



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



Washington Economy Watch

Looming Uncertainty

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The Stephen S. Fuller Institute
for Research on the Washington Region's Economic Future
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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

Uncertainty

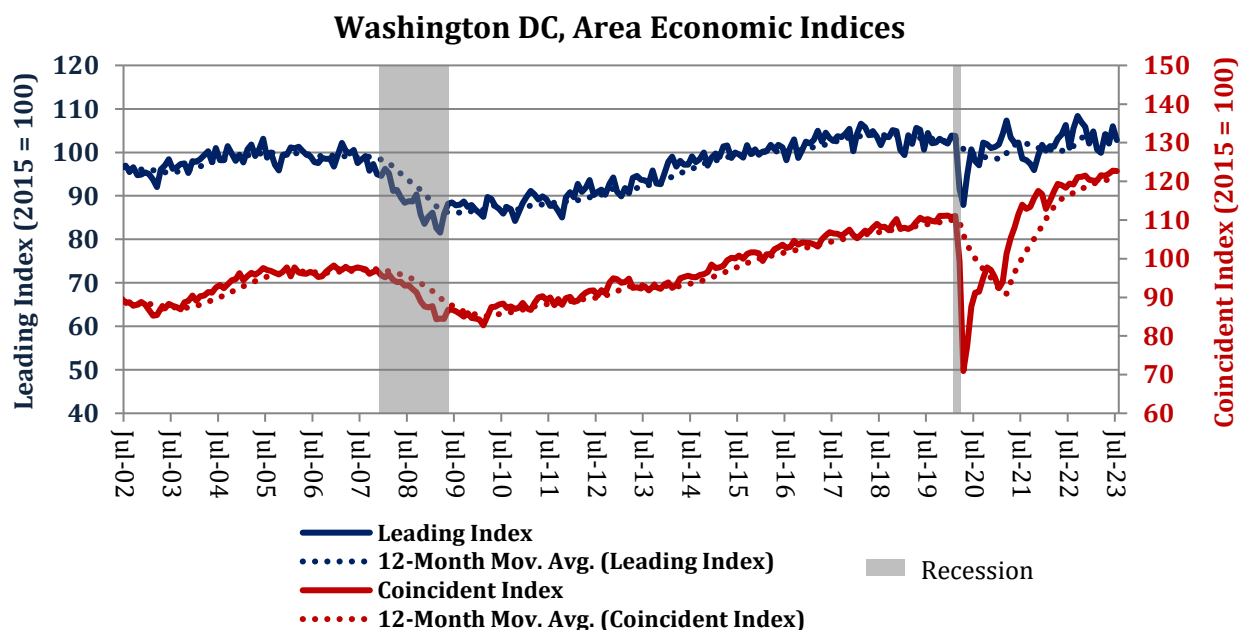
September 2023

Washington Area Economy: Looming Uncertainty

The Washington Coincident Index and the Washington Leading Index continue to provide mixed signals, as both the Coincident Index and the Leading Index were positive in July.

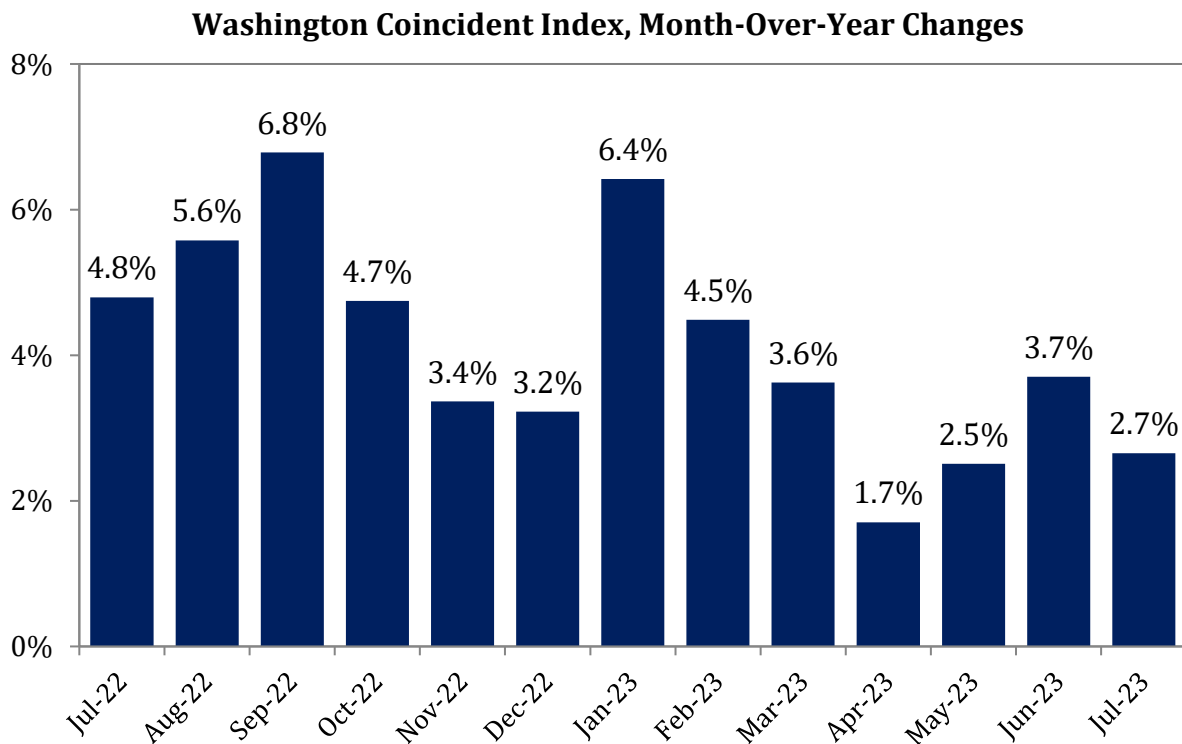
- The Coincident Index increased 2.7% from July 2022 to July 2023, a smaller month-over-year increase than in June but in line with May.
- The Leading Index increased 1.8% in July after two consecutive negative readings.

The mixed signals from the indices are perhaps unsurprising as the Federal Reserve only began lifting interest rates in spring of 2022. The long and variable lags of roughly 18 to 24 months that it takes policy actions to appear in the real economy suggest that the increased interest rates would only start to bite soon. Coupling the potential of monetary policy finally starting to impact the real economy with student loan repayments restarting, a potential government shutdown, and depleted savings accounts, a recession still appears likely. Positively, the previous government shutdown did not materially impact federal contract obligations for contractors in the Washington region, as discussed in the near-term outlook. However, it remains our expectation that the Washington region will record a short and shallow contraction, near the very end of 2023 or the beginning of 2024.



The **Washington Coincident Index**, which represents the current state of the Washington region's economy, increased by 2.7% from July 2022 to July 2023. The month-over-year increase in July marked the first deceleration since April. Following the month-over-year increase of 1.7% in April, the Coincident Index increased 2.5% in May and 3.7% in June. While all components of the Washington Coincident Index increased month-over-year in July 2023, three of the four decelerated from June to July. Furthermore, the increase in wage and salary employment was the smallest reading in over a year.

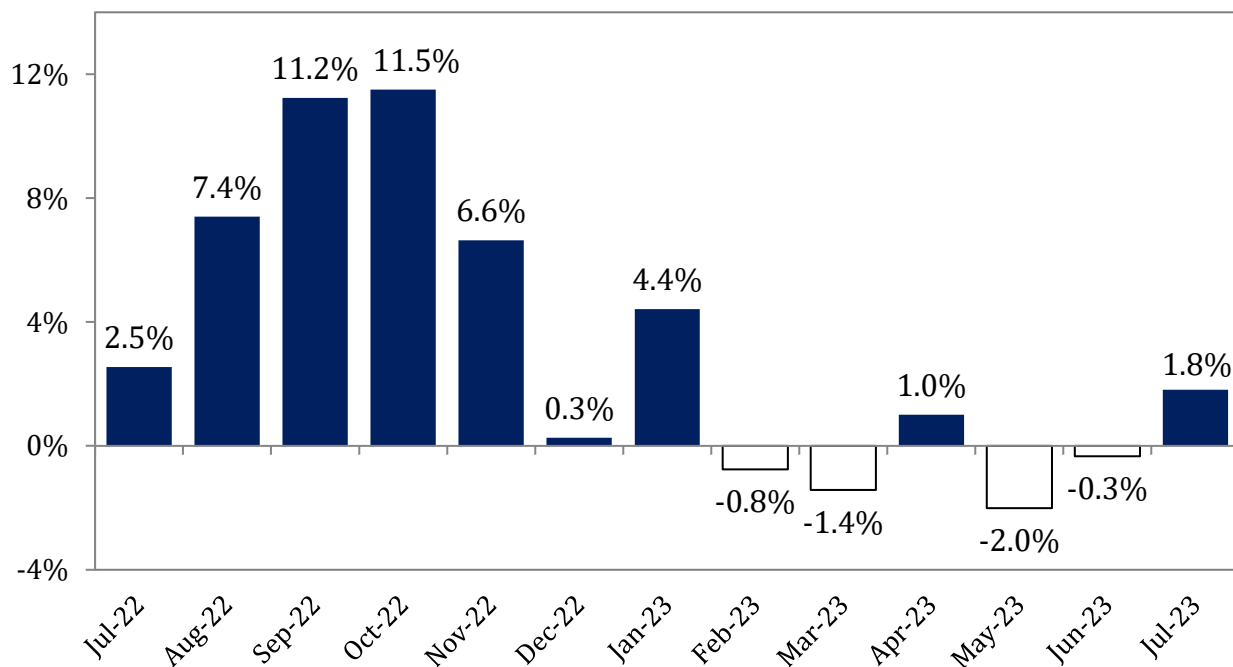
- *Consumer confidence (current circumstances)* increased 15.5% from July 2022 to July 2023, a strong reading following the strong 11.0% increase in June; and,
- *Domestic passenger volume at Reagan National and Dulles Airports* increased 6.2% from July 2022 to July 2023, the second month-over-year deceleration, down from 9.1% in May and 8.8% in June; and,
- *Non-durable goods retail sales* increased 1.9% month-over-year, down from a 2.6% month-over-year increase in June; and,
- *Wage and salary employment* in the Washington area increased 1.3% from July 2022 to July 2023, the lowest month-over-year increase in over a year.



The **Washington Leading Index**, designed to forecast the performance of the metropolitan area economy six to eight months in advance, increased 1.8% month-over-year in July 2023. Although two of the four components worsened month-over-year, initial claims for unemployment increased (worsened) for the second consecutive month. Furthermore, while the Leading Index increased from July 2022 to July 2023, the July 2022 reading was notably below 2022 readings in June, August, and September. Given the low reading in July 2022, it is likely that the leading index will be negative in August. While the economy has generally proven to be resilient, our expectation remains that the Washington region's economy will record a shallow recession during the end of 2023 or possibly early 2024.

- *Consumer expectations (consumer confidence six months hence)* increased 38.2% from July 2022 to July 2023, accelerating from the notable 22.9% month-over-year increase in June; and,
- *Durable goods retail sales* increased 4.2% month-over-year, the third consecutive month-over-year increase; and,
- *Initial claims for unemployment insurance* increased (worsened) 26.1% from July 2022 to July 2023, the second consecutive month-over-year increase; and,
- *Total residential building permits* decreased 26.3% month-over-year, the sixth negative reading in the first seven months of 2023.

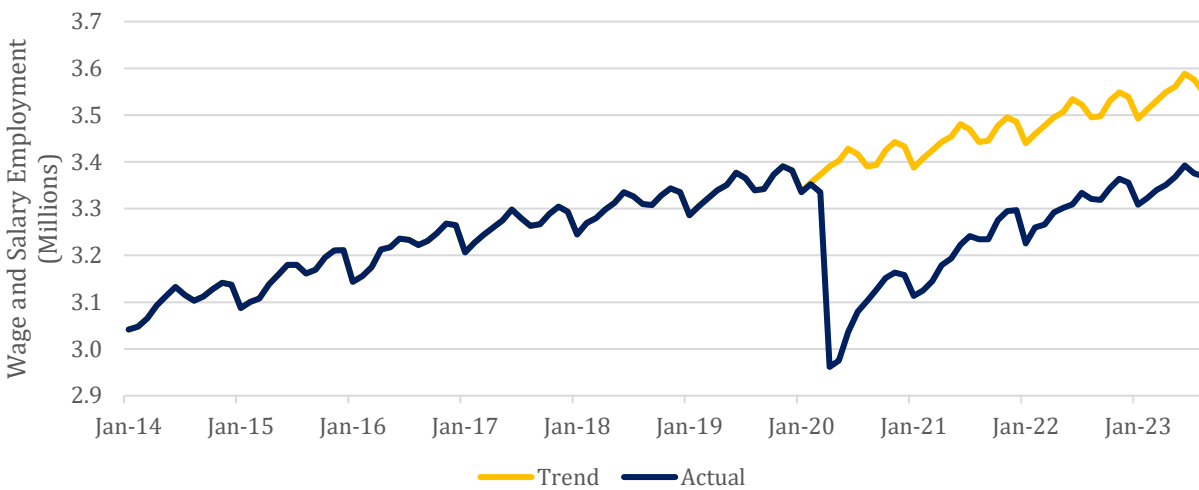
Washington Leading Index, Month-Over-Year Changes



Current Performance

Employment growth in the Washington Region has slowed to pre-pandemic levels. From January 2015 through December 2019, month-over-year employment growth averaged 1.5% before the pandemic interrupted the gains. Unfortunately, robust employment growth following the pandemic induced employment contraction has slowed to pre-pandemic rates, standing at 1.3% in July 2023, the smallest month-over-year increase since the onset of the pandemic. Unfortunately, despite returning to pre-pandemic growth rates, the region has roughly 180,000 fewer jobs than if the pre-pandemic growth rate of 1.5% had continued uninterrupted. In other words, the Washington region would have 5.3% more payroll jobs in July 2023 if the pandemic had not occurred.

Wage and Salary Employment: Trend vs Actual
January 2014 to July 2023



Source: Bureau of Labor Statistics (Not Seasonally Adjusted), GMU Stephen S. Fuller Institute

Near-Term Outlook

The most immediate threat to the Washington region is a potential government shutdown. The previous shutdown was a 5-week partial shutdown lasting from December 22nd, 2018 to January 25th, 2019. Nationally, the CBO estimated that the prior shutdown reduced GDP by 0.02% for 2019.¹ Locally, the immediate economic impacts of a shutdown are largely the result of reduced compensation of federal employees and federal spending on goods and services. As discussed in the [June](#) edition of Economy Watch, federal employment in the Washington region has been declining since August 2022, a federal shutdown would further reduce the economic impact of federal employees. While the threat of reduced federal employee compensation remains a real possibility, federal workers received back pay after the 2019 shutdown resulting in federal compensation being generally unaffected.

¹ <https://www.cbo.gov/system/files/2019-01/54937-PartialShutdownEffects.pdf>

To examine the spending impacts of the previous shutdown on federal spending on goods and services, contract obligations in the core Washington region are shown below. The core Washington region is defined as D.C., Montgomery County, Prince George’s County, Arlington County, Alexandria City, Fairfax County, Fairfax City, and Falls Church City. To strip out usual seasonal variation, only the first quarter of the years 2014 through 2019 are shown. 2020 is not shown as it included the onset of the pandemic. Overall, contract obligations appear to have been generally uninterrupted by the government shutdown. Contract obligations in the core Washington region increased 14.8% from \$14.33 billion in the first quarter of 2018 to \$16.5 billion in the first quarter of 2019. As discussed by the Congressional Budget Office, federal agencies that reduced spending as a result of the shutdown could simply shift the spending to after the federal shutdown was over. While this would imply that perhaps monthly spending in January 2019 would have been diminished and spending in February 2019 heightened, examining monthly data reveals little discernible interruption in spending. In the event of a government shutdown, the largest disruptions stemming from federal spending are likely to result from productivity losses from interrupted business flow. Apart from productivity losses stemming from federal uncertainty, federal spending is unlikely to be notably disrupted.

**Federal Contract Obligations in the Q1 in the Core Washington Region
2014 to July 2019**

Quarter	Contract Obligations (Billions)
2014.Q1	\$14.0
2015.Q1	\$14.7
2016.Q1	\$15.7
2017.Q1	\$14.3
2018.Q1	\$14.3
2019.Q1*	\$16.5

The larger threat to the region’s economy regarding federal spending is in the longer term. The ongoing negotiations appear likely to result in spending growth caps. Given that the Washington region has not diversified meaningfully away from reliance on federal spending, any cap on year-over-year federal spending growth will directly limit the economic growth of the Washington region. Moving forward, all individuals in the region will have to take meaningful steps in diversifying away from the federal government if the region is to enjoy economic growth recorded from the 1990’s through the early 2010’s.

Washington Area Economic Indicators Current and Previous Months

Economic Indicator	Estimates			Percent Change	
	Jul-23 Prelim.	Jun-23 Final	Jul-22 Final	Jun-23 to Jul-23	Jul-22 to Jul-23
Washington Area Business Cycle Indicators					
Coincident Index (2015 = 100)	122.6	122.8	119.5	-0.10%	2.65%
Leading Index (2015 = 100)	102.9	106.0	101.0	-2.92%	1.81%
Washington Area Coincident Index Components					
Total Wage & Salary Employment ('000) ^a	3,375.7	3,392.3	3,333.7	-0.49%	1.26%
Consumer Confidence (South Atlantic) ^a	168.3	158.9	145.7	5.92%	15.51%
Domestic Airport Passengers ('000) ^b	2,332.6	2,330.2	2,196.8	0.10%	6.18%
Nondurable Goods Retail Sales (\$000,000) ^c	4,209.4	4,230.8	4,129.0	-0.50%	1.95%
Washington Area Leading Index Components					
Total Residential Building Permits ^a	1,924.0	2,081.0	2,609.0	-7.54%	-26.26%
Consumer Expectations (South Atlantic) ^a	89.7	90.8	64.9	-1.21%	38.21%
Initial Unemployment Claims ^b	2,306.8	1,434.8	1,829.6	60.77%	26.08%
Durable Goods Retail Sales (\$000,000) ^c	3,854.6	4,024.5	3,700.2	-4.22%	4.17%
Washington Area Labor Force^a					
Total Labor Force ('000)	3,554.3	3,530.8	3,470.1	0.67%	2.43%
Employed Labor Force ('000)	3,468.7	3,442.4	3,360.8	0.77%	3.21%
Unemployed Labor Force ('000)	85.6	88.4	109.3	-3.13%	-21.66%
Unemployment Rate	2.4%	2.5%	3.1%	--	--
Washington Area Wage and Salary Employment^a					
Total ('000)	3,375.7	3,392.3	3,333.7	-0.49%	1.26%
Construction ('000)	170.5	171.4	164.2	-0.53%	3.84%
Manufacturing ('000)	56.6	57.0	57.2	-0.70%	-1.05%
Transportation & Public Utilities ('000)	75.9	76.9	76.3	-1.30%	-0.52%
Wholesale & Retail Trade ('000)	322.9	322.7	327.5	0.06%	-1.40%
Services ('000)	2,034.9	2,033.4	1,996.8	0.07%	1.91%
Total Government ('000)	714.9	730.9	711.7	-2.19%	0.45%
Federal Government ('000)	370.2	369.0	377.9	0.33%	-2.04%

^aUnadjusted data

^bSeasonally adjusted data

^cSeasonally adjusted constant (1996) dollars