

## ECONOMIC FORECAST



### Review of FY 2018

The economy performed close to expectations in FY 2018. Lower-than-expected gains for information, government, professional and business services, and education and health services were offset by higher-than-expected gains in the construction, manufacturing, trade, transportation, and utilities, and the financial activities sectors. Overall, six out of ten major employment sectors reached or surpassed the official forecast in FY 2018.

In the Virginia official forecast for FY 2018, employment was expected to be similar to FY 2017's rate and personal income in Virginia was expected to outpace growth in FY 2017.

### National economy – Underlying fundamentals support continued growth

At the time of IHS Markit's October 2017 forecast, the economy continued to improve. Although indicators were mixed, partially due to disruptions from hurricanes Harvey and Irma, solid underlying fundamentals suggested the economy would continue its moderate expansion.

Real GDP rose 2.6 percent for the fiscal year, ahead of the forecast of 2.4 percent growth.

Total personal income rose 4.5 percent in FY 2018, one percentage point ahead of the forecast. Wages and salaries grew 4.8 percent, 0.7 percentage point above the forecast of 4.1 percent.

**Consumer spending growth remains moderate.** Real consumer spending rose 2.5 percent in FY 2018, matching the forecast.

**National employment increased by 1.5 percent in FY 2018.** Total nonagricultural employment grew 1.5 percent, slightly ahead of the forecast of 1.4 percent. Most sectors finished the year ahead of expectations. The construction sector grew by 3.5 percent, ahead of the forecast of 2.2 percent growth. The only sector significantly below forecast was professional and business services.

### Virginia's economic performance in FY 2018 was close to expectations

Total personal income increased 4.1 percent, which was 0.8 percentage points above the forecast. Proprietor's income grew 4.6 percent in FY 2018, which was 1.7 percentage points above the forecast; and supplements to wages and salaries finished 2.0 percentage points ahead of the forecast. Net transfer payments, which increased by 5.3 percent, were 1.4 percentage points above the forecast. Wages and salaries, which accounted for 52 percent of total personal income in fiscal year 2018, grew 4.0 percent or 0.4 percentage points above the forecast. Dividends, interest, and rental income, which made up 20 percent of total personal income in FY 2018, grew 4.4 percent, ahead of the forecast.

Payroll employment growth was slightly above expectations in FY 2018. In the official forecast, total nonagricultural employment was projected to increase 1.3 percent, with the average annual employment level rising by 53,000 jobs. Actual job gains were 56,200, an increase of 1.4 percent. Lower-than-expected gains for information, government, professional and business services, and education and health services were offset by higher-than-expected gains in the construction, manufacturing, trade, transportation, and utilities, and the financial activities sectors. Overall, six out of ten major employment sectors reached or surpassed the official forecast in FY 2018.

**Here is a look at regional employment in Virginia during FY 2018:**

***Northern Virginia***

In Northern Virginia, which represents 37 percent of all jobs in the state, total employment rose by 22,100 jobs, below the predicted amount of 31,000. The professional and business services sector added 8,000 new jobs in FY 2018, up from the 7,500 gain in FY 2017. Education and health services added 4,400 jobs, down from 4,700 in FY 2017. State and local government added 2,000 jobs, while the federal government lost 1,200 jobs.

***Richmond/Petersburg***

Employment in the Richmond-Petersburg MSA (17 percent of state employment) was above expectations by growing 1.8 percent in FY 2018, ahead of the forecast of 1.4 percent. The region gained 12,100 jobs in FY 2018, compared with 8,000 in 2017. Employment in trade, transportation, and utilities posted the strongest gains.

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

Employment in the Norfolk-Virginia Beach-Newport News MSA (20 percent of state employment) was above expectations in FY 2018, rising by 1.3 percent compared with the forecast of 0.4 percent growth. The region gained 10,400 jobs in FY 2018, compared with 6,500 in 2017. Most sectors were close to the forecast. Employment in the leisure and hospitality and professional and business services posted the strongest gains, while government continued to decline.

***Balance of the state***

Outside of the three major metro areas, the remainder of the state (26 percent of state employment) increased 11,700 jobs in FY 2018, following a meager gain of 2,400 in FY 2017. Construction, professional and business services, other services, and education and health were the strongest performers, while trade, government, and information sectors lost jobs.

**U.S. economy expected to continue on a solid growth track**

Recent national indicators suggest the economy continues to grow at a solid pace. Real GDP grew at an annualized rate of 3.5 percent in the third quarter of 2018, lower than the 4.2 percent growth in the second quarter.

Job growth remains solid. Payroll employment grew by 250,000 jobs in October. September gains were revised down to 118,000 jobs. In a separate report, the unemployment rate fell to 3.7 percent in September.

Initial claims for unemployment fell by 5,000 to 210,000 in the week ending October 13. The four-week moving average increased by 2,000 to 211,750, a very low level not seen in nearly five decades.

In the October standard forecast, growth is somewhat stronger than the official forecast in FY 2019- FY 2020. IHS Markit believes solid underlying fundamentals will allow the U.S. economy to continue its modest expansion. Aided by fiscal stimulus, supportive financial conditions, strength in employment, income, and wealth, along with elevated consumer and business sentiment, IHS Markit expects GDP growth to remain near a 3 percent average over the second half of this year. They assign a 60 percent probability to the standard scenario. Highlights of the economic outlook for the next two years include:

- IHS expects real GDP growth of 3.0 percent in FY 2019. It is then expected to grow 2.4 percent in FY 2020, then drop to 1.7 then 1.5 percent in FY 2021 - FY 2022.
- The outlook for the job market in the October standard forecast is also stronger than the official forecast in FY 2019 and FY 2020. Payroll employment is expected to grow 1.6 percent in FY 2019 and 1.3 percent in FY 2020. The October standard forecast expects the unemployment rate to be about one-half percentage point below that predicted in the official forecast over the forecast horizon, falling to 3.5 percent in FY 2020, compared with the official 4.3 percent.
- Total personal income is expected to rise by 4.4 percent in FY 2019, close to the official forecast. Income then increases at a slower rate than the official forecast through 2022. The October forecast for the largest component of personal income, wages and salaries, is also lower than the official over the forecast horizon. IHS Markit expects wages and salaries to rise 4.6 percent in FY 2019, 4.8 percent in FY 2020, then 4.6 and 4.4 percent in FY 2021 – FY 2022.
- Real consumer spending is expected to grow 2.9 percent in FY 2019, higher than the official forecast of 2.4 percent. Growth falls each year reaching 2.0 percent in FY 2022.
- Chairman Jerome Powell recently defended the Federal Open Market Committee’s continued strategy of gradually raising the overnight federal funds rate. IHS Markit expects a rate hike in December, the fourth this year, followed by three rate hikes in 2019 and one in 2020, which would bring the upper end of the target range to 3.5 percent.

### **Virginia economy is expected to show continued growth**

In the official forecast, economic growth in the Commonwealth was projected to moderately strengthen in FY 2019 through FY 2022 relative to FY 2018. The October standard forecast has personal income and wage and salary income growing at about a 4.0 to 4.5 percent pace over the forecasted horizon, while employment is forecast to increase 1.7 percent in FY 2019 – faster than the 1.4 percent increase in FY 2018. Federal government spending was virtually flat in calendar year 2017, but is expected to grow 3.6 percent in calendar year 2018 and 4.4 percent in calendar year 2019. Here is a look at what economists are predicting for Virginia:

- Total nonagricultural employment is expected to increase 1.7 percent (68,400 jobs) in FY 2019, above the official forecast of 1.0 percent growth. The professional and business services sector and the education and health services sector are expected to be the main drivers over the forecast horizon. Overall, employment is expected to increase 1.1 percent in FY 2020 and 0.6 percent in FY 2021 as federal government stimulus fades.
- In the October standard forecast, total personal income is expected to grow somewhat faster over most of the forecast horizon than in the official forecast. Growth of 4.1 percent is expected in FY 2019, then growth between 4.5 and 4.8 percent in FY 2020 to FY 2022. Income from wages and salaries is

expected to grow 4.3 percent in FY 2019 and 4.2 percent in FY 2020, 0.2 percentage points above the official forecast. Growth of dividends, interest, and rental income is expected to increase 3.8 percent in FY 2019, and then accelerate to 6.8 percent in FY 2020.

- The outlook for proprietor's income is different from the official forecast: the October standard forecast predicts a 2.5 percent increase in FY 2019 and a decline of 2.5 percent in 2020, as opposed to a decline in both FY 2019 and FY 2020 in the official forecast. Net transfer payments are expected to increase 4.3 percent in FY 2019, and then increase to 9.8 percent and 12.0 percent in FY 2020 and FY 2021, respectively.