

Fed and BoE Expected to Hold Rates Steady Amid Ongoing Inflation Concerns

UNITED STATES: Job growth surprised to the upside in February, with the U.S. economy adding 275,000 jobs, according to a survey of employers from the Bureau of Labor Statistics. However, there were big downward revisions to job growth in January and December of a combined 167,000. Over the past three months job growth has averaged 265,000; this is about double long-term potential job growth, given underlying expansion in the labor force. On a year-over-year basis average hourly earnings were up 4.3% in February, down from 4.5% in January before revisions. Wage growth has slowed dramatically since 2022, but is still well above the 3.5% pace roughly consistent with the Federal Reserve's 2% inflation objective.

The unemployment rate rose to 3.9% in February from 3.7% in the previous three months. The unemployment rate has been below 4% for more than two straight years, the longest-such stretch since the late 1960s. The labor force participation rate—the share of adults working or looking for work—held steady at 62.5% for a second month; it has been between 62.5% and 62.8% for the past year, structurally below the 63%+ rate before the pandemic.

Consumer Price Index (CPI) inflation came in at 0.4% in February from January after seasonal adjustment, and up 3.2% versus one year ago. Core CPI inflation (excluding food and energy) also rose 0.4% for the month. On a year-ago basis core CPI inflation was 3.8%, down from 3.9% in January and above 6% in late 2022. Still core inflation remains well above the Fed's 2% inflation goal; the central bank prefers a slightly different measure, the personal consumption expenditures price index. The Fed is expected to keep interest rates unchanged at its meeting on March 20, 2024. PNC expects three 25 basis point cuts in the federal funds rate in 2024, starting in the second quarter. This would bring the fed funds rate down to a range of 4.50% to 4.75% by the end of 2024.

EUROZONE: According to the European Commission's final GDP report, real GDP in the fourth quarter was flat, after contracting 0.1% in the third quarter. Construction of dwellings weighed on economic growth in the fourth quarter, contracting 0.6% on a quarter-over-quarter basis and 1.6% from the fourth quarter 2022. Household consumption eked out a 0.1% gain in the last quarter of 2023 as employment continued to increase, but slower than growth than in the previous quarter. On a year-over-year basis employment growth slowed in the fourth quarter but still registered a 1.2% gain, above the long-run average level at 0.9%.

The ECB held its policy rates—the main refinancing operations (MRO) rate, the rate on the marginal lending facility, and the deposit facility rate—steady at its meeting on March 7, 2024. Total inflation continued to ease in early 2024 but remained well above the European Central Bank's (ECB) 2% inflation target. The Flash Harmonized Index of Consumer Prices (HICP) in February was down to 2.6% from a year earlier. The inflation rate for alcoholic beverages, tobacco, restaurants, and hotels eased a bit in the second half of 2023 but remained more elevated than the past decade. The inflation rate for food and non-alcoholic beverages, after peaking at 17.5% in March 2023, dropped to 5.4% year-over-year in January 2024.

UNITED KINGDOM: Real GDP contracted 0.1% in the rolling three months ending in January 2024 after contracting over four rolling months, with production industries contracting 0.2% and services remaining flat. The pace of economic contraction has slowed into 2024.

The labor market remained tight in the UK with a near historically-low unemployment rate. Wage growth, however, continued to slow at the end of 2023, with three-month average weekly earnings in January growing at 5.6% from last year, according to the UK Office for National Statistics (ONS). This marked the slowest pace of weekly wage growth since the first half of 2023, but wage growth is well above its long-run level and too high for the BoE's inflation objective of 2%. Consumer Price Index (CPI) inflation on a year-ago basis remained flat at 4% in January 2024 from December 2023. CPI services inflation has reaccelerated over the past three months and remained high at 6.5%. The inflation rate in health services, communications services, restaurants, and hotels, remained stubbornly high and well above the Bank of England's (BoE) inflation goal of 2%.

PNC's baseline outlook is for a mild recession in the UK in 2024 as high interest rates in response to elevated inflation continue to weigh on capital formation. PNC expects the BoE to hold its policy Bank Rate at 5.25% at its next meeting on March 21. With current monetary policy contractionary, slowing but elevated inflation and slowing wage growth will further weigh on UK consumers and the economy.

CANADA: The Bank of Canada (BoC) kept its policy bank rate unchanged at 5.00% on March 6. The labor market remained tight, but has softened with growth in the average hourly wage rate of permanent workers slowing to 4.9% in February from 5.3% in January. The pace of wage growth is still too hot for the BoC's inflation target of around 2%. Total inflation was 2.9% in January, down from 3.4% in December after it reaccelerated to end 2023. Core inflation, excluding food and energy, remained elevated at 3.1% in January. Real GDP expanded 1.0% annualized in the fourth quarter of 2023 after contracting in the third quarter; capital formation fell 3.8% in the fourth quarter, weigh on overall growth.

JAPAN: Japan's economy expanded 0.1% (not annualized) in the fourth quarter after revisions, after an initially reported 0.1% contraction. The Japanese economy contracted 0.8% in the third quarter. Drags on growth were across the board in the fourth quarter except for net trade and business investment, with the important private consumption component contracting 0.3% and private residential investment dropping 1.0% in the fourth quarter. Real GDP rose 1.3% in the fourth quarter year-over-year, with private residential investment up 0.4%. The GDP deflator grew 3.9% year-over-year in the last quarter of 2023, well above the long-run average of -0.3% since 1995.

CHINA: China's Consumer Price Index (CPI) ended a six-month deflation streak and rose 0.7% in February 2024 from one year earlier. Prices of consumables continued to contract in February, while services inflation jumped to 1.9%, the strongest since China's economy reopened in late 2022 following the COVID-19 pandemic.

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