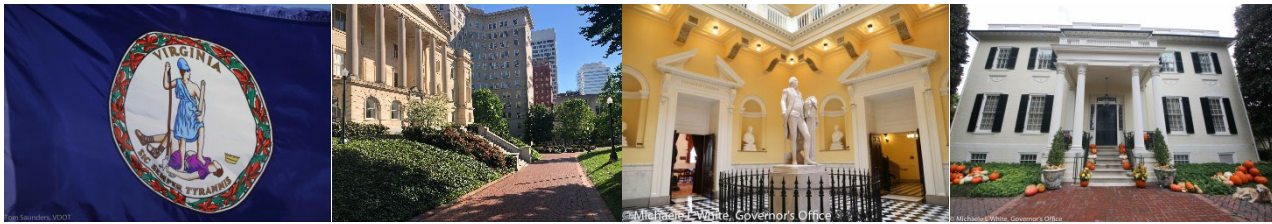


# ECONOMIC FORECAST



## The US Economy

### Review of FY24

The FY24 U.S. economic forecast was based on the continuation of post-pandemic trends leading to a mild recession from the second to fourth quarter of CY24. Namely, inflation expectations remained persistently high with an atypically high federal funds rates slowing economic growth. Consumer and business confidence was anticipated to decline due to a federal government shutdown, escalating military conflicts around the world, and bank failures, resulting in an economic downturn.

After the Fed raised interest rates seven times during FY23, the higher cost of financing and alleviation of global supply chain issues resulted in moderating inflation. Since September 2022, consumer price inflation has slowed by about 20 basis points each month as measured by year over year change in prices (CPI). The June 2024 increase was the smallest in recent years at 2.6 percent and has been steady at 2.7 percent for the past three months. Signaling that it feels inflation is under control, the Fed, eyeing a 3 to 4 percent target interest rate, has cut rates by 75 basis points over its September and November 2024 meetings.

U.S. job growth was stronger than expected in FY24, with total nonfarm employment rising 1.9 percent over the year, although unemployment rose from 3.6 to 4.1 percent. The moderate growth in employment largely came from above-average performance in the healthcare, hospitality, and construction sectors, while jobs in manufacturing and professional/business services grew less than one percent each.

Over the course of the fiscal year, the forecasted recession did not occur with all major industries avoiding net job loss. Labor market and retail spending data showed an economy that continued to be resilient as the Fed's interest rates have eased inflation for the time.

### Baseline US Forecast: Slow Growth

The baseline economic outlook is for slow growth over the next two fiscal years, as the delayed effect of tight monetary policy and the depletion of household savings constrain growth in the near term. U.S. real GDP growth accelerated in 2023 despite high interest rates, but the contractionary effects of Fed rate hikes had yet to fully play out, which is why we saw growth beyond our mild recession forecast last fiscal year. This and other headwinds should cause growth to slow in FY25 and FY26, before rebounding in the next biennium. In terms of annual growth rates, we expect real GDP to grow 1.4 percent in FY25 and 1.7 percent in FY26. In the next biennium, economic growth rebounds to 2.2 and 2.0 percent annually, as the impact of Fed rate cuts begins to stimulate further growth and investment.

## The Virginia Economy

### Review of FY24

With the mild three-quarter recession in the U.S. economy beginning in the fourth quarter of State FY24 not materializing, payroll employment grew steadily in most sectors operating in Virginia during the fiscal year, most notably Education and Health Services (4.6 percent), Construction (2.7 percent), and Leisure and Hospitality (3.0 percent). Relative to the rest of the country, Virginia performed relatively stronger in goods-producing industries, such as Construction and Manufacturing, which grew 1.5 to 2 percentage points more than the national average.

### Baseline Virginia Forecast: Slow Growth

In the Virginia baseline forecast, Virginia employment growth modestly outperforms the U.S. in FY25 growth. Growth slows in FY26 following the national slow-growth scenario. This slower growth is driven by national trends playing out within our state as hiring in key industries slows, consumer spending slows, and political tensions spill over to economic conditions.