Washington Economy Watch

Vol. III, No. 6
June 2019

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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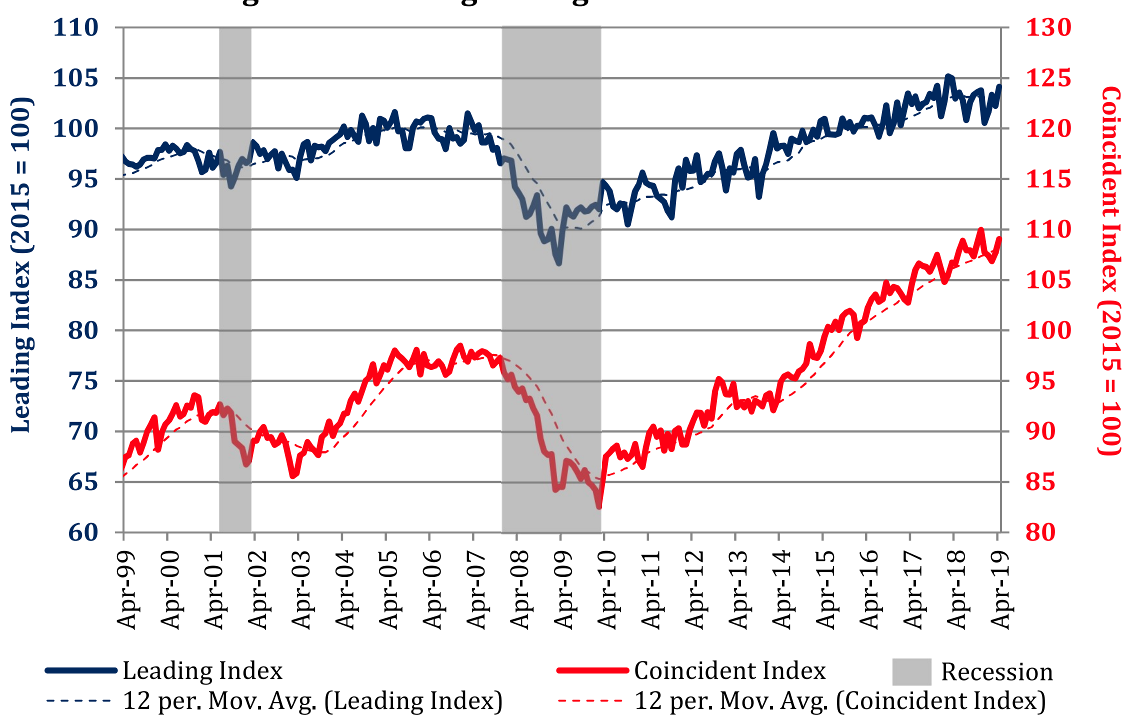
The Washington Region's Economy Gained Traction in April Reversing First Quarter Weaknesses

The Washington region's Coincident and Leading Indices both bounced back in April from their weak first quarter performances: the Coincident Index accelerated in April after registering its slowest growth in five years in March and the Leading Index turned positive in April reversing its downward trend dating back to July 2018. Seven of the two Indices' eight component indicators contributed to this overall positive performance. Still, this reversal represents just one month's performance and follows a slowing trend that may not be finished. Job growth in April remained well below forecast and May jobs numbers, released June 21st, showed this slower growth trend continuing. With the U.S. economy slowing, global trade tensions continuing, oil prices rising, and the FY 2020 federal budget impasse far from resolution, this year's economic performance remains uncertain.

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, increased for a second consecutive month, increasing 1.28 percent in April, on a month-to-month basis, building on its gain of 0.7 percent in March after having declined in the three preceding months. These gains reflect continuing recovery from the impacts of the 35-day partial federal shutdown and the general seasonal strengthening of the region's economy. The most significant performance change was reflected in the month-to-month change in consumer confidence that was down 12.0 percent in March and gained 13.1 percent in April.

On a monthly over-the-year basis, April's Coincident Index registered an increase of 2.32 percent from April 2018, its second strongest monthly over-the-year performance in the last year. This increase extended the Index's upward trend to 61 consecutive months, dating from April 2014. The Coincident Index's acceleration from March's weak 0.9 percent increase can be attributed to sharp increase in consumer confidence accompanied by strong gains in nondurable goods retail sales, both reversing their weak performances in March.

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

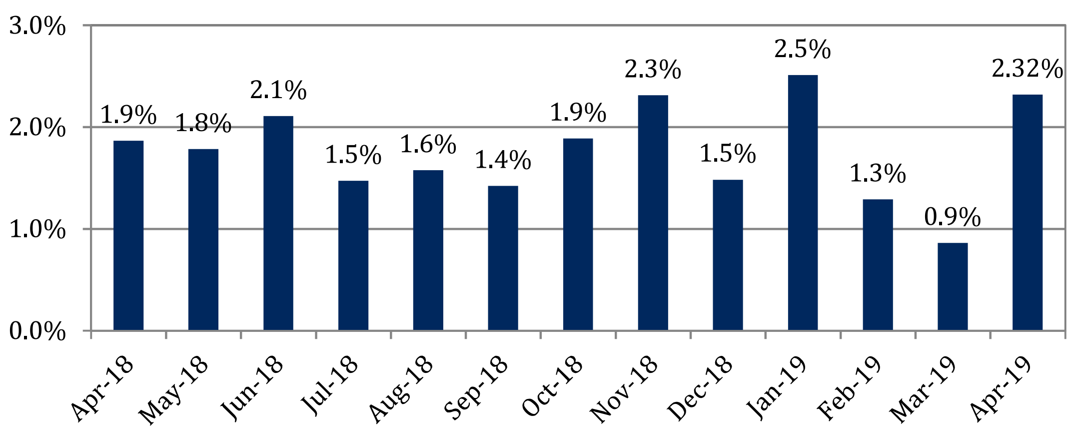
- *Wage and salary employment* in the Washington region increased 0.9% between April 2018 and April 2019;

- *Non-durable goods retail sales* were up 4.8% from April 2018 gaining for a 26th consecutive month on a monthly over-the-year basis;

- *Domestic passenger volume at Reagan National and Dulles Airports* increased 3.1% from April 2018; and,

- *Consumer confidence (in the present)* increased by 10.2% from April 2018.

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 by 1.12 percent in April on a monthly over-the-year basis; this was only its second increase since June 2018. The Leading Index's decline had accelerated over the previous five months raising concerns regarding the region's economic performance going forward into 2020. While April's Index gain tempers this concern, until a positive trend is sustained achieving this year's projected gain remains in doubt.

In April, three of the Leading Index's four components contributed to its increase. This performance contrasts with these components' performances in March and February when all of four components made negative contributions.

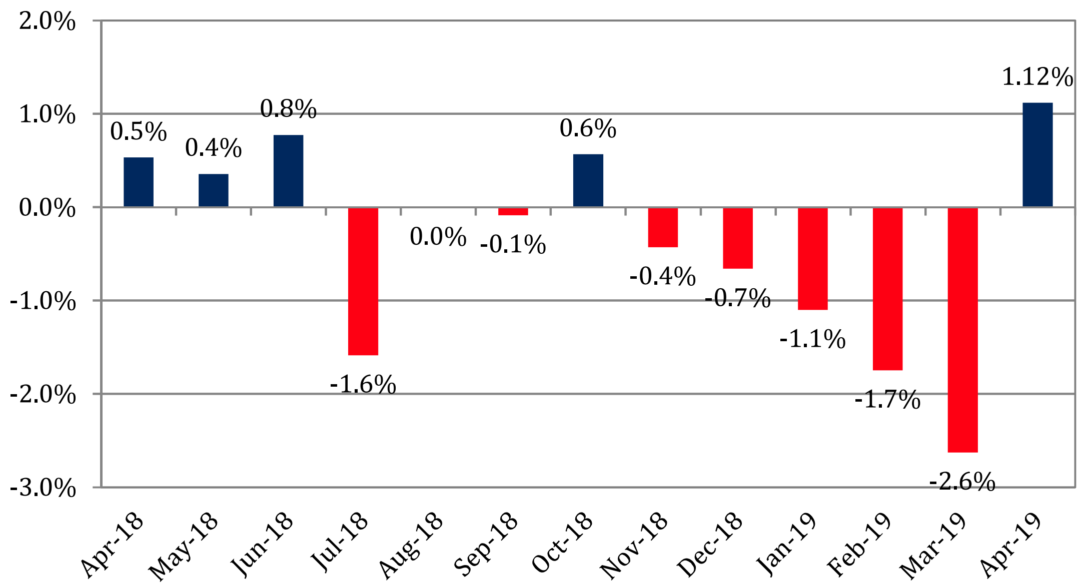
- *Consumer expectations (consumer confidence six months hence)* increased 12.2% from April 2018 after declining for three consecutive months;

- *Total residential building permits* increased 66.1% in April reversing two monthly over-the-year declines; and,

- *Durable goods retail sales* were up 3.6% from their April 2018 level after declining 0.2% in both March and February; while,

- *Initial claims for unemployment insurance* increased 51.2%, worsening for the eleventh consecutive month.

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 economy has sustained its expansion (recovery) from the negative impacts of the 2014 Sequester for 61 consecutive months; that is, the Washington region's Coincident Index, which is designed to measure the region's current economic performance, has increased each month since April 2014 (on a monthly over-the-year basis) through April 2019. The Coincident Index has tracked the Washington region's recovery from the economy's Sequester induced decline, its acceleration through 2018 and its slowdown during this year's 1st quarter.

Several weaknesses have emerged. Primary among them were the slowdown in the region's job growth and weakening of consumer confidence. With April's Coincident Index increasing to 2.3 percent from March's 0.9 percent (the slowest growth rate since March 2014), it would appear that what had been holding the region's economy back has been corrected. Consumers appear more confident, as confidence (in the present) increased 10.2 percent in April after declining 3.7 percent in March. This decline in consumer confidence could be blamed on the 35-day partial-federal shutdown or perhaps growing concerns about border security, a looming trade war with China or other uncertainties that emerged during the first quarter.

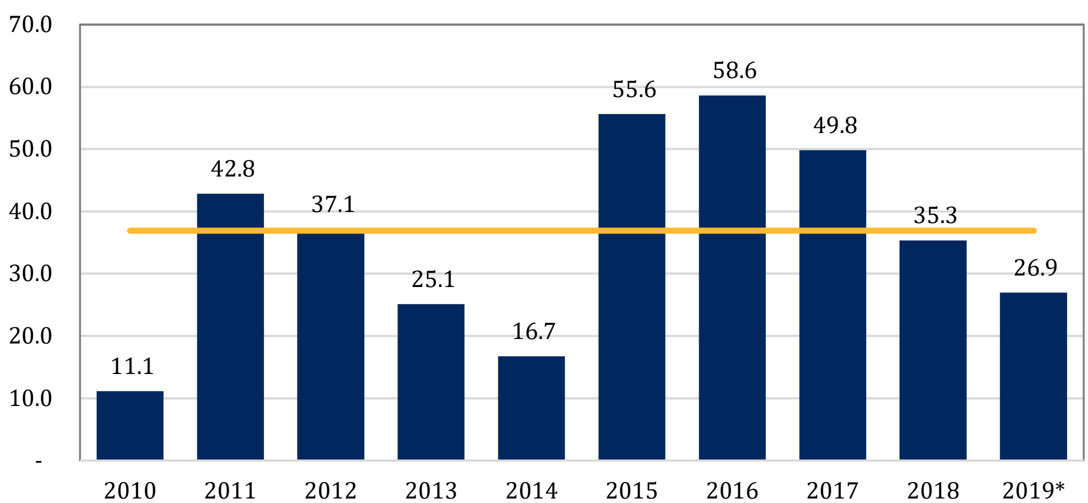
Consumer spending is an important driver of the local and national economies. When consumer confidence dips, so does retail spending as it did in March, nondurable retail sales slowed and durable goods retail sales declined. With consumer confidence increasing in April, both durable and nondurable goods retail sales also registered strong gains. If April's growth in consumer confidence continues, consumer spending is likely to continue to grow providing further stimulus to the economy and helping to extend its expansion.

Job growth with its associated gains in personal earning remains the key to growing consumer spending. The Washington region's job growth performance has slowed considerably since its peak in 2016. Job gains in 2017 remained strong but were down 15.0 percent from their 2016 total and this slowdown in job growth continued in 2018 with job gains were down 29.1 percent from 2017. Job growth in 2019, through five months, show this trend continuing with the annualize gain (based on five-months performance) averaging 26,900 jobs; down 23.7 percent from the number of jobs added in 2018. This annualized job increase through May was pulled down from April's annualized gain of 28,200; in May the region's gain from May 2018 is estimated at 25,000 jobs. These historic job growth trends for the Washington region are presented in Figure 4.

Besides slower job growth since 2016, the distribution of this job growth across the Washington region's sub-state areas has also changed. Job growth has favored Northern Virginia for more than fifty years but these differences have widened in recent years. During the 2015-2017 period, Northern Virginia accounted for 52.2 percent of the region's job gains, the District of Columbia accounted for 23.7 percent and Suburban Maryland's share was 24.1 percent. In 2018, these job growth percentages shifted even more to Northern Virginia's advantage: 71.1%, 20.4% and 8.5%, respectively. This job growth pattern has become even more unbalanced in 2019. Suburban Maryland has lost jobs in four of the year' first five months—job growth has declined and equaled 8.6 percent of the region's net gain through May and job growth in the District has slowed representing 16.2 percent of the region's gain. Job growth in Northern Virginia, through five months, is accounting for 92.4 percent of the region's estimated job gains.

This growing imbalance in the distribution of the region's economic growth, as measured by its generation of new jobs, raises a range of concerns. Important among these is the region's ability to compete economically with other large metropolitan regions when a large portion of it is structurally unable to support economic growth. This unbalanced growth pattern could also reshape commuting patterns and housing markets, and deepen the inequities in the quality of life available across the region.

Figure 4. Job Change in the Washington Region, 2010-2019* (in thousands)



Source: U.S. Bureau of Labor Statistics; The Stephen S. Fuller Institute at the Schar School, GMU *Average through May

The U.S. Economy's Outlook in 2019

The performance of the Washington region's economy is also being affected by the performance of U.S. economy. As the growth of the region's economy has become more strongly tied to the performance of its non-federal dependent businesses and organizations, national and global economic trends and conditions will either support or constrain the region's growth going forward.

The national business cycle turns 10-years old at mid-year and its uneven performance is being closely monitored and widely interpreted. The good news is that the U.S. economy continues to expand. The year started off with a strong 3.1

percent 1st quarter GDP increase. While employment growth has been uneven this year, it remains well above levels consistent with an aging business cycle, and unemployment holding at a 50-year low at 3.6 percent and still could go lower over the summer. Wage growth and job growth have fueled consumer spending without generating inflationary pressures and lower energy costs have been a positive factor in both lowering inflationary pressures and providing consumers with some additional disposable income, while also bolstering consumer confidence. Consumer spending rose in April and May after slowing at the end of 2018.

The interest rate environment remains favorable with 30-year fixed rate mortgages holding below 4 percent, down almost a full point from a year ago. And, the Federal Reserve Board's announcement last March that it was taking a pause in its planned sequence of rate increases, which had at least three more ¼ point increases planned, was received favorably by investors. With the Fed's announcement on June 19th that it was holding rates steady and that it would do whatever was necessary to sustain the business cycle, it has become clear to many Fed watchers that its next move, possibly as early as July, will be to lower the Federal Funds rate by ¼ point.

Some of what is concerning the Fed and other observers includes:

- A projected slowdown in GDP growth in the second quarter to 1.5% from 3.1% in the first quarter;

- IHS Markit's June manufacturing Purchasing Managers' Index slipped to its lowest level since late 2009, to just above the threshold between expansion and contraction;

- Weaker global economic performance, especially for China and the EU;

- Escalating trade conflicts with major trading partners;

- The Morgan Stanley Business Conditions Index fell in June to its lowest level since December 2008; and,

- The possible federal budget and U.S. debt-ceiling impasses leading to a federal shutdown October 1st.

The fact remains that the national economy is slowing and, after growing 2.9 percent in 2018, it is now on track to grow 2.5 percent in 2019 (IHS, June 2019). Other forecasters have the GDP growth rate down to 2.1 to 2.3 percent. This slowdown is projected to continue in 2020 with GDP growing 1.8 percent, falling below trend, and remaining at below-trend rates into the foreseeable future. To sustain GDP growth over several more years, even at these slower rates, will require resolution of a long list of threats that could disrupt the cycle. Already, there is growing acceptance that the record expansion could end in 2020. On June 17th, JP

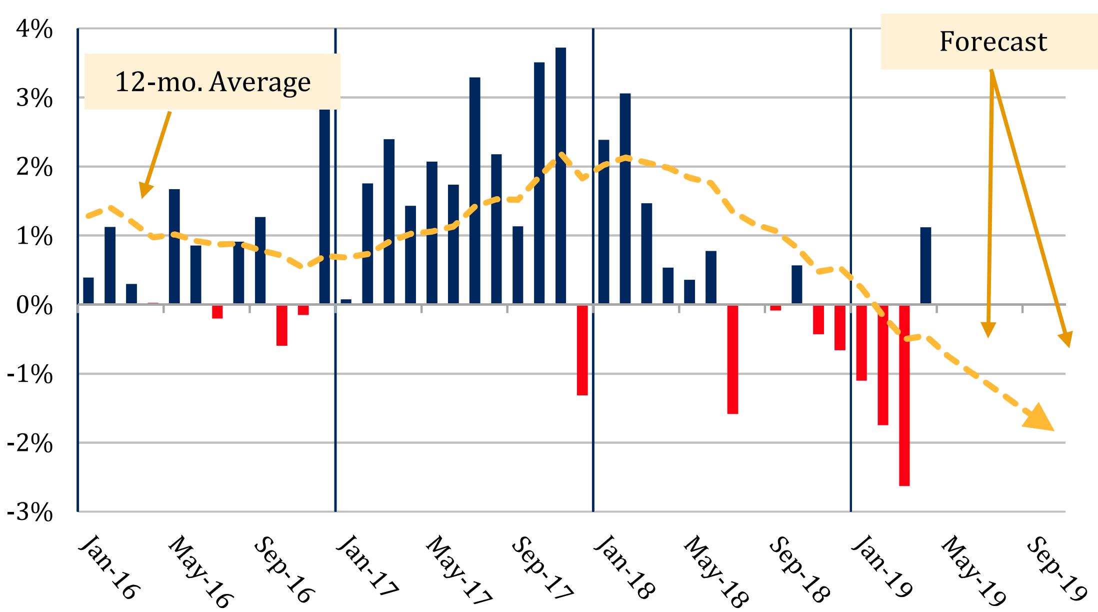
Morgan Chase predicted that there is a 45 percent chance that the U.S. economy will enter into a recession in 2020, up from 20 percent chance at the beginning of 2018.

Near-Term Outlook

The Washington Leading Index has had a negative trajectory for a full year. This decline has become broader and deeper through the year's first quarter. Based on this trend, it would have been easy to conclude that the region's economy was headed into a period of slower GRP growth or worse, a recession (six or more consecutive months of GRP decline).

With its performance in April, the Washington Leading Index has registered a strong monthly over-the-year gain, which if sustained over the second and third quarters, will indicate that the negative forces undermining the region's economic performance over the second half of 2018 and first quarter of 2019 have abated. Most worrisome over the near term is the growing potential for a federal shutdown in October, not a partial-federal shutdown in January when the economy performance is constrained by seasonal factors but a full shutdown in October, a prime month for economic growth. Should a federal shutdown occur, it could erase the other gains that the region's economy had secured during the first nine months of the year. The Stephen S. Fuller Institute will continue to carefully watch and report on these trends until these threats are resolved.

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



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

Washington Area Economic Indicators
Current and Previous Months

Economic Indicator	Estimates			Percent Change	
	Apr-19 Prelim.	Mar-19 Final	Apr-19 Final	Mar-19 to Apr-19	Apr-19 to Apr-19
Washington Area Business Cycle Indicators					
Coincident Index (2015 = 100)	109.0	107.7	106.6	1.28%	2.32%
Leading Index (2015 = 100)	104.1	102.2	103.0	1.86%	1.12%
Washington Area Coincident Index Components					
Total Wage & Salary Employment ('000)a	3,330.2	3,309.4	3,300.4	0.63%	0.90%
Consumer Confidence (South Atlantic)a	180.7	159.8	164.0	13.08%	10.18%
Domestic Airport Passengers ('000)b	2,209.8	2,169.8	2,142.4	1.84%	3.14%
Nondurable Goods Retail Sales ($000,000)c	3,326.7	3,324.4	3,173.6	0.07%	4.82%
Washington Area Leading Index Components					
Total Residential Building Permitsa	2,622.0	1,807.0	1,579.0	45.10%	66.05%
Consumer Expectations (South Atlantic)a	124.6	104.1	111.1	19.69%	12.15%
Initial Unemployment Claimsb	2,059.7	1,956.8	1,362.6	5.26%	51.15%
Durable Goods Retail Sales ($000,000)c	3,775.8	3,812.2	3,642.9	-0.95%	3.65%
Washington Area Labor Force[a]					
Total Labor Force ('000)	3,414.1	3,422.9	3,384.0	-0.26%	0.89%
Employed Labor Force ('000)	3,316.6	3,309.7	3,280.2	0.21%	1.11%
Unemployed Labor Force ('000)	97.5	113.2	103.8	-13.91%	-6.12%
Unemployment Rate	2.9%	3.3%	3.1%	--	--
Washington Area Wage and Salary Employment[a]					
Total ('000)	3,330.2	3,309.4	3,300.4	0.63%	0.90%
Construction ('000)	158.9	156.5	158.9	1.53%	0.00%
Manufacturing ('000)	54.7	55.0	55.1	-0.55%	-0.73%
Transportation & Public Utilities ('000)	68.4	68.6	67.5	-0.29%	1.33%
Wholesale & Retail Trade ('000)	329.8	328.9	334.9	0.27%	-1.52%
Services ('000)	2,008.9	1,992.4	1,976.5	0.83%	1.64%
Total Government ('000)	709.5	708.0	707.5	0.21%	0.28%
Federal Government ('000)	363.0	361.2	363.9	0.50%	-0.25%

[a]Unadjusted data
[b]Seasonally adjusted data
[c]Seasonally adjusted constant (1996) dollars