

NORTHERN ALABAMA MARKET OUTLOOK

Stuart Hoffman
Chief Economist

Gus Faucher
Deputy Chief Economist

William Adams
Senior Economist

Kurt Rankin
Economist

Mekael Teshome
Economist

THE PNC FINANCIAL SERVICES GROUP | The Tower at PNC Plaza | 300 Fifth Avenue | Pittsburgh, PA 15222-2401

JOB SITUATION

The Northern Alabama economy, which includes six metro areas stretching from Montgomery north to Huntsville, is growing steadily (Chart 1). Manufacturing gained momentum in the second half of 2016 as a number of weights lifted. After a rough couple of years, metals producers gained some breathing space as steel prices rose, energy demand improved and high tariffs stemmed the tide of cheap imports. Last year was the best on record for auto sales and this was a major boost to the region's supply chain. Non-durable goods producers, such as food and paper manufacturers, did not receive much of a cyclical boost from improving macroeconomic conditions the way durable goods producers did. Nevertheless, they are holding steady. Healthcare, education and professional services have been significant and reliable growth drivers. Also, persistent jobs and income growth is buttressing consumer industries such as retail, leisure and hospitality. Payroll employment in the region has now recovered to its pre-recession peak. The combined region's unemployment rate rose to 5.7 percent in December 2016 from a cyclical low of 5.0 percent in September 2016, but this was because workforce growth outpaced employment growth.

INCOME

Despite the positive outlook for job growth, wage growth is unlikely to improve much in 2017 because significant slack remains in the labor market. Fortunately, the drop in the median household income during the recession was mild relative to the U.S. and the recovery has lifted median income to almost six percent higher than its pre-recession peak (Chart 2). Per capita incomes range widely across the region. At the upper end of the range, per capita income in Birmingham and Huntsville is 18 percent higher than the state average and just shy of the U.S. average. Financial services and well-paying wholesale trade and transportation have big presences in Birmingham. A well-educated workforce supports Huntsville's large cluster of defense-related tech employment and

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

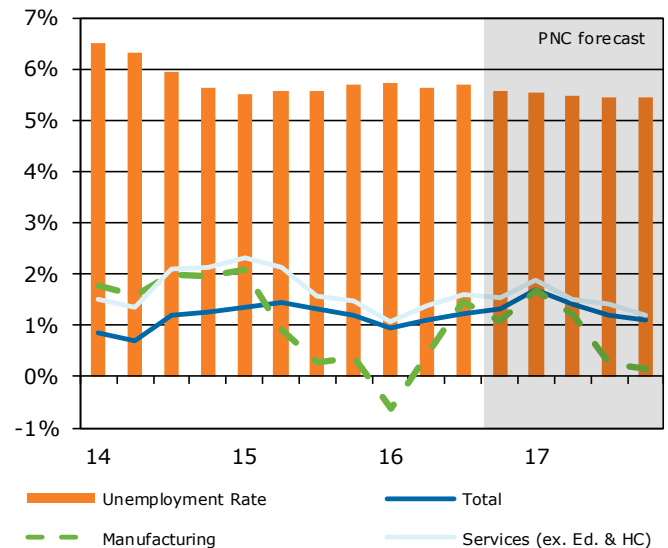


Chart sources: Bureau of Labor Statistics; The PNC Financial Services Group

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

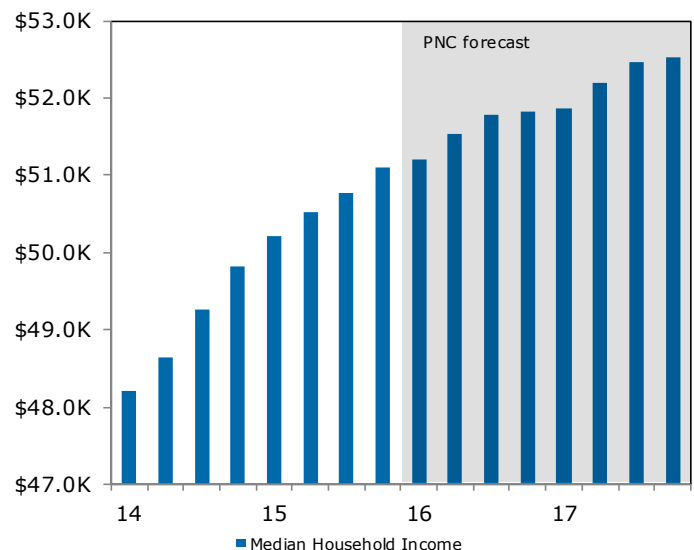


Chart sources: Bureau of Census; Moody's Analytics; The PNC Financial Services Group



incomes. At the bottom end of the spectrum, a large student population and a workforce tied to education keep Auburn’s per capita income 15 percent below the state average.

HOUSING

Home prices in Northern Alabama will rise 3 to 4 percent per year on average over the next several years (Chart 3). This pace is approximately in line with the national average. Home sales are increasing but construction remains subdued and this is keeping inventory in check. Prices fell by 10 percent from peak-to-trough during the Great Recession—far less than the national drop of about 26 percent. The shallower market correction is a positive for local consumer spending because households lost a smaller portion of their wealth than average. Another of the region’s advantages is that housing is affordable relative to local incomes, especially in Decatur and Montgomery. Auburn is a notable exception, where local prices relative to the average income are higher than the U.S. average. Easier access to credit and a continued increase in household formations will support housing demand. One downside risk to the housing outlook is that consistent increases in home prices could be delayed if the foreclosure pipeline takes longer to clear than expected. Parts of the Birmingham and Huntsville metro areas especially have higher-than-average foreclosure burdens.

DEMOGRAPHICS

Northern Alabama generally enjoys strong population growth that is buttressed by consistently positive in-migration (Chart 4). In-migration started to weaken significantly in 2010 and remained soft through 2015. This year will likely bring stronger in-migration and household formations as the labor market continues to heal. Over the long term, the area’s population will likely grow more slowly than the national average. However, there is some upside potential. Low business costs, strong infrastructure linkages and large universities will attract business investment. This, in turn, attracts job seekers who are also looking for low living costs and affordable housing. One key weakness in the area’s demographic profile is its low rate of labor force participation. Labor force participation rates range from about 2 percentage points below the national rate in Montgomery to about 5 points below in Decatur.

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

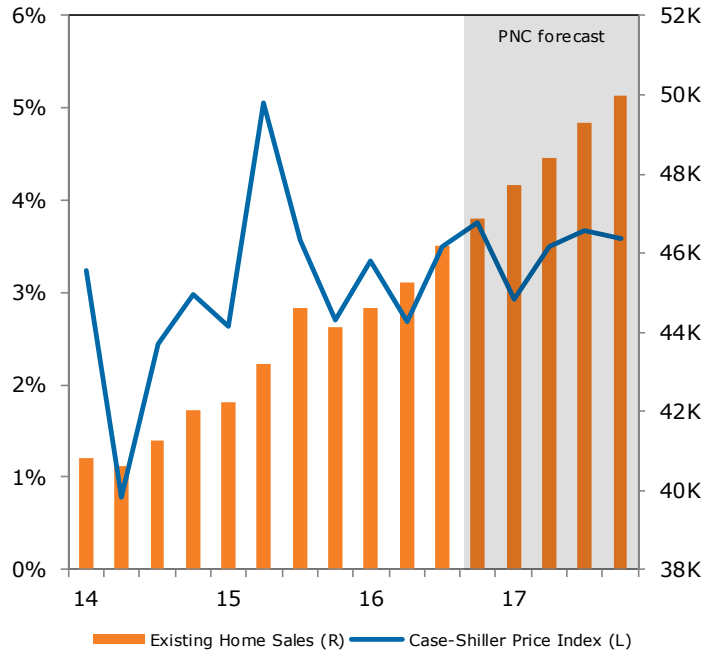


Chart sources: National Association of Realtors; Fiserv, Inc.; The PNC Financial Services Group

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

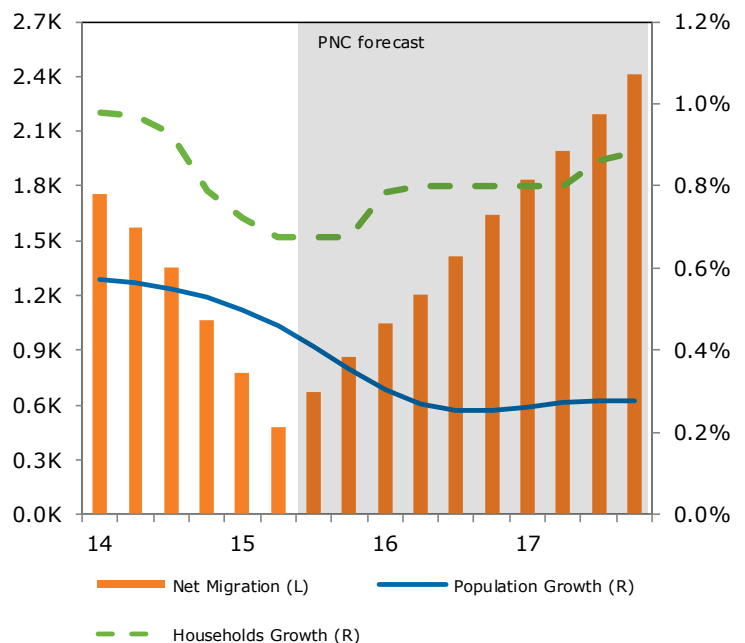


Chart sources: Bureau of Census; Bureau of Economic Analysis; Moody’s Analytics; The PNC Financial Services Group

OUTLOOK SUMMARY

Northern Alabama's economy will maintain a steady pace of job growth over the next couple of years. The U.S. economy's expansion will sustain manufacturing production and employment in the region. Nationwide, auto sales are have plateaued at a high level while steel prices and demand are set to trend higher. Government employment will increase as continued economic growth improves revenues. That said, the public sector faces both upside potential and downside risks. State spending will still need to be tight to balance the books and Jefferson County is still hurting from its 2011 bankruptcy. On the upside, proposed increases to Federal defense spending would be a plus, especially for Huntsville and Montgomery. Much of the region's outlook will depend on how these risks unfold, because one-fifth of total employment in the area is in the public sector. For the private sector, a trade war with either Mexico or China would be an important downside risk, given that Northern Alabama businesses import heavily from Mexico and export to China.

Although economic growth will likely improve across the board, performances will vary widely within the region in the next couple of years. Anchored by Auburn University and supported by a growing tech industry, Auburn will lead the pack with job growth that will top the national rate. Tuscaloosa, too, will enjoy above-average driven by auto-focused manufacturing. On the other end of the spectrum, Decatur's concentration in non-durable goods production, such as poultry, will cause the metro area to trail the U.S. Such industries do not respond as strongly to the macro business cycle and will not benefit from nationwide growth in the housing and auto industries. The rest of the region should approximately match the U.S. rate of growth.

The area's longer-term prospects are brighter. Low business costs, strong infrastructure linkages, and large universities will drive investment and above-average payroll growth. In-migration will drive healthy population growth, thanks to low living costs and affordable housing.

FORECAST TABLE

	U.S.			Northern AL		
	2015	2016E	2017F	2015	2016E	2017F
Employment Growth, (% change)	2.1	1.8	1.5	1.3	1.2	1.3
Unemployment Rate, (%)	5.3	4.9	4.5	5.6	5.7	5.5
Median Household Income, (Ths. \$)	55.8	57.1	58.2	50.6	51.6	52.3
House Prices, (% change)	4.6	5.2	4.6	3.5	3.3	3.4
Single-Family Permits* (% change)	10.2	10.0	8.2	8.5	7.4	3.0
Multifamily Permits* (% change)	11.5	-0.9	6.6	-32.0	2.6	2.2

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

	U.S.		Northern AL	
	2007-2012†	2012-2017†	2007-2012†	2012-2017†
Employment Growth, (% change)	-0.6	1.8	-0.9	1.2
Unemployment Rate, (%)	7.7	6.0	7.4	6.1
Median Household Income, (Ths. \$)	50.8	54.7	46.1	49.7
House Prices, (% change)	-4.8	6.1	-1.7	3.0
Single-Family Permits* (% change)	-12.3	9.6	-13.3	4.8
Multifamily Permits* (% change)	-4.2	11.1	-5.9	-1.7

**U.S. starts, †per annum, **Case-Shiller House Price Index*

LONG-RUN EMPLOYMENT TRENDS

Chart 5
Total Employment, (% change year ago)

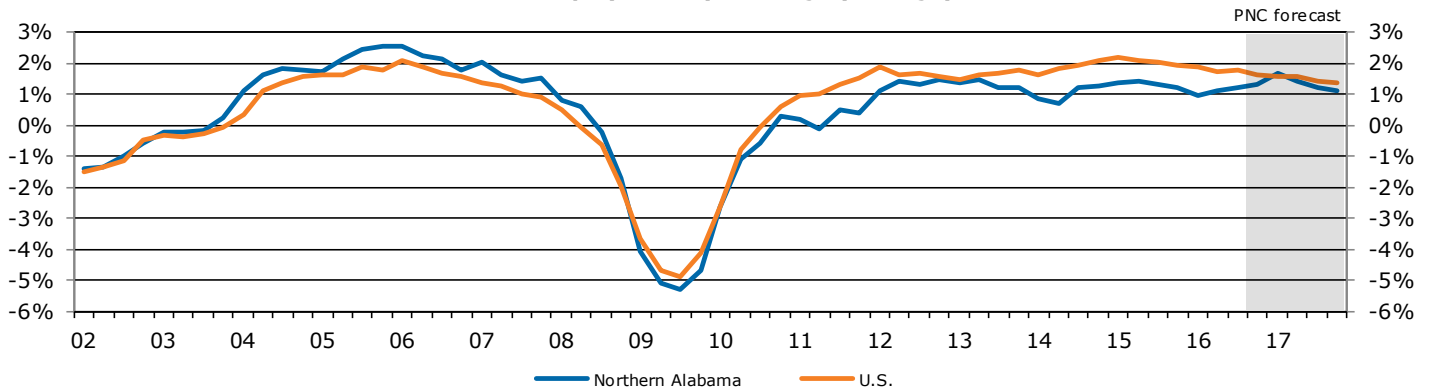


Chart sources: Bureau of Labor Statistics; The PNC Financial Services Group

LONG-RUN DEMOGRAPHIC TRENDS

Chart 6
Population, (% change year ago)

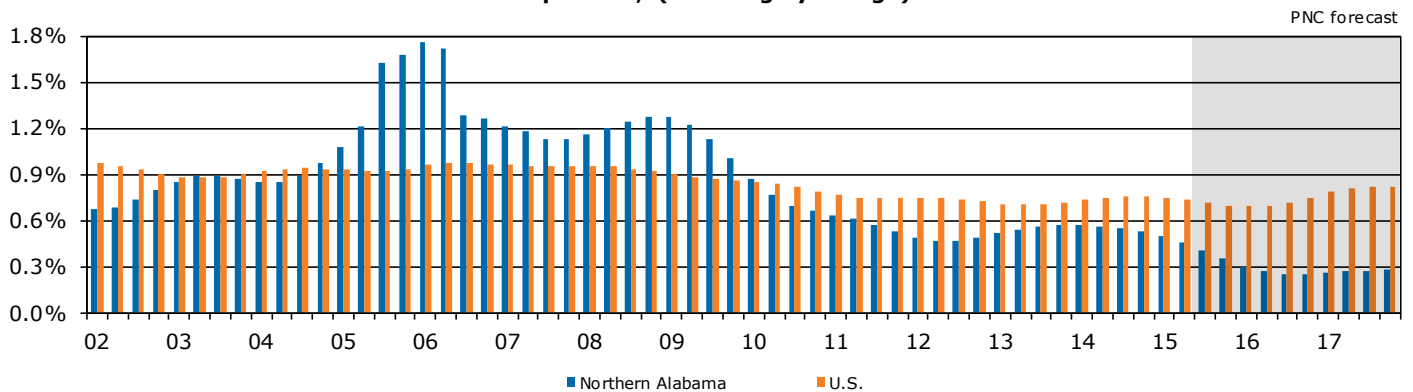


Chart sources: Bureau of Census; Moody's Analytics; The PNC Financial Services Group

LONG-RUN HOUSE-PRICE TRENDS

Chart 7
Case-Shiller House Price Index, (% change year ago)

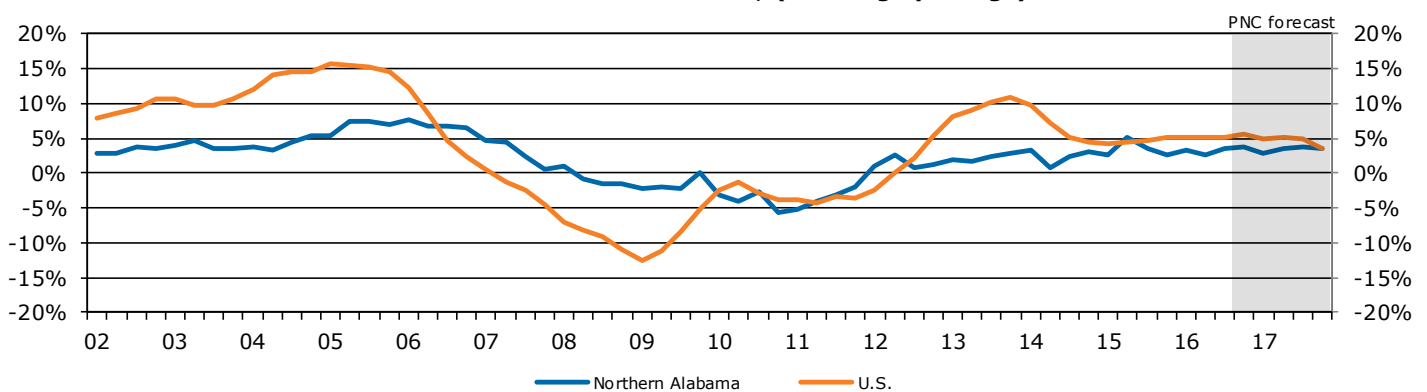


Chart source: National Association of Realtors; Fiserv, Inc.; The PNC Financial Services Group

Visit <http://www.pnc.com/economicreports> to view the full listing of economic reports published by PNC's economists.

Disclaimer: The material presented is of a general nature and does not constitute the provision of investment or economic advice to any person, or a recommendation to buy or sell any security or adopt any investment strategy. Opinions and forecasts expressed herein are subject to change without notice. Relevant information was obtained from sources deemed reliable. Such information is not guaranteed as to its accuracy. You should seek the advice of an investment professional to tailor a financial plan to your particular needs.