



The  
**STEPHEN S. FULLER INSTITUTE**  
for Research on the Washington Region's Economic Future



# Washington Economy Watch

Conference Issue  
November 2022

*See Page 9 for Conference Information*

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 area'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 six complete business cycles in addition to the Post-COVID 19 cycle that began in May 2020.*

# Washington Economy Watch

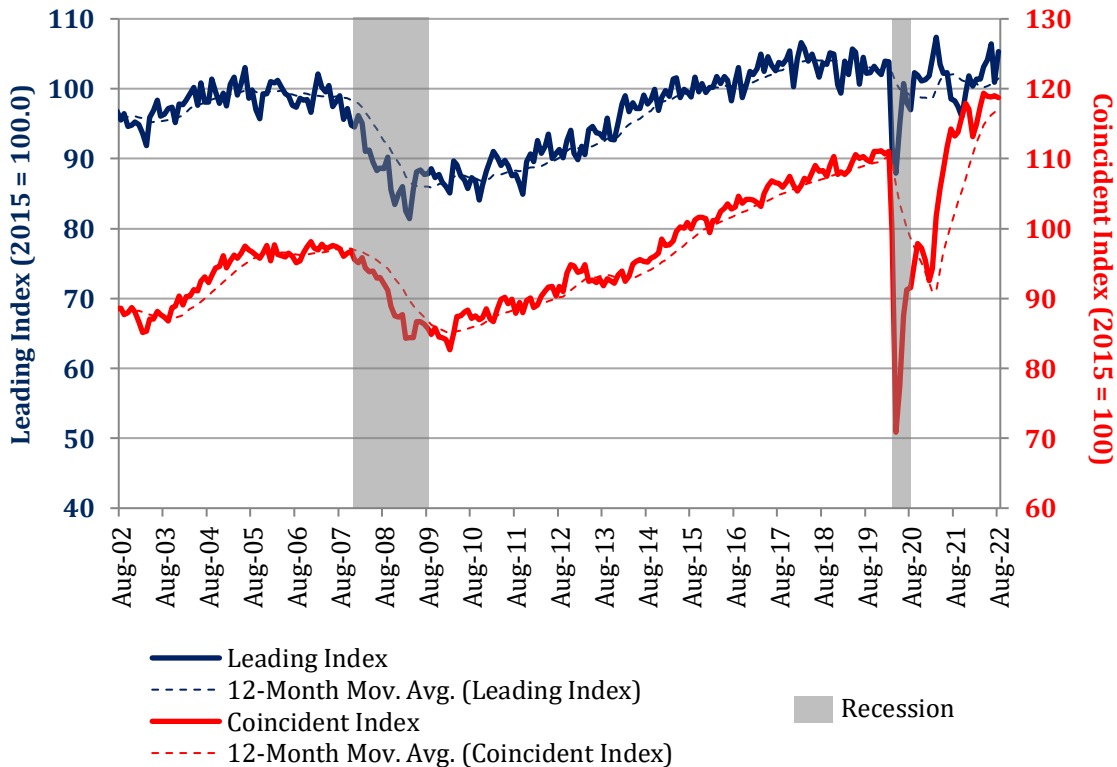
Conference Issue

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## The Washington Area's Economy Slowed in the 3<sup>rd</sup> Quarter; Outlook Remains Uncertain

The Washington area's economic performance, as tracked by the Washington Coincident Index, has experienced a slowing trend since February and does not appear to have benefited from the US economy's renewed GDP growth during the third quarter. However, the Washington Leading Index, which is designed to forecast the Washington area's near-term economic outlook, has been positive each month since April and its gains have been trending higher. This mixed performance offers insight into the underlying structure of the Washington area's economy that will shape its performance going forward as the Federal Reserve Board focuses on reducing the inflation rate by continuing to raise interest rates with only secondary concerns about tripping the national economy into recession in 2023.

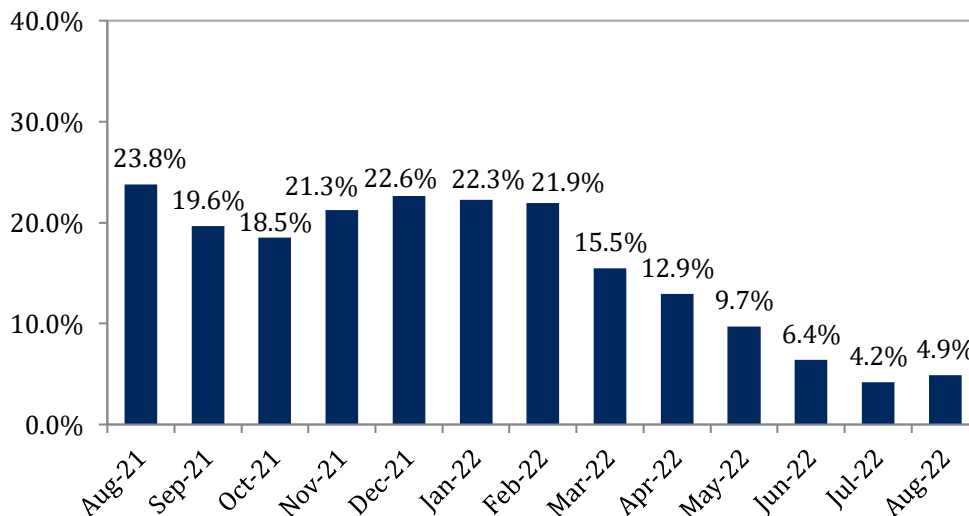
**Washington DC, Area Economic Indices**



The **Washington Coincident Index**, which represents the current state of the metropolitan area economy, extended its positive upward trend in August for an eighteenth consecutive month dating back to March 2021. This trend has been largely driven by the normalization of the economy following the initial shocks in spring 2020 that had resulted from the pandemic-generated disruptions to the supply chain, consumer spending, and business operations. The sequential moderation of this growth trend since February suggests that the normalization process is nearing completion. The Coincident Index’s performance reflects this flattening of the Washington area’s growth trend with only a marginal single monthly gain on a month-to-month basis over the last four months. Still, compared to August 2021, the Index was up 4.9 percent with two of its four indicators being positive.

- *Wage and salary employment* growth in the Washington area increased 2.2% between August 2021 and August 2022; and,
- *Domestic passenger volume at Reagan National and Dulles Airports* continued to normalize increasing 37.5 percent between August 2021 and August 2022; while,
- *Non-durable goods retail sales* declined for a third consecutive month on a monthly over-the-year basis and having registered only one slightly positive gain (in April) over the past six months; and,
- *Consumer confidence (current circumstances)* declined for the fourth consecutive month.

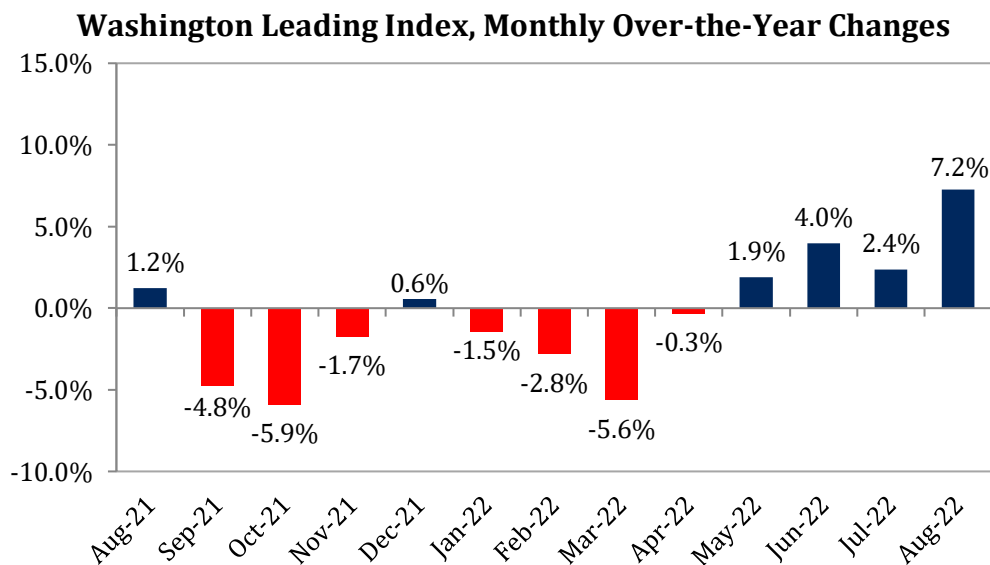
**Washington Coincident Index, Monthly Over-the-Year Changes**



The **Washington Leading Index**, which is designed to forecast the performance of the metropolitan area economy six to eight months in advance, registered a sharp increase in August, gaining 7.25 percent on a month-over-year basis. After tracking lower during the year’s first four months, the positive trajectory of the Leading Index has accelerated suggesting that the Washington area’s economy may experience accelerating growth into the

early months of 2023. While in August, all four of the Index’s components contributed to its sharp gain, an examination of individual components reveals a more nuanced assessment.

- *Total residential building permits* continue to rebound for a fourth consecutive month from their same-month 2021 levels;
- *Initial claims for unemployment insurance* continued to decrease (improve) for a seventh consecutive month reflecting a continuing tightening of the labor market; and,
- *Durable goods retail sales* increased slightly in August gaining 0.7% from August 2021 after tracking a downward trajectory for more than a year; while,
- *Consumer expectations (consumer confidence six months hence)* declined for a seventh consecutive month in August.



The August data underlying the Coincident and Leading Indices provide both a snapshot of the Washington area’s economic performance during that month and a longer view of performance patterns going backwards and pointing forwards from which forecasts of the economy’s near-term performance can be constructed. As for August’s performance, combined with June and July, its indicators show the Washington area economy to have largely recovered from the sharp losses and major disruptions it experienced because of the COVID-19 pandemic. However, while the economy appears to have largely returned to its pre-pandemic growth trend by early 2022, its performance over the past six months reveals underlying weaknesses that suggest vulnerabilities as it is being impacted by negative national and global economic forces: inflation rates ranging above 8 percent, rapidly rising interest rates—30-year fixed mortgage rates above 7%, energy supply disruptions generated by the war in Ukraine, continuing tight labor markets, and slumping consumer confidence and slumping consumer spending, just to mention a few.

In the Washington area, the weakening of consumer confidence—both in the present and for expectations—is already taking a toll on consumer spending, a major driver of the economy’s performance. While the rapid increase in home mortgage rates over the past six months has already cooled the home resale market, as seen in both the number of units sold and in a slowing of price increases, these trends have not yet been reflected in the number of residential building permits being issued. Of course, the issuance of residential building permits does not guarantee construction starts; permits are only an indication of future building activity.

With additional interest rate increases by the Federal Reserve Board expected in 2022 and possibly additional increases in 2023, mortgage rates will certainly increase further and slow housing production and resales. Higher interest rates, which in the short term may exacerbate inflation while also slowing demand, will weaken the labor market and push initial claims for unemployment insurance higher. With these negative forces undermining the economy’s performance indicators, which held up over the summer, they will likely weaken and turn negative in the coming months. The timing and magnitude of these indicators’ performances going forward will mirror the Washington area’s economic performance in 2023.

## **Recent Job Growth Trends**

A key measure of the Washington economy’s cyclical health is its generation of new jobs and the sectors that are adding and losing jobs. Job change also has implications for the economy’s productivity as all jobs do not generate the same GRP value. While the Washington area’s economy has been widely considered to be dominated by its federal functions, federal employment has not been the primary source of job growth over the past forty years with the area’s economic growth being driven by the expansion of professional and business services (much of which has been directly related to increased federal procurement spending since 1980) and the growth of the education and health services and the construction sectors.

During the 2012-2017 period, these sectors—professional and business services, health and education, and construction accounted for 66.2 percent of the area’s job growth while only representing 38.1 percent of the Washington area’s job base. These sectors together experienced an 8.2 percent job gain over these five years compared to the region’s total job gain of 4.7 percent. In contrast, Federal government jobs decreased 2.4 percent during this period.

Comparing this earlier period to the current period (2017 to mid-2022) and recognizing that these periods are not quite equal in length, reveals the differential effects of the COVID-19 recession and subsequent recovery, and provides evidence regarding the resiliency of the Washington area’s economic drivers as these have evolved over the longer term. The dominant job-producing sectors during the 2012-2017 period continued to grow in the current period, rising 5.3 percent in total. While these three sectors remained dominant job generators, it is notable that the education and health services sector, which grew by 12.8

percent between 2012 and 2017, has been slow to rebound only registering a net gain of 1.0 percent between 2017 and mid-year 2022. And, while the construction sector has continued to add jobs over the post-recession period, it is likely that this sector will experience its normal cyclical slowdown as the national economy experiences slow growth or slips into a mild recession in 2023.

Major Sources of Job Growth in the Washington Area  
2012-2017 and 2017-mid-2022

Sectors	% Change 2012-2017	% Change 2017-7/2022
<u>Growth Sectors</u>		
Professional & Business Services	5.3	8.0
Education & Health Services	12.8	1.0
Construction	<u>10.0</u>	<u>4.3</u>
Sub-Total	8.2	5.3
<u>Other Sectors</u>		
Retail Trade	5.0	-5.5
Hospitality & Leisure Services	16.6	-4.0
Financial Services	6.8	- 4.0
Other Services	12.0	-3.5
State & Local Government	7.1	-2.5
Federal Government	<u>-2.4</u>	<u>0.8</u>
All Jobs	4.7	-1.6

Source: U.S. Bureau of Labor Statistics

Still, these sectors' gains contrast with the region's overall loss of jobs during this period (1.6 percent down from 2017). While the federal government registered a slight job increase during this period, growing 0.8 percent, other sectors experienced significant losses during the COVID-19 recession and have yet to fully recover. These sectors include retail trade, down 5.5 percent, hospitality and leisure services, down 4.0 percent, financial services, down 4.0 percent, other services, down 3.5 percent, and state and local government, down 2.5 percent. With so many sectors struggling to recover in combination with the continuing weaknesses in the education and health services sector and weakened outlook for the construction sector in 2023, this raises concerns regarding the future performance of the Washington area's economy.

Another common measure of an economy's health is its unemployment rate. The Washington area's unemployment rate remains low tracking similarly to the U.S. rate ranging between 3.5 and 3.6 percent during the third quarter and is currently well below its 5.3% rate in August 2021. As this rate has declined over the past year, initial claims for unemployment insurance, also have declined. Both indicators tend to lag the economy's real time performance by several months, as employers tend to hold on to their workers even after

revenues soften hoping to avoid layoffs and opt to leave vacancies unfilled rather than immediately begin the painful process of shedding workers. Still, as the economy slows in response to the Federal Reserve Board's tight monetary policy, and with additional interest rate increases expected before the end of the year, the unemployment rate and the number of initial unemployment claims also can be expected to rise before the end of the year and will likely to continue this upward trend in 2023.

## **The Washington Area's Slowing Economy**

The near-term outlook for the Washington area economy will reflect a combination of (1) the cyclical behavior of its sectors—the balancing of their performance between those that are more and less sensitive to changes in local, national and international demand, and (2) the area economy's secular patterns—the underlying structure of the economy around which cyclical changes revolve. For the Washington area, its secular performance patterns are best seen in the economy's long-term gross regional product (GRP) growth rates. Rather than annual growth rates, which are used to map cyclical economic performance, secular performance is measured over multi-year periods, periods bounded by recessions or major economic events that fundamentally alter the subsequent trajectory of the economy.

For the Washington area, these longer-term periods can be related to a mix of local and national events that have shifted the area's historic structural pattern—sectoral shifts. For example, the shift towards privatization of federal activities sparked rapid gains in procurement spending by the federal government to the benefit of businesses located (or relocating to) the Washington area. This shift began in 1980 but appears to have flattened out over the last five years. A second event that accelerated the shift of the Washington area's economy from its dominance by federal employment and payroll spending to the advancement of the professional and business services sector, was the introduction of computer-based technologies to the work place that drove scientific and technical job growth in the Washington area beginning in the early 1990s and was one of the competitive advantages of the Washington area's labor force cited by Amazon in selecting Arlington County in 2018 for its HQ2 location.

The competitive advantages and disadvantages of the Washington area for business growth and investment and for attracting and retaining a productive and technologically advanced workforce have determined the rates of its economic growth over the long run and have affected the severity of cyclical patterns over this extended period. Looking backward over the Washington area's economic performance during periods of national economic recession, it appears that its mix of economic sectors and their net competitive position in the national and international economies have helped to moderate the negative effects of these recessions locally—those experienced by the Washington economy have been shallower and shorter and generally the recoveries have been more rapid.

For many, this outcome has been attributed to the economic stability associated with being the nation's capital and the large and steady federal employment base (and its payroll) and large and growing federal procurement spending that supports a major segment of the area's

economy, and to a degree this has been true. Still, the trajectory of growth before and after national recessions cannot be so easily explained. Understanding the underlying causes of these different growth rates is essential to guiding the area's future long-term growth path beyond managing the short-term impacts of a recession or slowdown.

As shown below, the Washington area's gross regional product experienced strong growth over the 1970-2010 period with average annual growth rates increasing 3.6% in the 1970s, peaking during the 1980s averaging 4.9% annually, and slowing to a still-respectable average annual rate of 3.2% in the 2000s. However, in the more recent years, the Washington area's GRP growth rate has moderated, averaging 1.1% annually between 2010 and 2017 and 0.5% between 2017 and 2021.

**Gross Regional Product in the Washington Area and Rank  
1970-2021 (Annual Average Percent Change)**

Decade	Annual Percentage	Ranking <sup>1</sup>
1970s	3.6	
1980s	4.9	
1990s	3.6	5th
2000s	3.2	4th
2010-2017	1.1	5th
2017-2021	0.5	6th

Source: U.S. Bureau of Economic Analysis, SFI.

<sup>1</sup>In 1950, the Washington area's economy ranked 9<sup>th</sup> in GRP size among the nation's fifteen largest metropolitan areas.

On a comparative basis, the Washington area's strong economic performance during the forty-year period between 1970 and 2010 made it once of the fastest growing metropolitan areas among the nation's fifteen largest. Its slower growth since 2010, compared to its peers (3<sup>rd</sup> slowest rate of gain among 15 largest metros), has resulted in its ranking dropping from the fourth largest metropolitan area economy in 2010 to sixth largest in 2022 having been overtaken by San Francisco/Oakland and Dallas/Fort Worth.

The Washington area's economic growth trajectory has flattened over the past decade and, as a result, will provide less cushion against the national economic slowdown anticipated for the next two years. While the area's unemployment rate will not increase as much as it does nationally during the downturn, our recovery will lag compared to national economic performance – unless public and business leaders across the Washington metropolitan area aggressively address challenges such as housing affordability, transportation options, regulatory issues, and support for the entrepreneurial and innovation eco-systems.



## Washington Area Economic Indicators Current and Previous Months

Economic Indicator	Estimates			Percent Change	
	Aug-22 Prelim.	Jul-22 Final	Aug-21 Final	Jul-22 to Aug-22	Aug-21 to Aug-22
<b>Washington Area Business Cycle Indicators</b>					
Coincident Index (2015 = 100)	118.8	119.0	113.2	-0.23%	4.89%
Leading Index (2015 = 100)	105.3	100.9	98.2	4.39%	7.25%
<b>Washington Area Coincident Index Components</b>					
Total Wage & Salary Employment ('000) <sup>a</sup>	3,304.8	3,313.4	3,234.8	-0.26%	2.16%
Consumer Confidence (South Atlantic) <sup>a</sup>	149.3	145.7	155.0	2.47%	-3.68%
Domestic Airport Passengers ('000) <sup>b</sup>	2,189.4	2,196.8	1,592.5	-0.34%	37.48%
Nondurable Goods Retail Sales (\$000,000) <sup>c</sup>	4,132.1	4,166.0	4,192.6	-0.81%	-1.44%
<b>Washington Area Leading Index Components</b>					
Total Residential Building Permits <sup>a</sup>	3,375.0	2,609.0	1,651.0	29.36%	104.42%
Consumer Expectations (South Atlantic) <sup>a</sup>	76.4	64.9	91.8	17.72%	-16.78%
Initial Unemployment Claims <sup>b</sup>	1,384.1	1,829.6	7,972.2	-24.35%	-82.64%
Durable Goods Retail Sales (\$000,000) <sup>c</sup>	3,810.0	3,702.7	3,781.7	2.90%	0.75%
<b>Washington Area Labor Force</b>					
Total Labor Force ('000)	3,382.7	3,421.1	3,375.1	-1.12%	0.23%
Employed Labor Force ('000)	3,259.2	3,301.7	3,195.2	-1.29%	2.00%
Unemployed Labor Force ('000)	123.4	119.4	179.8	3.36%	-31.36%
Unemployment Rate	3.6%	3.5%	5.3%	--	--
<b>Washington Area Wage and Salary Employment</b>					
Total ('000)	3,304.8	3,313.4	3,234.8	-0.26%	2.16%
Construction ('000)	164.3	166.5	162.5	-1.32%	1.11%
Manufacturing ('000)	56.6	56.5	55.3	0.18%	2.35%
Transportation & Public Utilities ('000)	80.1	79.2	74.2	1.14%	7.95%
Wholesale & Retail Trade ('000)	328.2	328.4	321.8	-0.06%	1.99%
Services ('000)	1,978.9	1,987.8	1,926.0	-0.45%	2.75%
Total Government ('000)	696.7	695.0	695.0	0.24%	0.24%
Federal Government ('000)	368.4	370.8	376.1	-0.65%	-2.05%

<sup>a</sup>Unadjusted data

<sup>b</sup>Seasonally adjusted data

<sup>c</sup>Seasonally adjusted constant (1996) dollars



## Stephen S. Fuller Institute/Center for Regional Analysis **ECONOMIC OUTLOOK FORUM**

Economic uncertainty, muddled outlooks for business and government, pandemics, war. Just another day doing business in the nation's capital. Still, if you need perspective and guidance on where the DC regional economy is headed, join us for this year's Economic Outlook Forum presented by the Stephen S. Fuller Institute and the Center for Regional Analysis at Mason's Schar School of Policy and Government as we examine our current challenges, opportunities, and where our regional economy is headed for 2023 and beyond.



Stephen S. Fuller  
Dir. Emeritus, SFI



Terry L. Clower  
Director, CRA

**November 15, 2022**  
**GMU Arlington Campus**  
**Van Metre Hall, 1<sup>st</sup> Fl Auditorium**

3351 Fairfax Dr., Arlington, VA 22201  
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Parking Garage Access off N. Kirkwood  
Questions? Email us at [cra@gmu.edu](mailto:cra@gmu.edu)

**Attendance is free but please register at [CRA Event](#)**

### Agenda

8:30 – 9:00	Coffee and Fellowship	
9:00 – 9:03	Welcome to Campus	Dean Mark Rozell
9:03 – 9:10	President's Welcome	Dr. Greg Washington
9:10 – 9:20	Opening remarks	Bob Buchanan
9:20 – 10:00	Is the Washington Region's Economy Still Recession Proof?	Dr. Stephen S. Fuller
10:00 – 10:40	Challenges, Opportunities, & Adaptation: The National Capital Region in 2023 and Beyond	Dr. Terry L. Clower
10:40 – 11:00	Q&A, Engagement	Dr. Clower & Dr. Fuller
11:00	Adjourn	