PHILADELPHIA MARKET OUTLOOK

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JOB SITUATION

Job growth in the Philadelphia market area has been lagging behind that in the rest of the U.S. for almost three years. Service industries are adding jobs, but at a below-average rate, with weak growth in cyclical industries such as financial activities and business/ professional services (Chart 1). Job growth in consumer industries is also lagging. One positive is consistent job gains in the region's key education and healthcare industry. Employment in goodsproducing industries has been flat since 2010, with small job gains in construction offsetting losses in manufacturing. Local government budgets remain under pressure with ongoing job losses, unlike in the rest of the country. With below-average job growth the unemployment rate has fallen less quickly than the U.S. rate, and is now slightly above the national average. Growth in the labor force halted in 2013 after two years of increases, another indicator of the area's subpar labor market, although employment growth as measured in the household survey is at the U.S. rate.

INCOME

With a well-educated workforce and well-paying industries, median household income in Philadelphia is high for Pennsylvania and the U.S., although it lags behind other major Northeastern metropolitan areas. High business costs relative to Central and Northeast Pennsylvania are a weight on job growth in the area. With low exposure to cyclical drivers and job growth largely in industries that pay below-average wages, income growth in Philadelphia will lag behind the nation, although median household income will remain above the U.S. figure (Chart 2). Disposable incomes took a hit in the first half of 2013 with tax increases. weighing on consumer spending. Disposable income growth is picking up now as the recovery continues and the impact of tax increases fades, but will continue to lag the U.S.

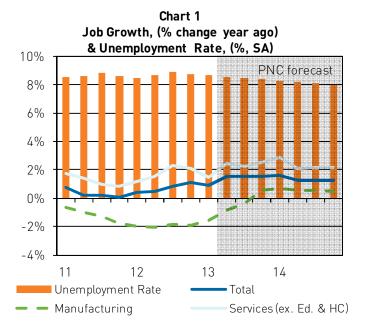


Chart sources: Bureau of Labor Statistics; The PNC Financial Services Group

Chart 2 Income Growth (% change year ago) & Median Household Income (Ths. \$. SA)

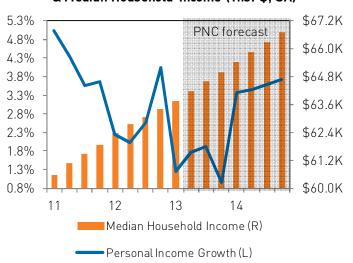


Chart sources: Bureau of Census; Moody's Analytics; The PNC Financial Services Group

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HOUSING

The Philadelphia housing market is recovering modestly. Sales of existing homes bottomed out in mid-2011, and prices have been increasing, albeit very slowly, since mid-2012 (Chart 3). Homebuilding has picked up over the last few years, with gains in both single-family and multifamily starts, leading to job growth in construction. Philadelphia was less exposed to the housing crash compared to other parts of the country, with less overbuilding and a smaller run-up in prices. Affordability is better than in other major East Coast markets, and foreclosures are also less of a problem. Starts, sales and prices will all continue to improve through the second half of 2013 and into 2014, with better access to credit a positive. The improving housing market will contribute to the area's overall recovery, as price gains will support consumer spending as households feel wealthier, and better homebuilding lead to further construction job gains. However, weak income growth and poor demographics will limit the recovery, and over the long run housing activity will be below average. The downtown condo market will lag the overall Philadelphia housing recovery, as it remains oversupplied.

DEMOGRAPHICS

According to the Census Bureau population growth in the Philadelphia area slowed for the third straight year in 2012, to 0.4 percent, well below the U.S. average of 0.7 percent. Because of consistent below-average economic growth, including a long-term decline in manufacturing, Philadelphia's population growth has lagged behind that of the nation's for decades (Chart 6). Over the forecast period population growth will stagnate at about 0.3 percent, remaining well below the U.S. average, due to a low birthrate and weak net migration (Chart 4). Slow population growth will also weigh on the housing market recovery in Philadelphia. One positive is Philadelphia's many colleges and universities, which provide a deep pool of highly-skilled labor, attracting well-paying firms seeking educated workers in industries such as finance and healthcare.

After a milder recession compared to the U.S.,

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

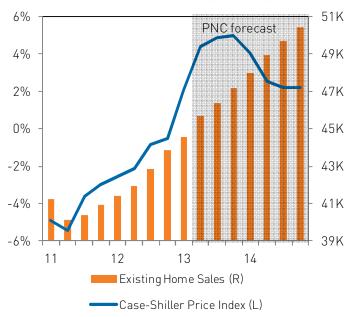


Chart sources: National Association of Realtors; Fiserv, Inc.; The PNC Financial Services Group

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

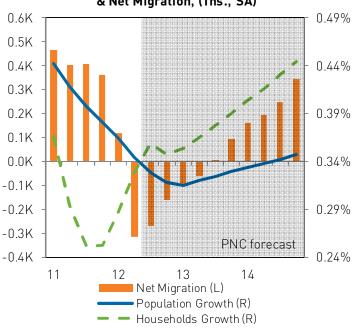


Chart sources: Bureau of Census; Bureau of Economic Analysis
Moody's Analytics; The PNC Financial Services
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OUTLOOK SUMMARY

Philadelphia's recovery will continue to lag the rest of the nation's. The area's concentration in education/health and a less-severe housing boom limited its downturn, but a lack of cyclical industries, particularly in manufacturing and high-tech industries, will constrain the upside. The area's mild housing market downturn and poor demographics also mean less of an upswing in homebuilding and house prices, another constraint on growth over the next few years. Government budget and job cuts at the Federal and local levels will also weigh on the Philadelphia area economy through 2013. As a result, job and income growth will be below the national average in the near term. This will also limit the rebound in industries tied to consumer spending, including retail trade and leisure/hospitality services.

The state is set to award a license for a second casino in Philadelphia in 2014. Building a new casino would support construction employment in the short run, and additional gaming would create permanent jobs in tourism, especially if the casino includes a hotel. One downside risk is that the process of awarding a license could be delayed by legal challenges. Another is potential Federal budget cuts: the area is home to many federal facilities and defense contractors, and further reductions in spending would be a major drag on economic growth in the area.

Over the longer run, the area's important concentrations in education/health services, pharmaceutical manufacturing and finance will provide protection against national recessions, but also limit gains during expansions. Philadelphia has a dearth of employment in well-paying cyclical industries, including high-tech industries, that will support long-run job and income gains. Weak long-run population growth will also deter investment in the area. Economic growth in Philadelphia will be below average over the long term, although incomes will remain above the national average.

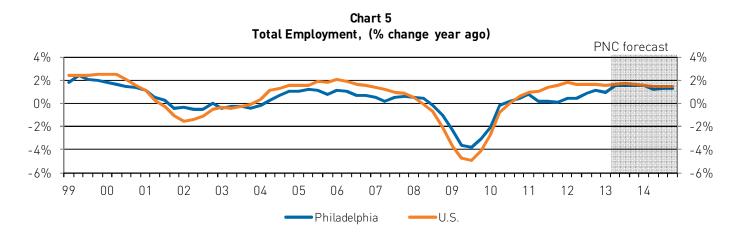
FORECAST TABLE

	U.S.			Philadelphia			
	2012	2013F	2014F	2012	2013F	2014F	
Employment Growth, (% change)	1.7	1.6	1.5	0.7	1.4	1.3	
Unemployment Rate, (%)	8.1	7.5	6.8	8.7	8.5	8.1	
Personal Income Growth, (% change)	3.7	2.7	4.0	2.7	1.5	3.5	
Median Household Income, (Ths. \$)	52.5	53.8	55.1	62.9	64.4	66.1	
House Prices**, (% change)	2.8	9.5	3.6	-1.5	4.1	2.7	
Single-Family Permits* (% change)	23.5	20.4	5.7	18.4	37.4	15.9	
Multifamily Permits* (% change)	38.7	36.8	12.3	31.1	-16.7	-0.7	
*U.S. starts, F = PNC forecast, **Case-Shiller House Price Index							

	U.	S .	Philadelphia		
	2004-2009†	2009-2014†	2004-2009†	2009-2014†	
Employment Growth, (% change)	-0.1	1.1	-0.2	0.7	
Unemployment Rate, (%)	5.8	8.4	5.4	8.5	
Personal Income Growth, (% change)	3.6	3.9	3.7	3.1	
Median Household Income, (Ths. \$)	48.7	52.2	57.9	62.7	
House Prices**, (% change)	-2.9	2.2	2.2	-0.3	
Single-Family Permits* (% change)	-22.7	9.1	-20.2	10.5	
Multifamily Permits* (% change)	-20.2	27.7	-18.3	6.6	

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LONG-RUN EMPLOYMENT TRENDS



LONG-RUN DEMOGRAPHIC TRENDS

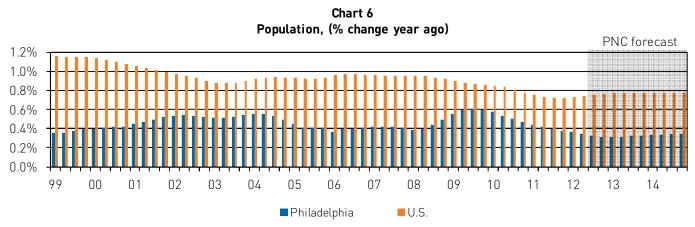


Chart sources: Bureau of Census; Moody's Analytics; The PNC Financial Services Group

LONG-RUN HOUSE-PRICE TRENDS

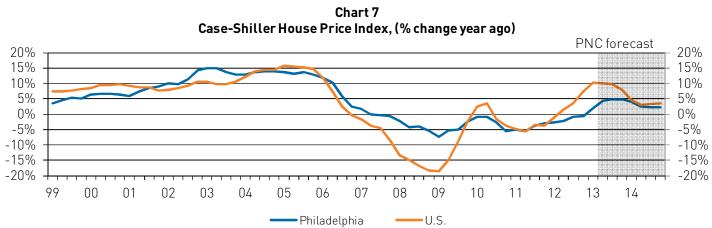


Chart source: National Association of Realtors; Fisery, Inc.; The PNC Financial Services Group

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