

# U.S. QUARTERLY STATE FORECAST



## TD Economics

June 27, 2013

### New England

- New England's economy underperformed the nation by a full percentage point last year. This theme will persist over the next two years, but to a lesser extent. Helped by a broadening recovery in housing, growth will accelerate to 1.6% this year, before picking up to 2.5% in 2014.

### Middle Atlantic

- After growing by 1.4% last year, the Middle Atlantic economy will advance by 1.6% this year and 2.0% in 2014. Post-Sandy rebuilding will boost construction activity this year, helping to offset weakness in the finance & insurance, manufacturing and government sectors.

### Upper South Atlantic

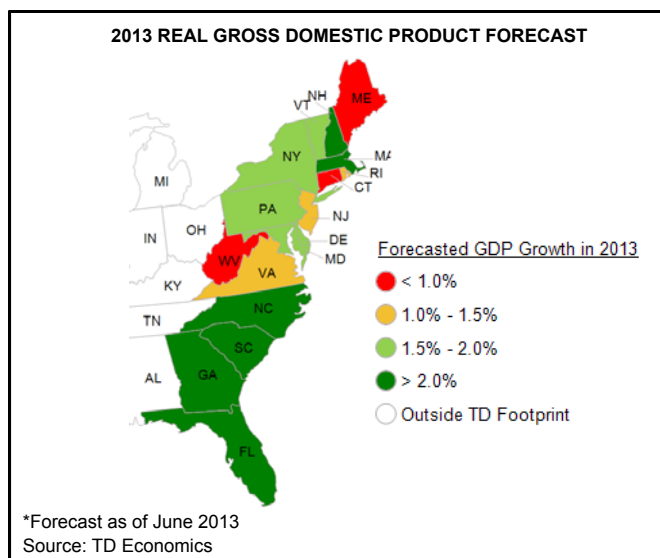
- The Upper South Atlantic region has underperformed since the recession. With fiscal consolidation in full swing, this is likely to continue. Government and professional & business services weigh on economic growth this year, slowing real GDP to 1.7%. As fiscal clouds clear, the region should nearly catch up to the nation, advancing by 2.7% in 2014.

### Lower South Atlantic

- The Lower South Atlantic outpaced the nation for the first time in five years, growing by 2.4% in 2012. The pace of economic growth should hold up at 2.3% this year and accelerate to 3.2% in 2014, amid rising national economic strength and favorable regional population dynamics.

### U.S. Macro Themes

- The outlook for the U.S. economy is framed by the increasing resiliency and confidence of its private sector up against ongoing fiscal consolidation and relatively weak global growth. The result is an economy likely to grow by 1.9% in 2013, but improve to 2.8% in 2014 as these weights lift.
- Home price growth continued to accelerate through early-2013 and reached 12% y/y in April. It is likely to decelerate as more supply is brought on line, but will continue to support consumer spending through the forecast horizon.
- Increased economic optimism has pulled forward expectations for the Federal Reserve to end asset purchases. With fiscal drag weighing on near-term growth alongside weak inflation, the Fed is likely to begin tapering its program later this year and end purchases outright in 2014.



TD State Forecasts															
	Real GDP (% Chg.)			Employment (% Chg.)			Unemployment Rate (average, %)			Housing Starts (thousands)			Home Prices (% Chg.)		
	2012A	2013	2014	2012A	2013	2014	2012A	2013	2014	2012A	2013	2014	2012A	2013	2014
<b>National</b>	2.2	1.9	2.8	1.7	1.6	1.8	8.1	7.5	7.1	783	985	1,207	3.7	9.4	3.7
New England	1.2	1.6	2.5	1.1	1.1	1.1	7.2	6.8	6.4	22	28	32	0.0	3.8	2.0
Middle Atlantic	1.4	1.6	2.0	1.2	1.0	1.1	8.5	7.8	7.0	58	64	77	-0.3	5.0	3.4
Upper South Atlantic	1.9	1.7	2.7	1.3	1.4	1.9	7.6	7.0	6.6	94	104	121	1.6	3.7	2.9
Lower South Atlantic	2.4	2.3	3.2	1.6	1.8	2.5	8.8	7.6	6.9	101	131	159	3.9	8.6	4.7

Sources: BEA, BLS, Census Bureau, CoreLogic, TD Economics. Forecasts by TD Economics as of June 2013.

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## NEW ENGLAND (CT, MA, ME, NH, RI, VT)

Last year, New England's economy expanded by a tepid 1.2% – lagging national growth by a full percentage point. The region will continue to underperform over the forecast horizon, but to a lesser extent, growing by 1.6% in 2013 and accelerating to 2.5% in 2014.

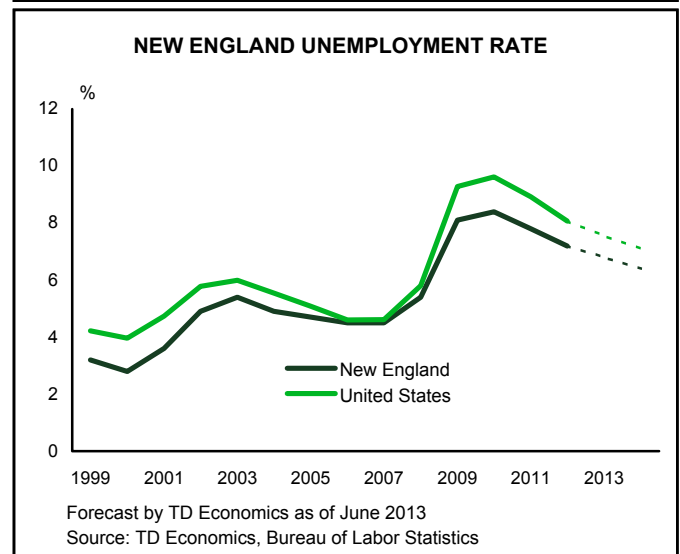
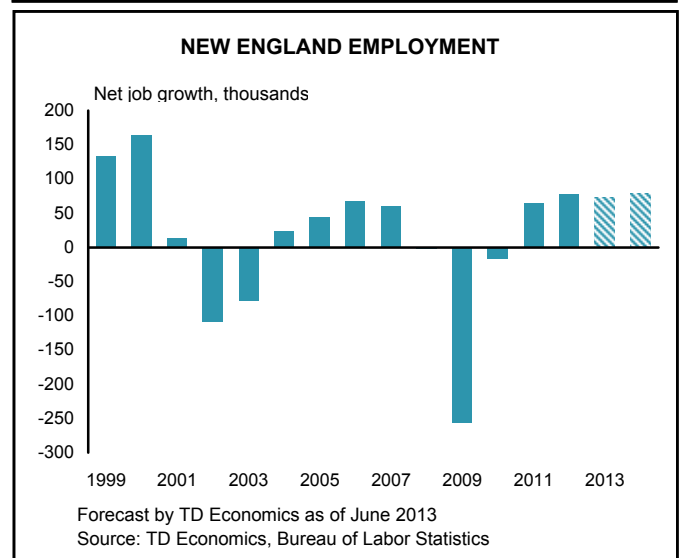
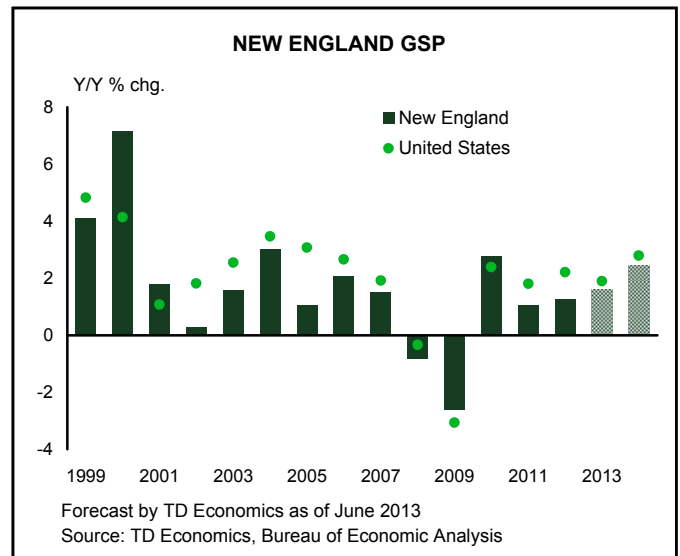
The housing recovery is essential to the economic outlook, and will help offset the impact of fiscal drag and lingering weakness in manufacturing and finance & insurance. Housing starts are projected to increase by nearly 50% over the next two years, as developers take their cue from rising property prices and broadening demand. Home prices are up across every state in New England for the first time since 2006. This has the added benefit of broadening out wealth gains and consumer confidence.

### Bay State still at the top of their game

Massachusetts entered 2013 like a lion, creating the equivalent of six month's worth of jobs in January. Not surprisingly, some payback has since materialized. Nonetheless, a sizeable majority of January's job gains remain in tact, and the recent weakness has not been concentrated in Massachusetts's core industries. In fact, hiring resumed in May, bringing employment growth to 1.5% year-over-year – on par with the 2012 pace. Over the next two years, Massachusetts's economy should grow faster than the rest of the country, with GDP projected to rise by 2.1% in 2013 and 2.9% in 2014.

Job creation remains robust in professional, scientific and technical services, and construction payrolls are also moving higher. The latter will benefit from the double impact of stronger housing activity and the construction of three new casinos. In the years to come, these casinos should boost employment in the hospitality industry. But, in the near-term, the industry will also benefit from the opening of passenger rail services between Boston and Cape Cod.

Massachusetts's well-diversified economy, relative to the rest of New England, has also shielded the Bay State from international weakness. New England's manufacturing industry continues to shed jobs, in part due to overweight export exposure to the European market. Reduced federal defense procurement spending as a result of sequestration will pose an additional challenge for manufacturers in the region. A turnaround for regional manufacturing is expected in 2014 alongside stronger global demand. As industrial production expands, the manufacturing sector's contribution to the regional economy will increase, directly adding



0.6 and 0.7 percentage points to growth in 2014 and 2015.

### Connecticut's fortunes are poised to improve

Although we expect a tepid 0.8% pace of growth for Connecticut this year, this is miles ahead of last year's performance. Preliminary estimates show that Connecticut's economy contracted for the second consecutive year in 2012, placing it in the unenviable position of being the worst performing state in the nation. The outturn was driven by a struggling finance and insurance industry, which subtracted a massive 0.6 percentage points from growth. The industry is a heavyweight in Connecticut, accounting for 16% of activity. Ongoing restructuring and cost-cutting efforts led to a steady stream of job losses in 2012. This impact should lessen in 2013, but not disappear.

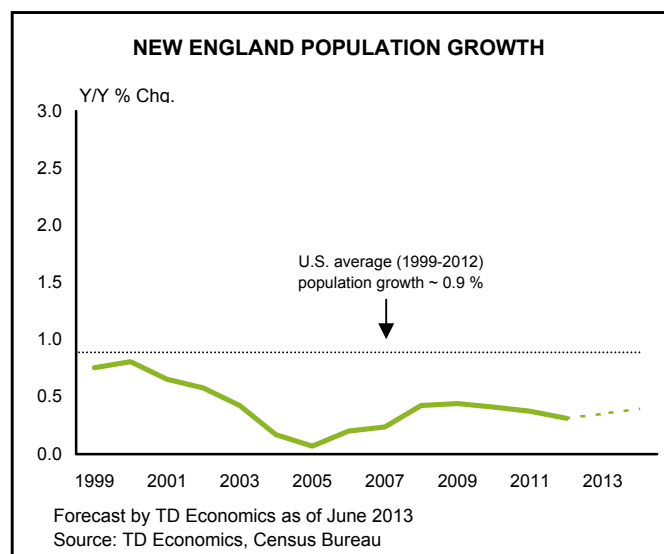
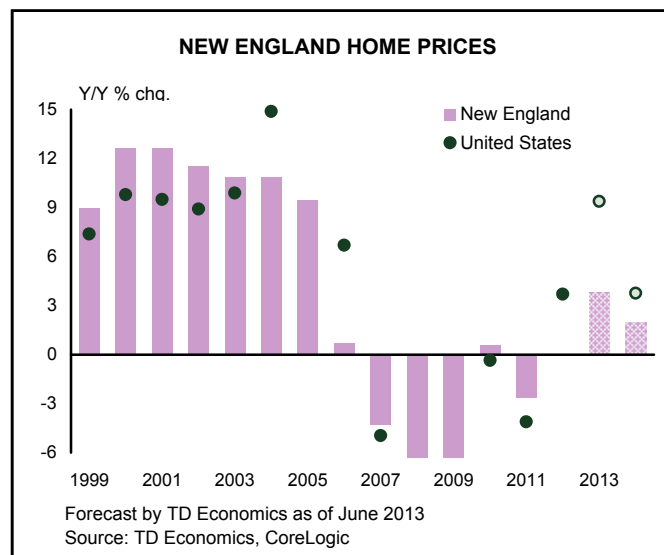
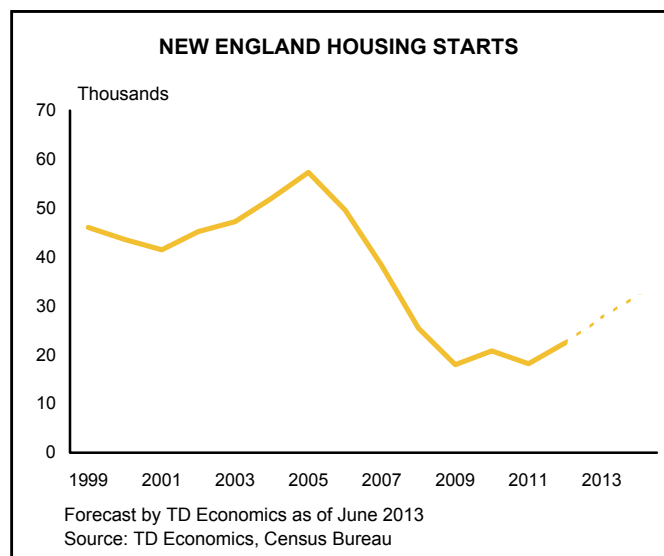
Payrolls in professional, scientific and technical services also took a turn for the worse, as contractors prepared for upcoming government spending cuts. While these challenges will persist in 2013, the rising tide of residential construction and spillovers to the rest of the economy should improve the state's fortunes.

This year there has been a 52% surge in housing starts in Connecticut— double the New England average. This, coupled with Sandy-related re-building efforts, led construction payrolls to account for a third of all new jobs in the state. Benefits will also accrue to other industries with close ties, such as real estate and leasing. So, while the industry dragged GDP growth by 0.4 percentage points in 2012, it will add to growth going forward, equal to 0.3 percentage points in 2014.

### A milestone for New England's housing market

Connecticut does not stand alone in experiencing the revival of housing demand. With the exception of Vermont, housing construction accelerated in all states, rising by 26% in the first four months of 2013. Like Connecticut, Rhode Island also opened 2013 with a bang, with housing starts expanding at a break-neck speed of 51%.

Even with the recent spur of construction activity, housing starts remain well below demographic fundamentals in most states, particularly Massachusetts, Rhode Island and New Hampshire. Housing starts in the Bay State are forecast to return to the pre-recession level by the end of 2014. It will take much longer for Rhode Island and New Hampshire, as construction there remains roughly 45% below 2007 levels. Meanwhile, regulatory hurdles and weak demographic fundamentals will continue to weigh on the pace of housing starts in Maine and Vermont.



## MIDDLE ATLANTIC (NJ, NY, PA)

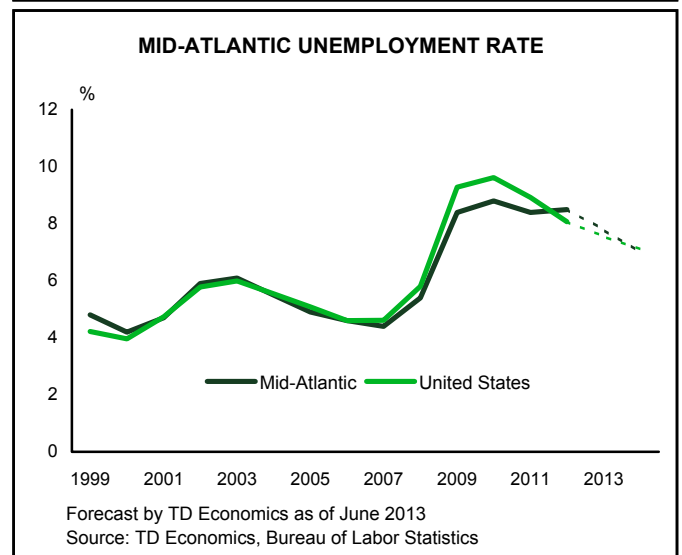
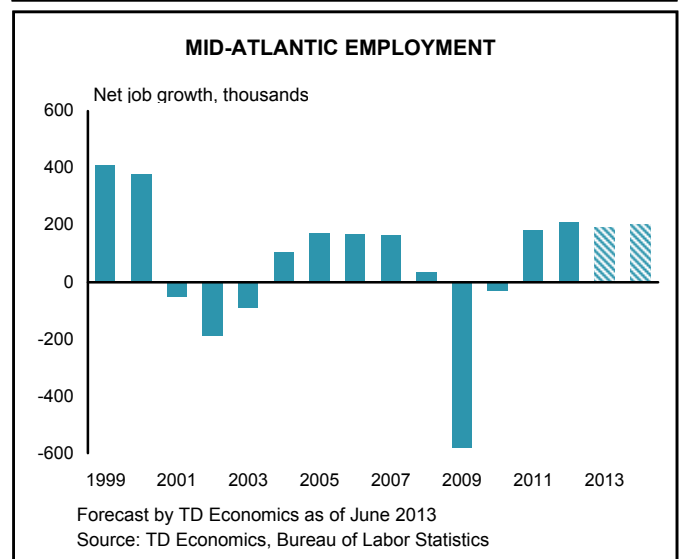
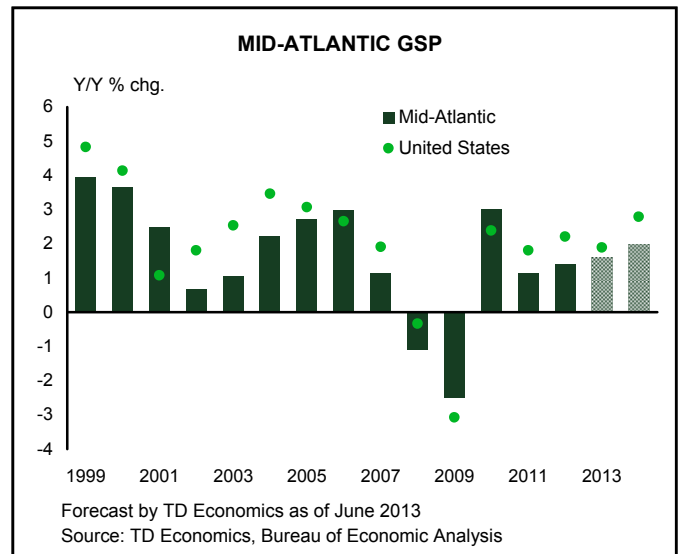
The Middle Atlantic economy expanded by 1.4% last year – 0.8 percentage points below the national rate. Growth will pick up over the next two years, with output advancing by 1.6% this year and 2.0% in 2014. Compared to 2012, the contribution from the manufacturing industry will diminish. A contraction in the government sector will also detract from growth, but a surge in construction will help to fill in the gap. Post-Sandy infrastructure rebuilding and housing repairs will reflect the bulk of the strength, but new residential construction will also play a part. Positive spillovers will extend to real estate & leasing and professional, scientific & technical services. Together with construction, they will account for almost half of the growth in 2013. Although many households in the mid-Atlantic will benefit from improved wealth, the level of distressed inventory remains a concern and will weigh on the rate of home price appreciation.

### Rebuilding continues in the Garden State

In spite of the devastation inflicted by Superstorm Sandy, the Garden State's economy expanded by 1.3% in 2012 – modest growth, but a significant improvement over the near-flat performance in 2011. This year, state GDP is forecast to expand at a similar pace, but the drivers will differ. In 2012, growth was scattered among a wide range of industries. This year, construction and professional, scientific & technical services will lead the way. Together, they will contribute an impressive 0.8 pp to growth, accounting for two-thirds of the expansion.

Sandy-related rebuilding efforts kick-started construction activity early this year, but given an estimated \$37 billion in damage, much work still remains. Reconstruction activity will continue to benefit New Jersey payrolls. In May, job creation accelerated to 1.9% year-over-year – the fastest pace since December 2000. For the year as a whole, employment growth is forecast to average 1.7% – a 0.4 percentage point improvement over 2012. However, by 2014, temporary impacts will begin to fade, and hiring will slow to 1.5%.

While NJ's labor market is healing, there is still a long road ahead. So far, only about half of all jobs lost in the recession have been recovered. In addition, limited home price growth is taking a toll on public finances. While many other states have recovered their tax revenues since the Great Recession, NJ is yet to follow suit. Hurricane Sandy also added to the challenge, contributing to a \$400 million shortfall in FY 2013. To bring additional revenue



to government coffers, the state is moving ahead with the legalization of online gambling. Assuming online casinos will complement and not substitute numerous existing brick-and-mortar gambling sites, this could help state finances. But, the ultimate solution still lies in a stronger recovery in job creation to boost income and sales taxes.

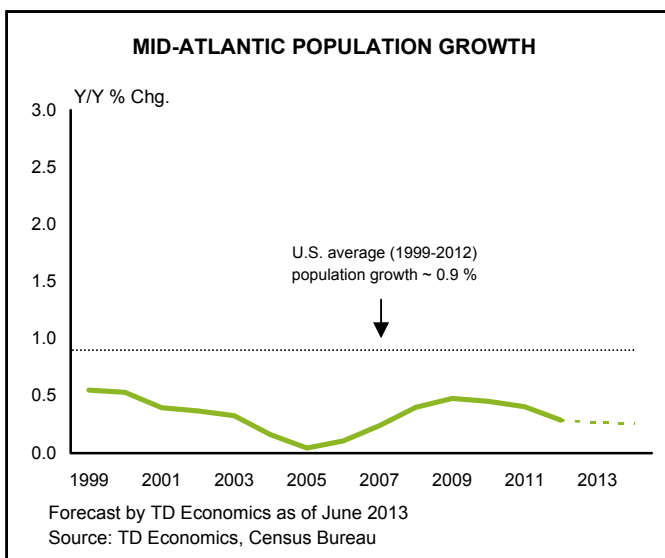
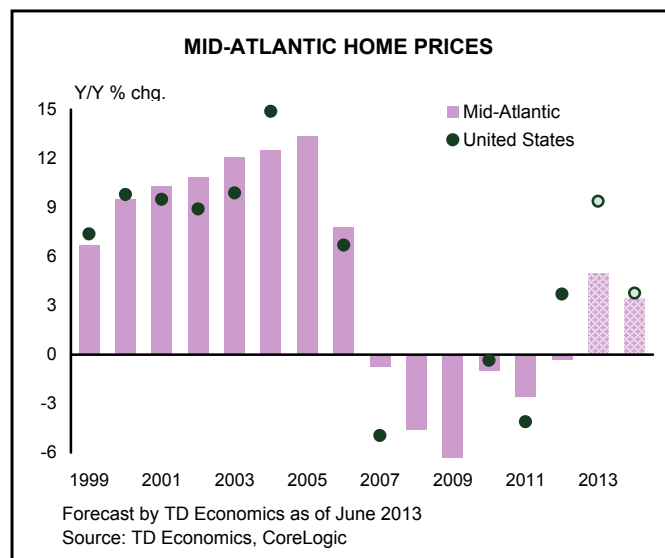
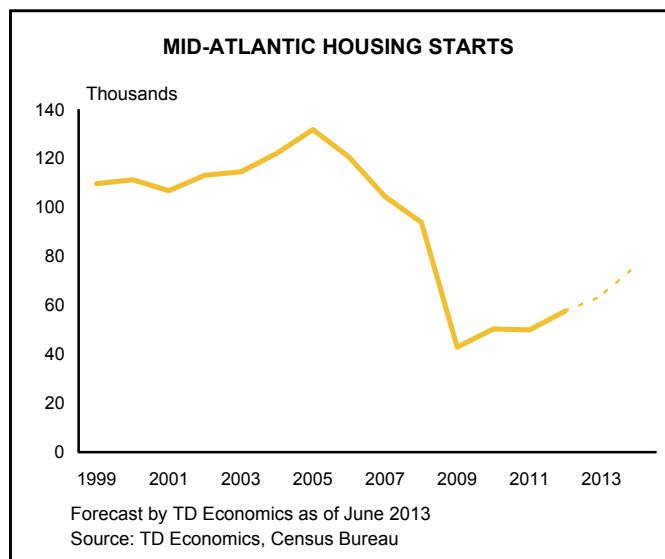
**New York: Slowly raising the bar**

New York’s economic growth disappointed last year, advancing by a tepid 1.3% and lagging the national average by almost a full percentage point. This year, growth is forecasted to accelerate to 1.8%, with construction and professional, scientific & technical services lending a helping hand. Some of the strength in construction, particularly in New York City and Long Island, is related to Hurricane Sandy rebuilding efforts. However, an uptick in new residential construction and a roll-out of large-scale infrastructure projects, such as the \$3.9 billion replacement of the Tappan Zee bridge, will also provide support.

Job growth will advance by 1.2% in 2013 and 1.1% in 2014. To put this in perspective, New York’s payrolls grew by an averaged 0.7% in a decade prior to the recession. Although the job market is on the road to recovery, some sectors remain vulnerable. The finance & insurance industry continues to restructure and cut jobs. Likewise, near-term momentum in manufacturing has softened due to above-average exposure to European markets. Finally, layoffs at IBM will also hurt job growth in professional, scientific & technical services.

**Pennsylvania: Leading the way**

Pennsylvania’s will stay ahead of the pack over the next two years. State GDP growth will slow to 1.5% this year, before accelerating to 2.3% in 2014. Federal spending cuts will weigh on the economy over 2013. Sequestration will be most apparent in the public sector, however it will also manifest itself in manufacturing, professional, scientific & technical services and even retail trade. Fortunately, increased residential construction will help to alleviate some of the weakness. While, home prices and sales have yet to show major improvement, home building activity continues to rise. Housing starts are projected to increase by 50% by the end of 2014. Finally, while PA continues to rise in ranks as a national natural gas producer, the mining sector is not expected to contribute to growth until 2014. Natural gas production surged 69% in 2012; however, a drop in drilling activity, due to limited pipeline and processing infrastructure, will slow growth over the next year.



## UPPER SOUTH ATLANTIC (DC, DE, MD, NC, VA, WV)

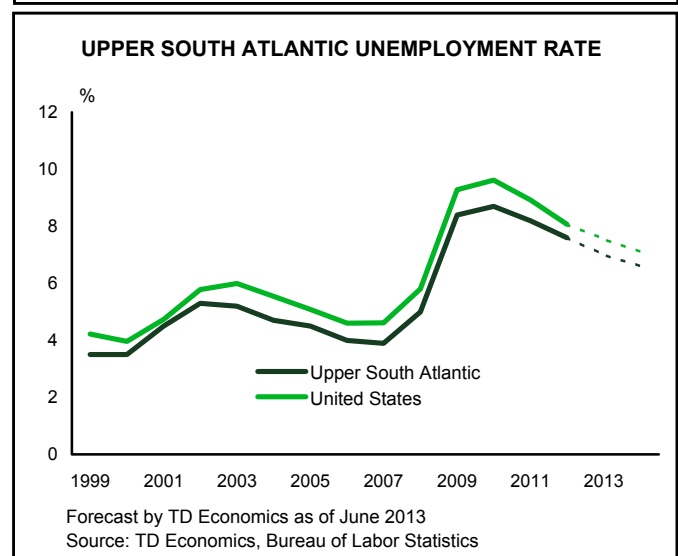
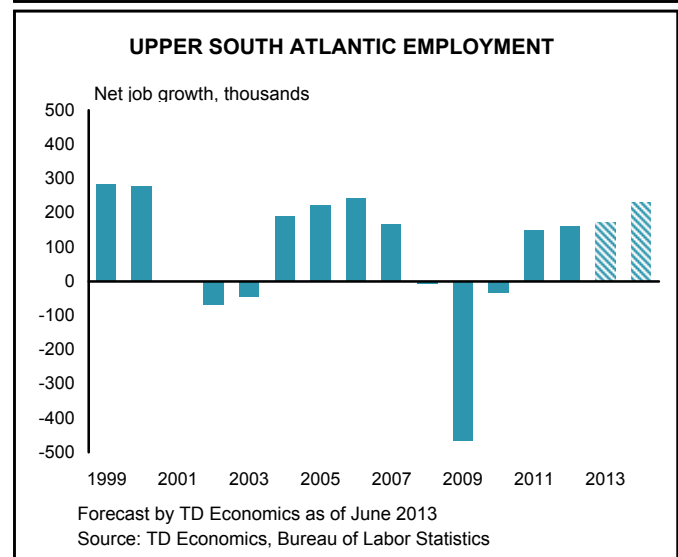
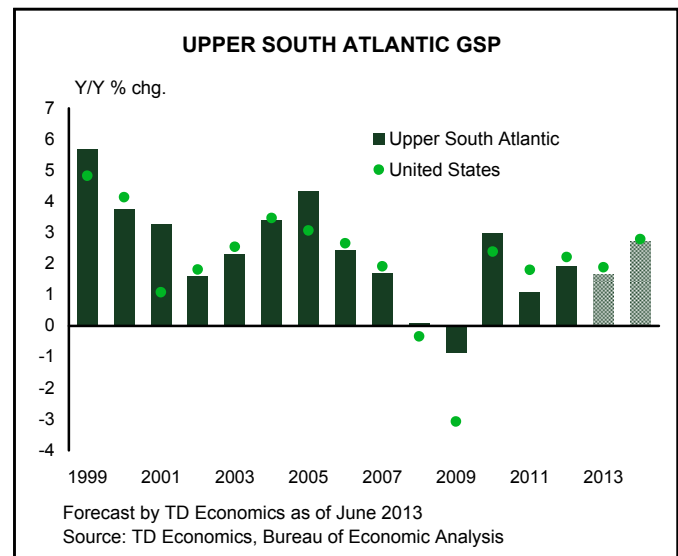
The Upper South Atlantic has been an underperformer since the recession. Much of this is simply due to a milder downturn and, subsequently, less pent-up demand. The regional economy, cushioned by stimulative fiscal policy, actually grew in 2008 and contracted just 0.8% in 2009 – a mere quarter of the national decline. With fiscal consolidation in full swing, the region will underperform again this year.

There is evidence that federal cuts are already weighing. With the help of state & local outlays, government did not detract from growth last year. But, spill-over was evident in stagnant professional & business services activity. Both of these sectors will again weigh on the region this year, with growth likely to slow to 1.7%. Since states are not all cut from the same cloth, those underexposed to federal spending will lead the pack. As fiscal clouds clear, the region will nearly keep up with the nation, advancing by 2.7% in 2014.

### D.C., Maryland, Virginia: Sequester-central

Virginia, Maryland and the District of Columbia are most exposed to federal cuts. Federal spending makes up over 20% of the economy – four times the national average – and one in twenty-five is on federal civilian payrolls. High vulnerability to government restraint led to a meager 1.5% expansion in 2012, compared to 2.2% nationally. This was due to the knock-on to the professional & business services sector. It accounts for 18% of output and includes many government contractors.

In anticipation of the ‘sequester,’ many of these firms stopped hiring or began to downsize. Payrolls in Virginia’s professional, scientific, & technical services – a key driver of growth – finished 2012 modestly in the red, after adding an average of 10,000 jobs in the previous two years. Momentum in this sector has deteriorated rapidly this year, with 6,300 lost payrolls through May. A meaningful comeback by year-end is unlikely. To make matters worse, the federal government will subtract from growth this year, with some offset stemming from state & local spending. A pick-up in economic activity from housing-related industries – construction and real estate & leasing – will push against this headwind, but will not be enough to prevent the DC-MD-VA region from decelerating to 1.3% this year. But, within the group, there will be a wide divergence. Maryland’s economy is less exposed to sequester-prone sectors, and will outperform at 1.8%. At the other end of the spectrum, D.C. will grow by just 0.6%. In 2014, as some drag diminishes, the region should begin to converge with the rest of the country.



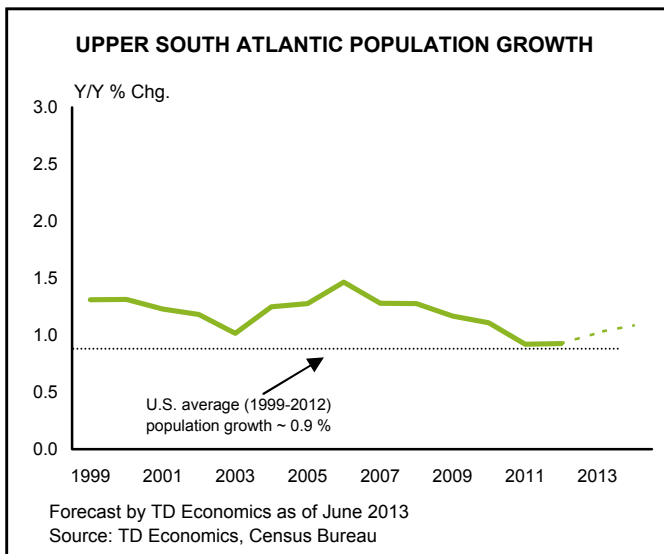
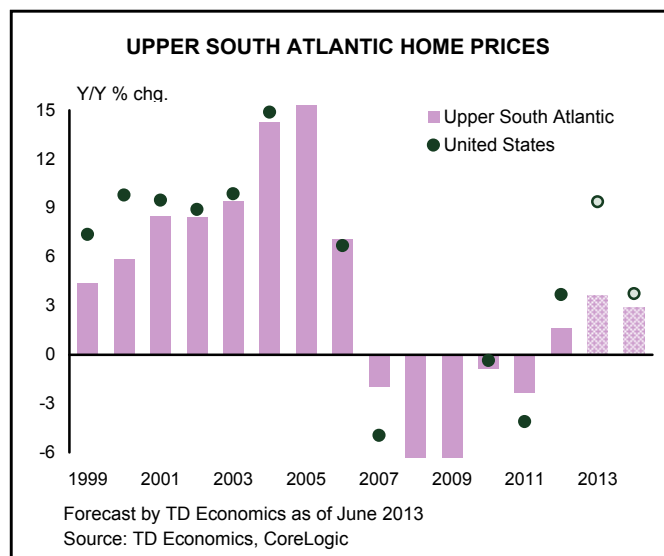
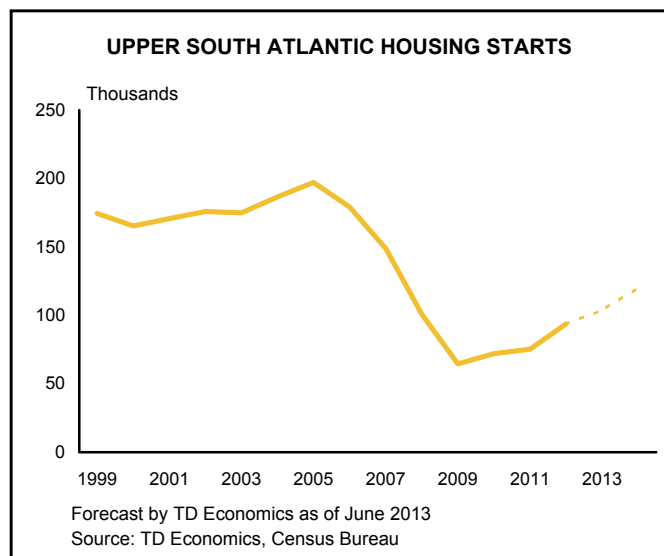
### North Carolina: Ahead of the pack

North Carolina's economy reasserted itself in 2012. After stumbling in 2011, growth surged to 2.7% – nearly on par with our projections. Growth was broadly based, with housing-related industries, manufacturing, trade, finance, and professional & business services contributing nearly 0.5 percentage points apiece. The economy churned out 90,000 jobs by year end – the fastest pace since mid-2007. The jobless rate improved only 0.4 percentage points over 2012, as people flocked back into the labor force. But, it has since fallen by more than half a point, supported by continued payroll gains – with 10,000 net positions added through May. The outlook for this year looks modestly dimmer, but the state should outpace the nation by a wide margin. Manufacturing slowed in response to weaker global growth. Payrolls decelerated from 2.4% y/y in January to just 0.3% in May. But, the engine of the state economy will not stall, due to continued rotation towards higher value-added manufacturing. Pharmaceutical and machinery payrolls continue to surge – up 5.8% and 2.7% y/y, respectively. Ditto for computers & electronics, which are up a solid 2.1%. Services industries have also been on a tear. All told, the Tar Heel economy looks well positioned to withstand federal cutbacks, with growth projected to reach 2.4% this year, before surging to 3.5% in 2014.

### Delaware and West Virginia: The volatile ones

The remaining regional economies are characterized by two inter-related factors: size and volatility. Their combined output is barely above that of D.C. By extension, growth in economic activity gets battered around by a small group of outsized industries. For Delaware, it is finance & insurance and housing-related industries (real estate & leasing and construction). These three account for exactly 50% of all output in the First State. Last year, real estate & leasing contracted 4%, while construction output fell 10%. Finance & insurance and nondurable manufacturing helped, but with little growth elsewhere, economic activity in Delaware effectively stalled – managing a 0.2% uptick. This year should be different. With housing starts and prices showing some resilience, the economic expansion should register a more appropriate 1.8% pace

This year will also be different for West Virginia, but for the opposite reason. Growth soared to 3.3% last year, but nearly two-thirds of it – 2.4 percentage points – was due to coal. Excluding this sector, the economy grew by 0.9%, which is slightly above the 0.7% pace projected for this year, with mining output little changed from its 2012 levels.



## LOWER SOUTH ATLANTIC (FL, GA, SC)

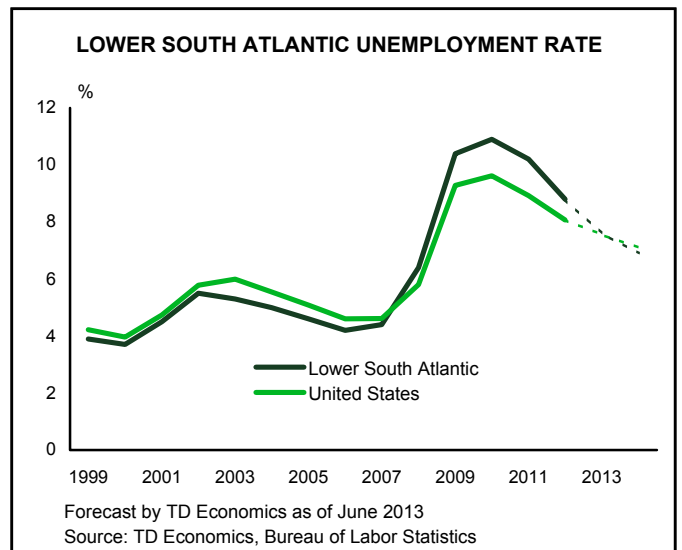
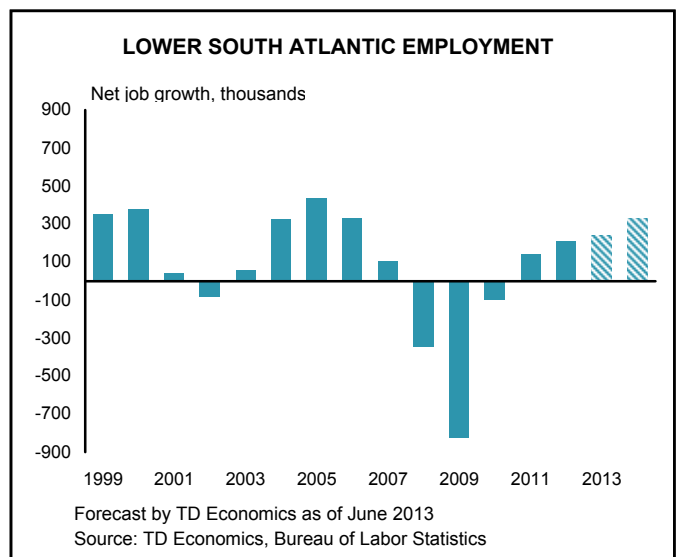
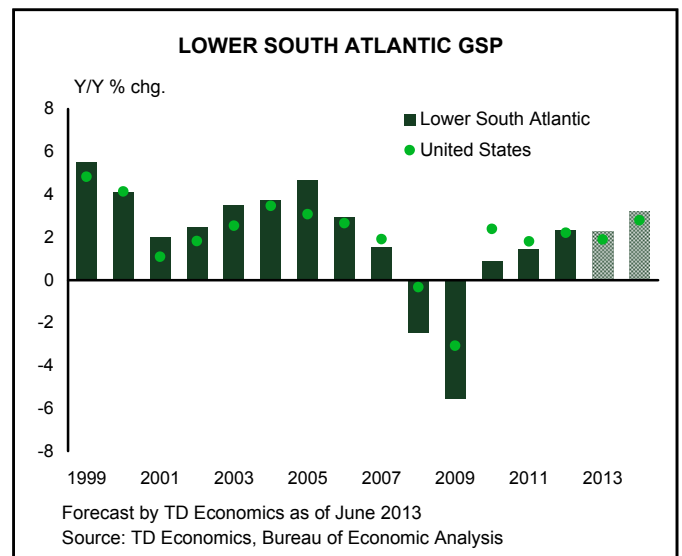
After underperforming for five years, the Lower South Atlantic finally outpaced the nation. A 2.4% advance in 2012 was led by manufacturing, finance, real estate & leasing, and trade. Combined, these accounted for nearly three-quarters of the growth. Government was the only sector to register significant declines, but transportation & warehousing, professional & business services, and construction also underwhelmed. The pace of economic growth should largely hold up this year, but the growth-drivers will shift. Construction will contribute more and offset the ongoing drag from government. Real estate & leasing will remain strong alongside slower manufacturing growth. Regional growth should accelerate to 3.2% in 2014 on an improved national backdrop and favorable regional population dynamics.

### Florida: Let the sunshine through

The housing recovery is nowhere as apparent as in Florida, where a revival in demand is now driving broader growth. The economy expanded by 2.4% last year – a touch higher than we projected – after rising by just 0.9% in 2011. Gains in real estate & leasing and construction accounted for more than half of the acceleration.

House prices have been rising for sixteen months straight, with all statewide measures indicating solid double-digit growth. And, this is not the end of the road. Home prices remain undervalued relative to rent and incomes. After rising 17% since the trough, prices remain a distant 40% from their 2006 peak. For perspective, they would need to rise at the current pace for five years to reach prior peaks. Sales activity is improving, with 450,000 homes sold in the 12-months through March – 10% more than the year before. This trend, together with a recovery in commercial real estate, will continue to support real estate & leasing.

Construction activity will also take on a larger role in the forecast. The state budget for FY 2014 is the first surplus in seven years, and earmarks sizeable infrastructure spending. Moreover, housing starts are up 54% through April – nearly twice the national pace. Starts should approach a 90,000 pace by year-end. Although this will roughly match the current demographic demand driven by 230,000 new residents, it does not fill the gap created by a dearth of construction over the past five years amidst ongoing population growth. Florida's population rose above that of New York this year for the first time in history, maintaining its appeal to both retirees and job-seekers. Many of the latter will be motivated by Florida's much improved jobless rate, which recently





fell below the national measure for first time in five years. All told, the housing recovery, strength in retail trade and education & health, as well as renewed spending among state & local governments will allow Florida to outperform. In fact, it will maintain a noticeably stronger tailwind, with growth of 2.4% this year accelerating to 3.4% in 2014.

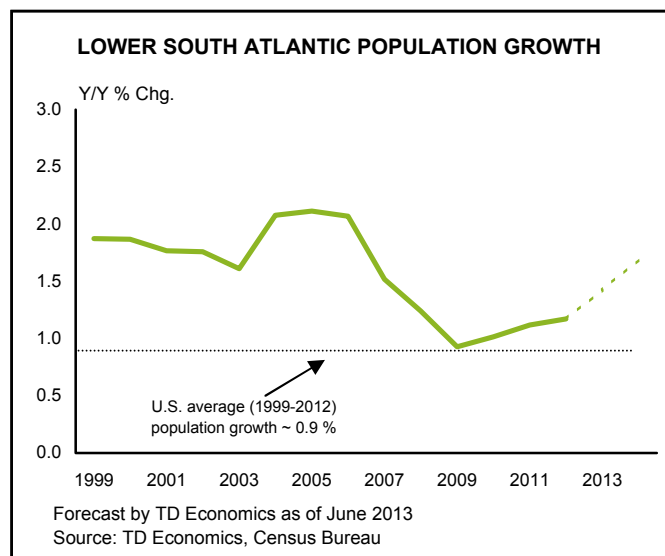
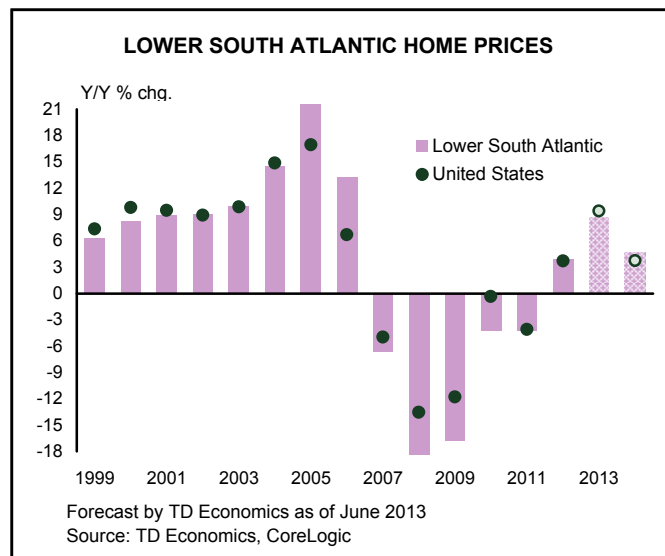
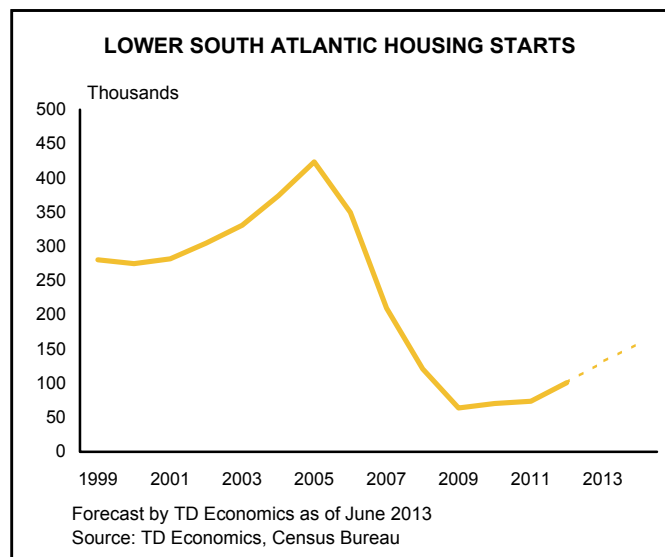
### South Carolina: Durable as ever

South Carolina's economy will slow in 2013, but still outperform the nation for the fourth consecutive year. Last year's growth reached 2.7% – slightly higher than we anticipated – due to remarkable strength in manufacturing. The sector accounted for nearly half of all growth as output in durables surged 9.8%. Production of transportation equipment led, as Boeing and BMW increased activity. Further expansion activity will support manufacturing and exports. But, this is unlikely to fully offset pressures stemming from sequestration and weak global growth.

The government sector was surprisingly resilient in 2012 – federal payrolls were unchanged, while state & local jobs surged 11,000. But, a repeat performance is unlikely alongside cutbacks in grants, nondefense spending and defense spending. South Carolina is home to eight military installations. Furloughs are expected to begin in mid-July and last at least until the end of September. Four counties are particularly exposed – Richland, Sumter, Beaufort, Charleston – but the impact will ripple through the entire state. Still, the economy should grow by 2.1% this year, supported by durables and housing-related industries, before accelerating to 2.6% in 2014, as some of the drag dissipates.

### Georgia: Lookin' peachy

The story is broadly similar in Georgia. Growth last year was a respectable 2.1%, supported by a 5.1% advance in manufacturing. But, the sector has already slowed this year and is expected to grow at half its 2012 pace. Fiscal cuts will also bite, as federal defense accounts for 5.2% of state GDP. Fortunately, a strong recovery in housing will offset much of this drag. Starts surged 30% in 2012, with this pace likely to continue. House prices have exploded in the Peach State to 14.5% y/y in April, after being nearly flat last Thanksgiving. Georgia's prices are now rising faster than Florida's. As a result, Georgia's economy should continue to expand at a pace similar to last year – approximately 2.1%. The story looks better for 2014, as the recovery in housing is joined by more robust manufacturing activity and broader strength in services. All-in-all, growth should ratchet up to a peachy 3.2% in 2014 – its best performance in more than a decade.





TD State Forecasts																		
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<b>New England</b>	1.2	1.6	2.5	1.1	1.1	1.1	7.2	6.8	6.4	22	28	32	0.0	3.8	2.0	0.3	0.4	0.4
Connecticut	-0.1	0.8	1.6	0.9	0.8	1.2	8.3	8.0	7.7	4.3	6.2	7.4	-3.5	1.2	1.7	0.1	0.1	0.2
Massachusetts	2.2	2.1	2.9	1.5	1.3	0.8	6.7	6.5	6.3	11	13	15	1.0	5.7	2.0	0.6	0.5	0.5
Maine	0.5	1.0	1.9	0.5	0.4	1.5	7.3	6.8	6.3	3.1	3.7	4.3	0.9	3.1	2.4	0.1	0.2	0.4
New Hampshire	0.5	2.1	3.4	1.0	1.3	2.0	5.5	5.3	4.5	2.3	2.6	3.1	0.9	2.9	2.8	0.2	0.5	0.7
Rhode Island	1.4	1.5	2.1	0.8	0.5	0.9	10.4	8.6	6.9	0.8	1.2	1.4	-2.3	0.5	0.2	-0.0	0.2	0.3
Vermont	1.2	1.7	2.9	1.2	1.2	1.6	5.0	4.0	3.5	1.3	1.1	1.2	2.1	3.2	3.3	-0.1	0.0	0.2
<b>Middle Atlantic</b>	1.4	1.6	2.0	1.2	1.0	1.1	8.5	7.8	7.0	58	64	77	-0.3	5.0	3.4	0.3	0.3	0.3
New Jersey	1.3	1.2	1.9	1.3	1.7	1.5	9.5	8.6	7.6	16	18	22	-2.3	2.5	2.4	0.3	0.4	0.4
New York	1.3	1.8	1.9	1.4	1.2	1.1	8.5	7.7	6.8	23	22	27	0.9	7.8	4.6	0.4	0.3	0.2
Pennsylvania	1.7	1.5	2.3	0.8	0.3	0.7	7.9	7.6	7.0	18	23	28	-0.9	1.9	2.0	0.2	0.2	0.2
<b>Upper South Atlantic</b>	1.9	1.7	2.7	1.3	1.4	1.9	7.6	7.0	6.6	94	104	121	1.6	3.7	2.9	0.9	1.0	1.1
District of Columbia	0.7	0.6	1.1	0.7	0.4	0.5	8.9	8.5	8.1	3.2	1.9	2.1	4.8	7.6	4.7	2.1	1.7	1.4
Delaware	0.2	1.8	1.4	0.3	1.8	1.7	7.1	7.1	6.9	3.9	4.6	5.2	-0.1	-0.5	0.3	1.0	1.0	1.1
Maryland	2.4	1.8	2.8	1.3	1.5	1.8	6.8	6.6	6.3	14	17	20	1.4	2.4	2.0	0.8	0.8	0.8
North Carolina	2.7	2.4	3.5	1.8	1.7	2.0	9.5	8.9	8.3	44	48	56	0.6	4.0	4.1	1.0	1.2	1.3
Virginia	1.1	1.2	2.6	1.1	1.3	2.2	5.9	5.2	4.8	25	28	32	2.4	4.2	2.2	1.0	1.2	1.2
West Virginia	3.3	0.7	1.5	1.3	0.6	1.0	7.4	6.3	4.9	2.6	3.5	4.1	2.4	3.2	2.1	0.0	0.0	0.1
<b>Lower South Atlantic</b>	2.4	2.3	3.2	1.6	1.8	2.5	8.8	7.6	6.9	101	131	159	3.9	8.6	4.7	1.2	1.4	1.7
Florida	2.4	2.4	3.4	1.8	1.8	2.6	8.6	7.1	6.4	59	81	101	6.1	8.1	5.5	1.2	1.5	1.9
Georgia	2.1	2.1	3.2	1.3	1.9	2.4	9.0	8.2	7.8	23	30	35	-2.0	11.2	4.9	1.1	1.4	1.6
South Carolina	2.7	2.1	2.6	1.5	1.4	2.0	9.1	8.0	7.2	18	20	23	1.8	6.8	4.6	1.1	1.2	1.3

Source: BEA, BLS, Census Bureau, CoreLogic, TD Economics. Forecasts by TD Economics as of June 2013



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