Summary of Economic Activity

Business activity in the Third District declined slightly after edging up in the prior period. Employment continued to grow somewhat, although firms were more reluctant to hire amid economic uncertainty. Nonauto retailers reported little or no change in consumer spending on balance but noted that low-income consumers are trading down as they continue to be burdened by high prices; auto sales increased slightly. Nonmanufacturing activity decreased slightly after edging up last period. Manufacturing activity increased modestly on average after falling slightly in December. Wages and prices continued to rise modestly, albeit at slightly lower rates. Firms noted that changes in fiscal and trade policies pose upside risks to general inflation. Firms expect modest economic growth over the next six months but expressed more uncertainty. Nonmanufacturers were less optimistic than manufacturers.

Labor Markets

Employment continued to grow slightly based on our January and February surveys. Nonmanufacturing firms reported slight increases in full-time employment on average, with a modest increase for part-time employment. The employment index for manufacturing firms also moved higher over the two-month period. The average workweek index rose for manufacturing firms but fell slightly and turned negative for nonmanufacturers. Notably, more than half of our respondents have reported no changes in employment since December.

Overall, our staffing contacts reported strong demand and supply of labor, and less trouble retaining workers. However, two contacts noted that their clients are more reluctant to hire citing economic uncertainty. Other contacts reported increased use of artificial intelligence (AI) to replace workers. For example, banking and hotel industry contacts noted AI replaced fraud monitoring staff and food and beverage workers.

Wage inflation eased further on balance, but firms continued to report modest increases. Across industries, contacts reported less upward wage pressures, with wage increases in the range of 1 to 3 percent.

On a quarterly basis, firms' expectations of the one-year-ahead change in compensation costs per worker fell to a trimmed mean of 3.3 percent in the first quarter of 2025, down from 3.5 percent in the fourth quarter (and down from 3.9 percent one year ago).

Prices

On balance, firms' prices again rose modestly during the period. Many contacts stressed that the budgets of lower-income consumers continue to be burdened. One contact reported that low-income households have begun to stockpile shelf-stable items and switch from purchasing beef and pork to chicken. Nonprofit organizations that support low-income and immigrant populations feared that federal funding changes will impact existing programs.

Firms reported that increases in prices received for their own goods and services over the past year fell slightly in the first quarter of 2025 compared with the fourth quarter of 2024. The trimmed mean for reported price changes at all firms, as indicated by responses to our quarterly survey, fell to 1.4 percent from 1.7 percent. Price increases fell to 0.8 percent among nonmanufacturers and to 2.1 percent for manufacturers.

Looking ahead one year, the increases that firms anticipated in the prices for their own goods ticked down after increasing in the fourth quarter of 2024. The trimmed mean for all firms fell to 2.6 percent in the first quarter of 2025, from 2.8 percent in the previous quarter. The expected rate of growth fell to 2.2 percent for nonmanufacturers and 3.1 percent for manufacturers. However, our contacts noted that changes in fiscal and trade policies may push prices higher.

Manufacturing

Overall, after decreasing slightly in December, manufacturing activity recorded a strong increase in

January, before falling to a modest increase in February. The indexes for new orders and shipments followed a similar trend to overall activity.

Manufacturers' expectations for growth over the next six months increased on average for future activity. However, the indexes for future general activity, new orders, shipments, employment, and capital expenditures all rose in January, then fell sharply in February. Each index remained positive near its nonrecession average.

Trade and Services

On balance, firms across a broad spectrum of nonmanufacturing industries reported a slight decrease in activity. The index for general activity weakened in January and turned negative in February. Meanwhile, the index for new orders turned slightly positive, while the sales/revenues index suggested a slight decline.

Retailers (nonauto) reported little to no change in sales during January, following a slight increase in the fourth quarter of 2024. Visits to stores remain down. Our contacts are not sure if this is attributable to weather—more snow days—or to rising financial constraints. One contact noted that customers are buying cheaper items and are using rewards more often.

Auto dealers reported a slight increase in motor vehicle sales after a modest increase in December. However, one contact reported a slowdown in leasing contracts that they expect to persist. One contact informed that the prices of cars with internal combustion engines continue to hold, while electric vehicle (EV) prices are falling as dealers offer incentives to meet their EV sales mandate.

Tourism activity increased moderately after recording flat to slight growth last period. One contact noted that the championship run and subsequent parade for the Philadelphia Eagles led to a significant boost in hotel demand and occupancy. Another contact noted that business travel continued to recover and is expected to strengthen further.

The share of nonmanufacturers expecting growth over the next six months fell further, with the index falling below its nonrecession average but remaining positive.

Real Estate and Construction

Brokers reported a slight decline in activity in the housing market due to fewer active buyers and sellers during January. One contact reported that pending transactions and new listings were both down 30 percent in January year over year.

Homebuilders also noted a slight decline. While one contact reported strong sales with delivery dates scheduled throughout 2025, most contacts noted that sales and inquiries are down slightly compared with one month and one year ago. One contact suggested that affordability issues were more common owing to high interest rates and high home prices; the contact further noted that incentives were not spurring demand as expected. Another contact has lowered prices on existing units and designed units with smaller square footage.

In nonresidential markets, leasing activity and transaction volumes remain suppressed in the retail, commercial, and industrial segments. The demand for office space remains weak. One contact reported that vacancies in the industrial real estate sector persist, but there has been more interest in that sector than there was one year ago. That said, industrial rents are holding, and there are no landlord concessions. One contact in the architect and engineering sector indicated that business is good, with a steady stream of projects planned for 2025.

Commercial real estate contacts continued to report a slight decrease in construction activity this period. One contact representing general contractors noted that 2024 was the third consecutive year of reduced hours worked. Federal spending cuts could also limit projects in the short to medium term.

Credit Conditions

The volume of bank lending (excluding credit cards) fell slightly during the current period (not seasonally adjusted)—much weaker than the slight growth and modest growth observed during the comparable periods in 2024 and 2023, respectively.

District banks reported a significant decline in commercial and industrial loans and modest drops in mortgages, auto loans, and other consumer loans. Home equity lines grew modestly, and commercial real estate lending edged up. Credit card volumes fell significantly as consumers paid down balances that had surged during the holiday season.

Banking contacts continued to report good asset quality despite a small uptick in delinquency rates among residential customers and in bankruptcies. Our contacts also noted that fewer credit opportunities are being extended as banks tighten lending criteria and customers request less credit simultaneously. Two contacts noted that rollover risks exist in commercial real estate as maturities become due in the short term. ■

For more information about District economic conditions, visit **www.philadelphiafed.org/regional-economy.**