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COMPTROLLER LEMBO PROJECTS $63.3-MILLION DEFICIT FOR FISCAL YEAR 2020; SAYS BUDGET RESERVE DISCIPLINE NECESSARY AS EVER

Comptroller Kevin Lembo today, in his monthly updated financial and economic outlook, projected that the state is currently on track to end Fiscal Year 2020 with a $63.3-million budget deficit and urged continued adherence to the state's commitment to establish an adequate and fiscally responsible budget reserve fund.

In a letter to Gov. Ned Lamont, Lembo said his office's projection is slightly higher than the most recent projection by the state Office of Policy and Management (OPM) due largely to updated information about spending from the state's Adjudicated Claims Account. That account is used to pay claims against the state, including significant settlement payments related to SEBAC vs. Rowland (at least $138 million has been paid out for SEBAC v Rowland from 2016 through 2020 so far).

Lembo highlighted recent disruptions in the financial markets due to the Coronavirus, as well as record high household debt and historically low personal savings rates, noting that Connecticut needs to maintain its commitment to financial preparedness.

"Connecticut may not have control over these global and national threats, but it can responsibly prepare for them by ensuring an adequate budget reserve fund," Lembo said. "Connecticut did not come so far in three short years to reverse the clock on financial discipline.

"The benefits of keeping our promise to build the state's reserves is not just essential to protect against the next recession. The rating agencies are taking note – and even held

Connecticut up as a standout state where 'the effects of that increased focus (on the Budget Reserve Fund) are beginning to show' as we jumped from the bottom half of the list in 2017 to the top half of the list in 2019 as among states most prepared for a moderate or severe recession."

The statutory revenue volatility cap, which requires revenue above a certain threshold to be transferred to the Budget Reserve Fund (BRF) – often referred to as the "rainy day fund" – is $3.3 billion for estimated and final income tax payments and revenue from the pass-through entity tax for Fiscal Year 2020.

The update for the BRF outlook is:

- If current projections are realized, a $318.3-million volatility transfer would be made to the BRF at the close of the fiscal year;
- The balance of the BRF currently stands at $2.5 billion;
- Adding the estimated $318.3-million volatility transfer, less the projected FY 2020 deficit of $63.3 million, would bring the year-end BRF balance to approximately $2.76 billion;
- This balance, if achieved, would represent approximately 13.8 percent of net General Fund appropriations for FY 2021 (Lembo has long recommended the state maintain a Budget Reserve Fund at 15 percent).

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

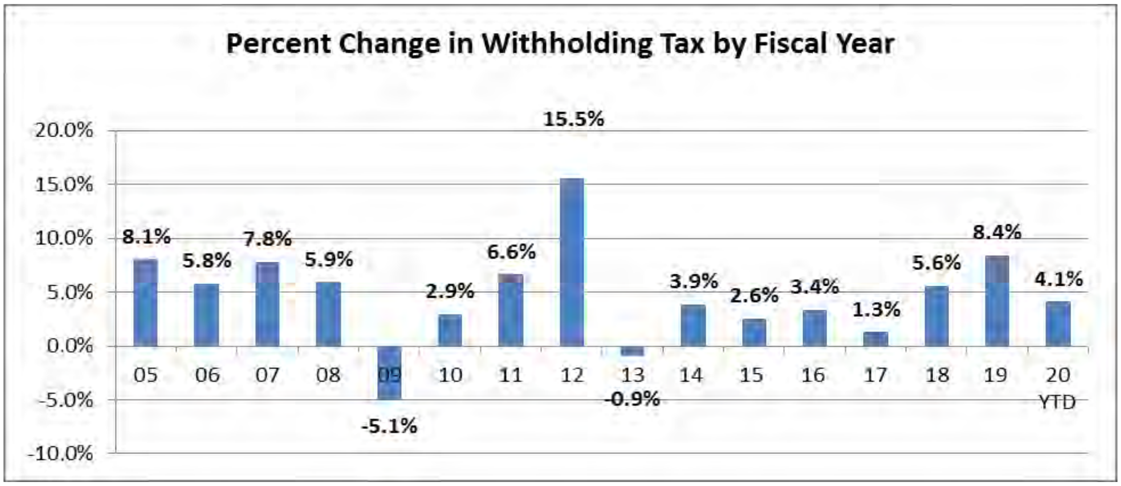
Lembo pointed to recent economic indicators and trends from national and state sources that show:

Employment

Final results for FY 2019 showed withholding receipts grew by a strong 8.4 percent compared with the prior fiscal year. This is especially significant because the withholding portion of the income tax is the largest single General Fund revenue source.

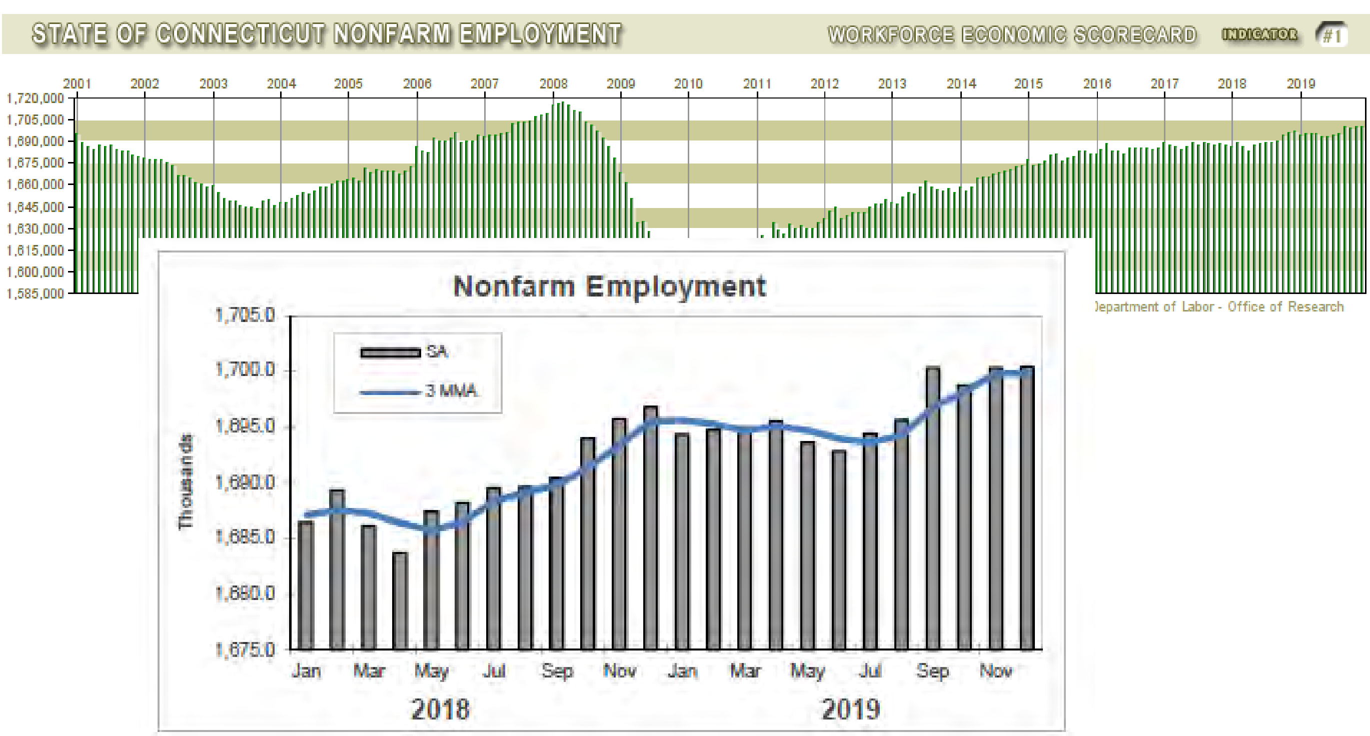
Through January 2020, withholding receipts are in generally line with the budget plan, which calls for growth of 4.1 percent over FY 2019 levels. This growth rate to date reflects the underlying trend for receipts (factoring out the year-end statutory revenue accruals). In the Jan. 15 consensus revenue forecast, the Office of Policy and Management (OPM) and the

Office of Fiscal Analysis (OFA) left the initial FY 2020 budget projection for withholding receipts unchanged at $6.91 billion.



On Jan. 23, Connecticut DOL (Department of Labor) reported the preliminary Connecticut nonfarm job estimates for December 2019 from the business payroll survey administered by the U.S. Bureau of Labor Statistics (BLS). DOL's Labor Situation report showed the state gained 100 net jobs in December, to a level of 1,700,400, seasonally adjusted. November's originally released job gain of 900 was revised upward by 700 to a gain of 1,600 jobs over the month.

Updated job data from the U.S. Bureau of Labor Statistics and the Connecticut DOL is scheduled to be issued on March 13. This upcoming release will include both results for January 2020 and new benchmarked job data for the 2019 calendar year.



Over the year, DOL reported that nonagricultural employment in the state grew by 3,600 jobs on a seasonally adjusted basis. Connecticut has now recovered 86.1 percent (103,600 payroll job additions) of the 120,300 seasonally adjusted jobs lost in the Great Recession (3/08-2/10). As of December, the job recovery was into its 118th month and the state needed an additional 16,700 new net jobs to reach an overall employment expansion.

Within the job recovery numbers, DOL points out a significant distinction. The private sector has recovered more than the total jobs lost in the recession (107.1 percent), which means the remaining employment losses are from the government sector. This sector includes all federal, state and local government employment, including public education, and Native American tribal government.

Connecticut's Recessionary Job Loss and Recovery March 2008 - December 2019

	March 2008	January 2010	December 2019	Jobs Lost	Recovered	
					Jobs	Percent
CT Nonfarm Employment	1,717.1	1,596.8	1,700.4	-120.3	103.6	86.1%
Total Private Sector	1,457.4	1,345.4	1,465.3	-112.0	119.9	107.1%

* March 2008 was employment peak. January 2010 was employment trough. Last Updated: January 23, 2020

Connecticut's unemployment rate stood at 3.7 percent in December, unchanged from the revised November figure and down one-tenth of a point from a year ago when it was 3.8 percent. Nationally, the unemployment rate was 3.5 percent in December 2019, unchanged from November and down four-tenths of a point from a year ago. The chart below shows a comparison of the Connecticut and U.S. unemployment rates since 2001.

Among the major job sectors listed below, five experienced gains and five had losses in December 2019 versus December 2018 levels. Education & health services, professional &

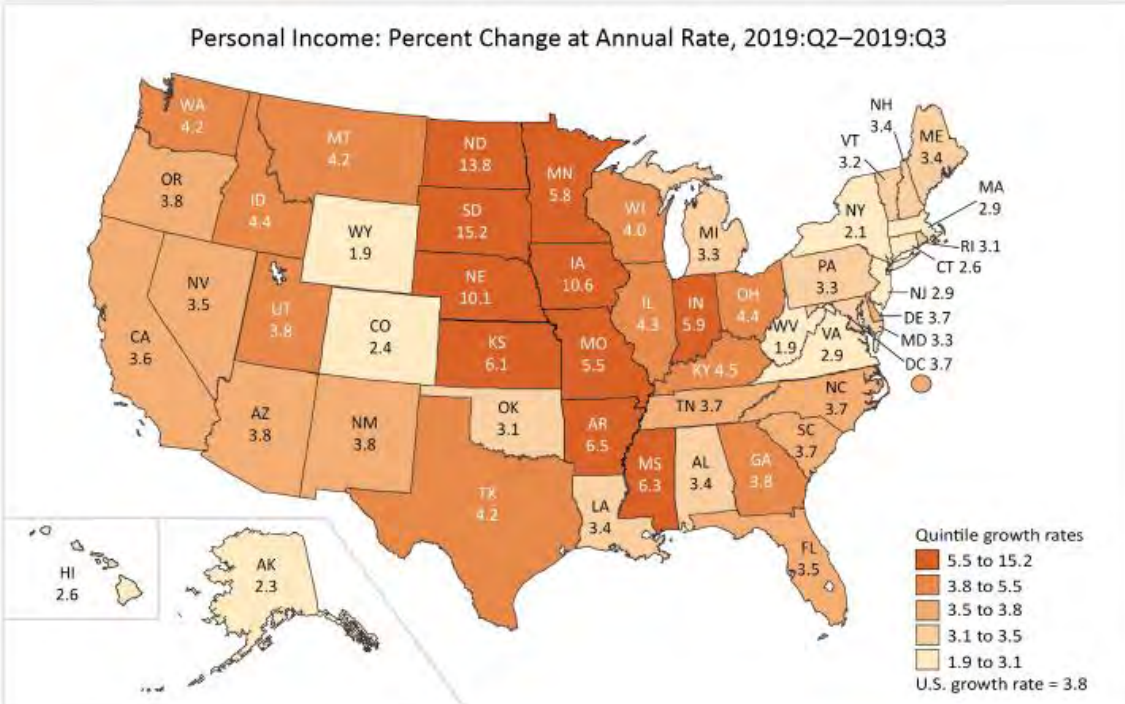
business services and information were the fastest growing sectors in the state's labor market on a percentage basis. The construction, trade, transportation & utilities and other services sectors experienced the largest job losses.

Payroll Employment Trend				
December 2019 Versus December 2018				
Sector	**Dec. 2019 (P)**	**Dec. 2018**	**Gain/Loss**	**% Change**
Construction and Mining	58,500	61,900	-3,400	-5.5%
Manufacturing	161,100	160,400	700	0.4%
Trade, Transportation & Utilities	291,600	296,100	-4,500	-1.5%
Information	33,000	32,700	300	0.9%
Financial Activities	127,600	127,000	600	0.5%
Professional & Business Services	222,800	219,500	3,300	1.5%
Education & Health Services	347,000	336,900	10,100	3.0%
Leisure & Hospitality	159,400	160,500	-1,100	-0.7%
Other Services	64,300	64,800	-500	-0.8%
Government	235,100	237,000	-1,900	-0.8%
Total Connecticut Non-Farm Employment	**1,700,400**	**1,696,800**	**3,600**	**0.2%**

Wage and $alary income

December 2019 average hourly earnings at $33.65, not seasonally adjusted, were up $0.17 or 0.5%, from the December 2018 estimate. Due to a fractional reduction in weekly hours, the resultant average private sector weekly pay amounted to $1,144.10, down $0.92 or -0.1 percent from a year ago. However, DOL warns that due to fluctuating sample responses, private sector earnings and hours estimates can be volatile from month-to-month.
The 12-month percent change in the Consumer Price Index for All Urban Consumers (CPI-U, U.S. City Average, not seasonally adjusted) in December was a modest 2.3%.

On Dec. 18, the Bureau of Economic Analysis reported that Connecticut's personal income grew by a 2.6 percent annual rate between the second and third quarters of 2019. Based on this result, Connecticut ranked 44th in the nation for third quarter income growth. This growth rate was below the national average of 3.8 percent and the New England region's average growth rate of 2.9 percent. The percent change in personal income across all states ranged from 15.2 percent in South Dakota to 1.9 percent in West Virginia and Wyoming. Fourth quarter and preliminary full year 2019 personal income data by state will be released on March 24.



The U.S. Private Sector Job Quality Index

Despite low unemployment and sustained job creation, the U.S. has continued to experience sluggish hourly wage growth in the aftermath of the Great Recession. Traditional employment data, while useful, is not revealing the full story. To get a better sense of the reasons behind this trend, a cooperative venture among several organizations developed a new index that measures the quality of jobs available in the United States.

The JQI focuses on Production and Non-supervisory (P&NS) jobs, which make up 82.3 percent of all U.S. private sector jobs. Jobs are classified as High Wage/High Hour Jobs (high quality) or Low Wage/Low Hour Jobs (low quality) compared with the weekly wage mean.

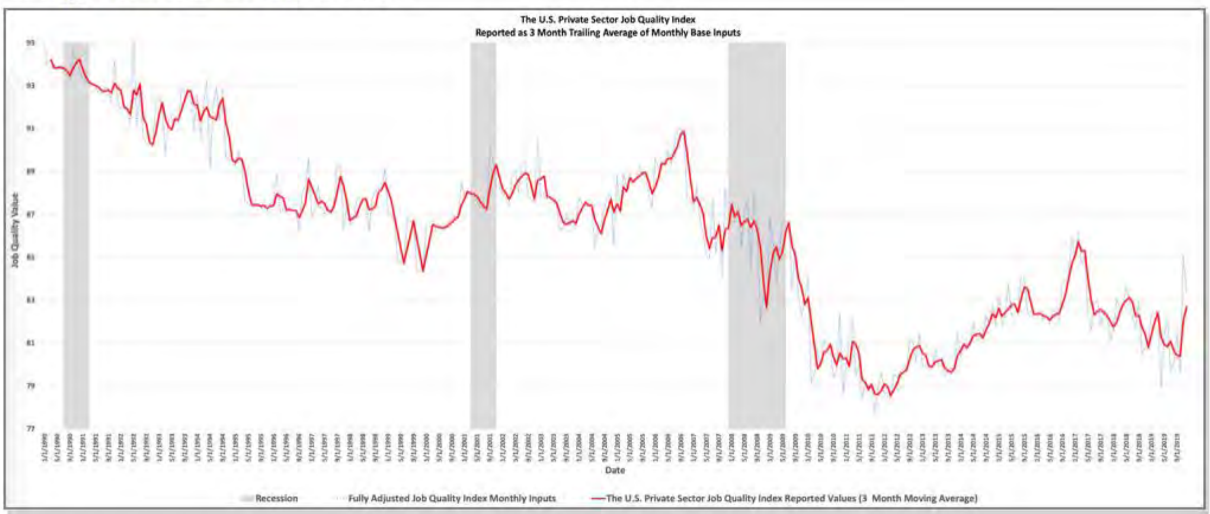
The initial white paper found the JQI has declined significantly in the period from 1990 through the Great Recession and has largely plateaued since then. This is partially, though not entirely, due to a persistent increase in service jobs compared with goods-producing jobs. In the 1960's service sector employment represented about 58 percent of private sector employment compared with about 83 percent in the period during and after the Great Recession. The decline in the goods producing side of the economy has forced an abundance of workers into the services sectors, which has resulted in the loss of pricing power among this labor group.

On a month-to-month basis the JQI uses U.S. Bureau of Labor Statistics (BLS) data to chart rises and falls in the quality of private sector jobs – again in terms of mean weekly income.

The total number of high-quality jobs is divided by the total number of low-quality jobs for that given month. This ratio represents the preliminary JQI value. A JQI reading of 100 would indicate an even distribution between higher quality and lower quality jobs. For January 2020, the JQI rose by 0.76 percent to a revised level of 82.68. However, this still indicates a greater concentration of lower quality positions.

The JQI Curve

Current Level is **82.68**
Change From Last Month is **0.76**%



Data As of January 1, 2020

Housing

Berkshire Hathaway HomeServices reported results for the Connecticut housing market for January 2020 compared with January 2019. Sales of single-family homes grew by 5.03 percent, with the median sale price increasing by 12.77 percent. New listings were down 2.88 percent in Connecticut, while the median list price rose 12.51 percent to $269,900. Average days on the market were up 4.71 percent in January 2020 compared to the same month in the previous year (89 days on average compared with 85 days).

The table below contains more detailed data for the Connecticut housing market.

MARKET SUMMARY

JANUARY 2020 | SINGLE FAMILY HOMES

Market	Month to Date			Year to Date		
Summary	January 2020	January 2019	Percent Change	Year-To-Date 2020	Year-To-Date 2019	Percent Change
New Listings	3501	3605	-2.88% ▼	3501	3605	-2.88% ▼
Sold Listings	2129	2027	5.03% ▲	2129	2027	5.03% ▲
Median Listing Price	$269,900	$239,900	12.51% ▲	$269,900	$239,900	12.51% ▲
Median Selling Price	$265,000	$235,000	12.77% ▲	$265,000	$235,000	12.77% ▲
Median Days on Market	70	65	7.69% ▲	70	65	7.69% ▲
Average Listing Price	$411,802	$354,221	16.26% ▲	$411,802	$354,221	16.26% ▲
Average Selling Price	$392,355	$339,922	15.43% ▲	$392,355	$339,922	15.43% ▲
Average Days on Market	89	85	4.71% ▲	89	85	4.71% ▲
List/Sell Price Ratio	96.9%	97%	-0.02% ▼	96.9%	97%	-0.02% ▼

For the U.S. housing market, the National Association of Realtors (NAR) reported existing-home sales declined in January, continuing a fluctuating pattern of monthly increases and decreases. January sales declined 1.3 percent from December to a seasonally adjusted annual rate of 5.46 million. On the regional level, significant declines in the West region dragged down nationwide numbers. The other three major U.S. regions reported either marginal or no changes from the previous month.

However, for the second straight month, overall sales increased significantly on a year-over-year basis, up 9.6 percent from a year ago (4.98 million in January 2019).

According to NAR, the median existing-home price for all housing types in January was $266,300, up 6.8 percent from January 2019 ($249,400), as prices increased in every region. January's price increase marks 95 straight months of year-over-year gains. NAR reports that low mortgage rates are helping with affordability, but limits in supply are driving price growth nationwide.

Total housing inventory at the end of January totaled 1.42 million units, up 2.2% from December, but down 10.7% from one year ago (1.59 million). NAR reports that the housing inventory level for January is the lowest level since 1999. Unsold inventory sits at a 3.1-month supply at the current sales pace, up from the 3.0-month figure recorded in December and down from the 3.8-month figure recorded in January 2019.

Population

According the U.S. Census Bureau, Connecticut's population declined by 6,623 between 2018 and 2019 and now stands at 3,565,287. This represents a small decrease of 0.17% compared with the prior year's estimate.

Over the longer term, Connecticut's population is smaller than it was nine years ago. While the decline is relatively small (8,860), Connecticut is one of only four states to lose population since 2010, along with Illinois, Vermont and West Virginia. As shown on the chart below, the components of the change followed a similar pattern in the long and the short-term: A higher number of births than deaths and gains from international migration into Connecticut helping to offset larger domestic migration out to other states.

Components of Connecticut Population Change

July 1, 2018 to July 1, 2019			Vital Events		Net Migration		
	Total Population Change	Natural Increase	Births	Deaths	Total	International	Domestic
Connecticut	-6,233	3,418	34,567	31,149	-9,736	12,323	-22,059
April 1, 2010 to July 1, 2019			Vital Events		Net Migration		
	Total Population Change	Natural Increase	Births	Deaths	Total	International	Domestic
Connecticut	-8,860	54,839	333,491	278,652	-63,899	136,392	-200,291

Source: U.S. Census Bureau

Connecticut's demographic trends can have an impact on the state's economy. As the baby boom generation continues to retire and leave the workforce, both economic demand and output could be further reduced. In short, Connecticut's lack of population growth remains a constraint to the State's potential for economic expansion.

Stock Market – Correction Territory in Last Week of February:

At the close of 2019, stocks were near historic highs. All-three indices were up over 20 percent for the year, with the NASDAQ up over 30 percent. For the first three weeks of January, stocks continued a generally upward trend. However, in the last week of the month, markets became more volatile and gave back gains due to concerns about the spread of coronavirus and possible disruptions to international commerce.

A similar pattern repeated itself in February. Stocks generally recovered losses and stabilized during the first three weeks of the month. However, there are growing concerns about the coronavirus as it has spread outside of China. The outbreak is placing strains on global supply chains, which caused a sharp selloff in stocks during the last week of February. Some factories in China are closed due to quarantine, while ships are sitting in ports unable to deliver their goods and companies that sell their products inside China are issuing profit warnings.

As of this writing all three stock indices have entered correction territory, having fallen 10 percent from their recent highs. During the last week of February, news outlets reported the stock market were having one of the worst weeks since the 2008 financial crisis.

One-year changes for the three major stock indices follow.

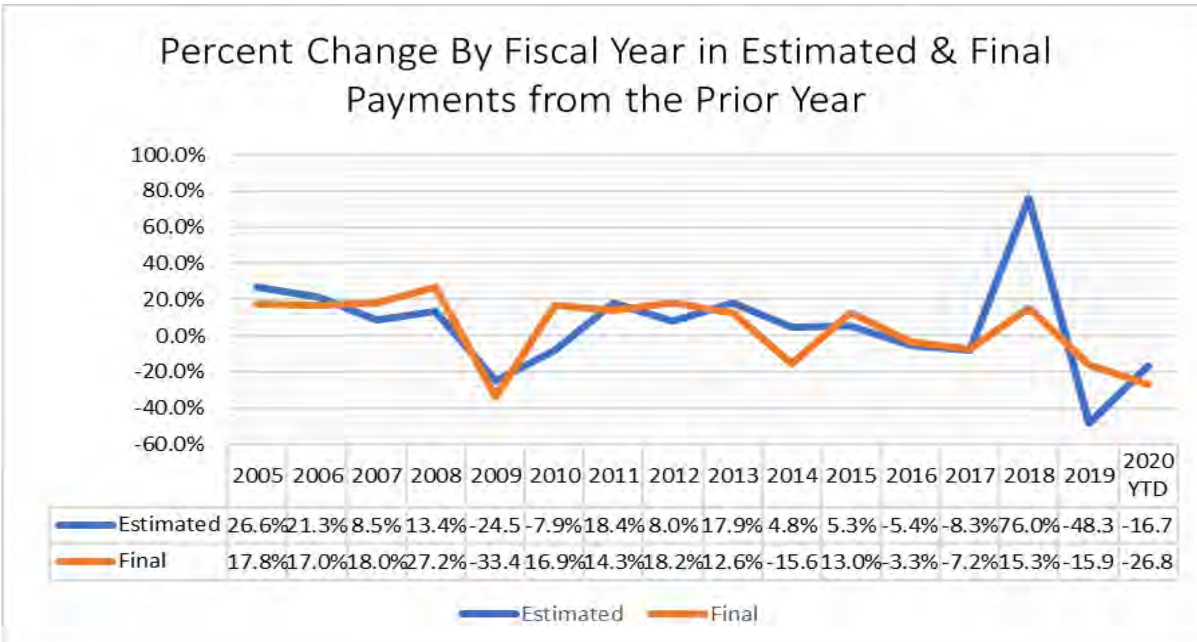
DOW

NASDAQ

S&P 500 INDEX

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 percent of total state income tax receipts, but can be an extremely volatile revenue source.

Final FY 2019 results showed combined collections of estimated and final payments totaled $2.974 billion, slightly better than anticipated by the budget plan. However, due to the extraordinary one-time results achieved in FY 2018, final and estimated payments came in 35.6 percent lower than the same period a year earlier.



	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020 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%	76.0%	-48.3	-16.7
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%	15.3%	-15.9	-26.8

Year-to-date through January 2020, estimated and final payments are down a combined 18.7 percent compared with the same period a year ago. However, some collections from this category are now flowing though the new Pass-Through Entity (PET) tax on partnerships and S Corporations. In fact, in the January 15th consensus revenue forecast, OPM and OFA reduced estimated and final income tax payments by $300 million but raised PET taxes by a corresponding $300 million to reflect this trend.

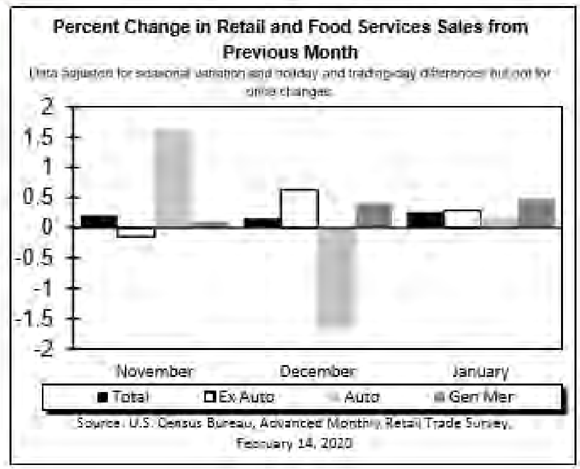
Consumer Spending

Consumer spending is the main engine of the U.S. economy, accounting for more than two-thirds of total economic output.

The Commerce Department reported that U.S. advance retail sales grew modestly in January 2020, increasing 0.3 percent. This result was in line with economists' projections. Data for December was revised down to show retail sales gaining 0.2 percent instead of climbing 0.3% as previously reported.

Automobile sales rebounded in January, growing 0.2 percent after a steep decline in December. Receipts at building material & garden supply retailers grew 2.1 percent, most likely due to mild weather. Sales at restaurants and bars increased 1.2 percent in January.

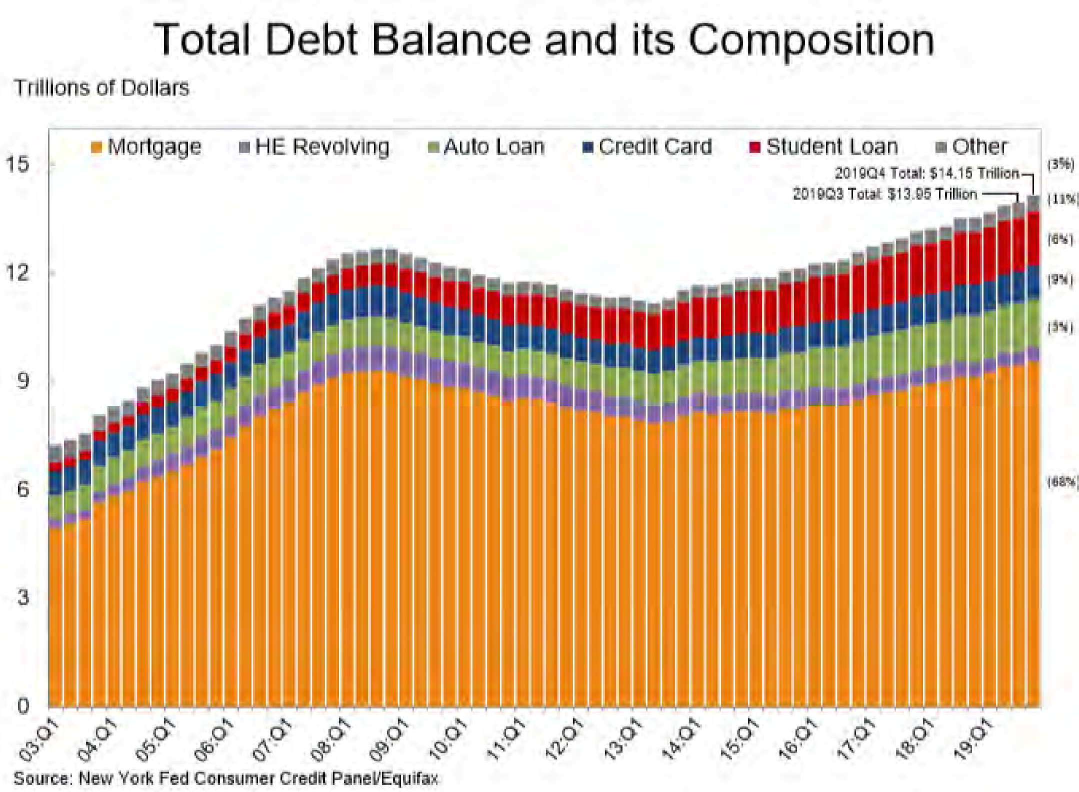
Clothing stores saw a significant drop in sales in January, declining 3.1 percent, which CNBC reported was the most since 2009. Sales at non-store (online) retailers grew by a modest 0.3 percent. Gas station receipts decreased 0.5 percent, likely due to lower gas prices and sales at electronics and appliance also declined 0.5 percent.



So called "core retail sales" were essentially unchanged in January after growing only a revised 0.2 percent in December. This category excludes automobiles, gasoline, building materials and food services and corresponds most closely with the consumer spending component of gross domestic product.

<u>Consumer Debt and Savings Rates</u>

According to the Federal Reserve Bank of New York, aggregate household debt balances rose to another new peak in the fourth quarter of 2019. Household debt has now grown

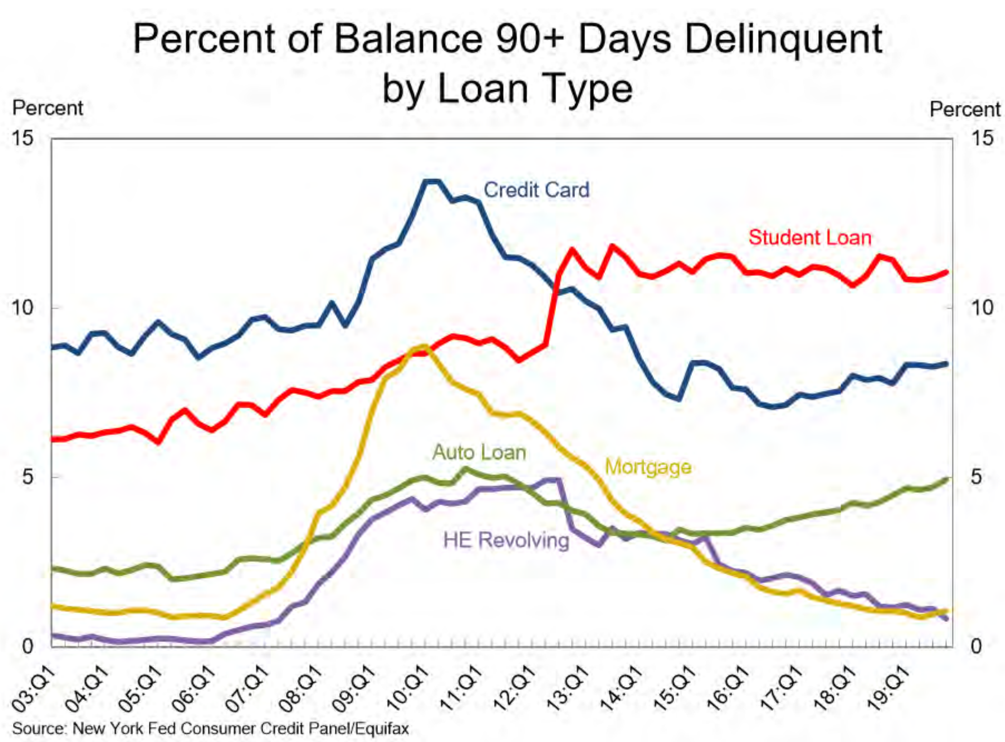


steadily for 5+ years (22 consecutive quarters). As of December 31, 2019, overall debt – including mortgages, auto loans, student loans and credit card debt – hit a record of $14.15 trillion. This represented an increase of $193 billion (1.4%) from the third quarter of 2019. In addition, overall household debt is now 26.8% above the post-financial-crisis trough (low point) reached during the second quarter of 2013.

The report titled "Quarterly Report on Household Debt and Credit" noted mortgage balances – the largest component of household debt – stood at $9.56 trillion during the fourth quarter, a $120 billion increase from the third quarter of 2019. At $1.51 trillion, student loans were the second largest category of household debt. Student loan balances increased by $10 billion in the fourth quarter of 2019. Balances on home equity lines of credit (HELOC), continuing their downward trend since 2009, declined by $6 billion to $390 billion. Auto loans grew by $16 billion in the fourth quarter to $1.33 trillion in total. Credit card balances increased by $46 billion to $927 billion, which represented growth of 5.2 percent between the third and fourth quarters, the largest increase on a percentage basis.

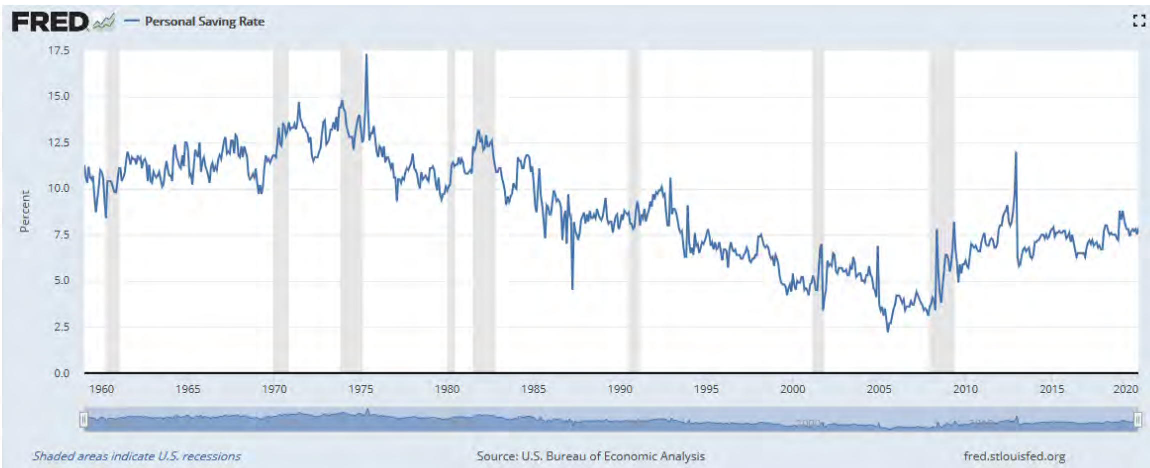
The Federal Reserve reported aggregate delinquency rates were mostly unchanged in the fourth quarter of 2019. As of December 31, 4.7 percent of outstanding debt was in some stage of delinquency, a 0.1 percentage point decrease from the third quarter due to a decrease in the 30 to 59 days late category. Of the $669 billion of debt that is delinquent, $444 billion is seriously delinquent (at least 90 days late or "severely derogatory", which includes some debts that have been removed from lenders books but upon which they continue to attempt collection).

The following chart shows percent of loan balances that are 90 or more days delinquent by type of loan.



Personal Savings Rate

In its Feb. 28 release, the Bureau of Economic Analysis (BEA) reported the personal-saving rate was 7.9 percent in January, an improvement from December's revised rate of 7.5 percent. The personal savings rate is defined as personal saving as a percentage of disposable personal income.



Personal income grew $116.5 billion (0.6 percent) in January while consumer spending only increased 0.2 percent. BEA reported the increase in personal income primarily reflected increases in employee compensation and social security benefit payments (related to annual cost of living adjustments).

The personal savings rate remains low by historical standards. A number of economists see the general decline in the personal savings rate as a red flag as consumers borrow more to fuel spending. In recent years, wage gains have been concentrated on the upper end of the income scale. This will leave little margin for error in case of a downturn, especially for families who are living from paycheck to paycheck.

Consumer Confidence

The U.S. consumer confidence index (CCI) is published by the Conference Board. The CCI looks at U.S. consumer's views of current economic conditions and their expectations for the next six months. The index is closely watched by economists because consumer spending accounts nearly 70 percent of U.S. economic activity.

The Conference Board reported that the Consumer Confidence Index improved slightly in February, following an increase in January. The Index now stands at 130.7, up from a revised 130.4 in January. February's growth in consumer confidence was attributed to positive short-term expectations combined with a strong labor market. (The cutoff date for the survey results was Feb. 13.)

The Atlantic – The Great Affordability Crisis Breaking America

The Feb. 7 edition of The Atlantic, staff writer Annie Lowry looked beyond the headline economic numbers to highlight the struggles of working-class American families despite a decade of economic growth after the Great Recession.

In the decade of the 2010's, the headline economic numbers looked very strong: unemployment declined substantially, the economy expanded, and wages rose – mostly for higher-income earners, but modestly for lower-income workers later in the decade. Recently, Americans' confidence in the economy hit its highest point since 2000. Why then do so many families feel left behind?

Ms. Lowry calls the problem the "Great Affordability Crisis" and focuses on cost of living issues facing American families and explores reasons why so many are classified as financially fragile despite the country's great wealth.

For many Americans, the spiraling cost of living has become a central facet of their economic lives. The article highlights four areas:

- ***Housing prices***, which represent the most acute part of the crisis for many families and turned many into renters.
- ***Health care costs***, with rising premiums, deductibles, and out of pocket costs consuming a growing share of family budgets, adding to their debt burden and consigning many to bankruptcy.
- ***Higher education costs and rising student loan debt***, which is now a bigger burden on households than car loans or credit card debt.
- ***Child-care costs***, which can range from $15,000 to $26,000 a year, are unaffordable for many families who need to work.

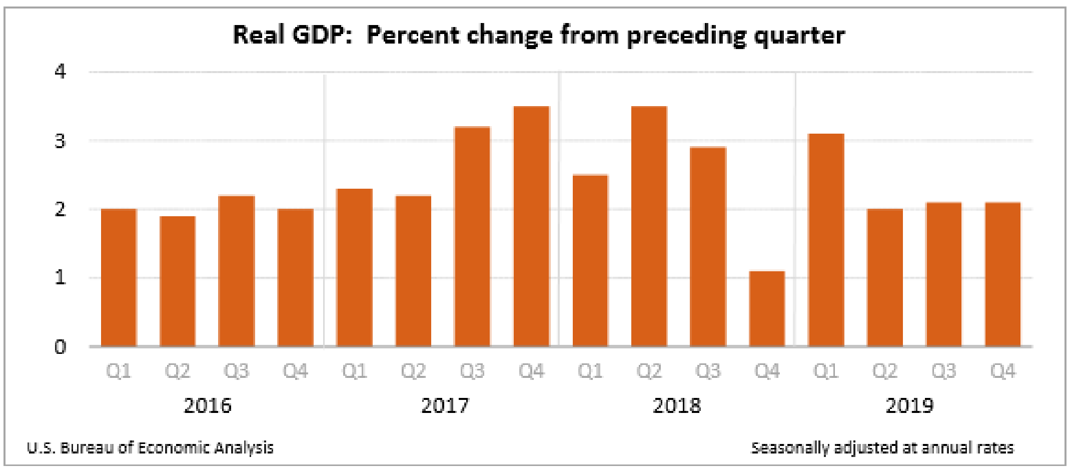
Ms. Lowry notes the affordability crisis hides in plain sight, obvious to families, but masked by headline economic numbers. In the end, all these costs add up and subtract from the wellbeing of American families. The full article can be found here:

https://www.theatlantic.com/ideas/archive/2020/02/great-affordability-crisis-breaking-america/606046/

Business and Economic Growth

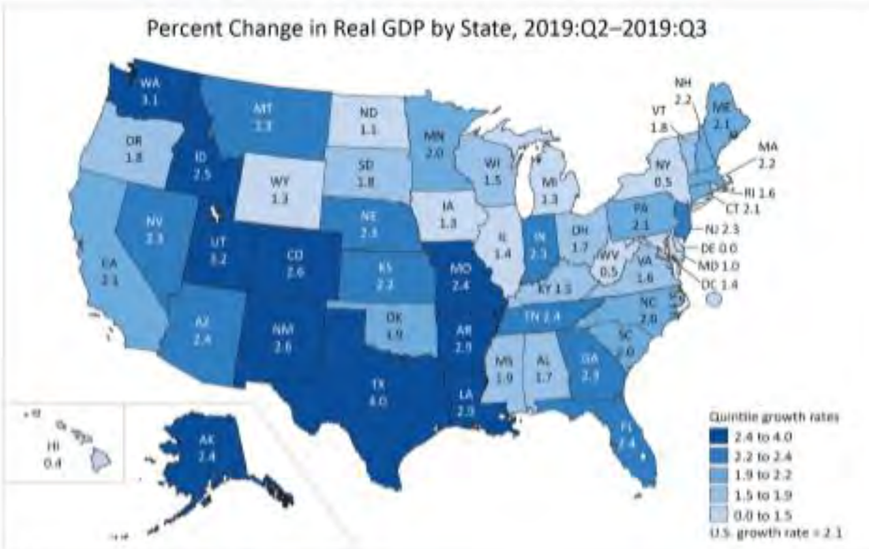
According to a Feb. 27 report from the Bureau of Economic Analysis (BEA), U.S. Real Gross Domestic Product grew at an annual rate of 2.1 percent in the fourth quarter of 2019, based on BEA's second estimate. In the third quarter, real GDP also increased 2.1 percent.

Fourth quarter GDP growth was largely the result of spending by consumers as well as by federal, state and local government. Residential fixed investment (i.e., spending on private residential structures and equipment) also made a positive contribution. On the downside, business investment in plant and equipment declined in the fourth quarter as ongoing trade disputes continued to dampen growth despite the recent first-phase trade agreement with China. Imports, which are a subtraction in the calculation of GDP, decreased.



For the full year, U.S. GDP increased by 2.3 percent in 2019, the slowest growth in three years. In 2017, for example, the U.S. economy grew 2.4 percent, followed by a 2.9 percent increase in 2018. The deceleration in GDP growth in 2019 was due to slowdowns in business investment (non-residential fixed investment) and consumer spending. This was partly offset by accelerations in both state, local and federal government spending. In addition, imports increased less in 2019 compared with 2018.

In a Jan. 10 report, the Bureau of Economic Analysis (BEA) released Real Gross Domestic Product (GDP) results by state for the third quarter of 2019. Connecticut experienced a seasonally adjusted annual growth rate of 2.1 percent, which ranked 25th in the nation overall. This growth rate was equal to both the national average and the New England regional average. The percent change in real GDP in the third quarter ranged from 4.0 percent in Texas to 0.0 percent in Delaware. Fourth quarter and full 2019 results for the year will be released on April 7, 2020.



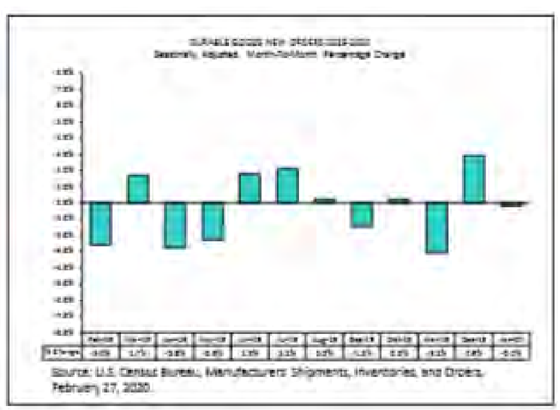
U.S. Bureau of Economic Analysis

Connecticut's performance in the third quarter was a vast improvement over the second quarter, where Connecticut's GDP grew at an annual growth rate of 1.0 percent, which ranked 47th in the nation overall.

The sectors that contributed most to Connecticut's GDP growth in the third quarter of 2019 were nondurable goods manufacturing (0.71%), retail trade (0.39%), professional, scientific & technical services (+0.37%), and information (+0.36%). The sectors that contracted the most included finance and insurance (-0.55%), utilities (-0.24%) and construction (-0.15%).

<u>Durable Goods</u>

According to a Feb. 27 report by the U.S. Department of Commerce, new orders of manufactured durable goods declined by $0.4 billion in January, down 0.2 percent to $246.2 billion. This decrease, the second in three months, comes after a 2.9 percent increase in December. Transportation equipment drove January's decrease, dropping $1.8 billion or 2.2 percent to $82.0 billion, as demand for cars, auto parts and military aircraft declined. New orders for transportation equipment have now been down four of the last five months.



The more positive news for January is that new orders of so called "core capital goods" increased by 1.1 percent, the largest gain in a year. Core capital goods include non-defense capital goods excluding aircraft and the measure is widely viewed as a proxy for business investment.

Analysts noted that recent signs of stabilization in business investment are likely to be tempered by the coronavirus and its disruptive impact on supply chains.

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