

# ECONOMIC FORECAST



## Review of FY 2015

The economy performed close to expectations in FY 2015. The economy continued to improve and underlying fundamentals seemed to support a more robust expansion. Conditions in the housing market and labor market had improved. Total nonagricultural employment grew 2.1 percent. Most sectors finished the year ahead of expectations. The only sector below forecast was professional and business services.

In the official forecast for FY 2015, employment in Virginia was expected to grow at a slightly higher pace than the prior year but still well below rates expected for an expansion. Personal income was forecast to rebound after sluggish growth in FY 2014.

### National economy – Growth continues at a modest pace

Current national indicators suggest the economy continues to expand at a modest pace. Conditions in the housing sector and job market have improved.

Real GDP rose 2.7 percent for the fiscal year, ahead of the forecast of 2.5 percent growth.

Total personal income increased by 4.6 percent, while wages and salaries rose by 4.9 percent. The federal funds target rate has remained unchanged although the Federal Reserve seems to be moving closer to raising the federal funds target rate.

**Consumer spending growth remains weak.** Consumer spending rose by 3.2 percent in FY 2015.

**National employment increased by 2.1 percent in FY 2015.** Total nonagricultural employment grew 2.1 percent, close to the forecast of 1.9 percent. Most sectors finished the year ahead of expectations. The largest variance from the forecast was in the construction sector, which grew 4.8 percent, ahead of the forecast of 4.0 percent growth. The only sector below forecast was professional and business services.

### Virginia's economic performance in FY 2015 remains below trend

Total personal income increased 3.9 percent, 0.2 percentage point ahead of the forecast; net transfer payments, which increased by 8.5 percent, were 4.7 percentage points above the forecast; and proprietor's income, rose 7.2 percent instead of the predicted 4.2 percent. Dividends, interest, and rental income, which made up 20 percent of total personal income in fiscal year 2015, grew 3.7 percent, ahead of the forecast. Supplements to wages and salaries finished 1.2 percentage points behind the forecast. Wages and salaries, which accounted for 51 percent of total personal income in FY 2015, grew 3.0 percent or 0.4 percentage points below the forecast.

Payroll employment growth slightly underperformed expectations in FY 2015. In the official forecast, total nonagricultural employment was projected to increase 0.9 percent, with the average annual employment level rising by 33,800 jobs. Actual job gains were 29,300, an increase of 0.8 percent. Lower-than-expected gains for the leisure and hospitality sector, financial activities, and the professional and business services sector were

offset by higher-than-expected gains in the trade, transportation, and utilities sector and the education and health services sector. Overall, five out of ten major employment sectors met or exceeded the official forecast in FY 2015.

In terms of the number of jobs, the largest variance was concentrated in the leisure and hospitality sector, which was expected to gain 8,200 jobs, however, only gained 1,700 jobs. Professional and business services gained 4,500 jobs; this sector underperformed the forecasted gain of 5,200 jobs. Government added 1,400 jobs (state and local government gains more than offset a decline of 1,800 in federal government), instead of gaining the predicted 1,000 jobs. The table on the following page displays FY 2015 job gains and losses by sector compared with FY 2014.

### **Here is a look at regional employment in Virginia during FY 2015:**

#### ***Northern Virginia***

On a regional basis, employment in Northern Virginia exceeded expectations. While the Richmond-Petersburg area and Hampton Roads underperformed expectations. In Northern Virginia, which represents 37 percent of all jobs in the state, total employment rose by 14,400 jobs, above the predicted amount of 10,900. The professional and business services sector added 2,800 new jobs in FY 2015, up from a loss of 6,900 in FY 2014. Education and health services added 4,900 jobs, up from 1,600 in FY 2014. State and local government added 2,500 jobs, while the federal government lost 1,400 jobs.

#### ***Richmond/Petersburg***

Employment in the Richmond-Petersburg MSA (16 percent of state employment) was below expectations by growing 1.2 percent in FY 2015, behind the forecast of 1.7 percent. The region gained 7,500 jobs in FY 2015, compared with 8,400 in 2014. Construction and state and local government posted employment gains, while leisure and hospitality lost jobs.

#### ***Norfolk/ Virginia Beach/ Newport News***

Employment in the Norfolk-Virginia Beach-Newport News MSA (20 percent of state employment) was below expectations in FY 2015, rising by 0.3 percent compared with the forecast of 1.4 percent growth. The region gained 2,000 jobs in FY 2015, compared with 4,800 in 2014. The professional and business services sector outperformed the forecast, while all other sectors underperformed. Employment in the tourism industry and government, long staples of the area economy, both declined.

#### ***Balance of the state***

Outside of the three major metro areas, the remainder of the state (27 percent of state employment) increased 5,400 jobs in FY 2015, close to the forecasted gain. Financial activities and construction posted employment gains, while trade and leisure and hospitality lost jobs.

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**Modest, but steady growth**

	Actual FY 2015	Forecast FY 2016	Forecast FY 2017	Forecast FY 2018
<b>Real GDP</b>	2.7	2.4	3.1	2.8
<b>Employment*</b>	2.1	1.8	1.5	1.3
<b>Unemployment</b>	5.7	5.1	5.0	5.0
<b>CPI</b>	0.7	0.5	2.3	2.6
	<b>Percent Growth</b>			

\*Total nonagricultural employment. Figures represent percent change over previous year, except the unemployment rate, which is a percentage. Data based on the November 2015 Global Insight standard forecast. Source: Department of Taxation

### U.S. economy expected to continue on a modest growth track

The November forecast anticipates that the U.S. economic recovery is on firmer ground as economic fundamentals show improvement. A continuation of economic growth is expected through at least 2018. This recovery is based on several things occurring: relatively robust domestic demand, a strengthening currency, increasing domestic oil production, which assists in keeping global oil prices in check, and the Federal Reserve implementing its tighter monetary policies smoothly. Highlights of the economic outlook for the next three years include:

- Real Gross Domestic Product is projected to grow by 2.5 percent in FY 2016, 3.1 percent in FY 2017, and 2.8 percent in FY 2018.
- Employment growth is expected to be below two percent over the next three fiscal years.
- Real consumer spending is expected to grow by 3.1 percent in FY 2016 and FY 2017.
- Inflation is expected to grow by 0.5 percent in FY 2016, jump to 2.3 percent in FY 2017 and 2.6 percent in FY 2018.
- The Federal Reserve is expected to slowly increase the federal funds rate, peaking at 3.25 percent by the end of 2018.

### Virginia economy expected to expand at below-trend rates

In the official forecast, economic growth in the Commonwealth was projected to moderately accelerate in FY 2016 relative to FY 2015. The November standard forecast concurs with this outlook and assumes that Virginia will grow slower than the nation in terms of employment and personal income. Federal government spending declined 0.3 percent in CY 2015 as the impact of sequestration phased out. Federal government spending is expected to move to a neutral position throughout the forecast horizon. Here is a look at what economists are predicting for Virginia:

- In the November standard forecast, total personal income is expected to grow somewhat slower in FY 2016, FY 2017 and FY 2018 than in the official forecast. Growth of 3.7 percent is expected in FY 2016, then trails the official forecast by about 1.0 percentage point in FY 2017 and FY 2018. Personal income growth increases to 3.8 percent in FY 2017 and to 4.2 percent by FY 2018. Income from wages and salaries is expected to grow 3.9 percent in FY 2016 and 4.3 percent in FY 2017, 0.3 percentage points above and 0.3 percentage points less than the official forecast, respectively. Growth of dividends, interest, and rental income is expected to increase 5.6 percent in FY 2016, and then taper off to a 4.3 percent increase in FY 2017.
- Total nonagricultural employment is expected to increase 1.5 percent (55,000 jobs) in FY 2016, slightly above the official forecast of 1.4 percent growth. The professional and business services sector and

the construction sector are expected to be the main drivers over the forecast horizon. Overall, employment is expected to increase 1.3 percent in FY 2017, below the official forecast of 1.8 percent.

- Employment in the professional and business services sector is forecast to increase by 2.7 percent in FY 2016.
- Construction employment is expected to grow by 3.0 percent in FY 2016.
- Employment in trade, transportation and utilities is expected to increase by 0.9 percent in FY 2016.