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GLOBAL ECONOMIC HIGHLIGHTS

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Federal Reserve to Stay the Course in April, but Other Major Central Banks Are Already Considering or Starting to Taper

UNITED STATES: PNC forecasts for the Federal Reserve to hold unchanged their monetary stance and forward guidance at their April 28 policy decision. The Federal Open Market Committee stated in March that their $120 billion in monthly asset purchases (a.k.a. quantitative easing) would continue "until substantial further progress has been made" toward maximum employment and inflation averaging 2% over time; they committed to wait until the labor market recovers to maximum employment, inflation has recovered to 2%, and inflation "is on track to moderately exceed 2 percent for some time" before raising the Federal Funds rate. PNC forecasts for the Fed to wait until early 2022 to begin tapering its quantitative easing program, and to wait until late 2023 to begin raising the Federal Funds rate. The economic outlook facing the Fed—a robust recovery and inflation that looks set to rise temporarily—is similar to those faced by other major central banks. But different central banks weigh different considerations differently and this is causing a divergence in the timing for monetary policy normalization across economies. In Canada, where inflation met the central bank's target before the crisis (unlike in the US where inflation chronically undershot 2%), and where household debt and high housing prices create financial stability concerns, the Bank of Canada already began tapering its quantitative easing program in April. In the Eurozone, where politically influential constituencies are pressuring the central bank to throttle back before the United States, the ECB looks likely to begin tapering its asset purchases in the second half of 2021. While central banks are all basically headed in the same direction, differences in how they time the normalization of monetary policies are a potential source of volatile swings in exchange rates over the next year.

The recovery is gaining momentum in April. The Markit services and manufacturing PMIs both hit record high levels in the April flash releases: The services index rose to 63.1 from 60.4 in March and the manufacturing index to 60.6 from 59.1. The manufacturing survey began in 2007 and the services survey in 2009. Manufacturers also reported the most widespread supplier delivery delays on record as all parts of the U.S. economy try to build inventories at the same time. Initial claims for unemployment insurance under regular state programs fell to 547,000 in the week ending April 17, down from 586,000 the previous week (revised up by 10,000). The four-week moving average of claims fell to 651,000 in the week ending April 17, down by almost 28,000 from the previous week. Initial claims have dropped sharply in the last few months after being stuck between 700,000 to 900,000 in most weeks between last August and March. The recent drop in initial claims is signaling another month of robust job growth in April after nearly a million jobs added in March.

Existing home sales fell 4% in March to 6.01 million units annualized, a seven-month low, with declines across all regions. Given the strength of other housing indicators, lagged effects of February's bad weather likely weighed on existing home sales in March. By contrast, new home sales jumped 21%, more than reversing February's 16% monthly decline and reaching a new 15-year high. Housing prices have risen in recent months, and inventories of homes for sale are very low, but other housing fundamentals remain very strong: interest rates are still very low relative to history, finances for middle- and upper-income households are strong, and confidence in the economic recovery is boosting consumer sentiment.

PNC forecasts for the April 29 release of the advance estimate for real GDP growth in the first quarter of 2021 to show a 5.8% annualized increase, up from a 4.3% increase in the prior quarter, and led by a nearly 10% surge in consumer spending in the quarter.

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CANADA: The Bank of Canada (BOC) began tapering its quantitative easing (QE) program at its April 21 monetary policy decision, reducing purchases of Government of Canada bonds to $3 billion weekly from $4 billion previously. The BOC held its benchmark policy rate steady at 0.25%. The decision made the BOC a leader among major central banks in reining in monetary stimulus. Canada entered the crisis with higher housing prices and household debt than other major economies; the BOC is anxious to get monetary policy back to a neutral stance to avoid worsening these vulnerabilities.

The BOC noted that the economy is "healing faster than expected" and revised up its 2021 GDP growth forecast to 6.5% from 4% in their January *Monetary Policy Report* (MPR). Central bankers anticipate the containment measures imposed during the current coronavirus wave to have a temporary and immaterial effect on the economy. PNC Economics expects the BOC to raise its benchmark policy rate in 2022.

CPI inflation edged up to 2.2% in March, the highest in over a year, from 1.1% in February; the Bank of Canada's three measures of core inflation, CPI-common, CPI-median and CPI-trim were 1.5%, 2.1% and 2.2% respectively, in March. March's higher CPI inflation largely reflects base comparisons to outright declines in prices last year. Unlike in the United States, Canadian inflation was at the bank's 2% target for most of the pre-crisis expansion, another reason the BOC sees less need to drag its feet during the recovery.

In the press conference following the decision, BOC Governor Tiff Mackem welcomed a decision by Canada's Office of the Superintendent of Financial Institutions (OFSI) to tighten mortgage qualification rules; this proposal is in addition to the "non-resident, non-Canadian-owned" 1% vacant-home tax proposed in the 2021 federal budget. Canada's Prime Minister Justin Trudeau released this budget on April 19; highlights of the C$101.4 billion (5% of GDP) spending package include additional pandemic relief programs, a new national childcare initiative, and an increase in pension benefits.

The latest economic data demonstrate why the Bank of Canada is keen to cool the booming housing market. Housing starts jumped to the highest level in at least four decades in March, rising by 335,200 units, following an upwardly revised 275,600 in February; the number of housing starts is a leading indicator of housing and overall economic activity. The Teranet-National Bank House Price Index™ jumped 10.8% in March from twelve months earlier, the fastest growth since late 2017; the Teranet-National Bank House Price Index™ increased 1.5% in March from a month earlier, the strongest growth rate since late 2017.

EUROZONE: The European Central Bank signaled their crisis-era policies will likely start winding down in the third quarter of 2022 at their April 22 Governing Council decision. The key moving piece in their policy stance is the Pandemic Emergency Purchase Programme (PEPP a.k.a. emergency QE). The ECB substantially accelerated PEPP at their March decision—purchases averaged around €20 billion euros weekly since then, up from around €15 billion in most of January and February (excluding holiday weeks). At the April decision, the ECB said PEPP purchases would stay at the higher rate throughout the second quarter, but the ECB will reevaluate their pace when they next update economic projections in June. If vaccine distribution goes well in the second quarter and the Eurozone service sector reopens, the ECB will likely begin tapering PEPP purchases in the third quarter, and end net purchases in March 2022. If the pandemic lingers on longer than expected, the ECB will stay in crisis-mode longer.

Other parts of the ECB's monetary policy stance are set to change more slowly. Even before the pandemic, the ECB was running an open-ended Asset Purchase Programme that buys €20bn euros in assets monthly; making long-term loans to Eurozone banks to ensure ample liquidity (Targeted Longer-Term Refinancing Operations TLTROs); and implementing a negative effective policy rate (the deposit rate) for six years. President Lagarde noted in the press conference following her April decision that the Eurozone economy is set to recover to its pre-crisis state by the second half of 2022, but that the Eurozone's weak trend inflation makes a wind-down of these programs unlikely to be justifiable over the foreseeable forecast horizon. The Eurozone services PMI rose to 50.3 in the April flash estimate from 49.6 in March, while the manufacturing PMI rose to 63.4 from 63.3 and was the highest since the survey began in 1997.

UNITED KINGDOM: The Markit/CIPS services PMI rose to 60.1 in April and was the strongest since August 2014, while the manufacturing PMI rose to the strongest since 1994. The Confederation of British Industry's Business Optimism Index rose to the highest since 1973 in April.

JAPAN: The au Jibun Bank manufacturing PMI rose to 54.2 in the April flash release from 53.3 in March, while the services PMI was unchanged at 48.3. The Bank of Japan is set to hold its monetary stance unchanged at its April decision, which will be announced the night of April 26 in US time zones.

BRAZIL: The IBC-BR economic activity index rose 1.7% in February from January, the strongest gain since July, following an upwardly-revised 1.3% increase in January; the IBC-BR was up 1.0% in the twelve months to February, following a downwardly-revised 0.5% decline in January. The Brazilian Congress has approved a bill which grants The Central Bank of Brazil formal autonomy and adds “full employment” to its mandate.

MEXICO: Employment rose by 800,000 (1.5%) in March to 53.8 million; employment was still down 3.6% from 55.8 million a year earlier. Nearly all of the month’s net job gains were in agriculture. The seasonally-adjusted unemployment rate dipped to 4.4% from 4.5% in February and the labor force participation rate rose to 57.2% from 56.7%. Retail sales rose 1.6% in February from January; they were down 6.3% from a year earlier. Mexico has provided much less stimulus to households than the U.S., translating into a much weaker recovery of consumer spending. Mexico’s vaccination drive is gradually picking up steam—9% of Mexicans have received a first vaccine dose as of mid-April versus 41% of Americans.