March 2019

NATIONAL ECONOMIC OUTLOOK

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Executive Summary

Weak February Job Growth, and Slow Retail Sales at the End of 2018

- The U.S. economy added just 20,000 jobs in February, far below consensus expectations for a gain of 180,000. This was the smallest number of net jobs created in a month since September 2017, when Hurricanes Harvey and Irma weighed on hiring. There were combined upward revisions of 12,000 in December and January. Private-sector hiring was 25,000 in February. Despite the very weak February report, job growth has averaged 186,000 over the past three months. The unemployment rate fell to 3.8 percent in February from 4.0 percent in January as government workers who had been on unpaid furlough because of the partial government shutdown, and were counted as unemployed in January, moved back into employed status. This is just slightly above the cyclical low unemployment rate of 3.7 percent in September and November of last year. Average hourly earnings rose 0.4 percent over the month after a gain of less than 0.1 percent in January. Year-over-year growth in wages was 3.4 percent in February, the strongest gain since March 2009.

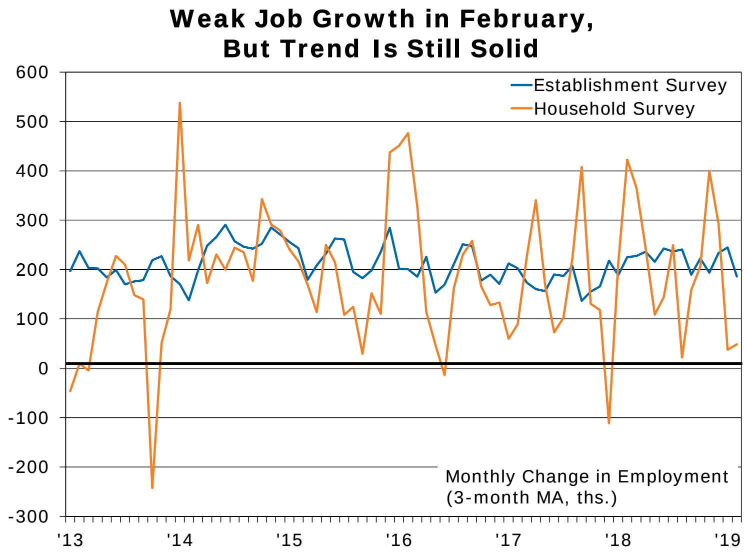
- U.S. gross domestic product, adjusted for inflation, increased 2.6 percent at an annual rate in the fourth quarter of 2018, better than the 2.4 percent consensus. This was the “initial” estimate from the Bureau of Economic Analysis. It combined the “advance” and “second” estimates; the advance estimate was canceled due to the partial government shutdown earlier this year. This was a solid result, although growth slowed from the second and third quarters. Real GDP increased 2.9 percent in 2018 from 2017, averaged across the four quarters of the year. On a year-over-year basis real GDP growth was 3.1 percent in the fourth quarter, up from 3.0 percent in the third quarter. Consumer spending and business investment led overall economic growth in the fourth quarter.

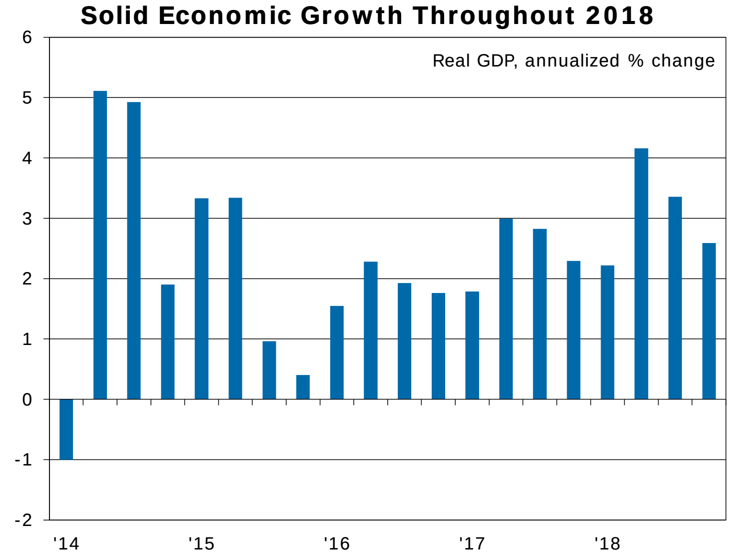
- Retail sales rose 0.2 percent in January, slightly better than the consensus expectation for a 0.1 percent increase. But this followed a huge 1.6 percent drop in December, revised even lower from the initially reported 1.2 percent decline. December was the biggest monthly drop since September 2009, after federal incentives for new car buyers expired. January details were better than the headline number. December’s decline does not appear to be related to data problems from the government shutdown. The big drop in stock prices in late 2018 may have spooked consumers.

*Baseline U.S. Economic Outlook, Summary Table**

	1Q'18a	2Q'18a	3Q'18p	4Q'18p	1Q'19f	2Q'19f	3Q'19f	4Q'19f	2017a	2018p	2019f	2020f
Output & Prices												
Real GDP (*Chained 2012 Billions $*)	18324	18512	18665	18785	18814	18952	19074	19180	18051	18571	19005	19399
Percent Change Annualized	**2.2**	**4.2**	**3.4**	**2.6**	**0.6**	**3.0**	**2.6**	**2.2**	**2.2**	**2.9**	**2.3**	**2.1**
CPI (*1982-84 = 100*)	249.3	250.6	251.8	252.8	253.3	255.0	256.6	258.1	245.1	251.1	255.8	261.8
Percent Change Annualized	**3.2**	**2.1**	**2.0**	**1.5**	**0.9**	**2.7**	**2.5**	**2.4**	**2.1**	**2.4**	**1.9**	**2.4**
Labor Markets												
Payroll Jobs (*Millions*)	148.0	148.7	149.4	150.1	150.7	151.2	151.6	152.0	146.6	149.1	151.3	152.7
Percent Change Annualized	**1.8**	**1.9**	**1.8**	**1.7**	**1.6**	**1.3**	**1.1**	**1.0**	**1.6**	**1.7**	**1.5**	**0.9**
Unemployment Rate (*Percent*)	4.1	3.9	3.8	3.8	3.9	3.7	3.6	3.5	4.4	3.9	3.7	3.6
Interest Rates (Percent)												
Federal Funds	1.45	1.74	1.92	2.22	2.40	2.40	2.40	2.40	1.00	1.83	2.40	2.40
Treasury Note, 10-year	2.76	2.92	2.92	3.04	2.66	2.62	2.63	2.64	2.33	2.91	2.64	2.63

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





Risk of Recession Is Low in 2019, But Likelihood Will Increase in 2020 and 2021

Although job growth was weak in February and retail sales plunged in December, overall the U.S. economy remains in solid shape in early 2019. With solid fundamentals the current U.S. economic expansion, now the second-longest in history, should continue at least through the rest of this year and into 2020. However, the risk of recession will increase in 2020 and again in 2021, as much of the support for the economy is coming from tax cuts and temporary increases in government spending; that fiscal stimulus is likely to turn into a drag on growth over the next couple of years.

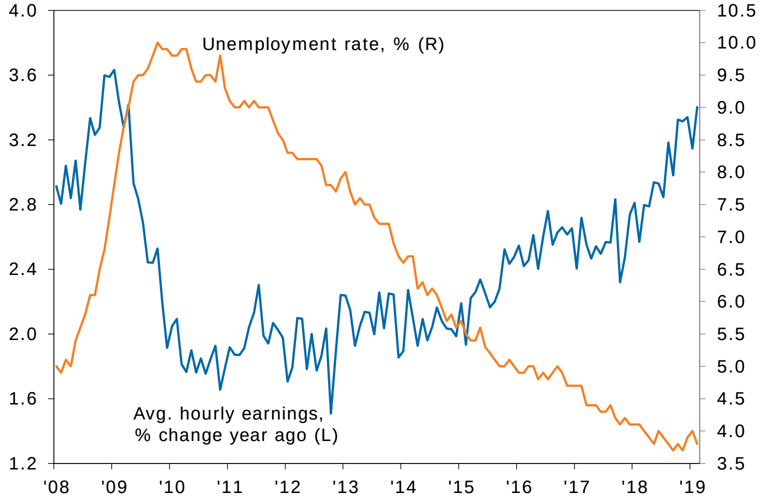
The current economic expansion started in June 2009, according to the National Bureau of Economic Research, which dates U.S. business cycles. If the current expansion lasts until mid-2019 it will become the longest in U.S. history; currently, the longest expansion lasted 120 months, from 1991 to 2001. Recessions are caused by imbalances in the economy, and right now there are few worrisome signs. Although job growth slipped in February, it has averaged better than 200,000 per month over the past year, well above what is needed to keep up with underlying growth in the labor force. And weekly initial unemployment insurance claims, a very timely labor market indicator, remain near a decades-long low. Despite the big drop in retail sales in December and weak January rebound, consumers are in good shape thanks to solid job growth, the best wage growth in a decade, and a high savings rate. As consumer spending accounts for about two-thirds of the economy, the expansion should continue as long as the labor market holds up. Business investment is also in good shape, as profitability is good and firms feel confident and need to invest to increase output. The corporate and personal income tax cuts passed at the end of 2017 and a big increase in federal spending legislated in 2018 are providing fiscal stimulus to the economy this year. And with inflation low, the Federal Reserve has the flexibility to provide monetary stimulus to the U.S. economy if weakness does emerge.

The biggest risks to the economy in 2019 are therefore geopolitical. There are a number of things that could go wrong. A hard Brexit could cause a steep recession in Great Britain and the Eurozone, pushing the U.S. economy into recession. Or a trade war erupts between the U.S. and China, leading to a global downturn. Or a domestic political crisis, like a debt limit standoff, leads to plunge in the stock market and spooks U.S. consumers and businesses. PNC puts the probability of recession in 2019 at a low 15 percent.

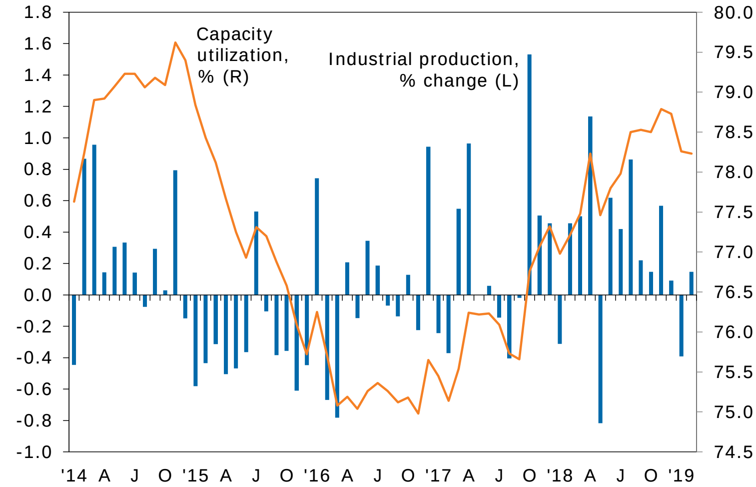
But the risk of recession will rise in 2020, and then again in 2021. The big reason is the withdrawal of fiscal stimulus. Right now the federal tax cuts and spending increases are fueling growth, but that positive impact will fade over the course of this year and into 2020, making the economy more vulnerable to an external shock. The Trump administration may try to avoid a recession in 2020, ahead of the presidential election, by attempting more fiscal stimulus, but by 2021 fiscal stimulus is likely to turn into fiscal drag. PNC puts the probability of a recession beginning by 2020 at 30 percent, and of one beginning by 2021 at about 50 percent. The baseline forecast calls for continued, albeit slower, economic growth over the next five years, because it is difficult to predict exactly when a recession will begin. But at some point over the next few years a recession will likely occur through some combination of economic excess; a policy mistake, either by the federal government or the Federal Reserve; and an external shock.

After growth of 2.9 percent in 2018, the U.S. economy should expand 2.3 percent this year. Growth was soft in the first quarter because of the partial federal government shutdown, will rebound in the second quarter, and then slow in the second half of this year as fiscal stimulus wears off. Monthly job growth will slow to around 150,000 in 2019 because of the tight labor market. The unemployment rate will fall slowly to end this year at around 3.5 percent, then rise a bit in 2020 with slower economic growth. With inflation slowing thanks to a big drop in energy prices, the Federal Open Market Committee signaled at its March 20 rate decision that policymakers do not expect to raise the target for the federal funds rate in 2019, and could be done raising interest rates for this cycle. Inflation will soften in the first half of 2019, then gradually trend higher toward the Federal Reserve's 2 percent objective.

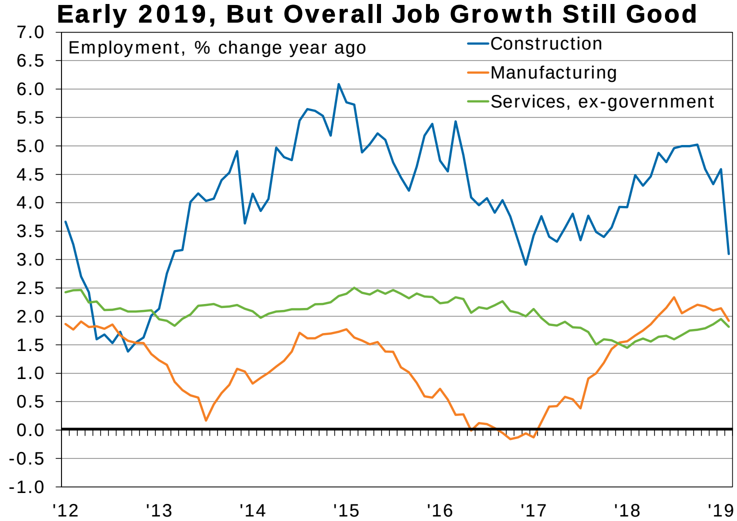
Tight Labor Market Spurs Strongest Wage Growth in a Decade



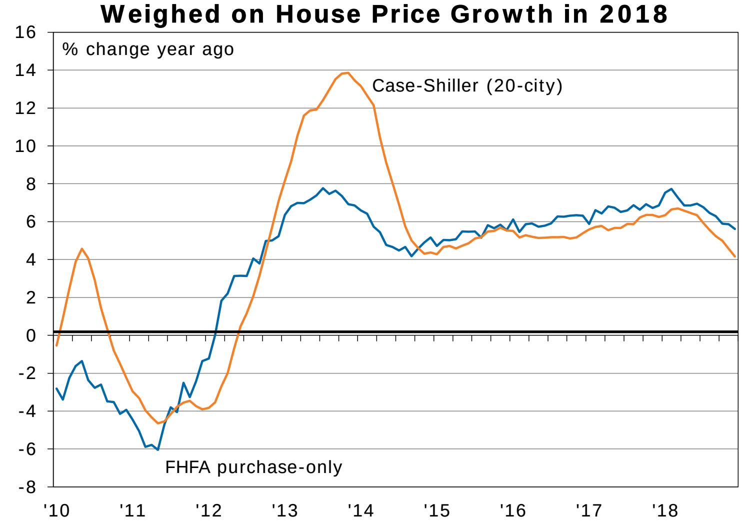
Some Softness in the Industrial Sector in Early 2019



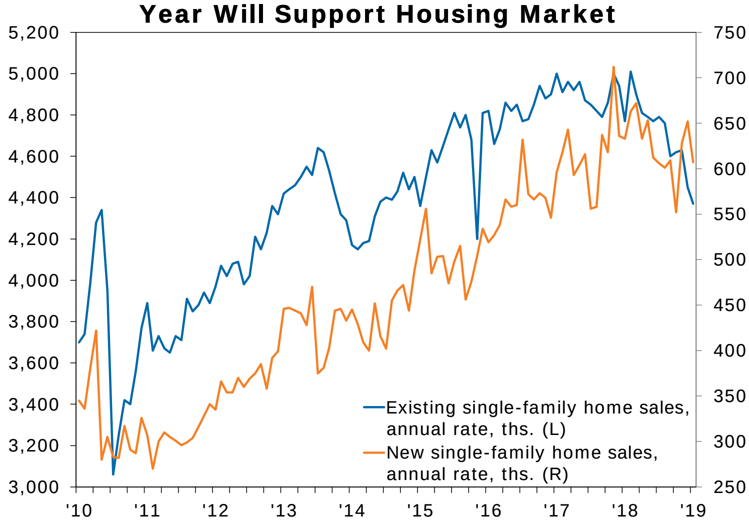
Weather Distorted Construction Activity in Early 2019, But Overall Job Growth Still Good



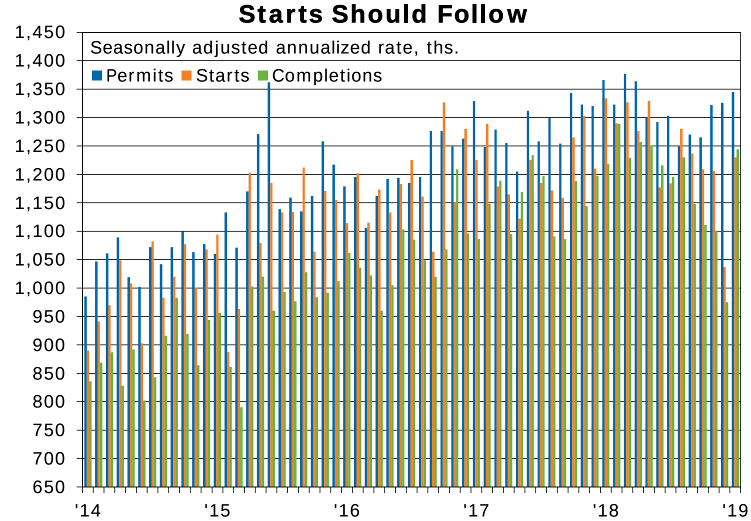
Tax Changes, Higher Mortgage Rates Weighed on House Price Growth in 2018



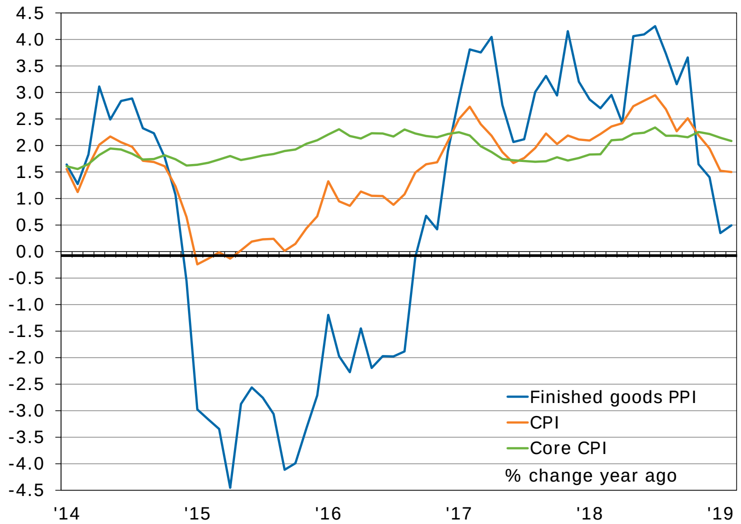
Lower Mortgage Rates So Far This Year Will Support Housing Market



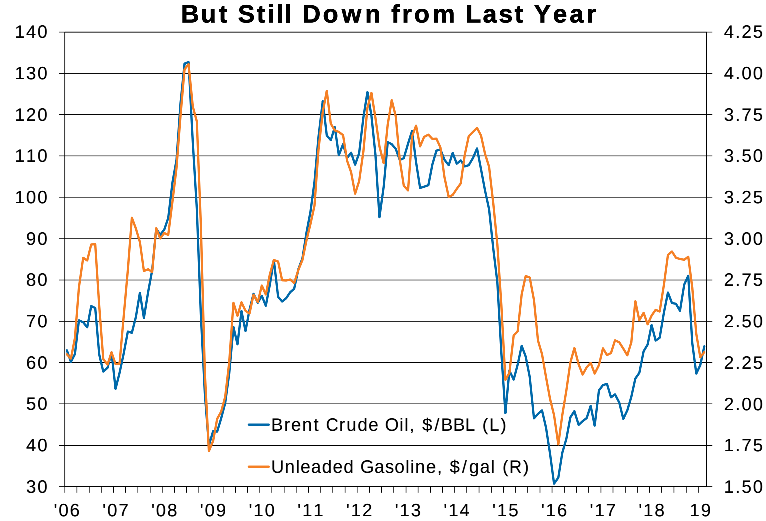
With Higher Permits, Housing Starts Should Follow



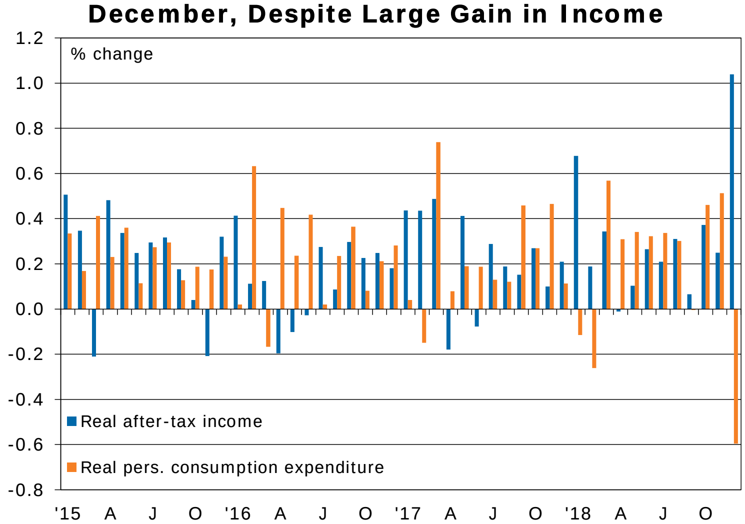
Lower Inflation Allows Fed to Be Patient



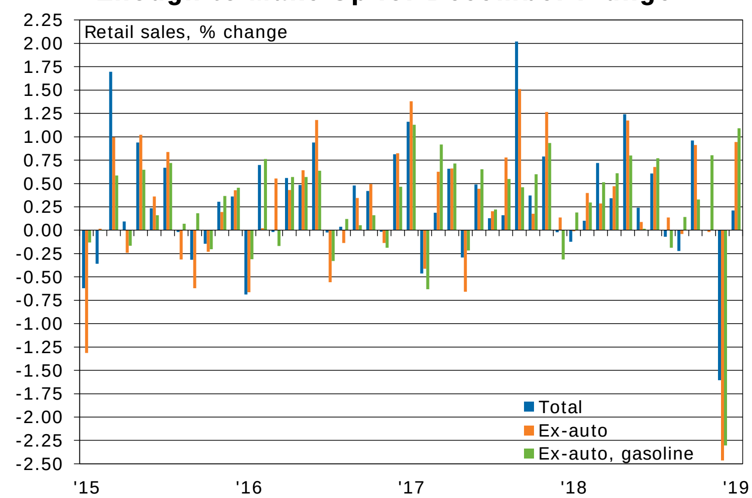
Energy Prices Up in February, But Still Down from Last Year



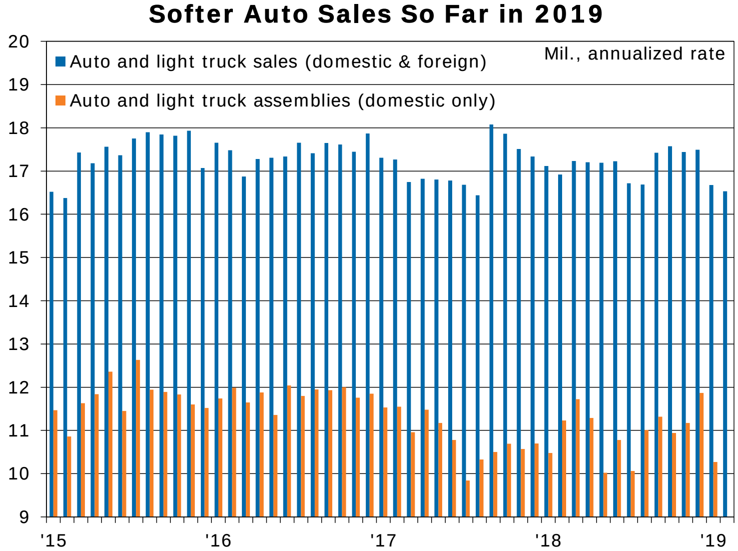
Big Drop in Consumer Spending in December, Despite Large Gain in Income



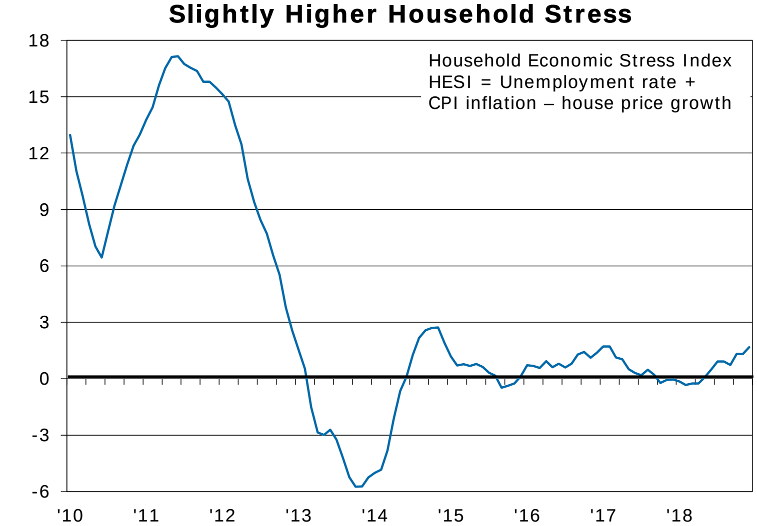
January Bounceback in Retail Sales Not Enough to Make Up for December Plunge



Softer Auto Sales So Far in 2019



Slower House Price Growth Means Slightly Higher Household Stress



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PNC Economics Group
March, 2019

Baseline U.S. Economic Outlook, Expanded Table

	1Q'18a	2Q'18a	3Q'18p	4Q'18p	1Q'19f	2Q'19f	3Q'19f	4Q'19f	2017a	2018p	2019f	2020f
Output												
Nominal GDP (*Billions $*)	20041	20412	20658	20891	20990	21249	21498	21745	19485	20501	21371	22293
Percent Change Annualized	**4.3**	**7.6**	**4.9**	**4.6**	**1.9**	**5.0**	**4.8**	**4.7**	**4.2**	**5.2**	**4.2**	**4.3**
Real GDP (*Chained 2012 Billions $*)	18324	18512	18665	18785	18814	18952	19074	19180	18051	18571	19005	19399
Percent Change Annualized	**2.2**	**4.2**	**3.4**	**2.6**	**0.6**	**3.0**	**2.6**	**2.2**	**2.2**	**2.9**	**2.3**	**2.1**
Pers. Consumption Expenditures	12723	12842	12953	13044	13073	13165	13242	13313	12559	12891	13198	13467
Percent Change Annualized	**0.5**	**3.8**	**3.5**	**2.8**	**0.9**	**2.8**	**2.4**	**2.2**	**2.5**	**2.6**	**2.4**	**2.0**
Nonresidential Fixed Investment	2654	2710	2727	2768	2796	2830	2861	2886	2538	2715	2843	2929
Percent Change Annualized	**11.5**	**8.7**	**2.5**	**6.2**	**4.1**	**4.9**	**4.4**	**3.6**	**5.3**	**7.0**	**4.7**	**3.0**
Residential Investment	615	613	608	602	606	607	609	613	611	610	609	622
Percent Change Annualized	**-3.4**	**-1.3**	**-3.6**	**-3.5**	**2.2**	**0.8**	**1.8**	**2.3**	**3.3**	**-0.2**	**-0.2**	**2.2**
Change in Private Inventories	30	-37	90	97	66	61	54	50	23	45	58	45
Net Exports	-902	-841	-950	-963	-964	-977	-988	-998	-859	-914	-982	-996
Government Expenditures	3152	3172	3192	3195	3197	3226	3256	3276	3130	3178	3239	3291
Percent Change Annualized	**1.5**	**2.5**	**2.6**	**0.4**	**0.2**	**3.7**	**3.7**	**2.6**	**-0.1**	**1.5**	**1.9**	**1.6**
Industrial Prod. Index (*2012 = 100*)	105.9	107.3	108.6	109.8	109.9	110.7	111.3	111.7	103.7	107.9	110.9	112.3
Percent Change Annualized	**2.5**	**5.2**	**4.9**	**4.6**	**0.4**	**2.9**	**2.1**	**1.5**	**1.6**	**4.0**	**2.8**	**1.2**
Capacity Utilization (*Percent*)	77.2	77.8	78.3	78.8	78.9	79.4	79.8	80.1	76.1	78.0	79.5	80.5
Prices												
CPI (*1982-84 = 100*)	249.3	250.6	251.8	252.8	253.3	255.0	256.6	258.1	245.1	251.1	255.8	261.8
Percent Change Annualized	**3.2**	**2.1**	**2.0**	**1.5**	**0.9**	**2.7**	**2.5**	**2.4**	**2.1**	**2.4**	**1.9**	**2.4**
Core CPI Index (1982-84 = 100)	255.7	256.9	258.2	259.6	260.9	262.2	263.5	264.8	252.2	257.6	262.9	268.1
Percent Change Annualized	**2.7**	**1.9**	**2.0**	**2.2**	**2.1**	**2.0**	**2.0**	**2.0**	**1.8**	**2.1**	**2.1**	**2.0**
PCE Price Index (*2012 = 100*)	107.5	108.1	108.5	108.9	109.1	109.7	110.3	110.9	106.1	108.2	110.0	112.2
Percent Change Annualized	**2.5**	**2.0**	**1.6**	**1.5**	**0.7**	**2.3**	**2.2**	**2.1**	**1.8**	**2.0**	**1.6**	**2.0**
Core PCE Price Index (*2012 = 100*)	109.2	109.8	110.2	110.7	111.2	111.6	112.1	112.5	108.0	110.0	111.8	113.7
Percent Change Annualized	**2.2**	**2.1**	**1.6**	**1.7**	**1.7**	**1.6**	**1.6**	**1.6**	**1.6**	**1.9**	**1.7**	**1.7**
GDP Price Index (*2012 = 100*)	109.4	110.3	110.7	111.2	111.6	112.1	112.7	113.4	107.9	110.4	112.5	115.0
Percent Change Annualized	**2.0**	**3.3**	**1.5**	**2.0**	**1.3**	**2.1**	**2.2**	**2.4**	**1.9**	**2.3**	**1.9**	**2.2**
Crude Oil, WTI (*$/Barrel*)	62.9	68.1	69.7	59.5	55.4	59.3	60.7	62.1	50.8	65.0	59.4	64.2
Labor Markets												
Payroll Jobs (*Millions*)	148.0	148.7	149.4	150.1	150.7	151.2	151.6	152.0	146.6	149.1	151.3	152.7
Percent Change Annualized	**1.8**	**1.9**	**1.8**	**1.7**	**1.6**	**1.3**	**1.1**	**1.0**	**1.6**	**1.7**	**1.5**	**0.9**
Unemployment Rate (*Percent*)	4.1	3.9	3.8	3.8	3.9	3.7	3.6	3.5	4.4	3.9	3.7	3.6
Average Weekly Hours, Prod. Works.	33.7	33.8	33.8	33.7	33.7	33.7	33.7	33.7	33.7	33.7	33.7	33.7
Personal Income												
Average Hourly Earnings ($)	22.42	22.61	22.79	22.99	23.18	23.38	23.57	23.76	22.05	22.70	23.47	24.24
Percent Change Annualized	**3.2**	**3.6**	**3.2**	**3.6**	**3.3**	**3.4**	**3.3**	**3.3**	**2.3**	**3.0**	**3.4**	**3.3**
Real Disp. Income (*2012 Billions $*)	14219	14281	14374	14523	14610	14630	14641	14657	13949	14350	14634	14720
Percent Change Annualized	**4.4**	**1.8**	**2.6**	**4.2**	**2.4**	**0.5**	**0.3**	**0.4**	**2.6**	**2.9**	**2.0**	**0.6**
Housing												
Housing Starts (*Ths., Ann. Rate*)	1317	1261	1234	1151	1229	1236	1239	1237	1208	1241	1235	1241
Ext. Home Sales (*Ths., Ann Rate*)	5507	5407	5307	5143	5039	5132	5232	5313	5531	5341	5179	5418
New SF Home Sales (*Ths., Ann Rate*)	656	633	605	590	614	616	620	622	616	621	618	625
Case/Shiller HPI (*Jan. 2000 = 100*)	199.7	201.9	203.6	206.0	207.8	209.3	210.7	211.8	191.6	202.8	209.9	214.6
Percent Change Year Ago	**6.4**	**6.4**	**5.7**	**5.0**	**4.1**	**3.7**	**3.5**	**2.8**	**5.8**	**5.9**	**3.5**	**2.3**
Consumer												
Household Economic Stress Index	-0.1	0.2	0.7	1.0	1.4	1.8	2.1	2.8	0.7	0.5	2.0	3.7
Auto Sales (*Millions*)	17.1	17.2	16.9	17.5	16.8	16.9	17.0	17.0	17.1	17.2	16.9	17.0
Consumer Credit (*Billions $*)	3863	3891	3957	4018	4031	4059	4082	4110	3758	3932	4070	4186
Percent Change Annualized	**3.3**	**3.0**	**6.9**	**6.3**	**1.3**	**2.8**	**2.3**	**2.7**	**5.6**	**4.6**	**3.5**	**2.8**
Interest Rates (Percent)												
Prime Rate	4.53	4.80	5.01	5.28	5.50	5.50	5.50	5.50	4.10	4.90	5.50	5.50
Federal Funds	1.45	1.74	1.92	2.22	2.40	2.40	2.40	2.40	1.00	1.83	2.40	2.40
3-Month Treasury Bill	1.58	1.87	2.07	2.36	2.41	2.38	2.33	2.28	0.95	1.97	2.35	2.25
10-Year Treasury Note	2.76	2.92	2.92	3.04	2.66	2.62	2.63	2.64	2.33	2.91	2.64	2.63
30-Year Fixed Mortgage	4.27	4.54	4.57	4.78	4.38	4.29	4.28	4.26	3.99	4.54	4.30	4.25

a = actual *f = forecast* *p = preliminary*

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