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2019 HAMPTON ROADS FORECAST

Despite uncertainty, the Hampton Roads economy will grow faster in 2019

The Hampton Roads MSA (formally the Virginia Beach-Norfolk-Newport News MSA) includes Currituck County NC, Gates County NC, Gloucester County, Isle of Wight County, James City County, Mathews County, York County, Chesapeake, Hampton, Newport News, Norfolk, Poquoson, Portsmouth, Suffolk, Virginia Beach and Williamsburg.

Real Gross Domestic Product (+2.4% in 2019)

The Hampton Roads economy, as measured by Real Gross Domestic Product (GDP), is expected to grow at a slightly higher rate in 2019 (2.4%) than in 2018 (2.2%). Regional growth in 2019 will also be higher than the historical annual average growth rate of 2.0%, observed from 1988 through 2017, but slightly slower than that of the nation.

From 2003 to 2006, real GDP in Hampton Roads grew annually on average by about 4.55%, compared to a 3.39% growth in national GDP. Whereas the inflation-adjusted U.S. GDP increased annually at a compounded rate of 1.42% from 2007 to 2016, Hampton Roads real GDP fell by 0.15%. Primary reasons for our regional economy's poor performance during this period included the Great Recession, the deceleration of Department of Defense (DOD) spending since 2012, and lack of job growth in the private sector. Between 2000 and 2012, nominal DOD spending in the region increased annually at a rate of 5.9%, compounded. However, DOD expenditures from 2012 through 2017 have declined or remained stagnant.

The Hampton Roads' economy remains heavily dependent on DOD spending. From a peak of 46% in 2011, DOD spending now provides approximately 40% of Hampton Roads GDP. With a large military and federal presence, the increase in DOD spending is one of the significant factors in Hampton Roads' economic growth in 2018, 2019, and possibly 2020.

The Bipartisan Budget Agreement of 2018 raised spending caps by $296 billion over Fiscal Years 2018 and 2019, with the defense caps rising by $165 billion and the non-defense caps by $131 billion. National defense spending increased by $80 billion during the FY 2018 and is expected to increase by $85 billion during FY 2019. For Hampton Roads, this is excellent news. Despite the Federal Government's partial shutdown, Congress had appropriated DOD funds for FY 2019. Direct DOD spending in Hampton Roads during 2019 is anticipated to increase 11% from 2017.

Civilian Non-farm Jobs (+0.80% in 2019) and the Unemployment Rate for the Civilian Labor Force (3.10% in 2019)

We forecast that annual civilian jobs in our region will increase by about 6,300 during 2019. Job growth is likely to be concentrated in manufacturing and in firms providing professional and business services, leisure and hospitality, and health care services.

From 2007 to 2010, the recession and its aftermath were responsible for the loss of an estimated 38,400 civilian jobs in Hampton Roads. Latest job data show that it took the regional economy ten years to recover these job losses. Annual civilian jobs in Hampton Roads in 2017 for the first time in ten years exceeded the peak level observed in 2007. The region gained about 6,000 jobs in 2018 and we expect continued steady job growth in 2019.

However, it appears that many of the jobs lost due to the recession were in occupations that paid relatively higher wages. Jobs created or gained since then, on the other hand, frequently have been in relatively lower paying occupations. Thus, the changing mixture of jobs in our region has not been favorable and is a phenomenon that decision-makers should not ignore. The Quarterly Census of Employment and Wage (QCEW) data show that Hampton Roads gained approximately 11,000 jobs during the first quarter of 2018 compared to the first quarter of 2017. However, we also find that average weekly wages from Q1 2017 to Q1 2018 increased by only 1.8% barely keeping up with inflation.

An examination of the annual data on jobs through 2018 show that while we have continued to struggle in creating jobs, large metro areas just south of us in North Carolina have continued to add significant numbers of jobs. Similar to Hampton Roads, many metro areas in the Commonwealth have struggled, while Northern Virginia and Richmond are the few bright spots in the labor market.

Another indicator of labor market performance is the size of the labor force and the number of individuals employed. Local Area Unemployment Statistics (LAUS) data show that from 2008 to 2018 the labor force increased by about 25,000 and the number of individuals employed increased by about 31,000 during the same period. This has resulted in a lower unemployment rate.

Our region's unemployment rate has declined since 2010. We expect the region's unemployment rate to fall from 3.34% in 2018 to 3.10% in 2019. Historically our unemployment rate has been much lower than the national unemployment rate. However, the gap between the unemployment rate in the US and in Hampton Roads has steadily narrowed.

Retail Sales (Taxable Sales, +3.30% in 2019)

Taxable sales include all retail sales except new automobile and gasoline sales. Compared to their pre-recession peak in 2007, retail sales in Hampton Roads were 8.6% lower in 2009 and continued to decline slightly, -0.2 percent, during 2010.

However, retail sales began to recover slowly in 2011 and in 2014, retail sales were 2.0% higher than the 2007 peak level. It took seven years to recover the losses in retail sales from the trough of the Great Recession. Retail sales since 2014 have been steadily increasing. Sales increased by 2.8 percent in 2017 and by 3.4 percent in 2018.

We expect retail sales in the region to grow by another 3.3 percent in 2018. Growth in regional economic activity, increased defense spending, rising incomes, consumer confidence, and the increase in wealth of households are all expected to result in a higher growth in taxable sales.

Tourism (Hotel Room Revenue, +3.80% in 2019)

The hotel industry's nominal revenue increased by 4.7% in 2018 after increasing by 4.7% in 2017. Factors contributing to higher hotel revenue during 2018 were: moderate increases in federal travel; higher per diem rates, relatively low gasoline prices; growth in the national economy, particularly in the main tourist market areas of Hampton Roads; and, a continued slowdown in the additional supply of hotel rooms. However, in real, price adjusted, terms despite substantial increases in hotel revenue since 2013, real revenue at the end of 2018 was only 2.6% above its peak observed in 2007.

The Norfolk/Portsmouth market continues to be the sub-market exhibiting the largest growth in Revenue or Revenue per Available Room (RevPAR) during 2017 and 2018 followed closely by the Hampton/Newport News market. The primary reason for growth in the Norfolk/Portsmouth market has been the opening of the MAIN hotel in Norfolk in 2017. RevPAR in Norfolk/Portsmouth during 2018 increased by 7.5% and by 9.1% in 2017.

Factors contributing to higher tourism revenue during 2019 will continue to be the same as those observed during 2018. We expect to see moderate increases in federal travel; slightly higher per diem rates; growth in the national economy, particularly in the main tourist market areas of Hampton Roads; and, a continued slowdown in growth of additional hotel rooms in Hampton Roads.

A challenge to the hotel industry in the coming years will be increased competition from short term online rental companies like AIRBNB, Flip Key, VRBO and the like. Evidence suggests that

AIRBNB, the largest of the online short term rental companies, has seen a phenomenal growth in Hampton Roads in the last few years. AIRBNB's monthly revenue steadily increased from $0.42 million in July 2015 to $7.32 million in July 2018. Seen differently, AIRBNB revenue in July 2015 represented only 0.36% of hotel revenue in Hampton Roads; it increased to 5.9% in July 2018.

Port: General Cargo Tonnage, (+2.00% in 2019); TEUs, (+3.60% in 2019)

Economic activity connected to the Port of Virginia long has been an important contributor to the region's economic well-being. The Great Recession adversely impacted the Port and the cargo flowing through the Port---whether measured by general tonnage or by twenty-foot equivalent container units (TEUs). In 2009, general cargo tonnage and TEUs were 16.4% and 18.0% below their peak levels respectively. The volume of general cargo and TEUs flowing through the Port increased every year, 2009 through 2016. Nevertheless, it took the Port almost six years to recover losses incurred during the recession; volumes finally exceeded pre-recession peak levels in 2013. General cargo tonnage and TEUs continued to increase in 2017---by 5.3% and 7.0%, respectively. However, there was no significant growth in either tonnage or TEUs in 2018; cargo tonnage at the port was basically flat and TEUs increased by only 0.5%.

One of the reasons for slow cargo growth in 2018 can be attributed to construction activities at both VIG and NIT. The Port was attempting to manage its growth while maintaining its service levels with an emphasis on safety. In addition, completion of the elevated Bayonne Bridge in 2017 resulted in increased volume of cargo going to the port of New York/New Jersey. Port of Virginia also lost one first-in service and two last-out services. Consequently the Port saw its share of loaded TEU containers drop from 17.6% in 2017 to 16.8% in 2018.

In 2016, the Port, supported by the Governor and General Assembly, announced two large expansion projects providing momentum for continued growth and progress---Norfolk International Terminal (NIT) South Optimization and Virginia International Gateway (VIG) II. By 2020, the Port will have the capacity to process 1 million additional container units, a 40% increase overall. The two projects represent a combined investment of $695 million: $350 million investment from the Commonwealth, $25 million from Virginia Port Authority for NIT South modernization and $320 million of private investment for VIG II. In February 2016, the Port executed a 40-year lease with the City of Richmond for the operating rights at Richmond Marine Terminal allowing the Port to improve service further diversifying the port's offerings. In April 2018, the Governor and General Assembly approved a financing package to deepen and widen the harbor and its shipping channels.

Housing (Value of Single Family Housing Permits (+2.00% in 2019)

The residential construction industry in Hampton Roads is expected to grow moderately in 2019. Sales volume of newly constructed homes has generally been increasing each year since 2010. The relatively small inventory of existing homes in the market, low mortgage rates relative to historical levels, and continued moderate prices should help stimulate the growth in new construction homes.

The market for existing residential homes in Hampton Roads has also been steadily improving since 2011. Measures of supply and demand indicate that it would take approximately 3.4 months to clear the existing inventory based on the current absorption rate. This is much lower than Hampton Roads' historic average of 5.5 months. Even so, we continue to be concerned with the volume of distressed (short sales and bank-owned) homes in the local residential market. Distressed homes, whether measured in distressed sales as a proportion of all existing homes sold, or in listings as a proportion of existing homes currently on the market, continue to represent a significant proportion (nearly a tenth) of residential market activity. The problem is that bank-owned homes, for example, often sell at prices barely more than one-half of non-distressed properties.

Mortgage interest rates are expected to remain at relatively low historic levels and household income in our region is recovering. However, recent changes in the tax code providing fewer benefits for homeownership and a persistent and large proportion of distressed market activity likely indicate only a modest increase in the sales prices of homes in Hampton Roads in 2019.

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The Dragas Center for Economic Analysis and Policy in the Strome College of Business at Old Dominion University undertakes a wide range of economic, demographic, transportation and defense-oriented studies. For eighteen years, the Center and its predecessors have produced the highly regarded State of the Region Report for Hampton Roads and economic forecasts for the region. If you would like more information about this topic, please contact Dr. Vinod Agarwal at 757 683 3526 or email at vagarwal@odu.edu.