



THE PNC ECONOMIC OUTLOOK

Survey of Small & Middle-Market Business Owners

February 2023

PNC SURVEY SHOWS SMALL BUSINESS OWNERS SEE BRIGHT FUTURES FOR THEIR OWN BUSINESS

ANALYSIS BY PNC CHIEF ECONOMIST GUS FAUCHER

Economic growth slowed in 2022 as the Federal Reserve aggressively raised interest rates throughout the year to push back against high inflation, but the U.S. economy remains solid in early 2023. In particular the labor market is historically strong, with continued solid job growth and the lowest unemployment rate in more than 50 years. Consumers continue to increase their spending despite high inflation and rising interest rates, thanks to solid job and wage gains.

But significant challenges remain. Inflation has slowed somewhat in recent months but is still near the

highest it has been in 40 years, making businesses and households anxious. The labor market is extremely tight, making it difficult for firms to find workers and pushing up wages and business costs.

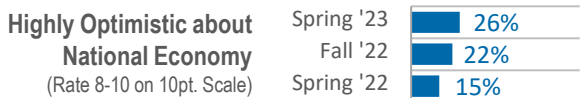
The Federal Reserve has aggressively tightened monetary policy, pushing up interest rates to cool off economic growth and slow inflation. Higher interest rates are weighing on the economy, in particular the housing market, with falling home sales and housing starts and declining home values. With inflation still elevated the Fed will continue to raise interest rates over the next few months, leading to a

further slowing in growth this year.

The central bank has a very difficult task: it is trying to raise interest rates enough to bring down inflation, but not by so much that the economy tips into recession. PNC's baseline forecast is that with inflation stubbornly elevated the Fed will overshoot and high interest rates will cause a U.S. recession in the second half of 2023. But the recession should be mild and short thanks to the tight labor market, solid consumer balance sheets, and a well-balanced housing market. And there is still a 40% chance that the U.S. economy can avoid a near-term recession.

SURVEY-HIGH SIX IN 10 HIGHLY OPTIMISTIC ABOUT OWN BUSINESS IN NEAR TERM

Based on the results of PNC's latest semi-annual survey of small and mid-sized businesses, which concluded February 6, resilient business owners appear to be defying predictions of an economic downturn later this year. In fact, business owner optimism about the outlook for their own businesses in the next six months has reached a 20-year survey high.

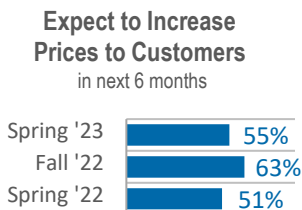


Six in 10 business leaders feel highly optimistic about the prospects for their own company in the next six months despite remaining cautious about the national and their local economies. The gap between optimism for their company versus the broader U.S. economy is now at a survey high of 34 percentage points, nearly double the historic survey average (18 percentage points), indicating a growing divide between the prospects for their own business and expectations for the broader economy.

The survey, now in its 21st year, also revealed that leaders are expecting a better business environment with nearly two-thirds (63%) expressing belief that business conditions in the U.S. will improve in the next six months.

A majority (58%) expect to see sales increases in the next six months. Amid these positive expectations, nearly three-quarters (73%) of business leaders are very confident about the future success of their business.

PRICING PRESSURES EASE



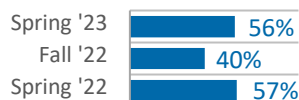
Business owners also expect an easing of pricing pressures. More than half (55%) of businesses expect to increase prices in the next six months, down from the survey high of 63% last fall, and similar to levels from a year ago (51%). Fewer businesses than in the last three waves of the semi-annual survey plan to increase their own prices to customers by 5% or more in the next six months. In addition, fewer than half (47%) anticipate supplier prices to increase in the next six months, down from over half (53%) last fall, to a level similar to a year ago (46%).



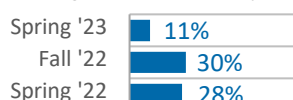
Fewer businesses (21%) expect consumer price increases of 5% or higher in the U.S. economy, overall, compared to last fall (36%), but the portion is similar to a year ago (25%).

SUPPLY CHAIN CONCERNS DECLINE

Expect Better Supply Chain Timeliness vs. 6 months ago, among those w/ supply chain



Expect Inventory Shortage in next 6 months, among those with inventory

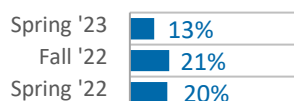


More businesses expect supply chain timeliness to improve compared to six months ago, and fewer are experiencing inventory shortages. A majority of those with a supply chain (56%) expect the timeliness to improve in the next six months, up from four in 10 last fall and similar to a year ago (57%). Only one in 10 (11%) of those who carry inventory are coming up short, down from 30% last fall and 28% a year ago.

While supply chain disruptions remain the top worry for two in 10 (18%) owners, this area of concern no longer stands out significantly from others, and in fact, matches the proportion primarily concerned about the cost of materials (18%).

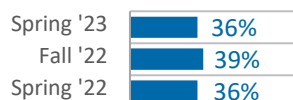
HIRING BARRIERS

Expect to Increase Full-Time Employees in next 6 months



The portion of business owners expecting to increase their number of full-time employees declined from six months ago, while the difficulty in hiring remains constant. Specifically, a little more than one in 10 (13%) business owners expect to increase their number of full-time employees over the next six months, down from two in 10 (21%) last fall and a year ago (20%). A similar portion (15%) expect to increase the number of part-time employees over the same timeframe, unchanged from last fall and up from 8% a year ago.

Harder to Hire Qualified Employees vs. 6 months to a year ago, among those hiring



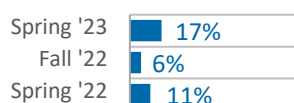
Among businesses actively hiring employees, more than one-third (36%) say it's become harder to hire qualified candidates over the past six months, similar to last fall (39%) and last spring (36%).

Among business leaders experiencing difficulty in hiring qualified candidates:

- **47%** say they have a lack of applicants
- **22%** say candidates lack job-related skills or experience
- **19%** say compensation requirements are higher than the business can afford to pay

QUEST FOR CREDIT

Expect to Seek Loan or Line of Credit in next 6 months

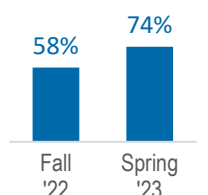


Nearly two in 10 (17%) business owners expect to request a loan or line of credit in the next six months, up from last fall (6%) and a year ago (11%). Among the eight in 10 unlikely to request a loan or line of credit:

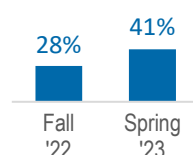
- **77%** say they have no need for funds
- **25%** are hesitant to take on debt
- **16%** feel the cost of credit is too high
- **8%** have a concern about the loan process or the ability of the business to qualify

PREPARING FOR CASH FLOW ISSUES

Maintain Emergency Cash Reserve Fund



Higher Reserve than Typical for Business among those with a reserve



Three-quarters (74%) of businesses are currently maintaining an emergency cash reserve fund, up sharply from 58% last fall. Among businesses with an emergency reserve, half consider the amount to be about average (50%), similar to last fall (54%), while four in 10 say their current reserves are higher than what is typical for the business (41%), an increase since last fall (28%). Construction businesses are among those most likely to report higher reserves than normal (56%), particularly compared to 35% of service and 38% of retail/wholesale industry businesses.