

# ECONOMIC FORECAST



## Review of FY 2019

The job market in the Commonwealth underperformed expectations in FY 2019. Lower-than-expected gains for construction, information, trade, financial activities, professional and business services, and leisure and hospitality were offset by higher-than-expected gains in the manufacturing, education and health services, and government sectors. Overall, four out of ten major employment sectors reached or surpassed the official forecast in FY 2019.

Payroll employment growth was below expectations in FY 2019. In the official forecast, total nonagricultural employment was projected to increase 1.7 percent, with the average annual employment level rising by 68,400 jobs. Actual job gains were 47,700, an increase of 1.2 percent.

## National economy – Continued moderate growth path

At the time of IHS Markit's October 2018 forecast, the economy continued to improve. Most indicators pointed to solid underlying fundamentals suggesting 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 5.1 percent in FY 2019, 0.7 percentage point ahead of the forecast. Wages and salaries grew 4.9 percent, 0.3 percentage point above the forecast of 4.6 percent.

**Consumer spending growth remains moderate.** Real consumer spending rose 2.8 percent in FY 2019, close to the forecast of 2.9 percent.

**Total nonagricultural employment grew 1.7 percent, slightly ahead of the forecast of 1.6 percent.** Most sectors finished the year ahead of expectations. The construction sector grew by 4.1 percent, half a percentage point ahead of the forecast. The only sector significantly below forecast was professional and business services which grew 2.5 percent compared with the forecast of 3.2 percent.

## Virginia's economic performance in FY 2019 was close to expectations

Total personal income increased 4.9 percent, which was 0.8 percentage point above the forecast. Proprietor's income grew 4.6 percent in FY 2019, which was 2.1 percentage points above the forecast; and net transfer payments, which increased by 9.9 percent, were 5.6 percentage points above the forecast. Also, supplements to wages and salaries finished 1.2 percentage points ahead of the forecast. Wages and salaries, which accounted for 51 percent of total personal income in fiscal year 2019, grew 4.4 percent or 0.1 percentage point above the forecast. Dividends, interest, and rental income, which made up 21 percent of total personal income in FY 2019, grew 5.4 percent, above the forecasted 3.8 percent pace.

Payroll employment growth was below expectations in FY 2019. In the official forecast, total nonagricultural employment was projected to increase 1.7 percent, with the average annual employment level rising by 68,400 jobs. Actual job gains were 47,700, an increase of 1.2 percent. Lower-than-expected gains for construction, information, trade, financial activities, professional and business services, and leisure and hospitality were offset by higher-than-expected gains in the manufacturing, education and health services, and government sectors. Overall, four out of ten major employment sectors reached or surpassed the official forecast in FY 2019.

### **Here is a look at regional employment in Virginia during FY 2019:**

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

Northern Virginia performed better than expected by 5,300 jobs, while all other regions under-performed the forecast. In Northern Virginia, which represents 37 percent of all jobs in the state, total employment rose by 26,900 jobs, above the predicted amount of 21,200. The professional and business services sector added 11,400 new jobs in FY 2019, up from the 10,000 gain in fiscal year 2018. Education and health services added 4,800 jobs close to the gain in FY 2018. State and local government added 4,800 jobs, while the federal government gained 600 jobs.

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

Employment in the Richmond-Petersburg MSA (17 percent of state employment) was below expectations growing by 1.3 percent in fiscal year 2019, below the forecast of 1.6 percent. The region gained 8,700 jobs in FY 2019, compared with 7,900 in 2018. Employment in construction, financial activities, and local government posted the strongest gains.

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

Employment in the Norfolk-Virginia Beach-Newport News MSA (20 percent of state employment) was below expectations in fiscal year 2019, rising by 0.4 percent compared with the forecast of 2.0 percent growth. The region gained 3,300 jobs in FY 2019, compared with 11,100 in 2018. Most sectors were close to the forecast. However, trade and local government were well below the forecast.

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

Outside of the three major metro areas, the remainder of the state (26 percent of state employment) increased by 8,800 jobs in fiscal year 2019, following a gain of 3,500 in FY 2018. Manufacturing and education and health services posted the strongest gains, while construction, information, financial activities, professional and business services, and local government lost jobs.

### **U.S. economy expected to experience slowing growth**

Recent national indicators suggest the economy continues to grow, albeit at a slower pace. According to the initial estimate, real GDP grew at an annualized rate of 1.9 percent in the third quarter of 2019, down from 2.0 percent in the second quarter.

The labor market expanded in October, with payroll employment growing by 128,000 jobs, above expectations. There were also upward revisions to previous months. In a separate report, the unemployment rate increased from 3.5 to 3.6 percent as more people entered the labor force. Initial claims for

unemployment rose by 5,000 to 218,000 in the week ending October 26, while the four-week moving average slipped by 500 to 214,750. The level of jobless is fluctuating around historically low levels.

In the October standard forecast, GDP growth is somewhat lower than the official forecast in FY 2020, but stronger in FY 2021- FY 2022. IHS Markit believes that slowing global growth, less of a boost to domestic spending from rising stock prices, the effects of recent tariffs, slowing inventory accumulation, and the approach to capacity constraints will be a drag on growth. They assign a 55 percent probability to the standard scenario. Highlights of the economic outlook for the next two years include:

- IHS expects real GDP growth of 1.9 percent in FY 2020, 2.1 percent in 2021, and 1.8 percent FY 2022.
- Similarly, the outlook for the job market in the October standard forecast is also slower than the official forecast in fiscal year 2020, but somewhat stronger in FY 2021 and FY 2022. Payroll employment is expected to grow 1.2 percent in fiscal year 2020, then slow to 0.8 percent in FY 2021, and 0.7 percent in FY 2022. The October standard forecast expects the unemployment rate to be close to the official forecast, 3.6 percent in fiscal year 2020, 3.5 percent in FY 2021, and 3.7 percent in FY 2022.
- Total personal income is expected to rise by 4.5 percent in FY 2020, 0.4 percentage point below the official forecast. Income then decreases at a slower rate than the official forecast through 2022. The October forecast for the largest component of personal income, wages and salaries, is higher than the official over the forecast horizon. IHS Markit expects wages and salaries to rise 5.2 percent in FY 2020, 4.8 percent in fiscal year 2021, and 4.6 percent in FY 2022.
- Real consumer spending is expected to grow 2.8 percent in FY 2020, higher than the official forecast of 2.6 percent. Growth falls to 2.6 percent in FY 2021 and 2.5 percent in FY 2022.
- Despite tight labor markets and inflation rising to slightly above its target, the Fed is focused on downside risks and is expected to cut the fed funds target range once more in December, but IHS expects a 100 basis-point reversal through 2023.

### **Virginia economy is expected to underperform the nation**

In the official forecast, economic growth in the Commonwealth was projected to accelerate FY 2020 relative to FY 2019, then slow in FY 2021 and FY 2022. 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 1.0 percent in fiscal year 2020 – slower than the 1.2 percent increase in fiscal year 2019. Federal government spending is expected to grow 3.2 percent in calendar years 2019 and 2020 before flattening in calendar 2021 and contracting in calendar year 2022. Here is a look at what economists are predicting for Virginia:

- Total nonagricultural employment is expected to increase 1.0 percent (41,900 jobs) in FY 2020, below the official forecast of 1.1 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 0.6 percent in FY 2021 and 0.4 percent in FY 2022 as the national economy slows.
- In the October standard forecast, total personal income is expected to grow close to a half of percentage point below the official forecast over the forecast horizon. Growth of 4.4 percent is expected in FY 2020, then growth between 4.2 and 4.1 percent in FY 2021 to FY 2022. Income from

wages and salaries is expected to grow 4.2 percent in FY 2020 and 4.6 percent in FY 2021, 0.6 percentage point above the official forecast. Growth of dividends, interest, and rental income is expected to increase 4.5 percent in FY 2020, and then accelerate in FY 2021.

- The outlook for proprietor's income in the October standard forecast predicts a 0.5 percent increase in FY 2020 and then declining 1.3 percent in FY 2021. Net transfer payments are expected to increase 6.3 percent in FY 2020, and then increase 4.5 percent and 7.3 percent in FY 2021 and FY 2022, respectively.