News from:

# COMPTROLLER KEVIN LEMBO

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## COMPTROLLER LEMBO PROJECTS $504.6-MILLION DEFICIT FOR FISCAL YEAR 2018

Comptroller Kevin Lembo today projected a Fiscal Year 2018 deficit of $504.6 million, an improvement of $89.9 million over last month's projection due to a combination of spending restraints and increased revenues.

In a letter to Gov. Dannel P. Malloy, Lembo said that the final unaudited report on the close of Fiscal Year 2018 revenues and expenditures will be presented at the end of September.

Lembo said that projected spending was $45.4 million lower than anticipated through June, while General Fund revenues have increased by $51 million compared with last month's projection. Revenue streams that exceeded budget expectations included the withholding portion of the income tax (+$29.2 million), and the corporation tax (+$18.8 million), while other categories increased by a net $3 million.

"In addition, OPM's (state Office of Policy and Management) forecast of the estimated and final portion of the income tax has increased by $110 million since last month based on strong June collections," Lembo said. "Due to the statutory volatility cap provision, this change will result in a higher than anticipated transfer to the Budget Reserve Fund (BRF) instead of reducing the General Fund deficit."

Lembo said that estimated and final income tax collections are expected to exceed the state's new volatility threshold by $1.46 billion. Due to Public Act 18-81, An Act Concerning Revisions to the State Budget for Fiscal Year 2019 and Deficiency Appropriations for Fiscal Year 2018, some of this windfall will be used to close the Fiscal Year 2018 deficit and provide resources for Fiscal Year 2019.

As a result, Lembo projects that $940 million will ultimately be transferred into the BRF after the close of the fiscal year. That deposit would bring the total balance of the BRF to $1.15 billion, which is approximately 6.1 percent of the revised General Fund budget for Fiscal Year 2019.

"My office has traditionally recommended the rainy day fund reach a level of 15 percent of General Fund expenditures to protect against a future downturn," Lembo said.

In his economic summary, Lembo included comprehensive data about Connecticut's, and the national, economic outlook.

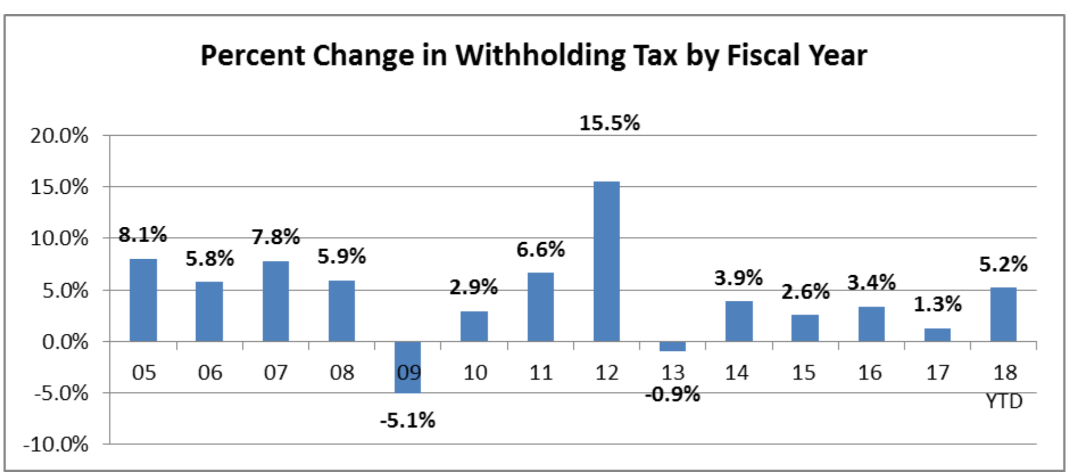
"I have said it before – but I must say it again – that slow wage growth demands watching," Lembo said. "Despite good news on the economic front, GDP growth and the recent tax cuts are only translating into modest wage gains for many families. A closer analysis shows wage growth has been concentrated at the top of the income scale, while lower and middle income groups have seen wages stagnating.

"Connecticut's budget results are ultimately dependent upon the performance of the national and state economies."

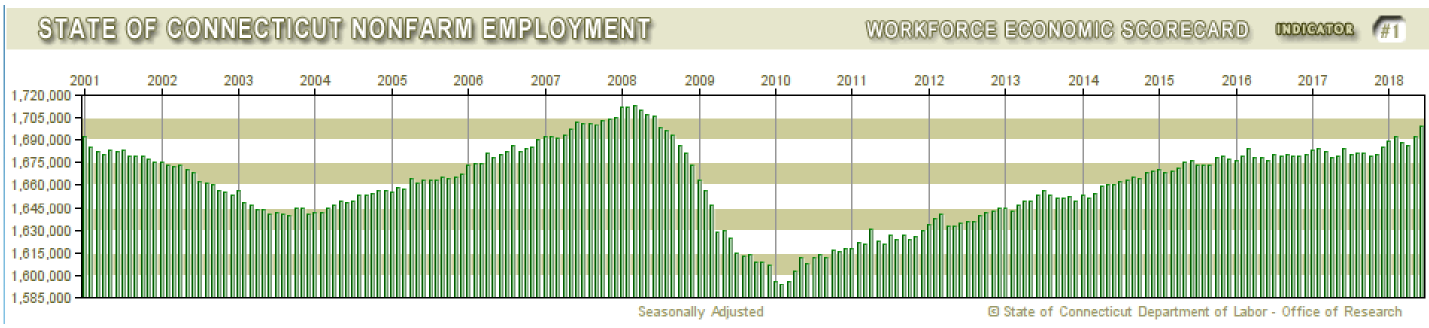
Lembo said the latest economic indicators from federal and state Departments of Labor (DOL) and other sources show:

## *Employment*

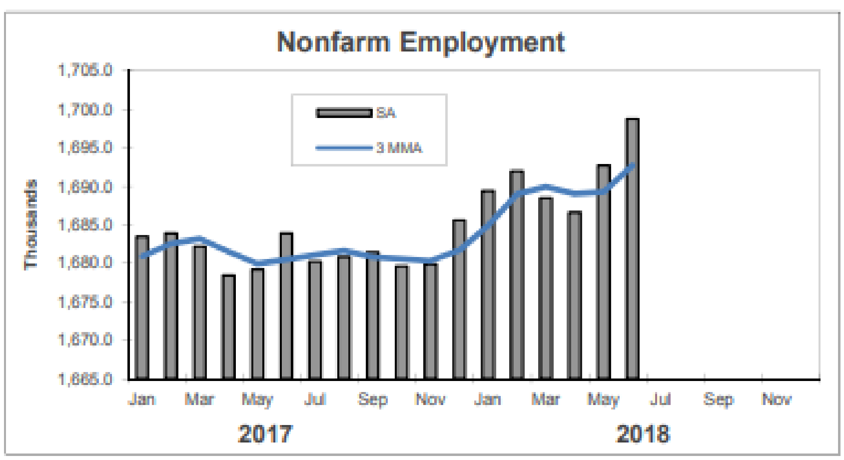
- Preliminary results for FY 2018 show withholding receipts were up 5.2 percent compared with the prior fiscal year. This positive development likely reflects a strong bonus season for the financial industry and more robust job growth toward the end of FY 2018. Please note: the State budget process includes statutory revenue accrual adjustment, which could have an impact on the final figures to be published at the end of September.



- On July 19, Connecticut DOL reported the preliminary Connecticut nonfarm job estimates for June 2018 from the business payroll survey administered by the US Bureau of Labor Statistics (BLS). DOL's Labor Situation report showed the state gained 6,100 net jobs (0.4%) in June, to a level of 1,698,800, seasonally adjusted. May's originally-released job gain of 4,100 was revised up by 2,000 to a gain of 6,100 over the month. May and June's increases followed two consecutive months of job losses.

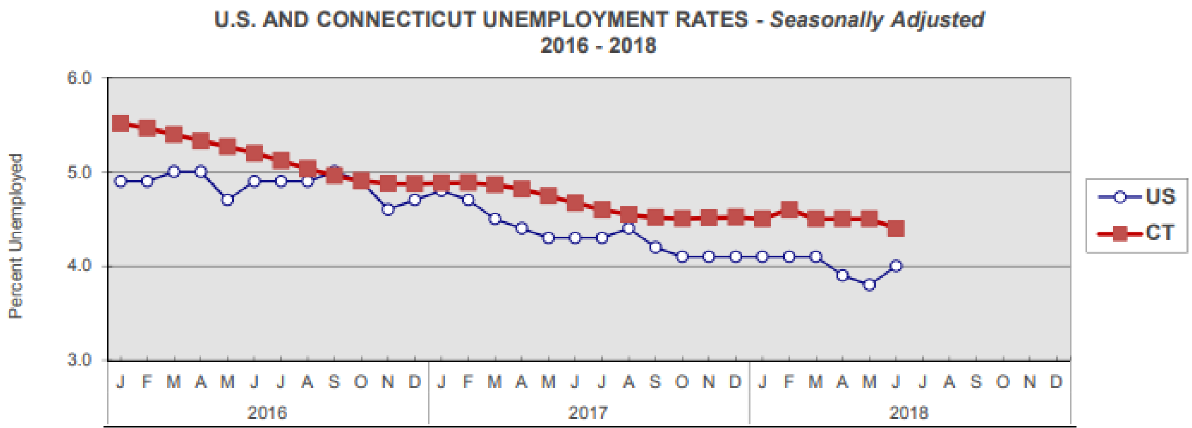



- The largest monthly job gains in June were in Leisure & Hospitality (+2,400), Education & Health Services (+1,900), Construction (+1,200) and Professional & Business Services (+1,100). The Government sector lost a total of 1,500 jobs in June. The Government category includes federal, state, local governments, public higher education and Native American casino employment.
- Over the year, DOL reported that nonagricultural employment in the state grew by 14,900 jobs on a seasonally-adjusted basis.




- Connecticut has now recovered 87.8% (104,600 payroll job additions) of the 119,100 seasonally adjusted jobs lost in the Great Recession (3/08-2/10). The job recovery is into its 100th month and the state needs an additional 14,500 jobs to reach an overall employment expansion. DOL notes that private sector job growth has outpaced that of the government sector. Connecticut's private sector has recovered 111.2 percent (127,900) of private sector jobs lost in the same downturn.

- Connecticut's unemployment rate is estimated at 4.4 percent in June, down one-tenth of a point from May 2018 and down three-tenths of point from a year ago when it was 4.7 percent. Nationally, the unemployment rate was 4 percent in June 2018, up two-tenths of a point from May. The chart below shows a comparison of the Connecticut and U.S. unemployment rates for the past three calendar years.



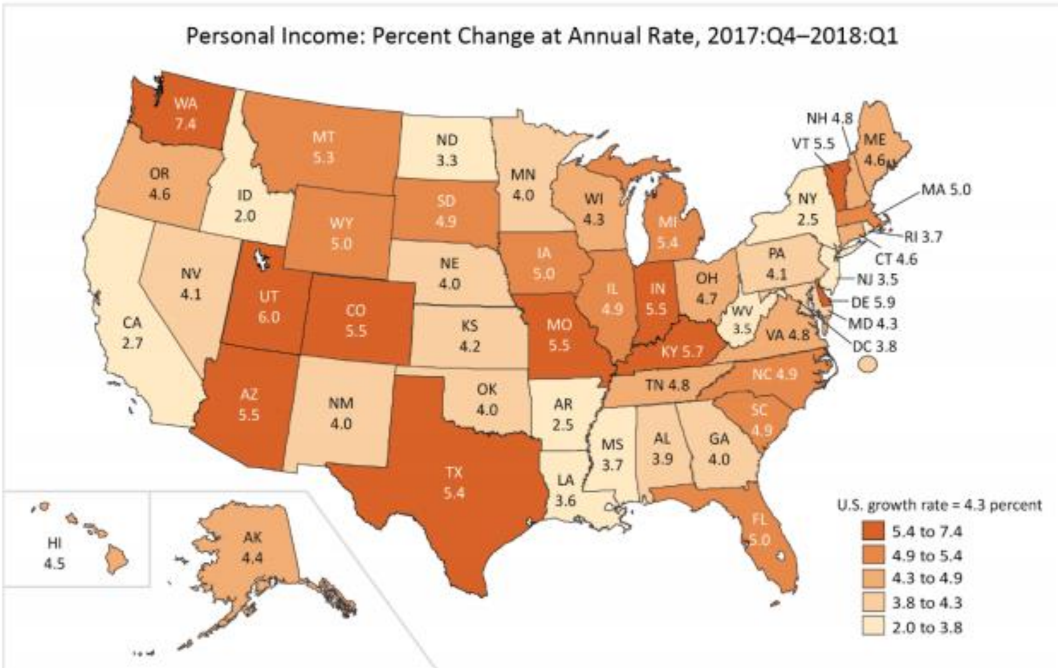

- DOL reports that June 2018 seasonally adjusted average weekly initial unemployment claims for first-time filers in Connecticut grew by 69 claimants (+2.2%) to 3,211 from May 2018 and were lower by 609 claims (-15.9%) from the June 2017 level of 3,820.
- Among the major job sectors listed on the following page, six experienced gains, three experienced losses and one sector was unchanged in June 2018 versus June 2017 levels. DOL noted construction and manufacturing are now the fastest growing sectors in the state's labor market.

| **Payroll Employment Trend** | | | | |
|---|---|---|---|---|
| ***Jobs in thousands*** | | | | |
| **Sector** | **6/18 (P)** | **6/17** | **Gain/Loss (000's)** | **% Change** |
| Construction | 60.7 | 58.6 | 2.1 | 3.6% |
| Manufacturing | 164.0 | 159.1 | 4.9 | 3.1% |
| Transp. & Public Utilities | 299.5 | 297.8 | 1.7 | 0.6% |
| Information | 30.9 | 31.7 | -0.8 | -2.5% |
| Financial | 127.9 | 128.0 | -0.1 | -0.1% |
| Prof. & Business Svc. | 222.3 | 218.3 | 4.0 | 1.8% |
| Education & Health Svc. | 341.1 | 334.9 | 6.2 | 1.9% |
| Leisure & Hospitality | 158.5 | 157.1 | 1.4 | 0.9% |
| Other Services | 65.2 | 65.2 | 0.0 | 0.0% |
| Government | 228.1 | 232.6 | -4.5 | -1.9% |

## *Wage and $alary income*

- June 2018 average hourly earnings at $31.31, not seasonally adjusted, were up $0.53, or 1.7 percent, from the June 2017 estimate. The resultant average private sector weekly pay amounted to $1,058.28, up $24.07 or 2.3 percent higher than a year ago.
- The 12-month percent change in the Consumer Price Index for All Urban Consumers (CPI-U, U.S. City Average, not seasonally adjusted) in June 2018 was 2.9 percent.
- On June 21, the Bureau of Economic Analysis reported that Connecticut's personal income grew by a 4.6-percent annual rate between the fourth quarter of 2017 and the first quarter of 2018. This ranked Connecticut 27th nationally in first quarter income growth, somewhat higher than the national average of 4.3 percent.  The change in personal income across all states ranged from 7.4 percent in Washington to 2.0 percent in Idaho.
- This represents an improvement from the annual results for 2017.  BEA reported that Connecticut's personal income grew by only 1.5 percent between 2016 and 2017, which ranked 44th nationally.

- The Bureau of Economic Analysis will release State Quarterly Personal Income for the 2nd Quarter of 2018 on September 25, 2018.




U.S. Bureau of Economic Analysis

## *Housing*

- In its July 7 release, Berkshire Hathaway HomeServices reported results for the Connecticut housing market for June 2018 compared with June 2017. Sales of single family homes fell 7.99 percent, while the median sale price rose 4.69 percent. New listings decreased by 5.57 percent in Connecticut and the median list price increased by 6.82 percent to $299,000. Average days on the market grew 20.29 percent in June 2018 compared to the same month in the previous year (83 days on average, up from 69 days). Finally, the list to sell price rose slightly to 97.8 percent, compared with 97.6 percent a year ago. The next table contains more detailed data for the Connecticut housing market.

MARKET SUMMARY

JUNE 2018 | SINGLE FAMILY HOMES

| Market Summary | Month to Date | | | Year to Date | | |
|---|---|---|---|---|---|---|
| | June 2018 | June 2017 | Percent Change | Year-To-Date 2018 | Year-To-Date 2017 | Percent Change |
| New Listings | 5641 | 5974 | -5.57% ▼ | 31408 | 32726 | -4.03% ▼ |
| Sold Listings | 4029 | 4379 | -7.99% ▼ | 16395 | 17040 | -3.79% ▼ |
| Median Listing Price | $299,000 | $279,900 | 6.82% ▲ | $267,999 | $256,650 | 4.42% ▲ |
| Median Selling Price | $290,000 | $277,000 | 4.69% ▲ | $260,000 | $250,000 | 4% ▲ |
| Median Days on Market | 59 | 39 | 51.28% ▲ | 66 | 50 | 32% ▲ |
| Average Listing Price | $430,581 | $426,064 | 1.06% ▲ | $399,023 | $395,000 | 1.02% ▲ |
| Average Selling Price | $416,404 | $412,800 | 0.87% ▲ | $383,880 | $379,044 | 1.28% ▲ |
| Average Days on Market | 83 | 69 | 20.29% ▲ | 94 | 82 | 14.63% ▲ |
| List/Sell Price Ratio | 97.8% | 97.6% | 0.13% ▲ | 97.3% | 97% | 0.32% ▲ |

- The following chart from Berkshire Hathaway HomeServices shows the total number of Connecticut single family homes for sale in June 2018 by list price:


**<u>Stock Market</u>**

- After a steady rise and strong gains throughout calendar 2017, several market indices reached their peak in late January 2018. Since then, there has been significant turbulence and uncertainty in the markets through July 2018.
- A number of issues have caused concerns for investors, including worries about inflation and rising interest rates; fears about an escalating trade war as the United States announced tariffs on products like steel and aluminum and threated to impose trade sanctions on China and other countries; apprehensions about rising bond yields that may cause investors to move from stocks to lower risk bonds; and general concerns that stocks may be over-valued and due for a correction.  On the up side, recent corporate earnings results have been generally positive.
- The technology-heavy NASDAQ index has continued its climb above the January 2018 peak, but experienced some significant declines in the past week.  The DOW

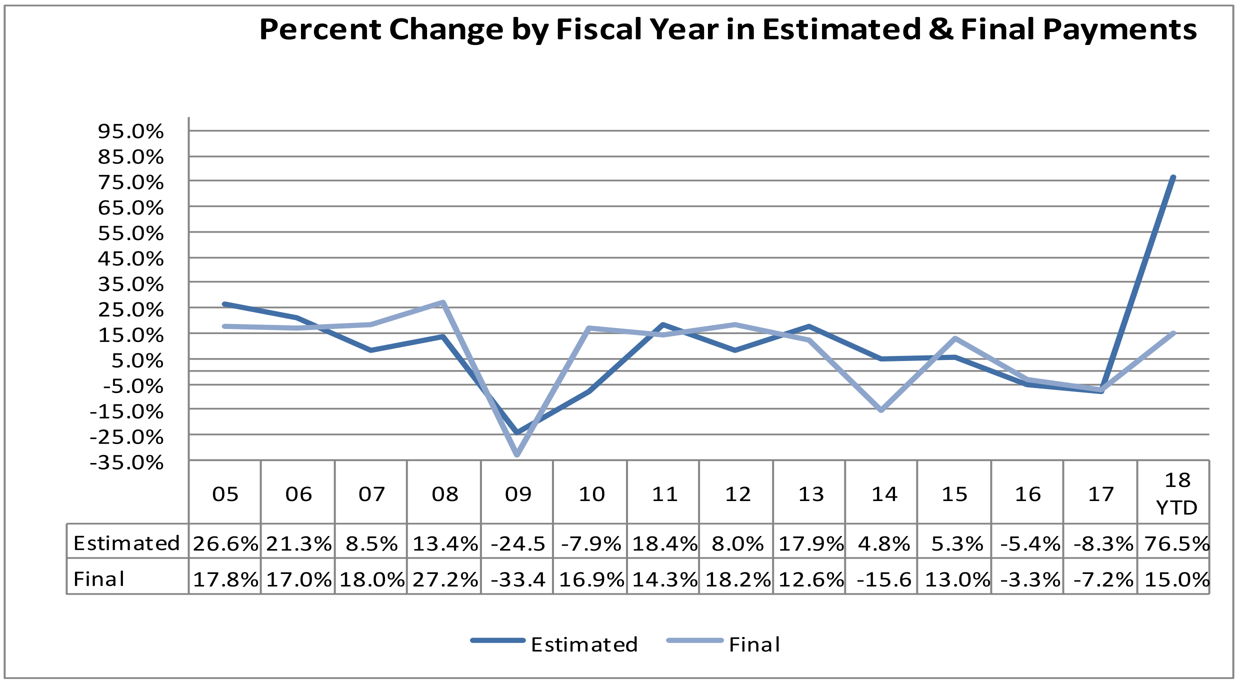
and S&P 500 index are still below highs set earlier in the year. Recent swings in the stock market are illustrated on the two charts that follow:

**DOW**


**NASDAQ**


- The performance of the stock market has a significant impact on the State of Connecticut's revenues. In a typical year, estimated and final income tax payments account for approximately 35 to 40 percent of total state income tax receipts, but can be an extremely volatile revenue source. Both estimated and final payments had negative growth rates in Fiscal Years 2016 and 2017.

- However, due to a combination of one-time events related to Federal tax changes, estimated payment collections increased substantially in December and January. June collections have also outperformed budget targets. Preliminary results through June 2018 show estimated payments growing by 76.5 percent fiscal year-to-date compared with the prior year, representing an increase of over $1.2 billion. Year-to-date final payments through June grew by $229.3 million or 15 percent over the same period a year ago.

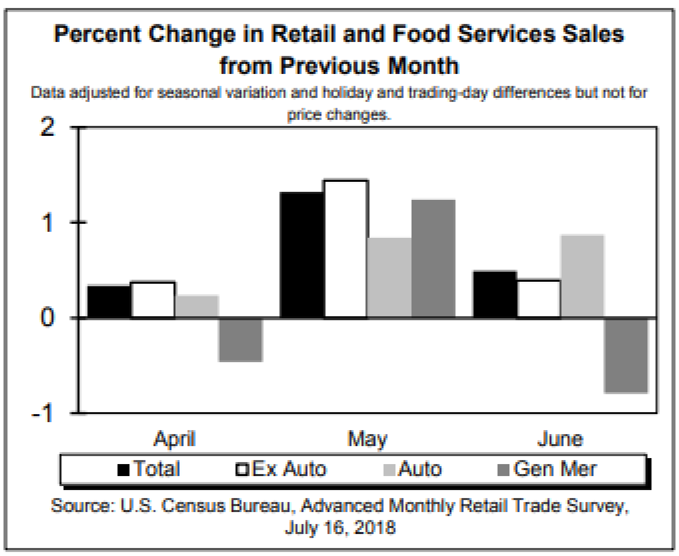



| | 05 | 06 | 07 | 08 | 09 | 10 | 11 | 12 | 13 | 14 | 15 | 16 | 17 | 18 YTD |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Estimated | 26.6% | 21.3% | 8.5% | 13.4% | -24.5 | -7.9% | 18.4% | 8.0% | 17.9% | 4.8% | 5.3% | -5.4% | -8.3% | 76.5% |
| Final | 17.8% | 17.0% | 18.0% | 27.2% | -33.4 | 16.9% | 14.3% | 18.2% | 12.6% | -15.6 | 13.0% | -3.3% | -7.2% | 15.0% |

- Initially, the revenue volatility adjustment contained in Section 704 of Public Act 17-2, June Special Session, required that any estimated and final payment collections amount above $3.15 billion would be transferred to the Budget Reserve Fund (BRF). Current projections by the State Comptroller's Office have estimated and final income tax collections totaling $4.61 billion for FY 2018, or $1.46 billion over the volatility threshold.
- However, based on the recently enacted state budget for FY 2019 (Public Act 18-81), a portion of this revenue windfall will now be used to close the General Fund deficit for FY 2018 and provide additional resources for FY 2019. After accounting for the projected FY 2018 deficit and various carry-forwards into FY 2019, approximately $940 million will be deposited into the BRF, bringing the total to $1.15 billion, about 6.1 percent of the revised budget for FY 2019. The State Comptroller recommends the BRF reach a level of 15 percent of General Fund expenditures to protect against a future downturn.

## Consumer Spending

- Consumer spending is the main engine of the U.S. economy, accounting for more than two-thirds of total economic output.
- U.S. retail sales rose solidly in June 2018, led by auto sales, gas station receipts and sales at building supply stores. The Commerce Department reported that advance retail sales grew 0.5 percent last month, to $506.8 billion. In addition, data for May was revised up to show sales rising 1.3 percent instead of the previously reported gain of 0.8 percent.
- Auto sales rose 0.9 percent and receipts at service stations grew 1.0 percent, reflecting higher gasoline prices. In June sales at building material stores rose 0.8 percent, after growing 2.5 percent in May. Sales at restaurants and bars increased 1.5 percent. On the down side, receipts at clothing stores fell 2.5 percent, the biggest drop since February 2017. In addition, spending at hobby, musical instrument and book stores declined 3.2 percent, representing the largest drop since December 2017.

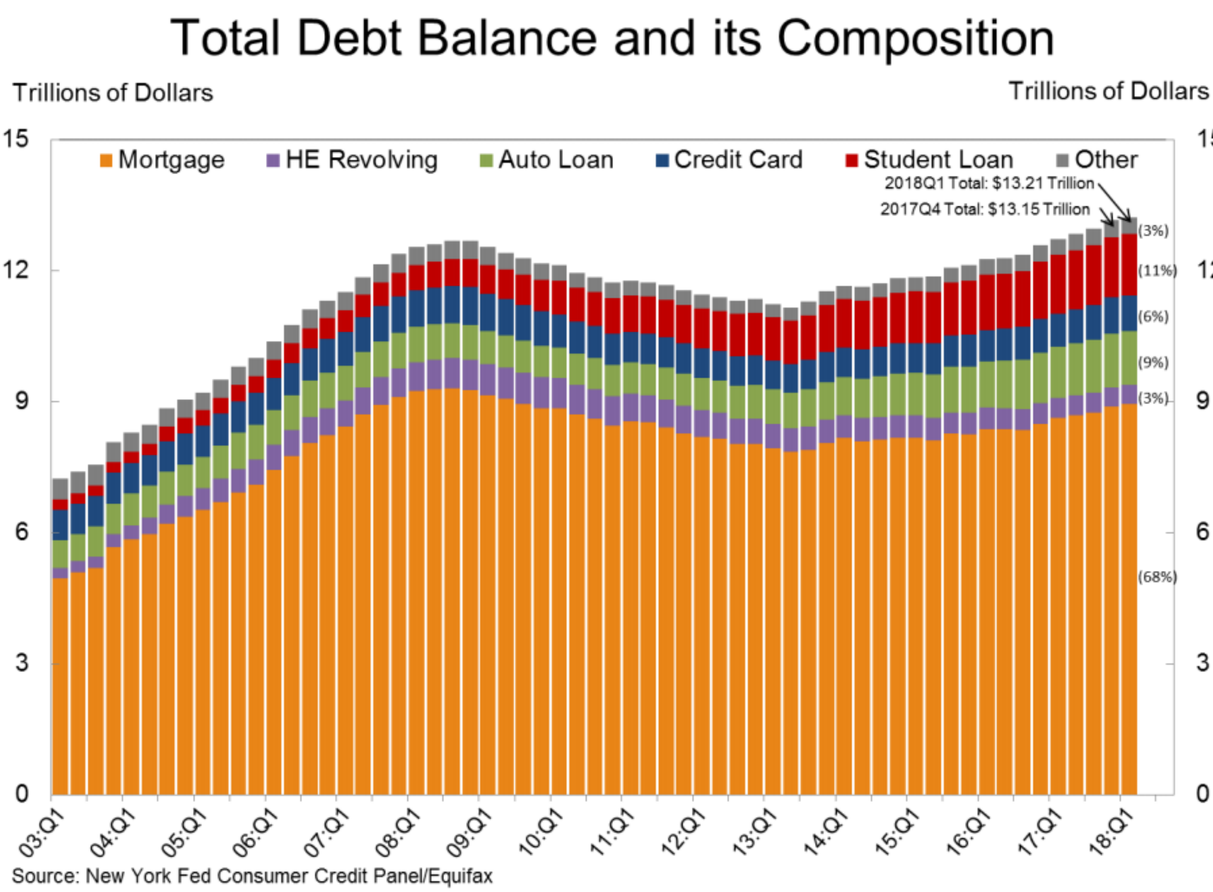



- In comparison to a year ago, the Commerce Department reported that retail sales were 6.4 percent above June 2017 levels. In addition, gas station sales were up 21.6 percent from June 2017, while non-store retailers grew 10.2 percent from last year.

## Consumer Debt and Savings Rates

- According to the Federal Reserve Bank of New York, aggregate household debt balances rose to another new peak in the first quarter of 2018. Household debt has now grown in 15 consecutive quarters. As of March 31, 2018, overall debt – including mortgages, auto loans, student loans and credit card debt – hit a record $13.21 trillion. This represented a $63 billion (0.5%) increase from the fourth quarter of 2017.

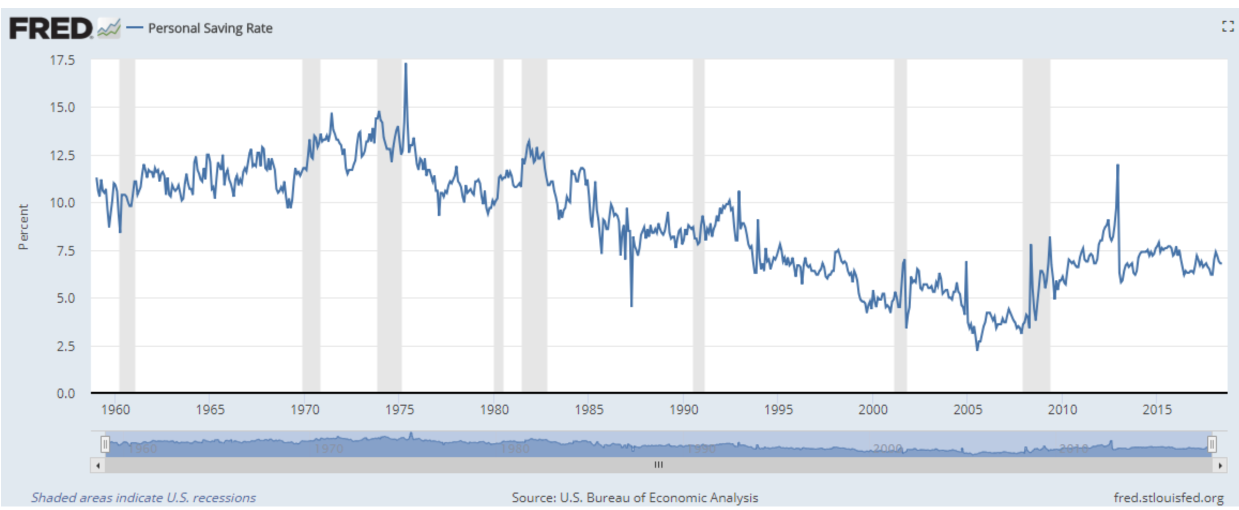
- The report noted balances climbed 0.6 percent on mortgages, 0.7 percent on auto loans, and 2.1 percent on student loans this past quarter, while they declined by 2.3 percent on credit cards. Although household debt has been growing for five years, its growth has been slow relative to earlier periods (see chart below), as mortgage debt has continued to be relatively flat.
- The next report, covering the second quarter of 2018, is scheduled for release in August 2018.




- In the first quarter, aggregate delinquency rates improved, as rates on mortgage and Home Equity Lines of Credit (HELOC) debt declined further, while delinquency on auto and credit card debt increased.
- In its July 31 release, the Bureau of Economic Analysis (BEA) reported the personal-saving rate was 6.8 percent in June, no change from May. Please note - BEA announced revisions to its methodology that are reflected in these estimates: In July,

the Bureau of Economic Analysis (BEA) released the initial results of the 15th comprehensive, or benchmark, update of the national income and product accounts (NIPAs). Comprehensive updates are usually conducted at 5-year intervals. The previous comprehensive update was released in July 2013.

- Higher debt levels and lower savings point to U.S. wage gains that are not keeping up with consumers' needs and desires to spend. This also signals a more uncertain outlook for future consumer spending gains. One explanation for this trend is the so-called wealth effect. Consumers may feel richer because the stock market is rising and home values have increased in recent years.
- The graph below provides a long-term view of the U.S. savings rate from the beginning of 1959 through June 2018. The personal savings rate is defined as personal saving as a percentage of disposable personal income. As can be seen, there is a general downward trend over the period. It should be noted that the U.S. Personal Saving Rate does not include capital gains from the sale of land or financial assets in its estimate of personal income. This effectively excludes capital gains – an important source of income for some.




- Despite the overall improvement in the nation's economy, income inequality continues to widen as wage growth remains modest. A number of economists see the decline in the personal savings rate as a red flag as consumers borrow more to fuel spending. This will leave little margin for error in case of a downturn, especially for families who are living from paycheck to paycheck.
- A recent Report on the Economic Well-being of U.S. Households in 2017 illustrates this point. The report notes that relatively small, unexpected expenses, such as a car repair or replacing a broken appliance, can be a hardship for many families without savings. When faced with a hypothetical expense of only $400, 59 percent of adults in 2017 say they could easily cover it, using entirely cash, savings, or a credit card paid off at the next statement.

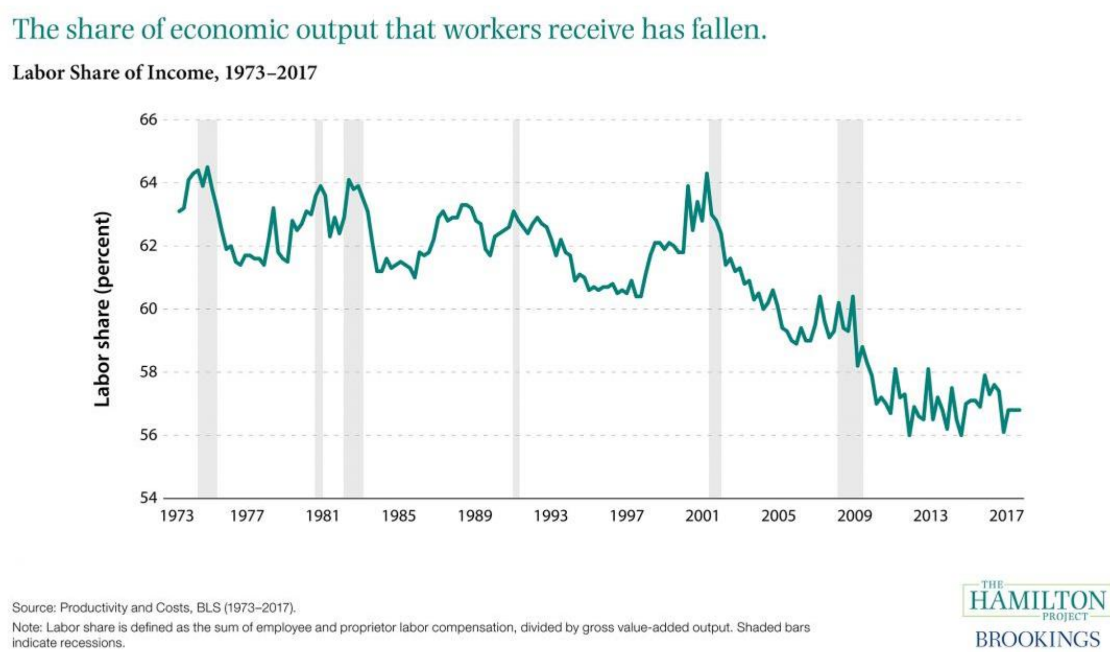
- However, the remaining 4 in 10 adults would have more difficulty covering such an unexpected expense. When surveyed, the most common approaches for this group included carrying a balance on credit cards and borrowing from friends or family.

**Workers' Declining Share of Economic Output**

A number of recent analyses by the New York Times and other sources have focused on the reasons that wage growth has lagged behind job growth. Some explanations include:

- Declining Levels of Unionization
- Retraints on Competition through Non-Compete Clauses
- A Lagging Minimum Wage which has not Sustained Purchasing Power
- The Impacts of Globalization and Automation on the Workforce
- Sluggish Productivity Levels
- Outsourcing of Jobs to Contractors

This trend is also reflected in the declining share of economic output workers receive compared to corporate profits. The following chart from the Brookings Institution's Hamilton Project shows the overall trend for wage earners.

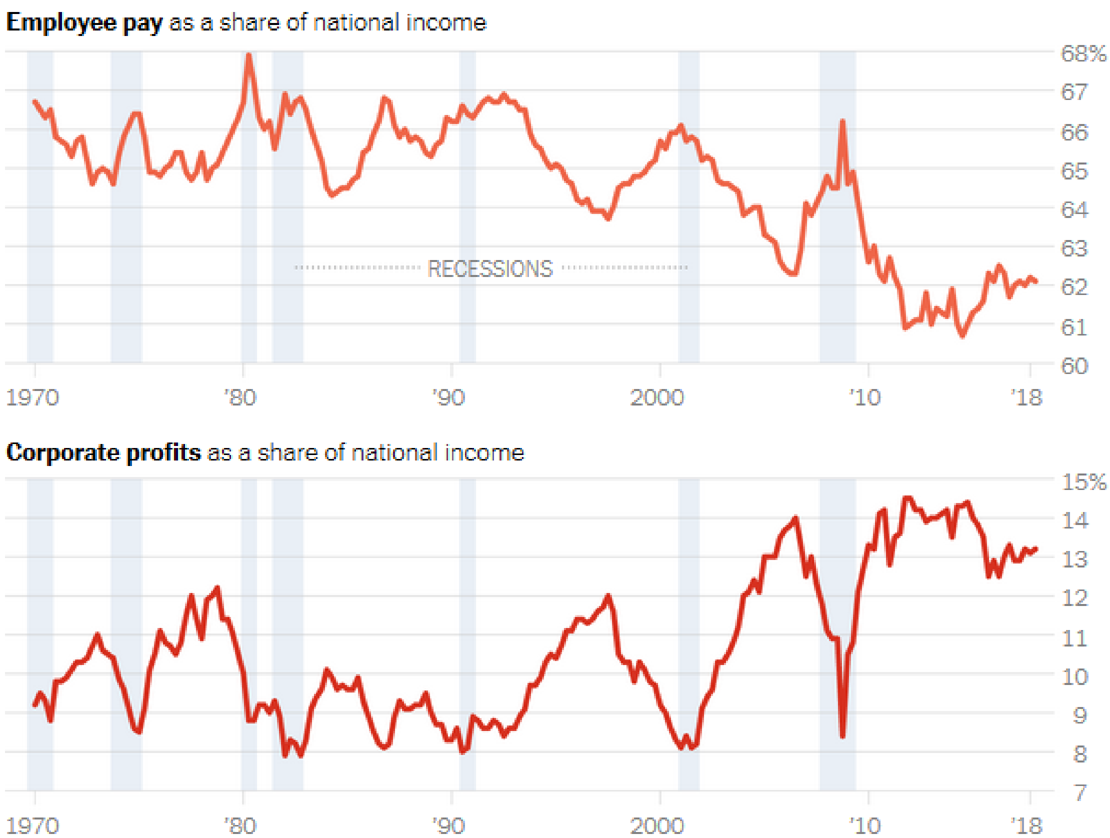



- A New York Times (NYT) analysis of data from the Bureau of Economic Analysis (BEA) indicates the pattern has worsened since the early 2000's and in the aftermath of the last recession.

- The NYT reports that in 2000, when the jobless rate last fell below 4 percent, corporations received 8.3 percent of the nation's total income in the form of profits. By comparison, wages and salaries across the entire work force accounted for roughly 66 percent of total income. Currently the nation's jobless rate is once again at or below below 4 percent. However, corporate profits now account for 13.2 percent of the nation's income while workers' compensation has fallen to 62 percent.

## Labor's Declining Share

Workers' paychecks account for much less of the nation's total income since the last recession, and the profits of businesses account for more.

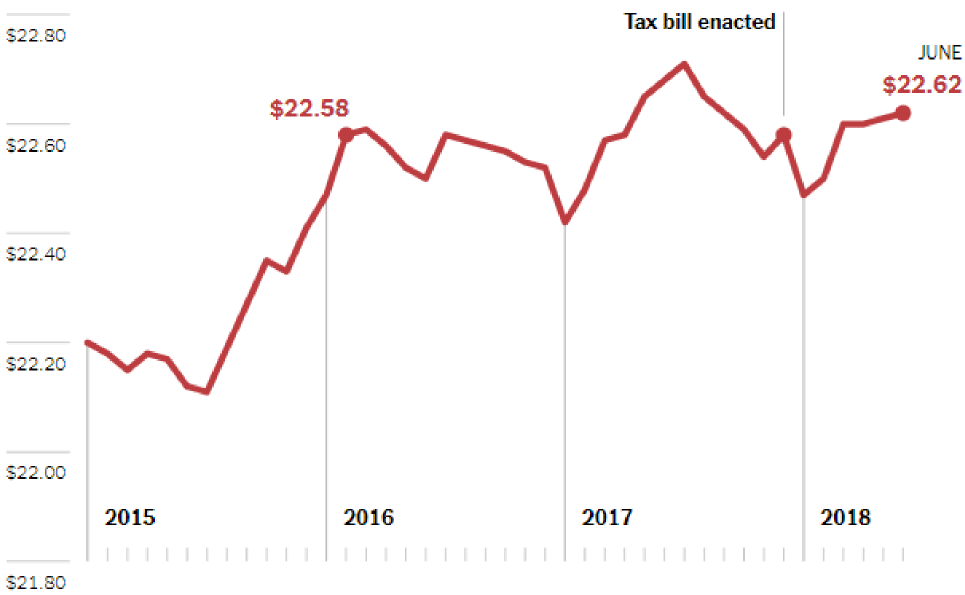



Source: Bureau of Economic Analysis | By The New York Times

- The structure of the recent federal tax cuts, especially reducing the corporate tax rate from 35 percent to 21 percent, will likely exacerbate this trend going forward.

## The Broken Promise of Wage Growth

Real wages have stagnated for more than two years.

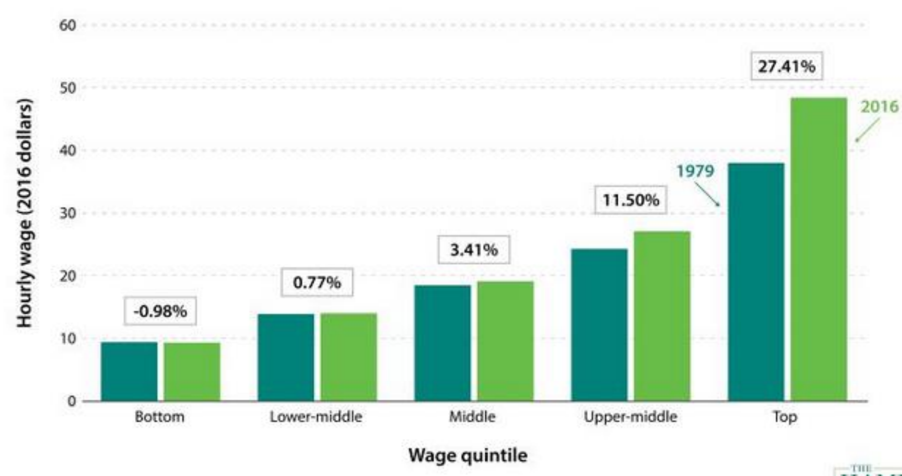



By The New York Times | Source: Jared Bernstein, Center on Budget and Policy Priorities; figures adjusted to June 2018 dollars.

- In addtion, the wage growth that has occurred over time has not been evenly distributed among income groups. In fact, wage growth has been concentrated at the top of the income scale. Those in lower and middle income groups have seen stagnant wages or very modest growth as demonstrated by the Hamilton Project researchers:

FIGURE 2.

Real Wages by Wage Quintile, 1979 and 2016




Source: Current Population Survey, BLS (1979–2016); authors' calculations.
Note: Wages are expressed in 2016 dollars, deflated using the CPI-U-RS. Sample restricted to workers ages 25–54. Growth rates are cumulative.

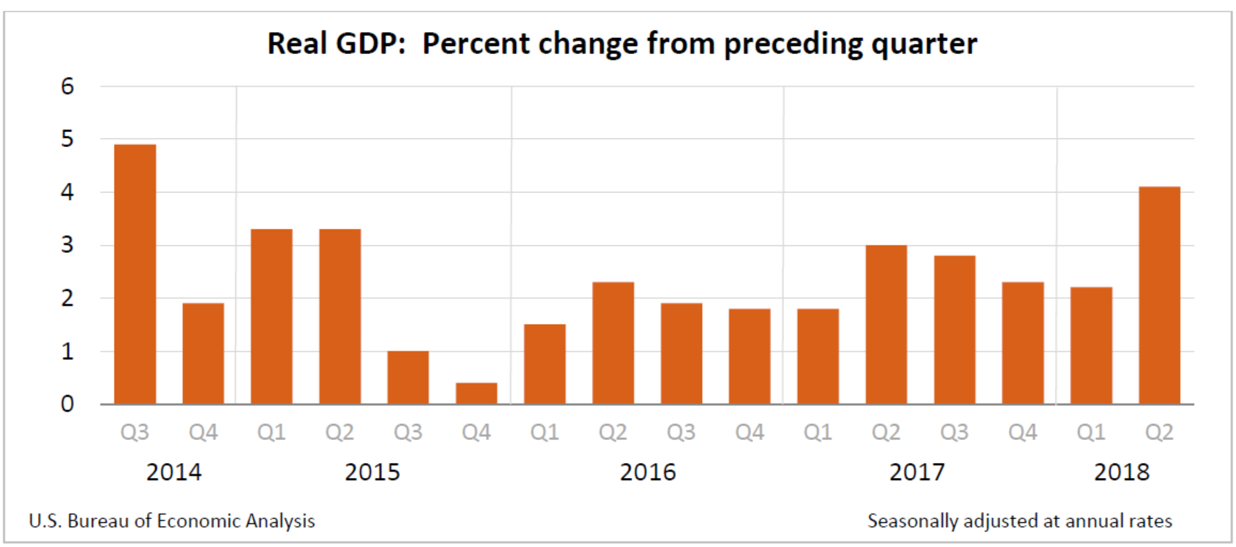
THE HAMILTON PROJECT
BROOKINGS

## Consumer Confidence

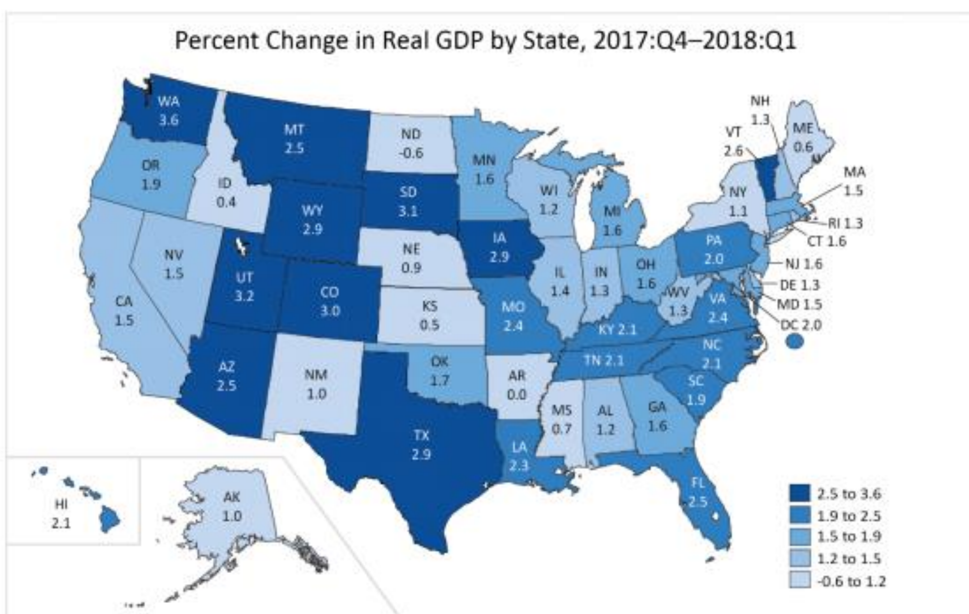
- The U.S. consumer confidence index (CCI) is published by the Conference Board. It is an indicator designed to measure consumer confidence, which is defined as the degree of optimism on the state of the economy that consumers are expressing through their activities of savings and spending.
- The Conference Board reported that the Consumer Confidence Index increased modestly in July, following a small decrease in June. The Index now stands at 127.4, up from 127.1 in June.
- The July 31 report noted that consumers' assessment of present-day conditions improved, signifying that economic growth is still strong. Expectations continue to reflect optimism in the short-term economic outlook. However, the survey indicated consumers do not foresee growth accelerating, suggesting some concerns about future growth prospects.

## Business and Economic Growth

- According to a much anticipated July 27 report from the Bureau of Economic Analysis, U.S. Real Gross Domestic Product grew at an annual rate of 4.1 percent in the second quarter of 2018, the strongest quarterly growth since 2014. This represented the advance estimate for the second quarter, which is subject to further revision. First-quarter growth was also revised to 2.2 percent, a slight increase from the previous estimate.



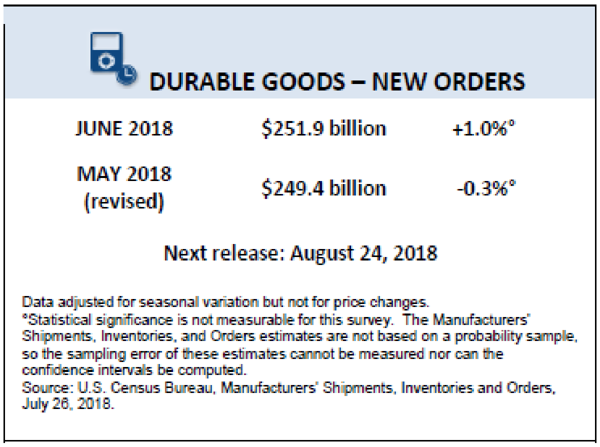
- BEA reported the increase in real GDP in the second quarter reflected positive contributions from personal consumption expenditures (PCE), exports, nonresidential fixed investment, federal government spending, and state and local government spending that were partly offset by negative contributions from private inventory investment and residential fixed investment. Imports, which are a subtraction in the calculation of GDP, increased.
- Economists noted that some of the GDP growth was due to one-time factors and would likely decelerate in the second half of the year. For example, exports surged in the second quarter in part due to mounting trade tensions as foreign buyers stocked up on American products like soybeans before tariffs were imposed. Consumer spending increased, partly aided by tax cuts, but could be hampered later by limited growth in wages. Government spending also helped drive the second quarter increase due to the budget deal that Congress passed earlier this year.
- In a July 24th report, the Bureau of Economic Analysis released Real Gross Domestic Product (GDP) results by state for the first quarter of 2018. Connecticut experienced a seasonally adjusted annual growth rate of 1.6 percent, which ranked 23rd in the nation overall. This growth rate was somewhat slower than the national average of 1.8 percent. However, Connecticut was second only to Vermont in growth among the New England states for the period. Among all states, Washington's GDP grew fastest at 3.6 percent for the quarter while North Dakota grew least at -0.6 percent

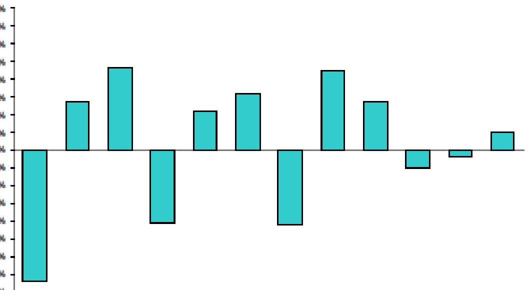


U.S. Bureau of Economic Analysis

- BEA data indicated the sectors that contributed most to Connecticut's growth in the first quarter of 2018 were real estate and rental & leasing (+0.43%), finance & insurance (+0.42%), and information (+0.27%).

- According to a July 26 report by the U.S. Department of Commerce, new orders for durable goods increased $2.5 billion in June or 1.0 percent to $251.9 billion. This increase followed monthly declines of 0.3 percent May and 1.0 percent in April.




| | Jul-17 | Aug-17 | Sep-17 | Oct-17 | Nov-17 | Dec-17 | Jan-18 | Feb-18 | Mar-18 | Apr-18 | May-18 | Jun-18 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| % Change | -7.4% | 2.7% | 4.7% | -4.1% | 2.2% | 3.2% | -4.2% | 4.5% | 2.7% | -1.0% | -0.3% | 1.0% |

Source: U.S. Census Bureau, Manufacturers' Shipments, Inventories, and Orders, July 26, 2018.

- Transportation equipment, also up following two consecutive monthly decreases, led the increase, growing $1.9 billion or 2.2 percent to $87.7 billion.
- The Commerce Department reported orders for non-defense capital goods excluding aircraft, a closely watched proxy for business spending plans, rose 0.6 percent last month. Data for May was revised higher to show these so-called "core capital goods" orders increasing 0.7 percent instead of the previously reported 0.3 percent gain.
- Business spending on equipment is being supported by the $1.5 trillion income tax cut package, which came into effect in January. However, a number of analysts warn that escalating tensions between the United States and its major trade partners, including China, Mexico, Canada and the European Union, could offset the fiscal stimulus, disrupt supply chains and undercut economic growth later in the year.

*****END*****