November 2015

Dear Reader:

This is the first State of the Commonwealth Report. It is jointly sponsored by the Strome College of Business at Old Dominion University and the Virginia Chamber Foundation. While the report represents the work of many people connected in various ways to the university, it does not constitute an official viewpoint of Old Dominion or its president, John R. Broderick. Similarly, it does not represent the views of the Virginia Chamber of Commerce or its president and CEO, Barry DuVal.

The goal of the report is to stimulate thought and discussion that ultimately will make Virginia an even better place to live, work and do business. We are proud of the Commonwealth’s many successes, but realize that it is possible to improve our performance. In order to do so, we must have accurate information about “where we are” and a sound understanding of the policy options open to us.

The 2015 report is divided into eight parts:

The Virginia Economy Struggles to Cope with Economic Headwinds: The Virginia economy grew 0.02 percent in real terms in 2014, will grow only about 1.33 percent in 2015, and we forecast only a 1.98 percent growth rate in 2016. The villain in this scenario is stagnant or declining federal spending, especially defense spending.

Northern Virginia: Standing at a Fork in the Road? Direct federal employment and procurement spending accounts for almost 40 percent of all economic activity in Northern Virginia, which in turn accounts for more than 40 percent of all economic activity in Virginia. Sequestration has hobbled Northern Virginia’s growth. However, George Mason University’s leading economic index suggests better times are on the horizon.

Digging Deeper: A Closer Look at Defense Spending in Virginia: An estimated 11.8 percent of Virginia’s GDP depends upon defense spending. An important part of this are the contracts awarded to Virginia businesses by the Department of Defense. Two regions – Northern Virginia and Hampton Roads – account for 86 percent of these contracts.

If You Can Make It There . . . You Can Make It Even Better in Virginia: The good news is that the “real,” inflation-adjusted incomes of Virginians in nearly every area of the Commonwealth are higher than in nearly all comparable regions along the Atlantic Coast, including New York City.

Fly Away With Me: A Look at Virginia’s Airports: For several years, both passenger traffic and the number of available seats have been in decline at nearly all of the Commonwealth’s airports. Reagan/Washington National and Charlottesville are the major exceptions. Decisions made by the U.S. Congress have placed a particular burden on Dulles International.

The Small-Business Story in Virginia: What a Quarter Century of Data Reveal: Very small businesses in Virginia (those with fewer than 10 employees) have been holding their own, but many have found it difficult to grow beyond this size. Very small businesses now account for smaller proportions of total employment and payrolls in Virginia than was true 25 years ago. However, public policy changes can alter this situation.

Consolidating or Merging the Public Service Provision in Virginia Cities and Counties: Where Can We Save the Most Money? Controlling for variables such as the cost of living and local characteristics, we examine the provision of 25 distinct public services by the 95 counties and 39 independent cities in Virginia. Could we save money and perhaps provide better services if we combined the provision of some of these services across county and city lines? The evidence suggests that the answer is yes for at least 13 of these public services and perhaps for another four.

Domestic Migration: What Moves Us? Virginians and all other Americans can vote with their feet and move from one location to another in response to job opportunities, amenities and other factors. Recently, Virginia has experienced very low or even negative levels of net domestic migration. We look at the migration experience of 358 metropolitan regions nationally (including the largest eight in Virginia) to provide some answers.
The Strome College of Business provides support for this report, which is produced by Old Dominion’s Center for Economic Analysis and Policy. George Mason’s Center for Regional Analysis and GMU Professor Terry L. Clower provided essential data analysis for Northern Virginia. However, the report would not appear without the vital backing of the private donors whose names appear below. They believe in the Commonwealth and the power of rational discussion to improve our circumstances, but they also are not responsible for the views expressed in the report.

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The State of the Commonwealth Report is available in PDF form at www.stateofthecommonwealth.com and www.jamesvkoch.com. If you have comments or suggestions, please direct them to James V. Koch at jkoch@odu.edu or 757-683-3458. Individual copies may be purchased for $25.

Sincerely,

James V. Koch

Board of Visitors Professor of Economics  
and President Emeritus, Old Dominion University
November 2015
Dear Reader:

The Virginia Chamber Foundation is pleased to present to you the first State of the Commonwealth Report, to give an unprecedented economic profile of significant trends that will affect Virginia’s future growth. This independent report, produced by Old Dominion University’s Center for Economic Analysis and Policy, is a key part of the Virginia Chamber Foundation’s mission to strengthen Virginia’s long-term competitiveness through research that provides relevant metrics for our economy’s progress.

Virginia for many years has been blessed by a strong economy, being recognized as the best state for business by CNBC as recently as 2011. However, our growth has slowed in recent years. Virginia faces economic headwinds, and it’s up to our businesses to have an accurate understanding of where we are in order to chart a course for long-term economic growth.

I would like to thank those who contributed their support to the Virginia Chamber Foundation, which allows us to invest in this statewide economic profile. Those foundation sponsors are recognized on the following page.

While the conclusions of this independent report are the authors’ alone, and do not necessarily reflect those of the Virginia Chamber of Commerce or our members, the State of the Commonwealth Report presents a critically important benchmark for Virginia’s economy. I hope that it will spark candid conversations about the best ways to overcome our challenges, and that those conversations turn into positive action.

The Virginia Chamber will continue to be a catalyst for ideas to improve Virginia’s long-term business climate and for implementing those policy ideas at the state and federal level. The Chamber’s Blueprint Virginia Business Plan for the Commonwealth engaged more than 7,000 business and community leaders to lay out our long-term vision. With 23,000 members, we will continue to be a strong voice for business in Virginia.

This year, the Virginia Chamber had a 94 percent success rate in implementing Blueprint priorities in the General Assembly, and we were recognized by the Southern Political Report as the top Virginia Government Affairs Association. Our work is not done.

Please give careful consideration to the content of this benchmark report. We know that when we strengthen the voice of the private sector and make it easier to start and grow a business, Virginia wins.

Sincerely,

Barry DuVal
President & CEO
Virginia Chamber of Commerce

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President & CEO
Virginia Chamber of Commerce
WITH SPECIAL THANKS TO OUR 2015 STATE OF THE COMMONWEALTH SPONSORS:
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Final Thoughts

With a few exceptions, Virginia’s net domestic migration numbers have been lackluster in recent years. After accounting for births, deaths and international immigration into Virginia, the Commonwealth has not been attracting large numbers of domestic migrants from other states. Our analysis of net domestic migration patterns exposes the major reason for this – stagnant job growth in the Commonwealth. Between 2005 and 2014, total employment in Virginia grew by only about 2 percent. By comparison, national employment increased by about 2.9 percent during the same period.\(^8\)

Virginia’s flaccid net domestic migration rates in recent years visibly reflect the impact that the slowing growth rate of federal expenditures has had on the Commonwealth. True, we avoided the worst economic blows that sequestration might have inflicted upon us, but we remain critically sensitive to federal expenditures in general and defense expenditures in particular. The regional economies of Northern Virginia and Hampton Roads, which together account for about 60 percent of the dollar value of the Commonwealth’s economic activity, are federal-spending thermometers. Both have seen much better times.

Domestic migrants are interested in many things, but especially job availability. Growing economies attract domestic migrants. We have come up short in this regard, particularly in Hampton Roads, and therefore have fallen well behind many other Southern and Western states in terms of domestic in-migration.

Compounding our federal expenditure problem, Virginia has been only a marginal participant in the fracking energy revolution that has rocketed many metropolitan economies forward. Our major energy entrant, the coal industry, has been contracting rather than expanding.

Reality is that Virginia has relatively little control over federal expenditures and cannot magically alter where oil deposits are located. We do, however, have the ability to exploit what we have termed in this chapter “economic freedom” and we do have the wherewithal to provide the public services (including education and infrastructure) that domestic migrants prefer.

If there is a lesson here, it is that breaking down barriers to economic activity, supplemented by critical investments in public services and infrastructure, is the most important key to attracting the domestic migrants who contribute to the production of long-term economic growth. It should come as no surprise that ensuring that economic actors are not burdened by excessive regulations and providing good schools and infrastructure are winning strategies.

Interestingly, those who reside on the right side of the political spectrum tend to applaud the notion that economic freedom is important to economic growth, but often are less enthusiastic about extensive investments in education and infrastructure. Those with more progressive political instincts frequently are the opposite – they strongly support investments in education and infrastructure, but find it hard to resist the temptation to regulate economic activity and narrow individual economic options. Our research, based upon 358 metropolitan areas, strongly suggests that both groups would be well advised to listen a bit more to each other and adopt some of each other’s ideas. The goal should be to develop a bipartisan program that will extract the parts of each agenda that now have been shown to influence where people wish to live and work. Charles Tiebout was right – people do vote with their feet.

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