News from:
COMPTROLLER KEVIN LEMBO

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COMPTROLLER LEMBO PROJECTS $244.6-MILLION DEFICIT

Comptroller Kevin Lembo announced today that the state is on track to end Fiscal Year 2018 with a $244.6-million deficit as a deficit mitigation plan proposed by the governor awaits action by the state legislature.

In a letter to Gov. Dannel P. Malloy, Lembo said that his office is projecting a slightly higher deficit than the most recent projection last month by the state Office of Policy and Management (OPM). Lembo's projection is larger due to an anticipated $26.4-million deficiency in the state's adjudicated claims account, which is responsible for paying SEBAC v. Rowland settlement claims and related attorney's fees, as well as other negotiated and often unpredictable settlements.

Lembo said the General Fund deficit projection has grown over last month, in large part, due to reduced revenue available in the General Fund. The state experienced a recent surge in estimated income tax revenue due to early payments related to federal tax law changes and a one-time repatriation of hedge fund profits at the end of 2017. These windfall amounts will largely be transferred to the state's Budget Reserve Fund based on a new revenue volatility provision. After accounting for that, overall General Fund revenue is down by approximately $16 million – and savings targets on the spending side may be challenging.

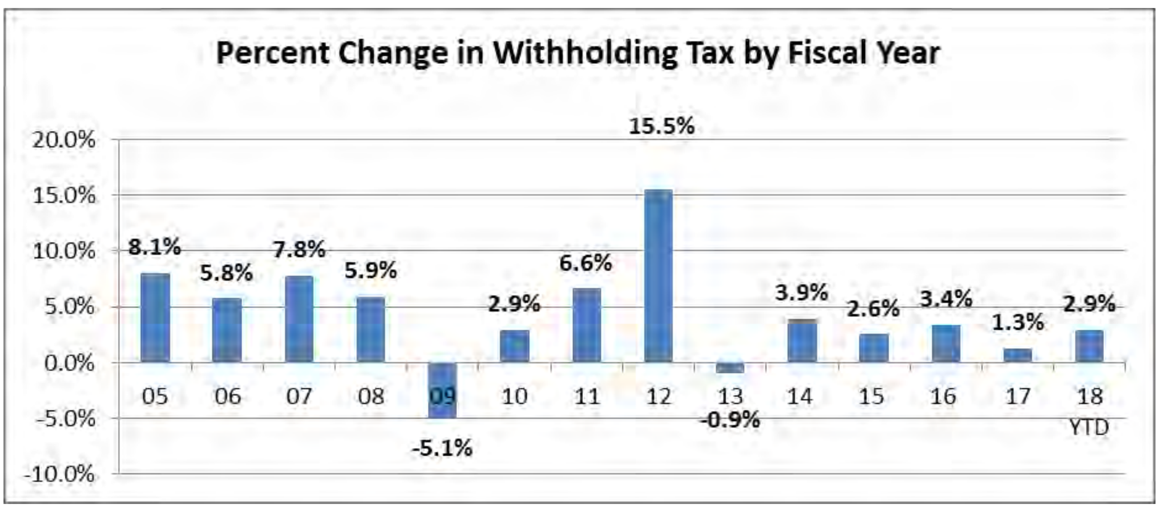
Looking ahead, Lembo said there are some positive economic developments worth watching.

"Connecticut's economic recovery continues to lag the nation's recovery – however, there are some positive economic indicators, including stock market performance, as well as state GDP growth and job growth related to manufacturing and finance," Lembo said. "These are promising signs – but should be taken with cautious optimism as one month does not make a trend. It's also important to recognize that, while a strong stock market is important, nearly half of Americans do not participate in the stock market – and economic research indicates that nearly half of U.S. households report being unprepared for an emergency expense and nearly a quarter of adults report being unable to pay current monthly bills."

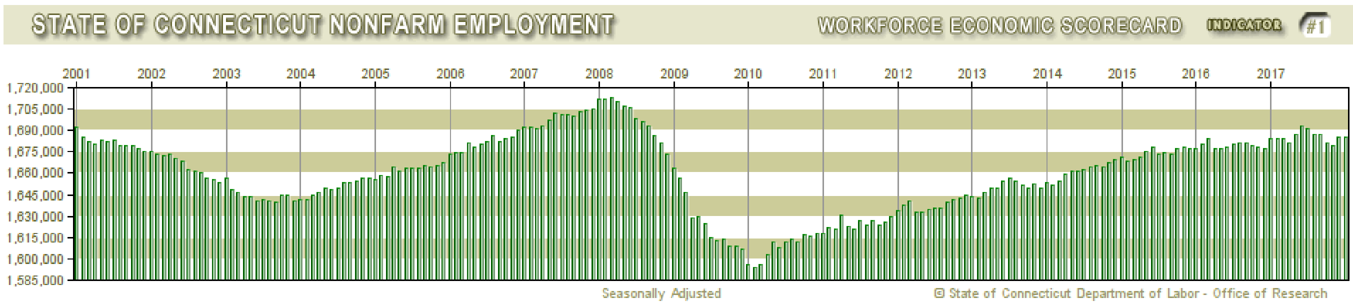
The latest economic indicators from federal and state Departments of Labor and other sources that show:

Employment

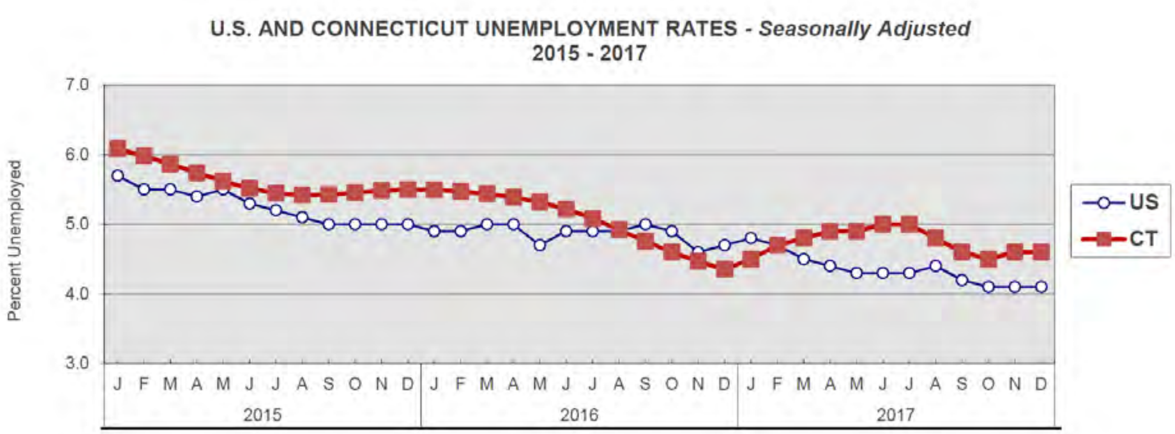
- Through the first six months of FY 2018, withholding receipts were nominally up 4.8% from last fiscal year. However, this growth is somewhat overstated due to revenue accruals related to FY 2017 year-end adjustments. Accounting for this activity, the FY 2018 year-to-date growth in withholding collections is closer to 2.9%. This more modest growth rate is more consistent with the job data that follows.



- Several months of bad news on the job front was reversed as calendar 2017 came to a close. The Connecticut Department of Labor (DOL) reported the preliminary Connecticut nonfarm job estimates for December from the business payroll survey administered by the US Bureau of Labor Statistics (BLS). DOL's Labor Situation report showed the state gained 6,000 net jobs (0.4%) in December 2017, to a level of 1,685,200, seasonally adjusted. In addition, November's originally-released job loss of 3,500 was revised down by the BLS to a loss of 1,800 for the month.



- For the year, DOL reported preliminary data show that Connecticut gained 7,700 jobs on a seasonally-adjusted basis and 6,200 jobs on an annual average basis. This compared favorably with 2016, which saw annual average growth of 5,000 jobs. However, this level of increase is still lower than the last period of economic recovery where employment growth averaged over 16,000 annually. DOL cautioned that the 2017 data is subject to revision by BLS as the result of the annual benchmark process that will be released in March 2018.
- Connecticut has now recovered 76.4% (91,000 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 94th month and the state needs an additional 28,100 jobs to reach an overall employment expansion.
- Connecticut's unemployment rate remained at 4.6 percent in December, unchanged from November 2017 and two-tenths of percentage point higher than from a year ago when it was 4.4 percent. Nationally, the unemployment rate was 4.1% in December 2017. The chart below shows a comparison of the Connecticut and U.S. unemployment rates for the past three calendar years.



- DOL reports that December 2017 seasonally adjusted average weekly initial unemployment claims for first-time filers in Connecticut fell by 652 claimants (-16.6%) to 3,279 from November 2017, and were lower by 533 claims (14.0%) from the December 2016 level of 3,812.
- Among the major job sectors listed below, six experienced gains and four experienced losses in December 2017 versus December 2016 levels. Manufacturing was the bright spot, adding 4,100 jobs year-over-year. DOL noted that the strategic manufacturing sector has not seen an employment increase since 2010 and before that in 1997. Sectors with the largest job losses included Government, Leisure & Hospitality and Construction.

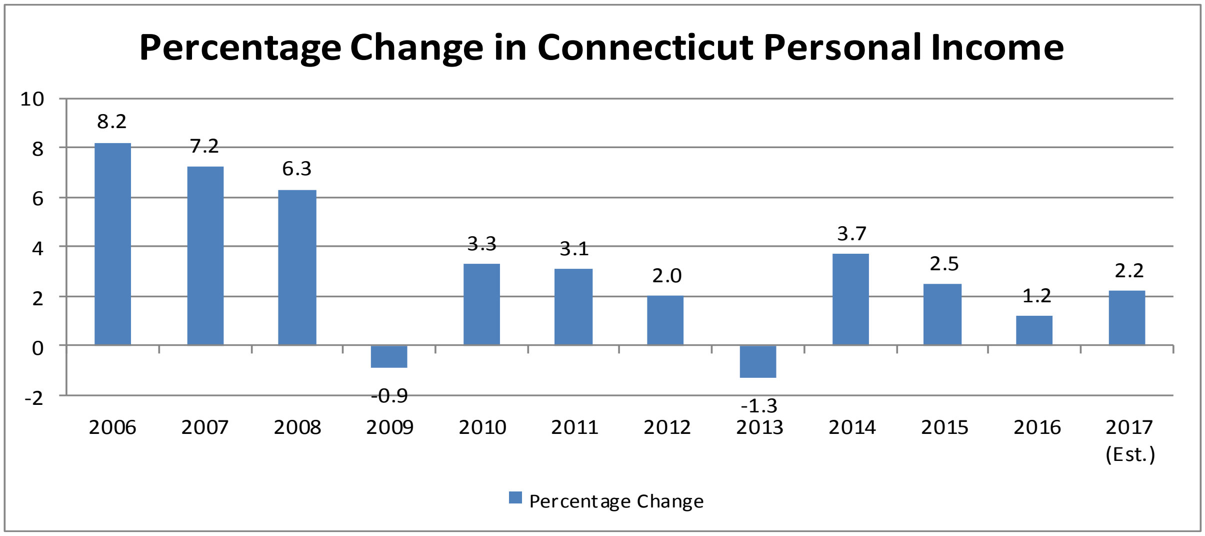
Payroll Employment Trend				
Jobs in thousands				
Sector	**12/17 (P)**	**12/16**	**Gain/Loss**	**% Change**
Construction	56.1	58.0	-1.9	-3.3%
Manufacturing	160.3	156.2	4.1	2.6%
Transp. & Public Utilities	300.3	298.1	2.2	0.7%
Information	31.1	31.9	-0.8	-2.5%
Financial	132.4	130.2	2.2	1.7%
Prof. & Business Svc.	219.0	216.4	2.6	1.2%
Education & Health Svc.	334.9	331.3	3.6	1.1%
Leisure & Hospitality	153.3	155.3	-2.0	-1.3%
Other Services	66.4	65.6	0.8	1.2%
Government	230.8	233.9	-3.1	-1.3%

Wage and $alary income

- December 2017 average hourly earnings at $31.00, not seasonally adjusted, were up $0.34, or 1.1%, from the December 2016 estimate. The resultant average private sector weekly pay amounted to $1,050.90, up $17.66, or 1.7% 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 December 2017 was 2.1%.
- The Bureau of Economic Analysis reported that Connecticut's personal income grew by 3% between 2015 and 2016. This ranked Connecticut 33rd nationally in 2016 income growth.
- A December 20th report from the Bureau showed Connecticut personal income increasing at a quarterly rate of 0.6% between the second and third quarters of 2017.

Based on these results, Connecticut ranked 36th nationally in personal income growth, and below the national average of 0.7% for the quarter. On an annualized basis, Connecticut's income growth would be 2.2%, which is just keeping up with the rate of inflation.

- State Personal Income for the fourth quarter 2017 and preliminary annual 2017 data are schedule to be released on March 22, 2018.



Housing

- In its January 7th release, Berkshire Hathaway HomeServices reported results for the Connecticut housing market for December 2017 compared with December 2016. Sales of single family homes declined 11.48 percent. However, the median sale price rose 3.09 percent. New listings in Connecticut decreased by 14.94 percent, but the median list price increased 3.26 percent to $258,150. Average days on the market increased 8.99 percent in December 2017 compared to the same month in the previous year (97 days on average, up from 89 days). The table below contains more detailed data for the Connecticut market.

MARKET SUMMARY

DECEMBER 2017 | SINGLE FAMILY HOMES

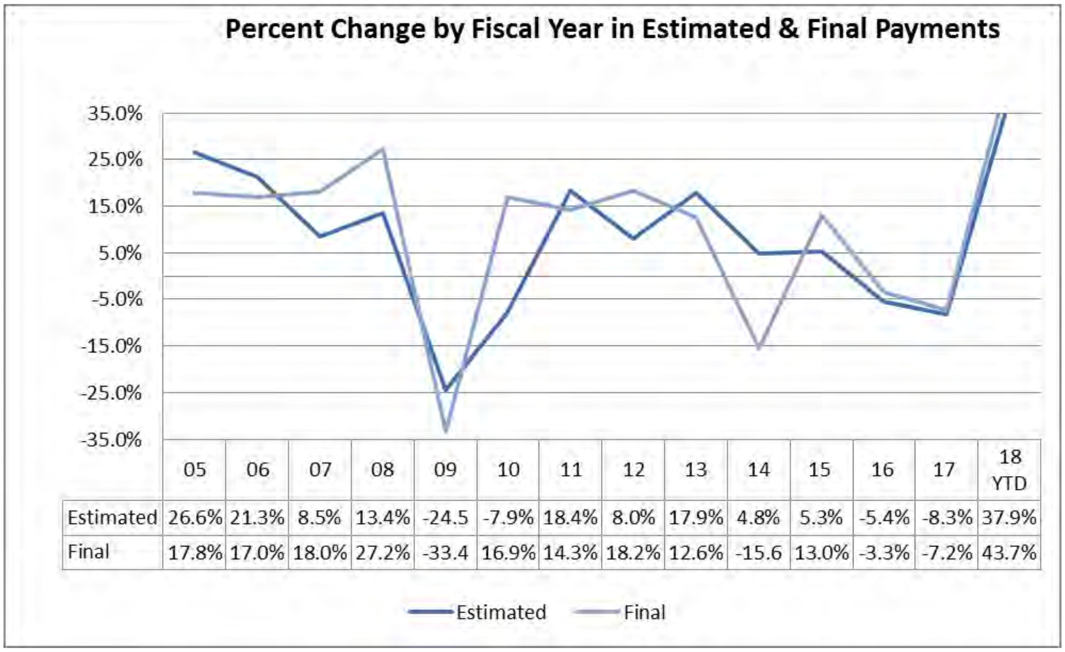
Market Summary	Month to Date			Year to Date		
	December 2017	December 2016	Percent Change	Year-To-Date 2017	Year-To-Date 2016	Percent Change
New Listings	2090	2457	-14.94% ▼	56445	59101	-4.49% ▼
Sold Listings	2582	2917	-11.48% ▼	36041	35170	2.48% ▲
Median Listing Price	$258,150	$249,999	3.26% ▲	$259,900	$259,000	0.35% ▲
Median Selling Price	$250,000	$242,500	3.09% ▲	$254,000	$250,000	1.6% ▲
Median Days on Market	71	60	18.33% ▲	54	56	-3.57% ▼
Average Listing Price	$403,738	$368,395	9.59% ▲	$397,405	$381,576	4.15% ▲
Average Selling Price	$385,722	$352,140	9.54% ▲	$381,051	$365,306	4.31% ▲
Average Days on Market	97	89	8.99% ▲	81	85	-4.71% ▼
List/Sell Price Ratio	96.5%	96.4%	0.17% ▲	97%	96.5%	0.56% ▲

- The following chart from Berkshire Hathaway HomeServices shows the total number of Connecticut single family homes for sale in December 2017 distributed by list price:

<u>Stock Market</u>

- Estimated and final income tax payments typically account for approximately 35 to 40% of total state income tax receipts. Both the estimated and final payments had a negative rate of growth in both Fiscal Years 2016 and 2017.
- However, due to a combination of one-time events, estimated payment collections increased substantially in December 2017, more than doubling the month-over-month total from the prior year. For example, December 2017 estimated payments

totaled $513.8 million versus $251.1 million in December 2016. In addition, year-to-date combined estimated and final payments were up 39.3 percent through December 2017 compared with the same period in 2016.



	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%	37.9%
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%	43.7%

- Two primary factors contributed to the significant increase in estimated payments in December 2017. The first is related to the recent Federal tax change that placed limits on the amount of state and local taxes (SALT) that can be deducted for Federal tax purposes. Based on this new provision, many Connecticut taxpayers made payments prior to the end of calendar 2017 to ensure these estimated income tax payments would be deductible for their Federal 2017 returns. Therefore, these payments represent a shift from collections that would likely have occurred in April 2018.
- The second factor was related to an October 2008 Federal law that eliminated a common mechanism used by hedge fund managers that enabled them to defer receipt of incentive or management fees earned by charging them to an offshore fund. Under the new rules (Internal Revenue Code Section 475A) hedge fund managers had to recognize these profits, earned prior to January 1, 2009, as income before December 31, 2017. Therefore, a significant amount of the estimated payments collected were related to hedge fund managers bringing these profits back to the United States from overseas. As such, they should be considered to be a one-time revenue source.

- All of the major stock market indices experienced significant gains in calendar 2017. The Dow added 25.1 percent, having hit 71 closing records over the course of the year. The S&P gained 19.4 percent, and the NASDAQ rose 28.2 percent in 2017. As of this writing, stocks continue their upward trend through January 2018.

DOW

NASDAQ

<u>Consumer Spending</u>

- 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 advance retail sales rose 0.4 percent in December, after a 0.9 percent growth in

November. Sales last month were supported by a 1.2 percent increase in receipts at gardening and building material stores. Sales at auto dealerships rose 0.2 percent, while gas station sales remained unchanged from the previous month.

- Last month, sales at electronics and appliance stores fell 0.2 percent. Clothing store receipts declined 0.3 percent, but sales at online retailers jumped 1.2 percent. Receipts at restaurants and bars rose 0.7 percent. Sales at sporting goods and hobby stores dropped 1.6 percent, the biggest decline since November 2016.
- For the year, retail sales grew 4.2 percent in 2017, the most in three years. Non-store retailers (online sales) were up 12.7 percent from December 2016, while building materials and garden equipment and supplies dealers were up 9.9 percent from last year.

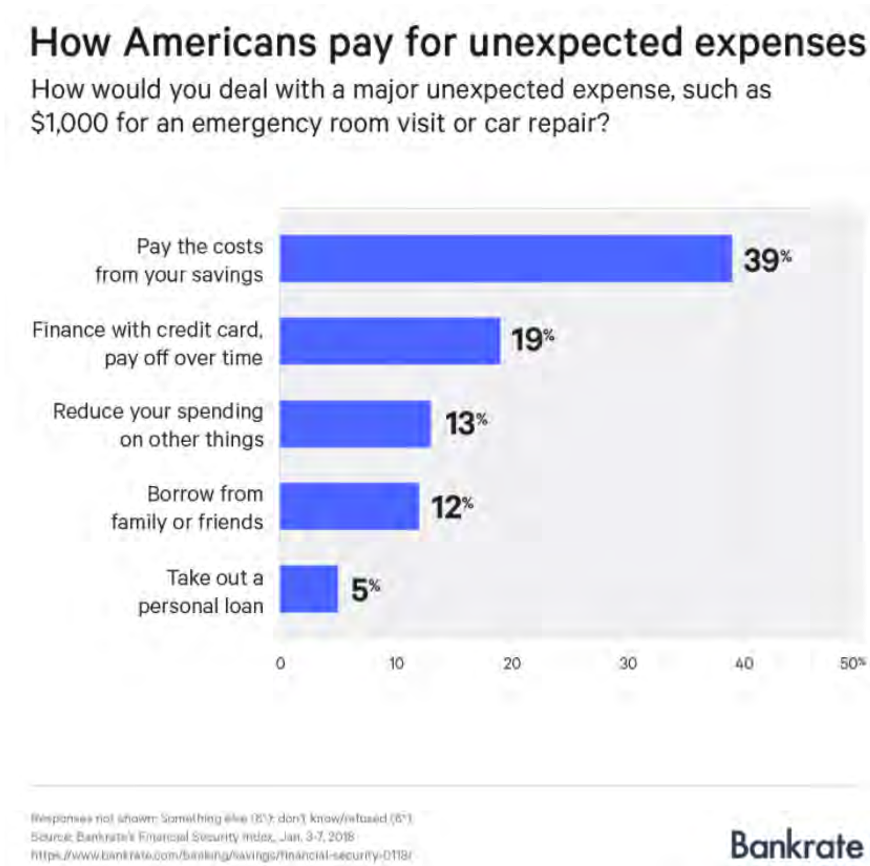
<u>Consumer Debt and Savings Rates</u>

- According to the Federal Reserve Bank of New York, aggregate household debt balances rose to another new peak in the third quarter of 2017. As of September 30, 2017, overall debt – including mortgages, auto loans and student loans – hit a record $12.96 trillion. This increase put overall household debt $280 billion above its peak in the third quarter of 2008, and 16.2 percent above its trough in the second quarter of 2013. Aggregate household debt balances have now increased in 13 consecutive quarters.
- The New York Federal Reserve also noted that mortgage balances, the largest component of household debt, increased again during the third quarter. Mortgage balances shown on consumer credit reports on September 30 stood at $8.74 trillion, an increase of $52 billion from the second quarter of 2017. Balances on home equity lines of credit (HELOC) have been slowly declining, dropping $4 billion from the second quarter and now stand at $448 billion. Non-housing balances, which have been increasing steadily for nearly six years, were up again in the third quarter, rising $68 billion. Auto loans grew by $23 billion and credit card balances increased by $24 billion, while student loan balances saw a $13 billion increase.
- In its January 29th release, the Bureau of Economic Analysis (BEA) reported the personal-saving rate declined to 2.4 % in December from 2.5% in November. This level has decreased steadily from a recent peak of 6.3% in October 2015 and is close to prerecession lows.
- The 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 December 2017. As can be seen there is a pronounced 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 dramatic 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.
- Two surveys in last year help to illustrate the point. In its May 2017 report on the Economic Wellbeing of U.S. Households for 2016, the Federal Reserve Board found despite improvement in recent years, substantial shares of adults struggle with their regular expenses or would have difficulty coping with an unexpected hardship:
    - Just under one-fourth of adults are not able to pay all of their current month's bills in full.
    - Forty-four percent of adults say they either could not cover an emergency expense costing $400, or would cover it by selling something or borrowing money.
    - Twenty-three percent of adults had to pay a major unexpected out-of-pocket medical expense in the prior year, and one-fourth report forgoing one or more type of health care in the prior year due to affordability.
- In January 2018, Bankrate completed its latest Financial Security Index survey and found similar results: Only 39 percent of Americans would use savings to cover an unexpected expense of $1,000. More than a third of respondents would resort to some type of debt to cover the expense. Almost 1 in 5 would pay with a credit card

and finance the balance over time; 12 percent would borrow from family or friends; and 5 percent would use a personal loan.

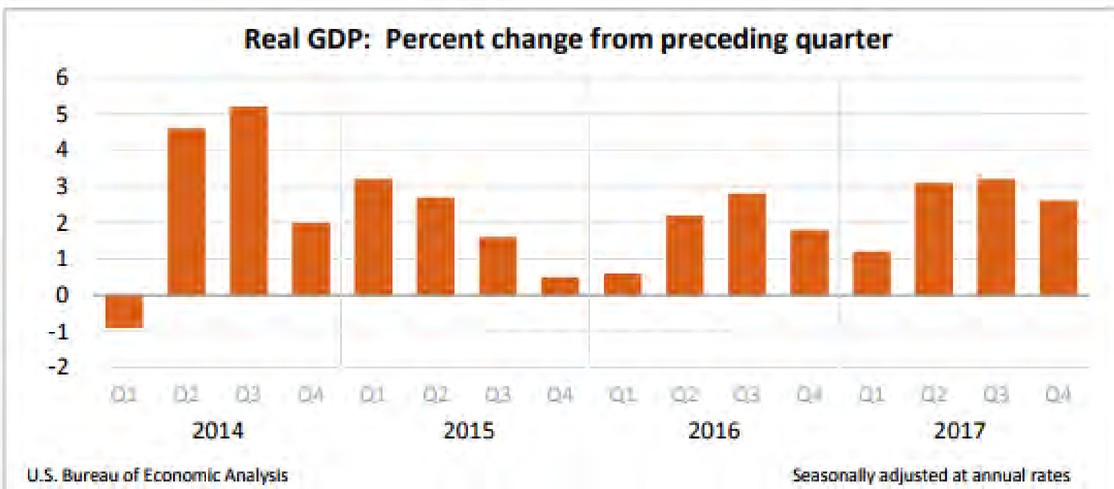


Consumer Confidence

- The U.S. consumer confidence index (CCI), published by the Conference Board, is an indicator designed to measure consumer confidence. This 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 consumers' assessment of current economic conditions increased in January 2018, following a decline in December. The Index now stands at 125.4, up from 123.1 in December. The board noted that expectations improved from the previous month, however consumers are somewhat ambivalent about their income prospects over the coming months.

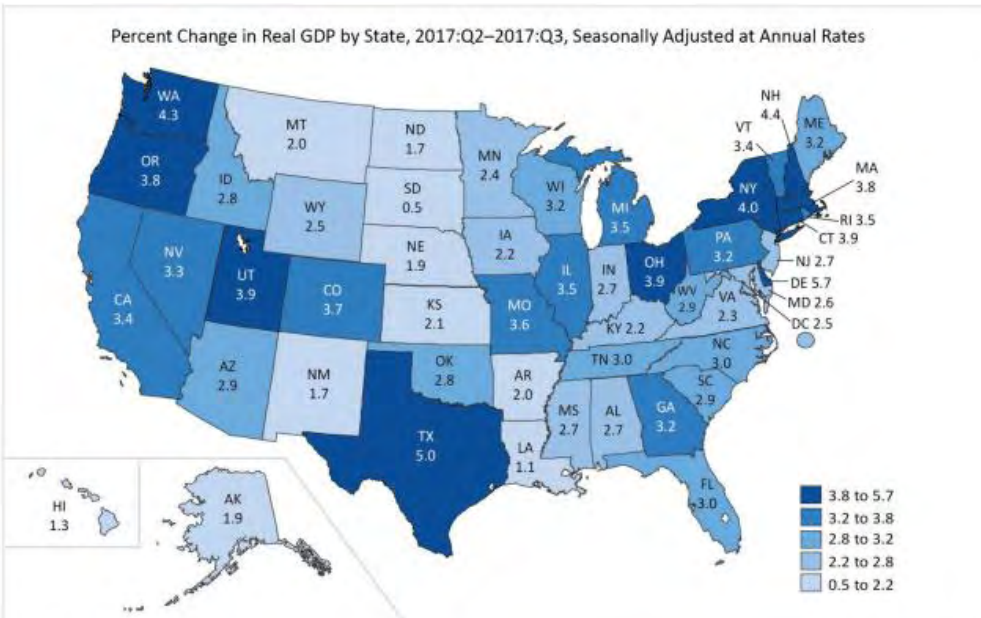
Business and Economic Growth

- According to a January 26th release from the Bureau of Economic Analysis, U.S. Real Gross Domestic Product increased at an annual rate of 2.6 percent in the fourth quarter of 2017. In the third quarter, real GDP increased 3.2 percent. For the year, the economy grew at 2.3 percent, up from the 1.5 percent growth rate experienced in 2016.
- The increase in real GDP in the fourth quarter reflected positive contributions from personal consumption expenditures (PCE), nonresidential fixed investment, exports, residential fixed investment, state and local government spending, and federal government spending that were partly offset by a negative contribution from private inventory investment. Imports, which subtract from GDP growth, increased at their fastest quarterly rate in more than seven years.



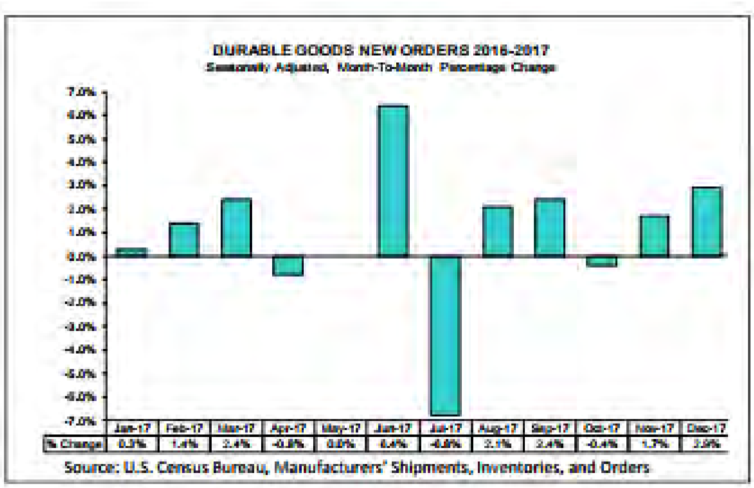
- Corporate profits rose 4.3 percent between the second and third quarter and grew 5.3 percent in the third quarter compared to the same period a year ago. Corporate profit for the fourth quarter and 2017 annual results are scheduled to be released on March 28, 2018.

- In a January 24th report, the Bureau of Economic Analysis released Real Gross Domestic Product (GDP) results by state for the third quarter of 2017. Connecticut experienced a seasonally adjusted annual growth rate of 3.9 percent, which ranked 8th in the nation overall. This was a significant improvement from the second quarter of 2017, when Connecticut ranked 44th in the nation with annualized growth of 1.9 percent. The sectors that contributed most to Connecticut's strong third



U.S. Bureau of Economic Analysis

quarter performance were finance and insurance, durable goods manufacturing, and information services.
- According to a December 22nd report by the U.S. Department of Commerce, new orders for durable goods in December increased \$7.0 billion or 2.9 percent to \$249.4 billion. This increase, up four of the last five months, followed a 1.7 percent November increase.
- Excluding transportation, new orders increased 0.6 percent. Excluding defense, new orders increased 2.2 percent. Transportation equipment, also up four of the last five months, led the increase, \$6.0 billion or 7.4 percent to \$87.2 billion.



- The January 24th Markit Flash Purchasing Manager's Index (PMI) reported that January data indicated another solid expansion of U.S. private sector business activity. Manufacturing production continued to increase at a much faster pace than service sector activity. The PMI was 53.8 in January, down from 54.1 in December. Any index reading above 50 indicates growth.

Key findings:

- Flash U.S. Composite Output Index at 53.8 (54.1 in December). 8-month low.
- Flash U.S. Services Business Activity Index at 53.3 (53.7 in December). 9-month low.
- Flash U.S. Manufacturing PMI at 55.5 (55.1 in December). 34-month high.
- Flash U.S. Manufacturing Output Index at 56.2 (55.9 in December). 12-month high.

Data collected January 12-23

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