August 2021

NATIONAL ECONOMIC OUTLOOK

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Executive Summary

Real GDP Now Above Pre-Recession Level; Very Strong July Job Growth, With Big Drop in Unemployment Rate

- Real GDP increased 6.6% an annual rate in the second quarter, after growing 6.3% in the first quarter. Real GDP contracted a huge 10% (not annualized) in the first two quarters of 2020 as the pandemic came to the U.S., but has since increased for four consecutive quarters, and in the second quarter of 2021 was 0.8% above its 2019Q4 level. Thus total output of goods and services in the U.S. economy is now slightly higher than it was before the pandemic. Given that the Viral Recession was the largest downturn in the U.S. economy since the Great Depression, as measured by the decline in real GDP, the rebound has been extremely fast. Consumer spending on goods and services added 7.8 percentage points to annualized growth in the second quarter, with fixed business investment also a positive. Residential investment, trade, private inventories, and government spending were all drags on second quarter growth.

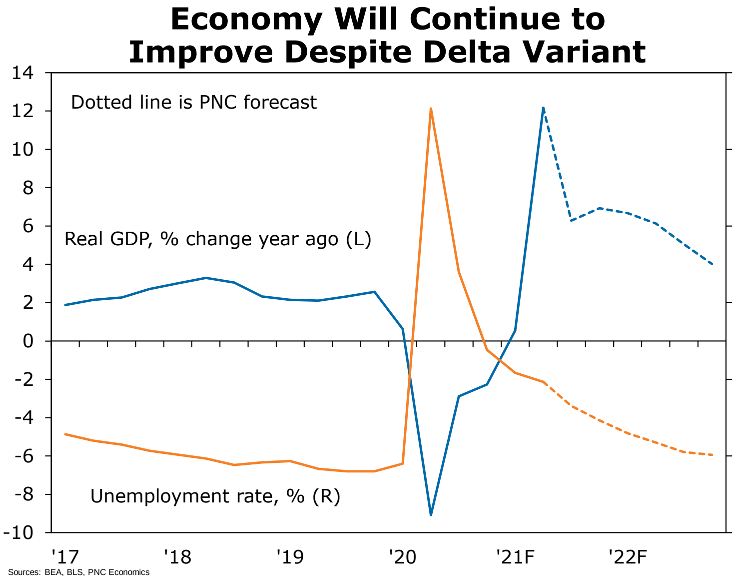
- The U.S. economy added 943,000 jobs in July, according to a survey of employers from the Bureau of Labor Statistics. This was the best month for job growth since August 2020. Job growth in June was revised sharply higher to 938,000 from 850,000, while May job growth was revised higher to 614,000 from 583,000, for a total upward revision of 119,000. The three-month moving average of job growth through July was 832,000, up from 607,000 in June and just 64,000 in January 2021, when there was a resurgence in the pandemic. At the current pace of job growth the U.S. economy would be back to its pre-pandemic level of employment in February 2022. The private sector added 703,000 jobs in July, while government employment was up by 240,000; almost all of those gains came from local government education as schools prepared to reopen fully.

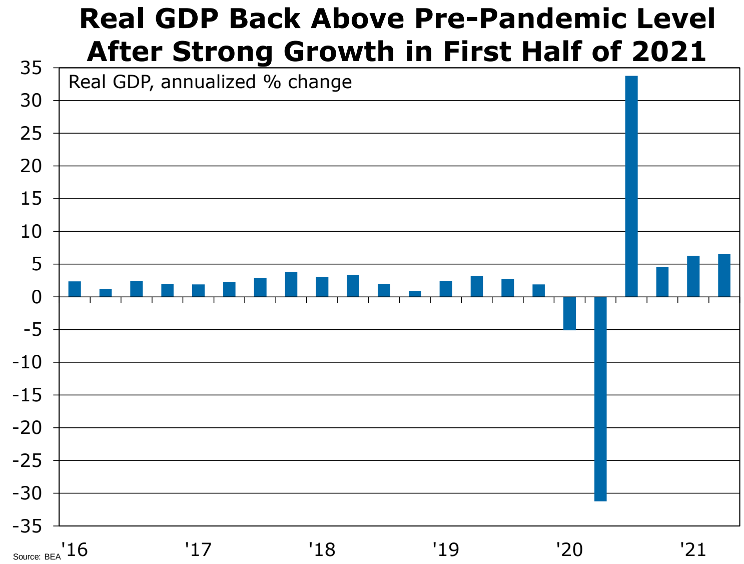
- The unemployment rate fell by 0.5 percentage point in July to 5.4%, the lowest rate since it was 3.5% in February 2020, before the pandemic. Employment in a survey of households (different from the survey of employers) rose by 1.043 million in July, the biggest one-month gain since October 2020. The labor force increased by 261,000 in July, with the labor force participation rate up by 0.1 percentage point to 61.7%. The labor force participation rate was above 63% before the pandemic. There are about 3 million fewer people in the U.S. labor force now than there were before the pandemic; labor force growth will need to pick up if the U.S. is to return to its pre-pandemic level of employment.

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

	1Q'21a	2Q'21p	3Q'21f	4Q'21f	1Q'22f	2Q'22f	2020a	2021f	2022f	2023f
Output & Prices										
Real GDP (*Chained 2012 Billions $*)	19056	19358	19726	20069	20328	20545	18385	19552	20618	21117
Percent Change Annualized	**6.3**	**6.5**	**7.8**	**7.1**	**5.3**	**4.3**	**-3.4**	**6.4**	**5.5**	**2.4**
CPI (*1982-84 = 100*)	263.4	268.8	273.3	274.9	276.0	277.6	258.8	270.1	278.6	286.2
Percent Change Annualized	**3.7**	**8.4**	**7.0**	**2.3**	**1.7**	**2.2**	**1.2**	**4.3**	**3.1**	**2.7**
Labor Markets										
Payroll Jobs (*Millions*)	143.4	145.0	147.2	149.4	151.4	153.1	142.3	146.2	153.4	156.5
Percent Change Annualized	**2.1**	**4.8**	**6.1**	**5.9**	**5.6**	**4.5**	**-5.7**	**2.8**	**4.9**	**2.1**
Unemployment Rate (*Percent*)	6.2	5.9	5.3	4.9	4.6	4.3	8.1	5.6	4.3	3.8
Interest Rates (Percent)										
Federal Funds	0.08	0.07	0.08	0.07	0.07	0.09	0.37	0.07	0.10	0.34
10-Year Treasury Note	1.30	1.58	1.35	1.56	1.67	1.70	0.89	1.45	1.72	1.87

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





Inventory Cycle Will Be Big Contributor to Near-Term Growth

U.S. economic growth was very strong in the first half of 2021, with inflation-adjusted GDP growth of 6.4% at an annual rate. But final demand growth was even stronger at 8.5%. GDP growth was weaker than final demand growth because inventories fell sharply in the first half of 2021 as businesses depleted their stocks. But inventories will shift from a drag on growth to a contributor to growth over the next few quarters as demand remains strong and supply chains normalize, allowing businesses to restock their shelves.

The level of inventories is the value of goods owned by private industries. Inventories may be products that a company sells but has yet to provide to purchasers, like finished goods in a warehouse or on a store shelf, or inputs into its production process, like iron ore for steel mills or packaging materials for a consumer goods company. Inventories are generally pro-cyclical, adding to economic growth during expansions and subtracting from growth during recessions. When demand is strong manufacturers want to have inputs on hand to make their products, and wholesalers and retailers want to have goods available for customers to buy. Alternatively during a recession, when demand is weak, manufacturers need fewer raw materials because of lower production, and wholesalers and retailers want to avoid having extra product sitting around that won't sell.

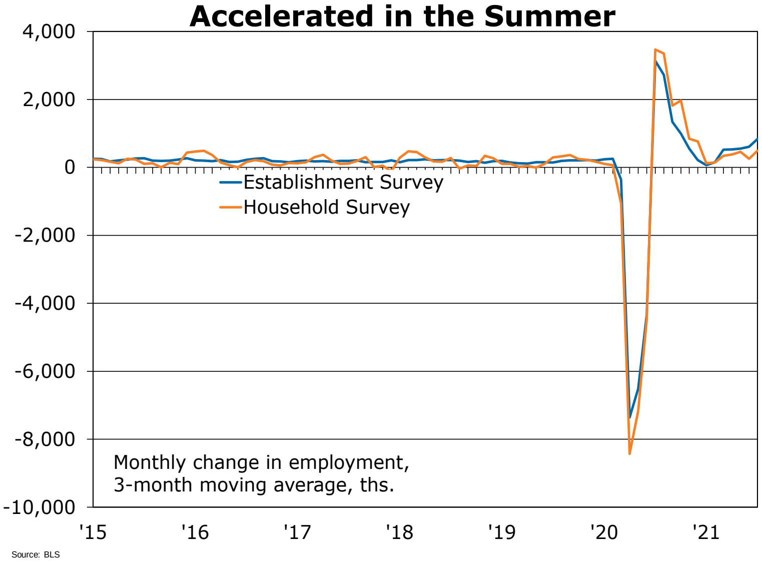
Inventories make up the difference between real GDP—total output of goods and services in the economy—and final demand—consumer and government demand for goods and services, fixed investment (by both businesses and in housing), and the trade balance. What matters for GDP growth is not the change in inventories, but the change in the change. So if businesses add to their inventories, but at a slower pace than in the previous quarter, inventories will subtract from GDP growth. Similarly, if businesses reduce their inventories, but the reduction is smaller than in the previous quarter, inventories are a positive for economic growth.

The importance of inventories to the U.S. economy has gradually declined over time for two reasons. First, goods have become less important to the economy as spending has shifted toward services. Second, businesses have adopted new processes, such as just-in-time production and online sales, to reduce their inventories relative to sales. Thus businesses are less likely now than in the past to have too much inventory heading into an economic downturn.

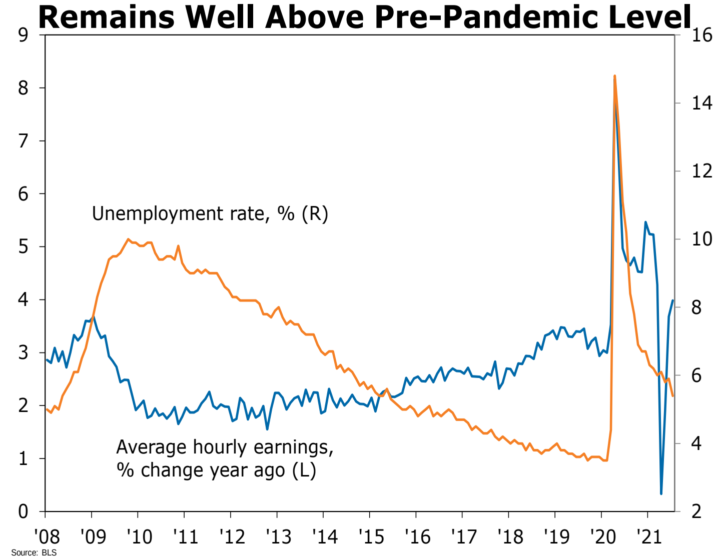
But despite this, inventories have been on a roller-coaster ride since the pandemic came to the United States. Businesses cut back sharply on inventories in the second quarter of last year as consumers stayed home and demand unexpectedly plummeted; inventories subtracted more than 4 percentage points from annualized growth in that quarter, the biggest drag in almost 40 years. Inventories then bounced back in the third quarter as consumer started to spend again. But inventories actually fell at an increasing pace in the first half of this year, subtracting almost 2 percentage points from annualized growth. Consumer demand for goods will remain strong as they spend their stimulus checks and start going to stores again thanks to vaccines. Business demand for goods is also very strong with firms investing again. With demand so strong businesses haven't been able to keep up. At the same time U.S. and global production bottlenecks are adding to inventory woes as manufacturers can't obtain inputs. For example, auto production is down because of a worldwide shortage of computer chips, despite very strong demand for new cars and trucks.

This drag will fade, however, and inventories should add to economic growth in the second half of this year and in early 2022 as demand growth slows somewhat and supply chains get back to normal. But there is a risk that production bottlenecks could last longer than expected, adding downside risk to the outlook. Consumer spending, business investment, homebuilding, and a stronger global economy will also support near-term growth. Real GDP will increase around 7% at an annualized rate in the second half of this year, and then around 4% in 2022, well above the economy's long-run average. PNC expects average monthly job growth of around 700,000 in the second half of 2021. The unemployment rate will continue to gradually decline, to around 5% by the end of this year and to around 4% by the end of next year. In addition to a delayed inventory cycle, a larger-than-expected drag from the delta variant or higher-than-expected inflation that would weigh on growth are other downside risks.

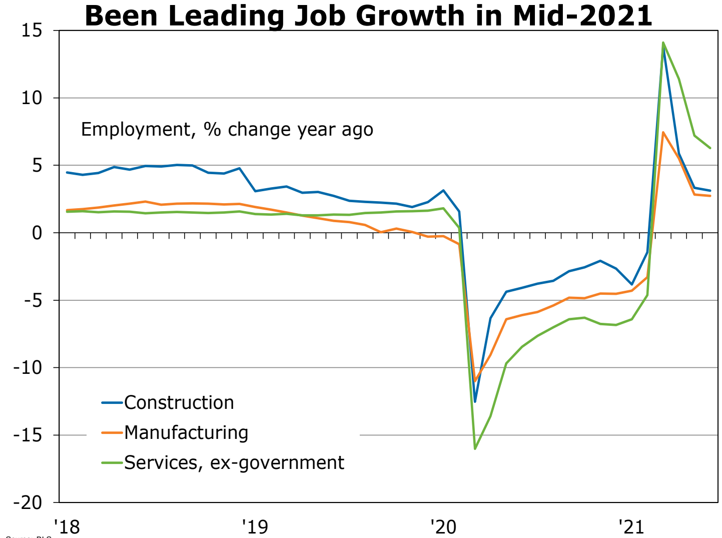
Labor Market Recovery Has Accelerated in the Summer



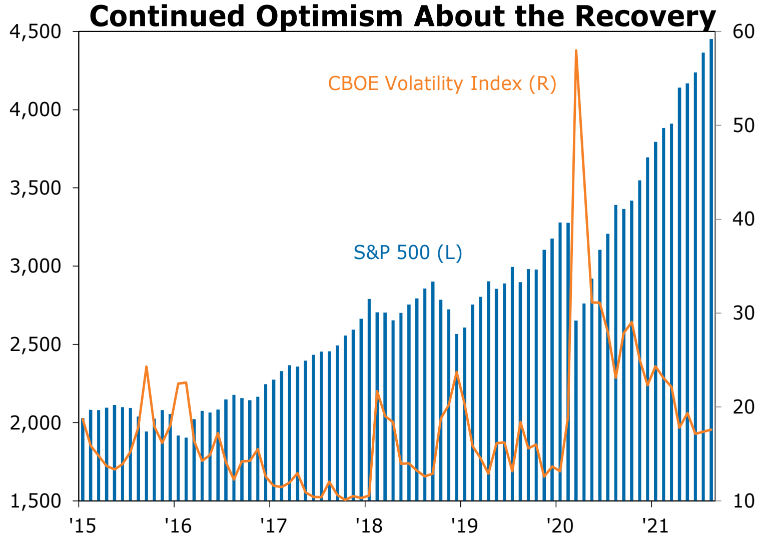
Unemployment Rate Continues to Fall, But Remains Well Above Pre-Pandemic Level



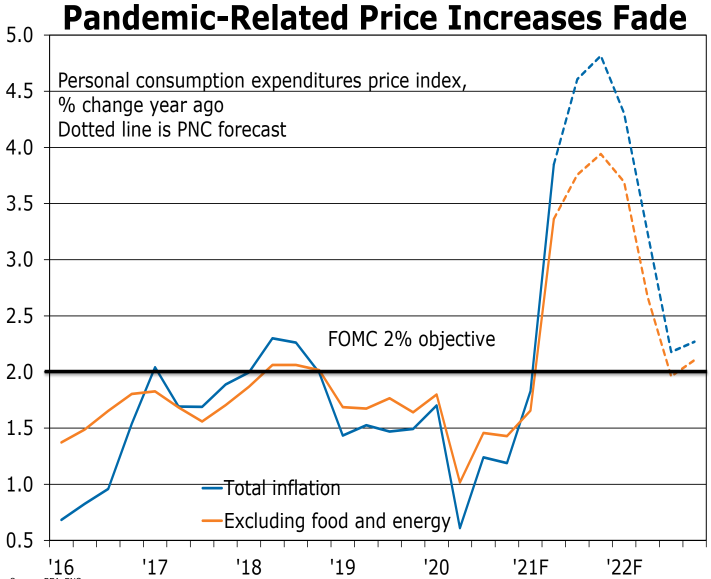
Leisure/Hospitality Services Has Been Leading Job Growth in Mid-2021



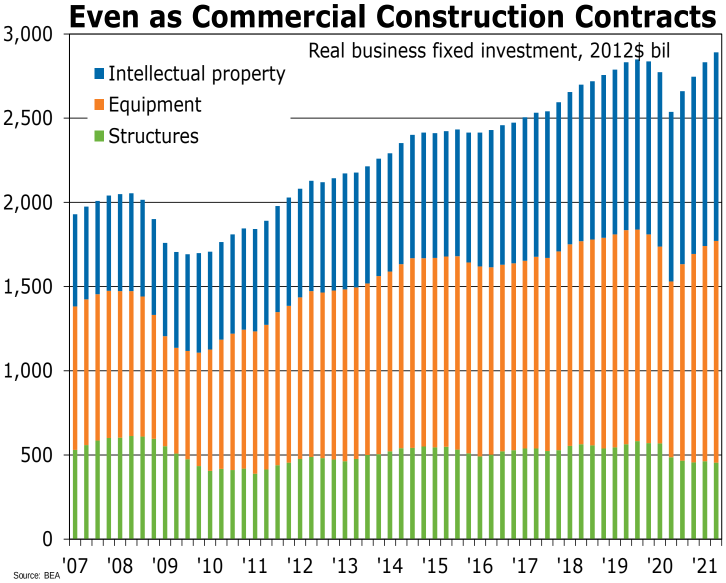
Record-High Stock Prices Indicate Continued Optimism About the Recovery



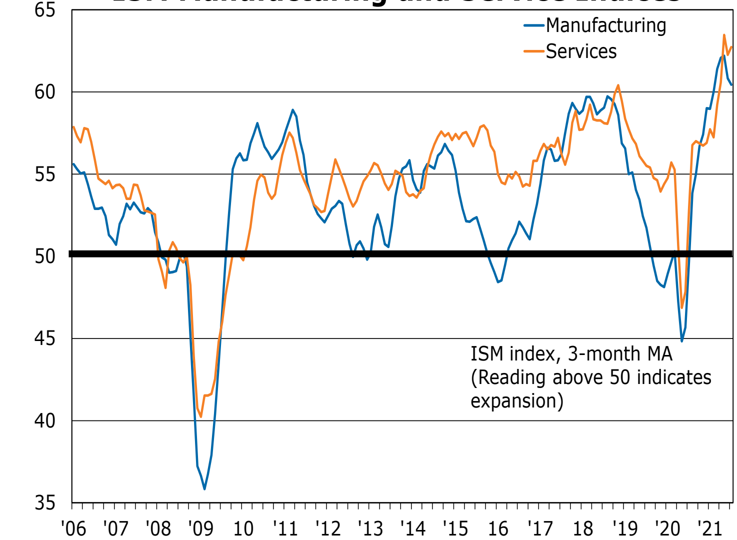
Inflation Will Slow Later This Year as Pandemic-Related Price Increases Fade



Business Investment Continues to Increase, Even as Commercial Construction Contracts

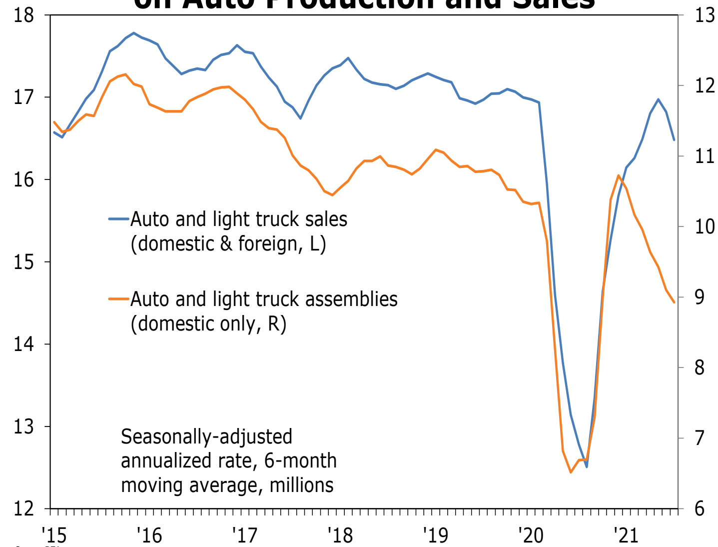


No Sign of Delta Variant Concerns in ISM Manufacturing and Service Indices



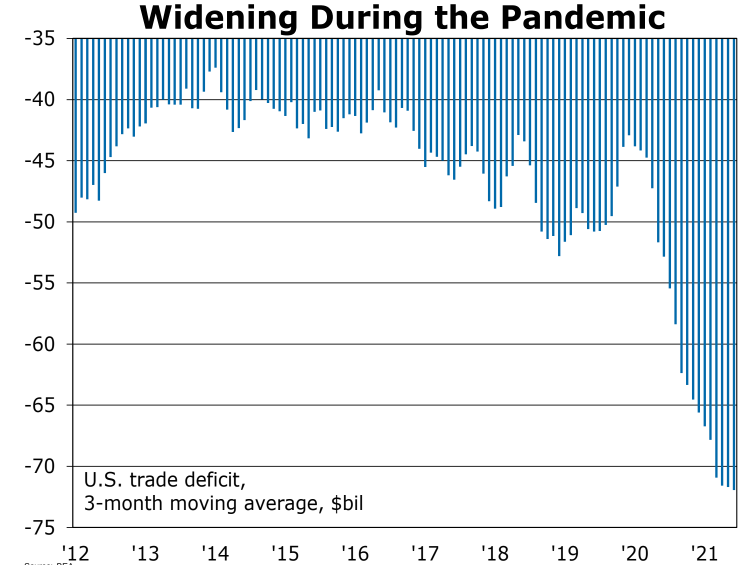
Source: ISM

Computer Chip Shortage Is Weighing on Auto Production and Sales



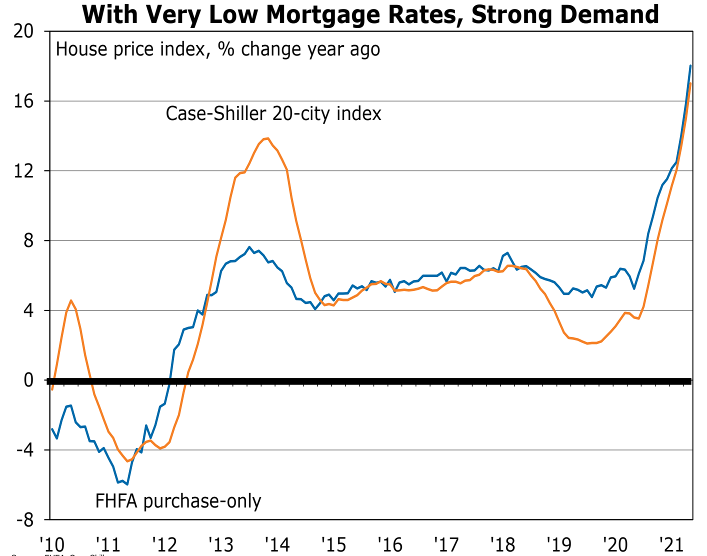
Source: BEA

Trade Deficit Has Stabilized After Widening During the Pandemic



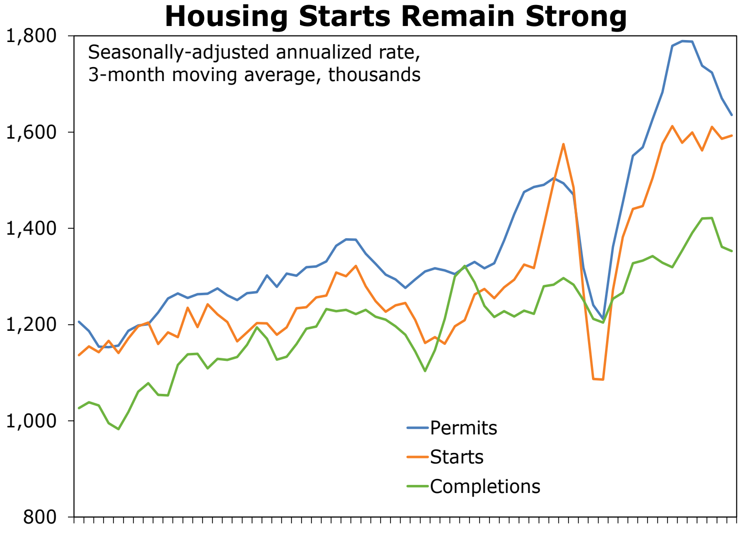
Source: BEA

House Price Growth Continues to Accelerate in Mid-2021 With Very Low Mortgage Rates, Strong Demand



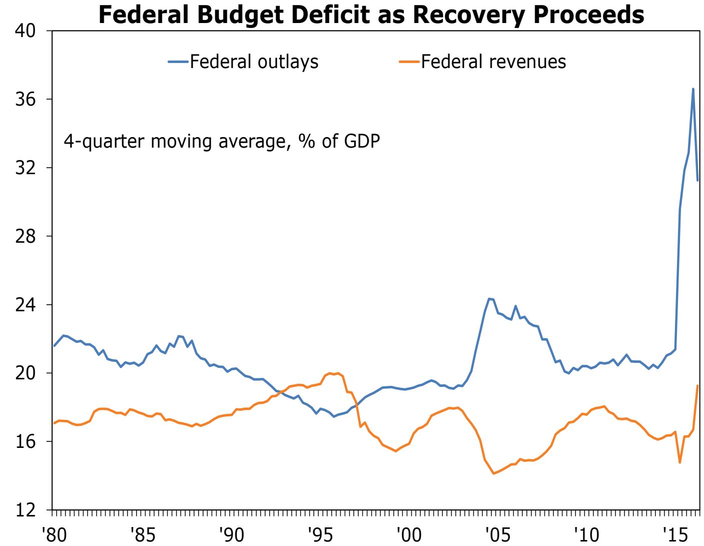
Sources: FHFA, Case-Shiller

Homebuilding Permits Have Fallen, But Housing Starts Remain Strong



Source: U.S. Census Bureau

Revenue Gains, Slower Spending Growth Will Reduce Federal Budget Deficit as Recovery Proceeds



Sources: U.S. Department of the Treasury, BEA

PNC Economics Group
August 2021

Baseline U.S. Economic Outlook, Expanded Table

	1Q'21a	2Q'21p	3Q'21f	4Q'21f	1Q'22f	2Q'22f	2020a	2021f	2022f	2023f
Output										
Nominal GDP (Billions $)	22038	22723	23503	24110	24575	24998	20894	23093	25180	26480
Percent Change Annualized	**10.9**	**13.0**	**14.5**	**10.7**	**7.9**	**7.1**	**-2.2**	**10.5**	**9.0**	**5.2**
Real GDP (Chained 2012 Billions $)	19056	19358	19726	20069	20328	20545	18385	19552	20618	21117
Percent Change Annualized	**6.3**	**6.5**	**7.8**	**7.1**	**5.3**	**4.3**	**-3.4**	**6.4**	**5.5**	**2.4**
Pers. Consumption Expenditures	13283	13659	13784	13927	14057	14155	12630	13663	14191	14487
Percent Change Annualized	**11.4**	**11.8**	**3.7**	**4.2**	**3.8**	**2.8**	**-3.8**	**8.2**	**3.9**	**2.1**
Nonresidential Fixed Investment	2810	2865	2929	3003	3068	3126	2671	2902	3141	3272
Percent Change Annualized	**12.9**	**8.0**	**9.2**	**10.5**	**8.8**	**7.8**	**-5.3**	**8.6**	**8.2**	**4.2**
Residential Investment	731	712	734	752	769	785	648	732	788	788
Percent Change Annualized	**13.3**	**-9.8**	**12.6**	**10.5**	**9.5**	**8.5**	**6.8**	**13.0**	**7.6**	**0.0**
Change in Private Inventories	-88	-166	-20	89	108	128	-42	-46	134	127
Net Exports	-1226	-1259	-1245	-1247	-1226	-1208	-943	-1244	-1200	-1135
Government Expenditures	3391	3378	3377	3376	3384	3391	3360	3380	3396	3410
Percent Change Annualized	**4.2**	**-1.5**	**-0.2**	**-0.1**	**0.9**	**0.9**	**2.5**	**0.6**	**0.5**	**0.4**
Industrial Prod. Index (2012 = 100)	98.2	99.6	102.0	103.5	104.7	105.7	95.0	100.8	105.9	107.5
Percent Change Annualized	**3.6**	**5.5**	**10.2**	**5.8**	**4.8**	**4.0**	**-7.2**	**6.2**	**5.1**	**1.5**
Capacity Utilization (Percent)	74.1	75.0	77.1	78.2	79.0	79.6	71.6	76.1	79.9	79.9
Prices										
CPI (1982-84 = 100)	263.4	268.8	273.3	274.9	276.0	277.6	258.8	270.1	278.6	286.2
Percent Change Annualized	**3.7**	**8.4**	**7.0**	**2.3**	**1.7**	**2.2**	**1.2**	**4.3**	**3.1**	**2.7**
Core CPI Index (1982-84 = 100)	270.5	275.9	280.3	281.8	282.9	284.4	267.7	277.1	285.5	294.0
Percent Change Annualized	**1.2**	**8.1**	**6.7**	**2.1**	**1.6**	**2.1**	**1.7**	**3.5**	**3.0**	**3.0**
PCE Price Index (2012 = 100)	113.0	114.8	116.6	117.3	117.9	118.5	111.2	115.4	118.9	121.8
Percent Change Annualized	**3.8**	**6.4**	**6.7**	**2.3**	**1.8**	**2.1**	**1.2**	**3.8**	**3.0**	**2.5**
Core PCE Price Index (2012 = 100)	115.0	116.7	118.2	118.8	119.3	119.8	113.6	117.2	120.2	123.2
Percent Change Annualized	**2.7**	**6.1**	**5.1**	**2.0**	**1.7**	**1.9**	**1.4**	**3.2**	**2.6**	**2.5**
GDP Price Index (2012 = 100)	115.7	117.4	119.1	120.1	120.9	121.7	113.6	118.1	122.1	125.4
Percent Change Annualized	**4.3**	**6.1**	**6.2**	**3.3**	**2.5**	**2.6**	**1.2**	**3.9**	**3.4**	**2.7**
Crude Oil, WTI ($/Barrel)	58.0	66.2	70.6	70.1	68.7	68.2	39.5	66.2	67.8	66.2
Labor Markets										
Payroll Jobs (Millions)	143.4	145.0	147.2	149.4	151.4	153.1	142.3	146.2	153.4	156.5
Percent Change Annualized	**2.1**	**4.8**	**6.1**	**5.9**	**5.6**	**4.5**	**-5.7**	**2.8**	**4.9**	**2.1**
Unemployment Rate (Percent)	6.2	5.9	5.3	4.9	4.6	4.3	8.1	5.6	4.3	3.8
Average Weekly Hours, Prod. Works.	34.3	34.3	34.2	34.1	34.1	34.0	33.9	34.2	34.0	33.8
Personal Income										
Average Hourly Earnings ($)	25.2	25.6	25.9	26.2	26.5	26.8	24.7	25.7	27.0	28.2
Percent Change Annualized	**3.8**	**6.2**	**5.1**	**4.2**	**4.9**	**4.9**	**5.0**	**4.2**	**4.8**	**4.5**
Real Disp. Income (2012 Billions $)	17304	15796	15431	15544	15681	15798	15676	16019	15858	16222
Percent Change Annualized	**57.6**	**-30.6**	**-8.9**	**3.0**	**3.6**	**3.0**	**6.2**	**2.2**	**-1.0**	**2.3**
Housing										
Housing Starts (*Ths., Ann. Rate*)	1599	1568	1562	1536	1576	1602	1397	1566	1593	1475
Ext. Home Sales (*Ths., Ann Rate*)	6303	5830	6391	6866	6680	6515	5657	6348	6392	5294
New SF Home Sales (*Ths., Ann Rate*)	896	728	693	707	715	709	828	756	699	632
Case/Shiller HPI (*Jan. 2000 = 100*)	241.9	254.4	263.1	268.7	271.4	272.9	232.5	268.7	274.3	276.3
Percent Change Year Ago	**12.2**	**16.7**	**18.1**	**15.6**	**12.2**	**7.3**	**9.4**	**15.6**	**2.1**	**0.7**
Consumer										
Auto Sales (Millions)	16.8	16.9	15.4	16.3	17.3	17.9	14.5	16.3	17.4	15.9
Consumer Credit (Billions $)	4224	4313	4368	4430	4500	4580	4186	4430	4734	5012
Percent Change Year Ago	**0.5**	**4.0**	**4.9**	**5.8**	**6.5**	**6.2**	**-0.3**	**5.8**	**6.8**	**5.9**
Interest Rates (Percent)										
Prime Rate	3.25	3.25	3.25	3.25	3.25	3.25	**3.54**	**3.25**	**3.25**	**3.46**
Federal Funds	0.08	0.07	0.08	0.07	0.07	0.09	**0.37**	**0.07**	**0.10**	**0.34**
3-Month Treasury Bill	0.04	0.01	0.05	0.08	0.10	0.12	**0.35**	**0.04**	**0.13**	**0.46**
10-Year Treasury Note	1.30	1.58	1.35	1.56	1.67	1.70	**0.89**	**1.45**	**1.72**	**1.87**
30-Year Fixed Mortgage	2.88	3.00	2.94	3.18	3.29	3.35	**3.11**	**3.00**	**3.37**	**3.57**

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

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