Global Economic Highlights

October 16, 2023

FOMC Participants Anticipate Another Rate Hike, While Cautiously Monitoring Incoming Data Amid Rising Uncertainties

UNITED STATES: The minutes from the Federal Open Market Committee meeting on September 19 and 20 were released on October 11. The minutes say that participants were willing to leave the fed funds rate unchanged, but a majority were leaning toward another near-term rate increase. The minutes say that "all participants agreed that the Committee was in a position to proceed carefully and that policy decisions at every meeting would continue to be based on the totality of incoming information…Participants expected that the data arriving in coming months would help clarify the extent to which the disinflation process was continuing and labor markets were reaching a better balance between demand and supply. This information would be valuable in determining the extent of additional policy firming that may be appropriate to return inflation to 2% over time."

In addition, participants agreed that current monetary is restrictive, weighing on economic growth, and that "it broadly appeared to be restraining the economy as expected." In addition, "all participants agreed that policy should remain restrictive for some time until the Committee is confident that inflation is moving down sustainably towards its [2%] objective." Several participants said that, given the fed funds rate was at or near a peak, the focus on communications should shift to discussion of how long the fed funds rate would remain elevated.

As of mid-October there are about 34,000 UAW members on strike, about one-quarter of the union's workers at the Big Three automakers. The economic impact so far has been limited, and PNC is not adjusting its forecast. Reduced supplies of vehicles could lead to higher new and used car prices. A new contract could also be inflationary. If the strike does lead to higher inflation, it could force the Federal Open Market Committee to raise the federal funds rate more aggressively.

At the end of September Congress passed a continuing resolution to fund the federal government through mid-November. But with Republicans unable to settle on a new Speaker of the House, the potential for a government shutdown next month has increased. A short shutdown would have little impact on the economy. But the longer a shutdown lasts, and the longer government employees and contractors are not paid, the greater the potential damage to consumer spending and economic growth.

Job growth in September came in far above the consensus expectation at 336,000, according to a survey of employers from the Bureau of Labor Statistics. In addition, there were large upward revisions to job growth in July and August of a combined 119,000. All of this means that the labor market picture looks very different from last month, when it appeared that job growth was slowing to a more sustainable pace. Over the past three months job growth has averaged almost 270,000, about double the long-run sustainable pace.

PNC still thinks that the fed funds rate is at its peak in the current cycle, in a range between 5.25% and 5.50%. Inflation will continue to slow in the near term, and after a strong third quarter growth is likely to soften at the end of 2023 and into 2024. This will allow the FOMC to keep the fed funds rate unchanged into next year.

Outside the FOMC minutes and the strong U.S. job report, the U.S. trade deficit narrowed 9.9% in August, to $58.3 billion from $64.7 billion (revised down from $65 billion) in July. This was the smallest trade deficit since June 2020. It also came in lower than the consensus estimates of $68 billion. Compared to last year, the trade deficit has shrunk 13.4%. The

Gus Faucher
Chief Economist

Stuart Hoffman
Senior Economic Advisor

Kurt Rankin
Senior Economist

Ershang Liang
Economist

goods trade deficit continued to narrow in August, with imports dropping and exports rising. With services exports rising more than imports, the services surplus increased in August. The increase in the services surplus came primarily from an increase in foreign travel to the U.S. Imports of capital goods, autos, and consumer goods dropped in August.

The ISM Manufacturing Purchasing Manager's Index report for September 2023 increased to 49.0 from 47.6 in August. Although below the 50 level for an eleventh straight month, meaning that manufacturing activity is contracting, September's gain is the second consecutive increase for the manufacturing PMI, with gains across most of the major components.

EUROZONE: The International Monetary Fund's latest forecast for the eurozone downgraded growth for the euro area for both 2023 and 2024, given persistent high inflation. Tight monetary policies continued to weigh on growth while weakness in industrial sectors and labor market continued. The Hamas attack on Israel on October 7 brought new risks of higher energy inflation if the current war spreads further in the Middle East.

Industrial production in Germany, the biggest economy in the eurozone, shrank in August, the third straight month of a decline in output. The Composite Purchasing Manager's Index in September rose from 44.6 to 46.4, also the third straight month below the 50 expansion level, showing overall business activity continues to contract in Germany, although the level was up from August. Germany's GDP growth was flat in the second quarter from the first, but was down 0.2% on a year-over-year basis. The trade surplus dropped in August, and trade is likely to remain a drag on GDP growth in the third quarter.

Germany's manufacturing PMI was 39.6 in September, an increase from the previous two months, but well below the expansion threshold of 50. Industrial manufacturing orders grew 3.9% in August after declining 11.7% in July, better than the consensus estimate.

CANADA: Labor force employment increased by 63,800 in September, much stronger than the consensus expectation and higher than August growth of 39,000. But most of the increase in September was in part-time work, up by 47,900. The labor market remained robust with the unemployment rate in September remaining flat at 5.5%, one of the lowest unemployment rates since the 1970s. Average hourly wages of permanent workers were up 5.3% in September from a year earlier, an acceleration from previous months and higher than pre-pandemic wage growth of around 2%.

JAPAN: Japan's business activities continued to expand in September. The Jibun Bank Japan Purchasing Manager's Index increased on the month to 52.1 from 51.8 in August, and the PMI services index also increased, from 53.3 to 53.8. The seasonally-adjusted annual rate of real GDP growth in the second quarter was 4.8%. Growth in private residential investment and exports drove growth; however, PNC expects global trade flows to weaken in the coming months, with drags from tight monetary policies across the U.S., Canada, and the eurozone and weak domestic demand in China.

MEXICO: Inflation in Mexico continued to cool off in September with CPI growing 4.45% year-over-year, and core inflation also slowing to 5.76%, from 6.08% in August. The manufacturing industry in Mexico weakened in September with the manufacturing PMI dropping below 50, the contraction after eight straight months of expansion.

CHINA: According to the National Bureau of Statistics of China, year-to-date industrial corporate profits continued to drop in August. Industrial profits in mining dropped over 20%, while manufacturing profits dropped 14%. Utilities profits increased more than 40%. The largest drop in industrial profits came in state-owned enterprises, down 16.5%, while profits of foreign-invested corporates dropped 11.1%.

The Manufacturing Purchasing Managers Index of the National Bureau of Statistics of China shows China's manufacturing industry moved back into expansion in September. Demand has picked up with the New Orders component rising to 50.5, the best read since April. Nonmanufacturing industries also experienced recovery with the PMI rising to 51.7.

Visit pnc.com/economicreports for more information from PNC Economics.