

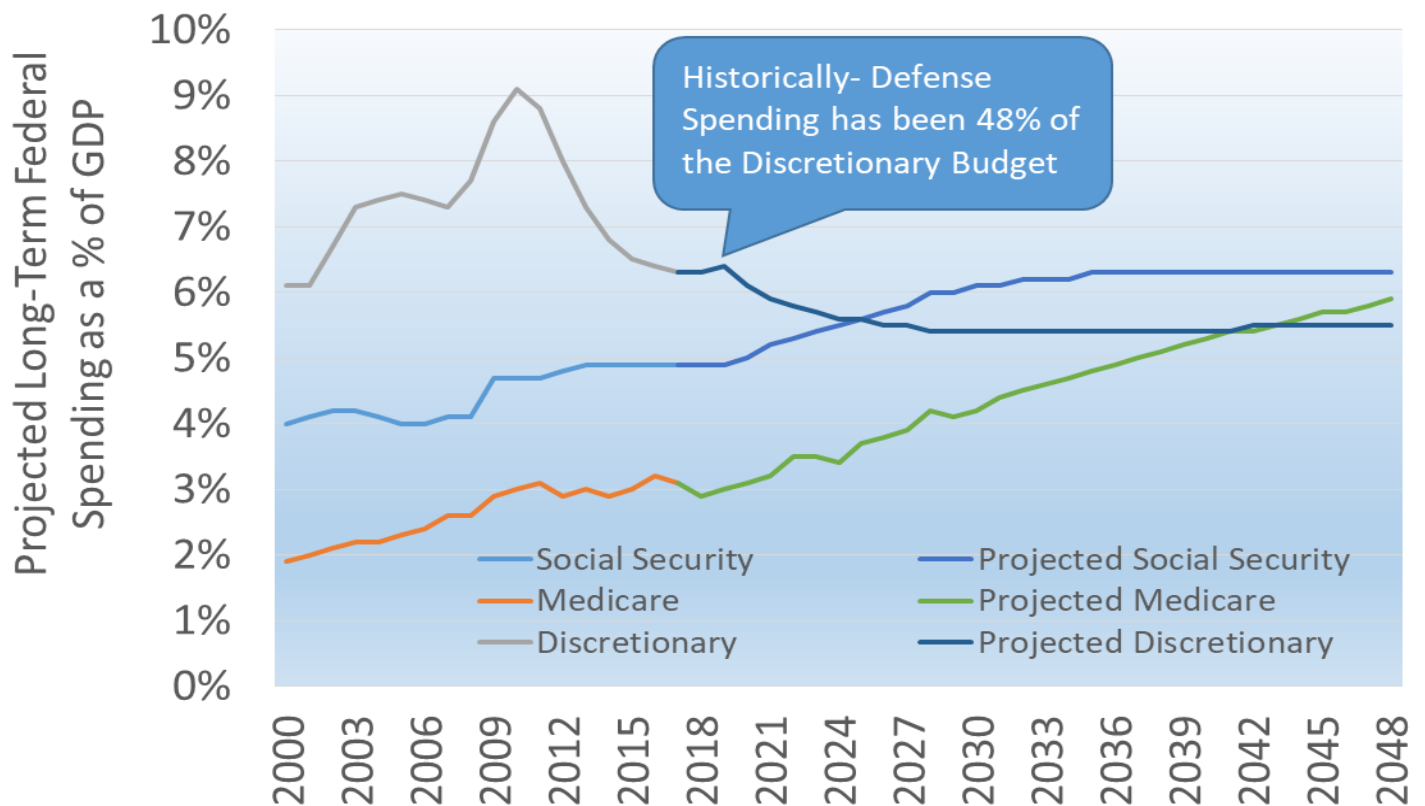
Where is Defense Spending Headed in the Future?

The Department of Defense (DoD) plays a significant role in the Hampton Roads economy, with uniformed military personnel constituting 8.1% of regional employment (in 2016, 84,089 personnel stationed in Hampton Roads), and 9.5% of regional incomes. Direct spending by the DoD, including federal civilian pay and contracts, constituted 22.8% of all regional economic activity; thus the growth or decline of DoD budgets has a tremendous impact the region's economy.

On August 13, 2018, President Trump signed the *John S. McCain National Defense Authorization Act for Fiscal Year 2019*, the first time in more than a decade that the defense bill was signed into law before the start of the federal fiscal year, which begins October 1st. The overall funding level for the DoD was set at \$674 billion, an increase of \$19.8 billion from the FY18 level (note the total funding authorized by the bill was \$717B). Additionally, the bill funds a personnel pay raise of 2.6% and provides \$24.1 billion for shipbuilding, including two Virginia-class submarines. The Congressional Budget Office indicates that if the 2019 Navy Shipbuilding Plan was adhered to, the DOD would spend an average of \$2.9 billion on carrier construction between now and 2048 (inflation-adjusted 2018 dollars).

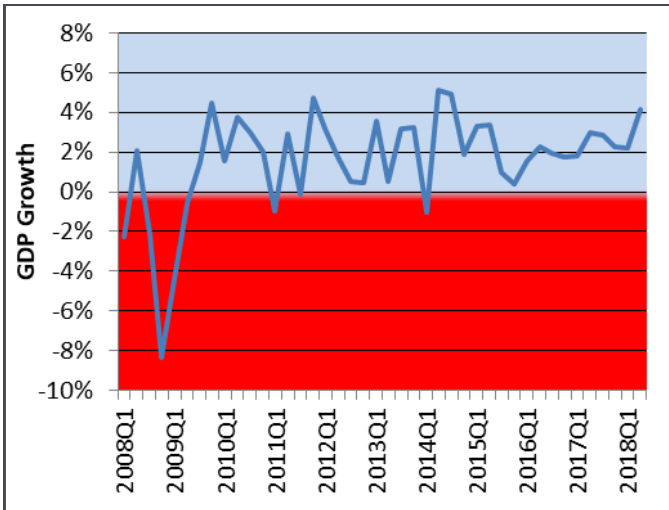
At the same time, we are facing uncertainties that may affect these levels of defense spending. The current budget deficit stands at 3.9% of Gross Domestic Product for FY18, which is extremely high given the relative health of the national economy. As interest rates rise and major programs such as Social Security and Medicare become increasingly expensive, Congress will face pressure to either raise taxes or to cut spending. As defense expenditure constitute almost half of discretionary spending, any significant cuts are likely to impact defense. Thus, even as current defense spending seems to point to strong opportunities for regional growth, the long-term federal budget will likely provide a challenging environment for economic growth in Hampton Roads.

Long-Term Federal Budget Spending as a Share of GDP
Projected by the Congressional Budget, June-2018



GDP, Annualized Growth Rate

United States, 2008Q1 – 2018Q2, Quarterly

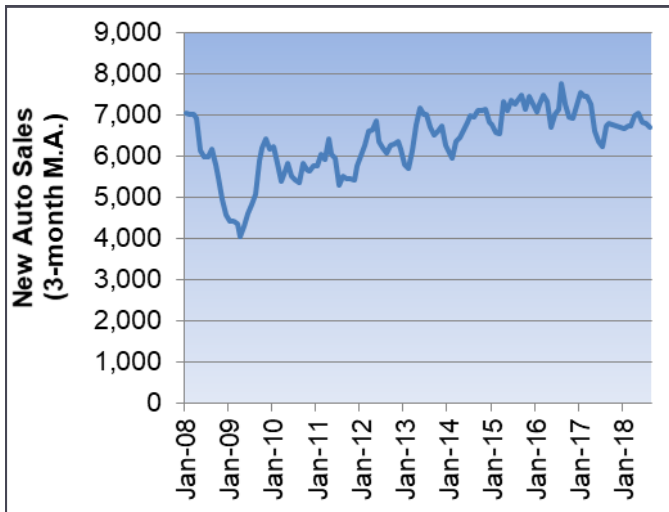


Source: Bureau of Economic Analysis, HRPDC

GDP: Gross Domestic Product combines consumption, investment, net exports, and government spending to determine the size and general health of the economy. Real GDP growth jumped to 4.2% in Q2 2018, driven primarily by strong consumer spending (+3.8%). Additionally, national defense spending grew an impressive 5.9% last quarter, which usually yields large benefits to the region. Private investment was essentially flat, but this was driven by a decrease in inventories, as non-residential investment increased by 8.5%.

New Car Sales, Seasonally Adjusted

Hampton Roads, Jan 2007 – Aug 2018, Monthly

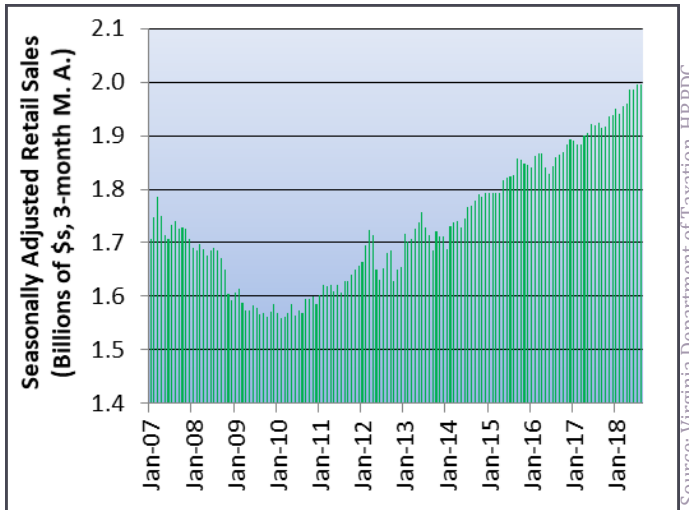


Source: Virginia Automobile Dealers Association, HRPDC

New Car Sales: Car sales, as a durable good, may be put off until such time as an individual’s economic prospects improve; thus, the number of new car sales indicate the level of confidence that households in Hampton Roads have in their financial future. Car sales increased to 6,712 in July 2018, but the three month average continues to be dragged down by extremely weak numbers in June (6,389). The long-term average stands at 7,010 for the region, and sales have been below that level since April 2017.

Hampton Roads Retail Sales, Seasonally Adjusted

Hampton Roads, Jan 2007– Aug 2018, Monthly

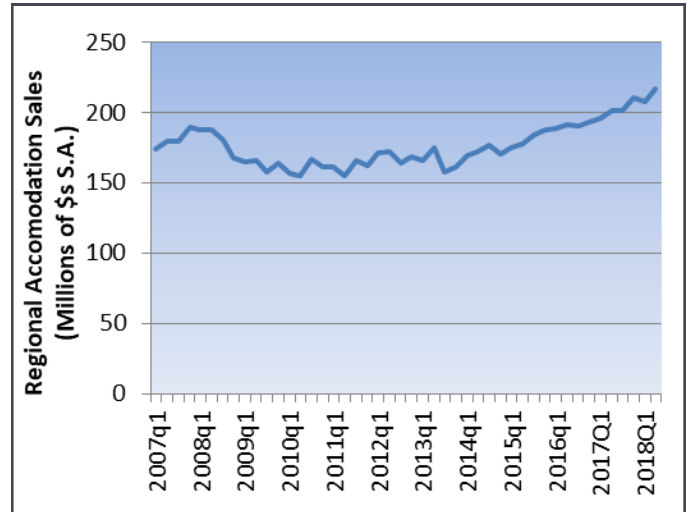


Source: Virginia Department of Taxation, HRPDC

Retail Sales: Retail sales in Hampton Roads, as measured by the 1% local option sales tax, serve as an indicator for consumption in the region. In August 2018, Hampton Roads’ taxable monthly sales tallied \$2.0 billion for the second month in row (seasonally adjusted 3-month average). Regional sales have grown 11.8% above pre-recession highs and are 28.0% higher than the recession lows. August 2018 sales grew 4.5% higher than they were in 2017, proving to be a strong month for both the retail industry and the economy overall.

Estimated Hotel Revenue, Seasonally Adjusted

Hampton Roads, 2007Q1 – 2018Q2, Quarterly

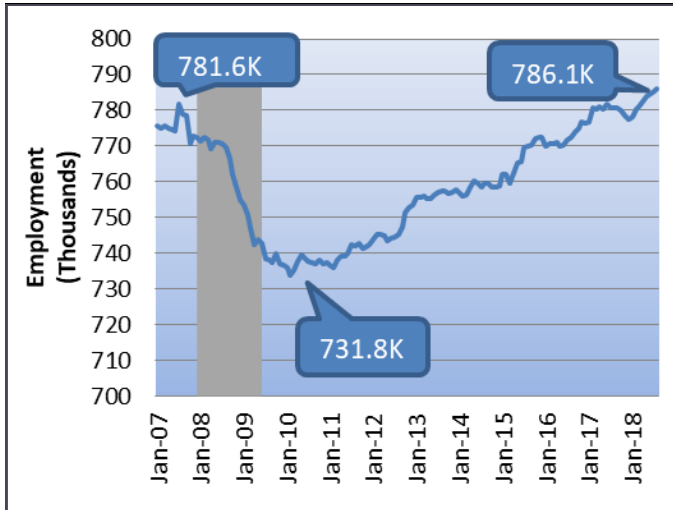


Source: Virginia Department of Taxation, HRPDC

Estimated Hotel Revenue: Hotel sales indicate the performance of the region’s tourism sector. In Q2 2018, accommodation sales increased by 4.44% regionally to \$217 million (seasonally adjusted). This is both an improvement on a slightly disappointing first quarter, and a significant increase (\$16M, +8.1%) over accommodation sales in the second quarter of last year. This is consistent with the other strong indicators that have emerged over the summer.

Civilian Employment, Seasonally Adjusted

Hampton Roads, Jan 2007 – Sep 2018, Monthly

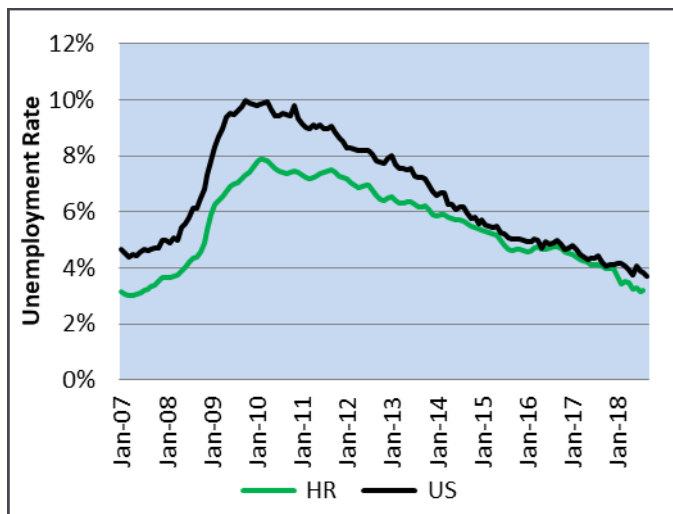


Source: Bureau of Labor Statistics, HRPDC

Employment: Non-agricultural civilian employment figures are considered the best estimate of labor market activity by the National Bureau of Economic Research. Hampton Roads' employment took a step back in September, losing 900 jobs (-0.1%). September's decline to 785,400 jobs served as the first month-over-month decline in employment of 2018. Both the Commonwealth and the nation continued to add employment through September.

Unemployment Rate, Seasonally Adjusted

Hampton Roads and U.S, Jan 2007 – Aug 2018, Monthly

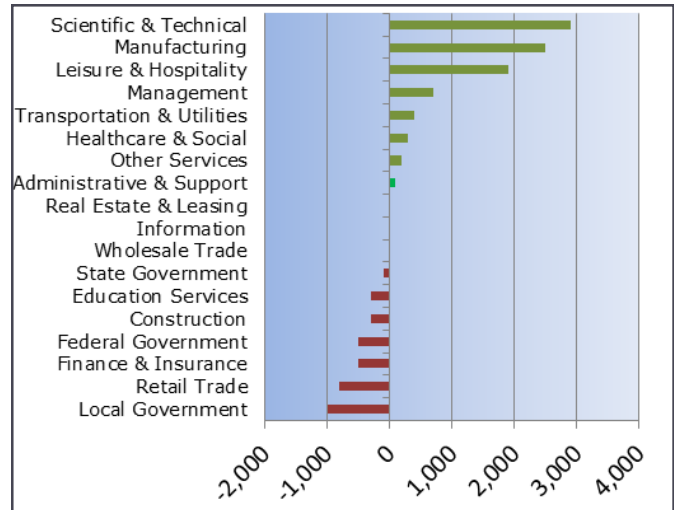


Source: Bureau of Labor Statistics, HRPDC

Unemployment Rate: The unemployment rate is the percentage of the population actively seeking work, but unable to obtain a position. Hampton Roads' unemployment rate increased slightly to 3.2% in August from 3.14% in July 2018. This was accompanied by a worrying decline in labor force participation in August (-4,678 or 0.57% seasonally adjusted) though this number has still registered a significant increase of 12,380 positions since August 2017.

Employment Growth by Industry

Hampton Roads Sep 2017 – Sep 2018, Year-over-Year

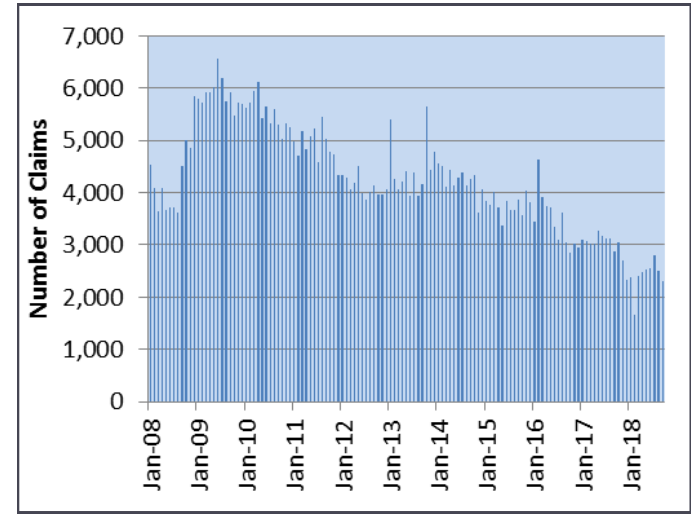


Source: Bureau of Labor Statistics, HRPDC

Employment Growth by Industry: As the job market grows or declines, there will be some industries whose experience does not resemble the regional trend. Regionally, scientific and technical employment (+2,900) and manufacturing employment (+2,500) have grown strongly over the past year; both industries have employment that has proven to be highly correlated with defense spending. Local government employment has declined both year-over-year (-1,100) and over the past decade (-7,700). Retail jobs have also fallen (-800).

Initial Unemployment Claims, Seasonally Adjusted

Hampton Roads, Jan 2008 – Sep 2018, Monthly

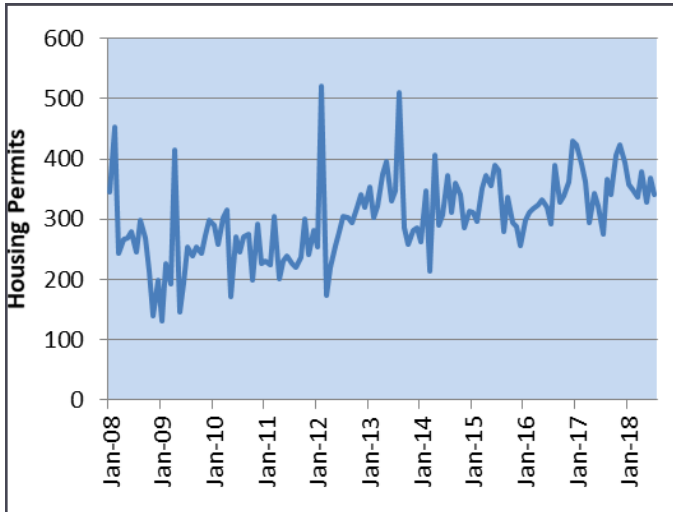


Source: Virginia Department of Labor, HRPDC

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. The region's initial unemployment claims fell by a significant amount, with only 2,311 new claims in September 2018, well off the spike seen in July 2018 (2,794). For the past year, the region has average nearly 1,300 fewer claims per month than the long-term average for Hampton Roads.

Single Family Housing Permits, Seasonally Adjusted

Hampton Roads, Jan 2007 – Aug 2018, Monthly

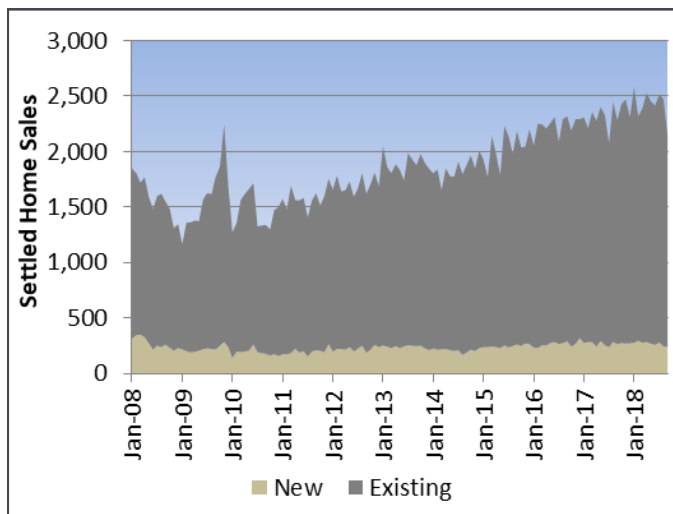


Source: U.S. Census Bureau, HRPDC

Single Family Housing Permits: Permit data signals the level of construction employment and confidence regarding the future trajectory of the local economy. Seasonally adjusted single family permits continued to decline in August 2018, declining to 309 units, the lowest level of the past 16 months. There was also a decline in building permits nationally in August, but national building permits recovered again in September.

Number of Homes Sold, Seasonally Adjusted

Hampton Roads, Jan 2007 – Sep 2018, Monthly

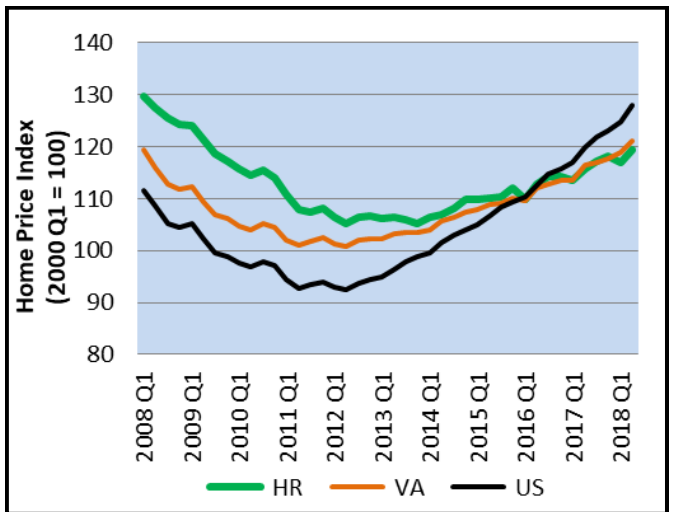


Source: REIN, HRPDC

Home Sales: Settled home sales measure the level of transactions on the real estate market over time, and a healthy real estate market should have a consistent level of activity. The levels of existing home sales declined significantly in September 2018, falling by 321 sales to 2,156 for the month, below the recent average of 2,400 a month. One should not overanalyze this month, as significant weather concerns and a mandatory evacuation temporarily effected the real estate market.

Home Price Index, All Transactions

Hampton Roads, 2008Q1 – 2018Q2 Quarterly

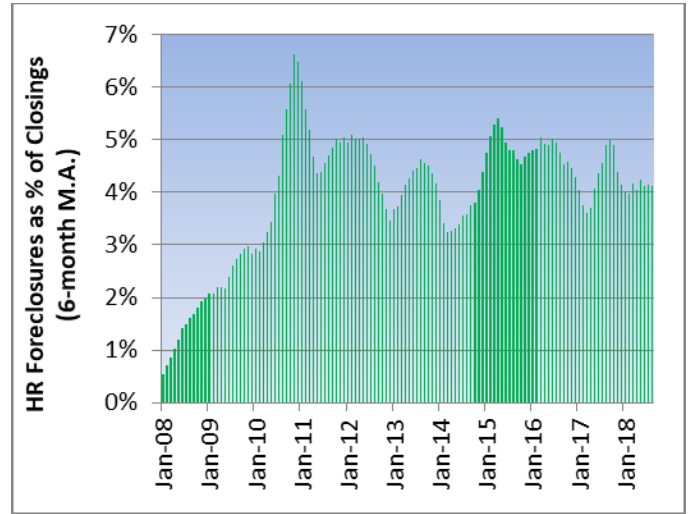


Source: Federal Housing Finance Agency, HRPDC

Home Price Index: The home price index measures the value of homes by evaluating changing price levels through repeated sales of properties. The index provides the highest quality data available on the trends in the real estate market. Hampton Roads' home prices increased in Q2 2018, and are 3.1% above the price levels during the same time last year, though lag behind the growth rate of home prices statewide (3.9%), and nationwide (6.6%). Regional home values remain 8.5% below 2007 levels.

Foreclosures and Distressed Sales

Hampton Roads, Jan 2008 – Aug 2018, Monthly



Source: Zillow, HRPDC

Foreclosures: Foreclosures have a significant impact on the real estate market and the community, and depress home values on both a neighborhood and regional level. Distressed homes' share of total sales has been shown to have an impact on the sale price of existing homes. While there continue to be fluctuations in the share of foreclosures within the housing market, the level is still elevated from the housing boom. Foreclosures constituted 4.1% of all existing home sales in August 2018, playing a role in the tepid growth of home values.