



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



Washington Economy Watch

Headwinds Increase as the Region's Economy Stagnates

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The Stephen S. Fuller Institute
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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. Given changes brought from the switch to hybrid and remote work in the wake of the pandemic, both are undergoing alterations. The Coincident Index has been temporarily simplified and the Leading Index has been temporarily discontinued.

Washington Economy Watch

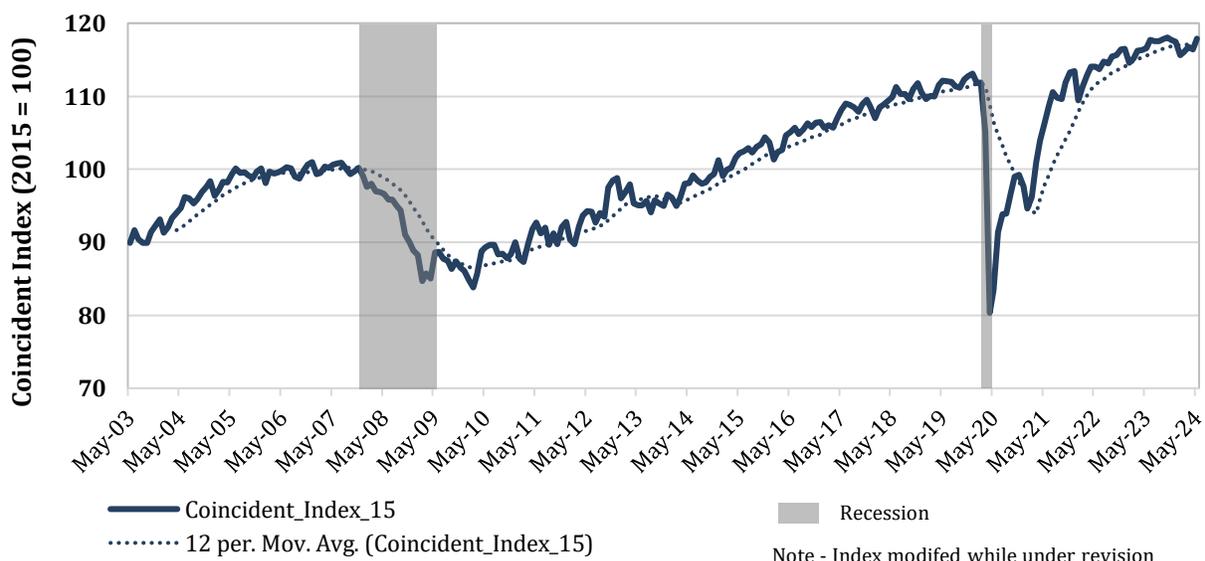
Headwinds Amongst Stagnation

June 2024

Washington Area Economy: Headwinds Increase as the Region's Economy Stagnates

The Coincident Index increased 1.15 from May 2023 to May 2024, an unexpected increase after months of steadily slowing.

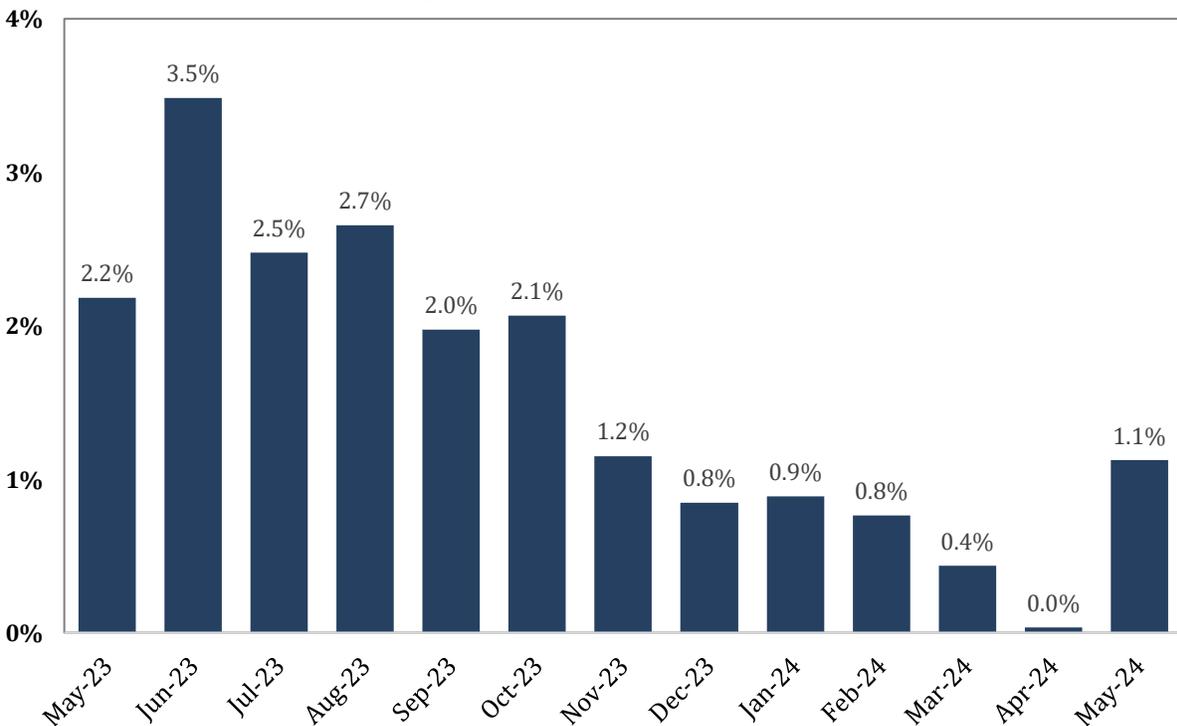
Despite the reacceleration of the Coincident Index, the Washington Region's economy effectively stalled in the spring. Unfortunately, data point to more headwinds than tailwinds in the near-term. While employment in the professional, scientific, and technical sector has stabilized and may return to growth in the coming months, multifamily housing construction has been contracting and office construction has declined precipitously in the wake of the pandemic, the rise of work-from-home, and higher interest rates. The decline in construction activity sparked a contraction in construction employment, whereby the number of payroll jobs has been negative on a month-over-year basis since July 2023. Additionally, if multifamily housing construction continues to contract, the slowing housing growth will continue to constrain labor growth, which in-turn hurts business growth. These forces, in addition to anecdotal evidence that businesses are pausing major investments in the lead up to the federal election, set the stage for the Washington Region's economy to remain flat through the remainder of 2024.



The **Washington Coincident Index**, which represents the current state of the Washington region’s economy, unexpectedly increased month-over-year in May. Overall, the Coincident Index reaccelerated slightly from flat in April to a 1.1% month-over-year increase, the largest increase since November 2023. Overall, the index reaccelerated due to marginal improvements in air travel along with wage and salary employment, but also a notably smaller month-over-year decline in consumer confidence. The reacceleration of employment growth is perhaps the most unexpected given the steadily slowing national employment growth along with the region’s housing shortage. Despite the one-month reacceleration, employment growth remained 0.7 percentage points below the national increase of 1.8% the same month. We anticipate the Coincident Index to slow again this summer.

- *Domestic passenger volume at Reagan National and Dulles Airports* increased 4.4% month-over-year in May, slightly above the revised 3.9% in April; and,
- *Wage and salary employment* in the Washington area increased 1.0% from May 2023 to May 2024, a slight reacceleration over the previous four months; while,
- *Consumer confidence (current circumstances)* decreased 0.6% month-over-year, a notably smaller decline than the 11.7% month-over-year decrease recorded in April.

Washington Coincident Index, Month-Over-Year



Current Performance

The Washington Region's current performance continues to be lackluster. Despite the reacceleration in employment growth, it was only a marginal reacceleration and remained below the national employment growth rate of 1.8% the same month. That is, even when the region outperforms expectations, it is still underperforming the nation.

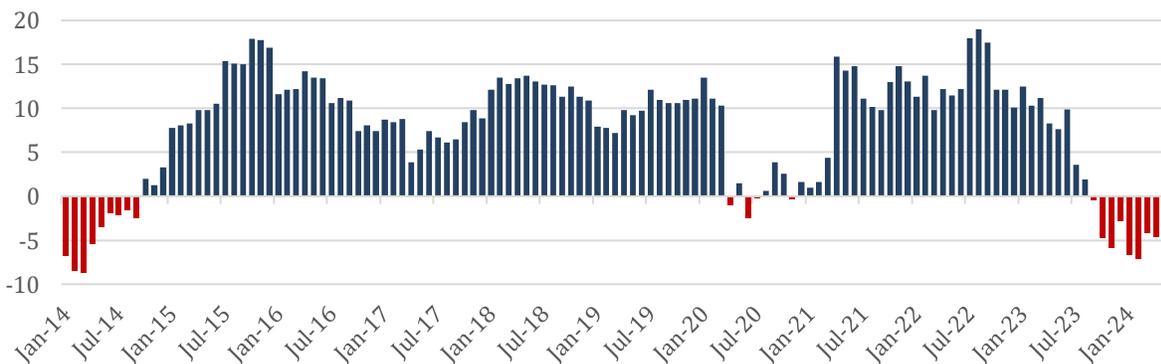
Near Term Outlook

As economic data has continued to provide mixed signals nationally and regionally, the region's near-term economy is softening in the lead up to federal elections. Given the uncertainty around the elections, anecdotal evidence suggests that business leaders are waiting on major investment decisions until after the election. This, combined with growing evidence of a slowly slowing national economy in the face of higher interest rates, suggests continued stagnation for the region. While the data are providing mixed signals, on balance, we are seeing headwinds for the region's economy. This is not to say there are no brightspots.

Tailwinds

One of a few potentially developing tailwinds is employment change in the Professional, Scientific, and Technical subsector, arguably the region's most important subsector. This subsector is comprised of lawyers, architects, engineers, and computer services, and accounts for the bulk of federal contractors. Employment growth in this subsector in the wake of the pandemic was comparable to growth rates in the lead up to the onset of COVID-19. From April 2021 through March 2023, month-over-year employment in the subsector ranged between 9,800 and 19,000 jobs. However, job growth reversed into contraction at the end of 3Q 2023 with month-over-year losses reaching 7,100 jobs in February 2024 and remaining negative through April of this year. By May, the month-over-year losses declined to 400. While it is only one data point, given the importance of the sector the region, if employment in the subsector begins to increase, this will represent a tailwind for the region. Our concern for this sector is amplified by overall trends in federal procurement spending, which continues to rise. Are we losing our traditional competitive advantage for contractor businesses?

**Professional, Scientific, and Technical Employment
Month-Over-Year Change**



Source: BLS. Not Seasonally Adjusted

Headwinds

As has been the case for the past year, there are more headwinds than tailwinds. A newly formed headwind is construction activity. Focusing on multi-family construction, the number of under-construction units in the Washington region has declined on a quarter-over-quarter basis for four consecutive quarters after peaking at 39,735 in the first quarter of 2023. While the 36,282 units under construction in the first quarter of 2024 is above pre-pandemic levels, the region's high housing costs are continuing to impact migration patterns and worker population growth, a persistent headwind. A key concern is that multifamily housing is dominating construction activity, a regional trend in place since the global financial crisis (see SFI regional economic note on permitting [HERE](#)). However, this is limiting housing options for young professionals with growing families and creates a disadvantage in retaining critical experienced workers needed by regional businesses.

**Multi-Family Space Under Construction
(Units)**



Source: CoStar

More dramatically, office construction is at the lowest levels in over thirty years. While well below the region's office boom of the late 1990s, office construction in the Washington Region ranged between 11.0 million square feet and 13.3 million square feet each quarter in the three years immediately prior to the pandemic. Despite the long lag time for the pandemic to fully impact the office market, construction declined precipitately from 9.0 million feet in the first quarter of 2022 to just 3.0 million square feet in the first quarter of 2024, the lowest in over 30 years. Office space under construction space will not increase in the coming quarters as there was an astonishingly low 2,408 square feet of office construction starts in the first quarter of 2024. Furthermore, office construction starts will not increase until office vacancies and valuations fully stabilize.

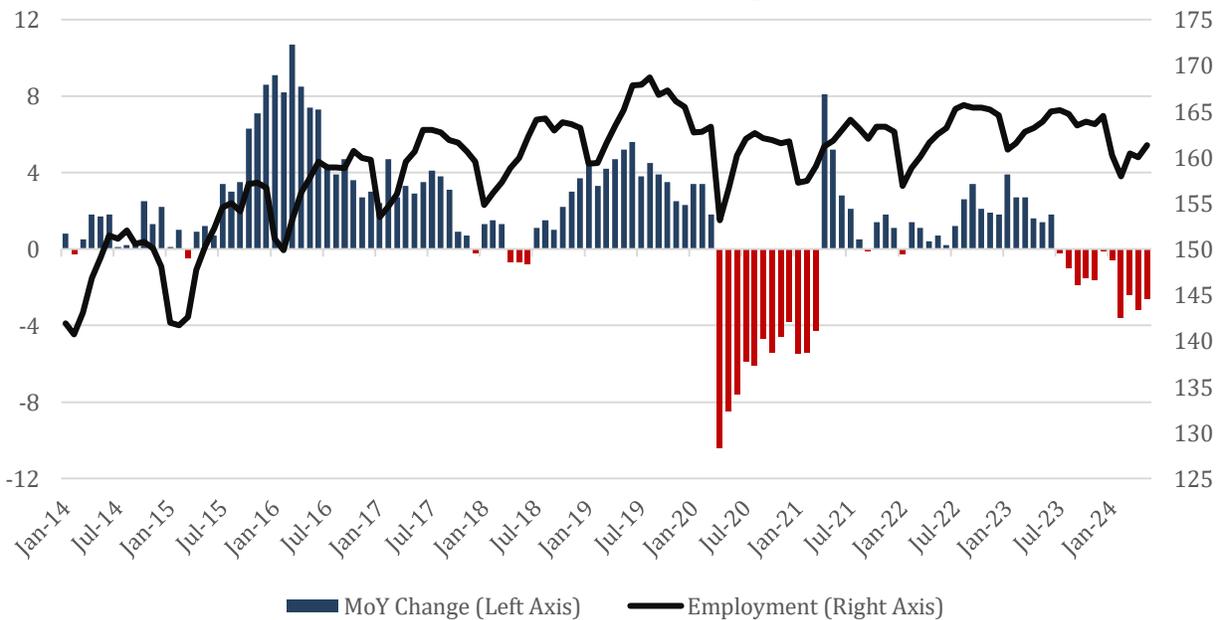
Office Space Under Construction (Millions of Square Feet)



Source: CoStar

The slowdown in both multifamily and office construction has already resulted in a contraction in the region’s construction employment. Construction employment in the Washington Region turned negative on a month-over-year basis in July 2023. After an initial month-over-year declines leveled off at around 1,700 each month through the end of 2023, construction employment losses accelerated in February 2024 to 3,600 and have remained above 2,400 since. The slowdown in multifamily and office starts discussed are likely to lead to continued construction employment losses in the region for the foreseeable future.

Construction Employment Month-Over-Year Change



Source: BLS. Not Seasonally Adjusted

Near-Term Outlook

While Professional, Scientific, and Technical services sector employment has stabilized, and we are hopeful that we will see growth in the second half of 2024, there is little to suggest that economic fair winds and following seas are on the horizon. Multifamily and office construction are contracting, pulling down construction employment. If the multifamily housing sector continues to contract, the region's housing shortage will continue, constraining labor growth, which is already constraining business expansion. These forces, in addition to a pause in business investment decisions in the lead-up to the federal election are all indicating that the Washington region's economy will remain flat through summer and well into the fall of 2024.