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GLOBAL ECONOMIC HIGHLIGHTS

Gus Faucher Chief Economist
Stuart Hoffman Senior Economic Advisor
William Adams Senior Economist
Abbey Omodunbi Senior Economist
Kurt Rankin Economist

Mexico Surprises With a June Rate Hike; U.S. Unemployment Rate Expected to Fall to 5.6% in the June Jobs Report

The next edition of Global Economic Highlights will be published July 12.

MEXICO: The Bank of Mexico (Banxico) surprised with a 0.25 percentage point hike in their policy interbank rate at the June 24 Monetary Policy Committee meeting, raising the rate to 4.25%; no economists surveyed by Bloomberg prior to the decision had expected a hike. Banxico's announcement cited the jump in U.S. CPI inflation to the highest since 2008 in May; Banxico rarely highlights a specific foreign data release in this way. They also noted that Mexican inflation jumped to 6.0% in year-ago terms in the first half of June, and core inflation to 4.6%, both overshooting Banxico's 3.0% target. Banxico explained the June rate hike as a response to the risk of a faster withdrawal of monetary stimulus outside of Mexico in response to higher inflation; Banxico also wants to prevent a rise in Mexican inflation expectations.

The peso appreciated to less than 20 per U.S. dollar after the decision, and held that level despite Banxico's Deputy Governor telling Bloomberg news on June 25 that the June hike is not necessarily the start of a hiking cycle for Mexico. Financial markets are unconvinced: After Banxico's decision, markets price in Banxico's policy rate rising to 6.5% by June 2022, a full percentage point higher than expectations from before the Fed's June 16 decision.

UNITED STATES: Personal income fell 2.0% in April as a 12% decline in transfer payments more than offset a 1% increase in labor market income. After-tax income fell 2.3% on the month. Personal expenditures were unchanged in May after an upwardly-revised 0.9% increase in April (reported as 0.5% in the prior release); consumer spending was 5% above the pre-pandemic level in May. Spending on services rose 0.7% on the month in May, offsetting a 1.3% decline in spending on goods; consumers are redirecting their spending back to high-contact services like hospitality, travel, and entertainment after the pandemic forced them to concentrate their spending power on goods. The personal consumption expenditures price index rose 0.4% in May after large 0.6% increases in both March and April. Core PCE prices excluding food and energy rose 0.5% in May after a 0.7% increase in April. Total PCE inflation was 3.9% in year-over-year terms in May and core inflation 3.4%—but this overstates inflation since prices fell outright last spring. Compared with February 2020, PCE prices were up 3.3% in May and core PCE prices up 3.1%.

Auto supply chain problems made the trade deficit widen in May, but the trend is still lower. The trade deficit in goods rose to $88.1 billion dollars from $85.7 billion in April, revised from the originally-reported $85.2 billion. Exports fell $0.5 billion (0.3%) to $144.3 billion in May and gave back some of April's $1.6 billion (1.1%) increase. Exports of automotive vehicles accounted for all of the net decline, falling $0.56 billion or 4.7% on the month; changes in other categories of goods exports were smaller and mostly offsetting. Imports rose $1.9 billion on the month (0.8%), partially reversing April's $4.6 billion (1.9%) decline. Imports of industrial supplies, foods/feeds/beverages, and consumer goods rose on the month. Auto imports fell $0.18 billion on the month. Shortages of semiconductors and other components held back auto exports and to a lesser extent imports in May, leading to a small widening of the trade deficit; exports and imports of capital goods also fell on the month, further sign of supply chain problems. Even so, May's goods trade deficit was down $3.8 billion from March's record high. And since motor vehicle and parts production rose 6.7% in May's industrial production report, auto exports should rise near-term. Existing home sales fell 5.9% in May to a

769,000 annualized rate, down from 817,000 annualized in April and 886,000 in March; March's and April's levels were revised down 3% and 5%, respectively. Supply issues and the sharp jump in home prices slowed existing home sales somewhat, but demand remains extremely strong, and supply will rise in coming months as older homeowners downsize.

Early sentiment surveys for June point to a continued strong recovery, which would be even faster if not for supply chain bottlenecks. The Markit services PMI for the U.S. pulled back to 64.8 in the June flash estimate from a record-high 70.4 in May, and the manufacturing PMI rose to 62.6 from 62.1. Businesses responding to both surveys continue to report strong growth despite hiring difficulties, supply chain shortages, and rising prices. The University of Michigan's consumer sentiment index was revised down to 85.5 in the June final release from 86.4 in the preliminary release, but was still up from 82.9 in May, and was the second-strongest since the pandemic.

The Bureau of Labor Statistics' June jobs report, to be released Friday July 2, is forecast to show the unemployment rate falling to 5.6% from May's 5.8%, with nonfarm payroll employment up 600,000 on the month and average hourly earnings up 0.4% on the month and 3.6% on the year.

EUROZONE: The Eurozone continues to follow the same reopening-fueled recovery path as the United States, lagged by a couple of months due to the slower start of vaccinations. The Markit manufacturing PMI for the Eurozone edged up to 62.4 in the June flash estimate from 62.2 in May, while the services PMI rose to 58.0 from 55.2 and was the highest since January 2018. The composite PMI—the simple average of the manufacturing and services PMIs—was the strongest since 2006. The European Commission's Consumer Confidence Index rose to the highest since January 2018 in June.

CANADA: Wholesale sales rose 1.1% in May from April according to the advance estimate from Statistics Canada; Canada's statistics agency launched this new statistic post-pandemic to provide a more timely measure of the recovery. Higher sales of machinery, equipment and supplies were tailwinds to May's wholesale sales increase. Manufacturing sales rose 1.0% in the May advance estimate, and growth was broad-based across manufacturing sectors. Manufacturing sales are reported in nominal terms, so much of May's increase reflects higher prices instead of volumes (May producer prices have not yet been released).

UNITED KINGDOM: As expected, the Bank of England held its monetary policy stance unchanged at its June 24 Monetary Policy Committee decision: They held the Bank Rate steady at 0.1% and continue to target a £875 billion pound sterling stock of government bond purchases (QE). The BoE revised up their nowcast of real GDP for the second quarter of 2021, but still see the level of real GDP at around two and a half percent below the pre-crisis level; this is quite a bit worse than the United States, where real GDP is almost definitely above the pre-crisis level in the second quarter. Like the Fed, the BoE describes the second quarter of 2021's jump in consumer prices as "transitory." They reiterated their commitment to keeping monetary policy in the current highly expansionary stance "at least until there is clear evidence that significant progress is being made in eliminating spare capacity and achieving the 2% inflation target sustainably." The Bank of England is likely to begin tapering its quantitative easing program before year-end, and to start raising the Bank Rate in mid-2022 if the recovery continues to proceed well.

The Markit services PMI for the UK dipped to 61.7 in the June flash estimate from 62.9 in May but still points to a rapid recovery of services activity. Similarly, the manufacturing PMI dipped to 62.0 from 63.0. Supply chain disruptions remain severe and inflation widespread in both the manufacturing and services sectors.

JAPAN: The Jibun au Bank manufacturing PMI for Japan fell to 51.5 in the June flash estimate from 53.0 in May, while the services PMI rose to 47.2 from 46.5. CPI for the Tokyo metro area rose 0.3% from a month earlier in the June preliminary release, with core CPI excluding food and energy up 0.1%. From a year earlier, both total and core CPI were unchanged.

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