1st Quarter 2017

# LOUISVILLE-LEXINGTON MARKET OUTLOOK

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## JOB SITUATION

Job growth in Louisville-Lexington downshifted from the 2.5 percent average growth rate per year it experienced between 2012 and 2015 to a little less than 2 percent in 2016. Business and professional services in Lexington retrenched throughout the year while hiring in Louisville's transportation and logistics industry took a breather. Those aside, the regional economy is on sound footing and there's no indication that these industries hit anything other than speed bumps. The ongoing increase of e-commerce bodes well for the logistics industry in the region. Continued improvement in housing markets throughout the country is lifting demand for household goods made in the region. Consumer spending continues to be the main engine of economic growth for the U.S. economy and this benefitted the region by lifting auto sales to their highest level on record in 2016. Strong auto sales nationwide, in turn, supported production and income gains in the region. Local consumer spending is strong as well, driving solid gains in retail, leisure and hospitality employment. Finally, education and healthcare continue to be reliable growth drivers and made the biggest contribution to employment growth in 2016. The unemployment rate hovered just above 4 percent in the second half of 2016 (Chart 1). Labor force growth quickened during this time, suggesting strong confidence in the regional economy.

**Chart 1**
**Job Growth, (% change year ago) & Unemployment Rate, (%, SA)**

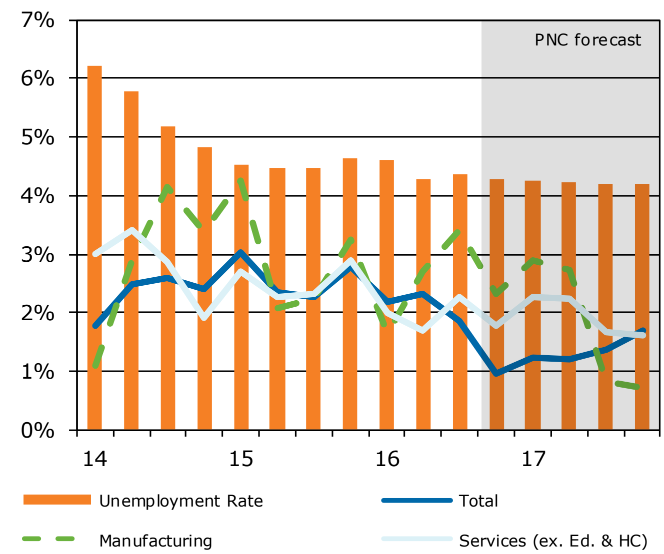


Chart sources: Bureau of Labor Statistics; The PNC Financial Services Group

## INCOME

A tight labor market and a favorable mix of jobs being created will lift wage growth in the region. The jobless rate is projected to average a low 4.2 percent in 2017 even as the workforce expands. This rate of unemployment will be low enough to generate wage pressures. Also, employers in healthcare, finance and IT have announced large expansions that will bring mid- to high-wage employment in those industries. Even with gasoline prices inching higher, wage gains will preserve consumer purchasing power. Longer term, income growth will likely settle at a pace in line with national income growth. Because the region's

**Chart 2**
**Median Household Income (Ths. $, SA)**

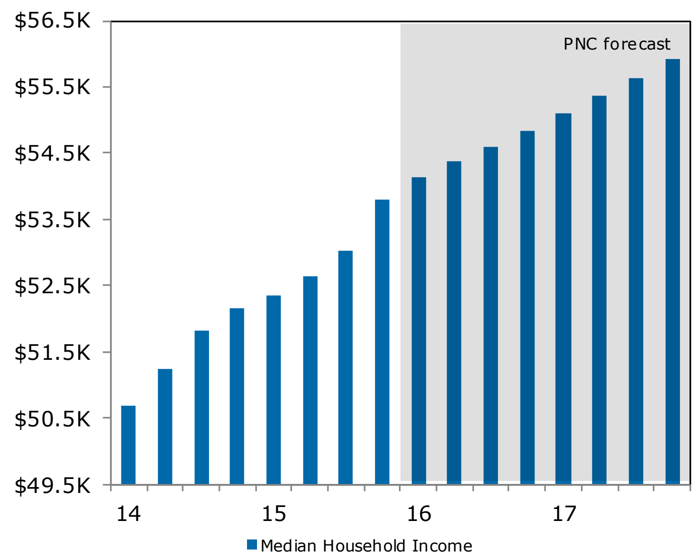


Chart sources: Bureau of Census; Moody's Analytics; The PNC Financial Services Group median income is a little below the U.S.'s median income, it is not likely to narrow the income gap between itself and the nation over the long-term (Chart 2). The good news is that living costs are also lower than the national average and this ensures purchasing power in the region is comparable to the nation. Also, unlike many other manufacturing-heavy regions, Louisville-Lexington has a variety of growth drivers to lean on as manufacturing becomes a smaller share of employment in the long-run. This creates the possibility that income grows faster than expected as higher-paying service jobs fill in the gap.

## HOUSING

Though home price appreciation can be volatile, the real estate market is still relatively healthy (Chart 3). A moderate pace of household formations is supporting housing demand as are persistent jobs and income growth, high affordability and easier access to credit. Permitting is rising at a strong rate but is not adding much excess supply. Single-family home prices will likely rise between 4 and 5 percent in 2017 and 2018, thanks to a good balance between supply and demand. Longer term, income growth and household formations that are about average will lead to moderate price increases and construction.

## DEMOGRAPHICS

The area's industrial diversity and low living costs have long attracted a steady stream of new residents migrating into the area. The Great Recession acted to slow demographic gains, but the population continues to grow moderately (Chart 4). Population growth will be stable over the next several years, though it will likely be slower than in the previous decade. The University of Kentucky and the University of Louisville will contribute to the market area's stability, and will support economic growth by supplying educated workers. Of the two metro areas, Lexington's demographic profile is more favorable for long-term economic growth. First, higher educational attainment increases Lexington's chances of attracting high-wage employment. About 36 percent of adults over age 25 hold at least a bachelor's degree versus 31 percent in the U.S. and 28 percent in Louisville. Lexington's population is younger and hence, the potential to improve labor force participation is higher than in Louisville or the U.S.

**Chart 3**
**Home Sales (Ths., SAAR)**
**& Price Growth, (% change year ago)**

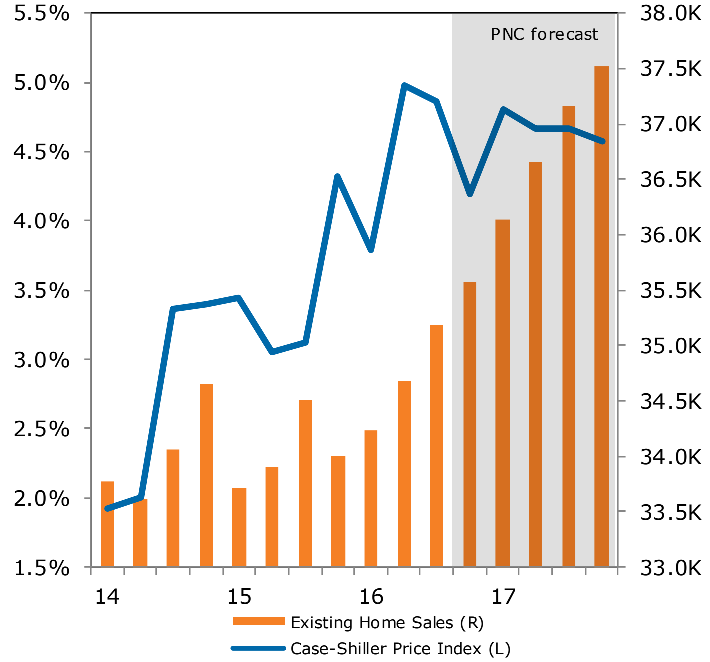


Chart sources: National Association of Realtors; Fiserv, Inc.; The PNC Financial Services Group

**Chart 4**
**Demographic Growth, (% change year ago)**
**& Net Migration, (Ths., SA)**

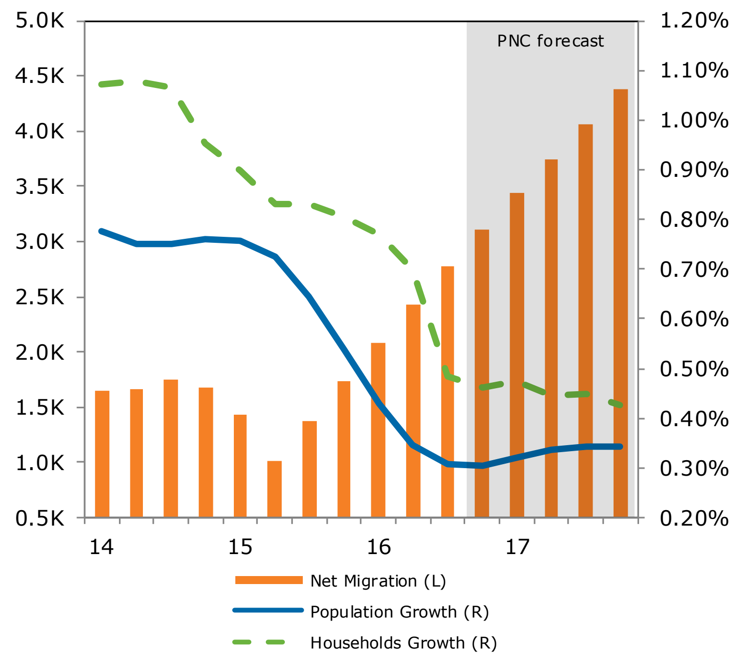


Chart sources: Bureau of Census; Bureau of Economic Analysis Moody's Analytics; The PNC Financial Services Group

## OUTLOOK SUMMARY

Louisville-Lexington's economy will settle into its long-term growth rate in 2017 as it leaves the Great Recession further behind. The U.S. economy will continue to grow moderately over the forecast horizon and this is a plus for the region, as many of the market area's core economic drivers respond strongly to macroeconomic trends. Regional growth will be broad-based and will include manufacturing, transportation, education, healthcare, finance and professional services. Housing markets across the country are gaining traction as finances improve for millenials and they begin to buy homes. This, in conjunction with stronger consumer finances overall and strong auto demand will bolster manufacturers such as GE at Appliance Park and auto producers and parts suppliers. The increasingly important role e-commerce is playing in retailing is a boon for regional transportation and distribution firms such as UPS and Amazon. The market area's unemployment rate will likely fluctuate around 4.2 percent throughout the year. Other aspects of the market area's economy, such as house prices and home sales, will remain on sound footing.

The regional economy's success in the coming years will be credited to its diverse industrial base. It hosts a wide array of large, successful employers from auto manufacturing to education and professional services. This sustains its ability to weather most economic turbulence, and at least to suffer less through downturns as was proven during The Great Recession. The University of Kentucky and the University of Louisville will be stable sources of employment and will attract young people to the area. Other big players such as Toyota, Ford, GE and UPS provide well-paying jobs in dynamic industries that respond strongly to the business cycle. Demographic trends are stable as a result of this resilience, which in turn keeps income growth competitive.

## FORECAST TABLE

| | U.S. | | | Louisville-Lexington | | |
|---|---|---|---|---|---|---|
| | 2015 | 2016E | 2017F | 2015 | 2016E | 2017F |
| Employment Growth, (% change) | 2.1 | 1.8 | 1.5 | 2.6 | 1.8 | 1.4 |
| Unemployment Rate, (%) | 5.3 | 4.9 | 4.5 | 4.5 | 4.4 | 4.2 |
| Median Household Income, (Ths. $) | 55.8 | 57.1 | 58.2 | 53.0 | 54.5 | 55.5 |
| House Prices**, (% change) | 4.6 | 5.2 | 4.6 | 3.5 | 4.5 | 4.7 |
| Single-Family Permits* (% change) | 10.2 | 10.0 | 8.2 | 10.9 | 12.0 | 10.1 |
| Multifamily Permits* (% change) | 11.5 | -0.9 | 6.6 | -5.5 | 31.7 | -43.3 |

*E = Full year estimate, F = PNC forecast, *U.S. starts*

| | U.S. | | Louisville-Lexington | |
|---|---|---|---|---|
| | 2007-2012† | 2012-2017† | 2007-2012† | 2012-2017† |
| Employment Growth, (% change) | -0.6 | 1.8 | -0.4 | 2.1 |
| Unemployment Rate, (%) | 7.7 | 6.0 | 7.6 | 5.5 |
| Median Household Income, (Ths. $) | 50.8 | 54.7 | 47.7 | 52.3 |
| House Prices**, (% change) | -4.8 | 6.1 | -0.2 | 3.7 |
| Single-Family Permits* (% change) | -12.3 | 9.6 | -12.0 | 8.2 |
| Multifamily Permits* (% change) | -4.2 | 11.1 | 5.7 | -8.4 |

*E = Full year estimate, F = PNC forecast, *U.S. starts, †per annum*

Table sources: Bureau of Census; Bureau of Labor Statistics; Bureau of Economic Analysis; National Association of Realtors; National Association of Home Builders; FHFA; Moody's Analytics; The PNC Financial Services Group

## LONG-RUN EMPLOYMENT TRENDS

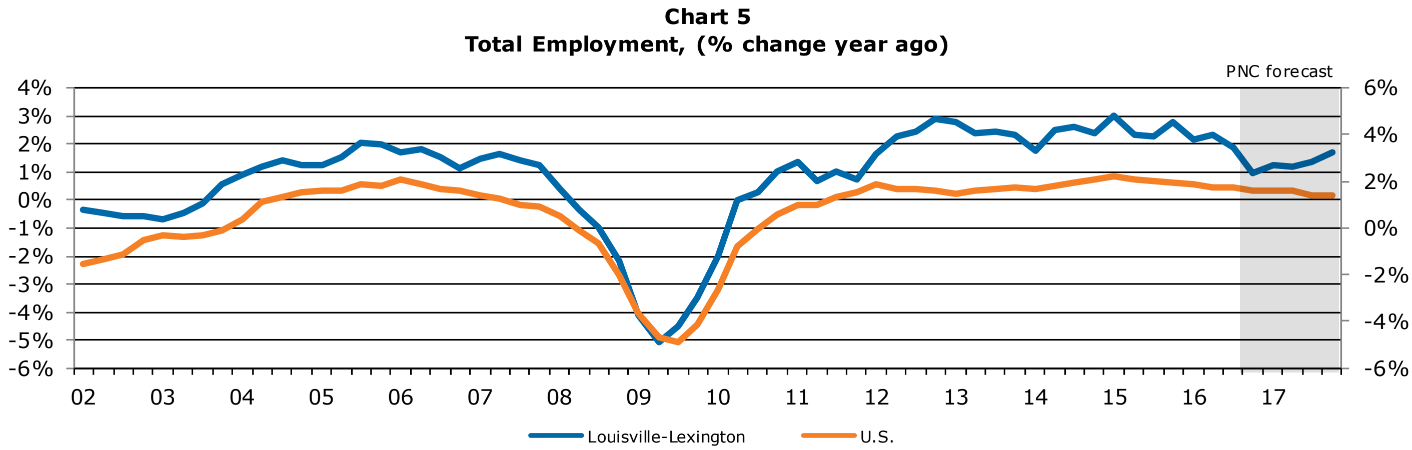


Chart sources: Bureau of Labor Statistics; The PNC Financial Services Group

## LONG-RUN DEMOGRAPHIC TRENDS

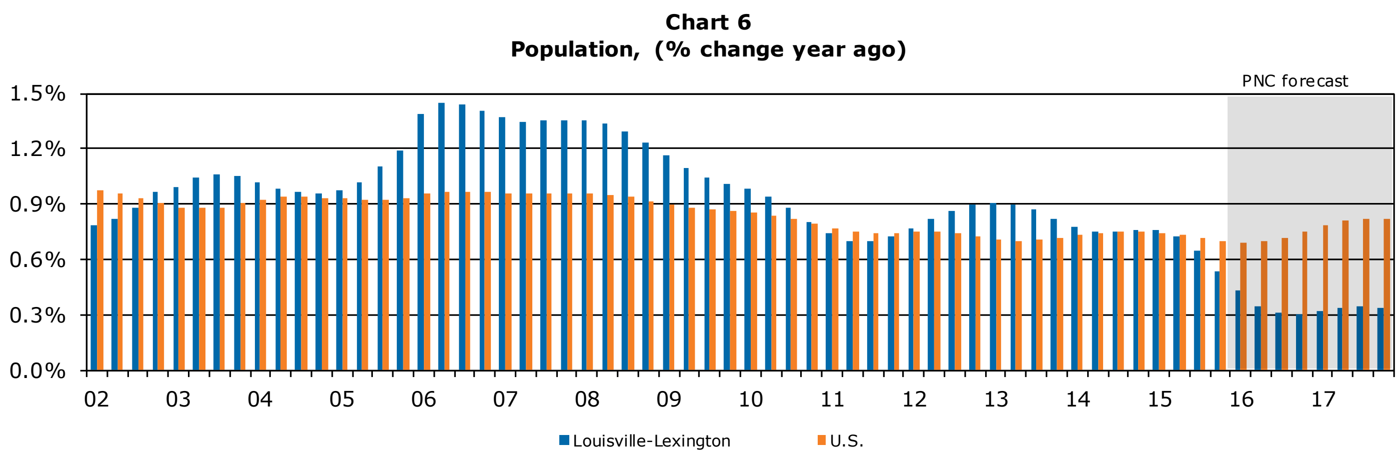


Chart sources: Bureau of Census; Moody's Analytics; The PNC Financial Services Group

## LONG-RUN HOUSE-PRICE TRENDS

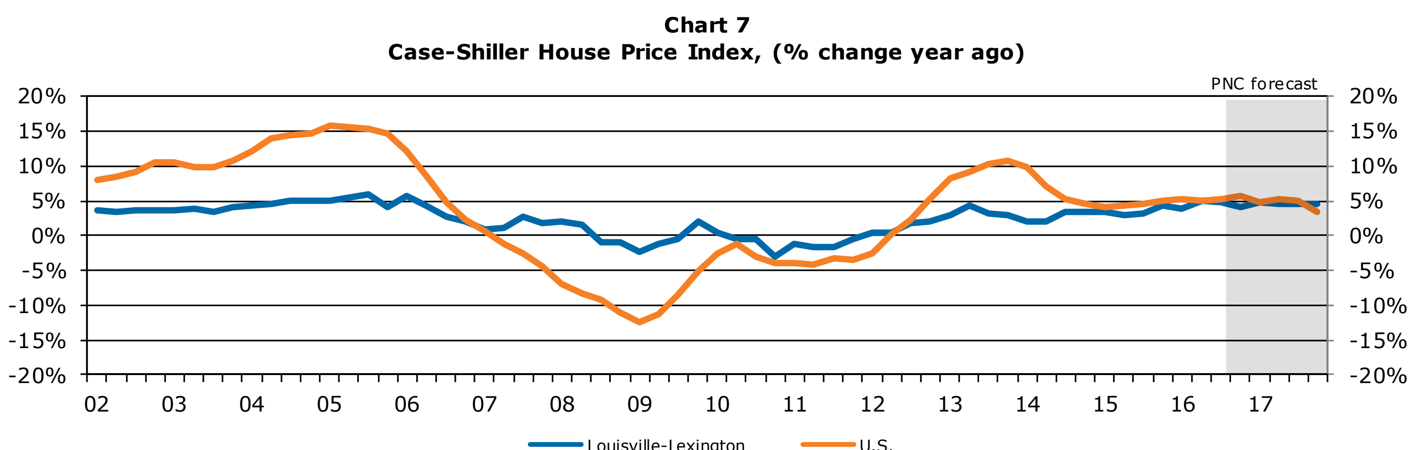


Chart source: National Association of Realtors; Fiserv, Inc.; The PNC Financial Services Group

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