

NATIONAL ECONOMIC OUTLOOK

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Executive Summary

Continued Solid Job Growth; Fed Raises Rates to Close out 2018

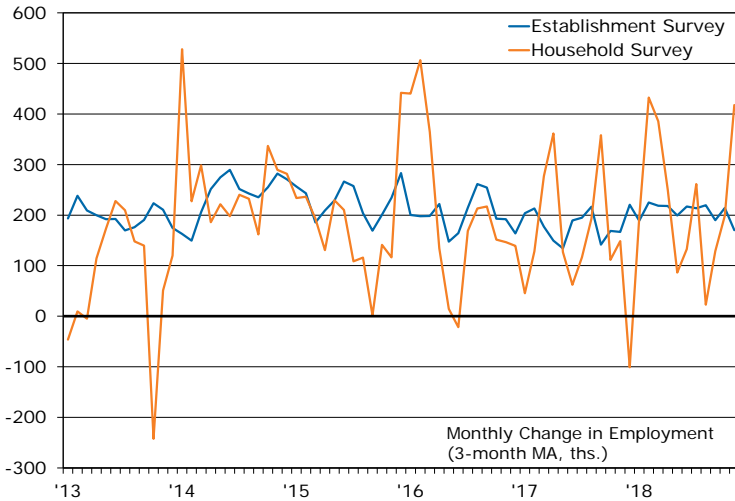
- The U.S. economy added 155,000 jobs in November, after a gain of 237,000 in October. Job growth has averaged 206,000 per month so far in 2018, up from 182,000 per month in 2017. Goods-producing industries added 29,000 jobs in November, after a big increase of 53,000 in October. Private service-providing industries added 126,000 jobs for the month, while there were job losses of 6,000 in government. The unemployment rate held steady at 3.7 percent in November for a third straight month, the lowest since 1969. With the tight labor market employers are boosting pay. Average hourly earnings were up 3.1 percent in November from one year earlier, the same rate as in October; wages are growing at their fastest pace since 2009.
- As expected, the Federal Open Market Committee raised the federal funds rate by one-quarter of a percentage point on December 19, to a range of 2.25 to 2.50 percent. The decision was unanimous. This was the fourth increase this year (every other FOMC meeting). The FOMC has been gradually raising the fed funds rate from a near-zero level since late 2015. In its forward-looking section, the FOMC statement said that “the Committee judges that some further gradual increases in the target range for the federal funds rate will be consistent with sustained expansion of economic activity, strong labor market conditions, and inflation near the Committee’s symmetric 2 percent objective over the medium term.” The addition of the word “some” to the statement in December suggests that while the FOMC expects to continue raising the rate fed funds rate in 2019, it may be approaching the end of its tightening cycle. The language on current economic conditions was unchanged from the previous statement, on November 8, and was quite positive, despite recent stock market volatility.
- Oil prices are falling at the end of 2018, down to around \$45 for a barrel of West Texas Intermediate crude, from \$76 in early October. Increased U.S. production in response to higher prices earlier this year, slightly slower global economic growth, and the decision by the Trump administration to grant waivers to major importers of Iranian oil have all pushed down oil prices. The big drop in oil prices will slow inflation in late 2018 and early 2019, giving the FOMC more leeway to keep interest rates low and support economic growth.

Baseline U.S. Economic Outlook, Summary Table*

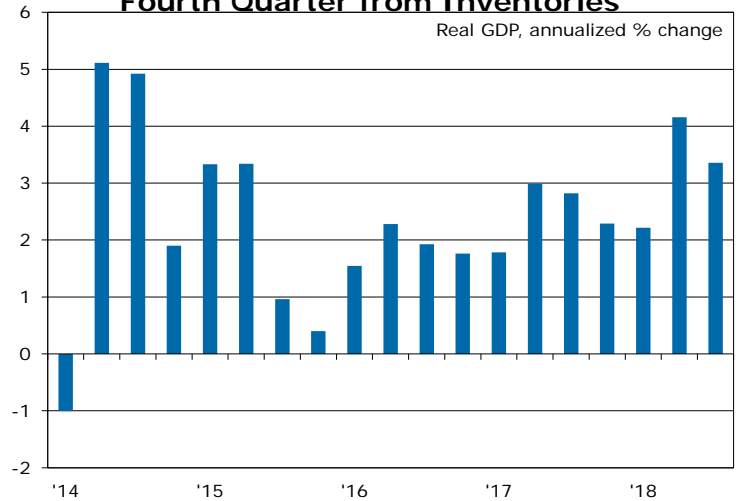
	1Q'18a	2Q'18a	3Q'18p	4Q'18f	1Q'19f	2Q'19f	3Q'19f	4Q'19f	2017a	2018f	2019f	2020f
Output & Prices												
Real GDP (Chained 2012 Billions \$)	18324	18512	18672	18765	18901	19028	19153	19247	18051	18568	19082	19458
Percent Change Annualized	2.2	4.2	3.5	2.0	2.9	2.7	2.7	2.0	2.2	2.9	2.8	2.0
CPI (1982-84 = 100)	249.4	250.5	251.7	252.0	253.1	254.7	256.4	258.0	245.1	250.9	255.5	261.9
Percent Change Annualized	3.5	1.7	2.0	0.5	1.8	2.5	2.6	2.6	2.1	2.4	1.8	2.5
Labor Markets												
Payroll Jobs (Millions)	148.1	148.7	149.3	149.9	150.4	150.9	151.4	151.8	146.6	149.0	151.1	152.6
Percent Change Annualized	1.7	1.7	1.7	1.6	1.3	1.3	1.3	1.1	1.6	1.6	1.4	1.0
Unemployment Rate (Percent)	4.1	3.9	3.8	3.7	3.6	3.5	3.4	3.4	4.4	3.9	3.5	3.5
Interest Rates (Percent)												
Federal Funds	1.45	1.74	1.92	2.21	2.38	2.41	2.66	2.88	1.00	1.83	2.58	2.88
Treasury Note, 10-year	2.76	2.92	2.92	3.22	3.35	3.35	3.34	3.34	2.33	2.96	3.35	3.29

a = actual f = forecast p = preliminary * Please see the Expanded Table for more forecast series.

Job Growth Remains Solid at the End of 2018



Growth to Temporarily Slow in Fourth Quarter from Inventories



Holiday Spending Set to Grow at Fastest Pace Since Before Great Recession

Consumer spending will close out 2018 on a strong footing, with holiday sales growth of around 6.5 percent compared to last year. This would be the fastest pace since 2007, right before the start of the Great Recession. However, much of the growth will take place at online retailers; gains at traditional “brick-and-mortar” retailers will be much smaller.

The fundamentals for consumers at the end of 2018 are excellent. Job growth is solid at around 200,000 per month, and has picked up somewhat this year. With the unemployment rate at 3.7 percent, the lowest it has been since 1969, firms are responding to the tight job market by boosting pay. Average hourly earnings were up 3.1 percent in October and November from one year earlier, the fastest wage growth since the job market was imploding in early 2009. Before-tax income is up more than 4 percent in late 2018 from one year earlier.

The personal income tax cut Congress passed at the end of 2017 is also a positive for holiday spending. Personal tax payments are up less than 1 percent in late 2018 from last year, well below income growth. As a result after-tax incomes are growing at a robust year-over-year pace of almost 5 percent at the end of 2018.

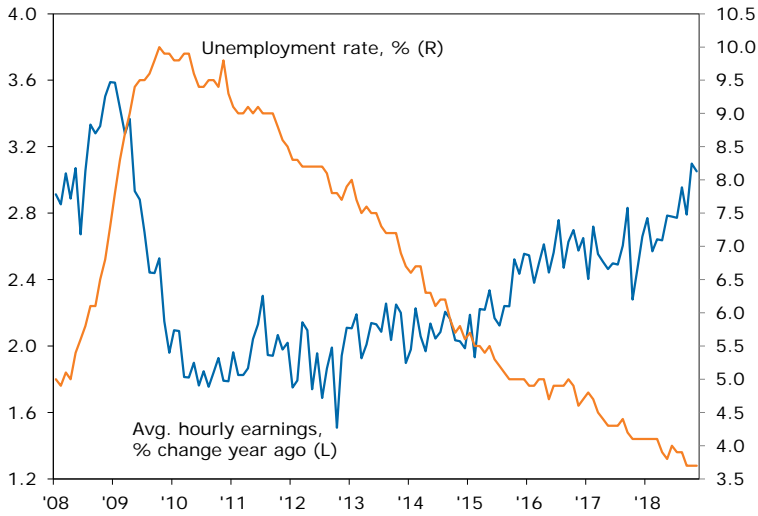
Low inflation, particularly falling energy prices, is also providing a boost to holiday sales. The price of a gallon of unleaded gasoline has fallen to around \$2.40 in mid-December, its lowest in more than a year, and is down around 1 percent from one year ago. Other prices are rising only slowly. As a result after-tax income, adjusted for inflation, is up almost 3 percent in late 2018 from one year ago.

There are some negatives for holiday spending this year. Stock market volatility may cause wealthier households to turn more cautious in their purchases, and the unsettled political outlook and concern over tariffs may also be drags. Higher interest rates that make it more expensive to borrow for big-ticket items are also a negative for holiday sales. Consumer confidence fell slightly in November, according to the Conference Board, but remained near its highest levels since 2000.

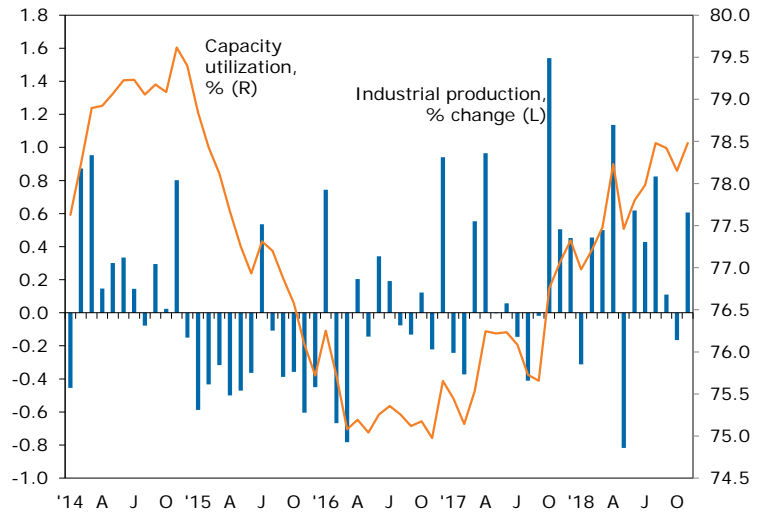
Although there are some negatives for holiday spending, the outlook is bright. Holiday sales should be up around 6.5 percent this year, after a gain of about 6 percent in 2017. This would be the fastest sales growth since 2007, before the Great Recession. About 4.5 percentage points of the increase will come from higher unit sales, with about 2 percentage points from higher prices. However, the composition of purchases will continue to shift, moving away from traditional retail stores and toward online sellers. Traditional retailers will eke out a small increase in sales this year of around 3 percent, while online sellers will enjoy another year of double-digit growth.

With a strong holiday season consumer spending will continue to drive economic growth at the end of 2018. However, fourth quarter growth will slow somewhat from its strong pace in mid-2018 because of a cutback in business inventory accumulation. Growth will then pick back up in the first half of 2019, to close to 3 percent on an annualized basis. Business investment and consumer spending are both getting boosts from tax cuts; a large increase in federal government spending is also a near-term positive. Assuming no significant disruptions trade will be a slight negative as growth in imports is stronger than growth in exports. Growth will slow over the course of 2019 as fiscal stimulus wears off. After averaging slightly above 200,000 in 2018, monthly job growth will slow to around 150,000 in 2019 because of the tight labor market. The unemployment rate will continue to move lower, to around 3.4 percent by the end of next year. To contain inflation the Federal Open Market Committee will continue with gradual rate increases in 2019; PNC expects two next year, down from four this year. With a big drop in energy prices inflation will slow in the near term, and then gradually return to the Federal Reserve’s objective of 2 percent.

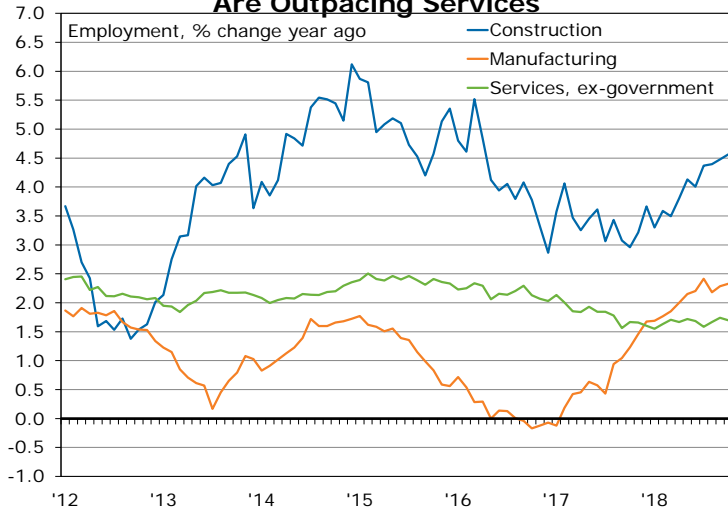
Tight Job Market Will Push Wages Higher in 2019



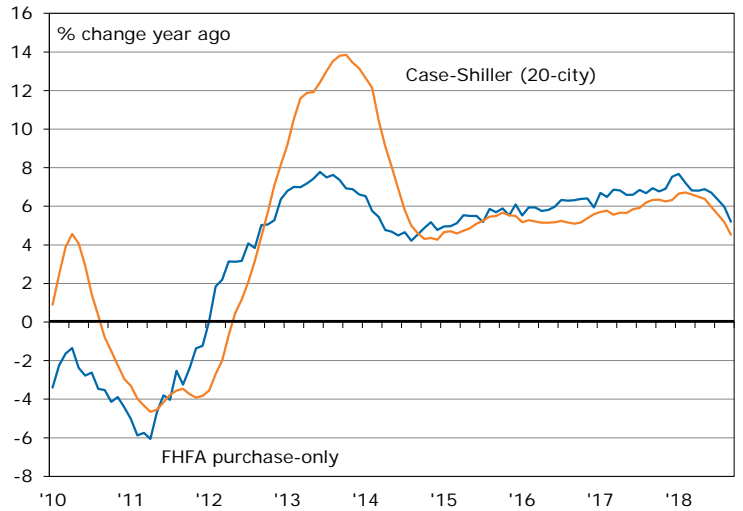
Industrial Sector Supporting U.S. Growth in Late 2018



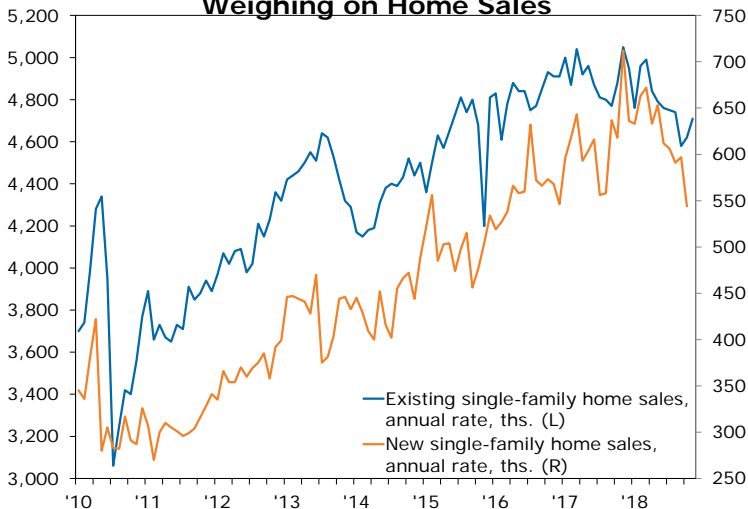
Construction and Manufacturing Are Outpacing Services



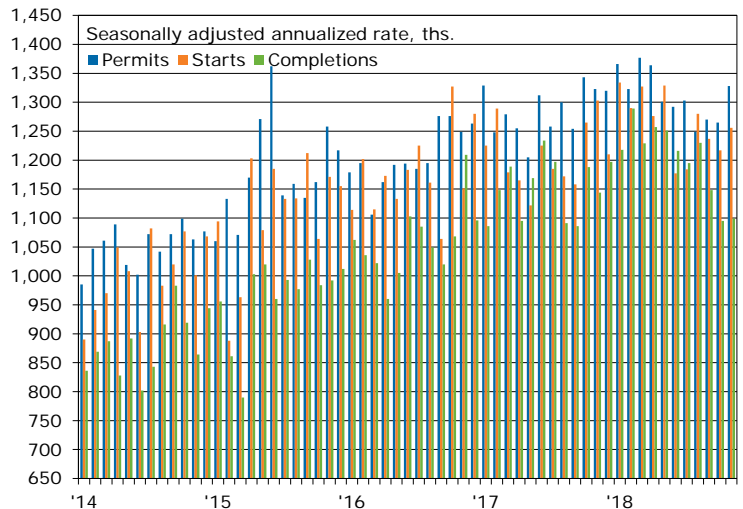
House Price Growth Set to Slow Further in 2019



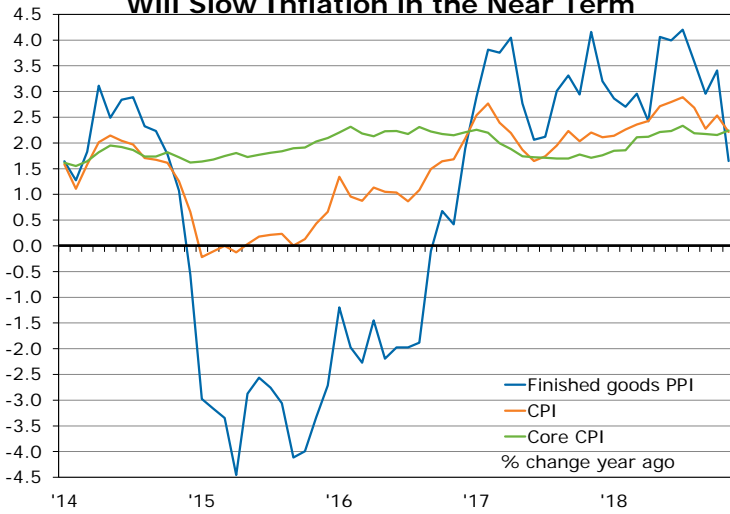
Higher Mortgage Rates Are Weighing on Home Sales



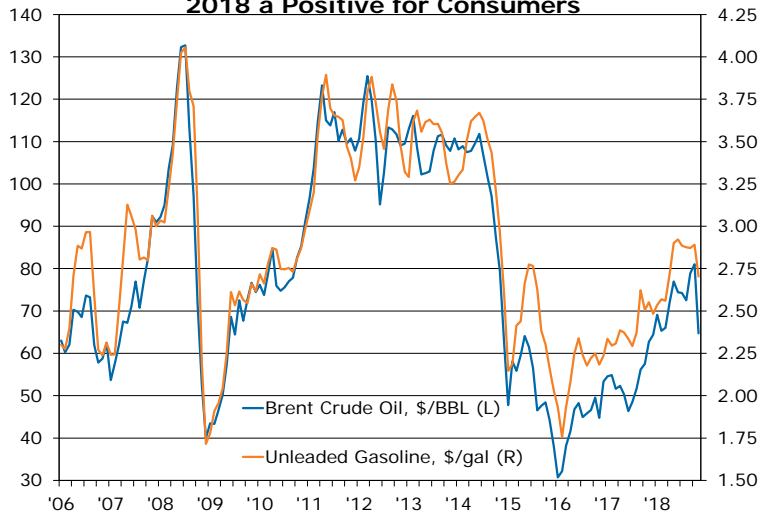
Homebuilding May Be Picking Back Up in Late 2018



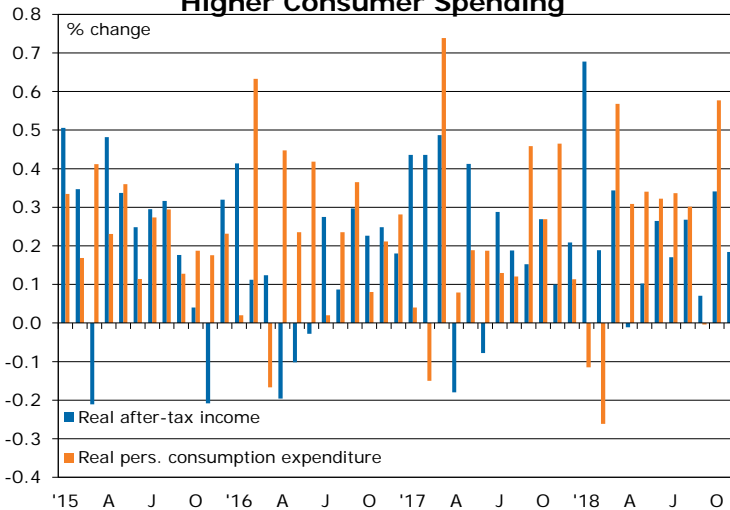
Recent Big Drop in Energy Prices Will Slow Inflation in the Near Term



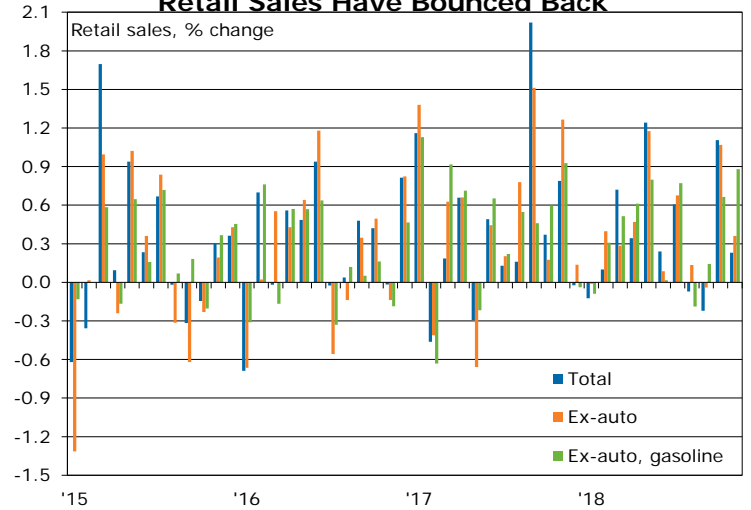
Drop in Gasoline Prices in Late 2018 a Positive for Consumers



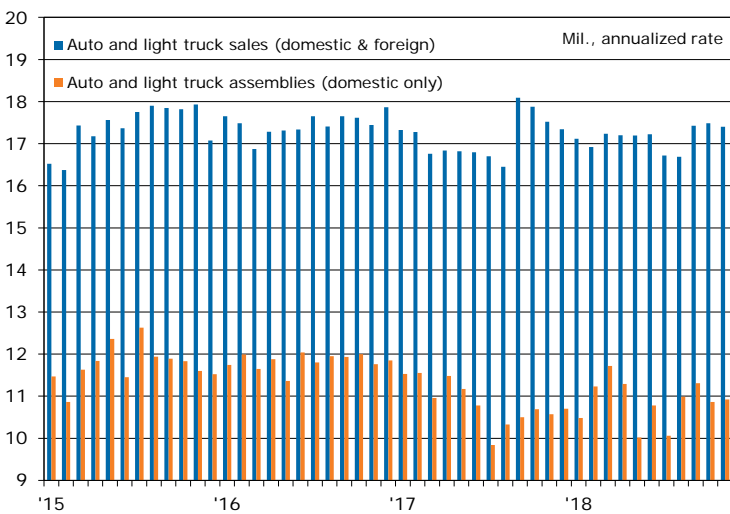
Higher Personal Income Means Higher Consumer Spending



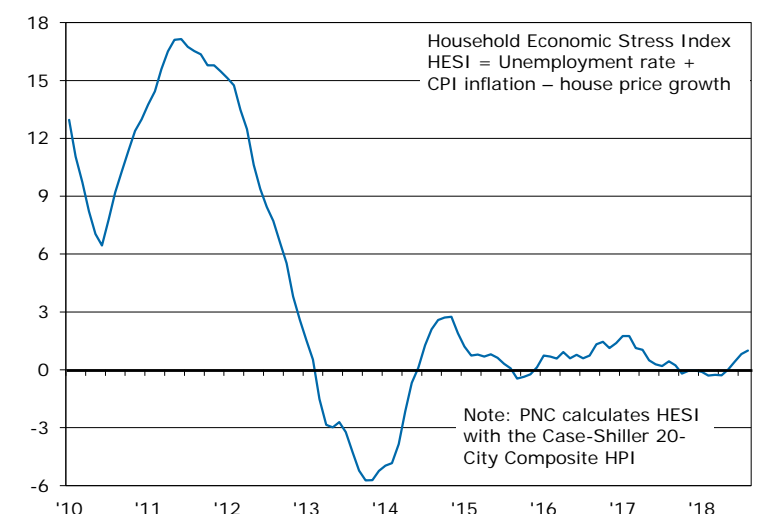
After Soft August and September, Retail Sales Have Bounced Back



Auto Sales Continue to Best 17 Million Per Year



Households Remain in Good Financial Shape



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NATIONAL ECONOMIC OUTLOOK

PNC Economics Group
December, 2018

Baseline U.S. Economic Outlook, Expanded Table

	1Q'18a	2Q'18a	3Q'18p	4Q'18f	1Q'19f	2Q'19f	3Q'19f	4Q'19f	2017a	2018f	2019f	2020f
Output												
Nominal GDP (Billions \$)	20041	20412	20660	20819	21066	21312	21581	21820	19485	20483	21445	22393
Percent Change Annualized	4.3	7.6	5.0	3.1	4.8	4.8	5.1	4.5	4.2	5.1	4.7	4.4
Real GDP (Chained 2012 Billions \$)	18324	18512	18672	18765	18901	19028	19153	19247	18051	18568	19082	19458
Percent Change Annualized	2.2	4.2	3.5	2.0	2.9	2.7	2.7	2.0	2.2	2.9	2.8	2.0
Pers. Consumption Expenditures	12723	12842	12957	13079	13154	13221	13293	13361	12559	12900	13257	13517
Percent Change Annualized	0.5	3.8	3.6	3.8	2.3	2.0	2.2	2.1	2.5	2.7	2.8	2.0
Nonresidential Fixed Investment	2654	2710	2727	2757	2791	2821	2848	2871	2538	2712	2833	2912
Percent Change Annualized	11.5	8.7	2.5	4.5	5.0	4.4	3.9	3.2	5.3	6.9	4.5	2.8
Residential Investment	615	613	609	611	614	615	617	620	611	612	616	630
Percent Change Annualized	-3.4	-1.3	-2.6	1.4	1.6	0.5	1.7	2.1	3.3	0.2	0.7	2.1
Change in Private Inventories	30	-37	87	23	31	44	56	52	23	26	46	48
Net Exports	-902	-841	-946	-979	-993	-1000	-1010	-1019	-859	-917	-1006	-1023
Government Expenditures	3152	3172	3192	3228	3259	3282	3303	3317	3130	3186	3290	3330
Percent Change Annualized	1.5	2.5	2.6	4.5	3.9	2.9	2.6	1.7	-0.1	1.8	3.3	1.2
Industrial Prod. Index (2012 = 100)	105.9	107.3	108.5	109.9	110.6	111.2	111.8	112.3	103.7	107.9	111.5	113.1
Percent Change Annualized	2.5	5.3	4.7	5.1	2.5	2.3	2.1	1.7	1.6	4.1	3.3	1.4
Capacity Utilization (Percent)	77.2	77.8	78.3	79.3	79.7	80.2	80.6	80.9	76.1	78.2	80.4	81.5
Prices												
CPI (1982-84 = 100)	249.4	250.5	251.7	252.0	253.1	254.7	256.4	258.0	245.1	250.9	255.5	261.9
Percent Change Annualized	3.5	1.7	2.0	0.5	1.8	2.5	2.6	2.6	2.1	2.4	1.8	2.5
Core CPI Index (1982-84 = 100)	255.7	256.9	258.2	259.5	261.0	262.5	264.0	265.5	252.2	257.6	263.2	269.3
Percent Change Annualized	3.0	1.8	2.0	2.1	2.3	2.4	2.4	2.3	1.8	2.1	2.2	2.3
PCE Price Index (2012 = 100)	107.5	108.1	108.5	108.6	109.0	109.6	110.3	110.9	106.1	108.1	109.9	112.4
Percent Change Annualized	2.5	2.0	1.5	0.4	1.5	2.3	2.5	2.4	1.8	2.0	1.6	2.3
Core PCE Price Index (2012 = 100)	109.2	109.8	110.2	110.7	111.3	111.8	112.5	113.0	108.0	110.0	112.2	114.5
Percent Change Annualized	2.2	2.1	1.5	1.8	2.0	2.1	2.2	2.1	1.6	1.9	2.0	2.1
GDP Price Index (2012 = 100)	109.4	110.3	110.7	111.0	111.5	112.0	112.7	113.4	107.9	110.3	112.4	115.2
Percent Change Annualized	2.0	3.3	1.4	1.1	1.9	2.1	2.5	2.5	1.9	2.2	1.9	2.5
Crude Oil, WTI (\$/Barrel)	62.9	68.1	69.7	59.4	58.3	59.7	61.1	62.4	50.8	65.0	60.4	64.6
Labor Markets												
Payroll Jobs (Millions)	148.1	148.7	149.3	149.9	150.4	150.9	151.4	151.8	146.6	149.0	151.1	152.6
Percent Change Annualized	1.7	1.7	1.7	1.6	1.3	1.3	1.3	1.1	1.6	1.6	1.4	1.0
Unemployment Rate (Percent)	4.1	3.9	3.8	3.7	3.6	3.5	3.4	3.4	4.4	3.9	3.5	3.5
Average Weekly Hours, Prod. Works.	33.7	33.8	33.8	33.8	33.8	33.8	33.8	33.8	33.7	33.8	33.8	33.8
Personal Income												
Average Hourly Earnings (\$)	22.40	22.58	22.75	22.93	23.12	23.32	23.51	23.70	22.05	22.66	23.41	24.18
Percent Change Annualized	2.8	3.3	3.1	3.2	3.4	3.4	3.3	3.3	2.3	2.8	3.3	3.3
Real Disp. Income (2012 Billions \$)	14219	14282	14365	14467	14531	14574	14615	14657	13949	14333	14594	14787
Percent Change Annualized	4.4	1.8	2.4	2.9	1.8	1.2	1.1	1.2	2.6	2.8	1.8	1.3
Housing												
Housing Starts (Ths., Ann. Rate)	1317	1261	1225	1236	1256	1272	1283	1292	1208	1260	1276	1311
Ext. Home Sales (Ths., Ann Rate)	5507	5413	5273	5375	5445	5479	5509	5534	5536	5392	5492	5603
New SF Home Sales (Ths., Ann Rate)	656	633	598	592	596	601	605	607	616	620	602	612
Case/Shiller HPI (Jan. 2000 = 100)	199.7	201.9	203.6	204.6	205.7	206.7	207.8	208.9	191.6	202.5	207.3	211.8
Percent Change Year Ago	6.4	6.3	5.7	4.3	3.0	2.3	2.0	2.1	5.8	5.7	2.4	2.2
Consumer												
Household Economic Stress Index	0.0	0.2	0.7	1.3	2.1	2.8	3.2	3.6	0.7	0.5	3.0	3.8
Auto Sales (Millions)	17.1	17.2	16.9	17.5	17.2	17.1	17.1	17.0	17.1	17.2	17.1	16.9
Consumer Credit (Billions \$)	3862	3899	3950	4003	4044	4086	4125	4165	3755	3929	4105	4277
Percent Change Annualized	3.3	3.8	5.4	5.5	4.1	4.2	3.9	4.0	5.6	4.6	4.5	4.2
Interest Rates (Percent)												
Prime Rate	4.53	4.80	5.01	5.28	5.50	5.53	5.78	6.00	4.10	4.90	5.70	6.00
Federal Funds	1.45	1.74	1.92	2.21	2.38	2.41	2.66	2.88	1.00	1.83	2.58	2.88
3-Month Treasury Bill	1.58	1.87	2.07	2.33	2.44	2.56	2.67	2.79	0.95	1.97	2.62	2.87
10-Year Treasury Note	2.76	2.92	2.92	3.22	3.35	3.35	3.34	3.34	2.33	2.96	3.35	3.29
30-Year Fixed Mortgage	4.27	4.54	4.57	4.91	5.00	5.00	4.99	4.99	3.99	4.57	5.00	4.94
a = actual f = forecast p = preliminary												

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