"Free-falling into Our New Normal: What's in Store for DC Metro Communities Post-COVID-19?"

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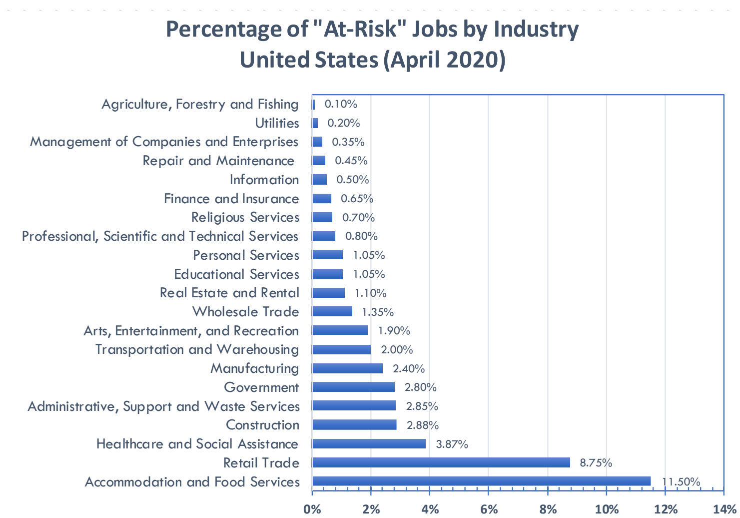
The Unemployment Pandemic Caused by a Global Health Pandemic

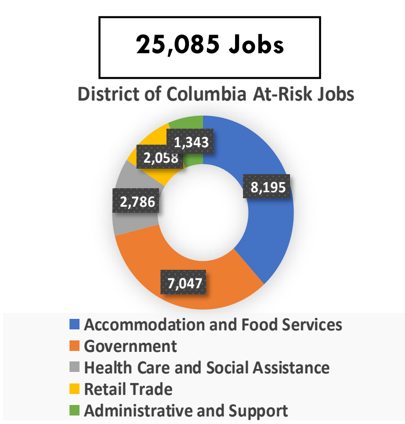
In the past few weeks, the COVID-19 pandemic has been reshaping the American economy. Some fear that it is reshaping it into our "new normal." In the past five weeks, nearly 26.5 million new workers have joined the unemployment ranks and economists estimate the national unemployment rate at approximately 20 percent and rising - just 4 percentage points below of the Great Depression's peak in 1933. That's right, I said the Great Depression not the Great Recession of 2008-2009. Can this be our future? Let us hope not, but it is our new normal for now and we need to understand it better.

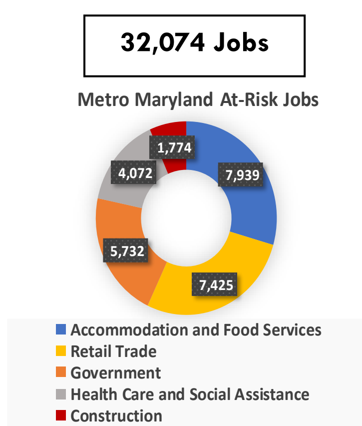
During the first ten weeks of this year, there were nearly 67,200 first time unemployment claims in the Greater DC Metropolitan Region. Since then, through the week ending April 18, 2020, there has been nearly 914,600 new jobless claims, more than a thirteenfold increase in just five weeks. All sectors of our economy have felt this shock, but not all industries are being impacted to the same degree, and the same can be said for different parts of the Metro Region.

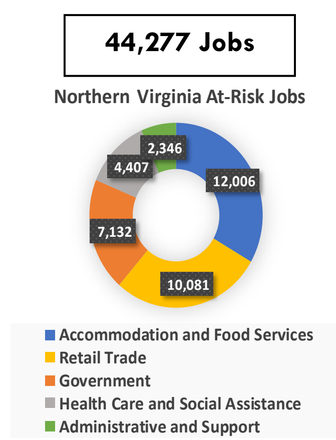


Source: McKinsey Global Institute (April 2020)

A recent report (April 2020) from the McKinsey Global Institute estimated that almost 51 million jobs in the U.S. are at risk – with a heavy concentration in accommodations and food services, retail, healthcare, construction and administrative services. RKG's obtained industry employment data from EMSI, Inc. to analysis the three areas comprising the DC Metropolitan Region. The analysis shows how local jobs in the District, Metro Maryland and Northern Virginia are most likely to be impacted by the current economic contraction. In total, RKG estimates that over 101,000 jobs are currently at risk in our region, but this could







change. The graphics above show the top five job sectors by subregion most likely to sustain significant job losses. Not surprisingly, the accommodation and food services industry is likely to take the biggest hit with over 28,100 jobs at risk and hundreds of establishments under threat of permanent closure.

The District with its heavy government employment base is likely to experience deeper government sector job losses as its primary sector. Metro Maryland and Northern Virginia with their large retail and service bases will see bigger losses in those sectors, perhaps as many as 17,500 jobs combined. Other employment industries under threat include healthcare (11,265 jobs) and administrative and support (5,229 jobs).

So, What will our "New Normal" Look Like?

It seems hard to believe that the world could experience such a profound event such as COVID-19 and not be fundamentally changed by it. Since RKG is in the business of assisting local communities in managing their economies and tax base; improving affordable housing opportunities; attracting new business investment and generally improving local quality of life e, we put our heads together and asked, "what new challenges are ahead for our clients (both private and public sector), and how do we all move forward as a community."

1. **Short-Term Challenges**

The Federal Government recent stimulus programs are roughly designed to get the country through the end of June, with the hopes that the virus will be diminished during the summer months and the virus threat will cease – at least temporarily. If that happens and

How are Governments Responding?

Despite the threat to the region's private sector job base, local and county governments are being stress tested like never before. March and April are typically important months for finalizing annual municipal budgets. This year, the economic crisis struck just as many local governments were finalizing their FY2021 budgets. This caused everyone to push "pause" and reassess the next twelve months of deep revenue losses and service cuts. The is a summary of local government responses

- **CAREAct Federal Stimulus Funding -** The Coronavirus Aid, Relief and Economic Security Act (CARESAct) has provided $2 trillion in federal stimulus money to counteract the economic crisis caused by the pandemic. Included in this initial package was direct relief allocations of $495 million for Washington D.C., $3.31 billion for Virginia, and $2.34 billion for Maryland, according to the National Conference of State Legislatures. It is a start, but not enough, and as the initial round of funding has already been depleted, local governments have begun implementing their own packages.

- **State of Maryland - T**he Maryland Comptroller estimates a loss to the state of $2.8 billion, in just three months, including an almost $1 billion decline in income tax revenues. This revenue drop would exceed the state's rainy-day fund by an estimated $700 million. The State placed restrictions on mortgage foreclosures for people losing their jobs due to COVID-19 causes.

- **Washington, DC -** The DC Council has passed legislation which includes prohibiting residential rent increases during the pandemic, a new requirement that mortgage lenders defer payments for both commercial and residential borrowers for up to 90 days after the state of emergency ends. The District's Chief Financial Officer warns of a possible $600 million impact to the City's budget.

- **Fairfax County, VA** – has proposed a revised budget for Fiscal Year 2021, dropping a previously proposed real estate tax rate rise and a 4.0 percent admissions tax increase on movie and concert tickets. The County is also planning to create an emergency loan program for small businesses. Fairfax County is projecting a $75 million shortfall.

- **Montgomery County, MD** – passed a range of measures in late March, including up to $20 million of grants for businesses impacted by the pandemic, and another $10 million in relief funds for local hospitals. Small businesses with 100 employees or fewer will be able to apply for funds of up to $75,000.

- **Prince George's County, MD** – the County Executive proposed a new "COVID-19 Business Relief Fund" of up to $15 million on April 1st, which provides loans of up to $100,000 and grants of up to $10,000.

- **Arlington County, VA** - County officials are in the process of creating a new grant program for small businesses and organization impacted by the pandemic. The County Manager has also proposed a new budget with around $40 million in spending cuts and a suspension of any tax changes.

- **Alexandria, VA** - has temporarily suspended the collection of meals tax, transient lodging tax and hotel tax, and allowed businesses to file personal property taxes before July 1, with a two-month extension. The Alexandria/Arlington Emergency Layoff Aversion Assistance Program will also award 11 grants to small businesses in need to keep their workforce.

people can filter back into the workforce, the worst case may be averted. However, if that does not happen or the current "shelter in place" orders persist into the second half of 2020 and beyond, the future starts to look very different.

In the short-term we can expect a lot of uncertainty in the real estate and financial markets. With an increasing number of people out of work and with little or no emergency funds to sustain them, mortgage and rent payments will eventually fall in arrear s. While there are temporary state-level prohibitions against mortgage foreclosures and evictions, and many banks and landlords are offering three-month payment holidays, those accommodations will eventually come to an end.

- <u>Deal Modifications and Restructuring</u> - Financial institutions will work with their existing customers to modify existing deals and restructure mortgage and lease terms to provide some temporary relief while state and federal leaders try to restore the economy so people care return to work.
- <u>Business Outreach and Support</u> - Local economic developers and elected officials will seek ways to support and sustain local businesses to keep them in place.
- <u>Provide Short-term Stimulus</u> - As stated above, Federal stimulus money is designed to keep businesses and workers in place and above water for the next three months. For example, the SBA Paycheck Protection Program is designed to keep people of business payrolls until the end of June.
- <u>Restarting the Economy</u> - The state and federal plan for getting people back to work is not coming together in a highly coordinated manner. This will make for disparate results and could result in setbacks that require reinstituting "shelter-in- place" orders.

2. Long-Term Challenges

Beyond the next three months, what can we expect? The longer the economic shutdown, the harder it will be to manage the impacts to the economy and society in general. For our clients, the following issues will become more prominent.

- <u>Commercial Real Estate Repricing and Value Adjustments</u> - Increasing commercial and residential vacancies will require a regionwide repricing of real estate assets. Lease rates and real estate values will drop as demand for such space drops.
- <u>Repositioning Commercial Assets</u> - REITS, developers and CRE investors will have to reposition and repurpose real estate assets due to declining demand. This will require changes in use over time; particularly in the retail segment, which was in transition before COVID-19.
- <u>Accelerated e-Commerce Growth</u> - Accelerated growth of e-commerce, which by some measures may include 15 to 18 percent of consumable retail purchases (excluding motor cars and gasoline), will accelerate as many traditional retail players go out of business or go through their owner restructuring. Some larger retail stores might be repurposed as regional e-Commerce delivery/pickup centers to reduce industry wide delivery costs.
- <u>Housing Market Pause and Resetting of Prices</u>- Regional resetting of housing prices due to financial dislocations will make housing more accessible in the near-term as the market sorts out the effects of COVID-19. However, the region's housing shortage could eventually counter-balance short-term price drops. If mass foreclosures occur, then rental properties will likely experience stronger demand, like the aftermath of the Greater Recession. Mortgage rates are currently very low and are likely to remain low for several years.
- <u>Increased Telecommuting and Decreasing Demand for Office Space</u> - Telecommuting may have been given a clear view into the future. While not available to all members of the workforce, the DC Region has a very large professional workforce that can work remotely and often does. Advances in video conferencing technology may allow for a larger segment of the office workforce to work from home. This may reduce the demand for office space, regional highways and public transit systems for certain workers.

- Tax Revenue Declines and Tax Base Instability - Local governments may see sustained drops in real property, sales and income tax revenues over the next several years, particularly if there is a drop in real estate values and increased foreclosure and commercial vacancies. This will require government leaders to reexamine the long-term stability of their tax base and their current taxing structure to reduce vulnerabilities in the future.

"A Journey of a Thousand Miles Begins with a Single Step"

Lao Tzu, a major figure in Chinese philosophy, is credited with this famous proverb and it speaks to our journey ahead. The Washington, DC Metropolitan Region will do what is necessary to recreate itself and to bring future prosperity to our communities. Until a vaccine or therapeutic drugs are found, we will have to endure the societal changes necessary to keep us safe and our economy will have to innovate from that baseline reality. As a company, RKG Associates is committed to working closely its clients to help devise creative solutions to address problems that have never been seen before. Whatever the circumstances, we will get through this together and will create our "new normal" in partnership to make a stronger region.

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