Global Economic Highlights

May 13, 2025

Cautious Fed Held While Uncertainty Remains High; BOE and PBOC Cut

UNITED STATES: As widely expected, the FOMC left the fed funds rate unchanged in a range of 4.25% and 4.50% in its policy statement on May 7. That marks the third straight hold after the FOMC cut the fed funds rate by a cumulative 100 basis points last year. The decision was unanimous. The FOMC stated that "although swings in net exports have affected the data, recent indicators suggest that economic activity has continued to expand at a solid pace. The unemployment rate has stabilized at a low level in recent months, and labor market conditions remain solid. Inflation remains somewhat elevated." In his post-meeting press conference, Fed Chair Powell suggested that the FOMC is not ready to cut the fed funds rate again until there is more clarity on tariffs and the impacts on inflation and economic growth. He also said that in terms of the potential impacts of tariffs on the economy, the range of possibilities is very wide. PNC's baseline forecast is for four additional fed funds rate cuts in 2025 of 25 basis points at each of the FOMC's last four meetings beginning in July. This would take the fed funds rate to a range of 3.25% to 3.50% by year end.

The seasonally adjusted nominal U.S. goods and services trade deficit rose 14% in March to $140.5 billion before adjustment for inflation from $123.2 billion in February. The trade deficit was also larger than the consensus expectation and dragged on Q1 real GDP growth. On a year-ago basis the total trade deficit was up 105% in March. The goods trade deficit broadened while the services trade surplus fell in March. The goods trade deficit jumped 11% on the month and a large 75% on a year-over-year basis, to $163.5 billion. The services trade surplus narrowed for a fourth consecutive month in March to the lowest level since early 2023. The services trade surplus dropped 3.5% to $23 billion, as services exports fell more than imports on the month. President Trump announced a 10% tariff on all countries taking effect on April 5, and individualized reciprocal tariffs are temporarily on hold. A 25% tariff on imported autos started in early April. The speculative moves ahead of tariffs are expected to be short-lived and should not show up in the following trade reports as record-high deficits. However, higher tariffs both in the US and abroad could lead to lower US imports and exports, and this will do little to change the overall trade deficit. PNC expects noticeably slower economic growth in 2025, with increased risk of near-term recession from the start of this year.

Nonfarm business sector labor productivity, or output per hour, decreased 0.8% at an annualized rate in the first quarter of 2025, the U.S. Bureau of Labor Statistics reported today. Output decreased 0.3% and hours worked increased 0.6%. This is the first decline in nonfarm business sector labor productivity since the second quarter of 2022. From the same quarter a year ago, nonfarm business sector labor productivity increased 1.4%, down from 2.1% in the fourth quarter. Moreover, annual gains in productivity have decelerated since the first quarter of 2024 when growth registered 3.3% – the fastest pace of growth since the first quarter of 2021. Manufacturing sector labor productivity increased 4.5% annualized in the first quarter of 2025, as output rose 5.1% and hours worked increased 0.5%. The increase in productivity is the sharpest since the second quarter of 2021 (5.3%). Durable manufacturing sector productivity increased 7.1% while nondurable manufacturing sector productivity rose 2.2%.

Unit labor costs, or how much a business pays its workers to produce one unit of output, surged 5.7% annualized in the first quarter of 2025, reflecting a 4.8% increase in hourly compensation and a 0.8% decrease in productivity. That marks the strongest increase in unit labor costs since the first quarter of 2024 (8.3%). On a year-on-year basis, unit labor costs are up 1.3%, the slowest pace of growth since the third quarter of 2023 and well below the Fed's 2% inflation target. Moreover, annual growth in unit labor costs has slowed since the first quarter of 2024 amid weaker job growth. Real

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hourly compensation, adjusted for inflation, climbed 1.0% in the first quarter following a downwardly revised 0.6% increase in the fourth quarter.

Initial claims for unemployment insurance fell by 13,000 to 228,000 in the week ending May 3, reversing half of the two previous weeks' rise. The four-week moving average of initial claims, which averages out some of the weekly volatility, edged up by 1,000 to 227,000 for the week ending May 3, near the middle of a 213,000 to 238,000 range in the past seven months. The Challenger Layoff report shows 552,000 layoffs announced in the past three months combined, more than double the number in the same three months in 2024. Layoffs of Federal workers by DOGE accounts for just over half of the total this year. Continuing unemployment insurance claims fell by 29,000 to 1.879 million in the week ending April 26. The four-week moving average of continuing claims rose by 9,000 to 1.875 million, the highest level since mid-November 2024, suggesting it is taking unemployed workers somewhat longer to find a new job. The insured unemployment rate edged down to 1.2 percent in the week ending April 26, the same as a year ago.

There is a growing but still small impact from the Department of Government Efficiency's layoffs of Federal government employees. Initial jobless claims filed by fired civilian Federal employees were 468 in the week ending April 26, down by 2 from the previous week. There were 6,716 continuing claims filed by fired civilian Federal employees in the week ending April 19, an increase of 82 from the previous week. This is below the 24,000 decline of Federal government employees in February, March and April combined according to the BLS. We expect bigger declines in May and June.

UNITED KINGDOM: The Bank of England cut the Bank Rate by 25 bps from 4.5% to 4.25% on May 8 as expected. According to the Monetary Policy Report released with this meeting, two Monetary Policy Committee (MPC) members preferred to maintain the Bank Rate unchanged at 4.5% while the other seven committee members voted interest rate cuts (five of them voted a 25-bps cut, and two voted a 50-bps cut). There is no doubt that the majority of the MPC preferred an interest rate cut in the May 8 meeting. But there was a divergence on Bank Rate cuts that had not been in the February meeting.

Inflation picked up somewhat in the beginning of 2025, with year-over-year CPI inflation up to 3% in January from 2.5% in December 2024. Since then, twelve-month CPI inflation eased, to 2.6% in March, but remained higher than the BOE's 2% year-over-year inflation objective. The bump in inflation seems to be only temporary as the inflation measure fell over the past three months. Global trade uncertainty and tariff developments will likely be a drag to global economic growth. The BOE expected world export prices to be "materially weaker, particularly in China (Key judgement 4). The current overall impact of trade developments on the UK is therefore more likely to be disinflationary than inflationary. Consistent with this, the effects incorporated into the baseline are negative, though not large particularly in the medium term." As of May 12, a temporary 90-day truce in the US-China trade war went into effect. Drags from trade will likely lessen with current or more easing in trade policies between the US and other sovereign economies, compared to early April. But tariff policies from the US remain restrictive from December 2024 and trade uncertainty remains high.

Seasonally adjusted real retail sales including auto fuel came in stronger than the consensus expectation and increased 0.4% in March according to UK Office for National Statistics. On a year-over-year basis, retail sales rose 2.6% and picked up from 1.8% in February and 0.6% in January. Excluding auto fuel, which declined 1.1% for the month, sales increased for a third straight month, up 0.5% in March. Retail sales made in food stores continued to fell in March, while sales from non-food stores increased further on the month after rising in February. Sales pace remained strong in the first quarter of 2025.

There was a decline in overall private business service activity following the first quarter of 2025. According to S&P Global, the Services Purchasing Managers' Index (PMI) fell to 49 in April from 52.5 in March, dipping below the expansionary threshold of 50 for the first time since late 2023. The Composite PMI, therefore, fell to 48.5 in April accompanied by below-50 Manufacturing PMI readings since September 2024. This indicates the first contraction in UK's private economic activity since October 2023 as service providers experienced a business activity downturn.

CANADA: Real GDP contracted 0.2% in February, after rising 0.4% in January and 0.3% in December according to Statistics Canada. Severe weather conditions have weighed on real GDP in the transportation and warehousing sector, but durable manufacturing expanded a second straight month in February. Transportation equipment manufacturing led the gains in real GDP, with auto parts manufacturing rising the most in the transportation equipment manufacturing subsector, ahead of President Trump's trade policy. On a year-over-year basis, real GDP grew 1.6% in February, a slower pace from 2.3% in January and 2.2% in December 2024.

The Canadian labor market added 7,400 jobs in April after falling 32,600 in March according to a Labor Force Survey. This is better than the consensus expectation for the month. Full-time employment increased 31,500 in April, and part-time employment fell 24,200. Goods-producing sector employment dropped 33,000 in April, with manufacturing industry employment declining 30,600 on the month. This is the third consecutive drop in Canada's manufacturing employment. Services-providing sector employment grew 40,300 in April, more than offsetting a 20,900 drop in the previous month. The unemployment rate rose to its long-run average at 6.9% in April.

CHINA: The National Bureau of Statistics' Manufacturing PMI fell to a contractionary level at 49 in April from 50.5 in March. The New Orders component fell back to a contractionary level at 49.2, and the Production component contracted marginally for the month to 49.8. As the US-China trade war escalated in April, the New Export Orders component dipped to the lowest level since late 2022, at 44.7. China's headline CPI inflation rate fell to -0.1% year-over-year in April, extending a third month of year-over-year price declines from March and February.

The People's Bank of China announced plans to cut multiple key interest rates on May 7. Central bank lending rates were lowered by 25 bps, targeting central bank lending for rural development and micro and small businesses (MSBs). The lending quota for rural development and MSBs was raised by 300 billion yuan. The 7-day reverse repurchase rate was down from 1.5% to 1.4%. The required reserve ratio will be lowered by 50 bps from 9.5% to 9% starting on May 15.

EUROZONE: According to Eurostat, seasonally adjusted Q1 real GDP grew 0.4%, surpassing the consensus expectation. Over the past year, real GDP increased 1.2%, maintaining the same year-over-year pace in Q4 2024. The preliminary Harmonized Indices of Consumer Prices (HICP) for the euro area was up 0.6% month-on-month in April and 2.2% year-over-year. Energy prices came down from April 2024. However, there was a pick-up in services and (unprocessed) food inflation, jumping to 3.9% and 4.9% from 3.5% and 4.2%, respectively.

JAPAN: The Tokyo CPI inflation rate jumped to 3.5% year-over-year in April from 2.9% in March according to the Statistics Bureau of Japan. Core CPI inflation, total inflation excluding fresh food and energy, rose to the highest level since early 2024, to 3.1% year-over-year in April from 2.2% in March. The Manufacturing PMI rose to 48.7 in April from 48.4 in March according to S&P Global, the 10th month of sub-50 reading and signaling further deterioration in manufacturing business conditions.

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