Washington Economy Watch

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The Stephen S. Fuller Institute
for Research on the Washington Region's Economic Future
Schar School of Policy and Government
George Mason University

The Washington Economy Watch is a monthly report issued by The Stephen S. Fuller Institute that is intended to inform its readers regarding the current and near-term performance of the Washington region's economy. The Leading and Coincident Indices were first reported in February 1991 and have been calculated each month since that first release and reflect an underlying data base that dates from 1978 covering five complete business cycles in addition to the current cycle that began in mid-2009.

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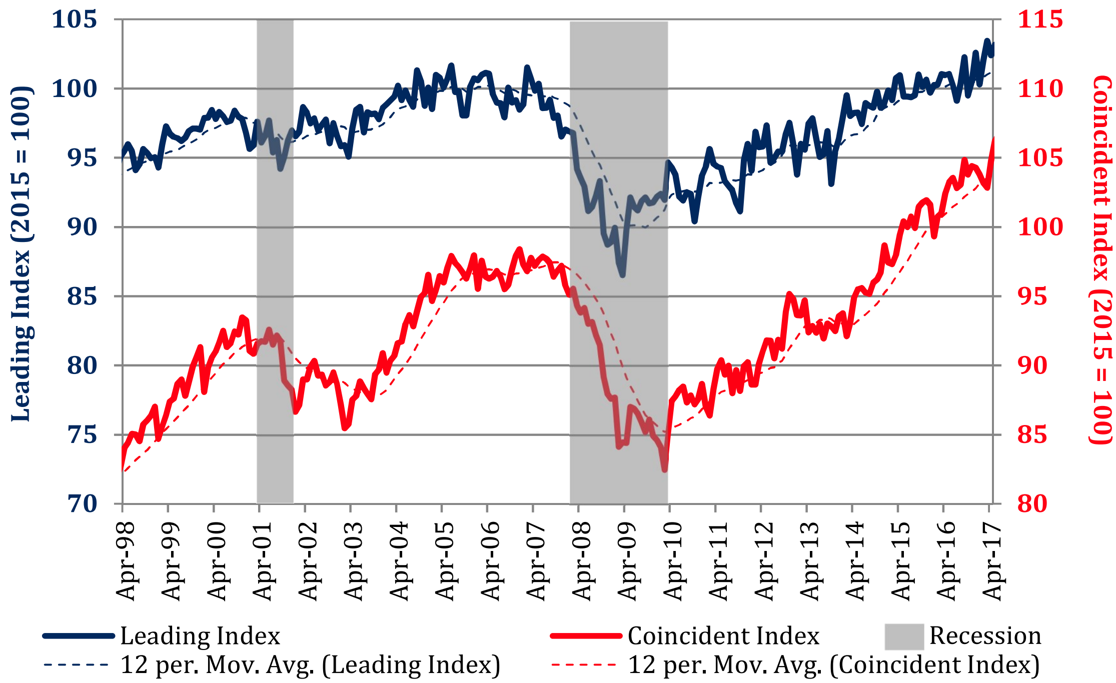
Growth Slows in April but Outlook Remains Good for the Washington Region's Economy

The April 2018 performances of Washington region's Coincident and Leading Indices, while continuing their respective positive trends from 2017, reflected some weaknesses compared to both their performances in March 2018 and in April 2017. The Coincident Index was negative on a month-to-month basis, with two of its four indicators underperforming their respective March values, but on a monthly over-the-year basis it managed to extend its positive trajectory to a 49th month. The Leading Index's April gain was the weakest of the year with only two of its four indicators contributing to its increase. Still, the Leading Index's positive trajectory points to the region's economic growth continuing at least through the third quarter of 2018. Other forecasts for the Washington region's economy are pointing to these gains accelerating over the course of this year and likely continuing in 2019 before moderating for several years beginning in 2020.

Figure 1. Washington Region Economic Indices



Source: The Stephen S. Fuller Institute at the Schar School, GMU

The **Washington Coincident Index**, which represents the current state of the metropolitan area economy, decreased 0.27 percent in April from March. This is the second month this year in which the Coincident Index declined on a month-to-month basis. In April, two of the Index's four components increased on a month-to-month basis. Total wage and salary employment and domestic airport passenger volume increased from their March levels while consumer confidence and nondurable goods sales declined. Consumer confidence has now declined in two consecutive months.

Still, on a monthly over-the-year basis, April's Coincident Index registered an increase of 1.75 percent from April 2017 extending its upward trend to 49 consecutive months, dating from April 2014. April's Index performance was broadly weaker than its performance in March when it had registered a monthly over-the-year gain of 4.0 percent.

In April, three of the Index's components were positive on a monthly over-the-year basis:

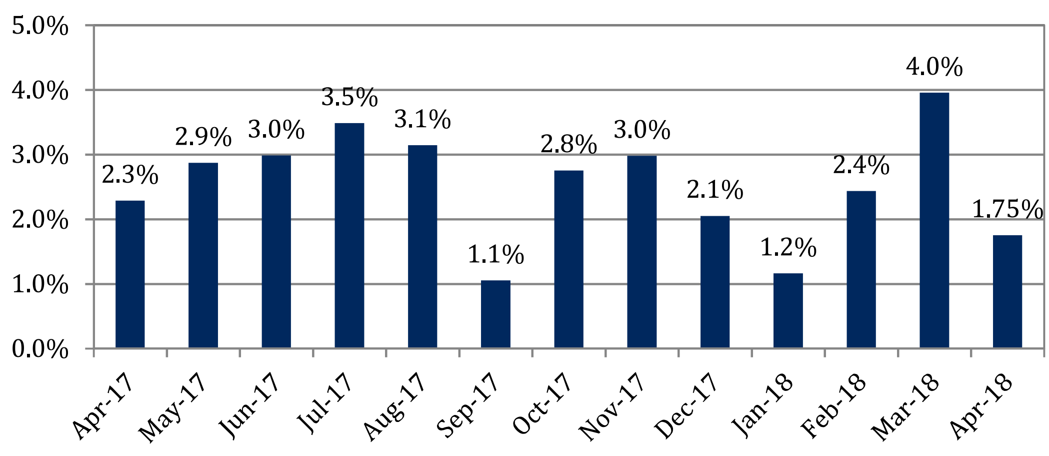
- *Wage and salary employment* in the Washington region increased 1.0% between April 2017 and April 2018;

- *Consumer confidence (in the present)* continued its positive trend, increasing 23.1% from April 2017 continuing its pattern of double-digit increases experienced over eleven of the last twelve months; and,

- *Non-durable goods retail sales* increased 0.8% from April 2017; while,

- *Domestic passenger volume at Reagan National and Dulles Airports*, while up from March, decreased 1.2% when compared to April 2017.

Figure 2. Washington Coincident Index, Monthly Over-the-Year Changes



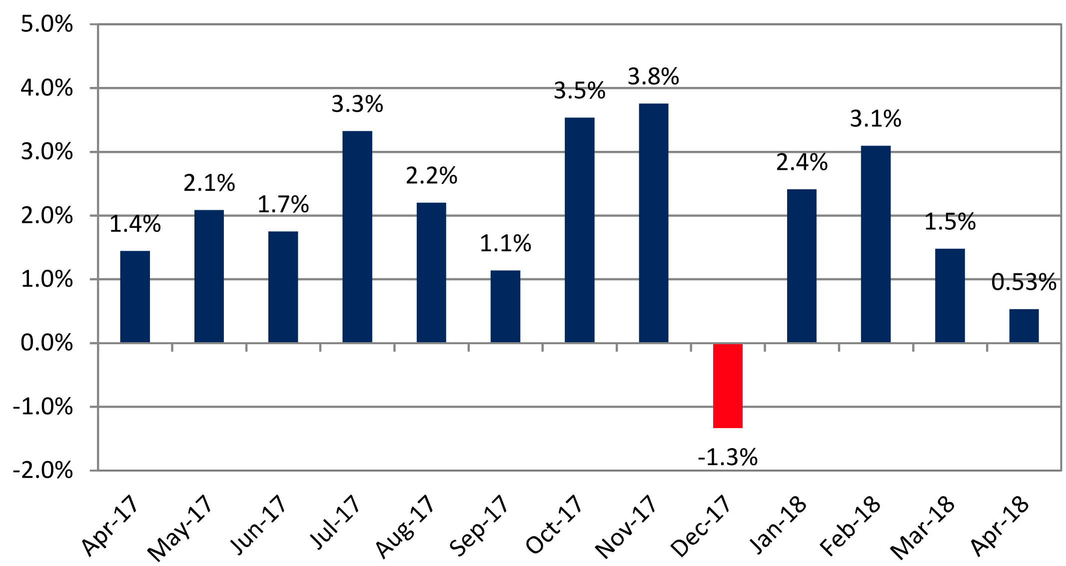
Source: The Stephen S. Fuller Institute at the Schar School, GMU

The **Washington Leading Index**, which is designed to forecast the performance of the metropolitan area economy six to eight months in advance, increased only slightly in April, gaining 0.53 percent from April 2017, and extended its positive trend to a fourth month in 2018 after having declined in December. However, April's gain was the smallest of the year and, with the exception of its December's decline, it was the smallest gain in more than a year. Still, the Leading Index's positive long-term performance points to the region's economic expansion continuing at least through the third quarter of 2018.

In April, two of the Leading Index's four components contributed to its gain from April 2016:

- *Durable goods retail sales* increased 4.5% between April 2017 and April 2018 continuing its positive trend from 2017; and,
- *Initial claims for unemployment insurance* decreased 13.0% (improved) extending its favorable trend to a fourth month; while,
- *Total residential building permits* declined 14.4% in April after increasing in both February and March; and,
- *Consumer expectations (consumer confidence six months hence)* declined 1.2% from its April 2017 level decreasing for only the second time over the previous twelve months.

Figure 3. Washington Leading Index, Monthly Over-the-Year Changes



Source: The Stephen S. Fuller Institute at the Schar School, GMU

Current Performance

The Washington region's economic performance in April continued its long recovery from the negative effects of the Sequester in 2013. The Coincident Index has now increased for 49 consecutive months beginning in April 2014, tracking the region's economic recovery from the Sequester. During this expansion, the region's economy has increased its growth rate from a negative 0.8 percent in 2013 to an estimated 1.9 percent in 2017, substantially closing the growth-rate gap with the U.S. economy and has added 165,800 net new jobs during the last three calendar years.

However, the region's job growth during the first five months of 2018 has fallen well below its levels of the last three years. While the average annual level of net new jobs added during the 2015-2017 period was 55,267 jobs, the pattern over this three-year period showed this trend was moderating each year from its peak in 2015. This slowdown has accelerated in 2018 with the annual rate averaging 39,700 jobs over the year's first five months with this average being well below the beginning-of-the-year forecast (47,400 jobs) for the full year.

The biggest change underlying this slowdown in the Washington region's job growth pattern is the distribution of this job growth across the region's sub-state areas. In the past, Northern Virginia has accounted for approximately 50% of the job growth, with the remaining 50% being shared between DC and Suburban Maryland with Suburban Maryland accounted for 30-35% of the total job gain and the District accounting for 15-20%. To date in 2018, through five months, DC's share is 17%; this is in the normal range. However, Suburban Maryland has only accounted for 5% of the region's job growth. This slow job growth pattern in Suburban Maryland dates back to mid-2017. Northern Virginia continues to generate jobs at roughly the same level (number) as it did in 2017 and 2016, but now this number accounts for 78% of the region's jobs. Accordingly, the slowdown in the Washington region's overall job growth number in 2018 is attributable to slower growth in Suburban Maryland while job growth in the District and Northern Virginia has not deviated significantly from recent patterns. This underperformance in Suburban Maryland seems to be concentrated in Calvert, Charles and Prince George's Counties.

The sectoral mix of the region's job growth (five-month average, annualized) continues to reflect disproportional gains in professional and business services (up by 12,000 jobs), continuing strong gains in education and health services and leisure and hospitality services (a combined increase of 16,200 jobs) and continuing losses of federal government jobs (down 6,300 jobs from the same five-month period in 2017). With the exception of wholesale trade, all of the economy's other sectors experienced job gains at the regional scale but many of these have experienced losses when broken out by sub-state area.

Recent job growth trends reported by BLS on June 15th show the preliminary estimate for April to have been revised downward from 38,700 jobs to 33,800 jobs, a 12.7 percent downward revision. The preliminary estimate for job growth in May, compared to May 2017, was an increase of 41,300 jobs with job gains in Northern Virginia accounting for 76.5 percent of the region's total, Suburban Maryland accounting for 7.5 percent and the District of Columbia accounting for 16.0 percent. On a monthly over-the-year basis, professional and business services jobs increased by 15,800 while educational and health services and leisure and hospitality services combined for a gain of 12,200 jobs. Retail trade registered a strong gain of 5,200 jobs. The federal government continued to lose jobs recording the largest monthly over-the- year decline (7,200 jobs) since September 2014, the last month of the federal fiscal year at the end of the Sequester.

Near-Term Outlook

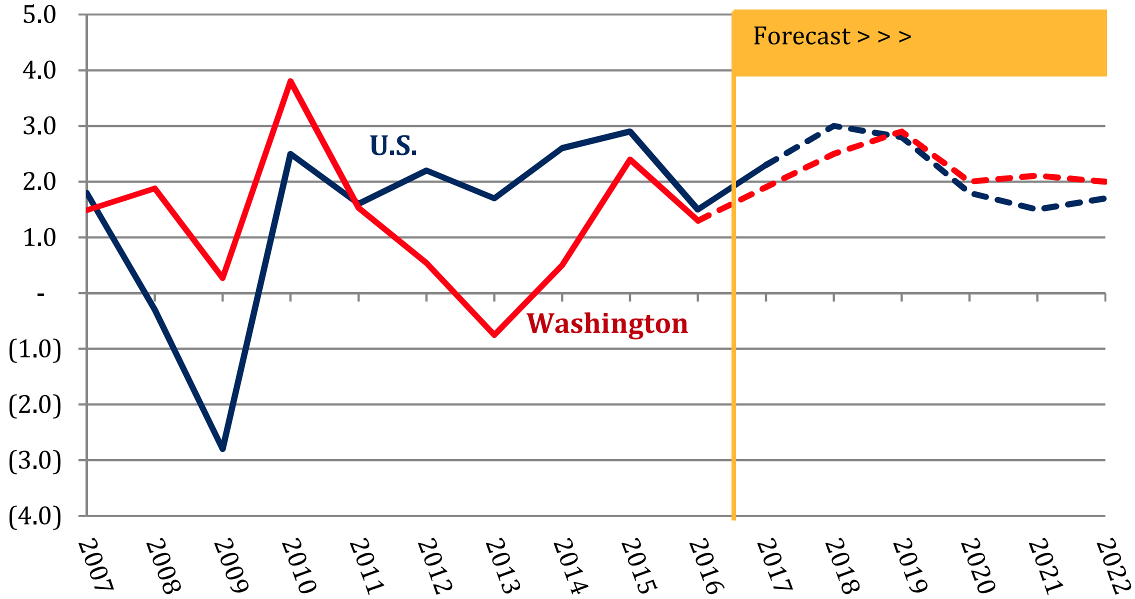
The U.S. economy is expected to accelerate in 2018 and remain strong through 2019. The most recent forecast (IHS Markit, June 2018) for the U.S. economy incorporates a reassessment of the magnitudes and timing of the fiscal impacts of recent federal initiatives: the 2017 Tax Cuts and Jobs Act and the Bipartisan Budget Act of 2018. Also reflected in these updated GDP forecasts are the anticipated higher energy costs in 2018 resulting in part from the suspension of the Iranian nuclear agreement and the effects of higher import tariffs imposed by the Trump Administration and the retaliation of US trading partners. The results are that GDP growth is now projected to reach 3.0% in 2018 and slip to 2.8% in 2019.

While this short-term growth presents a positive picture for the economy, the years following 2019 are now reported as weaker than in previous forecasts with GDP growth in 2020 projected at 1.8% slipping to 1.5% in 2021. These forecasts reflect the impacts of diminished fiscal stimuli that are largely responsible for the accelerated growth rates in 2018 and 2019, increasing energy costs, higher interest rates, and weaker consumer spending.

The aging of the business cycle is not a factor in these forecasts. Still, the potential for the forecast to be weaker than currently projected should be considered in any longer range planning. Rising international trade costs (tariffs) and decreasing business and consumer confidence could drive the economy negative in 2020 or in 2021 when its growth will already be slowing due to the loss of fiscal stimuli.

As shown in Figure 4, the Washington region's economy is projected to continue tracking closely with the growth of GDP this year and outperform it in 2019 and for the next several years being driven by a combination of strong federal spending and the growth of its higher-value added non-federally dependent sectors. These forecasts incorporate the projected impacts of most recent fiscal stimuli that will be generated by the increased spending included in the FY 2018-2019 federal budgets. These economic impacts may track differently than currently projected following the mid-term election cycle that will determine whether there is a change in control of Congress and from changes in future funding levels of domestic programs targeted by the Trump Administration for consolidation or downsizing.

Figure 4. U.S. GDP and Washington MSA GRP 2007 – 2017 – 2022 (Annual % Change)



Source: IHS Markit; The Stephen S. Fuller Institute at the Schar School, GMU

The Washington region's economic recovery from the Great Recession and from the impacts of the Sequester have helped to diversified it away from—reduced its dependence on—federal spending and positioned it to outperform GDP growth once the national economy begins to weaken due to changing federal fiscal policies or experiences a broad-based economic weakening due to changing global economic conditions. Still, the pattern is nominally the same for the region's economy as it is for the U.S. with it peaking in during the 2018-2019 period and slowing into the next decade.

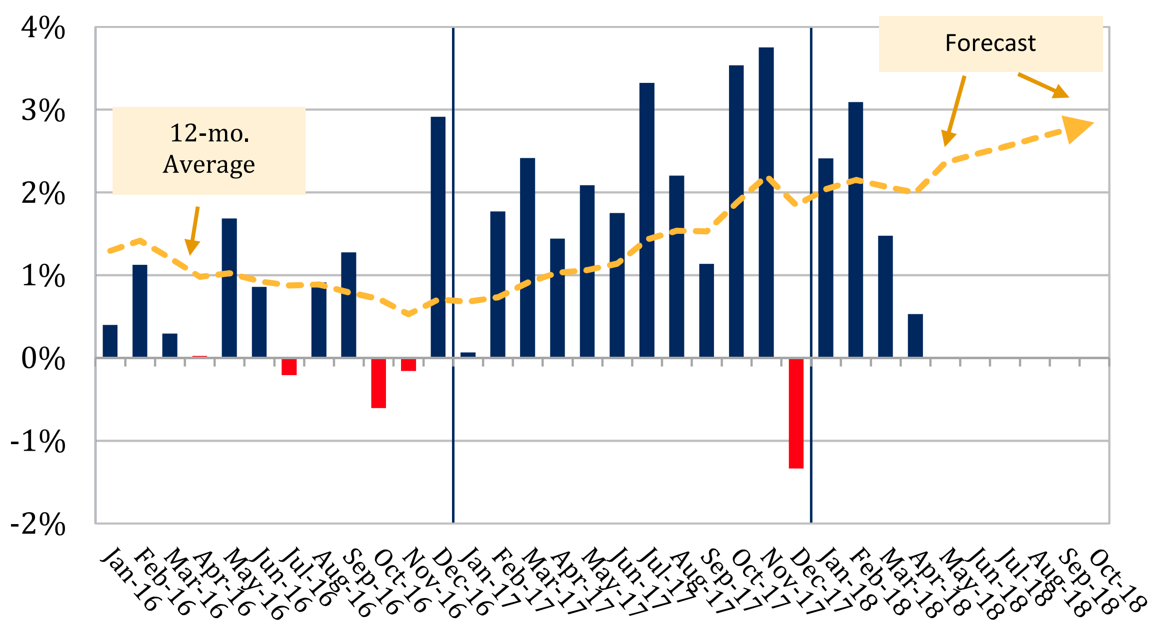
This pattern of near-term performance for the Washington region's economy is confirmed by the trajectory of the Leading Index as shown in Figure 5. The Washington Region Leading Index has presented an upward growth path dating back to mid-2014 with its performance during 2017 through the current month pointing to the expansion continuing at least through the third quarter of 2018.

Underlying the Index's performance are the individual performances of its four components, each indicative of range of performance indicators that may tell a different story. As such, each is important to examine separately. The month-to-month pattern of a single indicator might point to a fundamental change in the composite Index.

Consumer expectations—how consumers think the economy will perform six months enhance—is one of these indicators. When consumers begin to think the economy is better now than it will be in the future, they are less likely to take risk and this may translate into delaying major purchases and reducing personal debt. Consumer expectations have declined for three consecutive months and in four out of the past five months. Not surprising, durable goods sales have declined every other month starting in October 2017 with a very small gain of 0.2 percent in January. Residential building permits have experienced double-digit monthly declines in three of the last five months. All of these month-to-month declines could be explained by the winter weather; December January, March and April were colder than normal.

The fact that consumer confidence in the present—how consumers think the economy is performing today—declined in April, March and December on a month-to-month basis and registered only a small gain (0.6%) in January, suggests that consumers are becoming concerned about their economies. Nondurable goods sales declined on a month-to-month basis in three out of the last five months. These are counter-trends that will be tracked over the coming months as they could combine to slow the Washington region's accelerating economic growth trajectory. At this time, Leading Index remains positive, although it increased only 0.5 percent in April, and it continues to forecast a positive growth path through the third-quarter of 2018.

Figure 5. Washington Region Leading Index
Monthly Over-the-Year Percent Change



Source: The Stephen S. Fuller Institute at the Schar School, GMU

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Washington Area Economic Indicators
Current and Previous Months

Economic Indicator	Estimates			Percent Change	
	Apr-18 Prelim.	Mar-18 Final	Apr-17 Final	Mar-18 to Apr-18	Apr-17 to Apr-18
Washington Area Business Cycle Indicators					
Coincident Index (2015 = 100)	106.5	106.8	104.7	-0.27%	1.75%
Leading Index (2015 = 100)	103.0	105.0	102.4	-1.94%	0.53%
Washington Area Coincident Index Components					
Total Wage & Salary Employment ('000)[a]	3,303.0	3,288.3	3,269.2	0.45%	1.03%
Consumer Confidence (South Atlantic)[a]	164.0	166.0	133.2	-1.20%	23.12%
Domestic Airport Passengers ('000)[b]	2,142.4	2,131.5	2,168.5	0.51%	-1.20%
Nondurable Goods Retail Sales ($000,000)[c]	3,179.5	3,281.4	3,152.9	-3.11%	0.84%
Washington Area Leading Index Components					
Total Residential Building Permits[a]	1,579.0	2,315.0	1,845.0	-31.79%	-14.42%
Consumer Expectations (South Atlantic)[a]	111.1	118.6	112.4	-6.32%	-1.16%
Initial Unemployment Claims[b]	1,362.6	1,311.2	1,565.5	3.93%	-12.96%
Durable Goods Retail Sales ($000,000)[c]	3,640.4	3,819.0	3,484.4	-4.68%	4.48%
Washington Area Labor Force[a]					
Total Labor Force ('000)	3,411.7	3,422.6	3,375.0	-0.32%	1.09%
Employed Labor Force ('000)	3,304.6	3,298.3	3,260.2	0.19%	1.36%
Unemployed Labor Force ('000)	107.1	124.3	114.8	-13.87%	-6.74%
Unemployment Rate	3.1%	3.6%	3.4%	--	--
Washington Area Wage and Salary Employment[a]					
Total ('000)	3,303.0	3,288.3	3,269.2	0.45%	1.03%
Construction ('000)	161.3	160.4	159.2	0.56%	1.32%
Manufacturing ('000)	55.0	54.7	54.7	0.55%	0.55%
Transportation & Public Utilities ('000)	68.6	68.1	65.4	0.73%	4.89%
Wholesale & Retail Trade ('000)	338.4	338.1	337.3	0.09%	0.33%
Services ('000)	1,974.5	1,961.5	1,946.6	0.66%	1.43%
Total Government ('000)	705.2	705.5	706.0	-0.04%	-0.11%
Federal Government ('000)	363.1	361.3	367.6	0.50%	-1.22%

[a]Unadjusted data

[b]Seasonally adjusted data

[c]Seasonally adjusted constant (1996) dollars