Commission on Government Forecasting and Accountability

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MONTHLY BRIEFING FOR THE MONTH ENDED: DECEMBER 2016

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A Study of the Public Safety Employee Benefits Act Pursuant to P.A. 98-0561

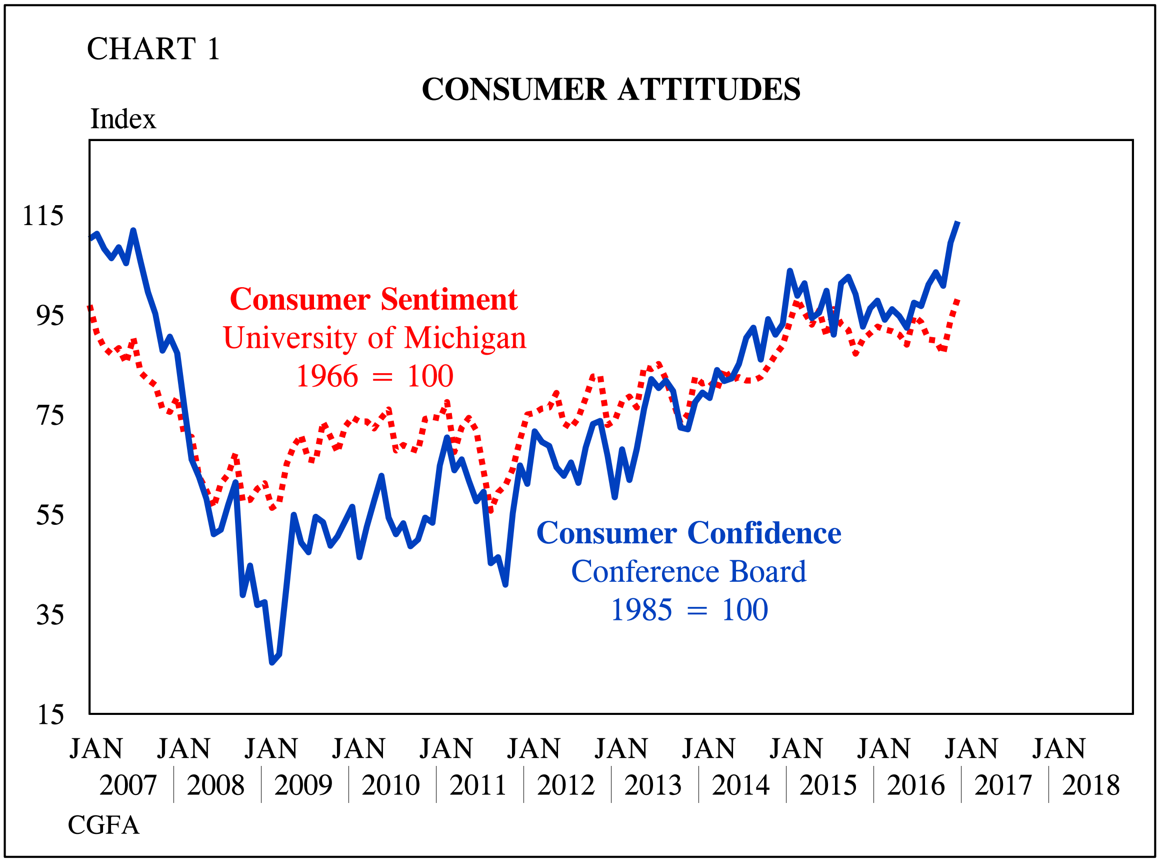
ECONOMY: Entering a New Year

Edward H. Boss, Jr., Chief Economist

Even as the latest GDP figures for the third quarter were revised upward from earlier estimates of 2.9% and 3.2% to a final figure of 3.5%, the highest rate of growth in two years, most forecasters were estimating a slowdown occurred in the final quarter. Fourth quarter estimates center around 1.7% which, when combined with a sluggish 1.1% annual rate in the first half of the year, would bring growth for 2016 to around 1.8%. This would be a slowdown from the 2.5% rate for 2015, 2.4% in 2014, and on a par with a 1.7% growth in 2013, and for only the second time since 2010 that the growth rate fell below 2.0%. Even so, as the year comes to an end, the outlook for the economy appears to have taken on an improved pace as the New Year begins.

Last minute shopping helped retailer's rack up bigger holiday sales than originally forecast. In July, the National Retail Federation reported retail sales were essentially unchanged from June while, retail sales dipped 0.3% in August. September saw retail sales rising a modest 0.2% with October sales healthy as the holidays approached. According to the research firm, Customer Growth Partners, November and December sales are on a path to be up an estimated 4.9% over the last holiday season to record the biggest year-over-year growth since the recession. It ascribes the rise to lower food and gas prices and an increase in wages making consumers more willing to spend, while colder temperatures, as well as Hanukkah falling late and Christmas coming on a Sunday, gave last minute shoppers a few more days to shop.

Not to be ignored in the improved outlook is the post-election surge in the stock market, which at the current time, is up to record levels having risen 8% since the presidential election. Also it is important to note that 19 states are set to increase their minimum wage in 2017. Per-



haps the best indicator of the improved sentiment since the elections, however, was recently released by the Conference Board in the form of its Consumer Confidence Index which in December rose to 113.7, up from an upwardly revised level of 109.4 in November. As shown in the Chart above, December's gain put the Index at its highest point in 13 years. Similar improvement had been shown by the University of Michigan's Consumer Sentiment Index which in December at 98.2 was at its highest point on the chart that goes back to the beginning of 2007.

The rise in the Consumer Confidence Index in December was entirely due to the Expectations Index that increased sharply from 94.4 to 105.5 while the Present Situation Index decreased from 132.0 in November to 126.1. According to Lynn Franco, the Director of Economic Indicators at the Conference Board, the post-election surge in optimism for the economy, jobs and income prospects, as well as for stock prices, was most pronounced among older consumers. At the same time, consumer's assessment of current conditions, which declined, nevertheless still suggest that economic growth continued through the final months of 2016.

As we enter 2017, whether or not the improved pace of economic activity is maintained, slows, or speeds up will depend on how the various factors behind current activity evolve. Proposed corporate and personal tax cuts, the reflow of corporate funds held abroad, and reduced regulation auger well for improved economic activity. At the same time, large proposed increases in infrastructure and military spending and tightening labor markets are expected to put upward pressure on prices. As fiscal policy takes over from total dependence on monetary policy, interest rates are likely to rise as well as a further strengthening in the U.S. dollar that could provide some restraints. Of course the major factor that may decide the state of the economy in the New Year may well depend on events both inside and outside the country in an increasingly dangerous world.

INDICATORS OF ILLINOIS ECONOMIC ACTIVITY

INDICATORS *	NOV. 2016	OCT. 2016	NOV. 2015
Unemployment Rate (Average)	5.6%	5.6%	6.0%
Annual Rate of Inflation (Chicago)	0.2%	0.1%	1.5%

	LATEST MONTH	% CHANGE OVER PRIOR MONTH	% CHANGE OVER A YEAR AGO
Civilian Labor Force (thousands) (November)	6,565.4	0.0%	0.4%
Employment (thousands) (November)	6,197.0	0.0%	0.9%
NonFarm Payroll Employment (November)	6,025,500	1,700	43,000
New Car & Truck Registration (November)	44,313	-11.5%	1.1%
Single Family Housing Permits (November)	788	-29.2%	-4.5%
Total Exports ($ mil) (October)	5,451.5	12.3%	-0.9%
Chicago Purchasing Managers Index (Dec.)	54.6	-5.2%	27.2%

* Due to monthly fluctuations, trend best shown by % change from a year ago

REVENUE
December Revenues Drop With First Half Performance Reminiscent of Past Recessionary Levels

Jim Muschinske, Revenue Manager

Overall base revenues fell $257 million in December. Troubling weakness in income tax receipts coupled with continued dismal federal source reimbursements were responsible for the bulk of the decline. December had one less receipting day compared to the same prior year period.

Gross personal income tax receipts dropped by $93 million, or $116 million net of refunds and diversions to the Fund for Advancement of Education and Commitment to Human Services Fund. Gross corporate income taxes fell by $88 million for the month, or $80 million net of refunds. Despite the significant falloff, it actually represents an improvement in the year to date performance. Again, to repeat comments from earlier monthly briefings, the new ledger accounting system at IDoR continues to manifest in dramatic shifts in receipt patterns, making interpretation of monthly income tax receipts very challenging. The Department has indicated that the new system's ability to "work returns" and make reconciliations is more timely and accurate than the previous accounting system. Public utility tax receipts fell $21 million for the month, inheritance taxes were down $12 million, cigarette taxes declined $6 million, insurance taxes and corporate franchise taxes dropped $3 million, while vehicle use tax dipped $1 million.

While the majority of revenue sources experienced a decline in December, a few areas did manage to post gains. As expected, sales taxes benefited from some "slippage" of November receipts into the first days of December. As a result, the monthly increase of $47 million likely is somewhat overstated. Other sources rose $7 million, liquor taxes grew $2 million, with interest income eking out a $1 million advance.

Overall transfers grew by $18 million in December. The lottery transfer grew $15 million and riverboat transfers were up $3 million. As mentioned, federal sources experienced another extremely weak month, falling $90 million below last year, reflecting reimbursable spending levels from the general funds.

Year To Date

With half of the fiscal year completed, base receipts are off $865 million, or 6.1%. Readers of the last several briefings likely have noticed growing concern with each successive month's disappointing revenue performance. Embedded within the overall falloff of 6.1%--of which a large part is due to a drop of $290 million or 22.4% in federal sources—is the combined drop of 4.5% from the "Big Three" [gross personal, gross corporate, and sales]. While that percentage falloff may slightly overstate the decline due to timing aspects still related to the income tax rate phase down, perhaps most unsettling is that the last time the Big Three experienced a combined decline during the first half of a fiscal year [absent tax rate changes] was during the recessionary years impacting FY 2009 and FY 2010, when performance was -0.9% and -10.4%, respectively. That is not to say we are in recession, as most economic measures would indicate otherwise, but rather gives context to what only can be described as troubling revenue performance thus far in FY 2017.

Gross corporate income taxes are off $386 million, or $340 million net of refunds. Gross personal income tax is down $189 million or $260 million if refunds and diversions to the education and human service funds are included. As mentioned, sales taxes are weak and have managed to grow only $45 million. Overall transfers are down $62 million to date. Only the one-time nature of this month's SERS repayment has allowed other sources to post a $111 million increase.

With continued dramatic falloffs month after month in federal sources, receipts are behind last year's dismal pace by $290 million. In all likelihood, federal sources will fall several hundred million below the Commission's forecast, and probably over a billion below the GOMB forecast released in Oct/Nov. [See last month's briefing for a more detailed discussion of the CGFA/GOMB revenue estimate comparisons].

To summarize, to date the State has experienced across the board revenue weakness. The most closely economically-tied major sources are experiencing levels of weakness not seen since the last recession. This poor receipt performance has limited the ability to direct more resources to reimbursable spending and as a result, federal source receipts have also suffered. That being said, economic conditions as measured by most conventional indices would reflect weakness, but not at recessionary levels. In addition, non-wage income from strong stock market performance in 2016 could translate into more positive performance in final payments. Additionally, as the Commission has indicated in earlier briefings, the DoR's ledger conversion has altered historical receipt patterns, likely contributing to some of the year to date declines experienced thus far. As we near the end of the first year's impact of that accounting conversion, the potential exists for a return to less volatile monthly swings, which up until now, has trended toward the negative.

DECEMBER
FY 2017 vs. FY 2016
($ million)

Revenue Sources	Dec. FY 2017	Dec. FY 2016	$ CHANGE	% CHANGE
State Taxes				
Personal Income Tax	$1,314	$1,407	($93)	-6.6%
Corporate Income Tax (regular)	236	324	($88)	-27.2%
Sales Taxes	789	742	$47	6.3%
Public Utility Taxes (regular)	64	85	($21)	-24.7%
Cigarette Tax	25	31	($6)	-19.4%
Liquor Gallonage Taxes	16	14	$2	14.3%
Vehicle Use Tax	2	3	($1)	-33.3%
Inheritance Tax	17	29	($12)	-41.4%
Insurance Taxes and Fees	58	61	($3)	-4.9%
Corporate Franchise Tax & Fees	17	20	($3)	-15.0%
Interest on State Funds & Investments	3	2	$1	50.0%
Cook County IGT	0	0	$0	N/A
Other Sources	31	24	$7	29.2%
Subtotal	$2,572	$2,742	($170)	-6.2%
Transfers				
Lottery	68	53	$15	28.3%
Riverboat transfers & receipts	27	24	$3	12.5%
Proceeds from Sale of 10th license	0	0	$0	N/A
Refund Fund transfer	0	0	$0	N/A
Fund sweeps	0	0	$0	N/A
Other	40	40	$0	0.0%
Total State Sources	$2,707	$2,859	($152)	-5.3%
Federal Sources	$129	$219	($90)	-41.1%
Total Federal & State Sources	$2,836	$3,078	($242)	-7.9%
Nongeneral Funds Distribution:				
Refund Fund				
Personal Income Tax	($156)	($137)	($19)	13.9%
Corporate Income Tax	($41)	(49)	$8	-16.3%
Fund for Advancement of Education	($29)	(27)	($2)	7.4%
Commitment to Human Services Fund	($29)	(27)	($2)	7.4%
Subtotal General Funds	$2,581	$2,838	($257)	-9.1%
Short-Term Borrowing	$0	$0	$0	N/A
Interfund Borrowing	$0	$0	$0	N/A
Budget Stabilization Fund Transfer	$0	$0	$0	N/A
Total General Funds	$2,581	$2,838	($257)	-9.1%

CGFA SOURCE: Office of the Comptroller: Some totals may not equal, due to rounding 4-Jan-17

GENERAL FUNDS RECEIPTS: YEAR TO DATE
FY 2017 vs. FY 2016
($ million)

Revenue Sources	FY 2017	FY 2016	CHANGE FROM FY 2016	% CHANGE
State Taxes				
Personal Income Tax	$6,579	$6,768	($189)	-2.8%
Corporate Income Tax (regular)	589	975	($386)	-39.6%
Sales Taxes	4,188	4,143	$45	1.1%
Public Utility Taxes (regular)	412	431	($19)	-4.4%
Cigarette Tax	172	177	($5)	-2.8%
Liquor Gallonage Taxes	89	86	$3	3.5%
Vehicle Use Tax	15	18	($3)	-16.7%
Inheritance Tax	138	192	($54)	-28.1%
Insurance Taxes and Fees	167	161	$6	3.7%
Corporate Franchise Tax & Fees	109	111	($2)	-1.8%
Interest on State Funds & Investments	15	10	$5	50.0%
Cook County IGT	56	56	$0	0.0%
Other Sources	298	187	$111	59.4%
Subtotal	$12,827	$13,315	($488)	-3.7%
Transfers				
Lottery	346	312	$34	10.9%
Riverboat transfers & receipts	166	171	($5)	-2.9%
Proceeds from Sale of 10th license	0	0	$0	N/A
Refund Fund transfer	0	77	($77)	-100.0%
Fund sweeps	0	0	$0	N/A
Other	299	313	($14)	-4.5%
Total State Sources	$13,638	$14,188	($550)	-3.9%
Federal Sources	$1,006	$1,296	($290)	-22.4%
Total Federal & State Sources	$14,644	$15,484	($840)	-5.4%
Nongeneral Funds Distribution:				
Refund Fund				
Personal Income Tax	($737)	($660)	($77)	11.7%
Corporate Income Tax	($102)	($148)	$46	-31.1%
Fund for Advancement of Education	($202)	($205)	$3	N/A
Commitment to Human Services Fund	($202)	($205)	$3	N/A
Subtotal General Funds	$13,401	$14,266	($865)	-6.1%
Short-Term Borrowing	$0	$0	$0	N/A
Interfund Borrowing	$0	$0	$0	N/A
Budget Stabilization Fund Transfer	$0	$125	($125)	-100.0%
Total General Funds	$13,401	$14,391	($990)	-6.9%

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

CGFA 4-Jan-17