

NATIONAL ECONOMIC OUTLOOK

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Executive Summary

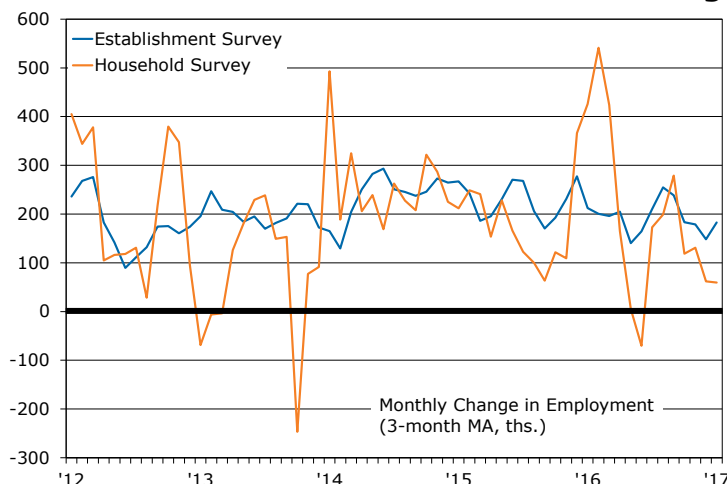
U.S. Economy in Good Shape In Early 2017, With Inflation Picking Up

- The U.S. economy expanded 1.9 percent at an annual rate in the fourth quarter of 2016, according to the advance estimate of real GDP. This followed growth of 3.5 percent in the third quarter. Compared to the third quarter, trade was the big drag in the fourth quarter, subtracting a large 1.7 percentage points from annualized growth. Soybean exports fell after surging in the third quarter, while imports rose in the fourth quarter as a stronger dollar encouraged consumers and business to buy products from overseas. But demand remained solid. Consumer spending growth slowed somewhat in the fourth quarter, to 2.5 percent at an annual rate from an unsustainable pace of 3.5 percent in the third quarter, but this was still a decent number. Business investment rose a steady, if unspectacular 2.4 percent in the fourth quarter, and investment in housing jumped 10.2 percent.
- Payroll employment increased by 227,000 in January, with a combined net downward revision to job growth in November and December of 37,000. Gains were broad-based across private industries, with a big jump in construction employment. The unemployment rate rose to 4.8 percent from 4.7 percent in December, but most of that came from more people looking for work, a vote of confidence in the job market. The weak spot was wage growth; it was a disappointing 0.1 percent in January, despite minimum wage increases in a number of states. Average hourly earnings were up 2.5 percent year-over-year in January, down from 2.8 percent in December. Wage growth has picked up over the past few years, but remains tepid, which is surprising given that the unemployment rate has been at or below 5.0 percent for 17 straight months.
- Overall inflation, measured using the consumer price index, was 0.6 percent in January, the biggest one-month increase since February 2013. A 7.8 percent increase in gasoline prices pushed the overall index higher in January. Core inflation, excluding volatile food and energy prices, was 0.3 percent in January, up from 0.2 percent in December, and the biggest increase since August 2016. On a year-ago basis overall inflation accelerated to 2.5 percent in January, from 2.1 percent in December. Core inflation, on a year-ago basis, was 2.3 percent, up from 2.2 percent in December and 2.1 percent in November. Accelerating inflation, particularly core inflation, will support interest rate increases from the Federal Open Market Committee over the next few years.

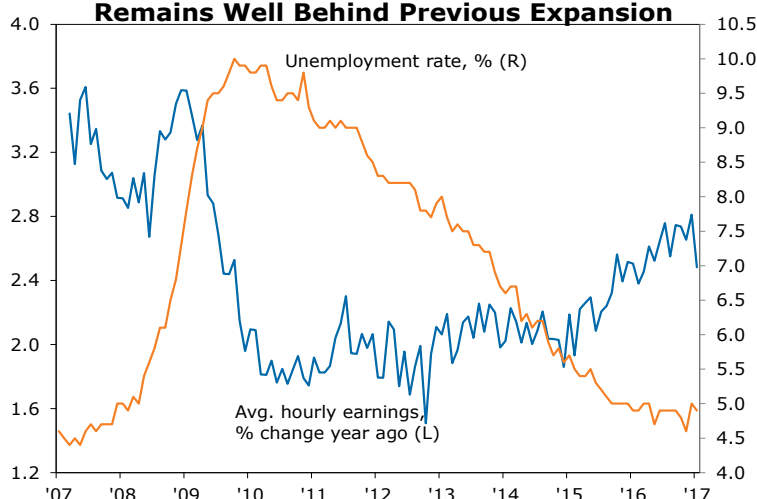
Baseline U.S. Economic Outlook, Summary Table*

	1Q'16a	2Q'16a	3Q'16a	4Q'16f	1Q'17f	2Q'17f	3Q'17f	4Q'17f	2015a	2016f	2017f	2018f
Output & Prices												
Real GDP (Chained 2009 Billions \$)	16525	16583	16727	16805	16890	16988	17101	17229	16397	16660	17052	17504
Percent Change Annualized	0.8	1.4	3.5	1.9	2.0	2.3	2.7	3.0	2.6	1.6	2.4	2.7
CPI (1982-84 = 100)	237.9	239.4	240.4	242.1	243.4	244.8	246.1	247.6	237.0	239.9	245.5	251.3
Percent Change Annualized	-0.3	2.5	1.6	2.9	2.2	2.2	2.3	2.4	0.1	1.2	2.3	2.4
Labor Markets												
Payroll Jobs (Millions)	143.5	144.0	144.6	145.1	145.7	146.2	146.6	147.1	141.8	144.3	146.4	148.3
Percent Change Annualized	1.9	1.3	1.8	1.4	1.5	1.5	1.3	1.3	2.1	1.7	1.5	1.3
Unemployment Rate (Percent)	4.9	4.9	4.9	4.7	4.6	4.6	4.5	4.5	5.3	4.9	4.5	4.5
Interest Rates (Percent)												
Federal Funds	0.37	0.37	0.40	0.45	0.62	0.67	0.87	0.92	0.13	0.40	0.77	1.54
Treasury Note, 10-year	1.91	1.75	1.56	2.14	2.51	2.62	2.72	2.81	2.14	1.84	2.66	3.13
a = actual f = forecast p = preliminary * Please see the Expanded Table for more forecast series.												

Labor Market Starts 2017 on a Solid Footing



Wage Growth Slips Again in January, Remains Well Behind Previous Expansion



The Trump Administration Will Find It Difficult to Meet Its Economic Goals

The Trump administration has set some very ambitious economic goals. A White House webpage, titled “Bringing Back Jobs and Growth,” says that “President Trump has outlined a bold plan to create 25 million new American jobs in the next decade and return to 4 percent annual real GDP economic growth.” But it is unlikely that the administration will hit these lofty benchmarks. That’s not because the administration’s proposed economic policies are bad for growth. Instead, it’s because no set of policies can realistically achieve those levels of consistent job and economic growth, given the current structure of the U.S. economy.

In terms of jobs, net creation of 25 million over ten years would be a record. There has never been a decade where the economy has added that many jobs; going back to the start of the data in 1950, the best 10-year performance was from 1992 to 2001, when the economy added 23.7 million jobs. Indeed, the economy has added 2.5 million jobs in a year only three times in this century. The demographic evolution of the U.S. economy will make the task even tougher. The workforce is now growing much more slowly than it did in the past, with the baby boomers aging into retirement. There was also a huge influx of women into the workforce from the 1960s to the 1980s as societal norms changed, but that process has run its course. As a result, it will become more and more difficult to find workers.

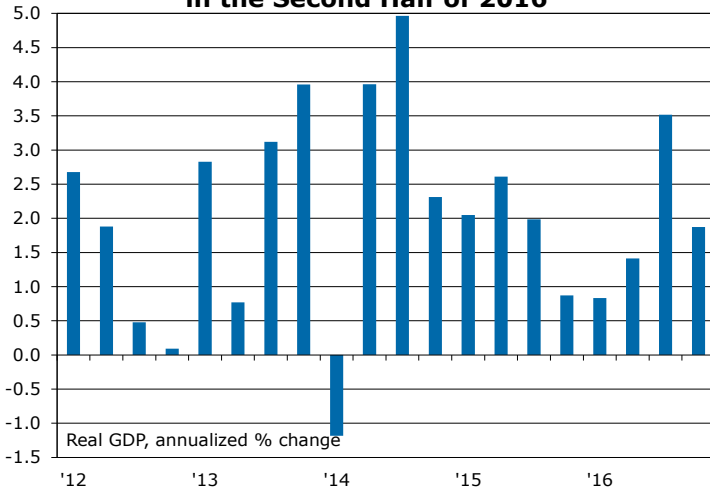
According to projections from the Census Bureau and calculations by PNC, the population available to work will grow by only 23 million over the next decade. This means that two million people of working age will need to move into the labor force, equal to an increase in the share of adults (ages 15+) working from 60 percent now to 64 percent in 2027. There is some room for growth in the near term, given that many people gave up looking for work after the Great Recession and could possibly move back into employment if the job market were stronger. But a lot of those who dropped out have already come back into the labor force; others have retired and cannot be lured back into working, and the number of retirees will only increase over the next 10 years given the aging of the U.S. population.

What about economic growth of 4 percent? (This is defined as growth in inflation-adjusted gross domestic product.) The United States has not achieved a single year of 4 percent growth since 2000, and has not achieved a decade of average annual growth of 4 percent since 1964 to 1973. A big reason why is slower growth in the labor force. Most economic growth comes from either more workers, or each worker producing more on average (what economists call productivity growth). With big demographic shifts in the economy, growth in the number of potential workers has slowed dramatically since the 1970s and the 1980s. And given the aging of the baby boomers, this slowing will continue over the next decade.

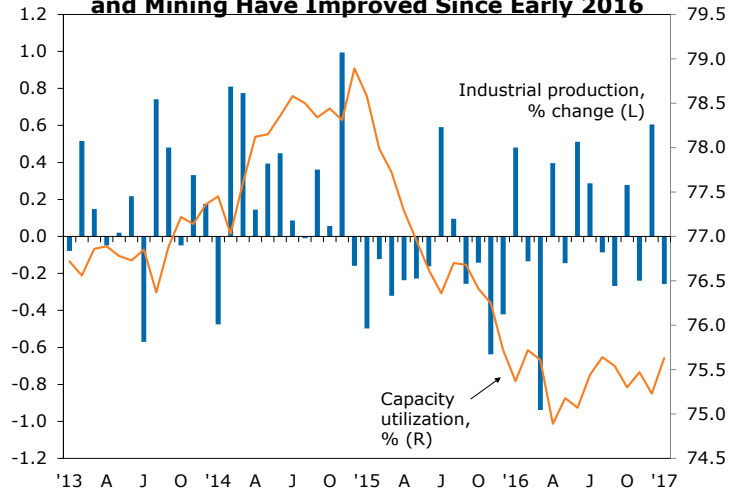
That leaves productivity—output per worker—as the most likely source of stronger long-run economic growth. Productivity growth has slowed over the past fifteen years. Some of the policies the Trump administration is considering could help to reverse that trend: incentives for business investment, lower personal and corporate income tax rates, reduced regulations on businesses, investment in infrastructure, and education reform. There is still a lot that economists do not understand about productivity growth, and it is possible that new technologies, such as driverless cars and trucks, could make U.S. workers much more productive in the future. But the types of productivity gains required to achieve more than a few quarters of 4 percent real GDP growth would be larger than those ever experienced in the post-World War II United States. Although some of the new Administration’s policies, if implemented, are likely to promote growth, it’s highly unlikely the U.S. economy can consistently expand at a 4 percent pace.

With support from tax cuts and infrastructure spending, U.S. real GDP growth will accelerate from 1.6 percent in 2016 to 2.4 percent this year and 2.7 percent next year. Job growth will slow from around 180,000 per month in 2016 to around 160,000 per month in 2017, 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. The tighter job market will push up wages, allowing for continued gains in consumer spending, supporting overall economic growth. Stronger wage gains will also contribute to a gradual acceleration in inflation over the next few years. To avoid a more sustained pickup in inflation, the Federal Open Market Committee will increase the Federal funds rate twice in 2017 and four times in 2018, by 0.25 percentage point each time. The FOMC will also start shrinking the central bank’s \$4.5 trillion balance sheet by the middle of 2018, gradually reducing it over the next several years.

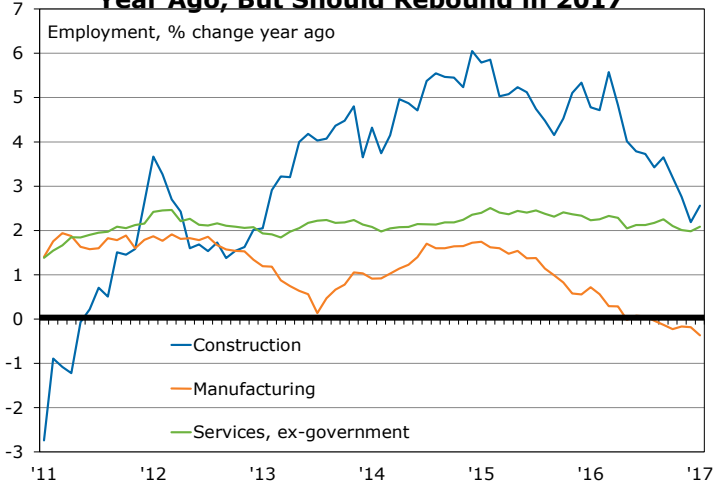
Economy Did Much Better in the Second Half of 2016



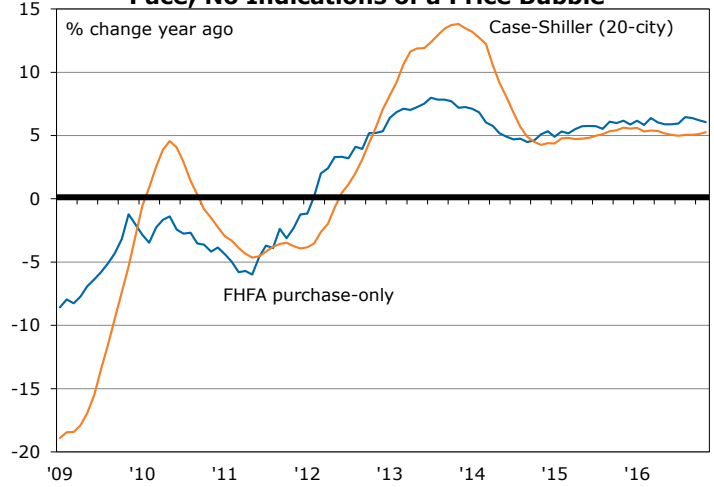
Utilities a Drag in January, But Manufacturing and Mining Have Improved Since Early 2016



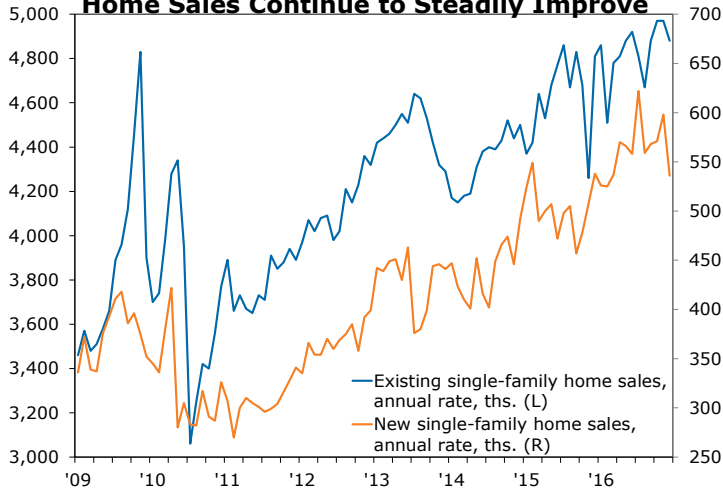
Manufacturing Employment Down From a Year Ago, But Should Rebound in 2017



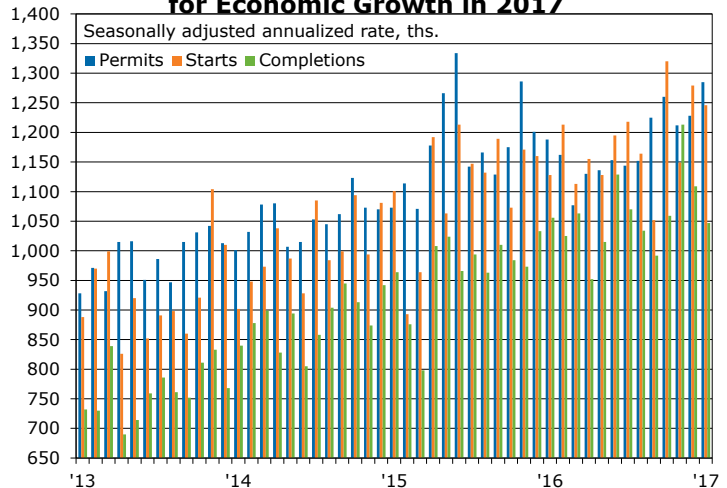
House Prices Growing at Moderate, Sustainable Pace; No Indications of a Price Bubble



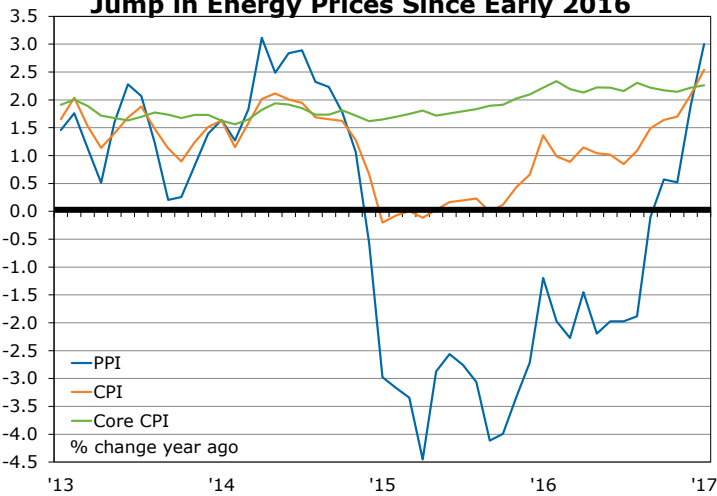
With Solid Fundamentals, Good Affordability, Home Sales Continue to Steadily Improve



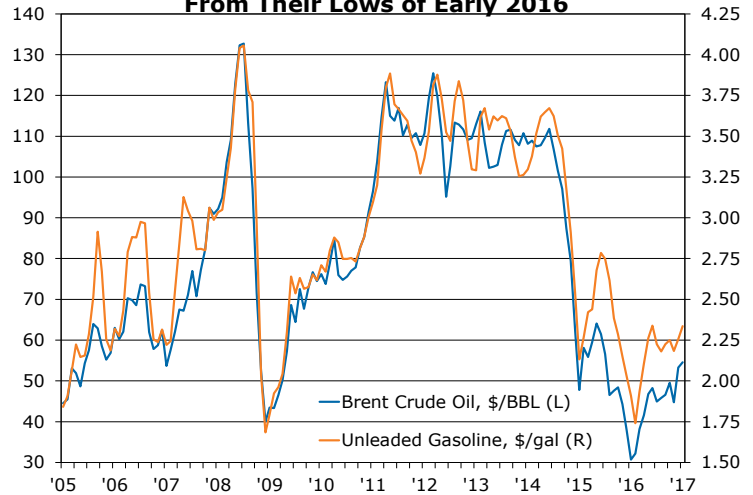
Homebuilding Will Be a Positive for Economic Growth in 2017



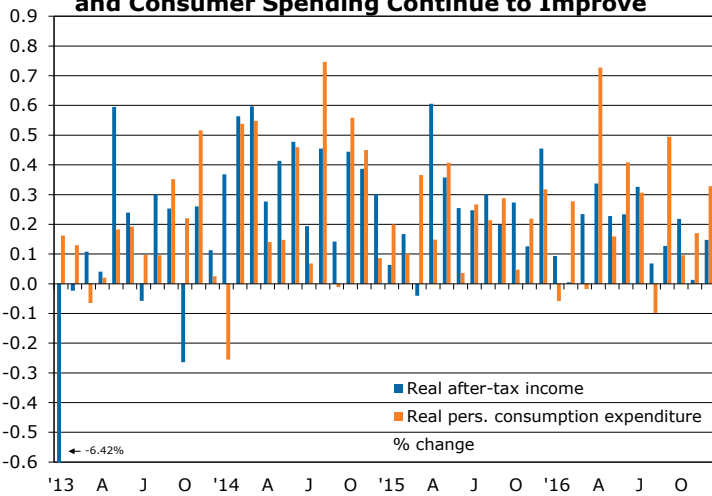
Inflation Has Picked Up With the Jump in Energy Prices Since Early 2016



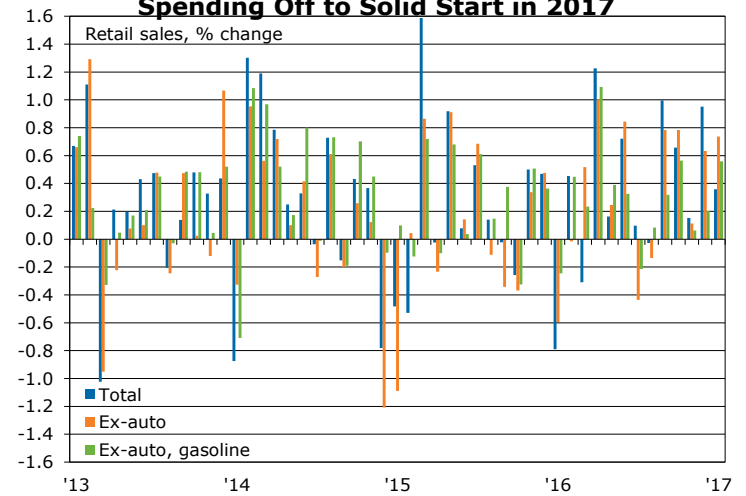
Energy Prices Continue to Move Higher From Their Lows of Early 2016



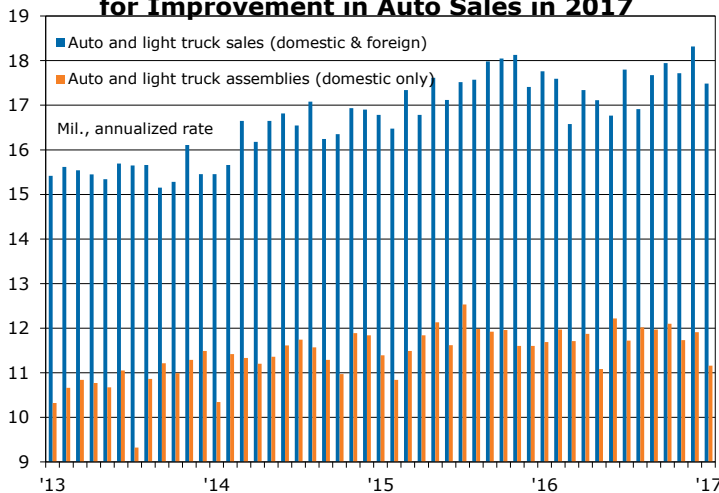
With Job Growth and Wage Gains, Household Income and Consumer Spending Continue to Improve



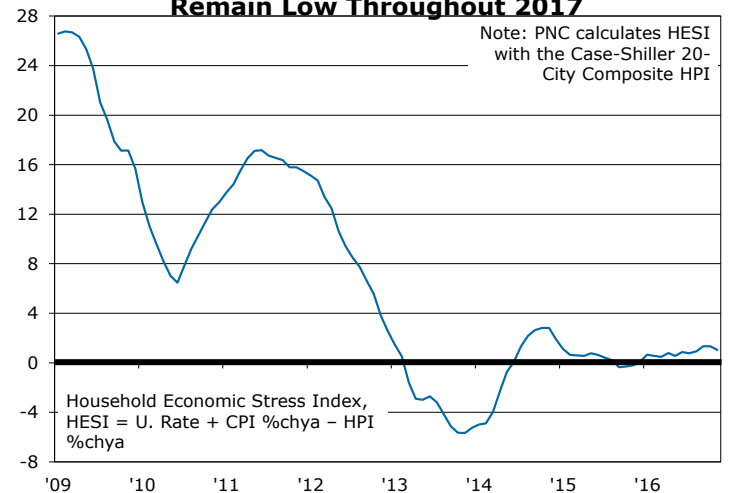
With Good Fundamentals, Consumer Spending Off to Solid Start in 2017



After Eight Years of Growth, Not Much Room for Improvement in Auto Sales in 2017



Household Economic Stress Will Remain Low Throughout 2017



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PNC Economics Group
February, 2017

Baseline U.S. Economic Outlook, Expanded Table

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Output												
Nominal GDP (Billions \$)	18282	18450	18675	18861	19044	19245	19465	19711	18037	18567	19366	20281
Percent Change Annualized	1.3	3.7	5.0	4.0	3.9	4.3	4.7	5.1	3.7	2.9	4.3	4.7
Real GDP (Chained 2009 Billions \$)	16525	16583	16727	16805	16890	16988	17101	17229	16397	16660	17052	17504
Percent Change Annualized	0.8	1.4	3.5	1.9	2.0	2.3	2.7	3.0	2.6	1.6	2.4	2.7
Pers. Consumption Expenditures	11365	11485	11569	11640	11710	11779	11848	11925	11215	11515	11815	12096
Percent Change Annualized	1.6	4.3	3.0	2.5	2.4	2.4	2.4	2.6	3.2	2.7	2.6	2.4
Nonresidential Fixed Investment	2180	2185	2193	2206	2218	2233	2249	2265	2200	2191	2241	2296
Percent Change Annualized	-3.4	1.0	1.4	2.4	2.2	2.7	2.9	2.9	2.1	-0.4	2.3	2.4
Residential Investment	601	589	583	597	604	610	616	621	565	592	613	628
Percent Change Annualized	7.8	-7.8	-4.1	10.2	4.9	3.9	4.0	3.5	11.7	4.9	3.5	2.5
Change in Private Inventories	41	-10	7	49	54	60	64	74	84	22	63	76
Net Exports	-566	-559	-522	-600	-610	-621	-624	-629	-540	-562	-621	-630
Government Expenditures	2913	2901	2906	2915	2923	2935	2956	2982	2884	2909	2949	3047
Percent Change Annualized	1.6	-1.7	0.8	1.2	1.1	1.6	3.0	3.5	1.8	0.9	1.4	3.3
Industrial Prod. Index (2012 = 100)	104.1	103.9	104.4	104.8	105.3	105.8	106.4	107.1	105.2	104.3	106.2	108.7
Percent Change Annualized	-1.7	-0.8	1.9	1.5	1.9	2.0	2.2	2.4	0.3	-0.9	1.8	2.4
Capacity Utilization (Percent)	75.4	75.2	75.5	75.8	76.0	76.3	76.6	77.0	76.7	75.5	76.5	77.7
Prices												
CPI (1982-84 = 100)	237.9	239.4	240.4	242.1	243.4	244.8	246.1	247.6	237.0	239.9	245.5	251.3
Percent Change Annualized	-0.3	2.5	1.6	2.9	2.2	2.2	2.3	2.4	0.1	1.2	2.3	2.4
Core CPI Index (1982-84 = 100)	245.8	247.0	248.2	249.5	250.8	252.2	253.6	255.1	242.2	247.6	252.9	258.7
Percent Change Annualized	2.7	2.1	1.9	2.1	2.2	2.2	2.3	2.3	1.8	2.2	2.1	2.3
PCE Price Index (2009 = 100)	110.0	110.5	110.9	111.6	112.1	112.6	113.1	113.7	109.5	110.8	112.9	115.2
Percent Change Annualized	0.3	2.0	1.5	2.5	1.8	1.8	1.9	2.0	0.3	1.1	1.9	2.0
Core PCE Price Index (2009 = 100)	110.7	111.2	111.6	112.1	112.6	113.1	113.7	114.2	109.5	111.4	113.4	115.6
Percent Change Annualized	2.1	1.8	1.7	1.8	1.8	1.8	1.9	1.9	1.4	1.7	1.8	2.0
GDP Price Index (2009 = 100)	110.6	111.3	111.6	112.2	112.8	113.3	113.9	114.5	110.0	111.4	113.6	116.0
Percent Change Annualized	0.5	2.3	1.4	2.2	1.9	2.0	2.0	2.1	1.1	1.3	1.9	2.1
Crude Oil, WTI (\$/Barrel)	33.2	45.4	44.9	48.8	49.0	49.0	49.5	50.0	48.7	43.1	49.4	53.4
Labor Markets												
Payroll Jobs (Millions)	143.5	144.0	144.6	145.1	145.7	146.2	146.6	147.1	141.8	144.3	146.4	148.3
Percent Change Annualized	1.9	1.3	1.8	1.4	1.5	1.5	1.3	1.3	2.1	1.7	1.5	1.3
Unemployment Rate (Percent)	4.9	4.9	4.9	4.7	4.6	4.6	4.5	4.5	5.3	4.9	4.5	4.5
Average Weekly Hours, Prod. Works.	33.7	33.6	33.6	33.7	33.7	33.7	33.8	33.8	33.7	33.6	33.8	33.9
Personal Income												
Average Hourly Earnings (\$)	21.36	21.49	21.63	21.78	21.93	22.09	22.25	22.42	21.04	21.56	22.17	22.84
Percent Change Annualized	2.4	2.4	2.6	2.8	2.9	2.9	3.0	3.1	2.1	2.5	2.8	3.0
Real Disp. Income (2009 Billions \$)	12556	12647	12729	12798	12882	12969	13070	13167	12343	12682	13022	13397
Percent Change Annualized	2.1	2.9	2.6	2.2	2.7	2.7	3.1	3.0	3.5	2.7	2.7	2.9
Housing												
Housing Starts (Ths., Ann. Rate)	1151	1159	1145	1182	1185	1193	1208	1220	1108	1159	1201	1235
Ext. Home Sales (Ths., Ann Rate)	5300	5503	5390	5556	5657	5733	5784	5816	5233	5437	5747	5941
New SF Home Sales (Ths., Ann Rate)	529	565	584	576	584	590	601	609	502	563	596	610
Case/Shiller HPI (Jan. 2000 = 100)	178.5	179.4	181.7	183.8	185.1	186.7	188.3	189.9	172.3	180.9	187.5	193.6
Percent Change Year Ago	5.2	5.0	5.2	4.4	3.7	4.0	3.6	3.3	4.6	5.0	3.7	3.3
Consumer												
Household Economic Stress Index	0.8	0.9	0.8	2.0	3.2	2.8	3.3	3.4	0.8	1.1	3.2	3.6
Auto Sales (Millions)	17.3	17.1	17.5	18.0	17.6	17.5	17.5	17.5	17.4	17.5	17.5	17.6
Consumer Credit (Billions \$)	3585	3643	3711	3756	3800	3842	3883	3924	3459	3674	3862	4029
Percent Change Annualized	5.8	6.6	7.7	4.9	4.7	4.5	4.4	4.3	6.9	6.2	5.1	4.3
Interest Rates (Percent)												
Prime Rate	3.50	3.50	3.50	3.55	3.75	3.79	4.00	4.05	3.26	3.51	3.90	4.67
Federal Funds	0.37	0.37	0.40	0.45	0.62	0.67	0.87	0.92	0.13	0.40	0.77	1.54
3-Month Treasury Bill	0.29	0.26	0.30	0.43	0.59	0.74	0.89	1.04	0.05	0.32	0.81	1.58
10-Year Treasury Note	1.91	1.75	1.56	2.14	2.51	2.62	2.72	2.81	2.14	1.84	2.66	3.13
30-Year Fixed Mortgage	3.74	3.59	3.45	3.76	4.10	4.18	4.25	4.31	3.85	3.64	4.21	4.54
a = actual f = forecast p = preliminary												

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