# Washington Economy Watch

Vol. III, No. 10
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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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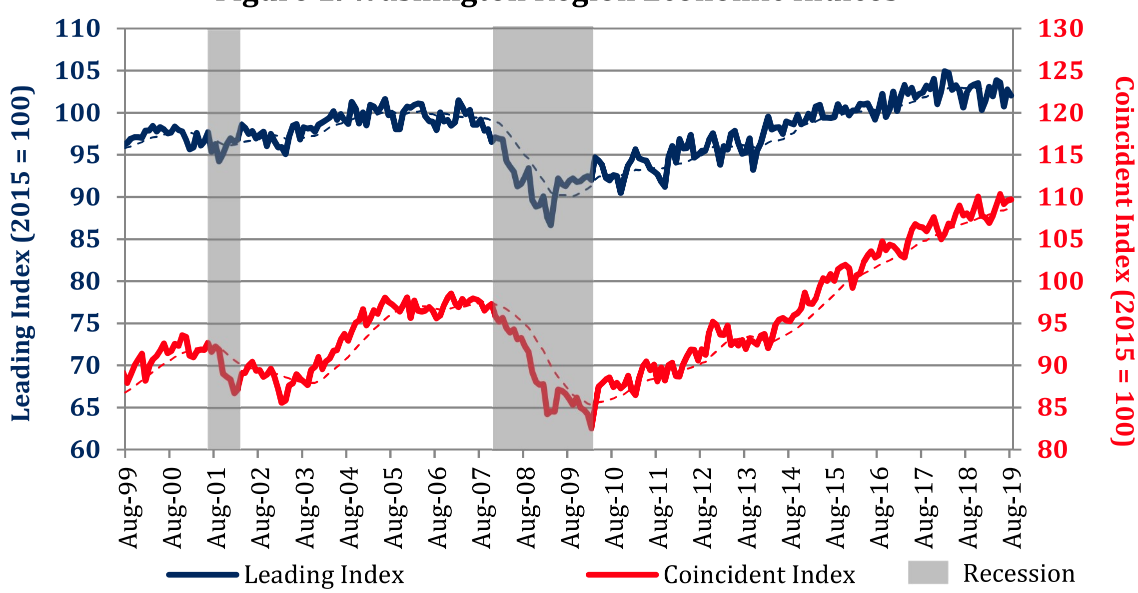
## The Washington Region's Economy Continues To Expand But Its Future Trend Remains Uncertain

In August, the Washington region's Coincident Index registered a second consecutive strong gain while the Leading Index declined reversing its strong one-month gain in July. For the Coincident Index's, this gain extended its consecutive monthly over-the-year increase to a 65th month. For the Leading Index, its August decline extended its volatile pattern in which it has decreased five times in eight months. This pattern, combined with the moderation in the growth rate of the Coincident Index, suggests that region's economic performance this year will not exceed its performance in 2018 as had been projected at the beginning of the year and that slower growth is likely to continue into 2020. Even if there is an agreement on FY 2020 appropriations funding by November 21st, when the Continuing Resolution (CR) expires under which current spending levels have been maintained since October 1st, its promised higher federal spending levels will not have time to benefit this year's performance although would boost growth in 2020. In the absence of the appropriations legislation by November 21st, the region's economy remains vulnerable to further slowing going forward.

**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 0.09 percent in August for a second consecutive gain and for its fifth increase in the last six months on a month-to-month basis. This month's gain further extends the Index's positive trend following the year's weak first quarter performance that had reflected the consequences of the 35-day federal government shutdown that had begun in December.

On a monthly over-the-year basis, August's Coincident Index registered a strong gain of 1.49 percent from August 2018 following its strong gain in July. August's gain extended the Index's upward trend to 65 consecutive months, dating from April 2014. This strong performance reflected increases in three of four the Index's indicators led by an uptick in the rate of job growth.

In August, three of the Coincident Index's four component indicators contributed to its gain:

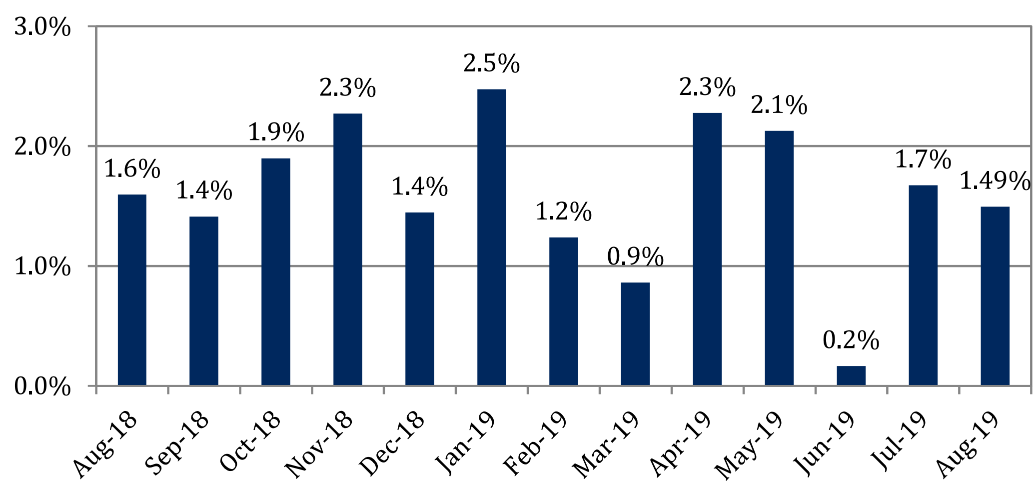
- *Wage and salary employment* in the Washington region increased 1.0% between August 2018 and August 2019;

- *Non-durable goods retail sales* were up 4.2% from August 2018 gaining for a 30th consecutive month on a monthly over-the-year basis; and,

- *Consumer confidence (in the present)* increased by 2.2% from August 2018; while,

- *Domestic passenger volume at Reagan National and Dulles Airports* decreased 0.2% from August.

**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 by six to eight months, decreased by 0.32 percent in August on a monthly over-the-year basis reversing it strong one-month July increase. Its August decrease was the Index' fifth decline in this year's first eight months and eighth decline over the last twelve months. This negative trend has reflected the slowdown in the region's economic performance dating from late 2018 as well as the uneven performance of the Index's components over the past year. The longer these conditions persist, the more difficult it will be to achieve and sustain trend-level growth leading into 2020.

In August, three of the Leading Index's four components contributed to its decrease.

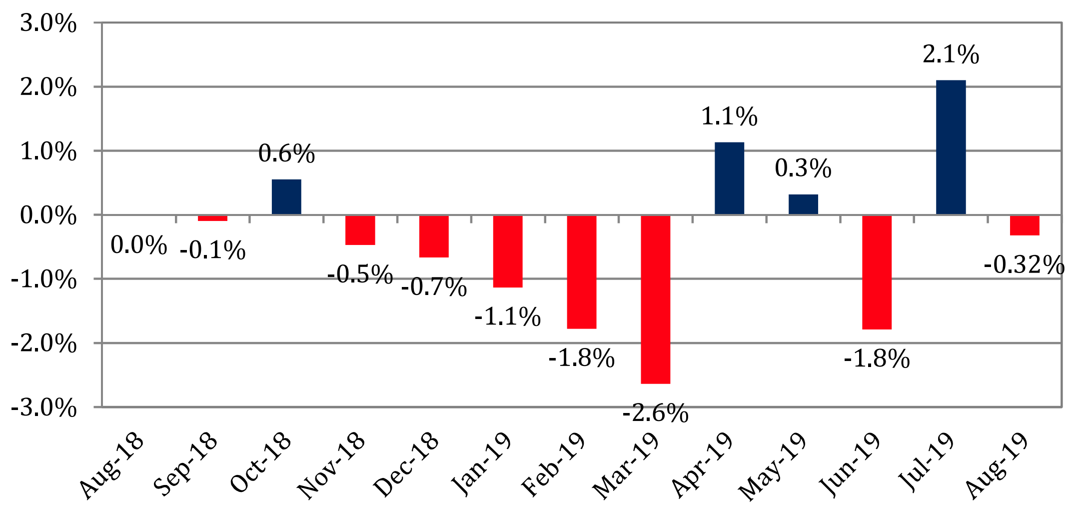
- *Consumer expectations (consumer confidence six months hence)* decreased 6.0% from August 2018 after registering a strong gain in July;

- *Total residential building permits* decreased 8.1% in August after recording a strong gain in July continuing its volatile pattern over the last year; and,

- *Initial claims for unemployment insurance* increased 5.7% (worsened) extending its upward trend to a fifteenth consecutive month; while,

- *Durable goods retail sales* increased 3.9% from their August 2018 level and have gained in six out of this year's first eight months.

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

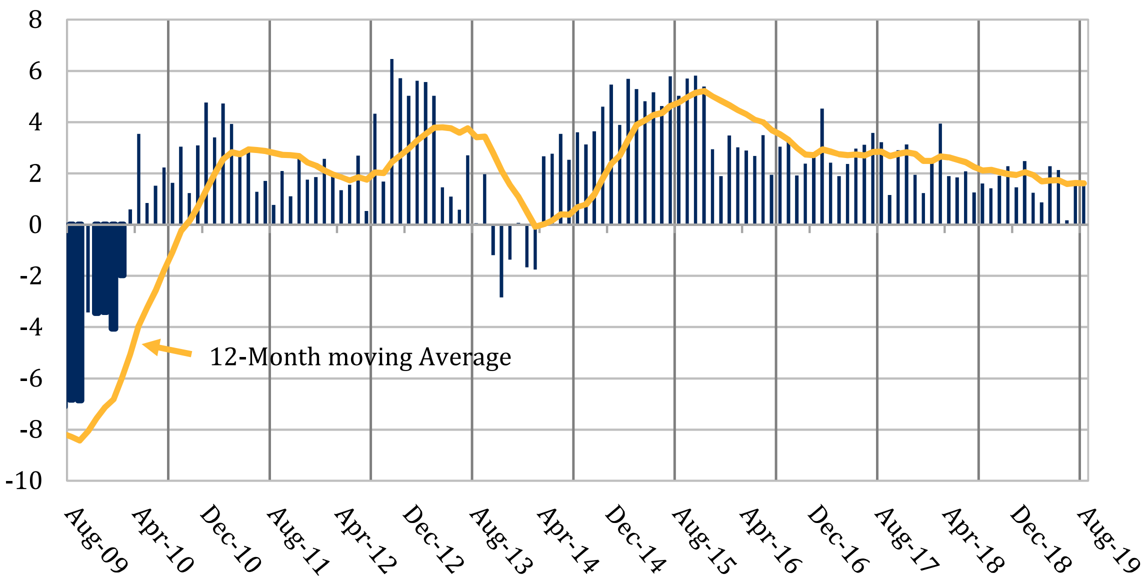



Source: The Stephen S. Fuller Institute at the Schar School, GMU

## Current Performance

While the Washington region's economy has experienced substantial gains since recovering from the effects of Sequester in 2014, as measured by the Coincident Index's 65-month long, monthly over-the-year gain spanning the period from April 2014 through the current month, the trajectory of this expansion has moderated as seen in the track of the Index's twelve-month moving average shown in Figure 4. This slowing of the Coincident Index's growth this year is attributable to both a slowdown in job growth and to the peaking of consumer confidence (in the present) and its uneven performance; its increases and decreases on a month-to-month basis have been almost off-setting since December 2018.

**Figure 4. Washington Region Coincident Index**
**Monthly Over-the-Year Changes**




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

Job growth is the largest component in the calculation of the Coincident Index. At the beginning of the year, 2019 was projected to have a gain of 38,200 new jobs, an increase from the 35,300 new jobs generated during 2018 (it should be noted that job growth in 2018 fell well below its forecast of 52,100 jobs). However, job growth during this year's first six months has averaged only 26,100 with the number of jobs in Suburban Maryland actually declining during this period. In addition to this loss of jobs in Suburban Maryland (in contrast to a projected annual gain of 11,000 jobs), the region's economy lost a total of 11,700 jobs across five sectors (federal, retail trade, financial activities, information services, and manufacturing). While these losses are important, the slower growth occurring in professional and business services and education and health services sectors, two of the three dominant growth sectors in the region since 2010, has also contributed to slower overall job growth.

There are signs that job growth is accelerating. September jobs data, released October 18th, show monthly over-the-year gains of 38,600 and August jobs data were revised higher from 33,600 to 38,400. With July job growth estimated at 42,300, the third quarter's average job gain for the region totaled 39,800.[1] For the year's first nine months, these stronger third quarter gains bring the annual average to 30,600 jobs.

While still below the beginning-of–the-year forecast, job growth in the region is clearly improving with gains in professional and business services, education and health services, and leisure and hospitality services leading the way. While federal government job losses have almost ceased, losses in the retail sector have increased. With unemployment at near historically low levels in the region (3.1%), sustaining faster job growth through the end of the year and beyond will become more challenging. Still, stronger job growth, combined with continuing increases in personal earnings, should sustain the region's strong consumer spending that has been key in supporting the economy's continued growth overall.

Consumer spending has been fueled by a combination of increases in personal earnings (job growth plus increases in wages) and strong consumer confidence (in the present) and consumer expectations. Changes in consumer confidence and expectations can either increase or decrease consumer discretionary spending, outlays for which consumers can find lower cost substitutes or can deferred such as for autos, clothing, personal services, recreation, and eating out. Through August, consumer confidence (in the present) has continued to rise in the region but its rate of increase has slowed (nationally it declined in September).

Consumer expectations, how consumers think the economy will be performing in six months, peaked in December 2018 and is now well off its peak level as it has declined in five of the year's first eight months. Durable goods retail sales, closely tied to consumer expectations, have experienced decreases in three of the year's first eight months but were strong in July and August. And, nondurable retail sales have continued to grow registering monthly over-the-year gains for 30 consecutive months. Still, with growing uncertainty as reflected in the daily volatility of the stock market indices and more broadly in the national and global economic indicators, consumer confidence could be dampened going into the holiday spending season and further constrain the economic growth at the end of the year.

Perhaps, the key uncertainty hanging over the Washington region's economy at this time is the dysfunction in the federal government that threatens approval of the 12 appropriations bills needed to fund its operations in FY 2020. With the Continuing Resolution (CR) under which the federal government is currently operating expiring on November 21st, the Congress and Executive branches will need to agree on a funding path forward to keep the federal government open. Approval of the

[1] The July estimate is likely too large and will be revised downward in March 2020. See https://sfullerinstitute.gmu.edu/2019/08/22/revisions-july/ for more.

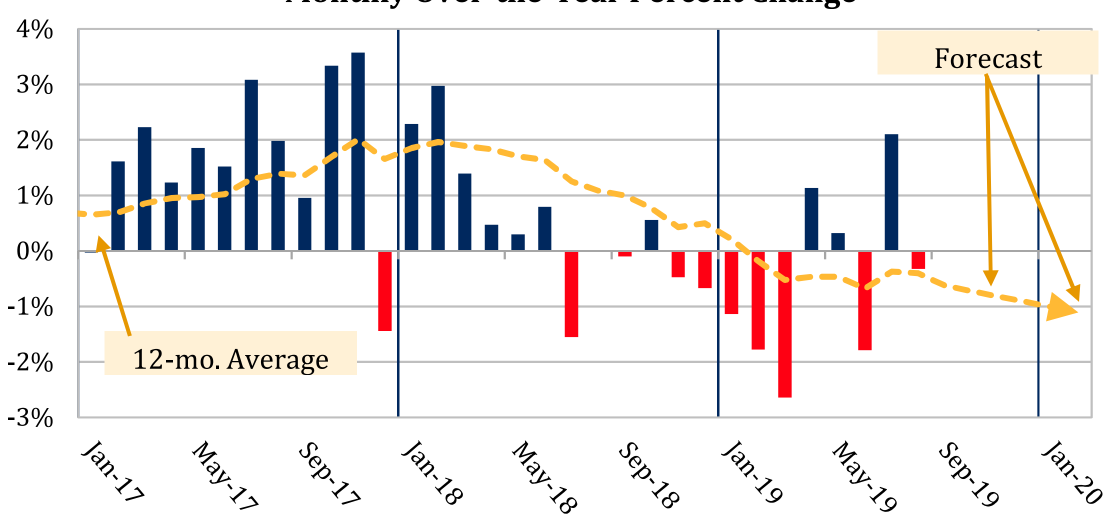
spending levels provided in the Bipartisan Budget Act of 2019 would increase federal spending above current levels and clearly benefit the Washington region's economy, although the economic benefits from this increased federal spending would not be realized until 2020 and 2021; it is too late in the calendar year for any increased federal spending approved in November of have significant benefit to this year's economic performance.

Failure to agree on these appropriations bills and agreeing to another CR, perhaps for the remainder of FY 2020, would keep federal spending at current levels; this would not benefit the economy beyond its current level of support and the resultant economic growth rates would likely continue to fall below forecast. A shutdown would have serious impacts on the economy's performance in 2019 and these would continue until the budget impasse was resolved; a repeat of 2018, except worse. This major uncertainty will be resolved within the month and, by the next issue of Economy Watch, the path forward should be much more clear.

## Washington Region's Near-Term Outlook

For a period now extending back more than twelve months, the Washington Leading Index (Figure 5) has been sending a signal that all is not well with some of the fundamental indicators of the region's future economic growth path. The Index's weaknesses early in 2019 might have been explained in part by the negative consequences of the 35-day partial federal shutdown that lingered through the first quarter. However this does not explain the Index's negative trend starting at midyear in 2018 and its growing volatility this year since March. The long-term track of the Leading Index can be seen in Figure 1 in comparison to the Coincident Index; it has peaked and turned down, quite the opposite of the Coincident Index, which shows the current economy continuing to expand.

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




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

It isn't just one component factor driving the Leading Index negative but rather several indicators have been tracking a negative trajectory over the past year. Resident building permits have been negative in seven of the last twelve months, consumer expectations have been negative in five of the last twelve months (all occurring in the last eight months), initial claims for unemployment insurance have increased (worsened) in each of the last twelve months (although this trend moderated significantly in July and August), and durable goods retail sales have been negative in four of the last twelve months. During this twelve-month period, the leading Index has been negative eight times.

Historically, when the Washington Leading Index has tracked negatively for six to eight months, the Coincident Index has also turned negative in the ensuing months. The Leading Index turned negative in June 2007 to be followed by the Coincident Index in December 2007 announcing the Great Recession. The Leading Index experienced a shallow downturn in December 2000 signaling the onset of the Tech-Bubble Burst and the 2001 Recession; the Washington Coincident Index turned negative in September 2001.

With all of the uncertainty at the national and global levels impacting those economies and having a filtered impact on the Washington region's economy and the region's economy continuing to have a significant federal base, even if it is much smaller than in 2007 (it is still approximately 30% of GRP), the performance of the national economy will not be as important to the Washington region's economic performance over the next six months as will federal spending levels. In the longer run, whether the national economy manages to achieve its currently forecasted 2.3% and 2.0% growth rates in 2019 and 2020, respectively, will be far less important to the growth rates of the region's economy than the final funding levels for the federal government.

The Washington region's economy will have difficulty growing faster than 2.3 percent if the federal government is forced to operate under a CR for much or all of FY 2020. If a shutdown ensues following the expiration of the CR on November 21$^{st}$, all bets are off. The economic impacts of a shutdown will depend on how long the shutdown lasts and by the agencies that are affected. The best outcome for the Washington region economically would be full funding of the approved budget agreement retroactive to the beginning of the Fiscal Year. With full funding, the region's growth rate in 2019 could possibly achieve its beginning-of-the-year rate of 2.5 percent and grow 2.4 percent in 2020, growth rates exceeding other projected US. GDP rates for those years. Stay tuned.

**Washington Area Economic Indicators**
**Current and Previous Months**

| Economic Indicator | Estimates | | | Percent Change | |
|---|---|---|---|---|---|
| | Aug-19 Prelim. | Jul-19 Final | Aug-18 Final | Jul-19 to Aug-19 | Aug-18 to Aug-19 |
| **Washington Area Business Cycle Indicators** | | | | | |
| Coincident Index (2015 = 100) | 109.7 | 109.6 | 108.1 | 0.09% | 1.49% |
| Leading Index (2015 = 100) | 102.0 | 102.8 | 102.4 | -0.70% | -0.32% |
| **Washington Area Coincident Index Components** | | | | | |
| Total Wage & Salary Employment ('000)[a] | 3,334.7 | 3,332.7 | 3,301.1 | 0.06% | 1.02% |
| Consumer Confidence (South Atlantic)[a] | 180.4 | 174.7 | 176.5 | 3.26% | 2.21% |
| Domestic Airport Passengers ('000)[b] | 2,223.9 | 2,261.8 | 2,229.3 | -1.68% | -0.24% |
| Nondurable Goods Retail Sales ($000,000)[c] | 3,412.0 | 3,395.4 | 3,273.0 | 0.49% | 4.25% |
| **Washington Area Leading Index Components** | | | | | |
| Total Residential Building Permitsa | 1,698.0 | 2,870.0 | 1,848.0 | -40.84% | -8.12% |
| Consumer Expectations (South Atlantic)[a] | 112.0 | 115.5 | 119.2 | -3.03% | -6.04% |
| Initial Unemployment Claims[b] | 1,905.7 | 2,040.7 | 1,803.2 | -6.62% | 5.69% |
| Durable Goods Retail Sales ($000,000)[c] | 3,765.9 | 3,719.1 | 3,625.7 | 1.26% | 3.87% |
| **Washington Area Labor Force[a]** | | | | | |
| Total Labor Force ('000) | 3,469.0 | 3,512.6 | 3,383.6 | -1.24% | 2.52% |
| Employed Labor Force ('000) | 3,359.4 | 3,395.7 | 3,269.1 | -1.07% | 2.76% |
| Unemployed Labor Force ('000) | 109.6 | 116.9 | 114.5 | -6.24% | -4.30% |
| Unemployment Rate | 3.2% | 3.3% | 3.4% | -- | -- |
| **Washington Area Wage and Salary Employment[a]** | | | | | |
| Total ('000) | 3,334.7 | 3,332.7 | 3,301.1 | 0.06% | 1.02% |
| Construction ('000) | 167.3 | 165.5 | 164.6 | 1.09% | 1.64% |
| Manufacturing ('000) | 55.4 | 56.1 | 56.0 | -1.25% | -1.07% |
| Transportation & Public Utilities ('000) | 69.7 | 69.8 | 68.1 | -0.14% | 2.35% |
| Wholesale & Retail Trade ('000) | 331.8 | 332.2 | 337.8 | -0.12% | -1.78% |
| Services ('000) | 2,030.7 | 2,019.1 | 1,997.3 | 0.57% | 1.67% |
| Total Government ('000) | 679.8 | 690.0 | 677.3 | -1.48% | 0.37% |
| Federal Government ('000) | 364.8 | 363.7 | 364.0 | 0.30% | 0.22% |

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