News from:

COMPTROLLER KEVIN LEMBO

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COMPTROLLER LEMBO REPORTS $393.4-MILLION DEFICIT AFTER CONTINUED INCOME TAX EROSION

Comptroller Kevin Lembo today announced that continued erosion of the state income tax – likely due to a combination of investors relying more on tax-friendly investment funds, an economic trend towards lower-paying jobs and population loss – has increased the current fiscal year deficit to $393.4 million.

The Budget Reserve Fund has a current balance of $235.58 million, which is insufficient to cover the current General Fund deficit.

In a letter to Gov. Dannel P. Malloy, Lembo said his deficit projection is approximately $3.6 million higher than the deficit reported by the Office of Policy and Management (OPM) because Lembo believes the state will spend more than initially planned on ongoing settlement payments related to the SEBAC vs. Rowland case.

"Connecticut's budget performance is a reflection of our national and state economies," Lembo said. "Over at least the past two months, I have expressed concern regarding final income tax collections.

"History demonstrates that final April collections typically move in the same direction as the quarterly estimated income tax payments collected earlier in the fiscal year. For the first two quarterly deposits of the fiscal year, estimated payments were running more than 8 percent below last year. This raised significant concerns – now proven true – about final payment collections. It now appears that final payments will be approximately 10 percent below last fiscal year's level."

Connecticut joins nearly 20 other states facing eroding income tax revenue – however, Lembo said that Connecticut also faces its own unique structural problems, including unfunded pension liabilities and retiree health costs.

Lembo said the most significant deterioration in the General Fund's fiscal outlook occurred in the projection for income tax receipts, which are now $450.7 million below last month's estimate and $532.2 million off from the original budget plan.

Gov. Malloy's administration had an optimistic view regarding the potential for gains due to a significant run-up in the stock market at the end of 2016, Lembo said.

"Those gains have not materialized," Lembo said, pointing to increasing popularity of "tax efficient" investments such as Exchange Traded Funds (ETFs). "These funds are designed, in part, to minimize capital gains taxes."

In the United States, ETF assets increased from $157 billion in 2003 to $2.8 trillion by March 2017.

In addition to the drop in estimated and final income tax payments, there has been a significant downturn in the withholding portion of the income tax, which is responsible for over 60 percent of total income tax revenue.

"A general shift in the composition of employment by sector to lower paying jobs may be a contributing factor," Lembo said. "In addition to greater use of tax advantaged investments, the state's population loss may also have played a role in the disappointing final payment results."

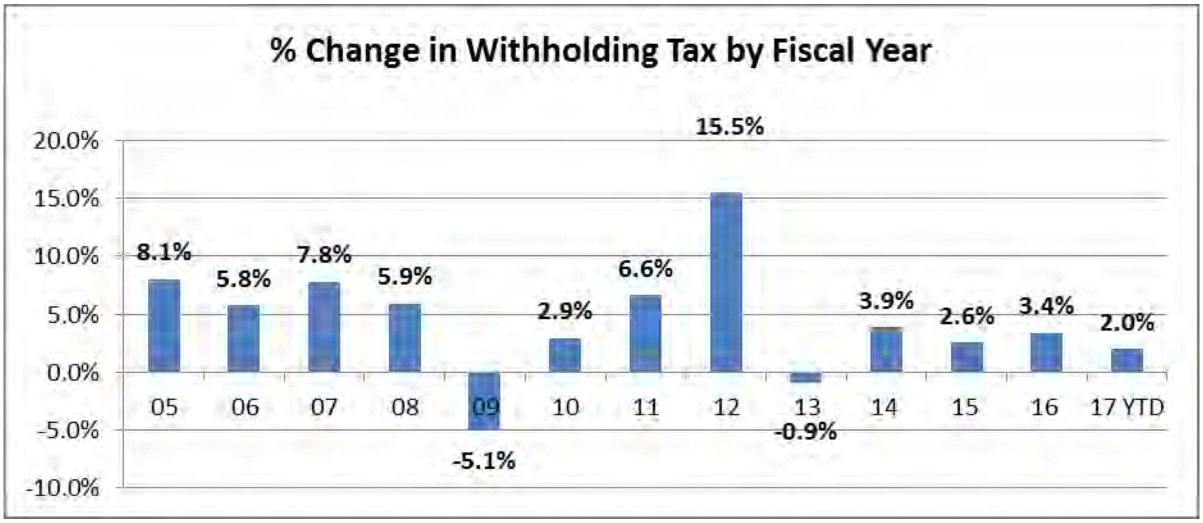
Lembo said U.S. census data shows that Connecticut experienced a decline in population of 8,278 residents between July 1, 2015 and July 1, 2016. Connecticut was one of only eight states to experience a decline in population during this period – and has now posted three consecutive years of population decline.

As far as spending, Lembo said aggressive budgeted saving targets are being largely achieved.

Lembo pointed to latest available economic indicators from federal and state Departments of Labor and other sources that show:

Employment

- In Fiscal Year 2016 the withholding portion of the income tax increased 3.4 percent from the prior fiscal year. Through March of Fiscal Year 2017, these receipts were up 2 percent from last year. Adjusting for timing differences between fiscal years in deposit days by month, the withholding tax trend has been running below last fiscal year and decelerating in recent months. That slowing trend appears to be continuing through April.



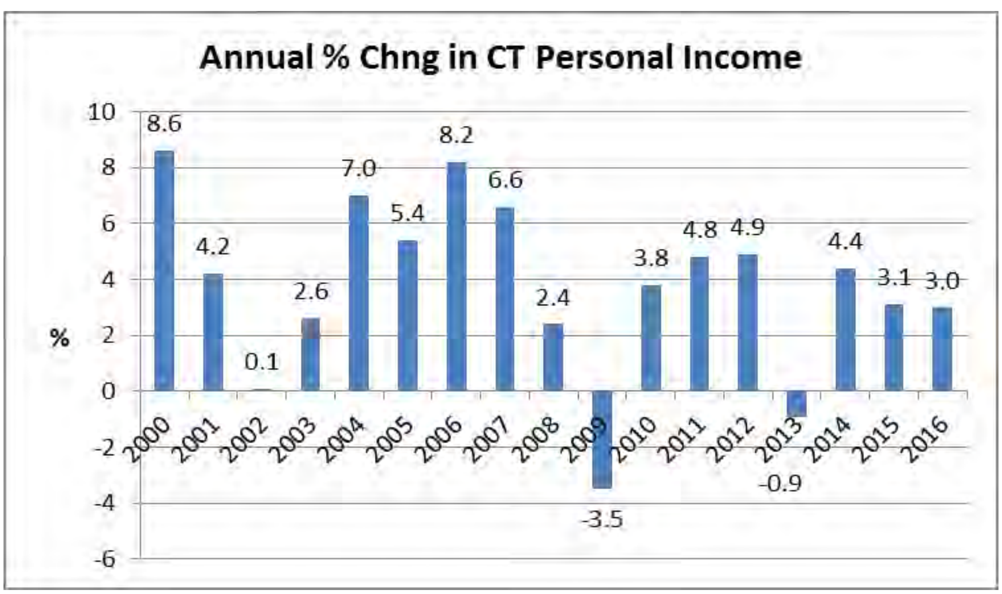
- According to 2016 benchmark revisions by the U.S. Bureau of Labor Statistics, Connecticut lost 200 jobs in calendar year 2016. After strong first-quarter employment growth, the employment situation in the state became more erratic. The final quarter of 2016 posted a net loss of jobs.
- The business payroll survey showed that the state gained 1,300 net jobs (0.1 percent) in March 2017, to a level of 1,685,400, seasonally adjusted. The state has now posted job growth in each month of the first quarter putting Connecticut ahead of last year's strong pace of employment growth. The 2017 first-quarter job gains total 7,900; in the first quarter of 2016 employment grew by 6,100.

jobs in thousands				
Sector	3/17	3/16	Gain/Loss	% Chng.
Construction	59.0	60.8	-1.8	-3.0%
Manufacturing	156.5	156.3	0.2	0.1%
Transp. & Public Utilities	299.1	299.3	-0.2	-0.1%
Information	31.6	32.4	-0.8	-2.5%
Financial	131.5	130.3	1.2	0.9%
Prof . & Business Svc.	218.3	218.7	-0.4	-0.2%
Education & Health Svc.	331.1	329.4	1.7	0.5%
Leisure & Hospitality	156.7	153.3	3.4	2.2%
Other Services	67.3	64.7	2.6	4.0%
Government	233.7	238.0	-4.3	-1.8%

- Connecticut's unemployment rate for March increased by one tenth of a point to 4.8 percent - six tenths of a point lower than it was a year ago. While the unemployment rate moved up in March, the labor force also expanded as discouraged job seekers re-entered the labor market.
- All of the employment and labor force data must be considered in light of the erosion in the state's total population over recent years. According to U.S. census data, Connecticut saw a decline in population of 8,278 residents between July 1, 2015 and July 1, 2016. Connecticut was one of only eight states to experience a decline in population during this period. Connecticut has now posted three consecutive years of population decline.

Wage and $alary income

- Average hourly earnings at $31.34, not seasonally adjusted, were up $1.24, or 4.1 percent, from the March 2016 estimate ($30.10). The resultant average Private Sector weekly pay amounted to $1,031.09, up $31.77, or 3.2 percent higher than a year ago.
- The Consumer Price Index (CPI-U) was 2.7 percent in February and remained at that level in March.
- According to a March 28 release from the Bureau of Economic Analysis, Connecticut's personal income grew by 3 percent between 2015 and 2016. This ranked Connecticut 33rd nationally in 2016 income growth. Connecticut had the slowest rate of growth in New England. However, Connecticut ranked number one nationally in per-capita personal income in 2016 with income of $71,033.



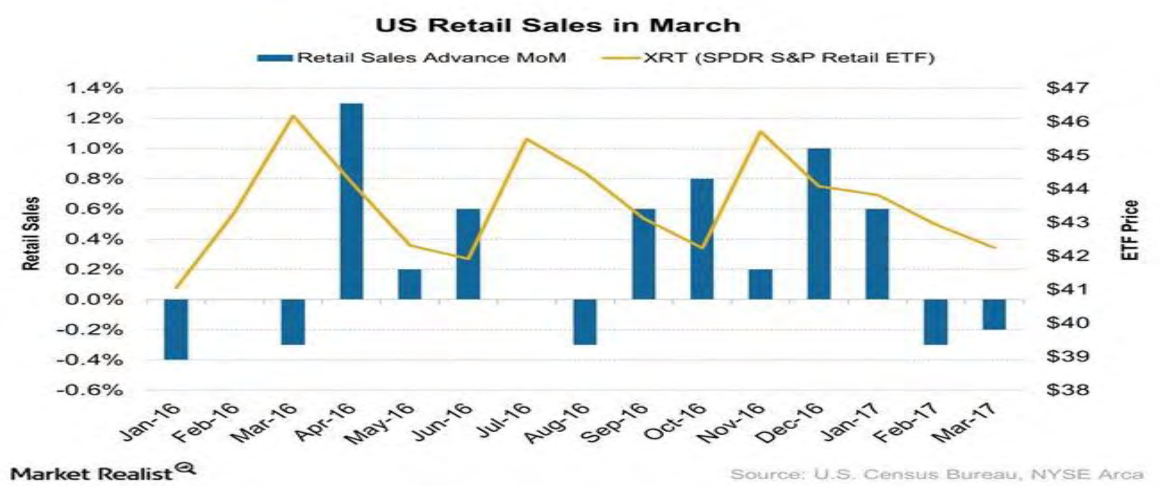
- Connecticut's fourth-quarter results for 2016 were better than the full year results. The fourth-quarter growth annualizes to a rate closer to 4 percent, which ranked the state at 21 nationally for fourth-quarter growth. Results for the first quarter of 2017 will be available on June 27.

Housing

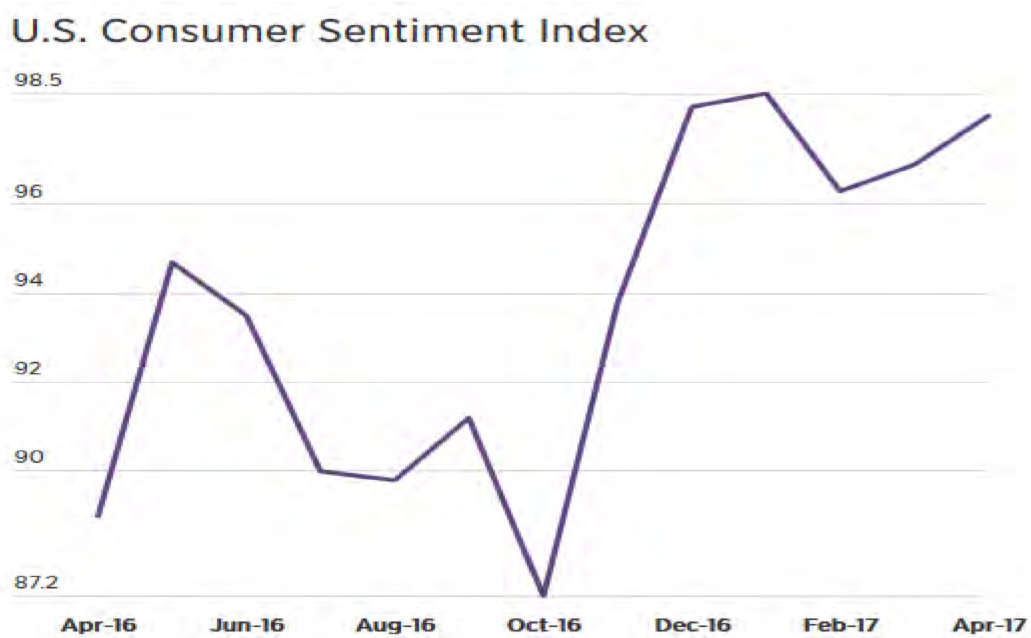
- According to a report from CT Realtors, the sale of single-family residential homes in Connecticut increased by 5.1 percent in March 2017 from the same month a year earlier. The median sales price of a home increased by 2.2 percent to $237,000. Connecticut has been in a sustained period of sales volume gains since 2012; prices have also been rebounding in recent months. Townhouse and condominium sales also grew 17.3 percent in March with the median price up 7.1 percent at $151,000.
- Nationally, existing-home sales took off in March to their highest pace in over 10 years, and severe supply shortages resulted in the typical home coming off the market significantly faster than a year ago, according to the National Association of Realtors. Only the West saw a decline in sales activity in March.
- The sale of existing homes in the U.S. increased by 4.4 percent in March. The median existing-home price for all housing types in March was $236,400, up 6.8 percent from March 2016 ($221,400). March's price increase marks the 61st consecutive month of year-over-year gains.
- With mortgage rates moving up, many economists have forecasted that 2017 will be a slower year for the housing market than 2016. Some of the strongest sales numbers in more than a decade were seen in 2016.

Consumers

- According to data provided by the U.S. Census Bureau on April 14, U.S. retail sales fell 0.2 percent in March 2017. Sales fell 0.3 percent in February 2017. It was the second consecutive month of falling sales.
- Weaker retail sales were mainly the result of small gains in motor vehicle sales. Core retail sales, which track to the performance of the consumer spending segment of the GDP, remained unchanged in March 2017. Consumer prices have been rising at the fastest pace in five years, eating into purchasing power amid slow wage gains.



- The University of Michigan Surveys of Consumers said its preliminary April consumer sentiment index rose to 98.0, its strongest level since November 2000. The survey is divided into two sections: current economic conditions, and future economic outlook. Consumers' views on current conditions jumped to 115.2 in April from 113.2 in March. That's the highest level since 2000. The gauge of consumers' expectations improved only slightly in April to 86.9 from 86.5 in the prior month.

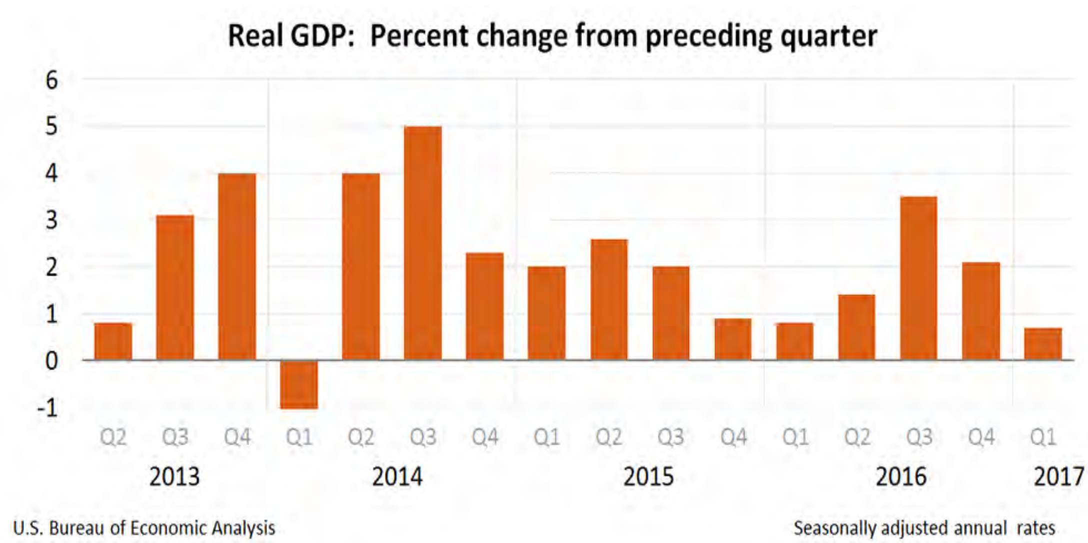


- Another measure of consumer confidence reported by the Conference Board showed an April pull-back in confidence with the index falling to 120.3 this month from 124.9 in March. The March index was the highest reading since December 2000. The index in April was the second highest reading since 2000.

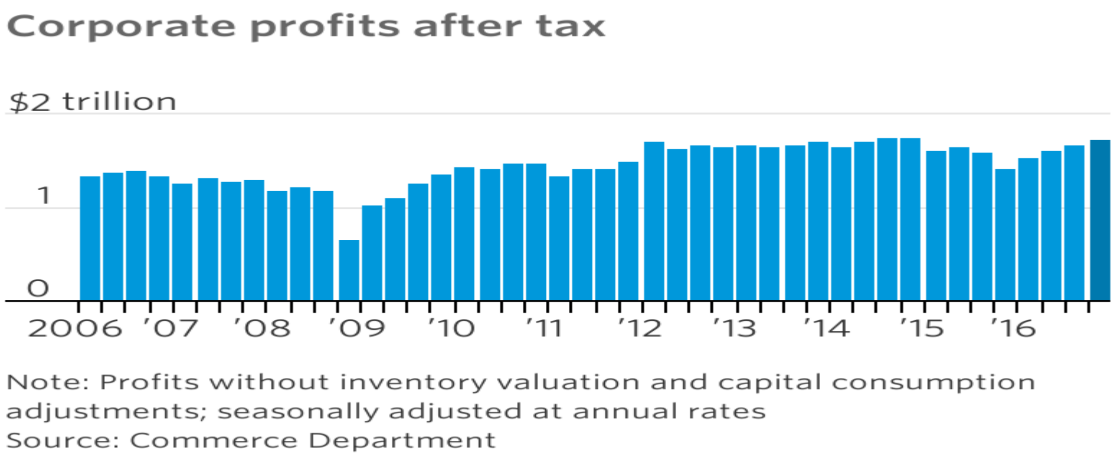
- The Federal Reserve Bank reported on April 7 that in February, consumer credit increased at a seasonally adjusted annual rate of 4.8 percent. Revolving credit decreased at an annual rate of 3.5 percent, while the much larger non-revolving credit category increased at an annual rate of 5.3 percent. Over the prior five-year period, consumer credit has expanded at an annual rate of 6.5 percent.

Business & Economic Growth

- According to the April 28 advance estimate from the Bureau of Economic Analysis, real GDP in the first quarter of 2017 grew at a 0.7-percent annual rate. In the fourth quarter of 2016 GDP grew at a 2.1-percent rate.
- The deceleration in real GDP in the first quarter reflected a deceleration in personal consumption expenditures and downturns in private inventory investment and in state and local government spending that were partly offset by an upturn in exports and accelerations in both nonresidential and residential fixed investment.

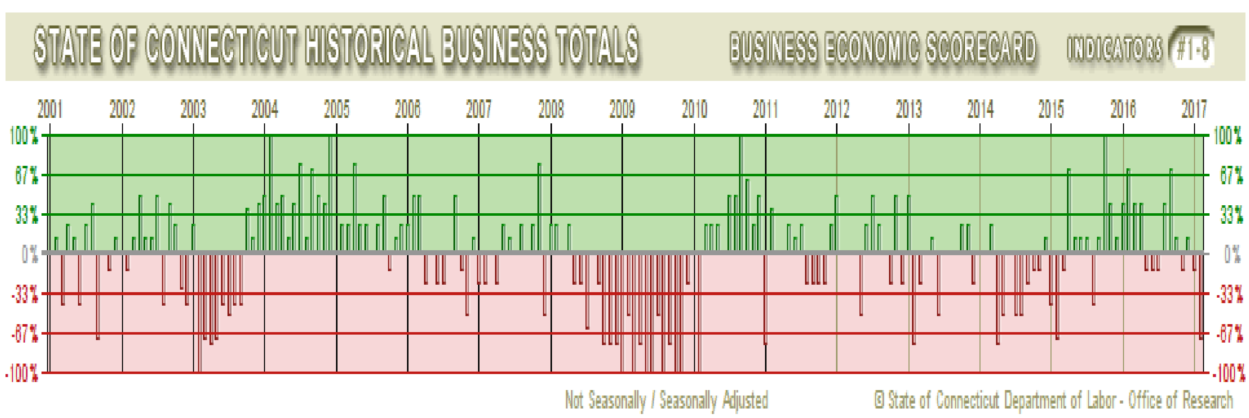


- Corporate profit figures for the first quarter will be available on May 26. Corporate profits after tax, without inventory valuation and capital consumption adjustments, rose 3.7 percent in the fourth quarter from the prior quarter to a seasonally adjusted annual rate of $1.741 trillion. It was the fourth consecutive quarter of profits growth.



- For all of 2016, profits rose 4.3 percent after falling 8.5 percent in 2015. Earnings fell in 2015 as exports declined on a strengthening dollar, energy prices and other commodity prices softened and global growth weakened. But oil prices stabilized last year and the global outlook has brightened, helping bolster U.S. businesses.
- According to the Commerce Department's April 27 report, orders for durable goods (products meant to last at least three years) rose 0.7 percent after a 2.3-percent February advance. Excluding transportation-equipment demand, which is volatile, orders fell 0.2 percent, the first decline since June. Orders for civilian aircraft and parts rose 7 percent in March; defense capital-goods orders jumped 12.2 percent.
- The figures indicate that the slowdown in auto demand from consumers and tepid business investment weighed on manufacturers and reduced economic momentum at the end of the first quarter.
- The service-sector, which is the largest sector of the economy, hit a seven month low in April with a reading of 52.7 according to the Markit Flash U.S. Services PMI Business Activity Index.
- April data showed the weakest rise in private sector payroll numbers since February 2010, driven by a softer pace of staff hiring among service providers. There were signs of diminished operating margins in April, as input price inflation reached its strongest since June 2015. At the same time, prices charged by U.S. private sector firms increased only marginally and at the slowest pace since November 2016.
- The Markit Composite PMI for all sectors also weakened in April.

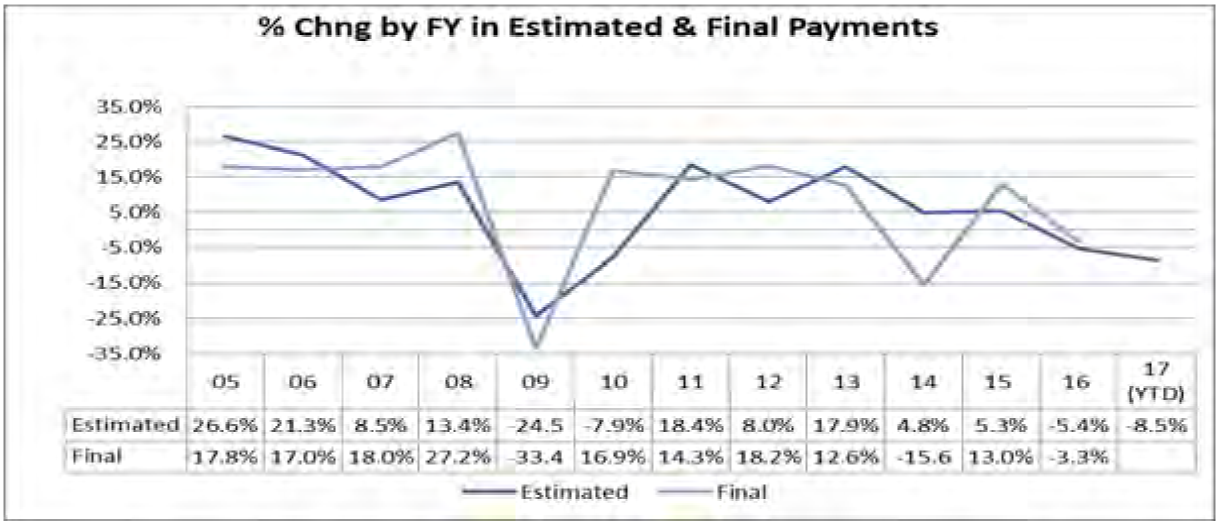
- The Department of Labor's Business Economic Scorecard tracks the up and down movement in some key indicators for the state, including: housing permits, air cargo, exports, gaming slots, visits to major attractions, air passenger count, the CT manufacturing production index and average weekly manufacturing hours. As the graph shows, the current recovery has not been as strong as the last recovery period. Between late 2003 and 2006 there were no negative readings. This recovery has seen sporadic negative results, but still well above the recessionary period.



Stock Market

- Estimated and final income tax payments account for approximately 40 percent of total state income tax receipts. Both the estimated and final payments had a negative rate of growth in Fiscal Year 2016.

- Two large quarterly estimated income tax payments for Fiscal Year 2017 have been deposited. Estimated payments through March were down 8.5 percent from last year. As can been seen from the graph, it is typical for final income tax payments to follow the direction of estimated payments.
- At this writing it appears that the final income tax payments will be approximately 10 percent below the level attained in Fiscal Year 2016. This results in a total decline in the income tax from last fiscal year of $532.2 million or -2.1 percent.
- The run-up in the stock market at the end of 2016 did not translate into higher capital gains revenue for the State of Connecticut.



	05	06	07	08	09	10	11	12	13	14	15	16	17 (YTD)
Estimated	26.6%	21.3%	8.5%	13.4%	-24.5	-7.9%	18.4%	8.0%	17.9%	4.8%	5.3%	-5.4%	-8.5%
Final	17.8%	17.0%	18.0%	27.2%	-33.4	16.9%	14.3%	18.2%	12.6%	-15.6	13.0%	-3.3%	

- The equity markets have experienced some recent volatility, but at this writing, 2017 results remain positive.

DOW

S&P

- Some of the diminishment in revenue from capital gains may be attributed to the increasing use by investors of tax-advantaged vehicles such as Exchange Traded Funds (ETF). The increase in these investments is shown in the graph below.

Year	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	Mar-17
# ETFs	123	157	207	350	608	704	778	902	1,093	1,161	1,259	1,377	1,570	1,706	1,734
# ETFs/ETPs	134	169	221	381	673	845	925	1,099	1,369	1,447	1,536	1,662	1,845	1,970	2,000
ETF assets	151	228	305	416	586	498	706	893	938	1,212	1,612	1,918	2,060	2,465	2,710
ETF/ETP assets	157	237	311	433	621	539	790	1,009	1,060	1,347	1,698	2,002	2,130	2,549	2,798

Source: ETFGI data sourced from ETF/ETP sponsors, exchanges, regulatory filings, Thomson Reuters/Lipper, Bloomberg, publicly available sources and data generated in-house.
Note: "ETFs" are typically open-end index funds that provide daily portfolio transparency, are listed and traded on exchanges like stocks on a secondary basis as well as utilising a unique creation and redemption process for primary transactions. "ETPs" refers to other products that have similarities to ETFs in the way they trade and settle but they do not use a mutual fund structure. The use of other structures including grantor trusts, partnerships, notes and depositary receipts by ETPs can create different tax and regulatory implications for investors when compared to ETFs which are funds.

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