

SOUTH BEND MARKET OUTLOOK

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JOB SITUATION

The South Bend market area, which is comprised of the South Bend, Elkhart and Michigan City metropolitan statistical areas, took a considerable turn for the worse in 2016. Manufacturers shed jobs over the year, led by an ongoing lockout at major employer Honeywell International, Inc. Temporary workers have been brought in to keep some level of operations, but the incomes lost to the lockout are more pressing for South Bend's local economy overall. A lack of consumer spending flows through to other local businesses, at the very least delaying new hiring and likely resulting in job losses downstream as well. Service industry employers maintained positive hiring trends through this past year's slowdown, but gains in 2017 are likely to be slower still. Professional & business service industry hiring has stalled, leaving little in the way of offsetting growth potential so long as manufacturing hiring in the market area is absent.

INCOME

Median household income in South Bend (Chart 2) is below the U.S. and Midwest regional averages. Growth in incomes has stalled as a result of manufacturing industry retrenchment endured in 2016. Wage growth potential will be dampened even after the market area's manufacturing employment issues right themselves. That eventual recovery will reorganize the local economy's labor force, but businesses will not be in a position to throttle up hiring until consumer sentiment, and thereby consumer spending, regains stability. Vehicle sales at the national level continue at a pace near all-time highs, which provides some degree of income stability. South Bend hosts a significant presence of auto parts manufacturers, and will benefit on the employment and income fronts while auto sales remain strong. But until labor market disputes are resolved at Honeywell International, Inc., one of South Bend's largest employers, income growth will underperform its potential.

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

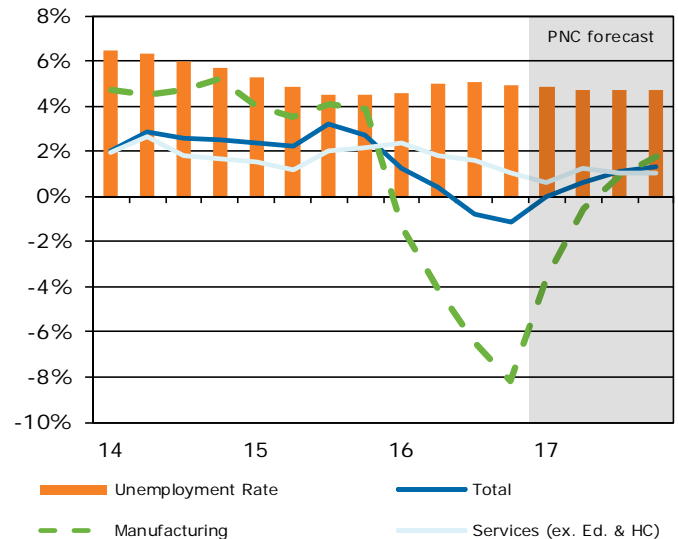


Chart sources: Bureau of Labor Statistics; The PNC Financial Services Group

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

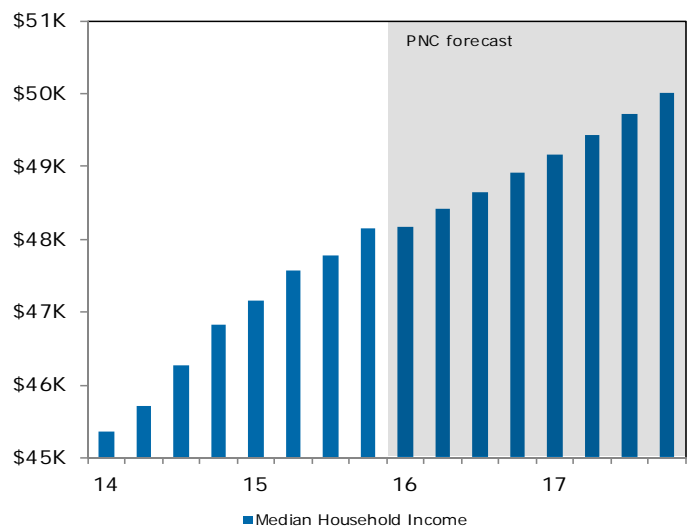


Chart sources: Bureau of Census; Moody's Analytics; The PNC Financial Services Group



HOUSING

South Bend's housing market is holding up well despite job market and income growth instability over the past year. Home price appreciation (Chart 3) settled into a pace not much slower than the national average in 2015 after lagging the national recovery for most of the post-recession period. Home values across South Bend's three metropolitan areas have all regained their pre-recession highs according to the Case-Shiller house price index. Demand-side support will struggle to maintain the momentum necessary to continue to match national growth averages over the near-term horizon. But some slowdown in South Bend's home price growth would not be unexpected, as the local economy hosts a less-dynamic housing market historically than much of the country.

Damaged confidence in the local economic environment has also prevented residential activity from regaining any semblance of its pre-bubble form. New building activity is still less than half of the pace observed prior to bubble-fueled growth overshoot. Given a subpar outlook in terms of job creation for the near term, a lack of new building is perhaps a blessing in disguise, as it will prevent oversupply from dampening future home price growth potential.

DEMOGRAPHICS

South Bend's demographic trends had stabilized from the damage inflicted by the recession, but manufacturing employment woes are applying new downward pressure. Population growth may remain slightly positive in the near term (Chart 4), but net out-migration will be a detracting influence. Stronger business investment and expansion would go a long way toward helping this cause, by creating more competition for labor resources, and thus the upward pressure on wages that would help to attract skilled workers to the market area. But although employment levels have come a long way during the recovery, median income remains significantly below the Midwest region's average. Relatively low median income in South Bend puts the market area at a disadvantage in the battle to retain labor resources, and will weigh on its ability to recharge population growth beyond its current pace in the near term.

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

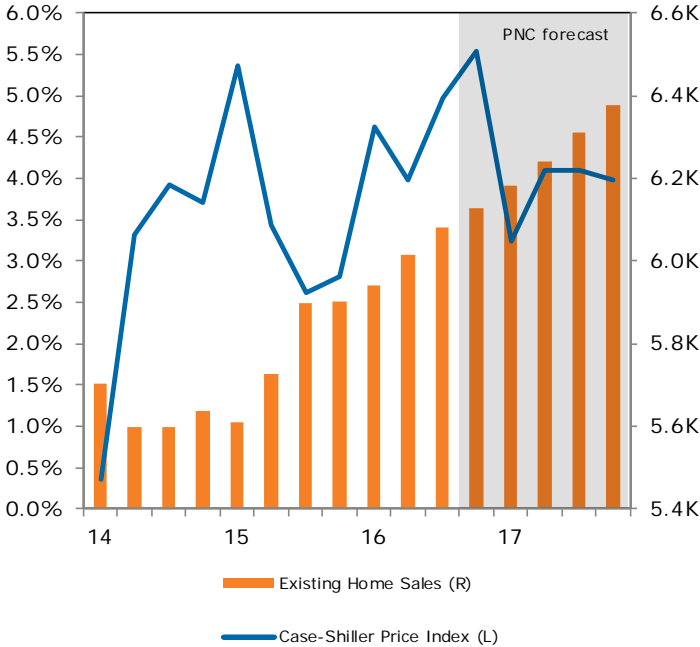


Chart sources: National Association of Realtors; Fiserv, Inc.; The PNC Financial Services Group

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

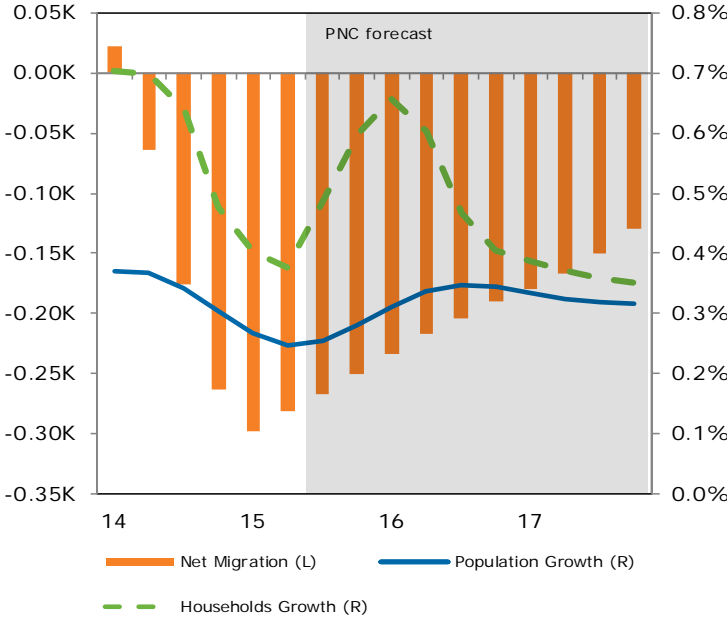


Chart sources: Bureau of Census; Bureau of Economic Analysis; Moody's Analytics; The PNC Financial Services Group

OUTLOOK SUMMARY

South Bend will struggle to maintain positive economic growth through the coming year. The job market is bifurcated between service industry employers dealing with diminished consumer sentiment and spending, and manufacturing jobs that declined severely throughout 2016. Even manufacturing industries on the whole are split between stable auto-related producers, and aerospace and residential components manufacturers which are experiencing weaker demand and in some cases are dealing with labor discord. The potential for an external boost from the national economy represents some upside potential for South Bend's economy. New business and infrastructure investment nationwide would further bolster job creation and income gains for South Bend as goods produced in the market area would find demand from outside of the local economy.

Housing and demographic trends in South Bend are stalled alongside the market area's job trends. There were not significant imbalances in either area entering the recession, and as a result the market area's current prospects for housing market improvement are not entirely sunk. But progress will be slow so long as household balance sheets are unsettled. South Bend offers highly competitive business cost advantages and a skilled labor pool—both of which will keep housing and demographic trends stable over the longer run once near term stability can be regained.

Beyond its traditional manufacturing presence, South Bend is home to the University of Notre Dame, a source of economic strength for the market area. The University's presence combines with health care providers such as Memorial Health System and St. Joseph Regional Medical Center to offer a stable base from which to reset growth patterns. Looking ahead, South Bend will need to continue to build its non-manufacturing core if it is to establish a less cyclically sensitive economic base.

FORECAST TABLE

	U.S.			South Bend		
	2015	2016E	2017F	2015	2016E	2017F
Employment Growth, (% change)	2.1	1.7	1.5	2.6	-0.1	0.8
Unemployment Rate, (%)	5.3	4.9	4.5	4.8	4.9	4.8
Median Household Income, (Ths. \$)	55.8	57.1	58.2	47.7	48.5	49.6
House Prices, (% change)	4.6	5.0	3.7	3.5	4.8	3.9
Single-Family Permits* (% change)	10.2	8.5	4.4	10.2	3.2	6.1
Multifamily Permits* (% change)	11.5	-2.5	2.1	6.2	-48.1	-58.9

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

	U.S.		South Bend	
	2007-2012†	2012-2017†	2007-2012†	2012-2017†
Employment Growth, (% change)	-0.6	1.8	-2.0	1.4
Unemployment Rate, (%)	7.7	6.0	9.6	6.3
Median Household Income, (Ths. \$)	50.8	54.7	45.9	46.9
House Prices, (% change)	-4.8	5.9	-1.9	3.1
Single-Family Permits* (% change)	-12.3	8.5	-19.2	8.9
Multifamily Permits* (% change)	-4.2	9.8	-0.7	-40.8

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

LONG-RUN EMPLOYMENT TRENDS

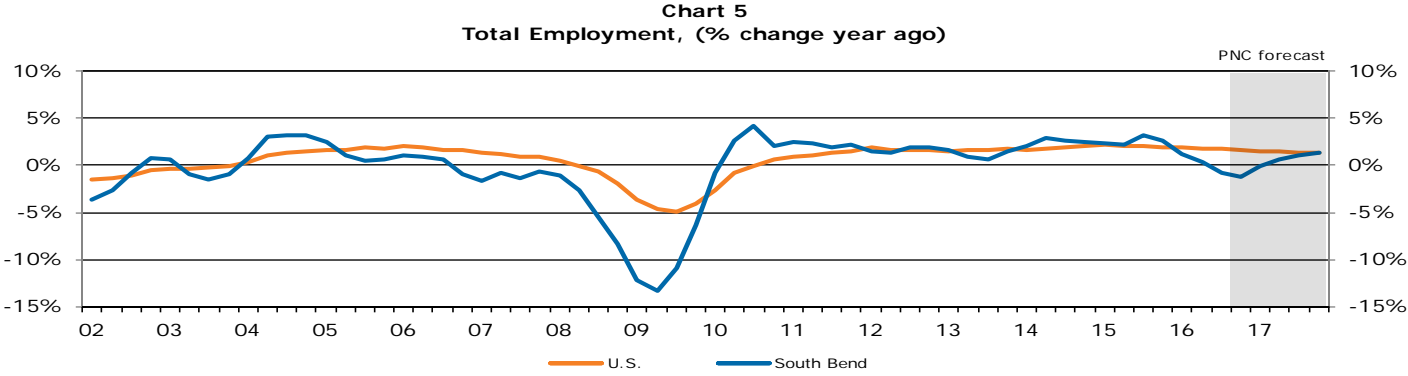


Chart sources: Bureau of Labor Statistics; The PNC Financial Services Group

LONG-RUN DEMOGRAPHIC TRENDS

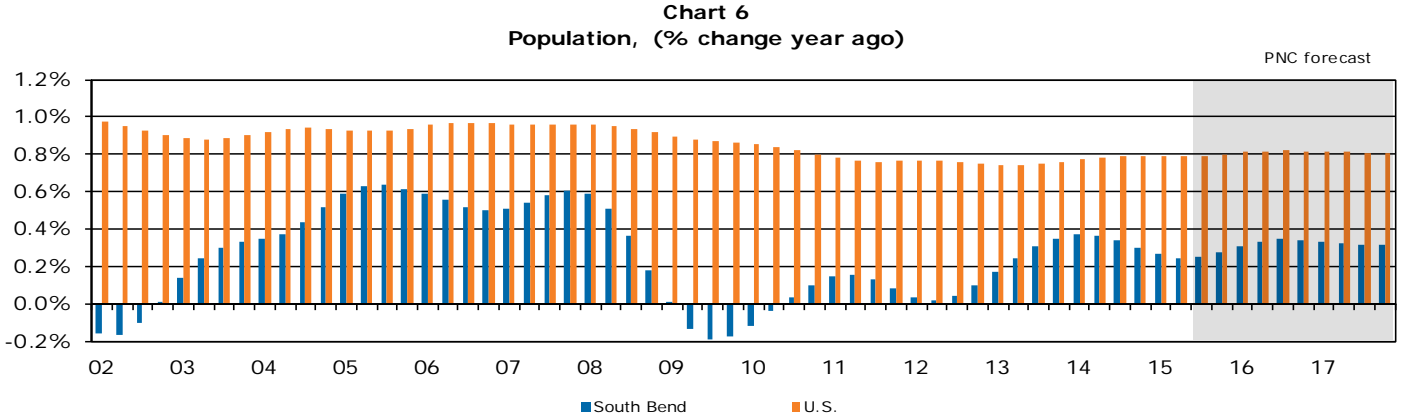


Chart sources: Bureau of Census; Moody's Analytics; The PNC Financial Services Group

LONG-RUN HOUSE-PRICE TRENDS

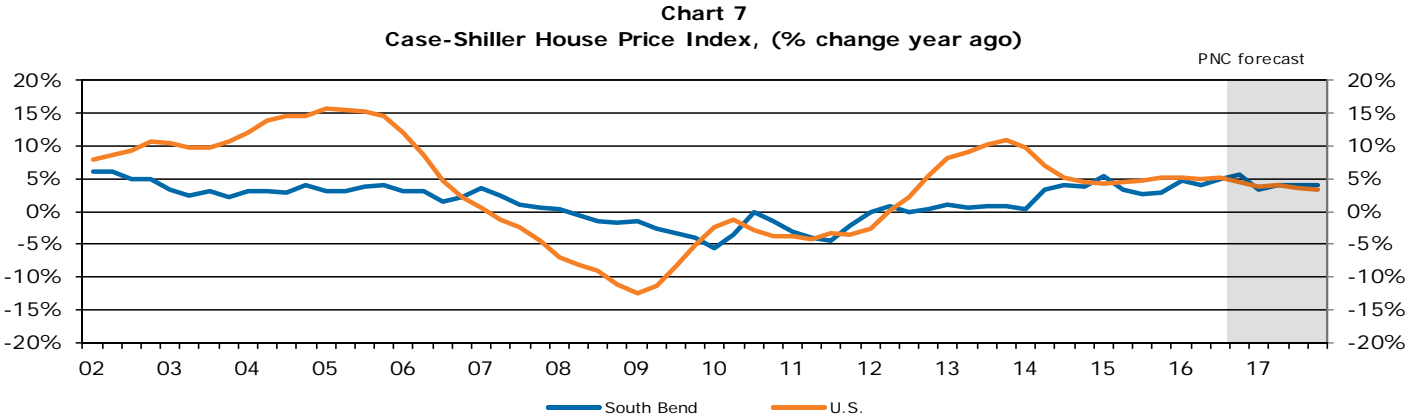


Chart source: National Association of Realtors; Fiserv, Inc.; The PNC Financial Services Group

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