



COMPANY UPDATE/ ESTIMATES CHANGE/ TARGET PRICE CHANGE/ RATING CHANGE

Key Metrics

PNC - NYSE (as of 04/13/17)	\$115.80
Price Target	\$123.00
52-Week Range	\$77.40-\$131.83
Shares Outstanding (mm)	485.0
Market Cap. (\$mm)	\$56,163
3-Mo. Average Daily Volume (000)	2,566.3
Institutional Ownership	84.6%
Tangible Equity / Tangible Assets	9.5%
ROE	8.6%
Tangible Book Value Per Share	\$66.84
Price/Tangible Book Value	173.2%
Dividend Yield	1.9%
Price/LTM Earnings	15.3x

Operating EPS CY 12/31

	2016A	Prior 2017E	Curr. 2017E	Prior 2018E	Curr. 2018E
1Q	\$1.68	\$1.80	\$1.94A	\$2.13	\$2.19
2Q	\$1.82	\$2.04	\$2.02	\$2.41	\$2.45
3Q	\$1.84	\$2.06	\$2.03	\$2.47	\$2.48
4Q	\$1.99	\$2.17	\$2.12	\$2.57	\$2.57
Year	\$7.33	\$8.07	\$8.11	\$9.58	\$9.69
P/E	15.8x		14.3x		11.9x

Common Dividends

	2016A	Curr. 2017E	Prior % chg.	Curr. 2018E
1Q	\$0.51	\$0.55A	7.8	\$0.60
2Q	\$0.51	\$0.55	7.8	\$0.60
3Q	\$0.55	\$0.60	9.1	\$0.65
4Q	\$0.55	\$0.60	9.1	\$0.65
Year	\$2.12	\$2.30	8.5	\$2.50

Company Description – PNC Financial is a commercial banking organization headquartered in Pittsburgh, Pennsylvania and one of the largest financial services firms in the country. The company's products and services include retail banking, corporate and institutional banking, asset management and residential mortgage banking. PNC's primary markets are located in the Mid-Atlantic, Midwest and Southeast regions of the U.S., although many of its products and services are provided nationally. The company also provides certain financial services internationally.

Banks

Analyst: Andrew W. Stapp
502-588-4190 / astapp@hilliard.com
Institutional Sales Desk: George Moorin
502-588-9141 / gmoorin@hilliard.com
J.J.B. Hilliard, W.L. Lyons, LLC
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The PNC Financial Services Group, Inc.

PNC -- NYSE -- Neutral -- 1

NIM Surprise to the Upside Helps Drive Beat; Upgrading to Neutral

- **Earnings Results:** Excluding non-core items that enhanced GAAP EPS by \$0.02, operating EPS were \$1.94, which beat our estimate of \$1.80 and the Street consensus of \$1.83. Drivers of the beat relative to our estimate were favorable variances regarding net interest income, the effective tax rate and the loan loss provision.
- **Positive Highlights:** Net interest income rose 1.4% linked-quarter (LQ) to \$2.16 billion on eight bps of net interest margin (NIM) expansion to 2.77% and a 0.3% lift in average earning assets. We had projected a net interest income of \$2.11 billion and a margin of 2.73%.

Operating noninterest expense rose 0.6% sequentially to \$2.40 billion and was essentially in line with our estimate of \$2.39 billion.

End-of-period loans increased 0.9% LQ, while average loans rose 0.7%.

The provision for loan losses rose \$21 million LQ to \$88 million, while Nonperforming Assets/Asset fell five bps to 0.60% and the net charge-off ratio rose three bps to 0.23%. We had modeled a provision of \$100 million and net charge-offs of 25 bps.

- **Negative Highlights:** Operating noninterest income fell 3.8% to \$1.68 billion versus our estimate of \$1.66 billion primarily on a 20.4% dip in mortgage banking.
- **Estimates:** We are increasing our 2017 and 2018 operating EPS estimates to \$8.11 and \$9.69 from \$8.07 and \$9.58, respectively. Given the increased uncertainties regarding regulatory and tax reform, we are reducing our price target by \$4.00 to \$123.00. With the recent decline in PNC's share price, we are raising our rating to Neutral from Underperform.

Note Important Disclosures on pages 5 and 6
Note Analyst Certification on page 5

OTHER KEY TAKEAWAYS & VALUATION

- The sequential NIM expansion was largely spurred by increased yields on both loans and securities stemming from higher interest rates. Approximately 22% of investment securities are floating rate. Lower premium amortization on mortgage-backed securities resulting from reduced prepayment activity also contributed to the margin expansion.
- Funding costs were contained. Management noted that retail deposit costs have remained relatively stable despite the recent Fed rate hikes. Commercial deposit costs were kept in check by modest yields on government money market funds, which are the primary alternative to bank deposits for commercial customers.
- Loan growth was primarily driven by gains in commercial & industrial loans, which is counter to industry trends. The company noted that the growth was attributable to market share gains in its newer markets.
- Asset quality remained strong with delinquencies showing improvements in all past due categories.
- Management noted that it is comfortable with its retail exposure despite the pressure this sector is facing. Exposure to retail areas vulnerable to internet competition is approximately \$7.8 billion or 3.7% of loans. The largest component is commercial real estate, which totals \$4.7 billion and is collateralized by over 400 projects that are geographically diversified, the vast majority of which are stabilized.
- The remainder of these retail credits include construction loans, loans to REITs and direct loans to retailers. Of the \$1 billion of loans to retailers, approximately \$0.3 billion is noninvestment grade or asset-based.
- The company also indicated that it is comfortable with its auto book, noting that it targets prime and super-prime customers. PNC does not have exposure to subprime customers or auto leases.
- The company returned 92% of 1Q17 earnings to shareholders through \$612 million in share repurchases and \$272 million in common stock dividends.
- The effective tax rate was 23.0% versus our estimate of 25.0%.
- PNC offered the following guidance for 2Q17 and full year 2017 in its call:
 - Modest sequential loan growth in 2Q17 and mid-single digit growth for the year
 - Revenue growth in the upper mid-single digit range in 2017
 - Net interest income and fee income should register low- and mid-single digit increases, respectively, in 2Q17 on a LQ basis
 - Low-single digit increases in noninterest expense in 2Q17 and 2017
 - Low-single digit noninterest expense growth in 2017
 - A Q2 loan loss provision of \$75 million to \$125 million, although it could be at the upper end of this range due to the establishment of reserves for a portfolio of loans and leases purchased in April
 - An effective tax rate of approximately 25% for 2017 absent potential tax reform.
- Our price target is derived through our discounted dividend model and the application of the stock's historical forward multiple of approximately 12.3X to our 2Q18-1Q19 EPS estimates.
- Major model assumptions include two Fed rate hikes this year and one next year, continued flattening of the yield curve and a 28% corporate tax rate in 2018.

SUITABILITY

Our suitability rating on PNC is 1 on our scale of 1 to 4 (1 = most conservative, 4 = most aggressive). Factors contributing to our suitability rating include the company's market capitalization, liquidity and trading volume, diversity of revenues and the geographic diversification of its footprint.

RISK FACTORS

- **Economy** – If the economy softens, loan demand could wane and credit quality could deteriorate.
- **Geography** – The company's operations are primarily clustered in three regions. Accordingly, its earnings are vulnerable to any regional shock and/or slowdown.
- **Competition** – The industry is highly competitive and is impacted by non-bank financial services firms.
- **Sector Rotation** – The share price of the company's common stock may be vulnerable to any sector rotation that might occur.
- **Regulatory Environment** – Banks operate in a highly regulated environment. Consequently, the company is vulnerable to regulatory uncertainties that could negatively impact shareholders. Moreover, the company is one of the largest commercial banking organizations in the nation and, accordingly, is subject to greater regulatory scrutiny compared to smaller financial institutions.
- **Other** – Please see the company's financial statements for a further discussion of risks and considerations.

	THE PNC FINANCIAL SERVICES GROUP, INC.										PNC: NEUTRAL					
	1Q16 A	2Q16 A	3Q16 A	4Q16 A	1Q17 A	2Q17 E	3Q17 E	4Q17 E	FY 2015 A	FY 2016 A	FY 2017 E	FY 2018 E	FY 2016 A	FY 2017 E	FY 2018 E	
\$Millions, Except for Per Share Data																
Balance Sheet Data:																
Assets	360,985	361,335	369,348	366,380	370,944	373,912	377,768	382,442	358,493	366,380	382,442	402,916	2.2%	4.4%	5.4%	
Loans Held for Investment	207,485	209,100	210,446	210,833	212,826	214,954	217,641	220,906	206,696	210,833	220,906	232,732	2.0%	4.8%	5.4%	
Average Earning Assets	310,750	312,436	162,675	320,145	321,093	324,012	326,980	330,691	311,966	320,145	325,694	309,017	2.6%	1.7%	-5.1%	
Deposits	250,359	249,778	259,895	257,164	260,710	262,796	265,506	268,791	249,002	257,164	268,791	282,346	3.3%	4.5%	5.0%	
Equity	41,677	42,103	42,251	41,797	41,774	41,815	41,962	42,114	41,258	41,797	42,114	42,789	1.3%	0.8%	1.6%	
Statement of Operations:																
FTE Net Interest Income	2,146	2,116	2,144	2,180	2,212	2,272	2,343	2,377	8,594	8,586	9,205	9,849	-0.1%	7.2%	7.0%	
Net Interest Income	2,098	2,068	2,095	2,130	2,160	2,218	2,288	2,321	8,278	8,391	8,988	9,617	1.4%	7.1%	7.0%	
Provision for Loan Losses	152	127	87	67	88	120	136	157	255	433	500	783	69.8%	15.6%	56.4%	
Non-Interest Income:																
Asset Management	341	377	404	399	403	410	417	429	1,567	1,521	1,659	1,767	-2.9%	9.1%	6.5%	
Consumer Services	337	354	348	348	332	368	362	363	1,335	1,388	1,425	1,496	4.0%	2.7%	5.0%	
Corporate Services	325	403	389	387	393	422	407	405	1,491	1,504	1,628	1,709	0.9%	8.2%	5.0%	
Residential Mortgage	100	165	160	142	113	123	119	121	566	567	476	502	0.2%	-16.1%	5.6%	
Deposit Service Charges	158	163	174	172	161	165	174	172	651	667	672	672	2.5%	0.7%	0.0%	
Other	297	260	252	299	324	267	268	270	1,294	1,108	1,129	1,092	-14.4%	1.9%	-3.3%	
Securities Gains	9	4	7	-4	-2	0	0	0	43	16	-2	0	-62.8%	-112.5%	-100.0%	
Total Non-Interest Income	1,567	1,726	1,734	1,744	1,724	1,755	1,748	1,760	6,947	6,771	6,987	7,238	-2.5%	3.2%	3.6%	
Non-Core Adjustment	-9	-4	-7	4	-45	0	0	0	-43	-16	-45	0	-62.8%	181.3%	-100.0%	
Adjusted Non-Interest Income	1,558	1,722	1,727	1,748	1,679	1,755	1,748	1,760	6,904	6,755	6,942	7,238	-2.2%	2.8%	4.3%	
Non-Interest Expense:																
Personnel	1,145	1,226	1,239	1,231	1,249	1,255	1,262	1,272	4,831	4,841	5,038	5,189	0.2%	4.1%	3.0%	
Occupancy	221	215	215	210	222	217	218	219	842	861	876	894	2.3%	1.8%	2.0%	
Equipment	234	240	246	254	251	252	254	256	925	974	1,014	1,045	5.3%	4.1%	3.1%	
Marketing	54	61	72	60	55	63	63	64	249	249	244	250	-0.8%	-1.1%	2.5%	
Other	627	618	622	686	625	635	638	641	2,616	2,553	2,540	2,606	-2.4%	-0.5%	2.6%	
Total Non-Interest Expense	2,281	2,360	2,394	2,441	2,402	2,422	2,436	2,453	9,463	9,476	9,712	9,984	0.1%	2.5%	2.8%	
Non-Core Adjustment	0	0	0	0	0	0	0	0	0	0	0	0	NA	NA	NA	
Adjusted Non-Interest Expense	2,281	2,360	2,394	2,441	2,402	2,422	2,436	2,453	9,463	9,476	9,712	9,984	0.1%	2.5%	2.8%	
Operating Pretax Income	1,223	1,303	1,341	1,370	1,349	1,433	1,464	1,471	5,464	5,237	5,718	6,090	-4.2%	9.2%	6.5%	
Operating Net Income for EPS	853	920	919	985	963	985	979	1,014	3,851	3,678	3,941	4,499	-4.5%	7.2%	14.2%	
Share & Per Share Data:																
Diluted EPS	1.68	1.81	1.84	1.97	1.96	2.02	2.03	2.12	7.39	7.30	8.14	9.69	-1.2%	11.4%	19.1%	
Operating EPS	1.68	1.82	1.84	1.99	1.94	2.02	2.02	2.12	7.37	7.33	8.11	9.69	-0.5%	10.6%	19.4%	
Dividends Per Share	0.51	0.51	0.55	0.55	0.55	0.55	0.60	0.60	2.01	2.12	2.30	2.50	5.5%	8.5%	8.7%	
Tangible Book Value	65.15	66.00	67.30	66.85	66.84	67.78	68.80	69.87	62.72	66.85	69.87	74.91	6.6%	4.5%	7.2%	
Common Shares Outstanding	499,000	493,000	488,000	485,000	485,000	479,250	474,688	469,930	485,000	485,000	469,930	448,740	0.0%	-3.1%	-4.5%	
Average Diluted Shares	507,000	503,000	496,000	494,500	492,000	487,125	481,969	477,309	517,245	500,125	484,601	464,529	-3.3%	-3.1%	-4.1%	
Key Financial Statistics:																
Return on Assets	1.06%	1.10%	1.11%	1.14%	1.17%	1.14%	1.14%	1.14%	1.17%	1.10%	1.15%	1.23%	(7)	5	9	
Return on Equity	8.27%	8.54%	8.75%	9.31%	9.50%	9.45%	9.28%	9.57%	9.49%	8.72%	9.45%	10.59%	(77)	73	115	
Net Interest Margin	2.75%	2.70%	2.68%	2.69%	2.77%	2.81%	2.84%	2.85%	2.73%	2.71%	2.82%	2.89%	(3)	11	7	
Noninterest Income/Operating Revenues	42.61%	45.44%	45.19%	45.07%	43.74%	44.17%	43.30%	43.12%	45.47%	44.58%	43.58%	42.95%	(90)	(100)	(64)	
Efficiency Ratio	61.60%	61.43%	61.09%	62.21%	61.03%	59.48%	58.90%	58.66%	60.80%	61.58%	59.52%	57.85%	79	(206)	(167)	
Tangible Common Ratio	9.17%	9.28%	9.12%	9.08%	8.97%	8.91%	8.86%	8.80%	9.10%	9.08%	8.80%	8.54%	(2)	(28)	(26)	
Reserves/Loans	1.31%	1.28%	1.24%	1.23%	1.20%	1.19%	1.18%	1.17%	1.32%	1.23%	1.17%	1.15%	(9)	(6)	(1)	
NCOs/Average Loans	0.29%	0.26%	1.08%	0.20%	0.22%	0.23%	0.25%	0.25%	0.19%	0.46%	0.24%	0.30%	27	(22)	6	

Source: Company reports and Hilliard Lyons estimates.

Additional information is available upon request.

Analyst Certification

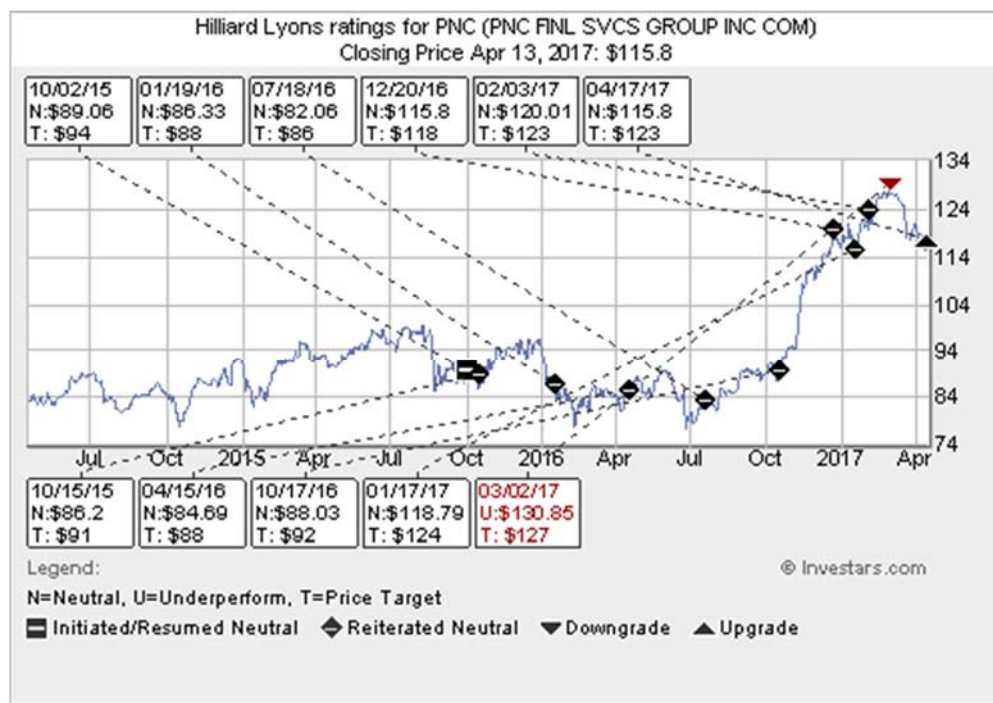
I, Andrew W. Stapp, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject company(ies) and its (their) securities. I also certify that I have not been, am not, and will not be receiving direct or indirect compensation in exchange for expressing the specific recommendation(s) in this report.

Important Disclosures

Hilliard Lyons’ analysts receive bonus compensation based on Hilliard Lyons’ profitability. They do not receive direct payments from investment banking activity.

From 1998 to 2008, Hilliard Lyons was owned by PNC Financial.

PNC Financial is/was a client of Hilliard Lyons within the past 12 months, received non-investment banking securities-related services, and Hilliard Lyons received compensation for those services.



Rating	Hilliard Lyons Recommended Issues		Investment Banking Provided in Past 12 Mo.	
	# of Stocks Covered	% of Stocks Covered	Banking	No Banking
Buy	36	30%	14%	86%
Hold/Neutral	71	58%	6%	94%
Sell	15	12%	7%	93%

As of 5 April 2017

Definitions of Ratings:

Buy - We believe the stock has significant total return potential in the coming 12 months.

Long-term Buy - We believe the stock is an above average holding in its sector, and expect solid returns to be realized over a longer time frame than our Buy rated issues, typically 2-3 years.

Neutral - We believe the stock is holding in its sector, is currently fully valued, and may be used as a source of funds if better opportunities arise.

Underperform - We believe the stock is vulnerable to a price decline in the next 12 months.

Definitions of Suitabilities:

1. A large cap, core holding with a solid history.

2. A historically secure company which could be cyclical, has a shorter history than a "1" or is subject to event driven setbacks.

3. An above average risk/reward ratio could be due to small size, lack of product diversity, sporadic earnings or high leverage.

4. Speculative, due to small size, inconsistent profitability, erratic revenue, volatility, low trading volume or a narrow customer or product base

Other Disclosures

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