged just 35,000, the slowest three-month pace of job creation since the economy was losing millions of jobs during the pandemic. Job growth averaged above 200,000 per month in 2023, and 168,000 per month in 2024. Private-sector job growth was 83,000 in July, with net government job losses of 10,000. Over the past three months private-sector job growth has averaged 52,000.

The US economy expanded 3.0% at an annualized rate in the second quarter, according to the advance estimate of real (inflation-adjusted) GDP from the Bureau of Economic Analysis. This followed a decline of 0.5% in the first quarter, the first contraction since the first quarter of 2022. Growth in the fourth quarter of 2024 was 2.4%. Tariffs have distorted GDP data in the first half of 2025. But the overall story is one of slowing, but still positive, economic growth in recent quarters. On a year-ago basis real GDP growth has slowed from 3% in the second half of 2023 and the first half of 2024 to around 2% currently. Growth has slowed after a surge with the recovery from the pandemic; higher interest rates and slower labor force growth have also weighed on growth over the past year. Growth is likely to slow further in the near term, to around a 1.5% annualized pace in late 2025 and early 2026. Higher prices from tariffs will weigh on business investment and consumer spending, and the uncertainty surrounding tariffs will also weigh on growth, as firms hold off on investments and households on big purchases until the picture is clearer. High interest rates will remain a drag, as will even slower labor force growth due to restrictions on immigration and federal government spending cuts.

As expected, the Federal Open Market Committee kept the federal funds rate unchanged in its policy statement on July 30, in a range between 4.25% and 4.50%. Two members of the Board of Governors dissented, Bowman and Waller, who both called for a 0.25 percentage point cut in the funds rate, although the statement did not provide a rationale for this view. This is the first time two members of the Board of Governors have dissented since 1993. The dissents may be tied to President Trump's pressure on the FOMC to cut the fed funds rate; the president has aggressively called for rate cuts, arguing that current monetary policy is too tight. PNC's current forecast is for one 25 basis point cut in the fed funds rate in 2025, at the last meeting of the year on December 9 and 10. By that point the inflationary impact of higher tariffs should be fading, giving the central bank more leeway to ease. PNC is then calling for two additional 25 basis point cuts in the fed funds rate at each of the FOMC's first two meetings of 2026. This would take the fed funds rate to a range of 3.50% to 3.75% by the spring of 2026.

The ISM Manufacturing Purchasing Managers' Index (PMI) fell to 48.0 in July 2025, giving back June's gain. The topline index has been in contractionary territory since February of this year after a healthy rise through the second half of 2024. New Orders and Employment both remained firmly in contractionary territory. Production posted a gain for the month—the component's second consecutive monthly rise—and was the only component in the report to have breached the

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expansionary threshold of 50.0. The ISM Manufacturing PMI diffusion index indicates the net percentage of manufacturers who are experiencing expanding or contracting activity across various categories, with a reading below 50 revealing net contraction across the manufacturing sector. July 2025's topline reading of 48.0 represents the fifth consecutive monthly contraction after two months above the expansionary threshold to open this year.

Initial claims for unemployment insurance edged up by 1,000 to 218,000 in the week ending July 26, with the four-week moving average of initial claims ending July 26 down into the lower half of a 213,000 to 240,000 range that had prevailed for the previous eight months after rising above the top of that range in the first half of June. Continuing unemployment insurance claims held steady at 1.946 million (revised down from 1.955 in the previous week) in the week ending July 19. The declining level of initial claims for the past six weeks shows that employers are reluctant to lay-off workers but the large rise in continuing claims in the past eight weeks shows that employers are also reluctant to hire new workers. This combination is a clear sign that the labor market started softening in the late-spring and early-summer months which we expect to persist for the rest of this year.

Personal income increased 0.3% in June from May before adjustment for inflation, with after-tax income also up 0.3%, according to the Personal Income and Outlays release from the Bureau of Economic Analysis. Disposable (after-tax) personal income fell 0.4% in May after rising 0.8% in April due to changes in Social Security benefits. Consumer spending increased 0.3% in June as well.

The S&P CoreLogic Case-Shiller US National Home Price Index fell for a third straight month in May, down 0.3% after seasonal adjustment. On a year-over-year basis the index was up 2.2% in May, a fourth straight month of a slowdown in yearly price gains. Single-family home prices rose for more than two years in a row before April and had been setting record highs since April 2023. Total existing home sales fell 2.7% to 3.93 million units at a seasonally adjusted annualized rate in June, from 4.0 million units in May, according to the National Association of Realtors (NAR). Sales came in weaker than the consensus expectation for a smaller decline. On a year-ago basis total existing home sales were flat in June. US total construction spending dropped for a second straight month in June, falling 0.4% from May to \$2.136 trillion at a seasonally adjusted annualized rate, from \$2.144 trillion (downwardly revised from \$2.152 trillion) in May, according to the Census Bureau. The drop in June came against the consensus expectation for no decline. Construction spending has fallen in nine of the past ten months. On a year-over-year basis total construction spending fell 2.9% in June, the fifth straight year-over-year decline, although this is up slightly from a 3.2% drop in May. Both residential and nonresidential construction spending fell on the month, down 0.7% and 0.1%, respectively.

JAPAN: The Manufacturing PMI retreated into contractionary territory in July, to 48.9 according to S&P Global, after reaching the highest level since June 2024 in the previous month. Led by a retreat in fuel and utilities, year-over-year Tokyo CPI inflation slowed to a four-month low of 2.9% in July from 3.1% in June according to Japan's Ministry of Internal Affairs and Communication. Prices of fuel and utilities fell for two straight months in July, down 1.2% on the month after falling 4.2% in June. On a year-ago basis, the CPI of fuel and utilities (electricity, gas and other fuel, light, and water and sewage) declined 4.5% in July. Excluding volatile energy and fresh food, core Tokyo CPI inflation remained unchanged in July from June, at 3.1%, and total inflation excluding energy and food remained below 2%, at 1.7%. The Bank of Japan (BoJ) kept its overnight call rate unchanged at around 0.5% on July 31 and has held the interest rate steady since late January 2025 as headline CPI inflationary pressure eased after bumps in volatile food prices. In the Outlook for Economic Activity and Prices released after July 31, growth projections remain about unchanged from April's economic outlook report, while year-over-year CPI inflation was adjusted higher for fiscal 2025 according to the BoJ. A highly uncertain and frequently changing international trade environment complicated the central bank's efforts in controlling inflation. The



BoJ acknowledged risks tied to trade uncertainty and evolvments around trade impacts. This would require more caution on the Japanese foreign exchange market, growth and inflation in the future.

UNITED KINGDOM: Recent economic data shows a weaker UK labor market and a slower economic growth in mid-2025 while UK inflation remained well elevated. According to the Office for National Statistics, payrolled employees fell for a fifth straight month in June, down 41,357 after the labor market lost 25,466 jobs in May. The three-month moving average of payrolled employees was a net loss of almost 30,000 jobs in June, the steepest since August 2024 when the number of payrolled employees started to fall. UK's composite PMI fell to 51 in July from 52 according to S&P Global, pointing to a slower overall economic growth on the month compared to June. Manufacturing activity contracted at a slower pace with its PMI up to 48 while the services sector grew slower in July with its PMI down to 51.2 from 52.8 in June. The consensus expects the Bank of England to cut back the official Bank Rate by 25 bps on August 7, to 4% from 4.25%. Core inflation remains sticky and elevated at 3.7% in June, and year-over-year topline CPI inflation came in at 3.6% after the CPI advanced 0.3% on the month. This will likely keep the nine votes divided within BoE's Monetary Policy Committee when it meets on August 7. The BoE has cut the Bank Rate four times in the current monetary policy easing cycle.

AUSTRALIA: Year-over-year Consumer Price Index (CPI) inflation unexpectedly fell to 1.9% in June from 2.1% in May according to the Australian Bureau of Statistics, below the Reserve Bank of Australia's (RBA) inflation target range of two to three percent and the lowest year-over-year CPI inflation since March 2021. This month's CPI report also concluded the second quarter with a Q2 CPI inflation at 2.1%, down from 2.4% in Q1 and the fourth consecutive quarter of topline inflation within the RBA's inflation tolerate band. Core annual CPI inflation, headline CPI inflation excluding volatile items, fell to 2.1% in June from 2.5% in May. Core CPI inflation has been under three percent for two straight quarters in Q2 2025 and will likely prompt the third interest rate cut within the existing interest rate easing cycle during RBA's meeting on August 12, 2025.

INDIA: Annual headline CPI inflation in June came in cooler than the consensus expectation and fell sharply to 2.1% from 2.8% in May according to India's Central Statistics Office. The annual growth of industrial production weakened sharply to 1.5% in June from 1.9% in May, the slowest since August 2024. Drags came from mining and electricity outputs which fell 8.7% and 2.6%, respectively, from last year. On a year-over-year basis, the manufacturing output, however, jumped 3.9% in June, up from 3.2% in May and 3.1% in April. This is consistent with the HSBC Manufacturing PMI of a faster expansion in manufacturing activity in June and July. The manufacturing PMI increased to 59.1 in July from 58.4 in June according to S&P Global, marking the highest reading since March 2024 and remaining firmly in expansionary territory entering the second half of 2025. According to S&P Global's PMI report, demand for goods strengthened substantially with a rise in new orders, while the sales pace and production growth accelerated steeply. The expansion in India's services sector slowed with the services PMI down to 59.8 in July from 60.4, but this is firmly in expansionary territory. Current slower inflation combined with strong expansion in both the goods-producing and the services sectors will likely put the Reserve Bank of India's Monetary Policy Committee on hold when it announces its monetary policy decision on August 6. The RBI unexpectedly lowered its monetary policy interest rate by 50 bps while the consensus was expecting a smaller cut in June.

MEXICO: Real GDP for the second quarter came in better than the consensus expectation and grew 0.7%, up from 0.2% in the first quarter according to Mexico's National Institute of Statistics and Geography (INEGI). Quarterly economic growth picked up from the previous two quarters, but year-over-year real GDP was up only 0.06% in Q2, down from 0.8% in Q1 2025. Mexico's manufacturing PMI jumped to 49.1 in July from 46.3 in June. Although this is up on the month, the



manufacturing sector continued to contract in July at a slower pace. US tariffs have weighed on goods producers in Mexico with new orders down on the month again, but the pace slowed according to S&P Global's PMI report. The biweekly headline 12-month CPI inflation moved closer to the Banxico's inflation objective of around 3% (+/- 1%), at 3.55% in the top two weeks of July. The consensus expects the central bank of Mexico to lower the Overnight Rate by 25 bps from 8% to 7.75% on August 7. Inflation within Banxico's tolerance band will likely favor an interest rate cut this week that will benefit a sluggish Mexican economy in 2025.

CHINA: Cumulative industrial total profits came in at -1.8% year-over-year, down from -1.1% in May according to the National Bureau of Statistics of China. The NBS manufacturing Purchasing Managers' Index fell in July to 49.3, the fourth straight month China's manufacturing activity was in contractionary territory. Demand for goods declined with the New Orders component down to 49.4 from 50.2, and new export orders also fell on the month which has been in the contractionary field for fifteen months through July.

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