



# Economic Outlook

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Mark Vitner, Managing Director & Senior Economist  
January 9, 2020

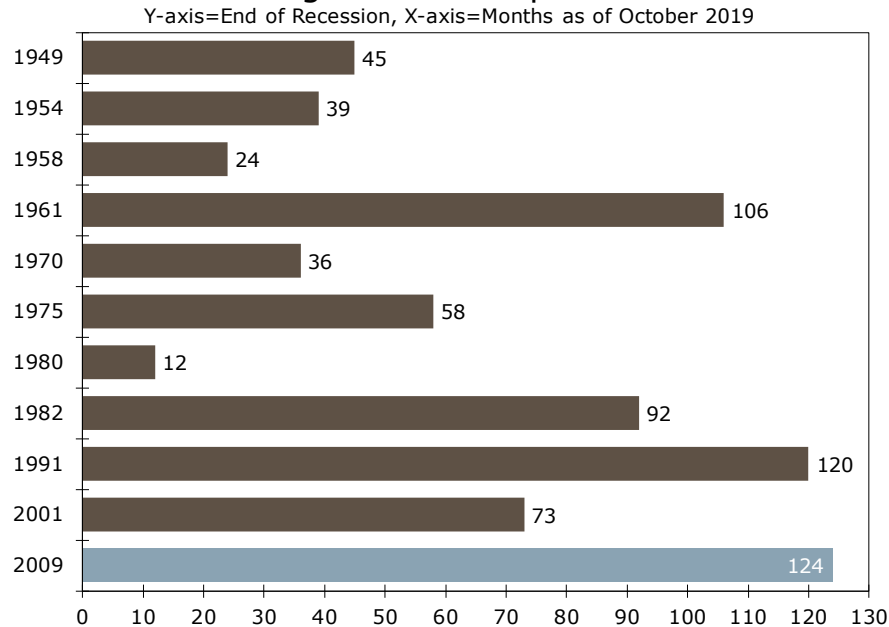


<b>Economic Outlook</b>	<ul style="list-style-type: none"><li>▪ <b>Real GDP growth has decelerated from a 3% pace last year to around 2% and looks set to slow even further. Most of the slowdown is tied to weakening global growth and its impact on exports, capital spending and inventories.</b></li></ul>
<b>Policy Environment</b>	<ul style="list-style-type: none"><li>▪ <b>Tax reform continues to bolster take-home pay but trade uncertainty upended capital spending. Capex should slowly grind higher. Fiscal policy remains expansionary. After cutting rates three times, the Fed is likely on pause.</b></li></ul>
<b>Trade Policy</b>	<ul style="list-style-type: none"><li>▪ <b>An agreement in principle has been reached with China that should result in a lessening of trade tensions that have been weighing on the global economy. The USMCA is another near-term positive that reduces uncertainty.</b></li></ul>
<b>Households</b>	<ul style="list-style-type: none"><li>▪ <b>Consumers remain optimistic about the economy and their finances. Wages &amp; salaries are rising fastest at the lower end of the pay spectrum, which has boosted spending at discount stores and restaurant chains.</b></li></ul>
<b>Recession Risk</b>	<ul style="list-style-type: none"><li>▪ <b>Recession concerns have abated significantly as the yield curve has normalized and equity markets have reached new all-time highs. There are few obvious imbalances present in the economy today and growth is broadening.</b></li></ul>

The current expansion is now the longest on record but has also been the weakest of the post-WWII era in terms of average GDP growth.

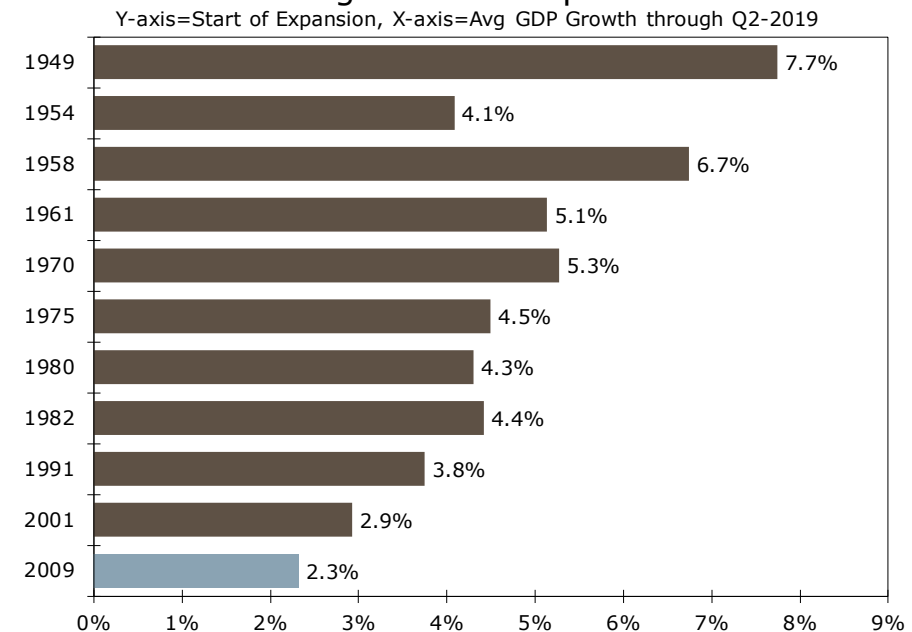
**The Longest Expansion**

**Length of U.S. Expansion**



**...but the Weakest**

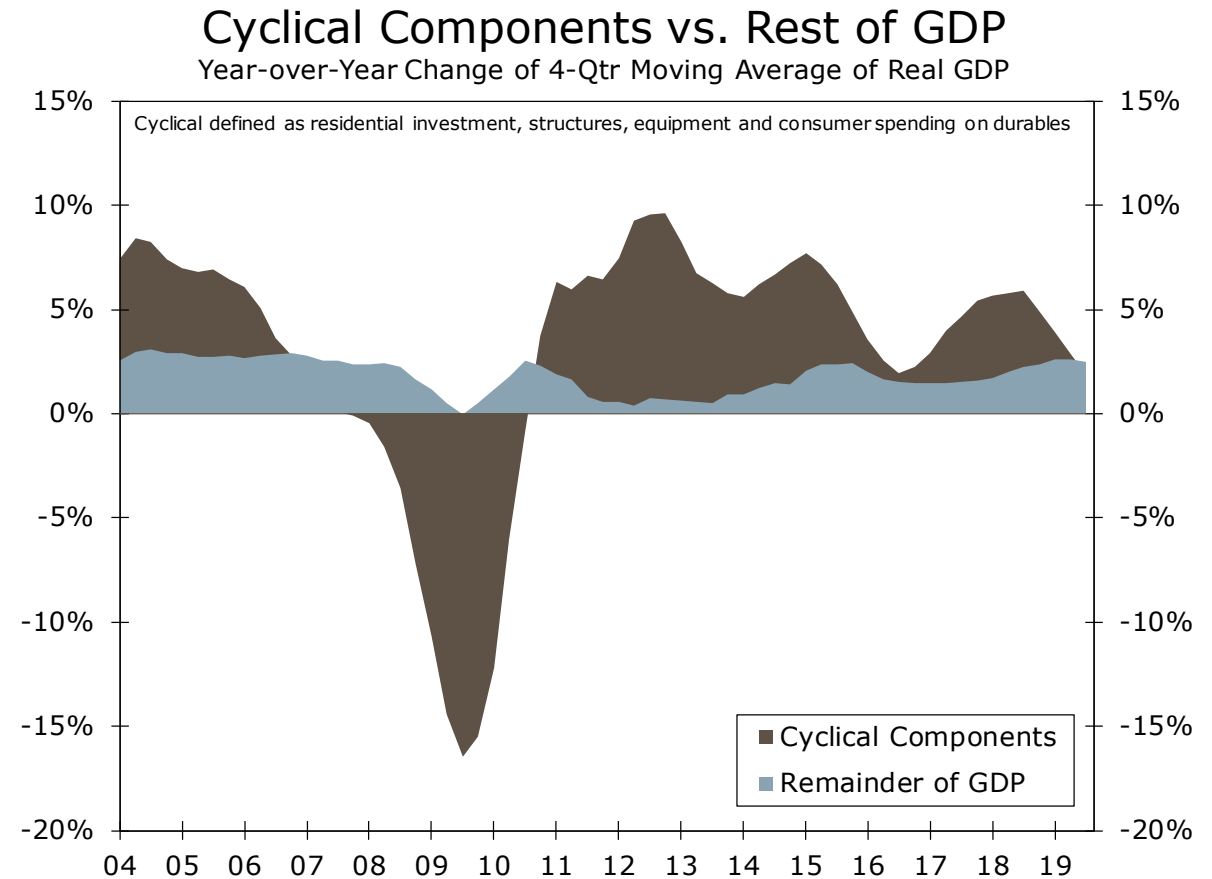
**Strength of U.S. Expansion**



Source: U.S. Department of Commerce, National Bureau of Economic Research and Wells Fargo Securities

Consumer spending on durable goods, housing, capital spending and nonresidential structures collectively account for 20% of GDP but over 100% of the decline in GDP during recessions.

We have seen less of a boom in the most cyclical parts of the economy during this cycle, which may push a correction further out and ultimately make that correction less severe.

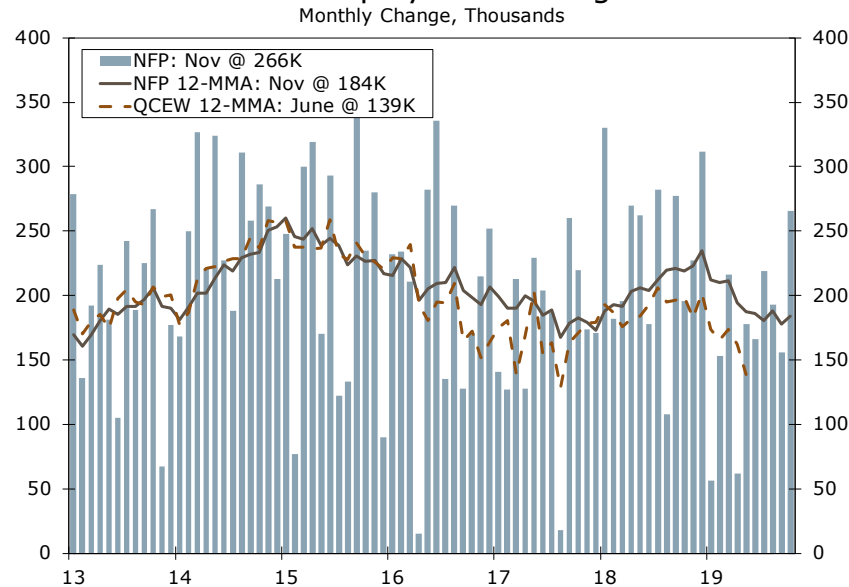


Source: U.S. Department of Commerce and Wells Fargo Securities

Hiring has reportedly picked up but will be revised lower in February. The quality of jobs being added is relatively good. Wage gains remain modest relative to prior periods when the labor market was this tight, but recent evidence suggests wage gains are accelerating for those at the lower end of the income spectrum and among younger workers, giving spending a boost.

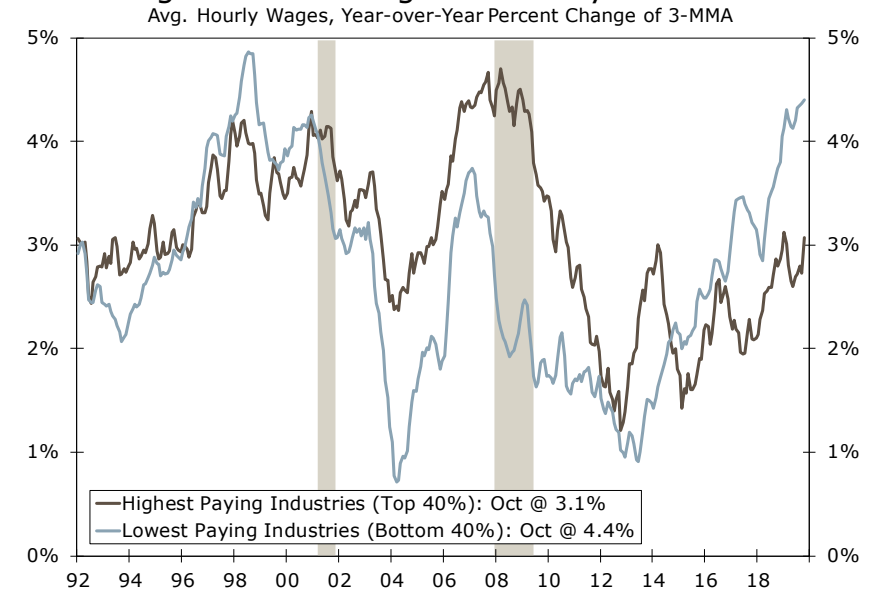
## Nonfarm Employment

### U.S. Employment Change



## Wages

### Wage Growth in High & Low Pay Industries



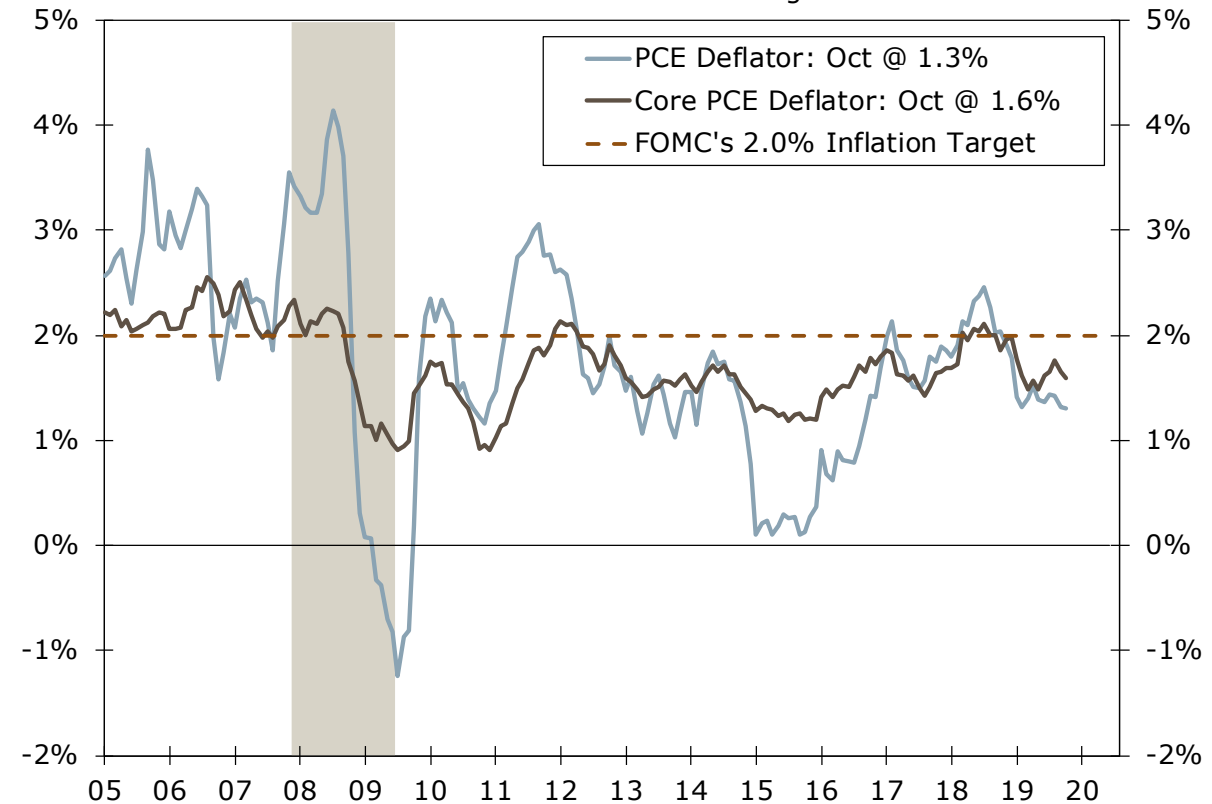
Source: U.S. Department of Labor, National Federation of Independent Business and Wells Fargo Securities

After briefly rising above the Fed's 2% target, core inflation appears to have decelerated once again, amid weakening final demand. Inflation expectations have also fallen over the past few months.

We see the Fed as being opportunistic in this environment, hoping to spur a broader and more durable economic expansion.

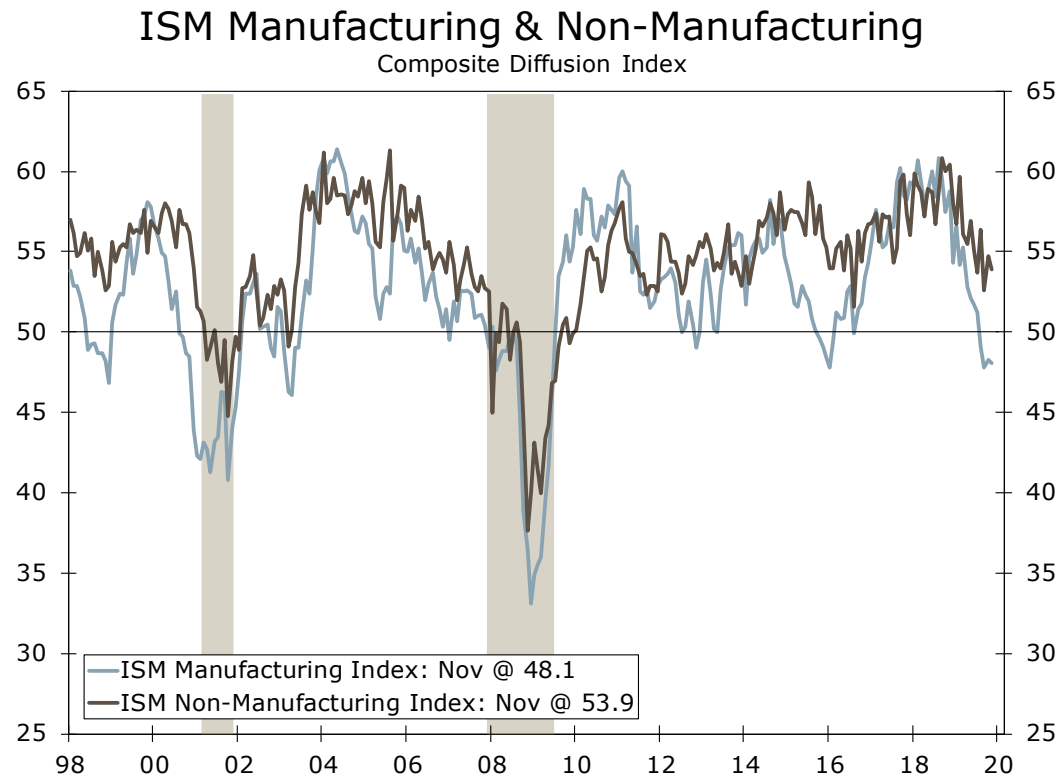
## PCE Deflator vs. Core PCE Deflator

Year-over-Year Percent Change



Source: U.S. Department of Commerce and Wells Fargo Securities

A rebound in the ISM is likely in store now that more firms believe they have too little inventory than believe they have too much. Orders are likely to surprise to the upside in coming months.

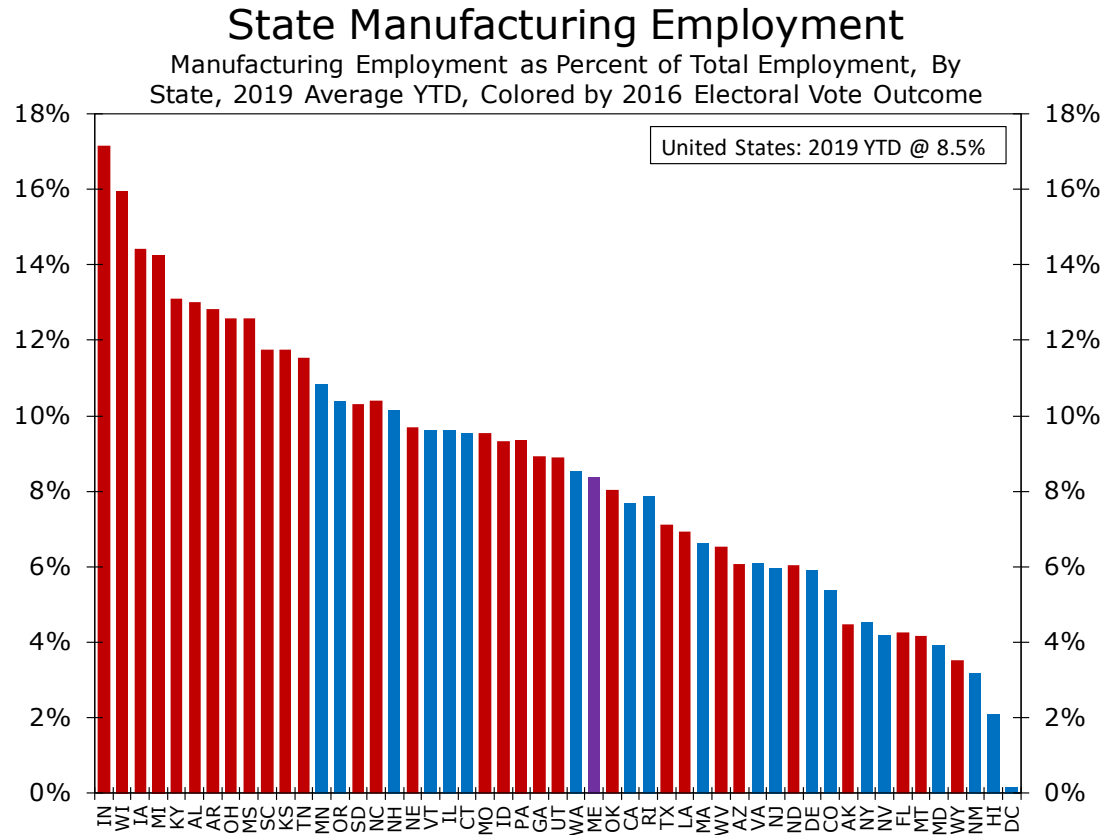


Source: Institute for Supply Management and Wells Fargo Securities

States that voted Republican in 2016 are generally more exposed to manufacturing.

Manufacturers are having a tough time finding workers, however, so the recent trade spat has not yet impacted staffing all that much.

Many firms are reluctant to let any workers go for fear they will not be able to hire them back when demand revives.



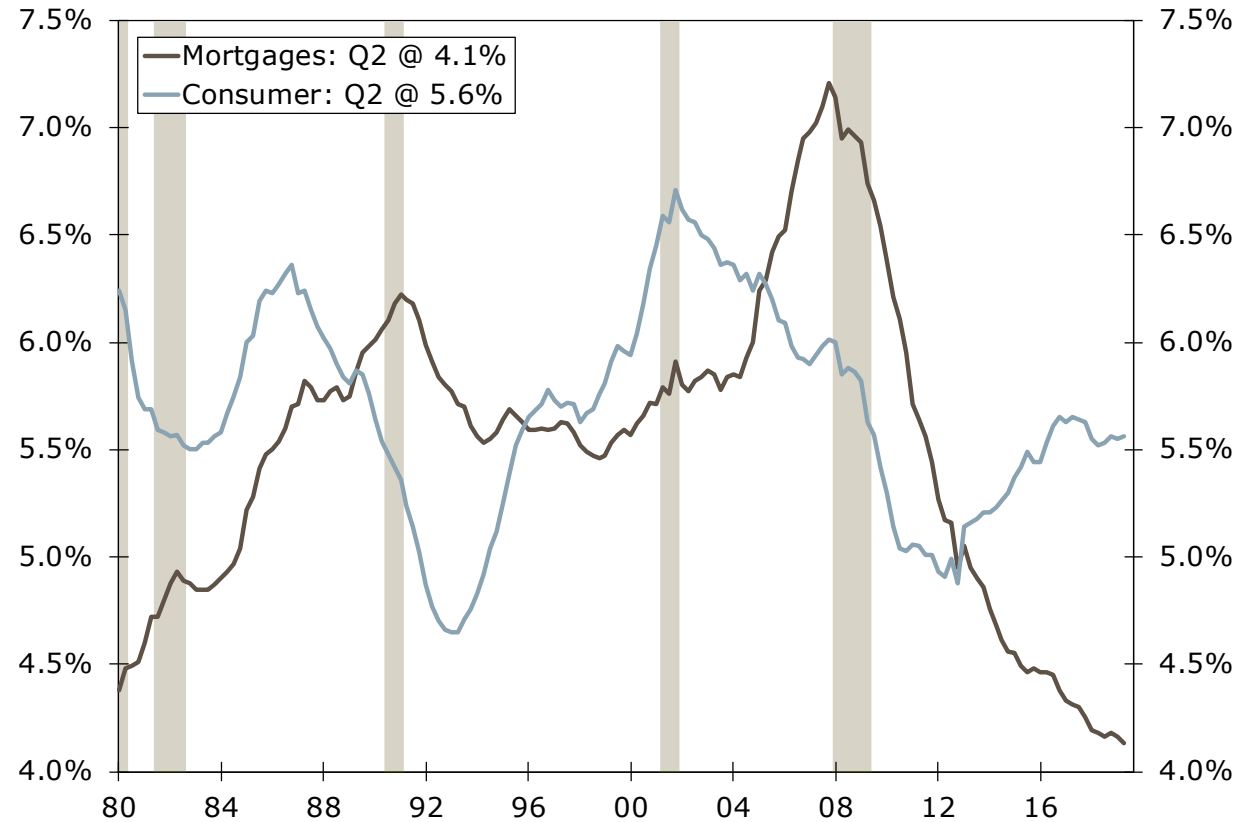
Source: Federal Election Commission, U.S. Department of Labor and Wells Fargo Securities



Monthly debt service remains fairly low, but has increased for non-mortgage debt. The rise in non-mortgage debt has almost entirely been driven by student and auto loans.

## Debt Service Ratios: Mortgages vs. Consumer

As a Percent of Disposable Personal Income



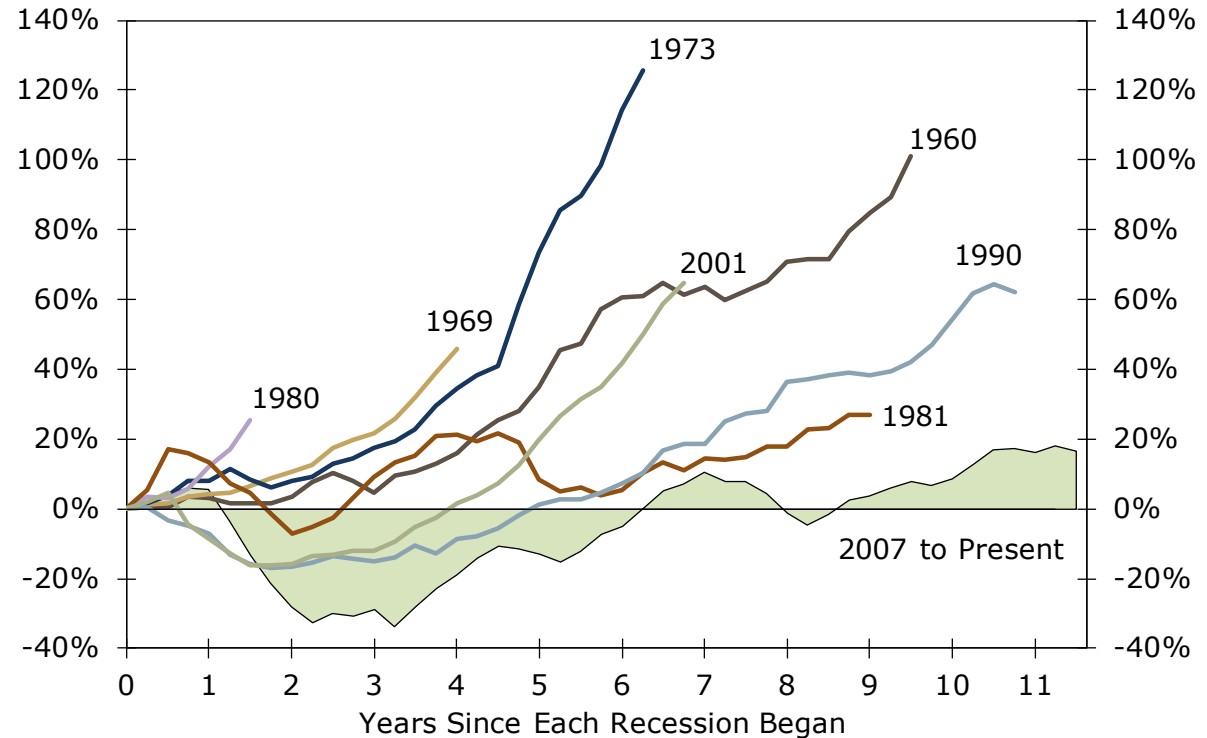
Source: Federal Reserve Board and Wells Fargo Securities

Overall building has remained relatively subdued this cycle.

Much of the activity has been concentrated in several large markets, which may present some risks of a sharp or prolonged pullback in the tech and energy sectors.

## Nonresidential Structures Investment

Percent Change Since Start of Each Recession



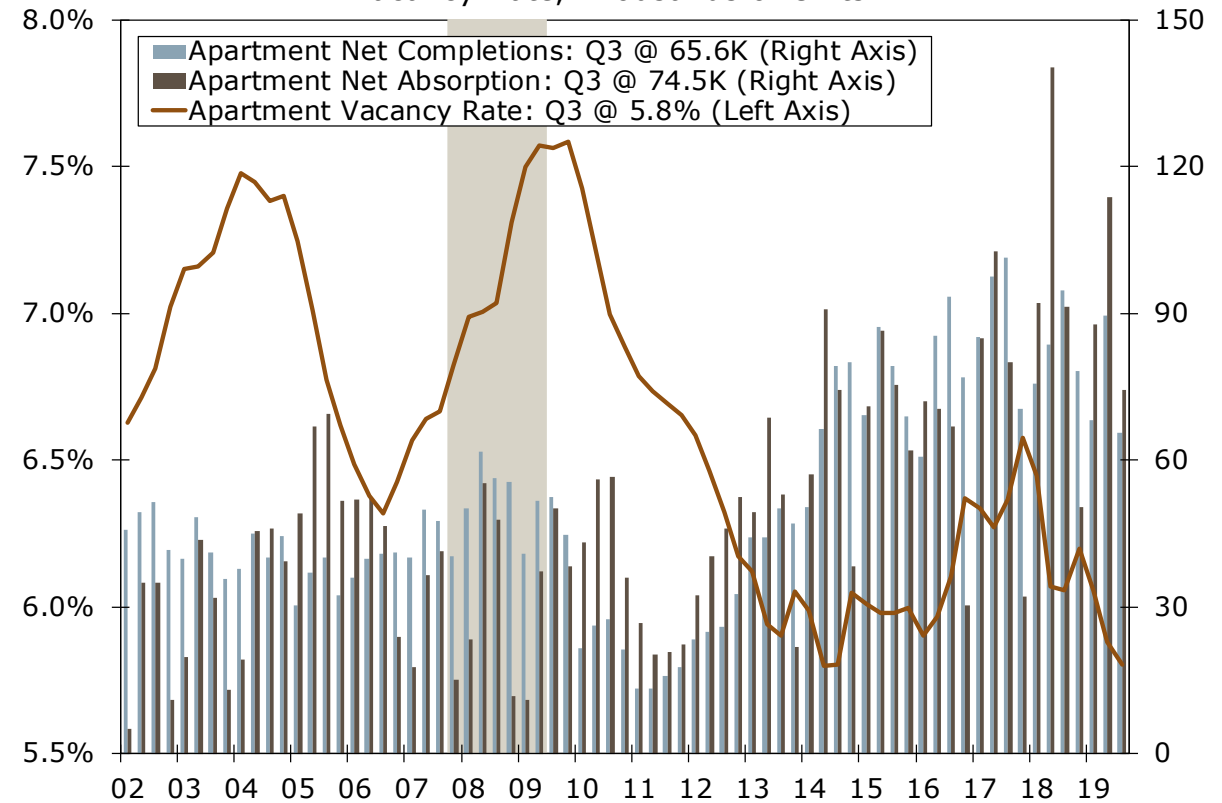
Source: U.S. Department of Commerce and Wells Fargo Securities

Apartment development has been fairly strong the past few years, with a disproportionate share of activity devoted to luxury and lifestyle units in a handful of rapidly growing metropolitan areas.

Development is now shifting to more affordable projects in suburban areas and in lower cost parts of the country.

### Apartment Supply & Demand

Vacancy Rate, Thousands of Units



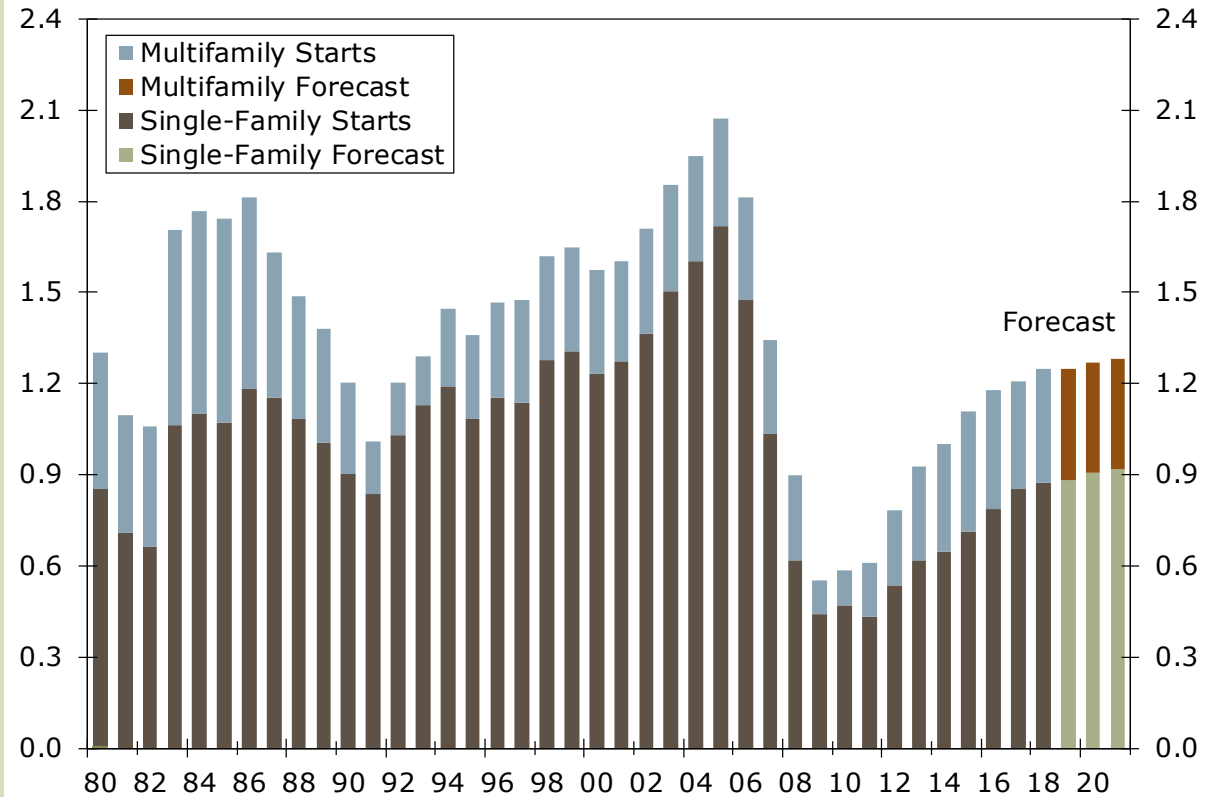
Source: CoStar, Inc. and Wells Fargo Securities

Single-family homebuilding has strengthened in recent months. Still, affordability concerns and development constraints will continue to limit new development.

Overall homebuilding is still lagging household formation and there are too few homes available in markets where population and employment are growing rapidly. Apartment construction is pivoting toward more affordable units.

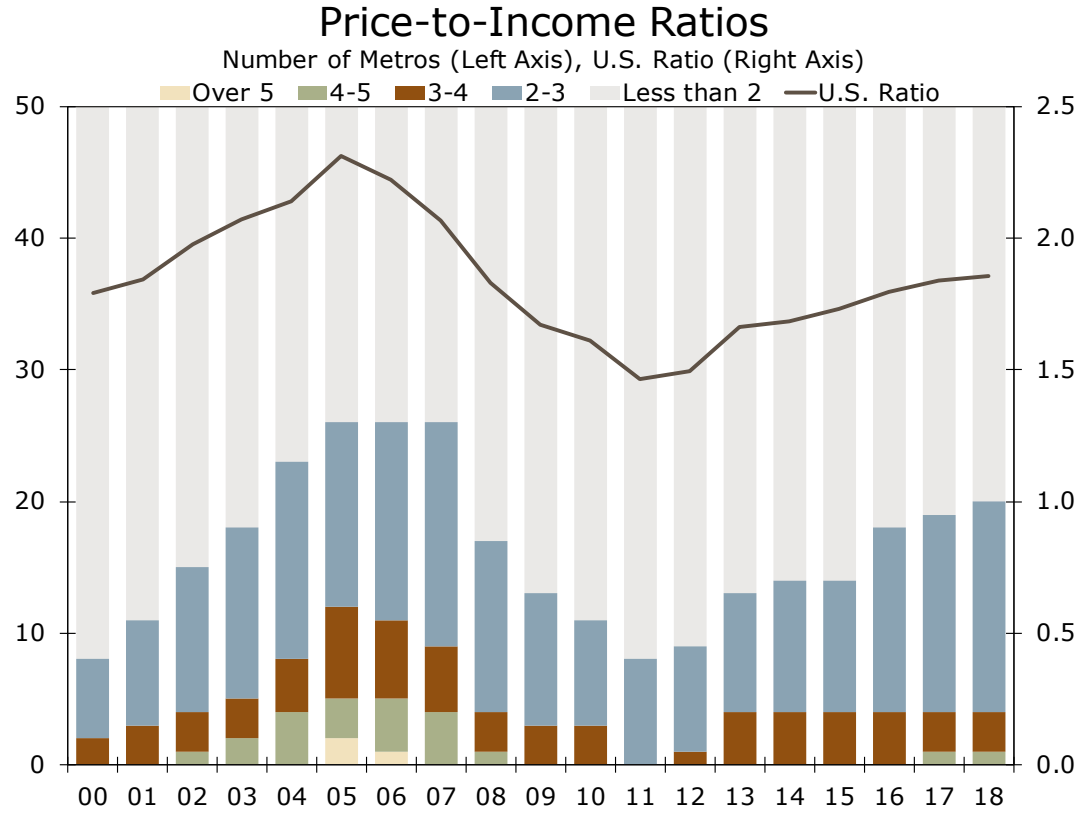
### Housing Starts

Millions of Units



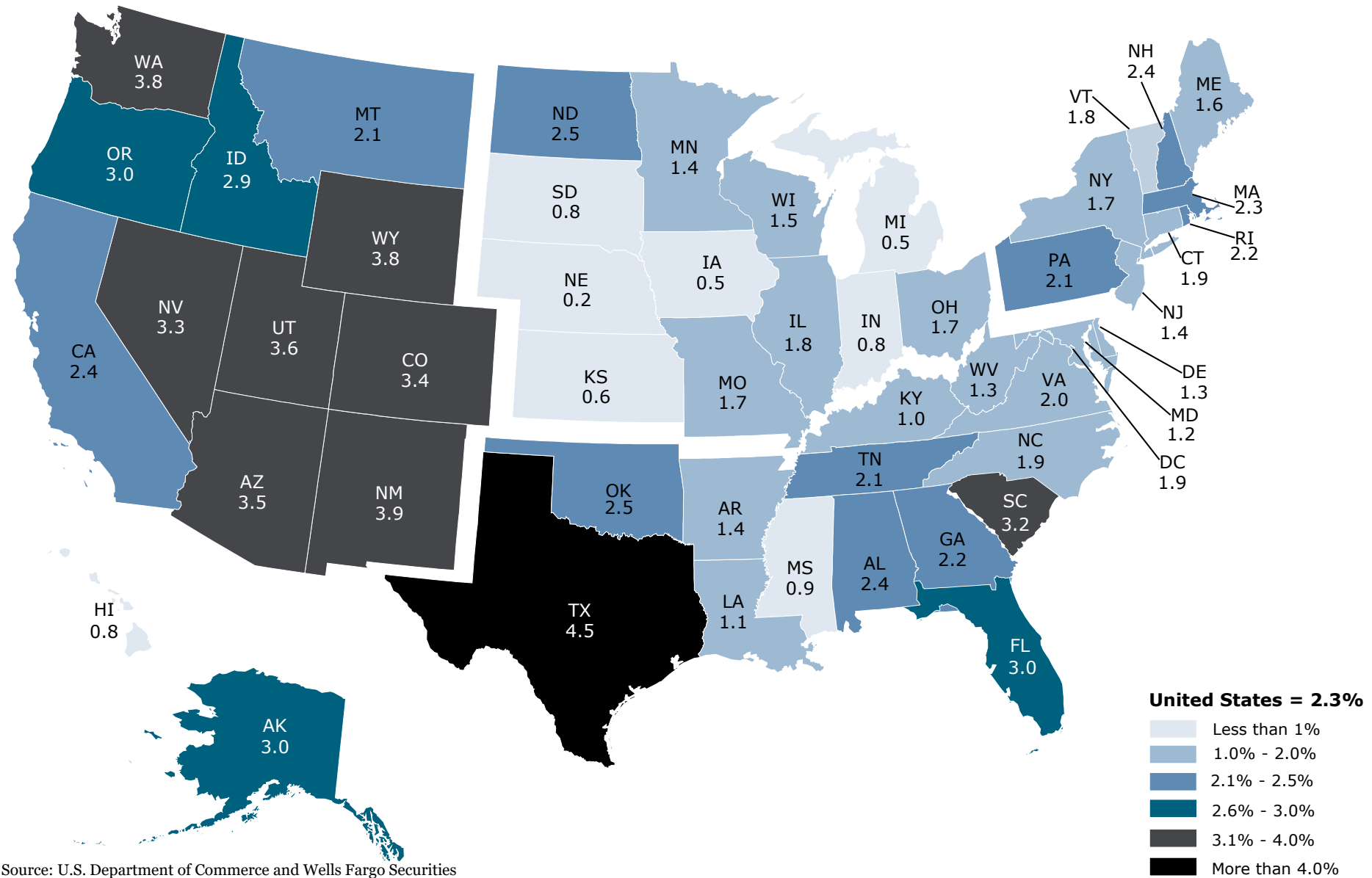
Source: U.S. Department of Commerce and Wells Fargo Securities

Home price-to-income ratios, particularly in large metros, are rising towards mid-2000 levels.



Source: NAR, U.S. Department of Commerce and Wells Fargo Securities

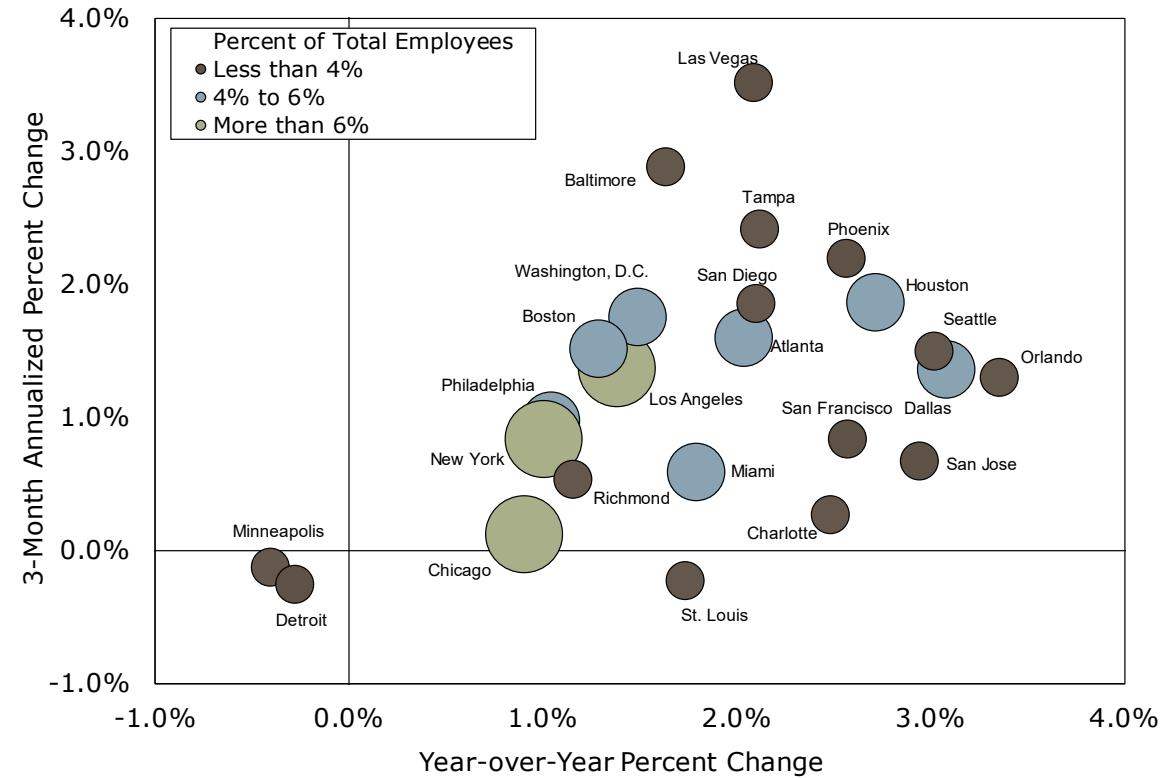
# Year-over-Year Percent Change in Real GDP by State (Q2-2019)



Source: U.S. Department of Commerce and Wells Fargo Securities

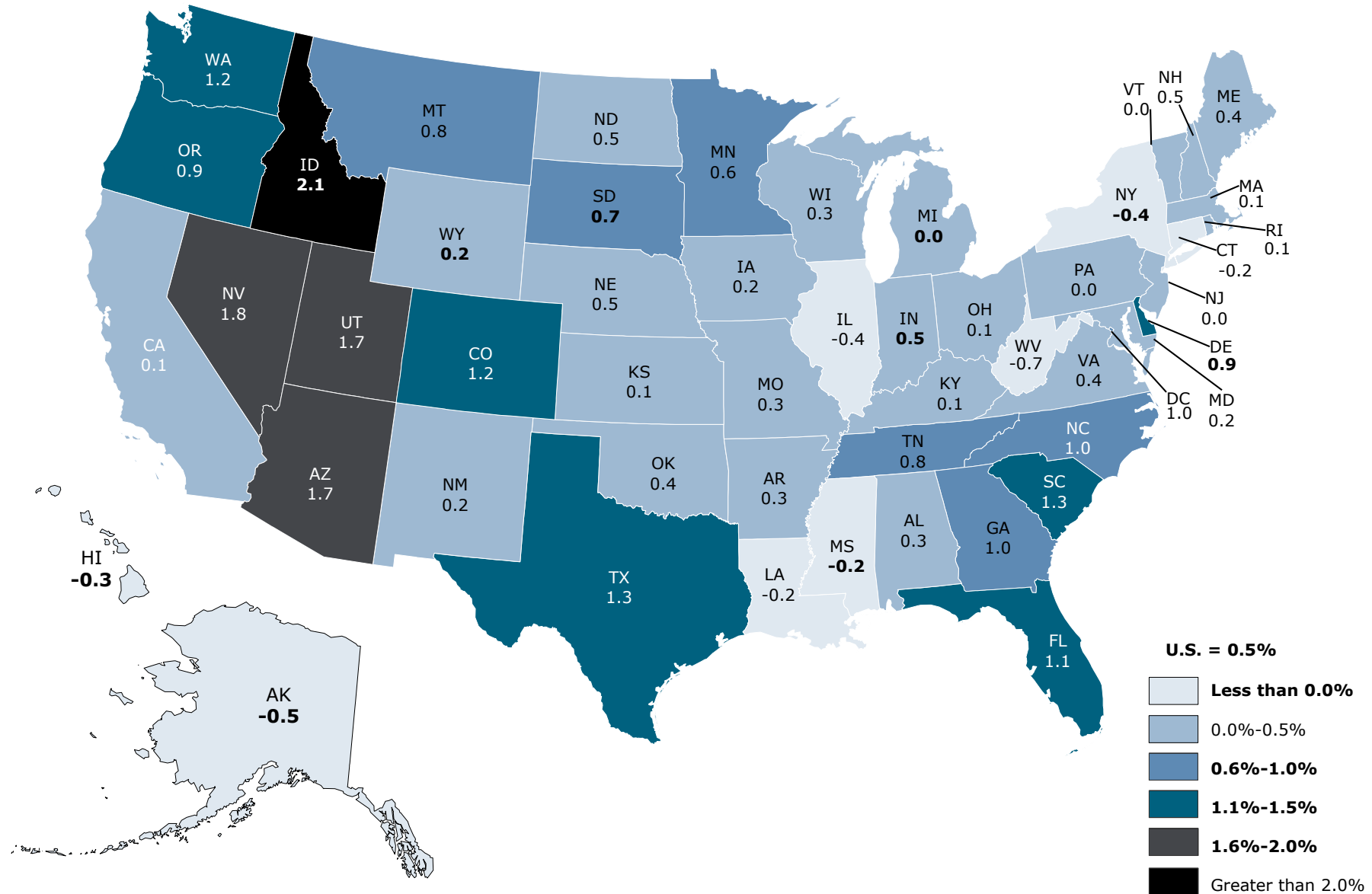
Employment growth is strongest in the South and West.

U.S. Employment Growth by MSA  
November 2019



Source: U.S. Department of Labor and Wells Fargo Securities

# Population Growth by State – 2019



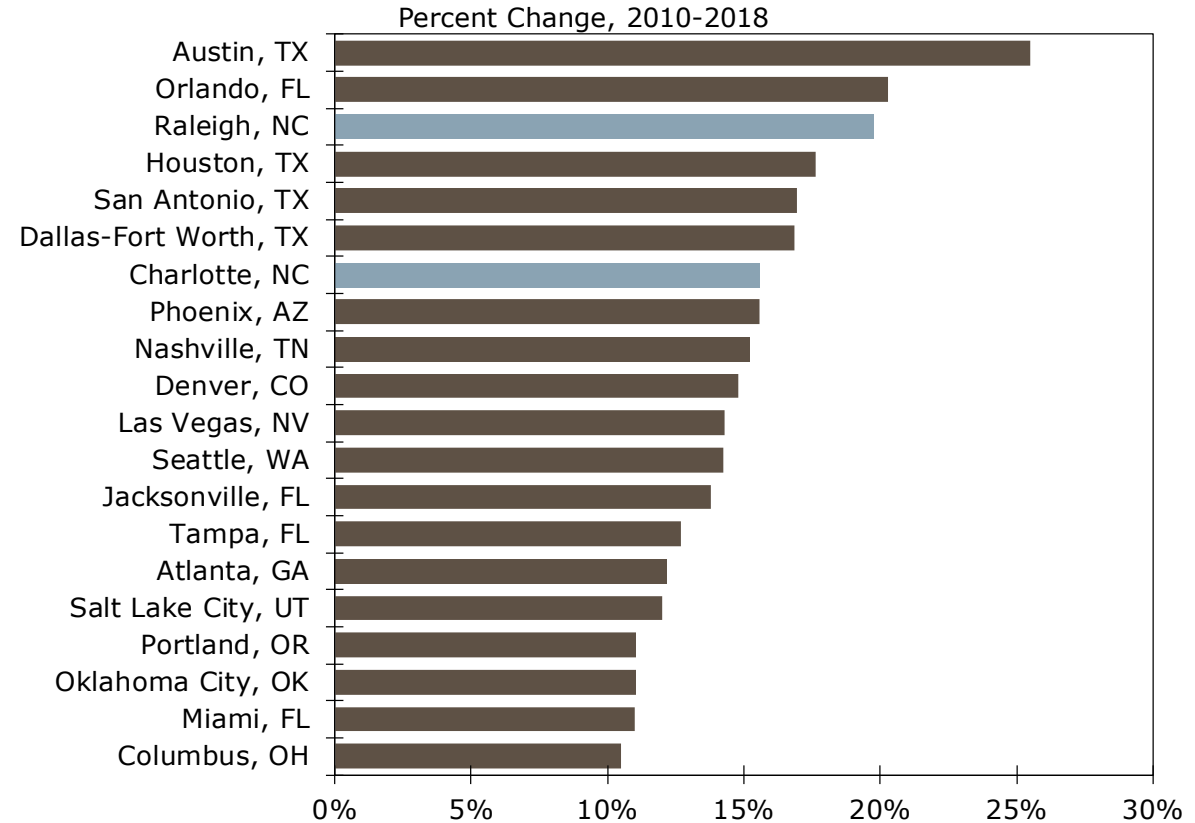


Raleigh and Charlotte both rank among the top 10 fastest growing large metropolitan areas since 2010.

North Carolina is the only state other than Texas and Florida to have more than one large metro area rank in the top 20.

Charleston, SC would have clearly made the cut if the criteria was reduced to areas with populations between 500,000 to 999,000.

### Metro Area Population Growth: Top 20

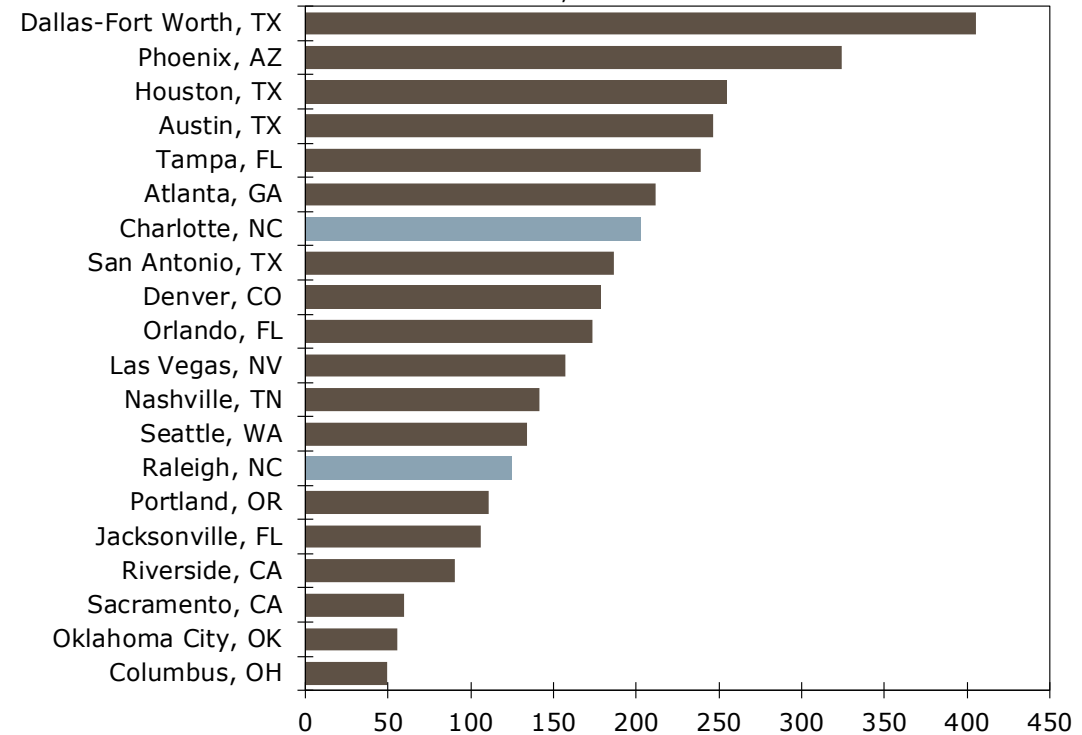


Source: U.S. Department of Commerce and Wells Fargo Securities

Domestic migration is a good proxy for the relative attractiveness of a region's labor markets. Retiree markets also rank among the leaders in attracting new residents.

## Metro Area Net Domestic Migration: Top 20

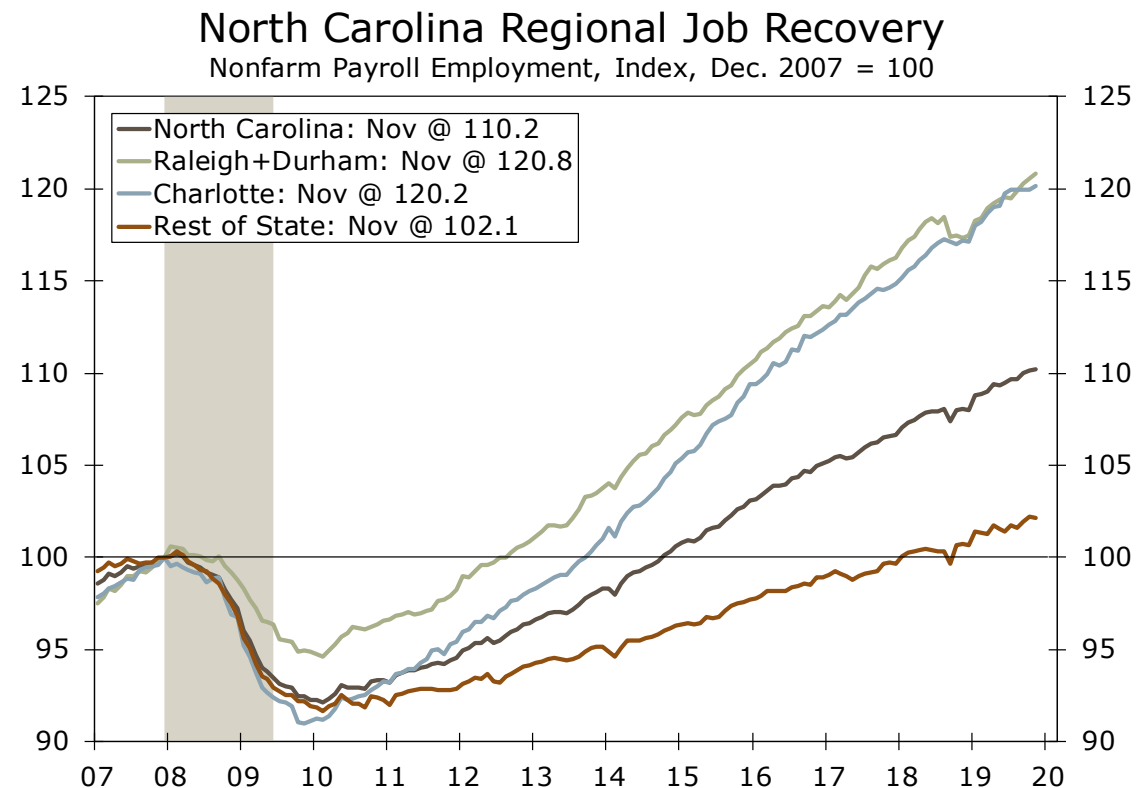
Thousands, 2010-2018



Source: U.S. Department of Commerce and Wells Fargo Securities

Raleigh recovered from the Great Recession much sooner than the rest of the state.

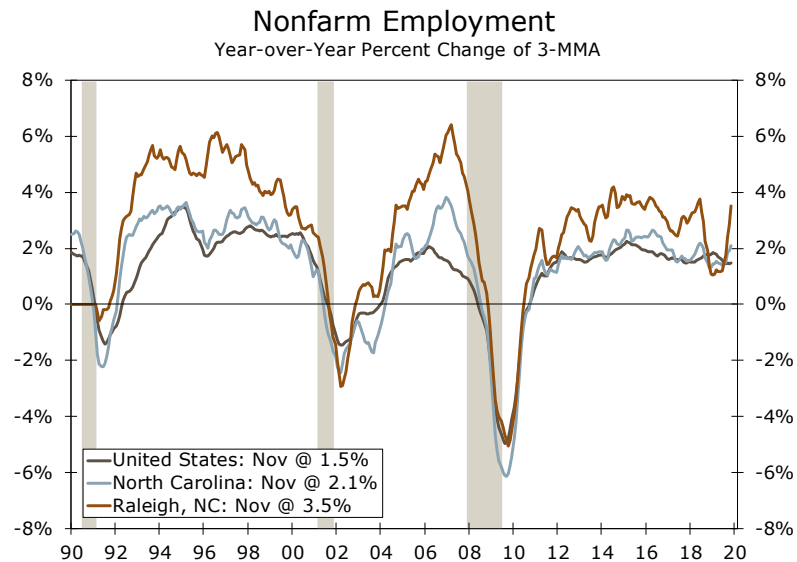
Areas outside of Raleigh and Charlotte gained momentum this past year and are poised for solid growth in 2020.



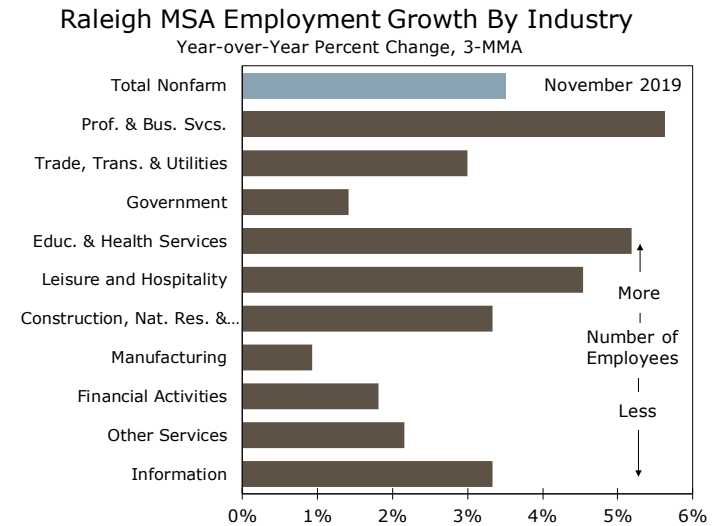
Source: U.S. Department of Labor and Wells Fargo Securities

Payrolls are expanding rapidly, led by professional & business services.

## Employment Growth

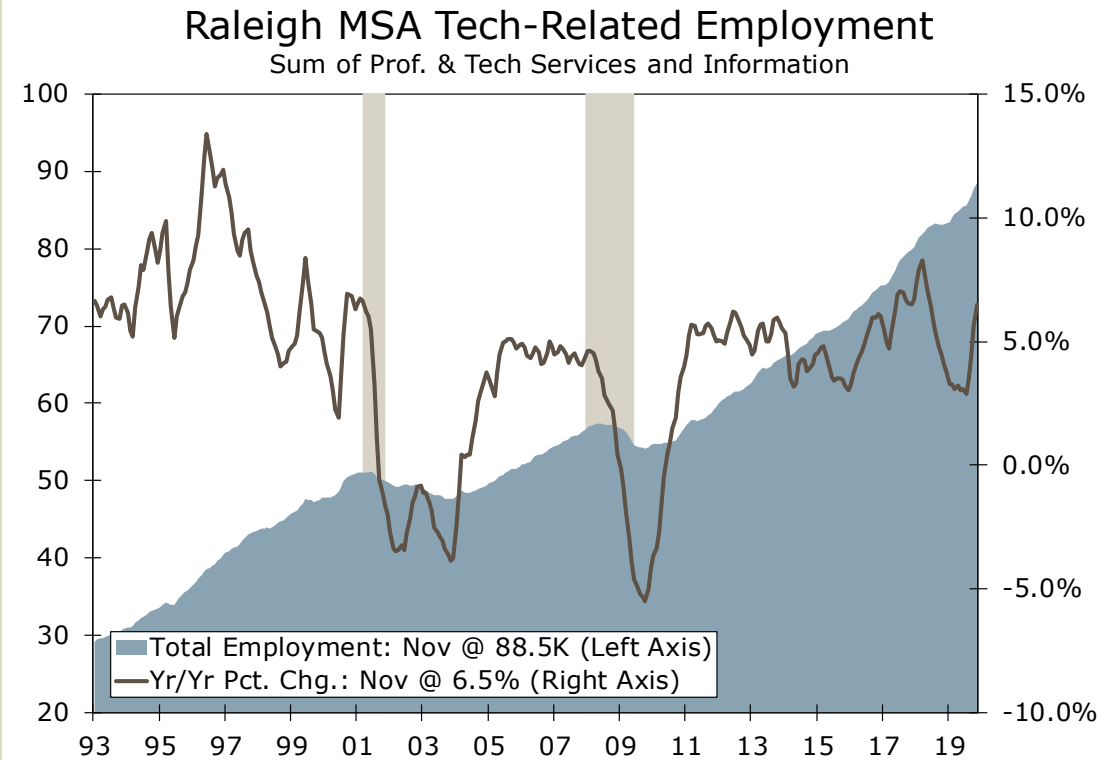


## Employment by Industry



Source: U.S. Department of Labor and Wells Fargo Securities

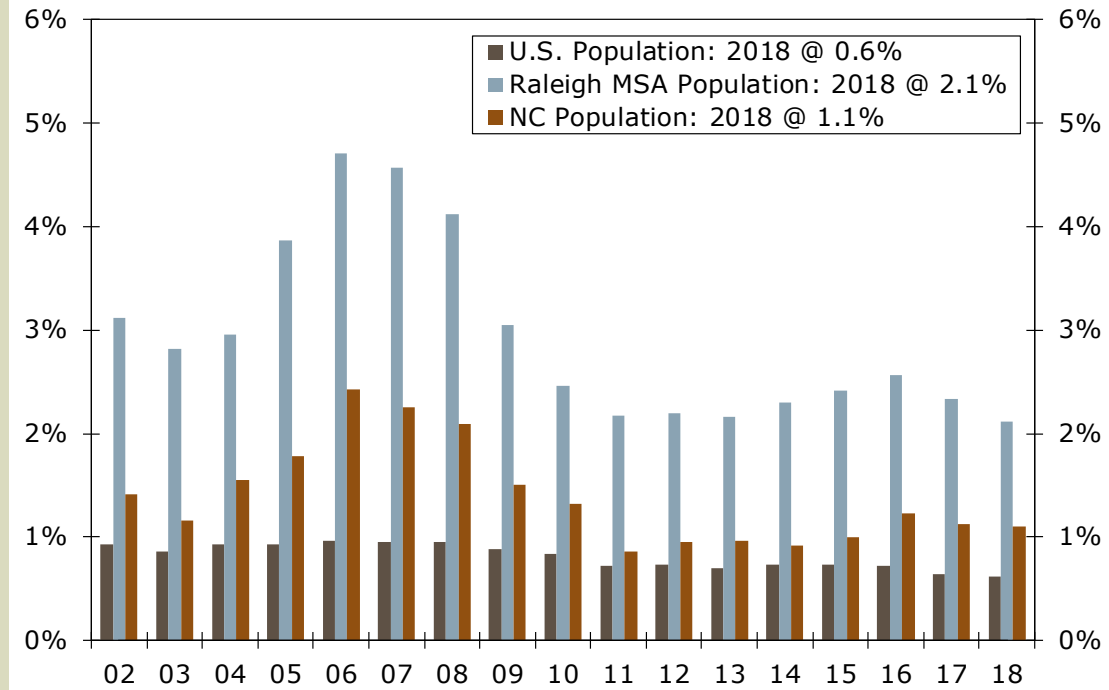
The Tech sector continues to drive the region's labor market



Source: U.S. Department of Labor and Wells Fargo Securities

Population growth has moderated the past two years, but remains relatively strong.

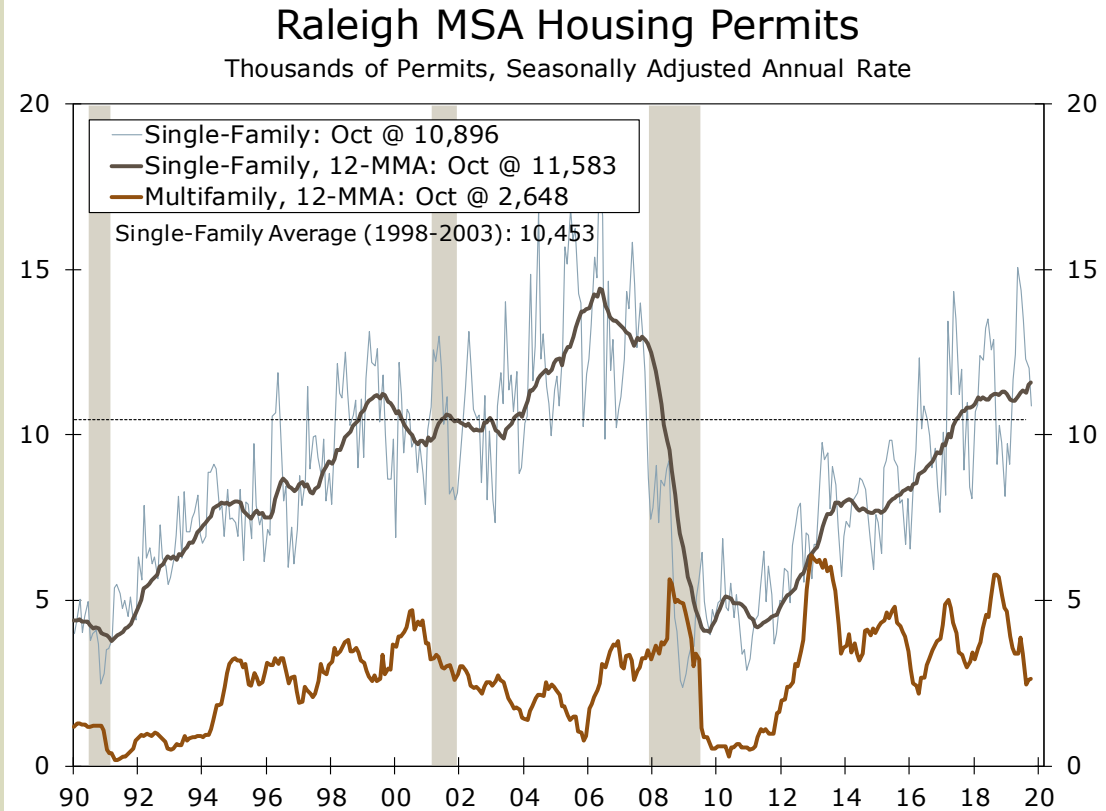
Regional Population Growth  
Year-over-Year Percent Change



Source: U.S. Department of Commerce and Wells Fargo Securities

Residential construction remains strong.

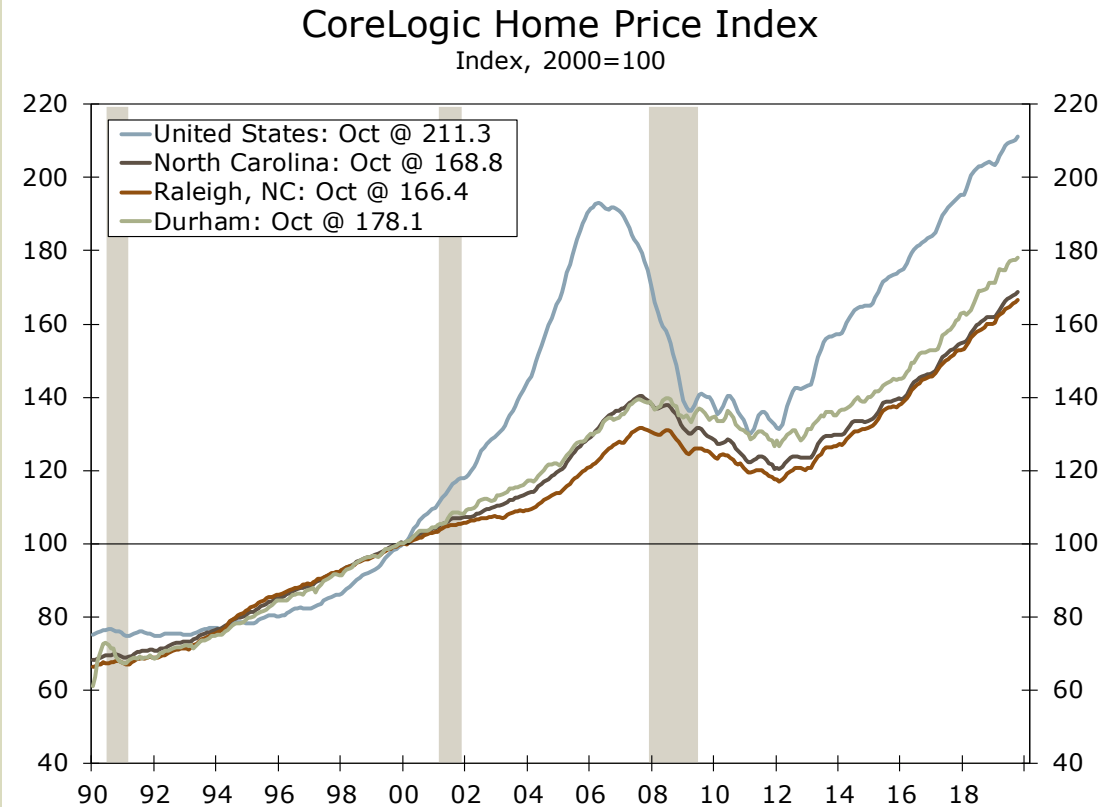
Single-family housing permits exceed their long-run average, which is much stronger than what is occurring nationwide.



Source: U.S. Department of Commerce and Wells Fargo Securities

Home price appreciation has not seen the roller coaster ride that some other parts of the country have. Prices did not fall hard during the housing slump and have rebounded less dramatically than they have nationwide.

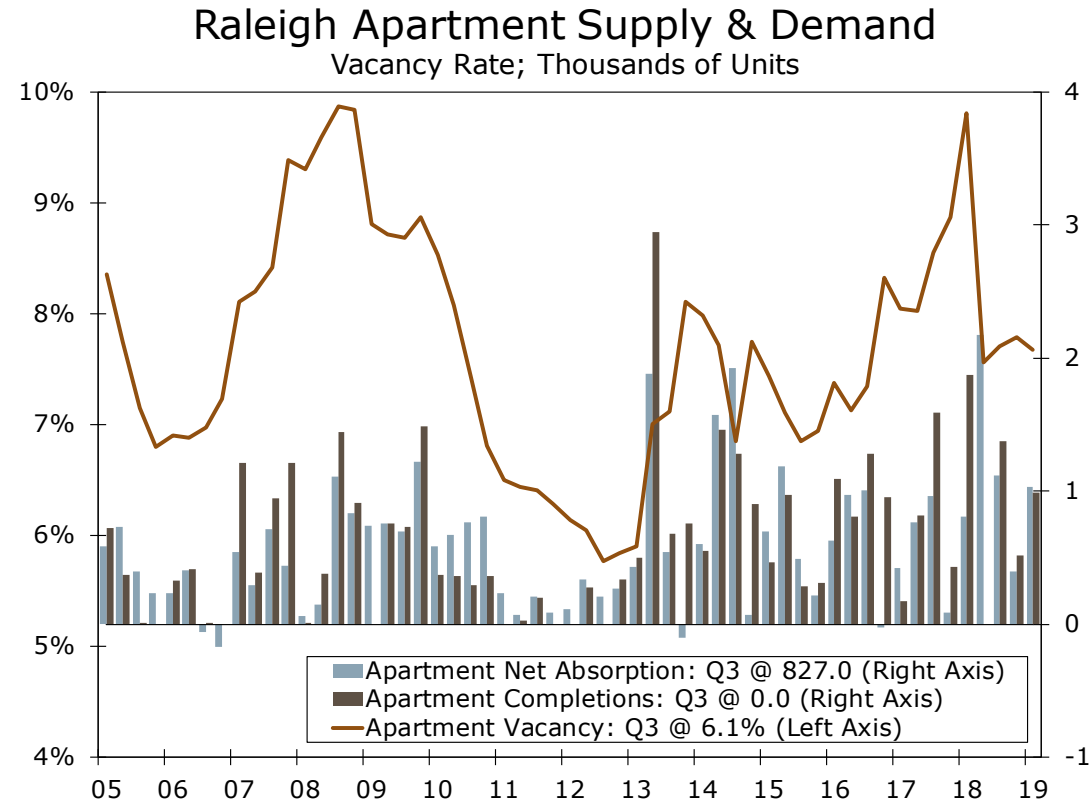
Home prices in Raleigh and Durham have risen past their previous highs, and affordability has become a bigger issue. Home prices are relatively affordable, however, compared to other rapidly growing technology centers.



Source: CoreLogic, Inc. and Wells Fargo Securities

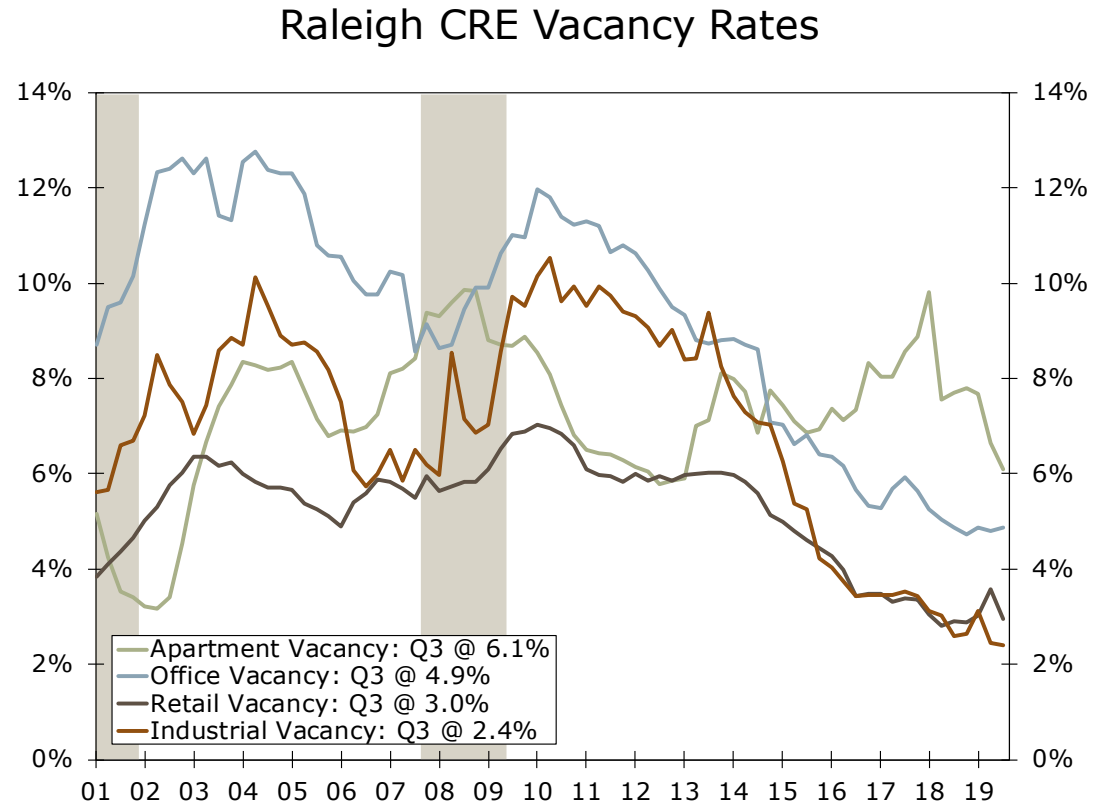


The apartment vacancy has risen modestly amidst a surge in completions. Demand remains strong, however, fueled by the continued influx of job seekers.



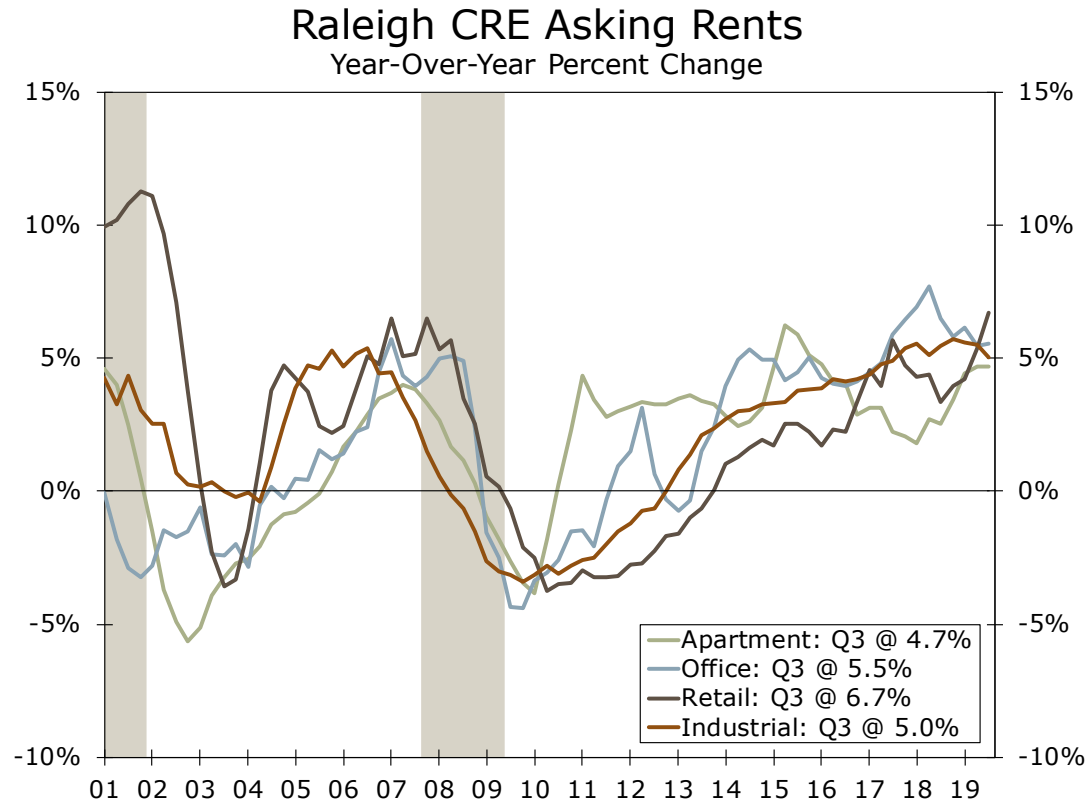
Source: CoStar, Inc. and Wells Fargo Securities

Overall, vacancy rates remain low from a historical perspective.



Source: CoStar, Inc. and Wells Fargo Securities

Rent growth remains solid.



Source: CoStar, Inc. and Wells Fargo Securities

Wells Fargo U.S. Economic Forecast																				
	Actual								Forecast								Actual		Forecast	
	2018				2019				2020				2021				2018	2019	2020	2021
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q				
Real Gross Domestic Product <sup>1</sup>	2.6	3.5	2.9	1.1	3.1	2.0	2.1	1.5	1.4	2.5	2.1	2.3	2.1	2.2	2.4	2.4	2.9	2.3	1.9	2.2
Personal Consumption	1.7	4.0	3.5	1.4	1.1	4.6	2.9	2.1	2.1	2.0	1.9	1.9	1.8	2.1	2.2	2.2	3.0	2.6	2.3	2.0
Business Fixed Investment	8.8	7.9	2.1	4.8	4.4	-1.0	-2.7	2.5	2.2	2.6	3.7	3.8	4.0	3.9	3.9	3.8	6.4	2.3	1.8	3.8
Equipment	6.6	3.4	2.9	7.4	-0.1	0.8	-3.8	1.1	1.4	1.5	2.6	2.9	3.4	3.4	3.2	3.0	6.8	1.6	0.9	3.0
Intellectual Property Products Structures	9.7	11.9	4.1	11.7	10.8	3.6	5.1	6.2	5.1	4.4	5.7	6.0	5.9	5.5	5.6	5.7	7.4	7.8	5.2	5.7
Residential Investment	12.1	11.0	-2.1	-9.0	4.0	-11.1	-12.0	-6.5	-1.5	1.5	2.5	2.0	1.8	1.9	2.0	2.1	4.1	-4.5	-3.2	2.0
Government Purchases	-5.3	-3.7	-4.0	-4.7	-1.0	-3.0	5.1	4.5	4.3	4.5	4.5	4.3	4.0	4.0	3.8	3.5	-1.5	-1.6	4.0	4.1
Net Exports <sup>2</sup>	1.9	2.6	2.1	-0.4	2.9	4.8	1.6	0.5	1.1	1.1	1.0	0.8	0.8	0.8	0.7	0.7	1.7	2.2	1.2	0.9
Inventories <sup>2</sup>	0.0	0.7	-2.1	-0.4	0.7	-0.7	-0.1	0.1	0.0	0.0	-0.2	-0.1	-0.2	-0.1	0.0	0.0	-0.4	-0.3	-0.1	-0.1
Inventories <sup>2</sup>	0.1	-1.2	2.1	0.1	0.5	-0.9	0.2	-0.5	-0.7	0.4	0.1	0.2	0.2	0.0	0.0	0.0	0.1	0.2	-0.2	0.1
Nonfarm Payroll Change <sup>3</sup>	228	243	189	233	174	152	193	184	180	405	-105	10	115	110	110	110	223	176	123	111
Unemployment Rate	4.1	3.9	3.8	3.8	3.9	3.6	3.6	3.6	3.6	3.5	3.6	3.6	3.7	3.7	3.7	3.7	3.9	3.7	3.6	3.7
Consumer Price Index <sup>4</sup>	2.2	2.7	2.6	2.2	1.6	1.8	1.8	2.0	2.4	2.1	2.2	2.2	2.2	2.2	2.2	2.1	2.4	1.8	2.2	2.2
Quarter-End Interest Rates <sup>5</sup>																				
Federal Funds Target Rate	1.75	2.00	2.25	2.50	2.50	2.50	2.00	1.75	1.75	1.75	1.75	1.75	1.75	1.75	1.75	1.75	1.96	2.19	1.75	1.75
Conventional Mortgage Rate	4.44	4.57	4.63	4.64	4.28	3.80	3.61	3.75	3.85	3.85	3.85	3.90	3.95	4.00	4.05	4.10	4.54	3.86	3.86	4.03
2 Year Note	2.27	2.52	2.81	2.48	2.27	1.75	1.63	1.65	1.75	1.80	1.80	1.85	1.90	1.90	1.95	2.00	2.53	1.83	1.80	1.94
10 Year Note	2.74	2.85	3.05	2.69	2.41	2.00	1.68	1.90	2.10	2.15	2.15	2.20	2.25	2.30	2.35	2.40	2.91	2.00	2.15	2.33

Forecast as of: December 18, 2019

<sup>1</sup> Compound Annual Growth Rate Quarter-over-Quarter

<sup>2</sup> Percentage Point Contribution to GDP

<sup>3</sup> Average Monthly Change

<sup>4</sup> Year-over-Year Percentage Change

<sup>5</sup> Annual Numbers Represent Averages

Source: IHS Global Insight and Wells Fargo Securities

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Recent Special Commentary		
Date	Title	Authors
<b>U.S. Macro</b>		
December-19	Budget Bill Leaves Little Room Under the Tree for Santa	Pugliese & Mathews
December-18	Forecast Update: When the Facts Change, We Change Our Minds	Bryson
December-17	Boeing Production Halt Is an About Face for Q1 Growth	Quinlan, House & Seery
December-13	A Phase One Trade Deal is Reached, What Does It Mean?	Quinlan & Seery
December-05	The 2020 Election and the Economy: Part II	Pugliese & Mathews
<b>U.S. Regional</b>		
December-20	Texas Payrolls Soar in November	Vitner & Dougherty
December-20	Florida Posts Modest Payroll Gain in November	Vitner, Dougherty & Honnold
December-20	November Gain for California Payrolls	Vitner & Dougherty
December-20	North Carolina Has Strong Momentum Headed into 2020	Vitner & Dougherty
December-19	Minnesota Payrolls Take a Hit in November	Vitner, Dougherty & Honnold
<b>Global Economy</b>		
December-17	China-Dependent Economies Showing Signs of Stabilization	Pugliese & Bennenbroek
December-13	The Election is Over, but Brexit is Not	Nelson
December-11	2020 International Economic Outlook	Bennenbroek & Licis
December-05	U.K. Election Preview-The Beginning of the End?	Nelson & Licis
December-02	Punting Our ECB Rate Cut Call	Nelson
<b>Interest Rates/Credit Market</b>		
December-20	Is the Fed on the Right Path?	Bryson, Iqbal & Mathews
December-11	Little Drama in Today's FOMC Decision	Bryson
December-03	December Flashlight for the FOMC Blackout Period	Bryson, Quinlan & House
October-30	FOMC Delivers Third Rate Cut in as Many Meetings	Bryson
October-30	Treasury Refunding Highlights	Bryson & Pugliese
<b>Real Estate &amp; Housing</b>		
December-18	Commercial Real Estate Chartbook	Vitner, Dougherty & Honnold
December-05	Housing Maintains Solid Momentum Headed into 2020	Vitner, Dougherty & Honnold
November-18	Apartment Market Outlook	Vitner, Dougherty & Honnold
November-07	Housing Chartbook: November 2019	Vitner, Dougherty & Honnold
October-17	Q3 CRE Chartbook	Vitner, Dougherty & Honnold

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