Economic Outlook

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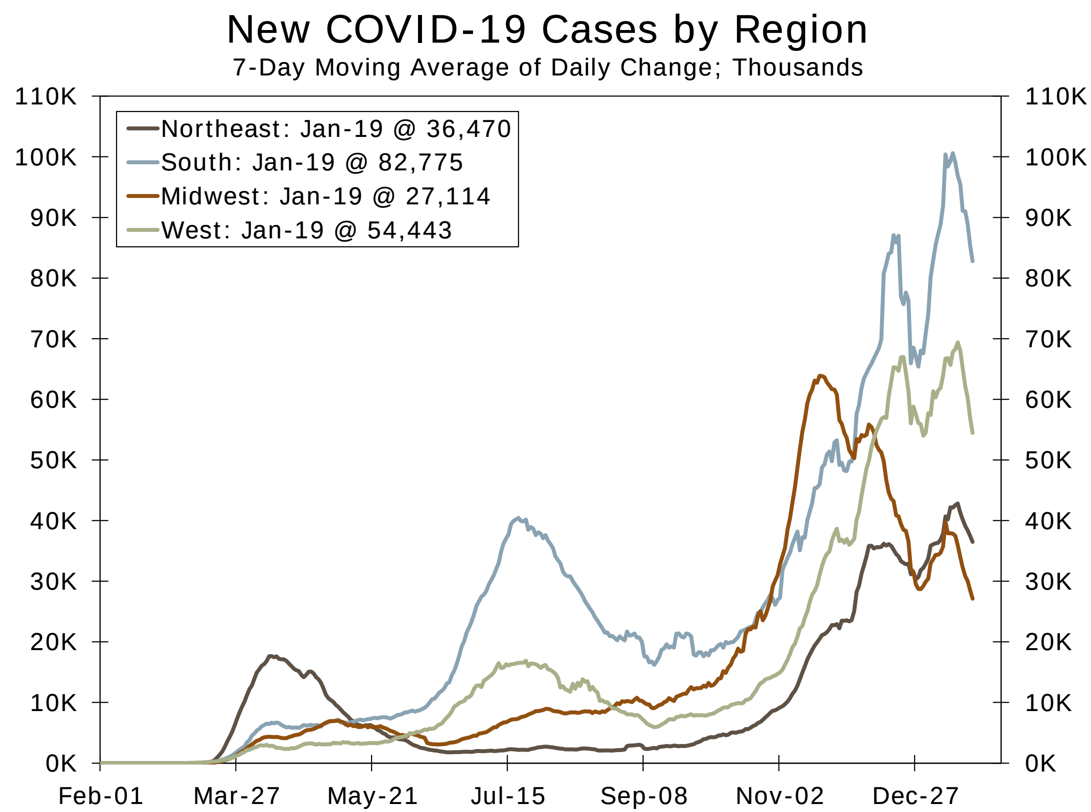
January 2021

Economic Outlook	The recently enacted stimulus package should help smooth over what will still be a challenging next few months for the U.S. economy. There is some near-term downside risk to growth but 2021 should be a better year.
High-Frequency Insights	With COVID spiking, people are spending more time at home. High-frequency data show activity has slowed at restaurants and small businesses. Travel picked up around the holidays but in-person shopping did not.
The Resurgence in COVID Cases	We are approaching the height of the cold and flu season and hospitalizations are spiking. While another lockdown seems unlikely, local lockdowns and independent actions by businesses will slow growth in coming weeks.
The Geography of Economic Growth is Changing	There continues to be a significant move away from large, globally connected urban areas. The suburbs and exurbs are booming in many parts of the country. Businesses are adjusting to this shift in preferences.
Housing is Set to Strengthen Further	Single-family housing is leading the recovery, thanks to low mortgage rates and the desire for more space. The shift to at-home work, education and entertainment will have lasting and far-reaching impacts.

Hospitals across the country are reaching capacity limits as coronavirus cases surged over the holidays.

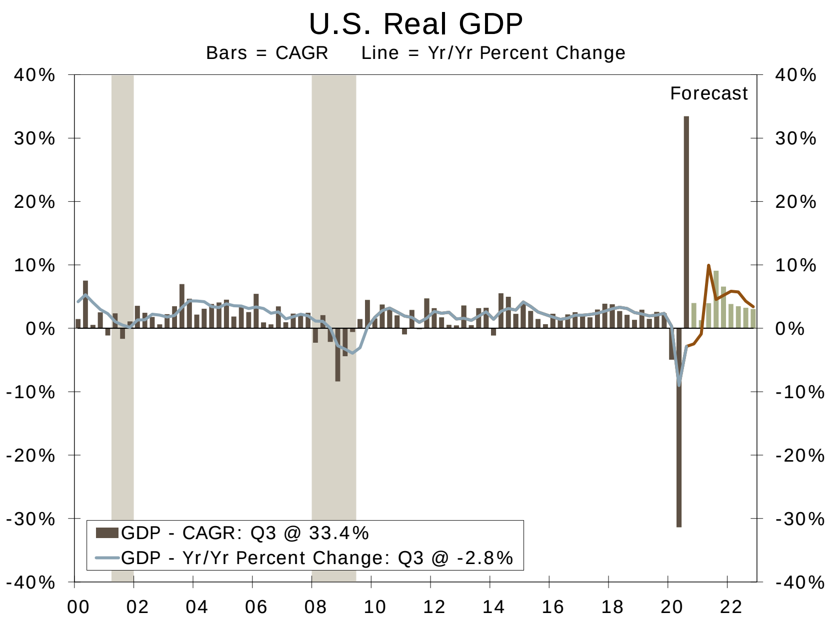
The increasing likelihood of regional lockdowns poses a risk to near-term economic growth.



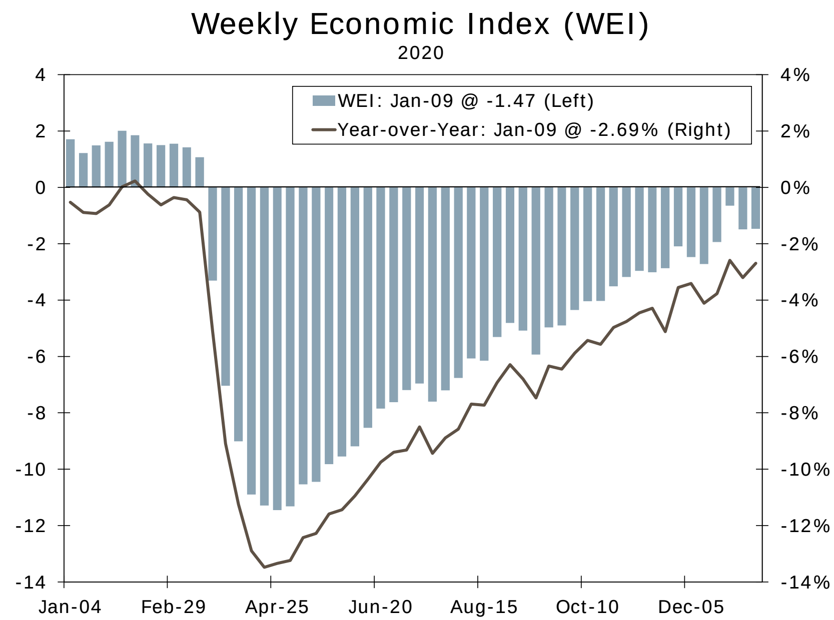
Source: Bloomberg LP and Wells Fargo Securities

Real GDP growth swung back into positive territory during the third quarter, as consumer spending, homebuilding and business fixed investment came roaring back. Aggregate measures of high-frequency data series suggest real GDP is still growing.

Blowout Q3 GDP



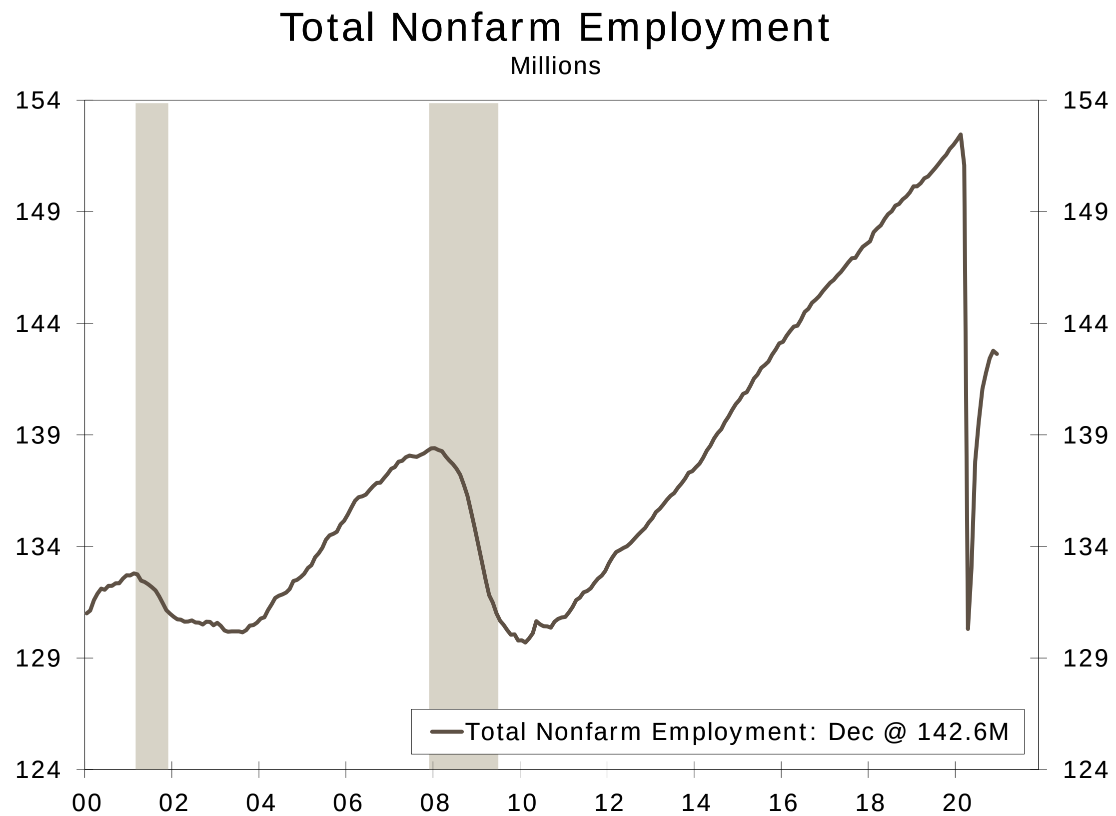
Recent Activity Moderating



Source: U.S. Department of Commerce, Federal Reserve Bank of Dallas and Wells Fargo Securities

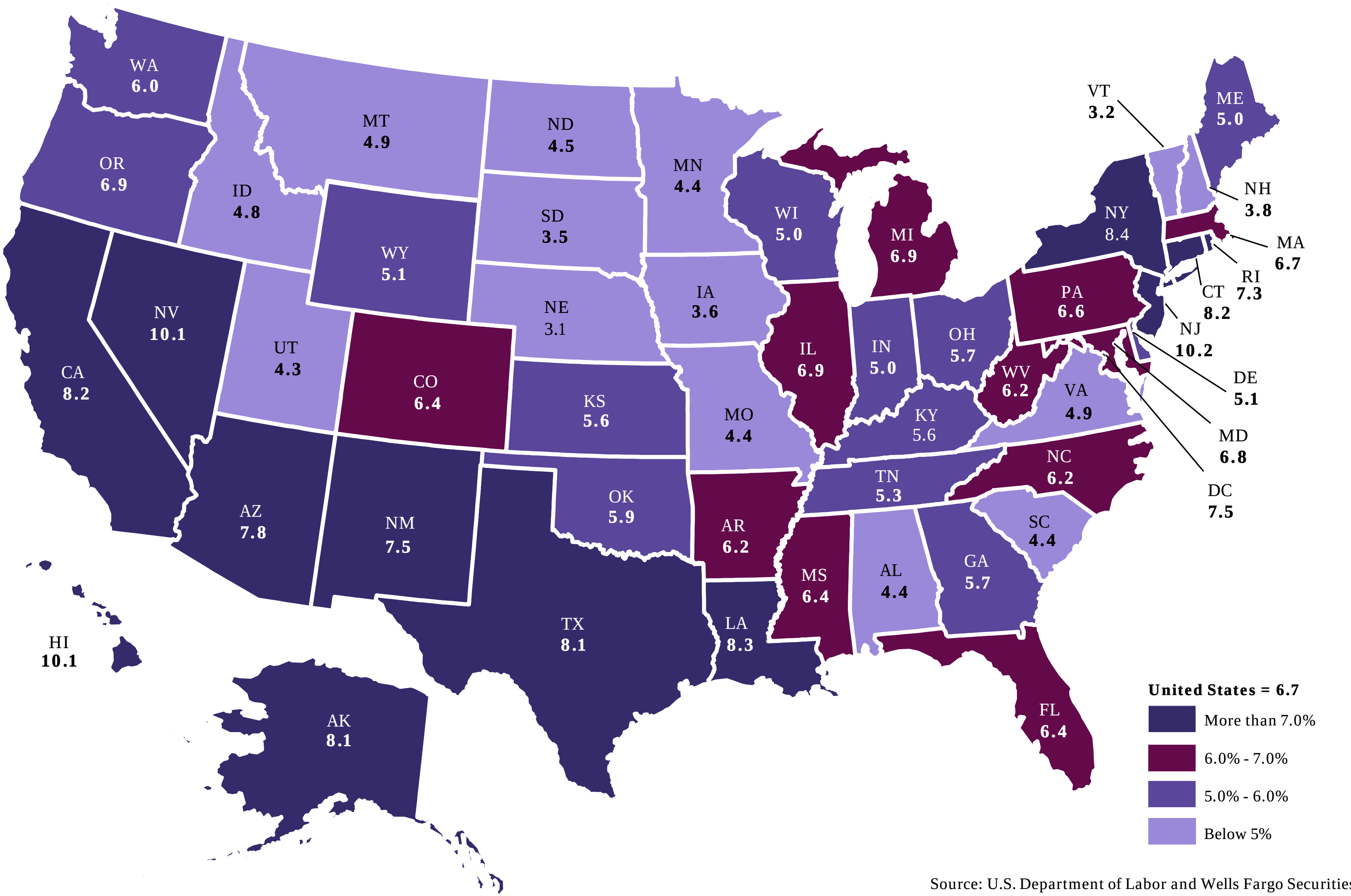
Strains of the latest COVID surge are taking a toll on the labor market. Nonfarm payrolls declined by 140K in December, marking the first contraction since April.

Much of the remaining 9.8 million job shortfall is in high-contact areas, such as restaurants, bars, travel and entertainment. Employment in the leisure & hospitality sector fell by nearly half a million jobs in December. By contrast, manufacturing, construction, logistics and tech all posted solid job gains.



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

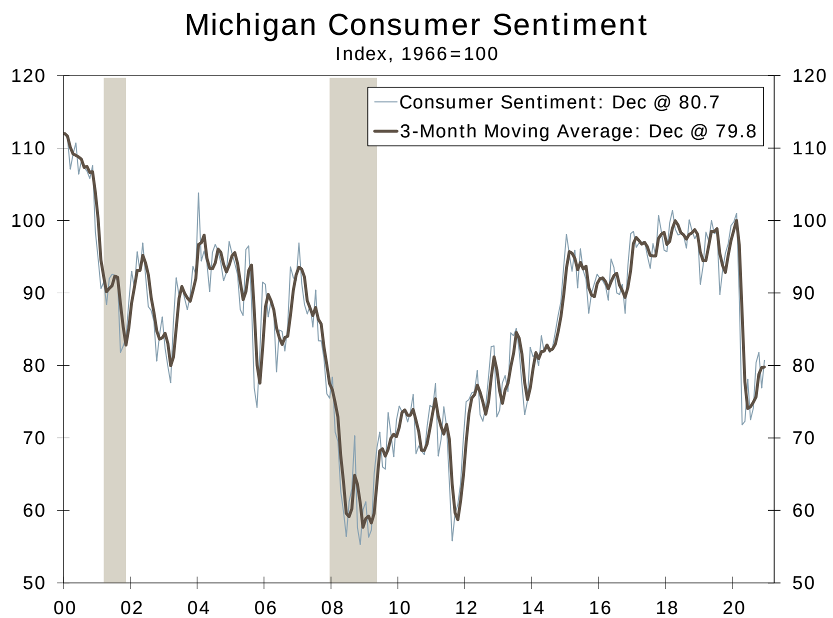
Unemployment Rate by State – November 2020



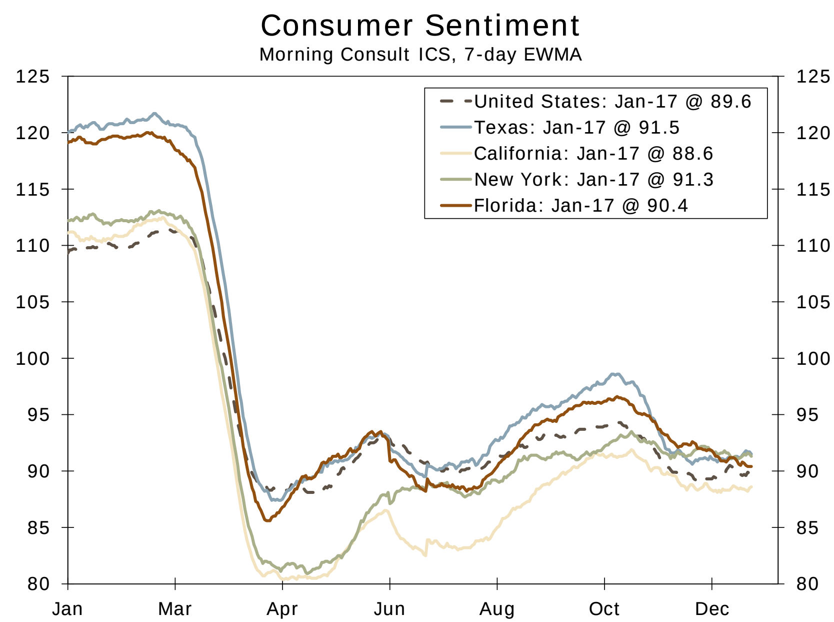
Source: U.S. Department of Labor and Wells Fargo Securities

Consumer sentiment ticked up in December as consumers' expectations were more upbeat than assessments of current economic conditions. Consumer confidence is highly coincident with overall economic activity and will be one of the first indicators to signal that economic growth is accelerating again. For now, however, the data show the economy losing momentum.

Uptick in Overall Sentiment

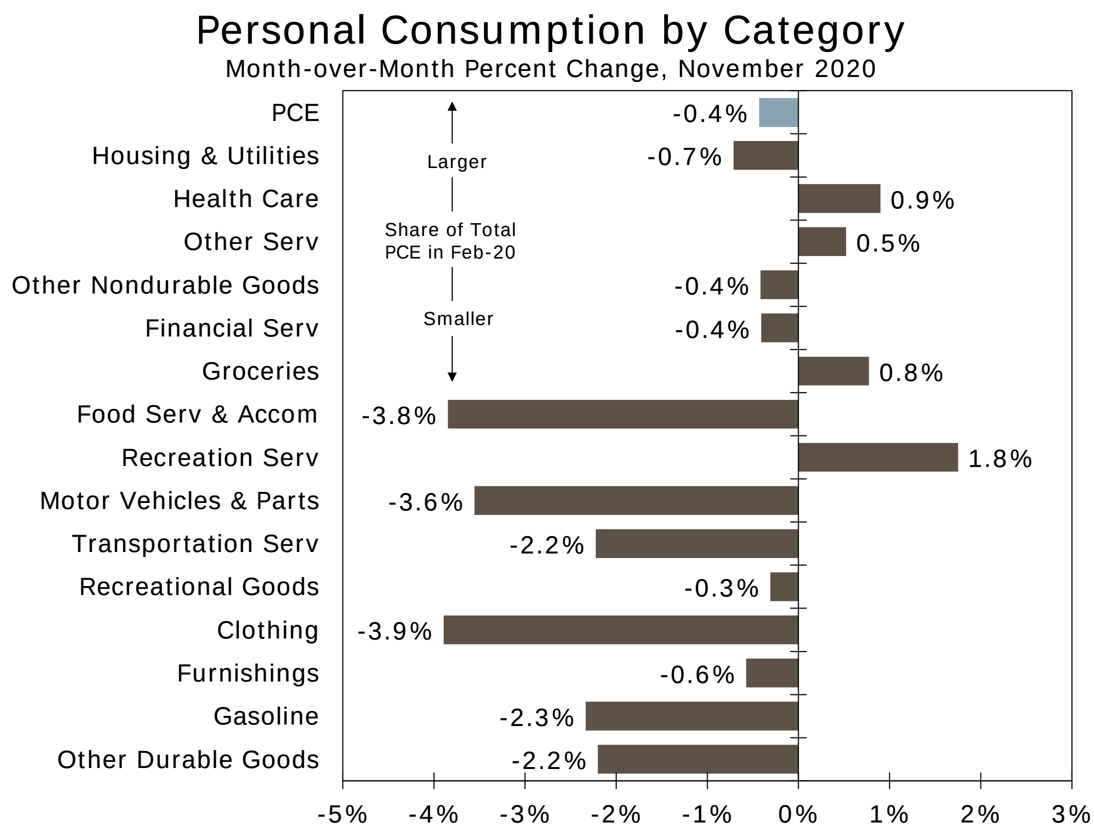


Lost Momentum in Regional Confidence



Source: University of Michigan, Morning Consult and Wells Fargo Securities

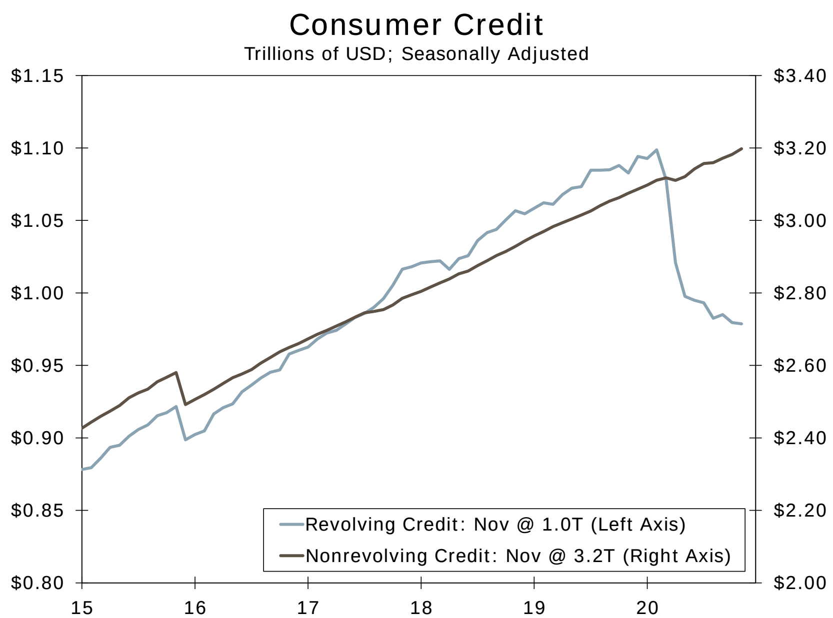
Personal spending has weakened amid fading fiscal stimulus. Every major category of goods consumption declined in November, except for groceries, which points to a greater degree of vulnerability than we would have expected.



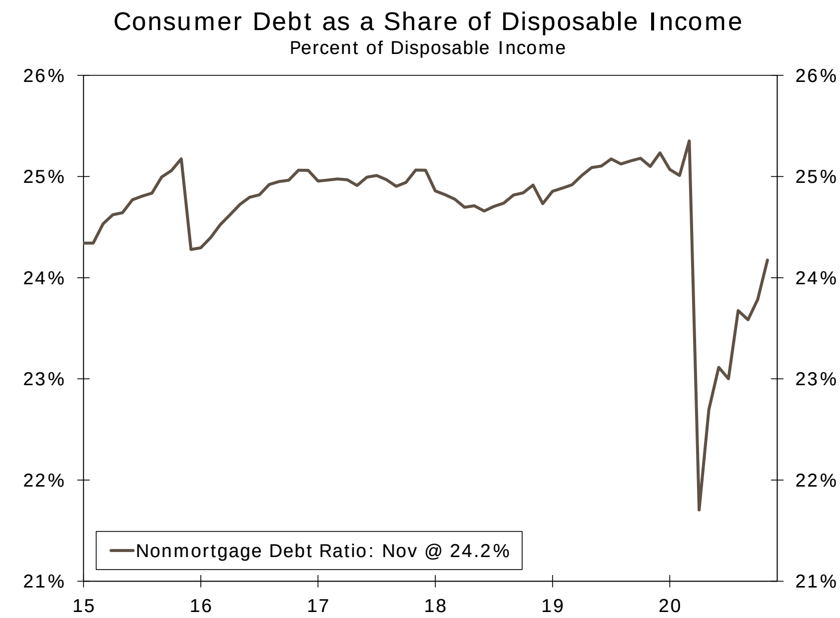
Source: U.S. Department of Commerce and Wells Fargo Securities

Revolving (mostly credit card) consumer debt continues to decline. The ratio of nonmortgage consumer credit to disposable personal income rose to 24.2% in November, however, as income fell amid slower job growth and the diminishing impact of fiscal stimulus.

Declining Credit Card Debt



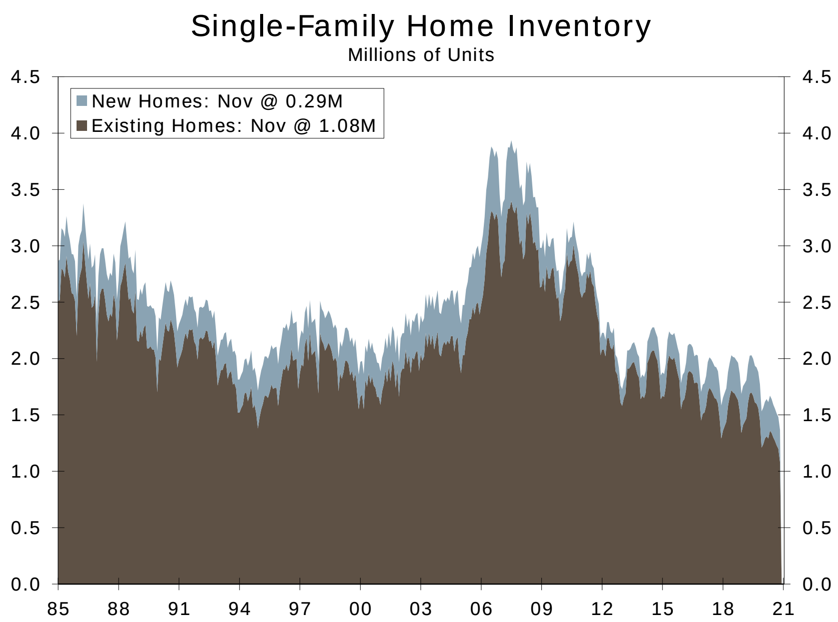
Debt/Income Ratio is Normalizing



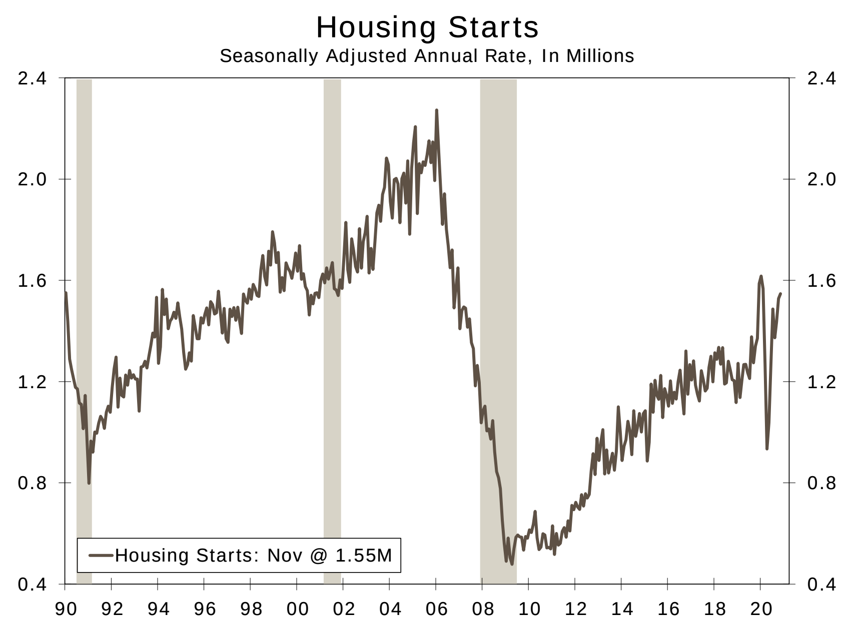
Source: IHS Markit and Wells Fargo Securities

The supply of housing has been disrupted. While more people want to buy homes, fewer want to sell them. The supply curve has shifted inward and the inventory of homes for sale has fallen to an all-time low. Housing starts have moderated recently, reflecting supply shortages.

Record-Low Inventory

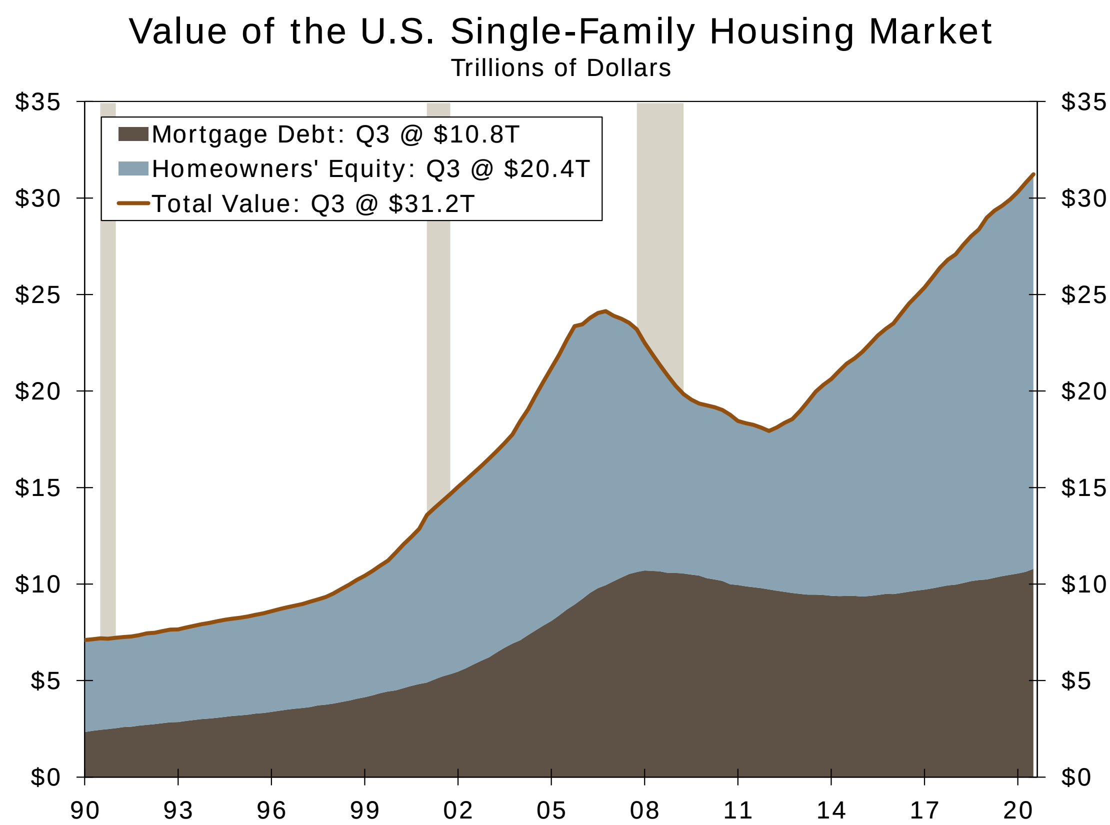


Rising Housing Starts



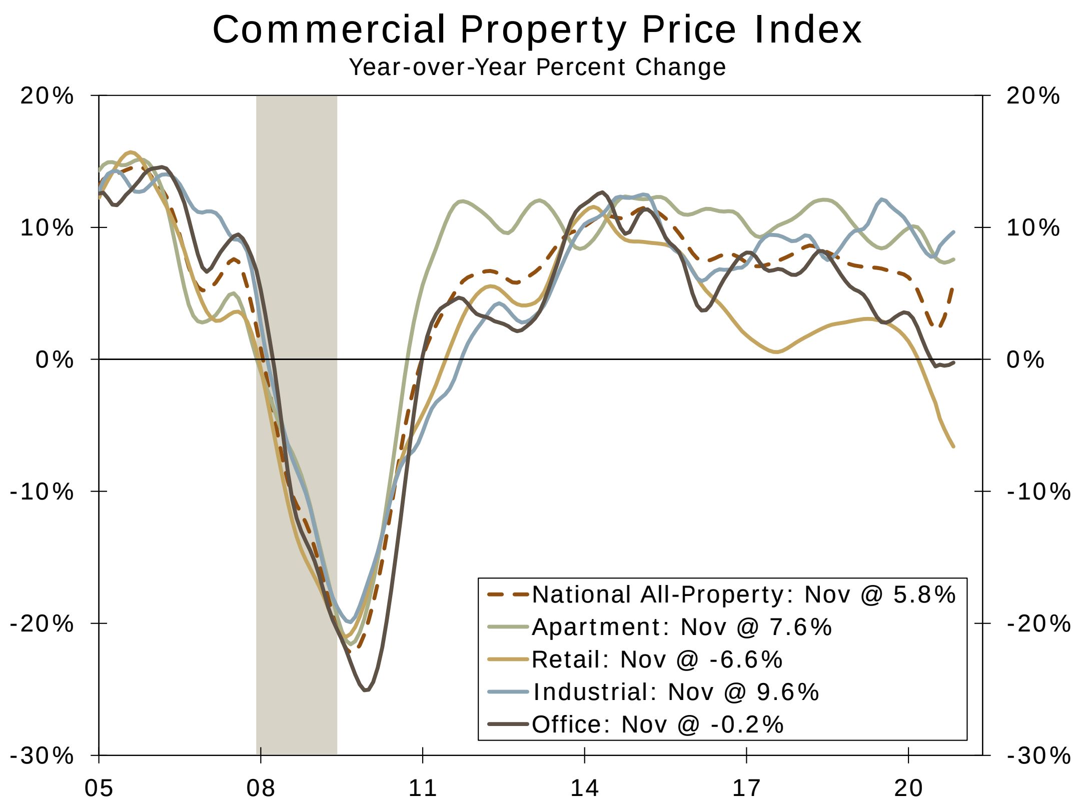
Source: U.S. Department of Commerce, National Association of Realtors and Wells Fargo Securities

Federal Reserve data show single-family home equity at record $20.4 trillion, or nearly two-thirds of single-family housing values.



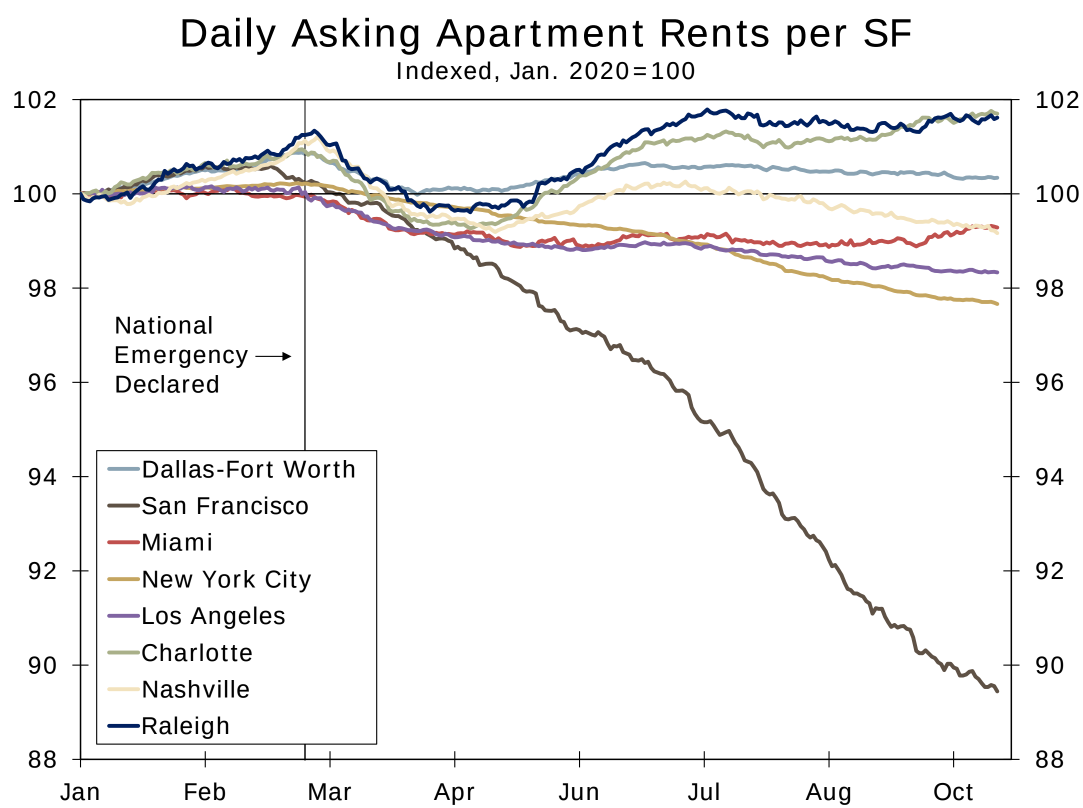
Source: Federal Reserve Board and Wells Fargo Securities

Commercial property price indices have weakened on concerns about the reshuffling of the retail landscape and uncertainty about the persistence of remote working.



Source: Real Capital Analytics and Wells Fargo Securities

Many apartment owners in higher-cost metros have lowered rents aggressively as tenants have fled these regions in the wake of the pandemic.

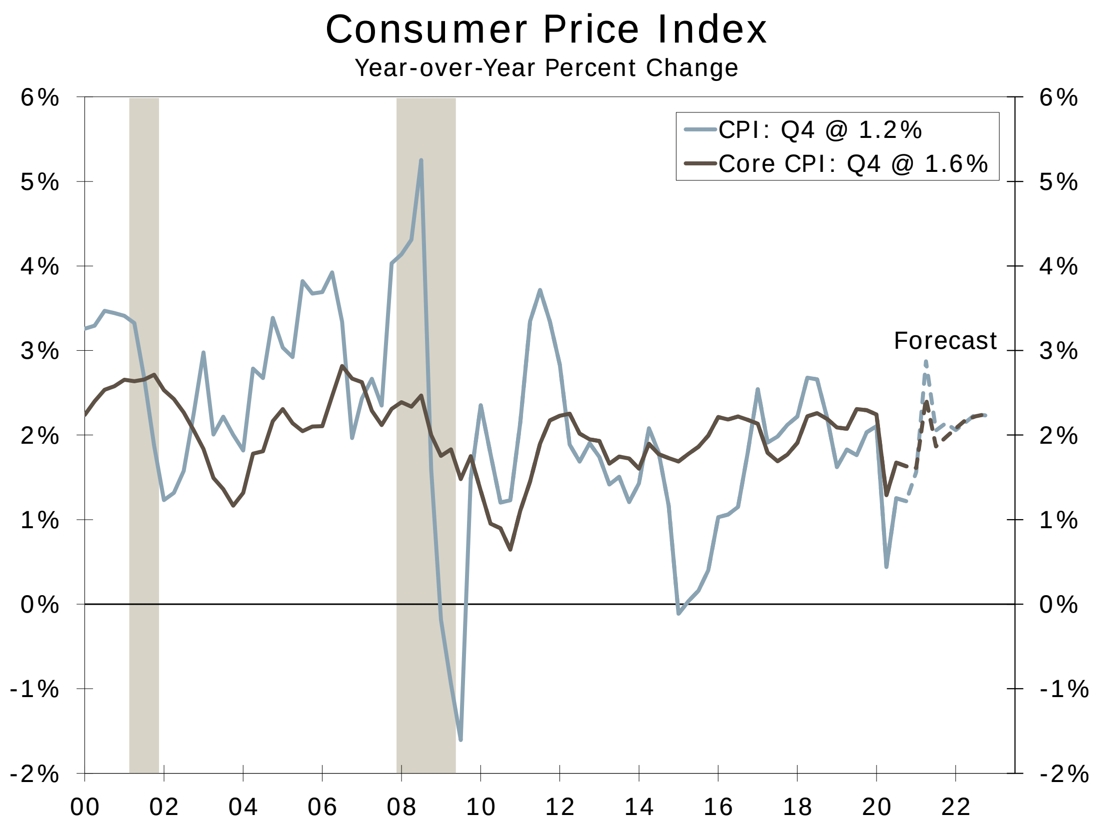


Source: CoStar Inc. and Wells Fargo Securities

We may be poised for a snap back in inflation, if the vaccines unleash pent-up demand.

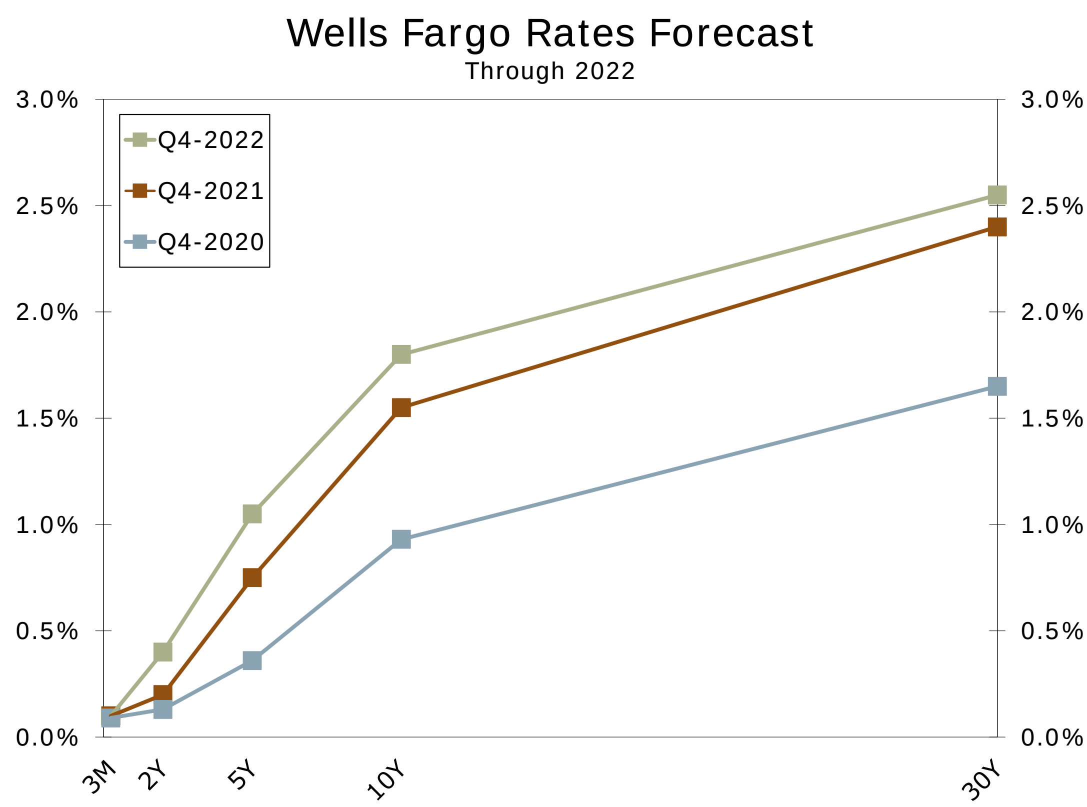
We expect inflation to rise in coming months due to base effects, or year-over-year changes against the sharp declines seen one year ago, at the onset of the pandemic.

COVID has also led to labor and parts shortages, which is keeping inventories lean and adding to near-term price pressures.



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

While interest rates will likely remain low for quite some time, we expect the yield curve to steepen once the pandemic is safely behind us.



Source: IHS Markit and Wells Fargo Securities

Phase 5: COVID Relief Bill (CARES Act "lite")

$900B

~4.8% of GDP

Status: **Passed.** Became law on December 27, 2020.

Targeting: **Direct checks, unemployment insurance, more money to small businesses**

- Direct payments of **$600** to individuals making <$75,000 and **$1,200** to couples making <$150,000, plus a **$600** per child bonus (~$160B total)
- Enhanced unemployment benefits
  - **PEUC**—benefits extended for **24 weeks** (13 previously) to people who exhausted all regular state benefits
  - **PUA**—benefits extended to **50 weeks** (39 previously) to people who are not usually eligible for benefits
  - **PUC**—PUC provides enhanced benefit with an extra $300/week for those receiving jobless benefits until Mar. 14.
- **$285B** additional support for Paycheck Protection Program (PPP) loans
- **$40B** in Economic Injury Disaster Loan advances, emergency grants to entertainment venues and other assorted small business relief
- Conditional funding to a variety of state and local services (no direct grants) such as: K-12 education (**+$54B**), higher education (**+$23B**), transit agencies (**+$14B**) and highway transportation (**+$10B**)
- Extends authority to spend the $150B given to state and local governments in the CARES Act through 2021.
- Farm aid (**+$11B**), airline payroll support (**+$15B**), loan forgiveness for the United States Postal Service (**+$10B**) and health care measures (**+$60B**)

Source: U.S. House of Representatives website and Wells Fargo Securities

Wells Fargo Securities U.S. Economic Forecast

	Actual							Forecast									Actual	Forecast		
	2019				2020				2021				2022				2019	2020	2021	2022
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q				
Real Gross Domestic Product [1]	2.9	1.5	2.6	2.4	-5.0	-31.4	33.4	4.0	1.3	4.0	9.1	6.6	3.8	3.5	3.2	3.0	2.2	-3.5	4.6	4.8
Personal Consumption	1.8	3.7	2.7	1.6	-6.9	-33.2	41.0	4.0	-1.0	5.6	11.7	7.9	4.1	3.9	3.7	3.5	2.4	-3.8	5.2	5.7
Business Fixed Investment	4.2	0.0	1.9	-0.3	-6.7	-27.2	22.9	14.0	2.6	2.2	4.1	5.9	5.7	4.9	4.6	4.3	2.9	-4.0	5.0	4.9
Equipment	2.0	-3.8	-1.7	-1.7	-15.2	-35.9	68.2	18.9	1.9	1.3	3.9	7.1	6.9	5.3	5.0	4.4	2.1	-5.3	8.7	5.5
Intellectual Property Products	4.5	4.1	5.3	4.6	2.4	-11.4	8.4	7.5	4.0	5.2	6.9	6.3	6.0	5.6	5.1	4.9	6.4	1.6	4.9	5.8
Structures	8.2	1.6	3.6	-5.3	-3.7	-33.6	-17.4	3.5	1.5	-1.5	-1.1	1.5	1.9	2.1	2.5	2.8	-0.6	-10.5	-4.3	1.4
Residential Investment	-1.7	-2.1	4.6	5.8	19.0	-35.6	63.0	26.0	7.5	7.5	14.0	12.0	9.0	7.0	6.5	6.5	-1.7	5.5	13.9	9.2
Government Purchases	2.5	5.0	2.1	2.4	1.3	2.5	-4.8	-3.2	3.5	-2.8	1.9	1.1	0.8	0.5	0.5	0.5	2.3	1.0	-0.5	0.6
Net Exports [2]	0.6	-0.8	0.0	1.5	1.1	0.6	-3.2	-1.6	0.0	0.2	-0.2	-0.3	-0.3	-0.3	-0.4	-0.4	-0.2	0.0	-1.0	-0.3
Inventories [2]	0.2	-1.0	-0.1	-0.8	-1.3	-3.5	6.6	1.4	0.7	-0.2	-0.2	-0.1	0.0	0.0	0.0	0.0	0.0	-0.7	0.9	-0.1
Nonfarm Payroll Change [3]	139	159	203	210	-303	-4427	1322	283	233	600	683	392	300	247	230	215	178	-781	477	248
Unemployment Rate	3.9	3.7	3.6	3.6	3.8	13.1	8.8	6.8	6.6	6.4	6.0	5.7	5.4	5.1	4.8	4.5	3.7	8.1	6.2	5.0
Consumer Price Index [4]	1.6	1.8	1.8	2.0	2.1	0.4	1.3	1.2	1.6	2.9	2.1	2.1	2.1	2.2	2.2	2.2	1.8	1.2	2.2	2.2
Quarter-End Interest Rates [5]																				
Federal Funds Target Rate	2.50	2.50	2.00	1.75	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	2.25	0.50	0.25	0.25
Conventional Mortgage Rate	4.28	3.80	3.61	3.72	3.45	3.16	2.89	2.69	2.95	3.10	3.15	3.25	3.35	3.40	3.45	3.50	3.94	3.12	3.11	3.43
2 Year Note	2.27	1.75	1.63	1.58	0.23	0.16	0.13	0.13	0.15	0.15	0.20	0.20	0.25	0.25	0.30	0.40	1.97	0.39	0.18	0.30
10 Year Note	2.41	2.00	1.68	1.92	0.70	0.66	0.69	0.93	1.20	1.35	1.45	1.55	1.65	1.70	1.75	1.80	2.14	0.89	1.39	1.73

Forecast as of: January 13, 2021

[1] Compound Annual Growth Rate Quarter-over-Quarter [2] Percentage Point Contribution to GDP [3] Average Monthly Change

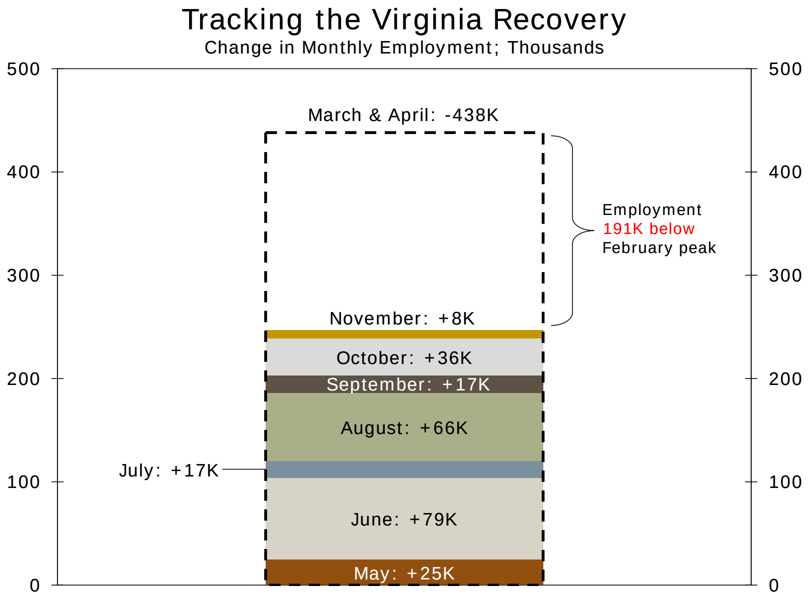
[4] Year-over-Year Percentage Change [5] Annual Numbers Represent Averages

Source: IHS Markit and Wells Fargo Securities

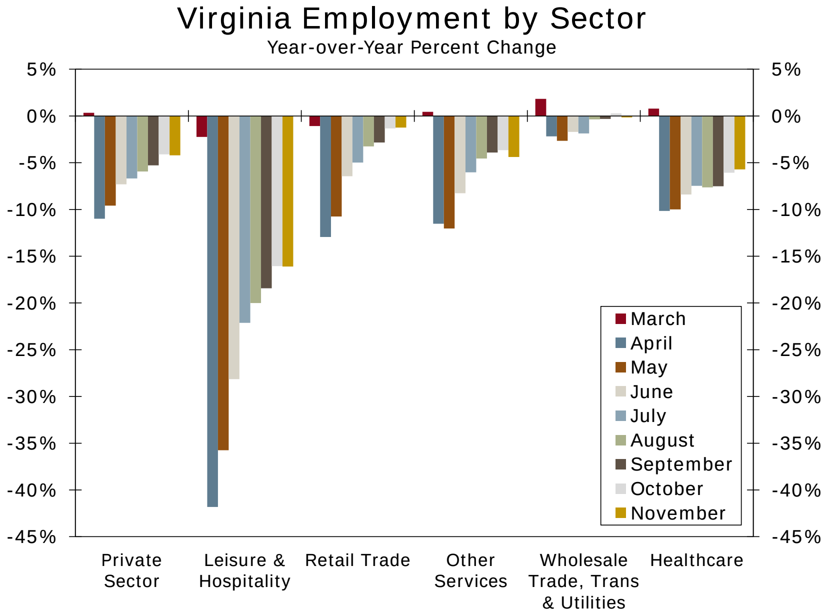
Regional Commentary

Employers added 8,000 jobs in November, while the unemployment rate fell to 4.9%. Job growth will likely cool further in coming months but should rebound this spring, as vaccines rollout across the country.

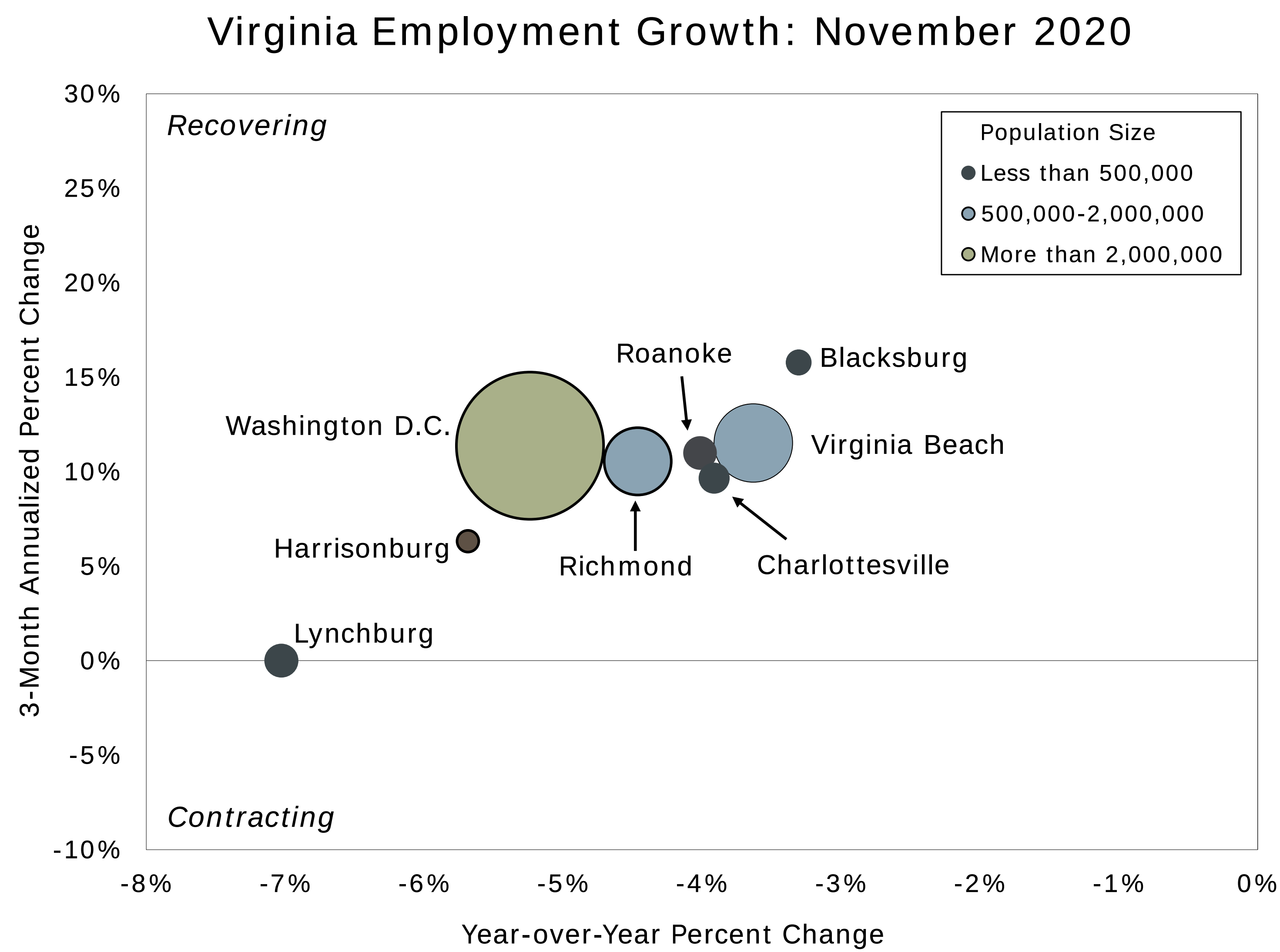
Employment Since March



High-Contact Sectors Reeling



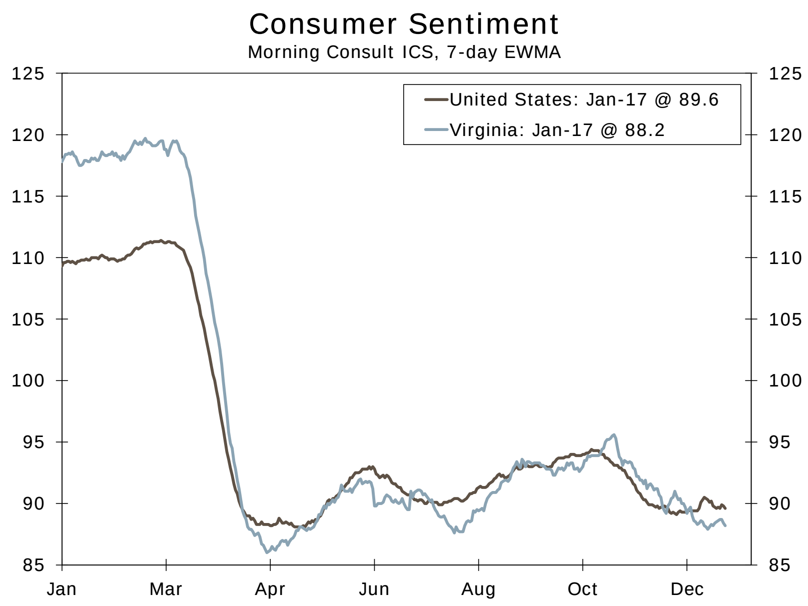
Source: U.S. Department of Labor and Wells Fargo Securities



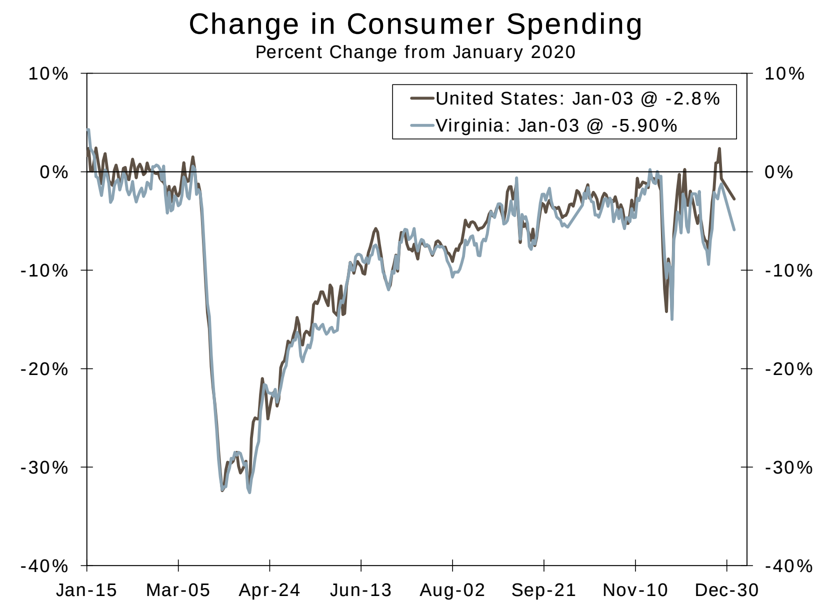
Source: U.S. Department of Labor and Wells Fargo Securities

According to high-frequency indicators, improvement in Virginia consumer sentiment lost momentum in December and now trails the national average. Total spending by Virginia consumers is predicted to be 5.9% below where it was at the beginning of the year.

Sentiment Behind National Average

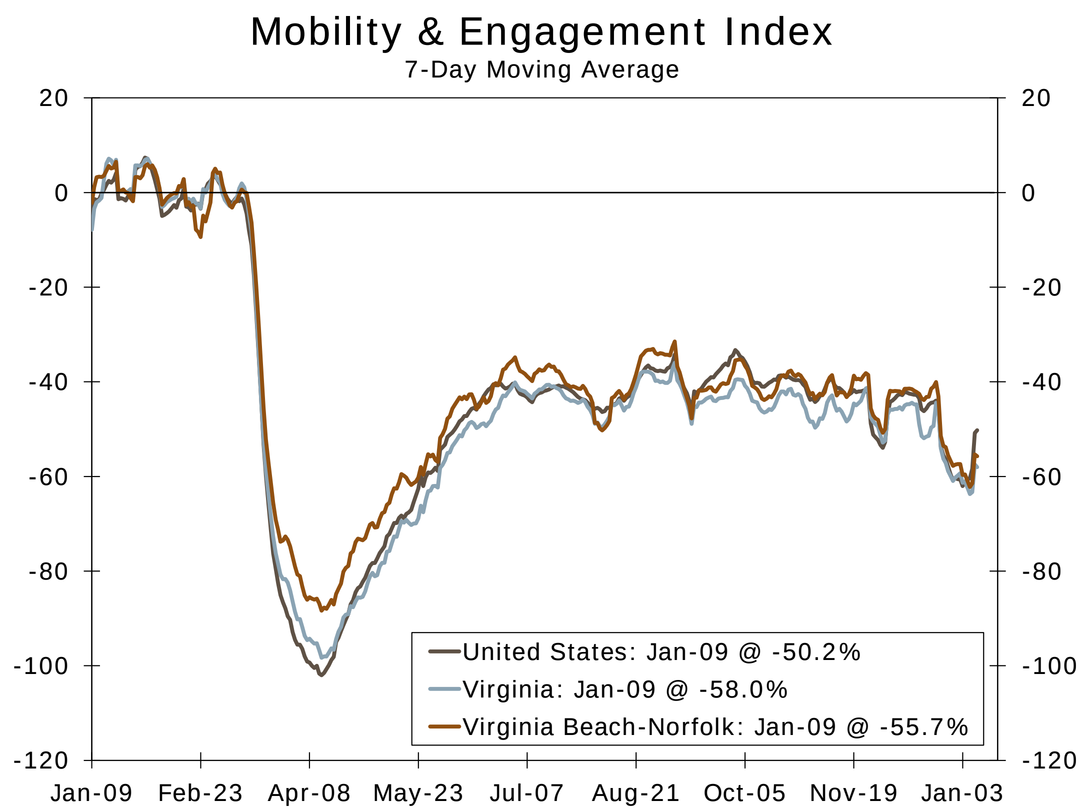


Spending Picked Up Around the Holidays



Source: Morning Consult, Opportunity Insights and Wells Fargo Securities

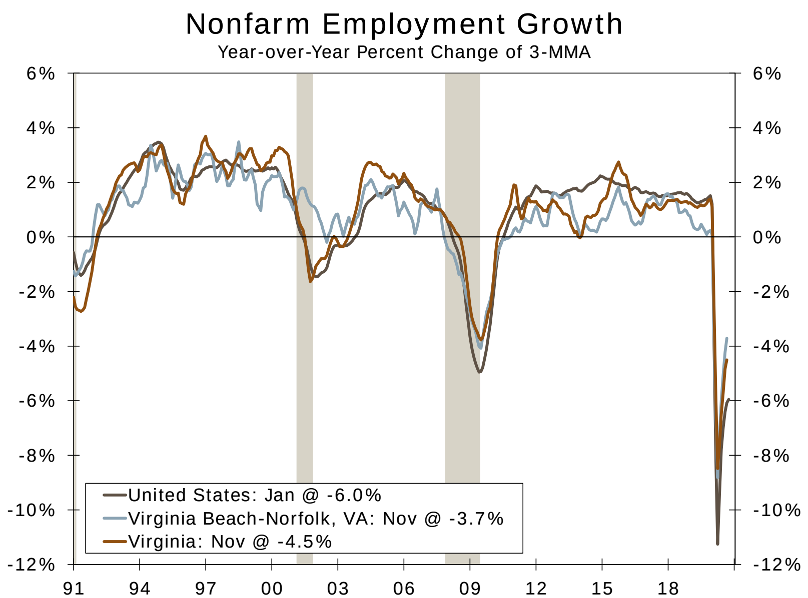
Mobility and economic engagement (measured by geolocation data from mobile devices) is gaining momentum, but remains well below its pre-pandemic level.



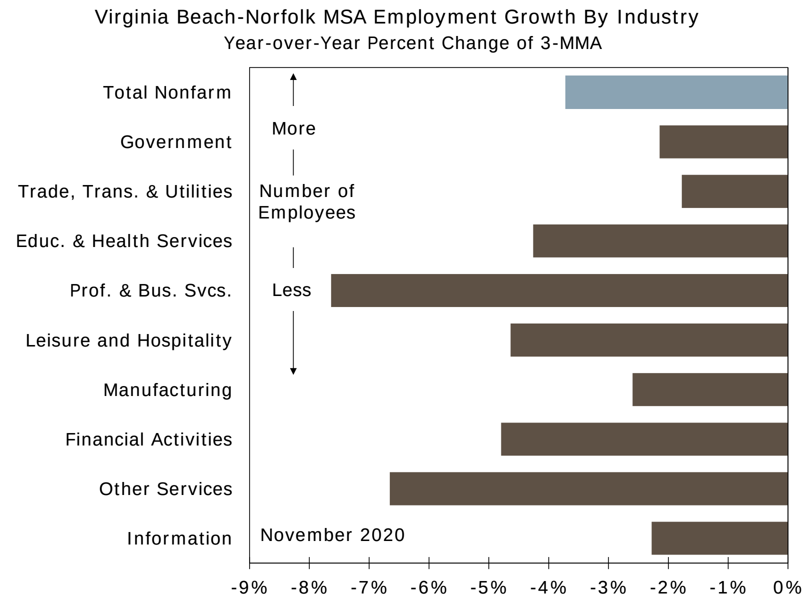
Source: Federal Reserve Bank of Dallas and Wells Fargo Securities

Virginia Beach's economy continues to gradually regain ground lost to COVID induced lockdowns. Employers have recouped just under 70% of the jobs lost in March and April.

Employment Growth Moderating

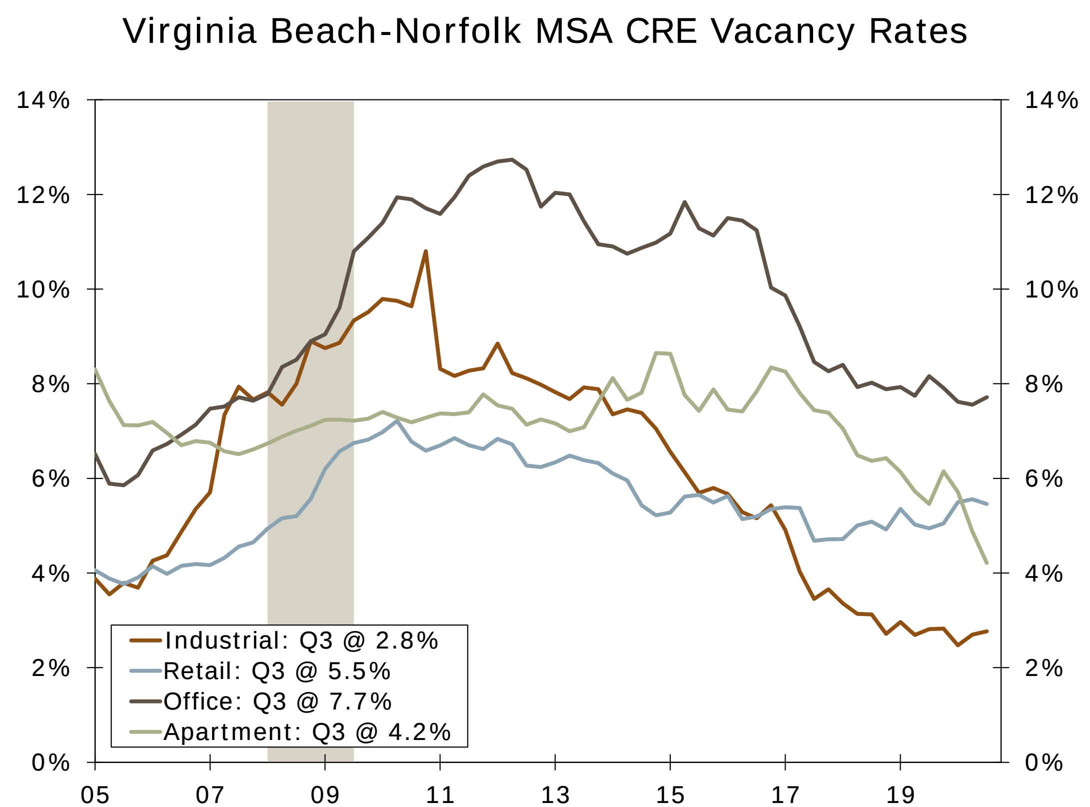


Prof. & Bus. Services Slow to Recover



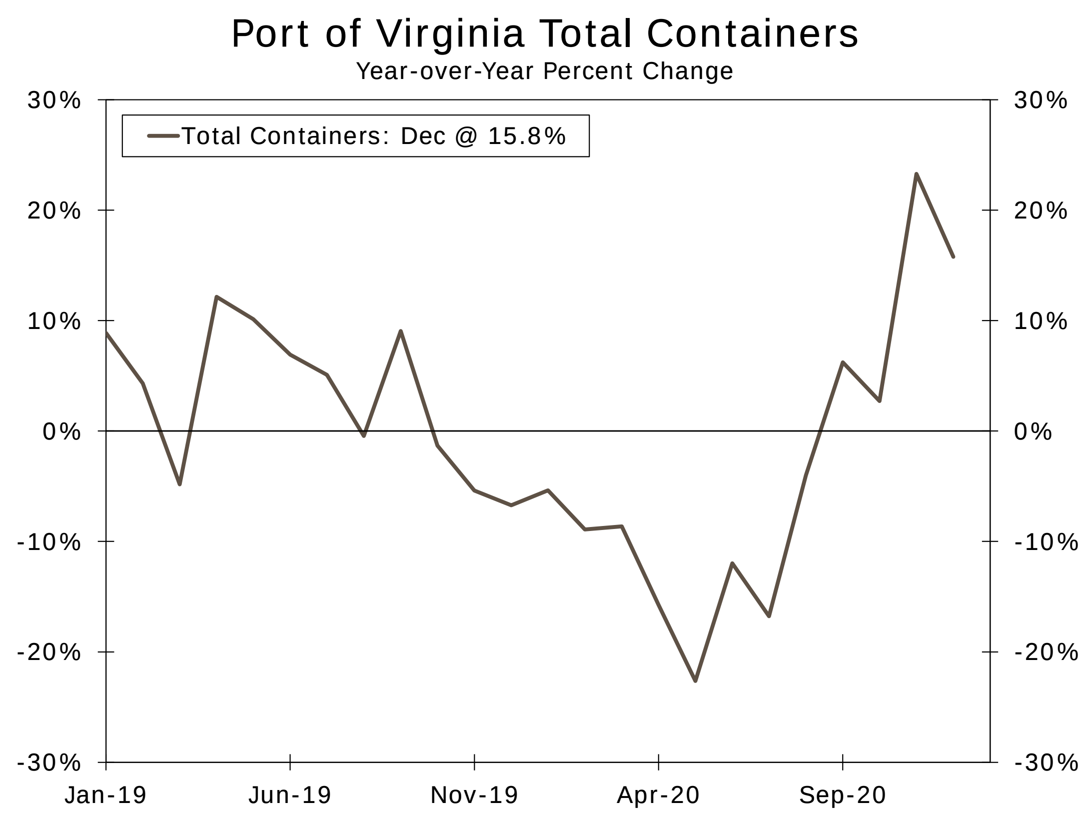
Source: U.S. Department of Labor and Wells Fargo Securities

Apartment vacancy rates fell to 4.2% in Q3-2020, down from 4.9% the prior quarter, as some of the pent-up rental demand from last spring's lockdowns were unleashed.



Source: CoStar Inc. and Wells Fargo Securities

Activity at the Port of Virginia has risen above prior-year levels following last spring's lockdowns.



Source: Bloomberg LP and Wells Fargo Securities

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