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Regional Retail Sales Lag the Nation, Remain Volatile

By James Clary, Senior Economist

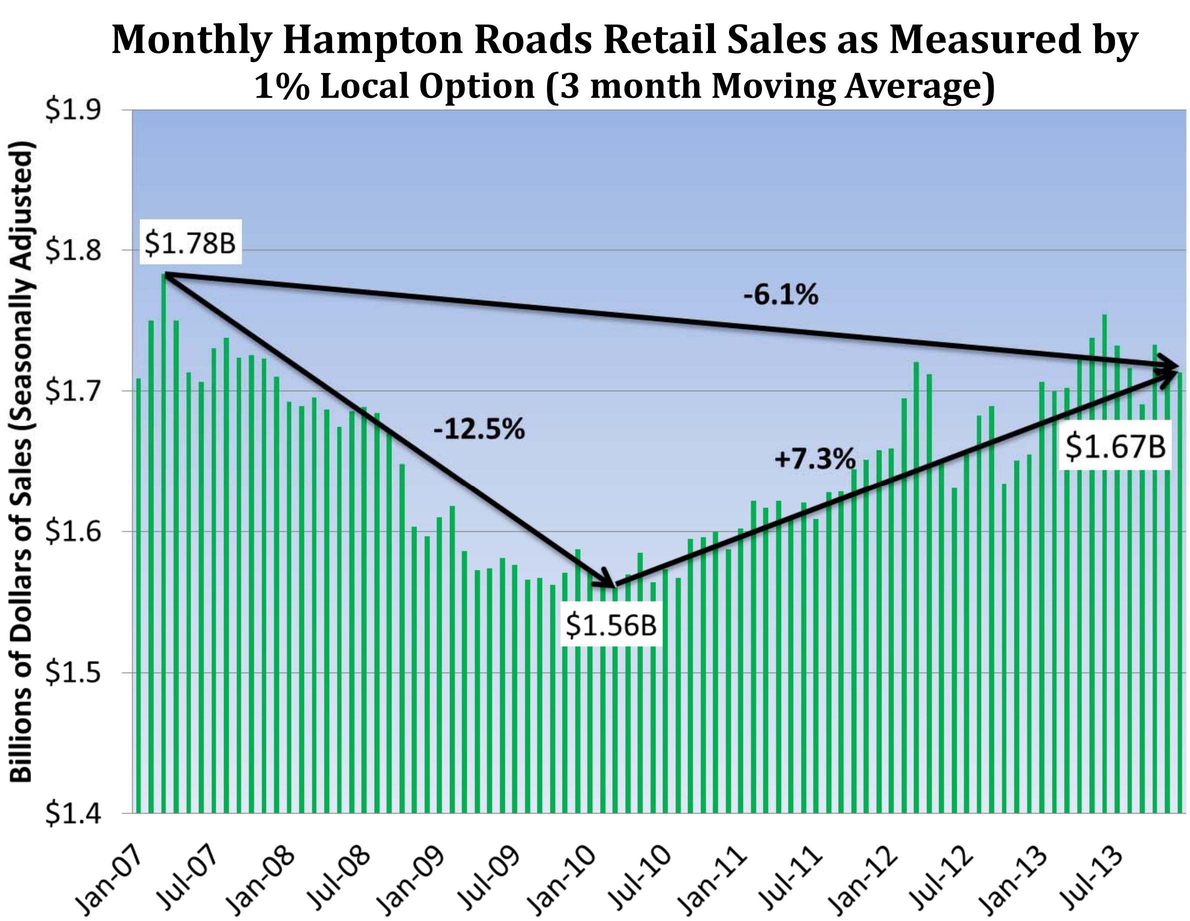
Trade is the backbone of an integrated regional economy because the exchange of goods and services is a primary driver in creating value and providing benefit to market participants. One of the best readily available ways to measure trade is through retail sales. When Hampton Roads' economy grows, retail sales grow even more quickly as increased income is quickly passed through to consumption of goods and services. Conversely, during the most recent recession retail sales shrunk considerably as individuals had to cut back on their purchases.

Billions of Hampton Roads Retail Sales (Measured by the 1% Local Option)

Year	4th Quarter	Annual
2007	$5.4	$20.7
2008	$5.0	$19.9
2009	$5.0	$19.0
2010	$5.0	$18.9
2011	$5.1	$19.6
2012	$5.1	$20.1
2013	$5.3	$20.6

Source: Virginia Department of Taxation, HRPDC

Hampton Roads' seasonally adjusted retail sales increased to $1.67 billion for December 2013, a slight increase over the $1.66 billion in sales during November 2013. When coupled with a very strong October, Hampton Roads' 4th quarter sales totaled $5.30B, a 3.06% increase over the 4th quarter of 2012.



Source: Virginia Department of Taxation, HRPDC

About this Document

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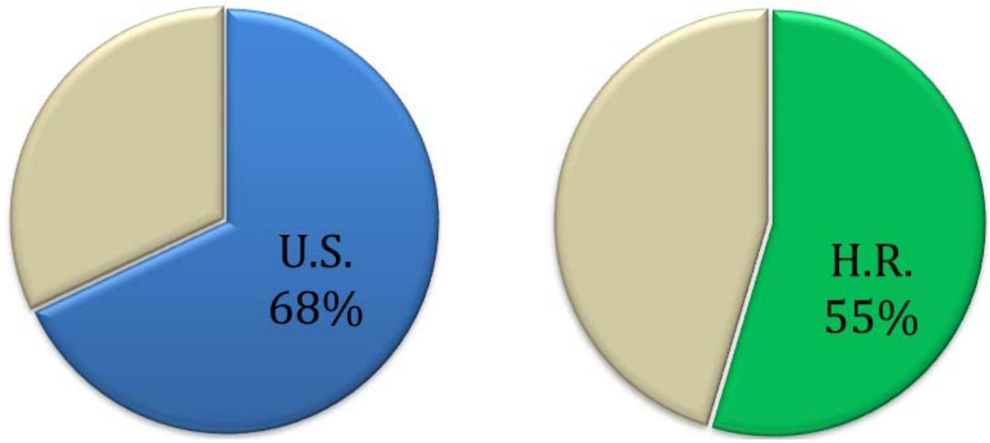
Regional sales still lag 2007, the last prerecession period, with fourth quarter sales down 1.0% and annual sales down 0.75% from the 2007 levels.

Personal Consumption Expenditures as a Share of Gross Product in 2013, U.S. and Hampton Roads



Source: Bureau of Economic Analysis, HRPDC

Even adjusting for seasonal variances, monthly retail sales exhibit a tremendous amount of variation. This makes it difficult to judge the performance of the regional economy using data from a single month. March 2007 realized the highest retail sales level, with $1.78 billion in seasonally adjusted sales. During the recession retail sales tumbled by $220 million, a 12.5% decline. Retail sales have gradually increased since January 2010, but the growth has been very volatile and has included some very strong and some very weak months.

Retail Sales Impact on the Economy

First, growth in personal consumption expenditures, particularly retail sales, typically drives economies out of recessions. Thus economists watch retail sales closely to judge where the economic turning points are occurring.

Second, personal consumption forms an extremely large portion of the national and regional economy. In 2013, personal consumption expenditures was 68% of all economic activity in the nation. Regionally it drives less of the economy because of the influence of defense spending; however, the HRPDC analysis indicates that it still constituted a majority of regional economic activity at 55%.

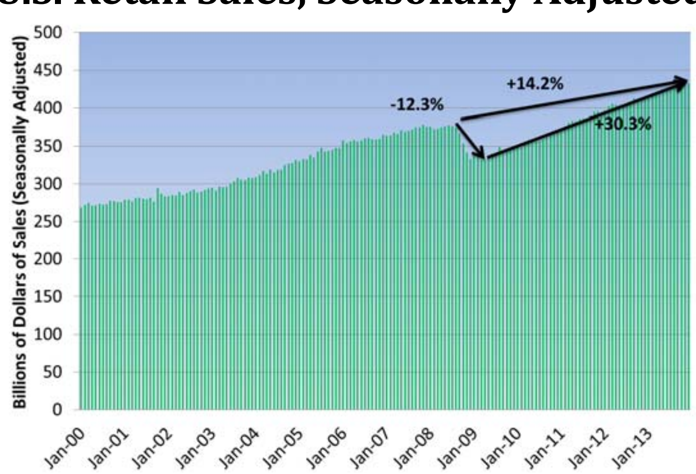
Comparing Hampton Roads and U.S. Retail Sales

Comparing regional and national retail sales gives perspective on how trends affecting Hampton Roads retail compare to those affecting the national experience. The two charts below show the difference between national and regional retail sales. Compared to the region's decline in retail sales since the beginning of the recession, U.S. retail sales grew 14.2% from its prerecession peak, and did not decline to the same extent during the recession. The indexed retail

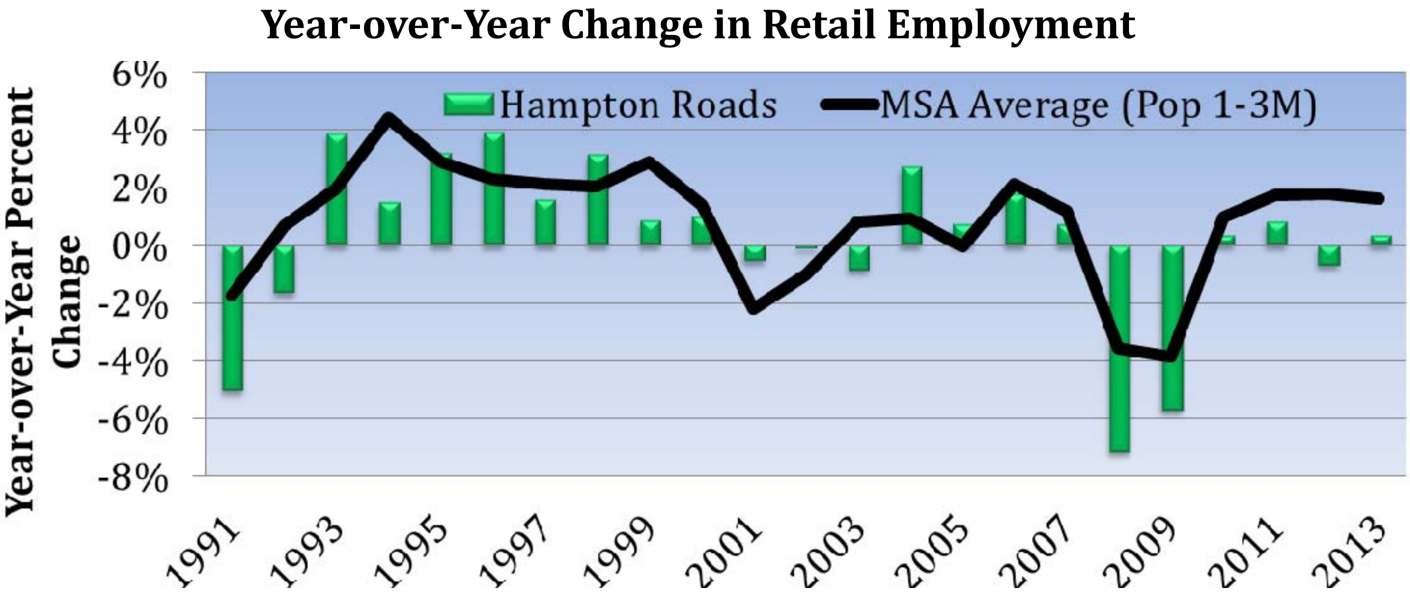
Index Retail Sales, H.R. vs. U.S.

Source: U.S. Census Bureau, Virginia Department of Taxation, HRPDC

U.S. Retail Sales, Seasonally Adjusted



Source: Virginia Department of Taxation, HRPDC



Source: Bureau of Labor Statistics, HRPDC

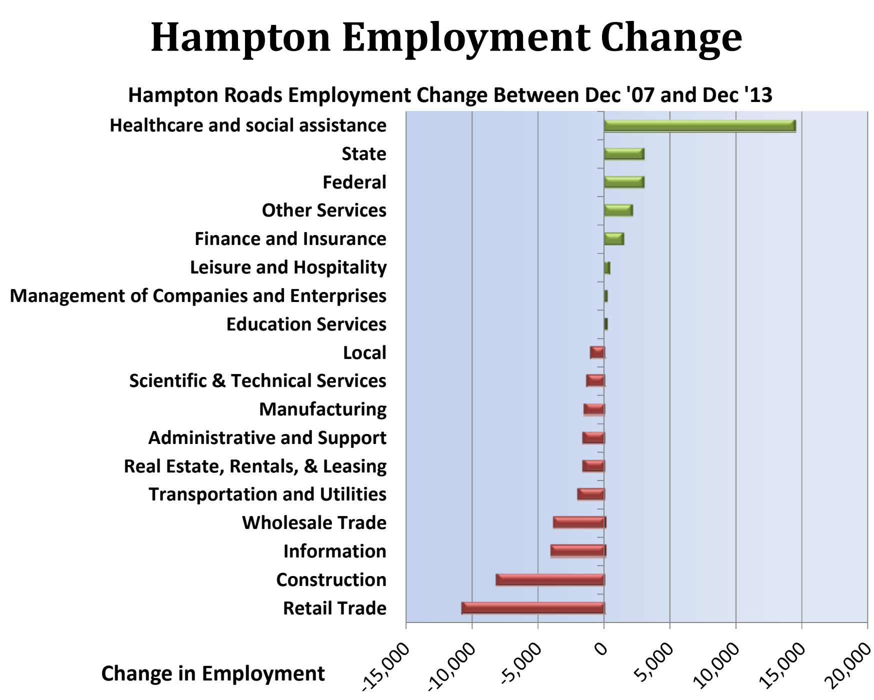
sales chart shows that while Hampton Roads' retail sales remained at a comparable level throughout the 90's, they began to lose pace with the nation in 2008 when the nation began to experience a retail recovery while Hampton Roads lagged until the beginning of 2010.

Unfortunately, there are significant issues with comparing the two data series. The Hampton Roads retail sales data is derived from Virginia taxable sales numbers, while the U.S. data comes from a survey conducted by the U.S. Census Bureau. While actual data typically proves superior to survey data, there is a significant volume of sales that are not taxed, and thus are not measured by the Virginia Department of Taxation. Items that are taxed through a separate mechanism in Virginia, including gasoline sales and motor vehicle sales, are not included in the Hampton Roads estimate. Also, a significant number of transactions are conducted in an untaxed environment, including those during Virginia sales tax holidays (back to school, hurricane preparedness, etc.), and purchases at military exchanges. Lastly, there are whole categories of sales that are untaxed in Virginia, including many services and most online sales.

Despite these limitations, the comparison between regional and national retail sales does indicate that the retail sales in Hampton Roads continues to lag.

Retail Employment

Retail employment is another important measure of the role of retail sales in the regional economy. In December 2013, retail employment formed 11.4% of the region's civilian workforce. There are 34 Metropolitan Statistical Areas (MSAs) with populations between 1 and 3 Million, and Hampton Roads tends to have average retail employment density for this size of region (retail density is retail's percentage of total employment). Typically, the region's retail employment growth tracks that of comparable MSAs, but during this recession



Source: Bureau of Labor Statistics, HRPDC

Hampton Roads suffered a greater decline in retail employment followed by a slower recovery than experienced by its reference MSAs.

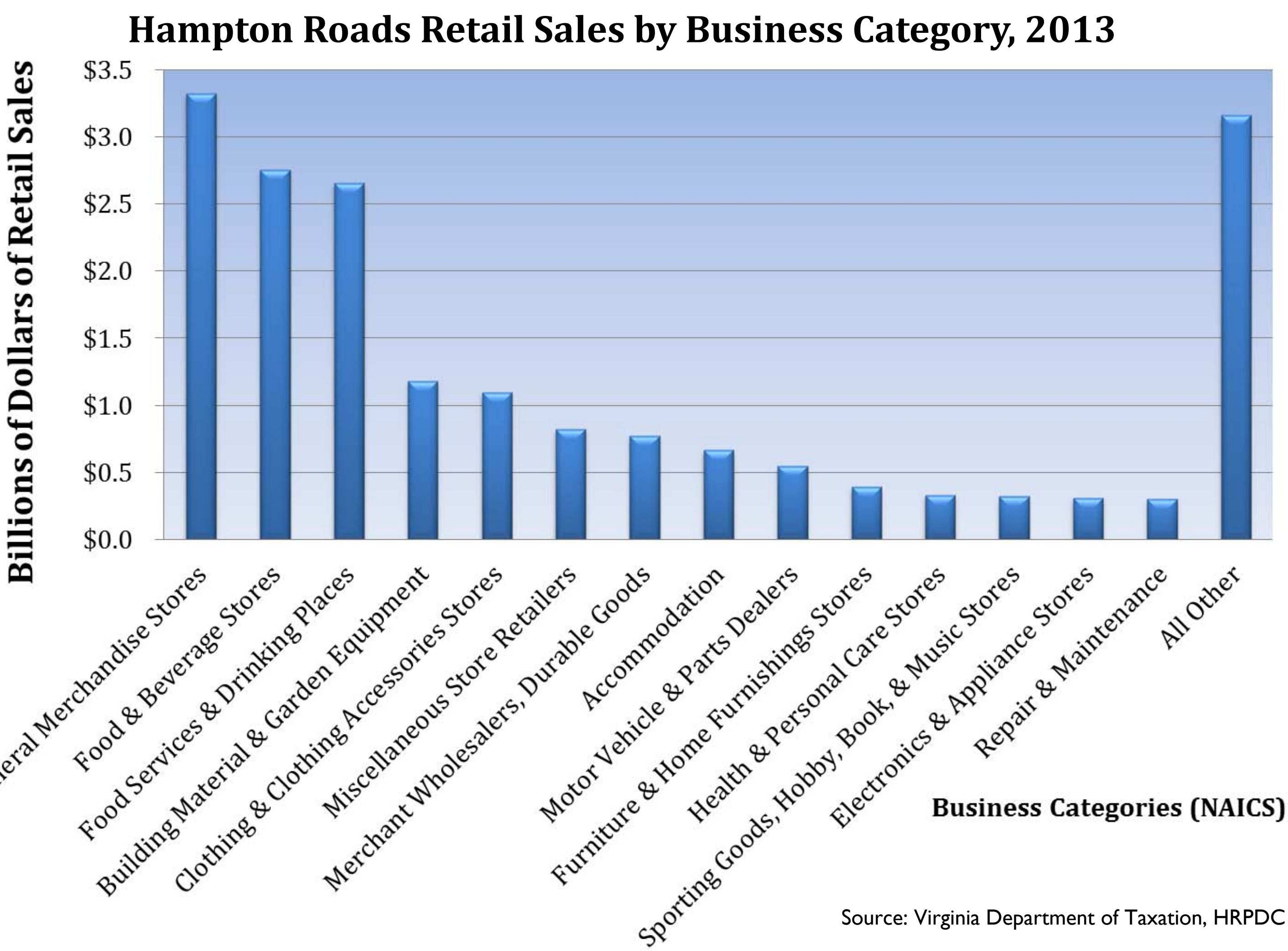
Hampton Roads' retail employment has even lagged construction employment's performance since the onset of the great recession (construction lost more employment, but has recovered to a greater extent). While retail employment grew 1,100 between December 2012 and December 2013, it would take an additional 10 years of growth at this pace to return to its previous peak.

The good news is that retail employment is very cyclical, and as the regional and national economy continues to expand in 2014, retail employment should expand more quickly than employment in other sectors.

Retail sales by Business Category

Within Hampton Roads retail sales, there are a variety of different businesses that help create this region's diverse marketplace. General merchandise stores, a group that includes department stores as well as retailers like Walmart and Target, contributed $3.3B in retail sales in 2013 (17.8% of total sales). Other major contributors were food & beverage stores ($2.8B, 14,8%) and food services & drinking places ($2.6B, 14.3%). The chart below shows a list of the 14 business categories with the largest retail sales in Hampton Roads; in all there were 69 separate business categories with retail sales in the region.

As one examines the changes within retail categories over time, it becomes apparent that different categories of retailers have had very different experiences since the onset of the great recession, as consumer spending habits have adjust-



Source: Virginia Department of Taxation, HRPDC

ed to the recession, as well as structural changes to the regional economy that have manifested themselves over the past six years.

The decline of the construction industry following the housing correction provides one of the clearest examples of a structural trend impacting retail. Lower levels of home building led quickly to a decline in sales of building materials as well as the sales of home furnishings (which are often tied to home purchases). While both of these home construction related businesses have declined since 2007, building material sales have begun to recover with construction employment, and it would be reasonable to expect home furnishing sales to begin following quickly.

Retail Sales for Construction Related Business Categories and Construction Employment in Hampton Roads

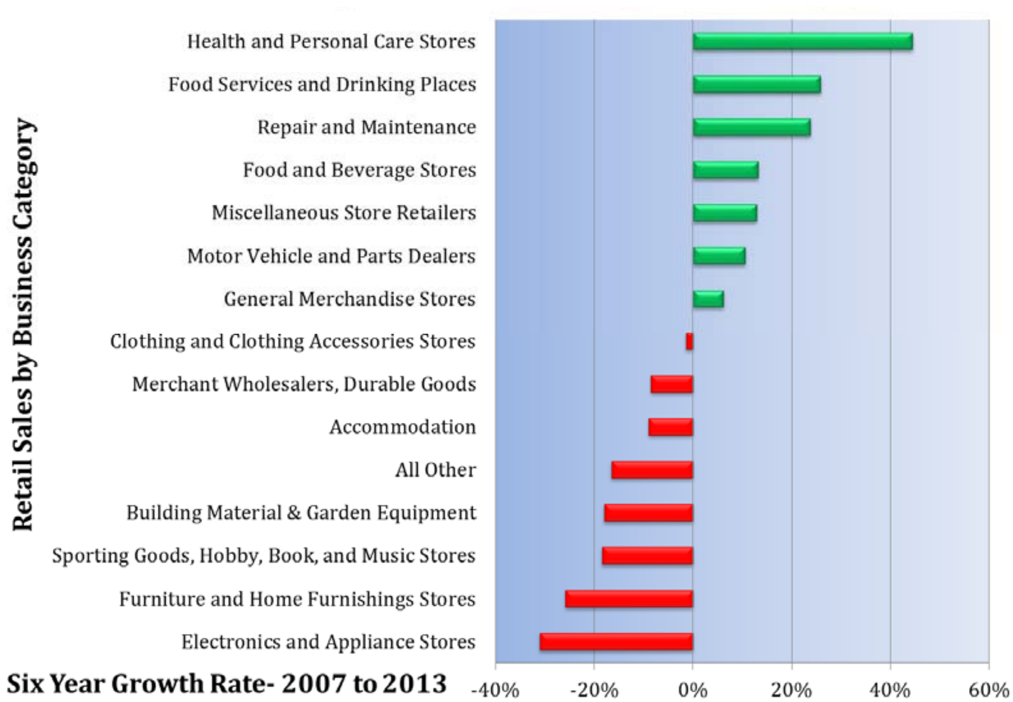
Source: Virginia Department of Taxation, Bureau of Labor Statistics, HRPDC

Another interesting trend that has developed has been the decline in some discretionary purchases in Hampton Roads, as seen in sporting goods, hobby, books, & music class of retailers as well as with retailers of electronics & appliances. This results from both consumers cutting back on these categories of purchases during a period of economic uncertainty, as well as additional competition from both internet sales and entertainment in digital forms.

Food service & drinking places have defied economist's expectations by growing during a weak business cycle. Typically, as a discretionary item, spending would decline during periods of economic uncertainty; however, food service & drinking place sales have grown over the past six years. Additionally, this growth occurred at both the national (+24.2%) and the regional levels. It is also noteworthy that the number of establishments in this category has increased to 3,584 in Hampton Roads, an increase of 5% from 2007. The total number of retail establishments declined by 7% during the same time frame. Additionally, the retail sales per establishment increased by 19% in this category over that time period, compared to an increase of just 7% per establishment for all retail establishments in Hampton Roads.

Lastly, the gains in sales at both motor vehicles & parts dealers (which does not include auto sales) and repair & maintenance indicates that companies as well as individuals are trying to extend the life of large purchases. While this is natural, large purchases should recover in the region as equipment and automobiles reach the point where they require replacement.

Growth in Hampton Roads Retail Sales by Business Category



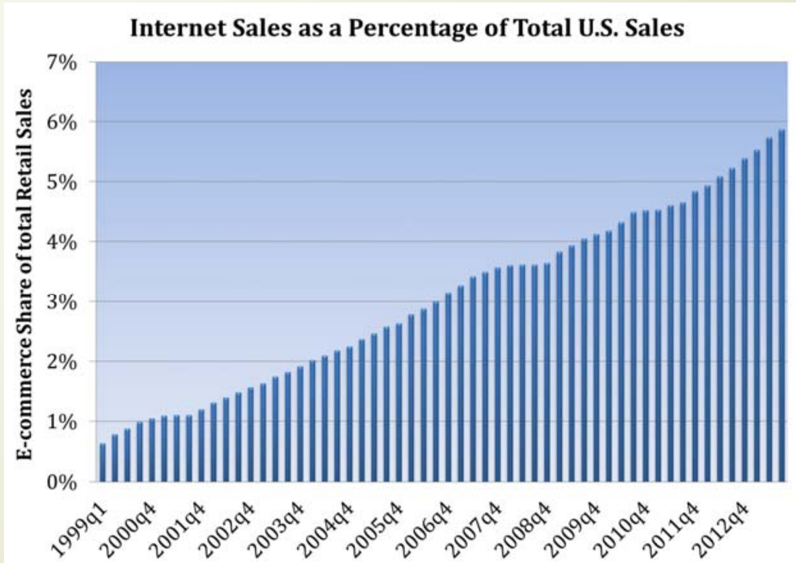
Source: Virginia Department of Taxation, HRPDC

Internet Sales

The U.S. Census Bureau's survey system allows it to track the growth in Internet sales nationally. This allows for some analysis of the regional impact of Internet sales. As Internet sales are not included in local retail sales, the 2.3 percentage point increase in Internet sales only offsets a portion of the 12.5% decline in regional sales, indicating that the substitution of Internet sales is not alone in driving the decline of regional sales. Additionally, Internet sales flat-lined during the recession, which suggests that either typical Internet sales fall in categories of goods that individuals cut back on during the recession (discretionary items), or that the growth of Internet shopping is not predominately driven by value shoppers, but rather by changes in the way that people shop.

While there are exceptions, typically the following transactions remain unaffected by internet sales.

- Services. While there are some services that are being provided over the internet, especially some professional services, typically services are delivered in person.
- Food and Dining.
- Automobiles. While individuals shop for cars online, the legal and tax structure requires a dealership for the transaction.
- Gasoline.



Source: U.S. Census Bureau, HRPDC

HRPDC 2014 Regional Economic Forecast

	2013 (Year to Date)	2014 Forecast
U.S.		
Real GDP	1.7%	2.6%
Interest Rates		
Short Government Rates	0.1%	0.2%
Long Government Rates	2.4%	3.1%
Hampton Roads		
Gross Product	NA	1.9%
Civilian Employment	1.4%	1.9%
Unemployment Rate	5.8%	5.4%
Retail Sales	2.9%	3.4%
Auto and Truck Sales	4.9%	3.9%
Value of Single-Family Residential Building Permits	18.9%	8.4%

Hampton Roads Economic Outlook:

Economic Forecast

By Greg Grootendorst, Chief Economist & James Clary, Senior Economist

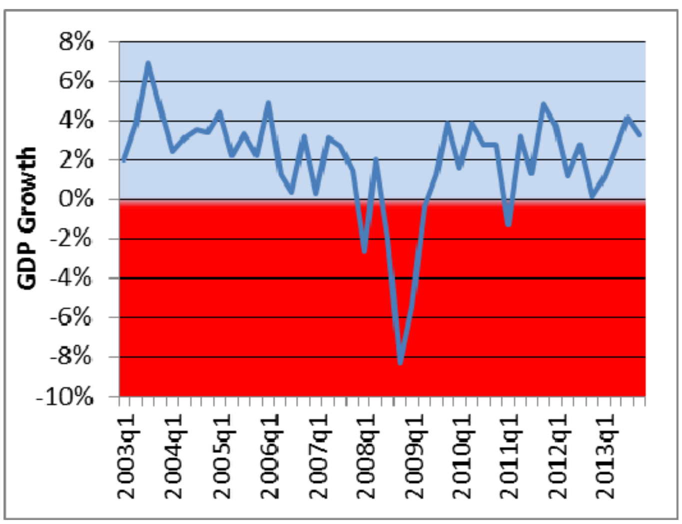
After some tough years, the economy is slowly starting to improve. Over the past three years, the region has managed to recapture many of the jobs lost during the recession and is now only 20,000 jobs below peak employment. The housing market has turned the corner, housing values are now slowly beginning to increase, and building permit and construction activity are on the rise. The heavy burden of uncertainty brought about by the Sequester and budget crisis has begun to dissipate, as Congress works to resolve budget issues and provide clarity on federal expenditures.

For 2014, the HRPDC Economists expect to see the region's economy grow at a rate of 1.9%. Expected gains in the Retail and Construction industries will assist in adding roughly 14,500 jobs to civilian employment in Hampton Roads. The unemployment rate is likely to continue its slow decline, while increased budget certainty will help propel retail sales. Building permit activity and motor vehicle sales are expected to continue to experience strong growth in the coming year.

Hampton Roads Economic Indicators

GDP, Annualized Growth Rate

United States, 2003Q1 – 2013Q4, Quarterly

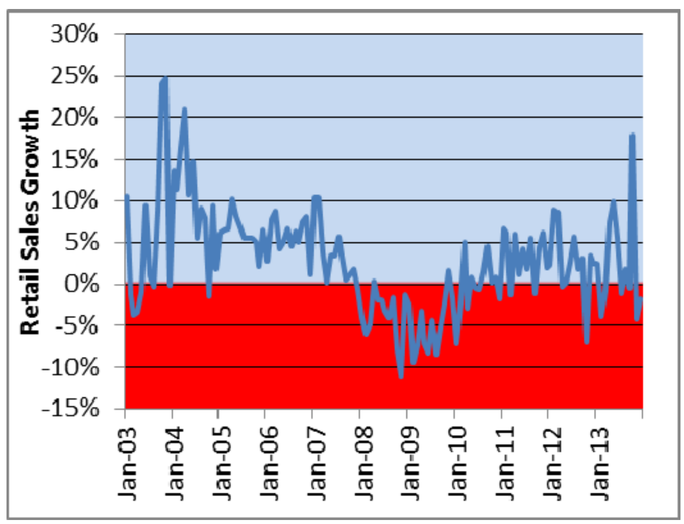


Source: Bureau of Economic Analysis, HRPDC

GDP: Gross Domestic Product combines consumption, investment, net exports, and government spending to determine the size and general health of the economy. U.S. gross product grew at 3.2% in the fourth quarter of 2013, resulting in an annual GDP growth in 2013 of 2.74%. Additionally, the last two quarters were the strongest of the year, leading to the hope that the nation will experience consistent growth in 2014. Blue Chip Forecasts indicates that U.S. GDP growth should continue this year at a rate of 2.7%.

Retail Sales, Year over Year Growth

Hampton Roads, Jan 2003 – Dec 2013, Monthly

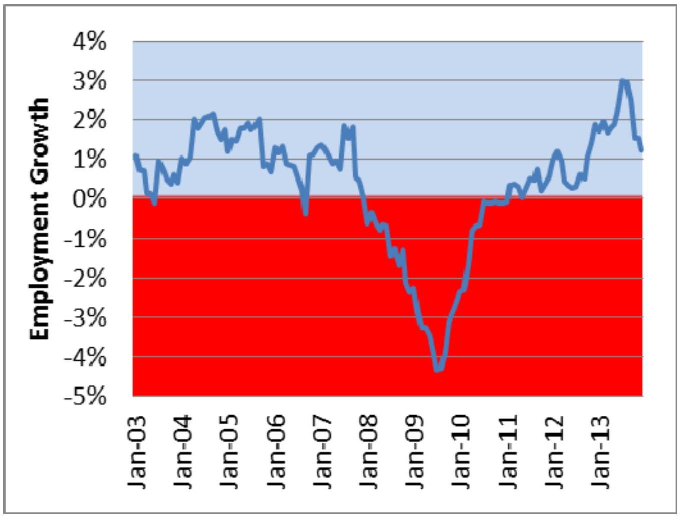


Source: Virginia Department of Taxation, HRPDC

Retail Sales: Hampton Roads' retail sales, as measured by the 1% local option sales tax, serve as an indicator for consumption in the region. Since consumption composes 68% of economic activity in the U.S., the growth or decline of retail sales gives a strong indication of the direction of the local economy. Retail sales decreased 1.7% between December 2012 and December 2013 On a seasonally adjusted basis December spending was slightly above the levels in November (+0.65%).

Employment, Year over Year Growth

Hampton Roads, Jan 2003 – Dec 2013, Monthly

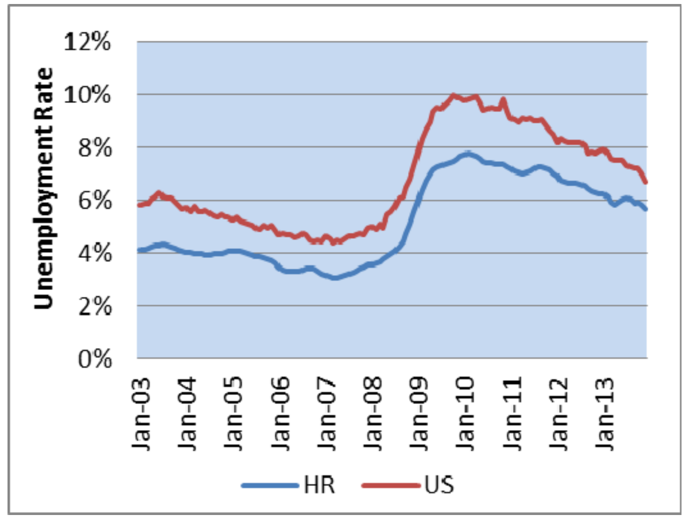


Source: Bureau of Labor Statistics, HRPDC

Employment: Non-agricultural civilian employment figures are considered the best estimate of labor market activity by the National Bureau of Economic Research. Year-over-year employment growth has been positive since Feb-11, a period of 35 months, indicating a general trend towards recovery. While employment is still 11,400 below the Dec-07 levels, the region grew strongly over the past year, with employment increasing by 9,200 since Dec-12, an increase of 1.2%.

Unemployment Rate, Seasonally Adjusted

U.S. & Hampton Roads, Jan 2003– Dec 2013, Monthly

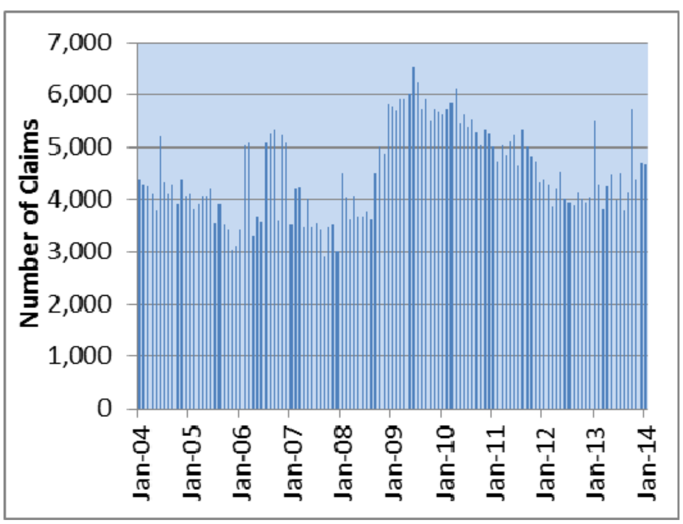


Source: Bureau of Labor Statistics, HRPDC

Unemployment Rate: The unemployment rate is the percentage of the population which is actively seeking work, but is unable to obtain a position. Hampton Roads' unemployment rate fell to 5.65%. in Dec-13, its lowest level since Dec-08. The regional unemployment rate remains 1.03% below that of the nation's, and the regional labor force has increased more quickly than the national labor force during the recovery.

Initial Unemployment Claims, Seasonally Adjusted

Hampton Roads, Jan 2004 – Jan 2014, Monthly

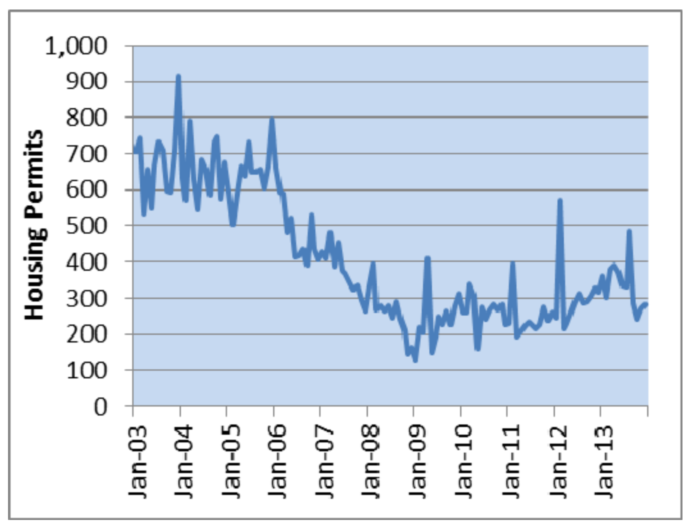


Source: Virginia Department of Labor, HRPDC

Initial Unemployment Claims: The number of Initial Unemployment Claims is a leading economic indicator, reflecting those who are forced to leave work unexpectedly and thus revealing the strength of the job market with little lag time. After a spike in initial unemployment claims in October, likely due to the government shutdown, initial claims stabilized at a higher level than before, with 4,675 claims in January 2014, above the long term average of 4,386 per month.

Single Family Housing Permits, Seasonally Adjusted

Hampton Roads, Jan 2003 – Dec 2013, Monthly



Source: U.S. Census Bureau, HRPDC

Single Family Housing Permits: Permit data indicates the level of construction employment and confidence regarding the future trajectory of the local economy. The number of seasonally adjusted permits continues to rise, but still remain below the long-term average of 477 single family homes permitted per month. As the housing market continues to stabilize, and the region moves into spring, new home construction should begin to increase slightly.