Commission on Government Forecasting and Accountability

703 Stratton Ofc. Bldg., Springfield, IL 62706

MONTHLY BRIEFING FOR THE MONTH ENDED: DECEMBER 2013

HAPPY NEW YEAR

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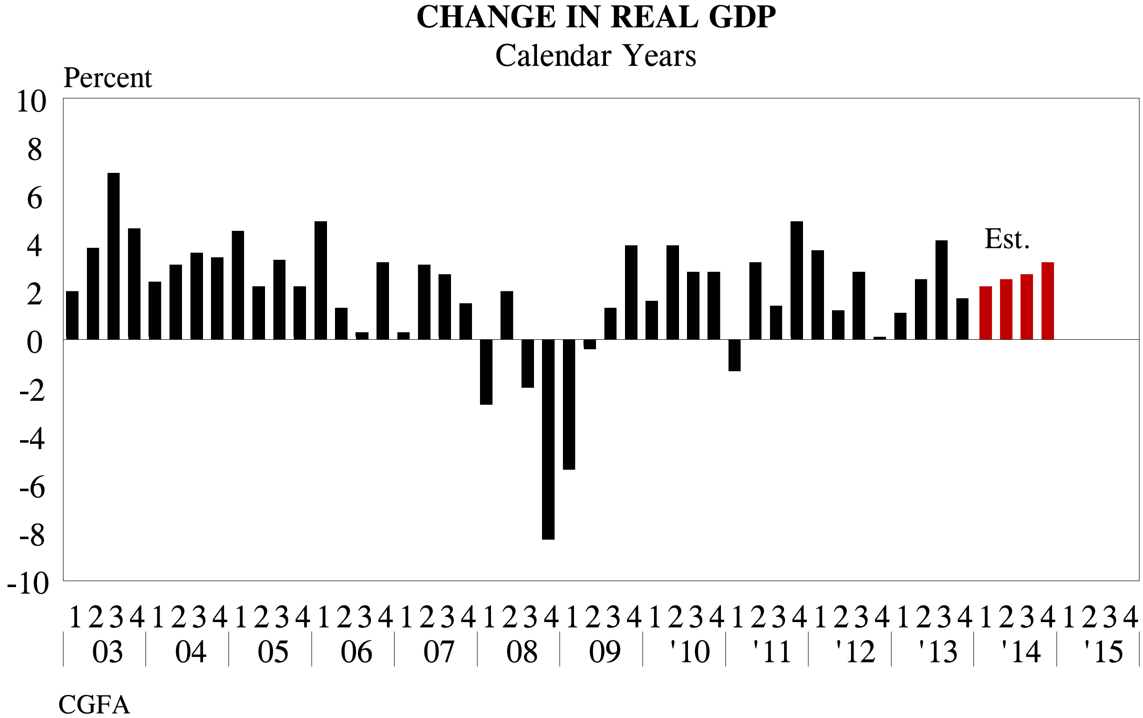
ECONOMY: What Lies Ahead?

Edward H. Boss, Jr., Chief Economist

Hopes run high that the economy will strengthen in the New Year following four and a half years of sub-par growth, marking it as the weakest economic recovery in the post WWII period. Growth improved throughout 2013, with an annual rate of gain in inflation-adjusted GDP of 1.1% in the first quarter, rising to 2.5% in the second, and 4.1% in the third. Similarly, the nation's unemployment rate, which began the year at 7.9% dropped to 7.0% by November. In December, the Federal Reserve announced the economy had strengthened enough to begin a path to taper their quantitative easing purchases of Treasury and mortgage-backed securities. On the fiscal front, Congress passed a budget deal on a bi-partisan basis, removing at least one uncertainty overhanging the economy. These developments were reflected in the stock market that reached record highs by year-end.

While there can be little doubt that the economy continues to advance, it is not out of the woods yet. For example, much of the increase in the third quarter was due to an inventory buildup which added to growth but, to the extent this was involuntary, will not be repeated in the fourth quarter. At the same time, consumer spending, the major force in the economy accounting for two-thirds to 70% of total spending rose at a 2.0% annual rate, less than half the 4.1% GDP gain that quarter and smaller than the 2.2% registered in 2012. Expectations for holiday sales in 2013 by the National Retail Federation were for a 3.9% increase, up from 3.5% last year and a ten year average of 3.3%. Even so, they are sticking to that forecast although there are some recent reports that raise questions as to whether this target will be attained.

CHART 1



Shoppertrak, which tracks data at 40,000 locations, reported that after a strong start, holiday sales were down for the third consecutive week and in the week ended December 22nd, dropped 3.1% from a year earlier. For November and December, Shoppertrak estimates that sales at stores so far are up 2.0% compared to a year earlier, below the 2.4% forecast for this group by the National Retail Federation. At the same time it reports that online spending from home and work from November through mid-December was up 9% from a year ago, less than the 14% forecast and points out those online sales only account for about 11% of spending during the three months that include the holiday shopping season.

Overall retail sales improved in November, perhaps buoyed by an early Hanukkah, but may have dampened overall holiday sales gains in December. In addition, a major contributor to the economy has been the continued turnaround in the housing sector. Even so, a recent edging up in mortgage interest rates and a moderation in median home prices could soften the pace of housing advancement. There also remain uncertainties over fiscal policies.

While there was the bipartisan agreement on the budget there is yet to be an agreement on the debt ceiling. And, there are some 55 tax breaks that expired at year end unless Congress retroactively reinstates some or all of them. This makes it hard for businesses to plan. One such benefit is the tax treatment of any reduction in a person's mortgage debt due to a short sale by a bank. This now will be taxed as ordinary income and, if not reversed could be devastating to the housing sector. In addition, extended unemployment benefits expired at year-end and could impact the economy in various ways, from reducing consumer spending and increasing food stamps further to increasing the labor force participation rate, putting upward pressure on the reported unemployment rate.

In conclusion, while the economic expansion appears to be on a sustainable path, the accelerated growth pattern during the first three quarters of last year is unlikely to be representative of the path taken in 2014. As shown in the chart above, the latest forecast by Global Insight, a forecasting service used by the Commission, indicates growth slowed sharply in the fourth quarter of 2013 and its forecast for this year is for a gain in real GDP of 2.5%, up from last year but in line with that recorded on average during the previous four years.

INDICATORS OF ILLINOIS ECONOMIC ACTIVITY

INDICATORS	NOV. 2013	OCT. 2013	NOV. 2012
Unemployment Rate (Average)	8.7%	9.9%	8.7%
Annual Rate of Inflation (Chicago)	-3.8%	-4.0%	0.6%

	LATEST MONTH	% CHANGE OVER PRIOR MONTH	% CHANGE OVER A YEAR AGO
Civilian Labor Force (thousands) (Nov.)	6,523	0.10%	-1.3%
Employment (thousands) (Nov.)	5,955	0.2%	-1.3%
New Car & Truck Registration (Nov.)	41,201	-17.8%	1.8%
Single Family Housing Permits (Nov.)	848	-22.9%	-14.7%
Total Exports ($ mil) (Oct.)	6,359	26.2%	12.4%
Chicago Purchasing Managers Index (Dec.)	59.1	-6.2%	18.2%

DECEMBER 2013 BOND SALE

Lynnae Kapp, Senior Bond/Revenue Analyst

In December, Illinois sold $350 million of taxable General Obligation Bonds. The true interest cost was 5.40%, with a spread over Treasuries of 251 basis points. This spread is 59 basis points lower than an identical sale in April of 2013. The Governor's Office of Management and Budget attributes the smaller spread to the passage of SB 1 pension reform. This smaller spread will save the State over $20 million over the life of the bonds.

The State sold $600 million of Build Illinois refunding bonds in June 2013. The sale received a 2.70% true interest cost, and gave the State approximately 9% in present value savings equaling $55 million. The refunding also freed up $30 million - $40 million of reserves that will no longer be required.

Illinois also sold $1.3 billion of General Obligation bonds at the end of June 2013. This occurred after four days of massive sell-offs of bonds in the market. Illinois' G.O. bonds "received more than $9 billion in bids from 145 investors…and it was able to pare between 6 to 14 basis points off yields on some maturities after lowering some by as much as 10 basis points from preliminary marketing levels" ["Buyers Devour Illinois GOs As Market Rallies Back From Selloff", The Bond Buyer, June 26, 2013]. Even though the State was able to somewhat lower the yields of the bonds, the Governor stated that the ratings downgrades cost the State an additional $130 million in debt service over the 25-year maturity of the bonds.

DATE	BOND SALE TYPE	AMOUNT	TAXABLE v. TAX-EXEMPT	NEGOTIATED v. COMPETITIVE SALE	TRUE INTEREST COST	S&P	FITCH	MOODY'S
Apr-13	GO Series A bonds	$450 million	tax-exempt	competitive	3.92%	A-	A	A2
Apr-13	GO Series B bonds	$350 million	taxable	competitive	4.97%			
May-13	BI bonds	$300 million	taxable	competitive	3.29%	AAA	AA+	A2
Jun-13	BI Refunding bonds	$604 million	tax-exempt	negotiated	2.70%	AAA	AA+	A3
Jun-13	GO bonds	$1.3 billion	tax-exempt	negotiated	5.04%	A-	A-	A3
Dec-14	GO bonds	$350 million	taxable	competitive	5.40%	A-	A-	A3

In FY 2013, the State sold a total of $2.15 billion in G.O. capital projects bonds, $300 million in Build Illinois project bonds, and $604 million in Build Illinois refunding bonds. Bond Principal outstanding is approximately $31.3 billion:

GO	$13.488 billion
Pension	$14.686 billion
Build Illinois	$3.032 billion
Civic Center	$63 million

REVENUE

December Receipts Perform Well With Income and Sales Tax Leading the Gains

Jim Muschinske, Revenue Manager

Overall base revenues advanced $231 million in December. The larger economically related sources of income and sales taxes posted sizable gains for the month. An extra receipting day was a significant contributor to the gains, particularly in the case of personal income taxes.

Gross personal income tax receipts grew $201 million, or $185 million net of refunds. Gross corporate income taxes advanced $58 million, or $53 million net of refunds. Sales taxes continued to perform quite well, growing $37 million for the month. Corporate franchise taxes increased $5 million, while interest earnings managed to post a $1 million gain.

While overall revenues performed well for the month, a few sources experienced declines to end 2013. Insurance taxes fell $8 million, inheritance taxes were off $5 million, while other sources eased $4 million, and public utility fell $3 million.

Overall transfers grew $14 million in December. Lottery transfers rose $14 million and riverboat transfers gained $12 million. Those gains were partially offset by a $12 million loss in all other transfers. Federal sources experienced a down month, falling $44 million to end the year.

Year to Date

Through the first half of FY 2014, base general funds are up $815 million compared to last fiscal year. Nearly half of that growth can be attributed to the one-time surge in transfers related to the refund fund [$397 million]. However, despite the pause in October and November, the larger economically-related sources fared quite well at the fiscal year's halfway mark.

With a strong December, gross personal income taxes are up $349 million, or $335 million net of refunds. Sales taxes continue to do quite well, up $200 million to date. Gross corporate income tax is up a strong $130 million, or $121 million net of refunds. Other sources are up $61 million for the year, although all of that increase can be attributed to September's receipt of one-time court settlement proceeds.

Despite the performance of the larger sources, a number of smaller revenue lines suffered declines worth noting. The Cook County IGT is off $30 million, inheritance tax is down $29 million, and public utility tax is down $15 million.

Through December, overall transfers are up $404 million. Nearly all of those gains stem from the one-time $397 million transfer from the Income Tax Refund Fund. Federal sources are down $230 million thus far, reflecting lower reimbursable spending.

As we enter the second half of the fiscal year, revenue performance thus far would have to be viewed in a positive light and reaffirm observations made during the Commission's revised November forecast. Both personal and corporate income taxes have performed at levels that, barring a near-term turn around, should result in an upward revision to the estimates scheduled to occur in late February. Sales tax continues to perform surprisingly well, and should be able to meet, and perhaps even exceed, the upward revision made earlier. However, to reiterate concerns made in the fall, absent an unlikely surge in reimbursable spending, federal sources continue to fall further behind projections.

GENERAL FUNDS RECEIPTS: DECEMBER
FY 2014 vs. FY 2013
($ million)

Revenue Sources	Dec. FY 2014	Dec. FY 2013	$ CHANGE	% CHANGE
State Taxes				
Personal Income Tax	$1,542	$1,341	$201	15.0%
Corporate Income Tax (regular)	575	517	$58	11.2%
Sales Taxes	692	655	$37	5.6%
Public Utility Taxes (regular)	79	82	($3)	-3.7%
Cigarette Tax	30	30	$0	0.0%
Liquor Gallonage Taxes	14	14	$0	0.0%
Vehicle Use Tax	2	2	$0	0.0%
Inheritance Tax (Gross)	18	23	($5)	-21.7%
Insurance Taxes and Fees	61	69	($8)	-11.6%
Corporate Franchise Tax & Fees	20	15	$5	33.3%
Interest on State Funds & Investments	2	1	$1	100.0%
Cook County IGT	0	0	$0	N/A
Other Sources	24	28	($4)	-14.3%
Subtotal	$3,059	$2,777	$282	10.2%
Transfers				
Lottery	77	63	$14	22.2%
Riverboat transfers & receipts	46	34	$12	35.3%
Proceeds from Sale of 10th license	0	0	$0	N/A
Refund Fund transfer	0	0	$0	N/A
Other	40	52	($12)	-23.1%
Total State Sources	$3,222	$2,926	$296	10.1%
Federal Sources	$252	$296	($44)	-14.9%
Total Federal & State Sources	$3,474	$3,222	$252	7.8%
Nongeneral Funds Distribution:				
Refund Fund				
Personal Income Tax	($147)	($131)	($16)	12.2%
Corporate Income Tax	($77)	(72)	($5)	6.9%
Subtotal General Funds	$3,250	$3,019	$231	7.7%
Short-Term Borrowing	$0	$0	$0	N/A
FY'13/14 Backlog Payment Fund	$0	$0	$0	N/A
Budget Stabilization Fund Transfer	$0	$0	$0	N/A
Total General Funds	$3,250	$3,019	$231	7.7%

CGFA SOURCE: Office of the Comptroller: Some totals may not equal, due to rounding 3-Jan-14

GENERAL FUNDS RECEIPTS: YEAR TO DATE
FY 2014 vs. FY 2013
($ million)

Revenue Sources	FY 2014	FY 2013	CHANGE FROM FY 2013	% CHANGE
State Taxes				
Personal Income Tax	$7,927	$7,578	$349	4.6%
Corporate Income Tax (regular)	1,530	1,400	$130	9.3%
Sales Taxes	3,895	3,695	$200	5.4%
Public Utility Taxes (regular)	468	483	($15)	-3.1%
Cigarette Tax	177	176	$1	0.6%
Liquor Gallonage Taxes	85	86	($1)	-1.2%
Vehicle Use Tax	15	14	$1	7.1%
Inheritance Tax (Gross)	129	158	($29)	-18.4%
Insurance Taxes and Fees	154	158	($4)	-2.5%
Corporate Franchise Tax & Fees	107	107	$0	0.0%
Interest on State Funds & Investments	9	8	$1	12.5%
Cook County IGT	26	56	($30)	-53.6%
Other Sources	244	183	$61	33.3%
Subtotal	$14,766	$14,102	$664	4.7%
Transfers				
Lottery	314	308	$6	1.9%
Riverboat transfers & receipts	211	221	($10)	-4.5%
Proceeds from Sale of 10th license	0	0	$0	N/A
Refund Fund transfer	397	0	$397	N/A
Other	268	257	$11	4.3%
Total State Sources	$15,956	$14,888	$1,068	7.2%
Federal Sources	$1,460	$1,690	($230)	-13.6%
Total Federal & State Sources	$17,416	$16,578	$838	5.1%
Nongeneral Funds Distribution:				
Refund Fund				
Personal Income Tax	($753)	($739)	($14)	1.9%
Corporate Income Tax	($205)	($196)	($9)	4.6%
Subtotal General Funds	$16,458	$15,643	$815	5.2%
Short-Term Borrowing	$0	$0	$0	N/A
FY'13/14 Backlog Payment Fund Transfer	$50	$264	($214)	N/A
Tobacco Liquidation Proceeds	$0	$0	$0	N/A
Pension Contribution Fund Transfer	$0	$0	$0	N/A
Budget Stabilization Fund Transfer	$275	$275	$0	0.0%
Total General Funds	$16,783	$16,182	$601	3.7%

SOURCE: Office of the Comptroller, State of Illinois: Some totals may not equal, due to rounding.

CGFA 3-Jan-14