

NATIONAL ECONOMIC OUTLOOK

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Executive Summary

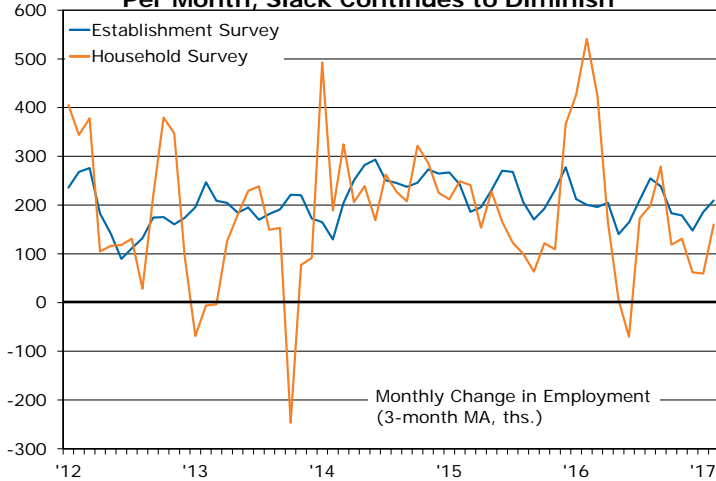
Another Fed Rate Hike in Early 2017 as Economic Expansion Continues

- The U.S. economy grew 1.9 percent at an annual rate in the fourth quarter of 2016, according to the second estimate from the Bureau of Economic Analysis. This was a slowing from the strong 3.5 percent pace of the third quarter, but growth was a solid 2.7 percent in the second half of last year, up from 1.1 percent in the first half. Despite slowing from the third quarter, consumer spending added 2.0 percentage points to annualized growth in the fourth quarter, as job gains and wage growth are supporting household incomes and consumption. Inventories were a positive for growth in the second half of the year, after being a weight for the previous five quarters. Trade was a big drag at the end of the year, subtracting 1.7 points from annualized growth, as a surge in soybean exports in the third quarter reversed. Business fixed investment and homebuilding both contributed modestly to fourth quarter growth.
- Payroll employment increased by 235,000 in February, with a combined net upward revision to job growth in December and January of 9,000. Job growth has averaged just over 200,000 over the past three months, a slight acceleration from the recent trend. The mild winter has boosted construction employment, although industry job growth will slow in the near term with a smaller-than-usual pickup in spring hiring. Manufacturing jobs rose by 28,000 in February, the third straight increase, while private service-providing industries added 136,000 jobs. The unemployment rate fell from 4.8 percent in January to 4.7 percent in February; the labor force increased as more people looked for a work, a positive, but there were even more jobs added according to the household survey (different from the survey of employers). Average hourly earnings rose 0.2 percent in February, and were up 2.8 percent from one year earlier; a tighter labor market is driving wage growth.
- The Federal Open Market Committee raised the Federal funds rate by 0.25 percentage point on March 15, to a range of 0.75 to 1.00 percent. After keeping the fed funds rate in a range of 0.00 to 0.25 percent from late 2008 to late 2015, and then holding it steady in a range of 0.25 to 0.50 percent for a year, the FOMC has now raised the rate at two of its last three meetings. After a decade of highly expansionary monetary policy, normalization is now underway. The projections released along with the FOMC statement are consistent with PNC's forecast for two more rate increases this year and three in 2018. The pace of rate hikes will be gradual compared to previous tightening cycles.

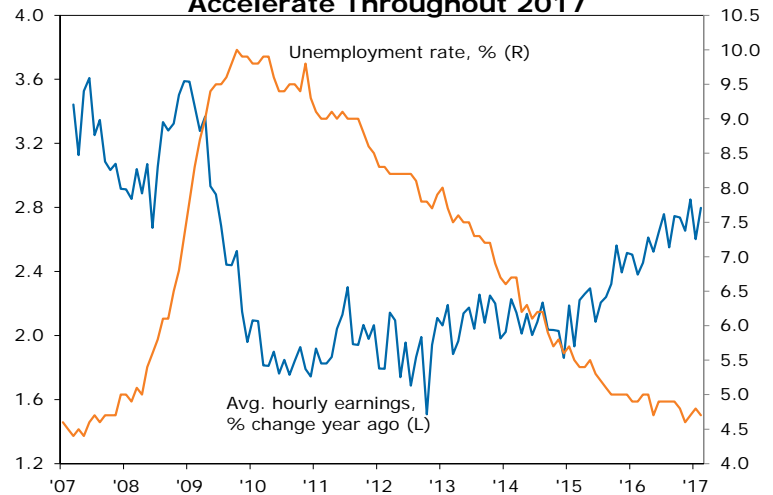
Baseline U.S. Economic Outlook, Summary Table*

	1Q'16a	2Q'16a	3Q'16a	4Q'16p	1Q'17f	2Q'17f	3Q'17f	4Q'17f	2015a	2016f	2017f	2018f
Output & Prices												
Real GDP (Chained 2009 Billions \$)	16525	16583	16727	16804	16851	16987	17117	17234	16397	16660	17047	17536
Percent Change Annualized	0.8	1.4	3.5	1.9	1.1	3.3	3.1	2.8	2.6	1.6	2.3	2.9
CPI (1982-84 = 100)	238.0	239.4	240.4	242.2	244.0	245.2	246.6	248.0	237.0	240.0	246.0	251.8
Percent Change Annualized	0.1	2.3	1.8	3.0	2.9	2.0	2.3	2.4	0.1	1.3	2.5	2.4
Labor Markets												
Payroll Jobs (Millions)	143.4	144.0	144.7	145.2	145.7	146.3	146.7	147.2	141.8	144.3	146.5	148.5
Percent Change Annualized	1.7	1.4	2.0	1.4	1.5	1.5	1.3	1.4	2.1	1.8	1.5	1.3
Unemployment Rate (Percent)	4.9	4.9	4.9	4.7	4.7	4.6	4.5	4.5	5.3	4.9	4.6	4.5
Interest Rates (Percent)												
Federal Funds	0.37	0.37	0.40	0.45	0.69	0.92	1.13	1.17	0.13	0.40	0.98	1.59
Treasury Note, 10-year	1.91	1.75	1.56	2.14	2.47	2.72	2.91	3.00	2.14	1.84	2.77	3.16
a = actual f = forecast p = preliminary * Please see the Expanded Table for more forecast series.												

With Job Growth Running at Around 200,000 Per Month, Slack Continues to Diminish



Wage Growth Will Continue to Accelerate Throughout 2017



Global Economic Growth Is Picking Up, But Strong Dollar Will Limit Benefit to the U.S.

The global economy is in better shape in 2017. The International Monetary Fund is forecasting inflation-adjusted global GDP growth of 3.4 percent, up from 3.1 percent last year. Much of the improvement is coming from Europe. Monetary policy from the European Central Bank has been very aggressive, with negative interest rates and massive quantitative easing—central bank purchases of financial assets in an effort to push down borrowing costs for households and businesses. A weakening in the euro has boosted Eurozone exports. Growth in the two biggest Eurozone economies, Germany and France, picked up at the end of 2016, and those gains appear to be continuing into 2017. Conditions in the United Kingdom are more tenuous. Although the fallout from the British referendum to leave the European Union (“Brexit”) has been limited so far, in part because the Bank of England cut interest rates to support the economy in the wake of the Brexit vote, some recent data has been weaker, suggesting that uncertainty may be weighing on investment and consumer spending.

The Japanese economy is also looking better this year. The Bank of Japan also implemented aggressive monetary policy, with a massive QE program buying up many of the country’s assets. Deflation has turned to inflation, a positive sign, although growth is lackluster. The Japanese economy faces many structural impediments, including a rapidly aging population and a shrinking workforce, but the economy should continue to expand over the next few years.

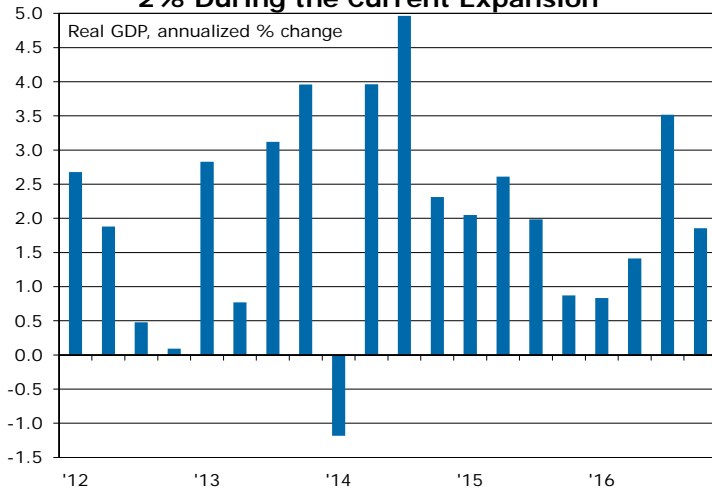
Growth in China has slowed over the past few years, but stabilized in 2016. Chinese authorities are trying to transition the economy away from growth led by exports and investment in infrastructure, and toward consumer spending. This has been tricky, and the government has supported the process through fiscal stimulus. But the effort appears to be working, and Chinese growth should remain at between 6 and 7 percent over the next few years. Other developing economies in Asia will benefit from stable growth in China. Commodity-producing economies were hit hard by the downturn in global commodity prices from late 2014 to early 2016, with a very deep recession in Brazil (exacerbated by political problems), substantial problems elsewhere in Latin America, and downturns in Russia and South Africa. But the worst appears to be over now that commodity prices have moved higher, with OPEC production cuts supporting oil prices.

Although U.S. economic performance has been mediocre over the past few years, it has led among developed economies. With the Federal Reserve gradually raising interest rates since late 2015, while other central banks have been keeping rates very low, the U.S. dollar appreciated by 25 percent against a basket of global currencies between mid-2014 and late 2016. This strong dollar makes U.S. exports abroad more expensive, and imports into the U.S. less expensive, boosting global growth, but also increasing the U.S. trade deficit. Growth has slowed in commodity-dependent Canada and Mexico, but both nations have benefitted from their trade ties with the United States.

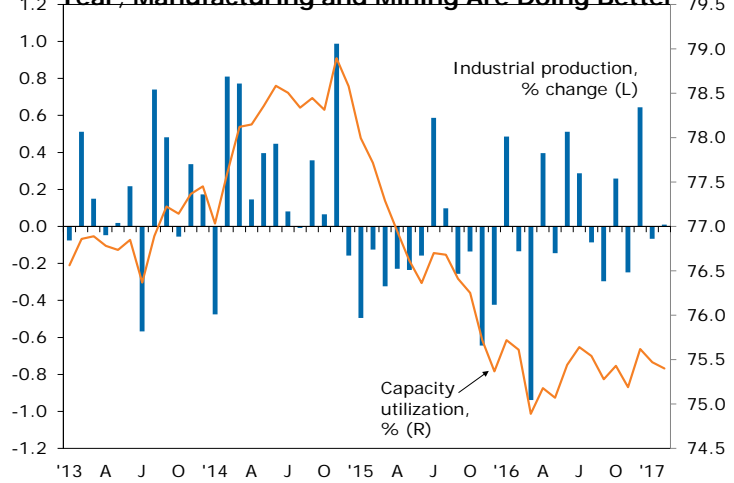
Although global growth is expected to pick up this year, there are many downside risks to the outlook. Political upheaval, led by anti-globalist sentiment, could cause instability. Trump administration policies could spark a global trade war, slowing growth around the world. China could start to slow again, leading to weaker economies throughout Asia. And problems could intensify in the European banking system, sparking another financial crisis.

Although an expanding global economy will support U.S. exports, the strong dollar will limit the gain. At the same time, the strong dollar and growth in consumer spending will boost imports, and the U.S. trade deficit will widen by about 7 percent this year, creating a drag on growth. However, the U.S. economic expansion will continue for an eighth straight year. Consumer spending will increase thanks to higher incomes from more jobs and rising wages, as well as likely tax cuts, and housing will be another positive for the domestic economy. U.S. real GDP growth will accelerate from 1.6 percent in 2016 to 2.3 percent this year, and to 2.9 percent in 2018. Job growth will slow slightly to around 170,000 per month this year, not because of weaker demand for labor, but from more difficulty in finding workers with the necessary skills. The U.S. will approach full employment late this year, with the unemployment rate settling in near its long-run level of 4.5 percent. With rising wages, consumer price inflation will gradually accelerate over the next few years. To avoid a more sustained pickup in inflation, the Federal Open Market Committee will increase the Federal funds rate another two times this year, likely at its June and December meetings, and three times in 2018, by 0.25 percentage point each time.

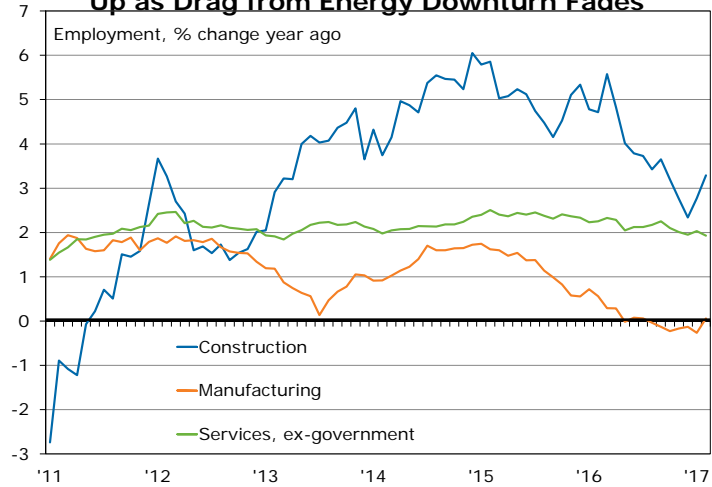
Annual Economic Growth of About 2% During the Current Expansion



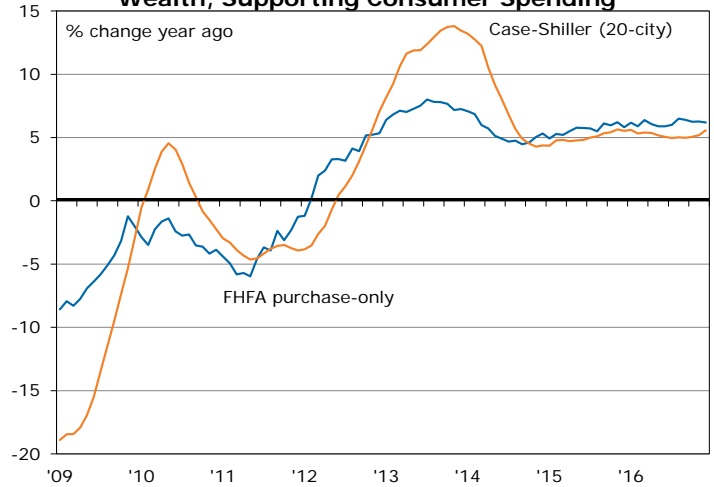
Warm Weather Has Weighed on Utilities Production This Year; Manufacturing and Mining Are Doing Better



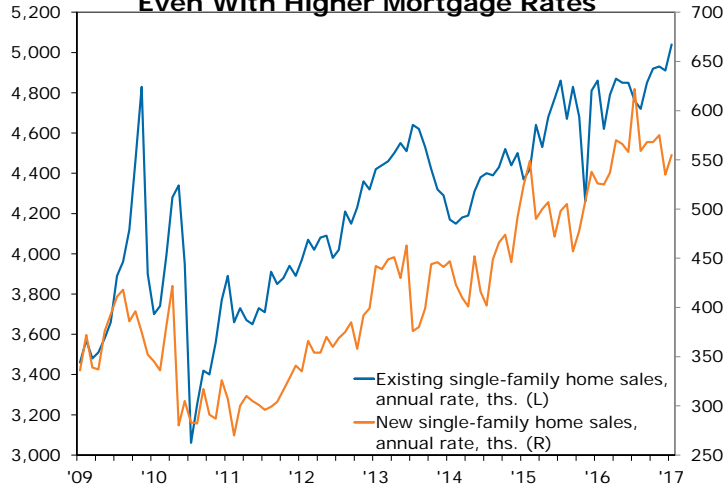
Manufacturing Employment Is Picking Back Up as Drag from Energy Downturn Fades



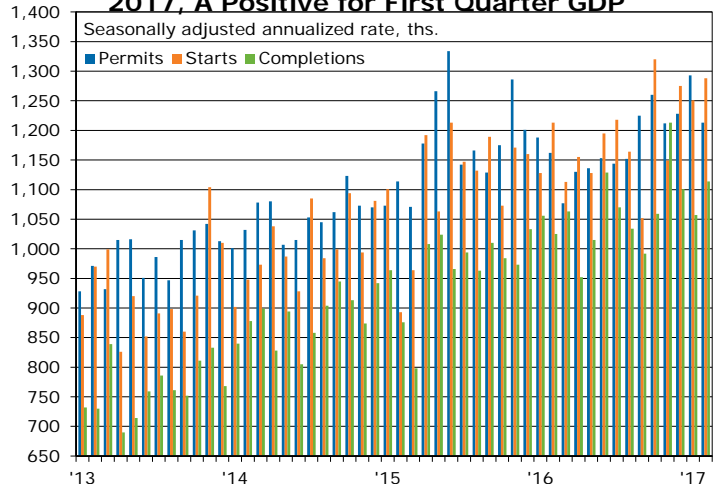
Steady House Price Gains Adding to Household Wealth, Supporting Consumer Spending



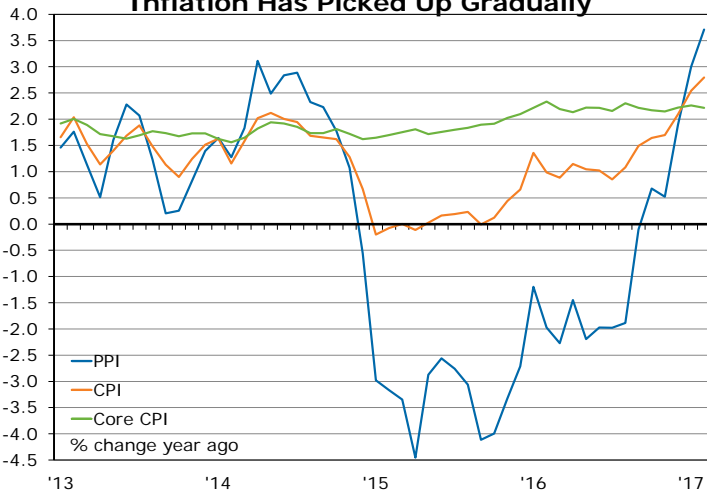
Home Sales Continue to Improve Even With Higher Mortgage Rates



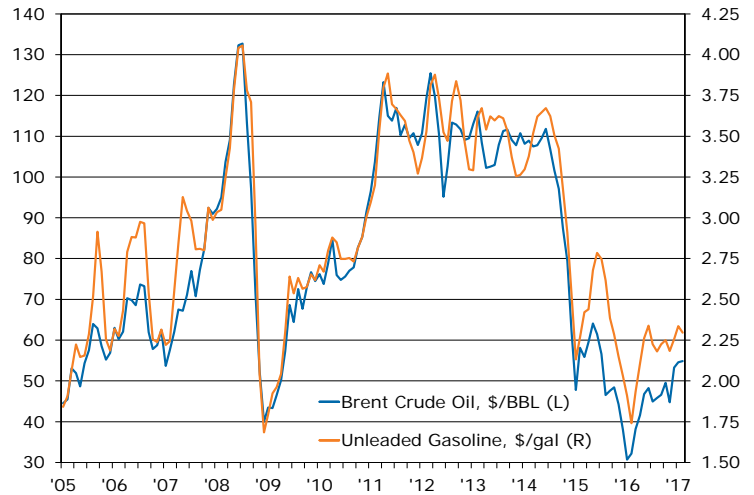
Mild Winter Boosted Housing Starts in Early 2017, A Positive for First Quarter GDP



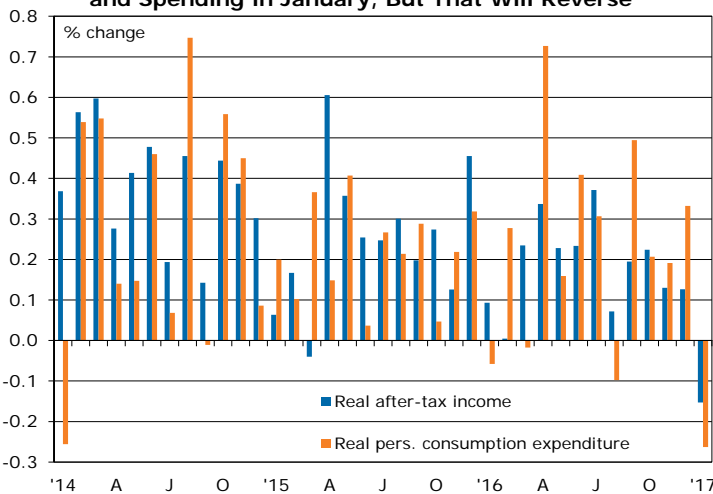
Fed Is Raising Rates as Core Inflation Has Picked Up Gradually



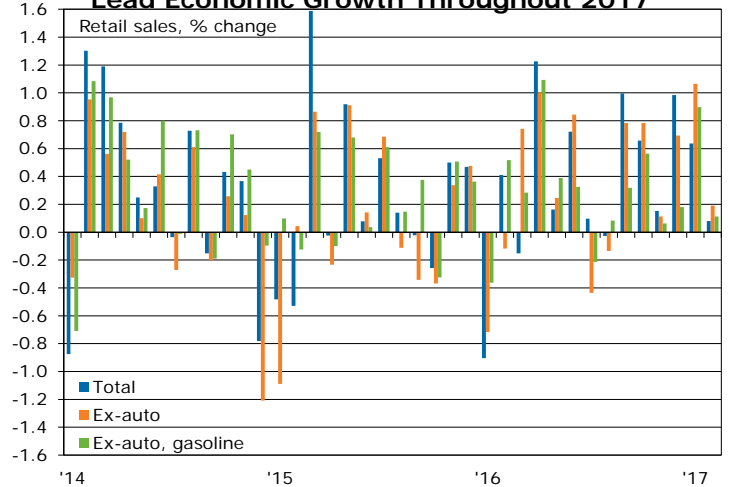
Oil Has Stabilized at Around \$50 Per Barrel in Early 2017



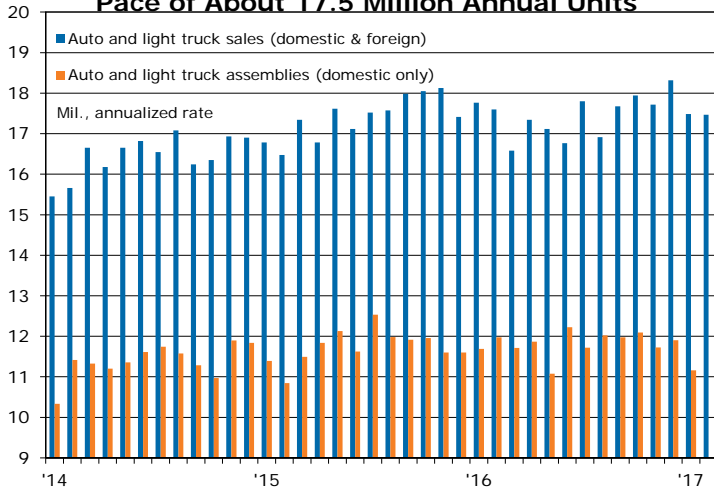
Higher Energy Prices Pushed Down After-Inflation Incomes and Spending in January, But That Will Reverse



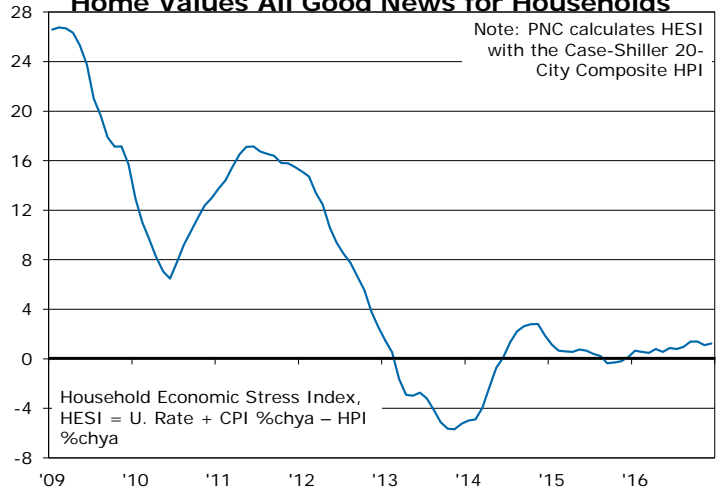
Consumer Spending Will Continue to Lead Economic Growth Throughout 2017



Auto Sales Settling In at Sustainable Pace of About 17.5 Million Annual Units



Low Unemployment, Low Inflation, Rising Home Values All Good News for Households



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PNC Economics Group
March, 2017

Baseline U.S. Economic Outlook, Expanded Table

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Output												
Nominal GDP (Billions \$)	18282	18450	18675	18856	19024	19250	19490	19723	18037	18566	19372	20325
Percent Change Annualized	1.3	3.7	5.0	3.9	3.6	4.9	5.1	4.9	3.7	2.9	4.3	4.9
Real GDP (Chained 2009 Billions \$)	16525	16583	16727	16804	16851	16987	17117	17234	16397	16660	17047	17536
Percent Change Annualized	0.8	1.4	3.5	1.9	1.1	3.3	3.1	2.8	2.6	1.6	2.3	2.9
Pers. Consumption Expenditures	11365	11485	11569	11655	11707	11794	11870	11939	11215	11519	11828	12125
Percent Change Annualized	1.6	4.3	3.0	3.0	1.8	3.0	2.6	2.3	3.2	2.7	2.7	2.5
Nonresidential Fixed Investment	2180	2185	2193	2200	2217	2239	2261	2283	2200	2189	2250	2325
Percent Change Annualized	-3.4	1.0	1.4	1.3	3.1	4.1	4.1	3.9	2.1	-0.5	2.8	3.3
Residential Investment	601	589	583	596	603	611	617	622	565	592	613	633
Percent Change Annualized	7.8	-7.8	-4.1	9.6	4.9	5.4	4.0	3.5	11.7	4.9	3.6	3.2
Change in Private Inventories	41	-10	7	46	40	47	55	58	84	21	50	60
Net Exports	-566	-559	-522	-600	-630	-631	-635	-640	-540	-562	-634	-642
Government Expenditures	2913	2901	2906	2909	2916	2928	2950	2974	2884	2907	2942	3037
Percent Change Annualized	1.6	-1.7	0.8	0.3	1.0	1.7	3.0	3.2	1.8	0.8	1.2	3.2
Industrial Prod. Index (2012 = 100)	104.1	103.9	104.4	104.5	105.0	105.6	106.3	106.9	105.2	104.2	106.0	108.6
Percent Change Annualized	-1.7	-0.8	1.7	0.4	2.0	2.3	2.7	2.4	0.3	-0.9	1.7	2.5
Capacity Utilization (Percent)	75.4	75.2	75.5	75.4	75.6	75.8	76.1	76.3	76.7	75.4	76.0	76.9
Prices												
CPI (1982-84 = 100)	238.0	239.4	240.4	242.2	244.0	245.2	246.6	248.0	237.0	240.0	246.0	251.8
Percent Change Annualized	0.1	2.3	1.8	3.0	2.9	2.0	2.3	2.4	0.1	1.3	2.5	2.4
Core CPI Index (1982-84 = 100)	245.7	247.0	248.2	249.5	251.1	252.5	253.9	255.3	242.2	247.6	253.2	259.0
Percent Change Annualized	2.5	2.1	2.1	2.0	2.6	2.2	2.3	2.3	1.8	2.2	2.3	2.3
PCE Price Index (2009 = 100)	110.0	110.5	110.9	111.5	112.1	112.6	113.1	113.7	109.5	110.7	112.9	115.2
Percent Change Annualized	0.3	2.0	1.5	1.9	2.5	1.6	1.9	2.0	0.3	1.1	2.0	2.0
Core PCE Price Index (2009 = 100)	110.7	111.2	111.6	112.0	112.6	113.1	113.6	114.2	109.5	111.3	113.4	115.6
Percent Change Annualized	2.1	1.8	1.7	1.2	2.3	1.8	1.9	2.0	1.4	1.7	1.8	2.0
GDP Price Index (2009 = 100)	110.6	111.3	111.6	112.2	112.9	113.3	113.9	114.5	110.0	111.4	113.7	116.0
Percent Change Annualized	0.5	2.3	1.4	2.0	2.5	1.6	2.0	2.1	1.1	1.3	2.0	2.1
Crude Oil, WTI (\$/Barrel)	33.2	45.4	44.9	49.1	49.3	49.3	49.8	50.3	48.7	43.1	49.7	53.7
Labor Markets												
Payroll Jobs (Millions)	143.4	144.0	144.7	145.2	145.7	146.3	146.7	147.2	141.8	144.3	146.5	148.5
Percent Change Annualized	1.7	1.4	2.0	1.4	1.5	1.5	1.3	1.4	2.1	1.8	1.5	1.3
Unemployment Rate (Percent)	4.9	4.9	4.9	4.7	4.7	4.6	4.5	4.5	5.3	4.9	4.6	4.5
Average Weekly Hours, Prod. Works.	33.6	33.6	33.6	33.6	33.6	33.7	33.7	33.7	33.7	33.6	33.7	33.8
Personal Income												
Average Hourly Earnings (\$)	21.35	21.49	21.63	21.75	21.91	22.06	22.23	22.39	21.03	21.56	22.15	22.82
Percent Change Annualized	2.5	2.6	2.6	2.3	2.9	2.9	3.0	3.0	2.1	2.5	2.7	3.0
Real Disp. Income (2009 Billions \$)	12556	12647	12738	12802	12826	12914	13014	13105	12343	12686	12965	13334
Percent Change Annualized	2.1	2.9	2.9	2.0	0.7	2.8	3.1	2.8	3.5	2.8	2.2	2.8
Housing												
Housing Starts (Ths., Ann. Rate)	1151	1159	1145	1249	1225	1235	1245	1256	1108	1176	1240	1273
Ext. Home Sales (Ths., Ann Rate)	5357	5477	5380	5547	5601	5671	5725	5758	5233	5440	5689	5887
New SF Home Sales (Ths., Ann Rate)	529	565	583	559	550	565	576	584	502	559	569	589
Case/Shiller HPI (Jan. 2000 = 100)	178.5	179.5	181.6	185.8	187.5	188.7	189.8	191.3	172.3	181.3	189.3	194.9
Percent Change Year Ago	5.2	5.0	5.1	5.6	5.1	5.1	4.5	3.0	4.6	5.2	4.4	2.9
Consumer												
Household Economic Stress Index	0.8	0.9	0.9	0.9	2.2	1.9	2.6	4.0	0.8	0.9	2.6	3.9
Auto Sales (Millions)	17.3	17.1	17.5	18.0	17.7	17.5	17.5	17.5	17.4	17.5	17.5	17.6
Consumer Credit (Billions \$)	3585	3642	3707	3765	3807	3848	3889	3930	3459	3675	3869	4036
Percent Change Annualized	5.7	6.5	7.4	6.3	4.6	4.4	4.3	4.3	6.9	6.2	5.3	4.3
Interest Rates (Percent)												
Prime Rate	3.50	3.50	3.50	3.55	3.79	4.04	4.25	4.30	3.26	3.51	4.10	4.72
Federal Funds	0.37	0.37	0.40	0.45	0.69	0.92	1.13	1.17	0.13	0.40	0.98	1.59
3-Month Treasury Bill	0.29	0.26	0.30	0.43	0.61	0.97	1.20	1.33	0.05	0.32	1.03	1.66
10-Year Treasury Note	1.91	1.75	1.56	2.14	2.47	2.72	2.91	3.00	2.14	1.84	2.77	3.16
30-Year Fixed Mortgage	3.74	3.59	3.45	3.81	4.20	4.43	4.60	4.66	3.85	3.65	4.47	4.76
a = actual f = forecast p = preliminary												

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