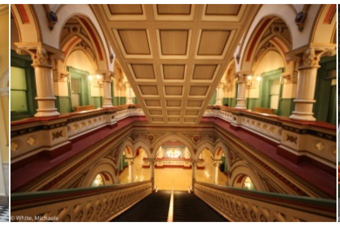
Economic Forecast


Review of FY 2016

The economy performed slightly better than expected in FY 2016. 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 2.4 percent. Only the construction, manufacturing, and information sectors grew at lower than expected rates.

In the official forecast for FY 2016, employment and personal income in Virginia were expected to grow at a faster pace than in FY 2015. Personal income was forecast to grow at a rate similar to FY 2015.

National economy – Growth continues at a modest pace

Current national indicators suggest the economy continues to expand at a modest pace with improvements expected over the second half of calendar year 2016. Conditions in the housing sector and job market have improved.

Real GDP rose 1.7 percent for the fiscal year, lagging the forecast of 2.4 percent growth.

Total personal income rose 3.7 percent in FY 2016, lagging the forecast of 4.2 percent growth. Wages and salaries grew 4.5 percent, 0.5 percentage point ahead of the forecast of 4.0 percent.

The federal funds target rate has remained unchanged although the Fed seems to be moving closer to raising the federal funds target rate with a December 2016 rate increase increasingly likely.

Consumer spending growth remains moderate. Consumer spending rose by 2.7 percent in FY 2016.

National employment increased by 1.9 percent in FY 2016. Total nonagricultural employment grew 1.9 percent, close to the forecast of 1.8 percent. Most sectors finished the year ahead of expectations. The largest variance from the forecast was in the construction sector, which grew 4.1 percent, ahead of the forecast of 2.9 percent growth. The only sectors below forecast were government and information.

Virginia's economic performance in FY 2016 exceeded expectations

Total personal income increased 4.1 percent, 0.4 percentage point ahead of the forecast; net transfer payments, which increased by 6.9 percent, were 3.8 percentage points above the forecast; and proprietor's income, rose 5.7 percent instead of the predicted 3.7 percent. Dividends, interest, and rental income, which made up 20 percent of total personal income in FY 2016, grew 3.6 percent behind the forecast of 5.6 percent. Wages and salaries, which accounted for 52 percent of total personal income in FY 2016, grew 4.7 percent or 0.8 percentage points above the forecast.

Payroll employment growth outperformed expectations in FY 2016. In the official forecast, total nonagricultural employment was projected to increase 1.5 percent, with the average annual employment level rising by 55,000 jobs. Actual job gains were 91,100, an increase of 2.4 percent. Lower-than-expected gains for the manufacturing, construction and mining, and information sectors were offset by higher-than-expected gains in the professional and business services, leisure and hospitality, and education and health sectors. Overall, seven out of ten major employment sectors met or exceeded the official forecast in FY 2016.

Here is a look at regional employment in Virginia during FY 2016:

Northern Virginia

Employment in Northern Virginia was in line with expectations. While the Richmond-Petersburg area exceeded expectations and Hampton Roads underperformed expectations. In Northern Virginia, which represents 37 percent of all jobs in the state, total employment rose by 32,300 jobs, above the 2015 gain of 11,200. The professional and business services sector added 9,900 new jobs in FY 2016, up from the 1,600 gain in FY 2015. Education and health services added 4,800 jobs, up from 3,200 in FY 2015. State and local government added 1,600 jobs, while the federal government gained only 100 jobs.

Richmond/Petersburg

Employment in the Richmond-Petersburg MSA (16 percent of state employment) was above expectations by growing 4.0 percent in FY 2016, well ahead of the 0.6 percent gain in the forecast. The region gained 15,600 jobs in FY 2016, compared with 7,500 in 2015. Construction and professional and business services lead the employment gains, while government 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 2016, rising by 1.1 percent compared with the forecast of 1.6 percent growth. The region gained 8,300 jobs in FY 2016, compared with 2,800 in 2015. Construction, education and health services and leisure and hospitality all posted growth above 4.0 percent, while professional and business services and government were the weakest sectors.

Balance of the state

Outside of the three major metro areas, the remainder of the state (27 percent of state employment) increased 15,700 jobs in FY 2016, exceeding the forecasted gain. Construction and professional and business services lead the employment gains, while government posted the weakest gain.

Moderate Growth Expected			
	Actual FY 2016	Forecast FY 2017	Forecast FY 2018
Real GDP	1.7	1.7	2.3
Employment*	1.9	1.5	0.9
Unemployment	5.0	4.9	4.7
CPI	0.7	1.9	2.5
	Percent Growth		

*Total nonagricultural employment. Figures represent percent change over previous year, except the unemployment rate, which is a percentage. Data based on the November 2016 HIS Markit's standard forecast. Source: Department of Taxation

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

In the October standard forecast, growth is close to the interim forecast. IHS Markit believes solid underlying fundamentals will allow the U.S. economy to continue its modest expansion, with real GDP growth of 1.9 percent in the third quarter of CY 2016 and 2.1 percent in the fourth quarter. Continued growth in employment and gradual acceleration in wage gains should support GDP growth. IHS Markit assigns a 65 percent probability to the standard scenario. Highlights of the economic outlook for the next three years include:

- IHS expects real GDP growth of 1.7 percent in FY 2017, the same as FY 2016, and slower than the interim forecast. It is then expected to pick up to 2.3 percent in FY 2018, and 2.2 percent per year in FY 2019 and FY 2020.
- The outlook for the job market in the October standard forecast is slightly lower than the interim forecast in FY 2017 and FY 2018. Payroll employment is expected to grow 1.5 percent in FY 2017, 0.9 percent in FY 2017, and 0.9 to 1.0 in FY 2019 and FY 2020. The October standard forecast expects the unemployment rate to be similar to that predicted in the interim forecast in the near term, but improves more quickly than the interim, falling to 4.6 percent by 2020, compared with 5.1 percent in the interim.
- Real consumer spending is expected to grow 2.8 percent in FY 2017, matching the interim forecast. Growth falls to 2.2 percent in FY 2018, half a percentage point lower than the interim forecast. In FY 2019 and FY 2020, growth again matches the interim estimate.
- At its September meeting, the Federal Open Market Committee statement said that the case for an increase in the federal funds rate has strengthened. IHS Markit assumes they will raise the federal funds rate by 25 basis points at the December meeting. They expect two rate hikes of 25 basis points each in 2017 and three increases in 2018 and 2019, bringing the funds rate to a long-term equilibrium of 2.75 percent.

Virginia economy expected to mirror national trends

In the interim forecast, economic growth in the Commonwealth was projected to continue to advance, but at a slower rate in FY 2017 relative to FY 2016. The October 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 was virtually flat in CY 2016 and is expected to move to a neutral position through CY 2017, after which it is expected to be a drag on economic activity. Here is a look at what economists are predicting for Virginia:

- In the October standard forecast, total personal income is expected to grow in line with the interim forecast over the forecast horizon. Growth of 3.9 percent is expected in FY 2017. Personal income growth increases to 4.2 percent in FY 2018, 4.9 percent in FY 2019, and to 4.8 percent in FY 2020. Income from wages and salaries is expected to accelerate due to a tightening labor force; in FY 2016 wages and salaries grew 4.7 percent – the largest gain since FY 2007. Wages and salaries are forecast to grow 4.4 percent in FY 2017 and 3.9 percent in FY 2018, followed by close to 5.0 percent growth in FY 2019 and FY 2020. Growth of dividends, interest, and rental income is expected to increase 3.7 percent in FY 2017, and then accelerate to 6.3 percent in FY 2018 and 7.3 percent in FY 2019 before tapering off in FY 2020. Proprietor's income is 0.8 percentage points weaker than the interim forecast for FY 2017. The October standard forecast predicts a 1.3 percent increase in FY 2017, followed by 3.9 percent in FY 2018 and small declines in both FY 2019 and FY 2020. Net transfer payments are expected to increase 4.4 percent in FY 2017, and then increase to 0.5 percent in FY 2018.

- Total nonagricultural employment is expected to increase 1.5 percent (59,600 jobs) in FY 2017, in line with the official forecast. 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 1.0 percent in FY 2018, then to advance 0.9 percent in the two forecast years to follow.