Commission on Government Forecasting and Accountability

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MONTHLY BRIEFING FOR THE MONTH ENDED: MARCH 2017

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INSIDE THIS ISSUE

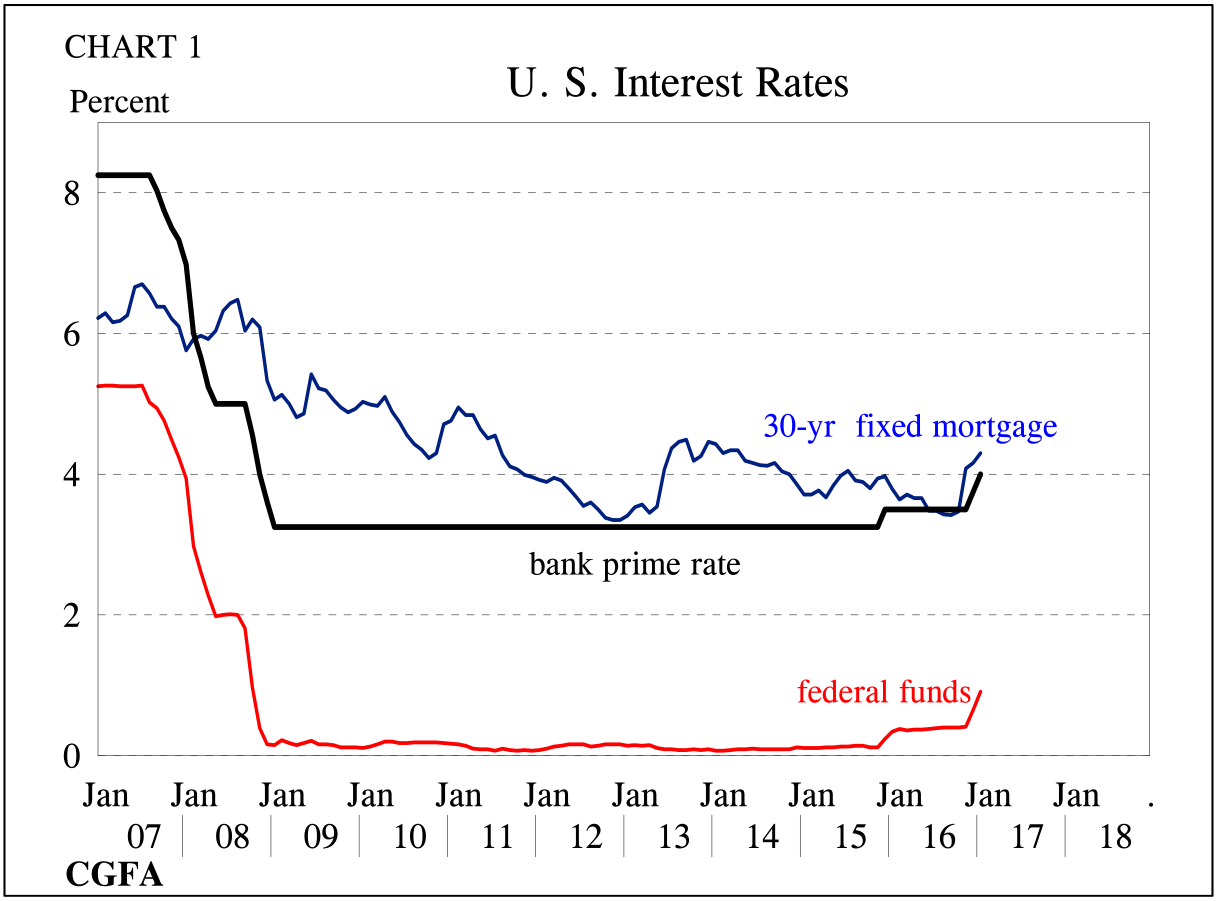
ECONOMY: The Federal Reserve Revisited

Edward H. Boss, Jr., Chief Economist

Last month's Monthly Revenue Report looked at expectations for upward pressure on key interest rates by the Federal Reserve due to rising inflation measures in the realm of an improving economy and the beginning of better conditions in the labor market. Following a federal funds targeted range of 0 to 0.25%, which prevailed from 2009 to December 2015 when it raised its range to 0.25% to 0.50%, the Federal Reserve moved up the range again from 0.50% to 0.75% at year-end 2016. Attention then shifted to a further increase at one of the upcoming FOMC meetings scheduled for March, May, and June of 2017.

While at the time, many analysts gave low odds for another rate increase as early as March of this year, that is exactly what the Fed did when at its mid-March meeting it raised the federal funds target range from 0.75% to 1.00%. See chart at top of next page. (One member voted to retain the existing target range rather than raise it, citing he voted no because inflation was still below the central bank's 2 percent target and the labor market keeps improving, suggesting slack still remains.)

The chart also displays a rise in lending rates, in the form of the commercial bank prime rate, which was raised in mid-March 2017 for the third time since 2009, to a level of 4%, the highest since 2008. The rate on 30-year fixed mortgages also edged up, but only slightly from a year earlier and remains low on a historical basis. To date the rise in rates seemingly has yet to dampen sales of new single-family homes. In February of this year single-family home sales were 6.1% above January's level and 12.8% higher than a year earlier.



Some analysts point to the past where when mortgage interest rates began to rise, home sales initially increased in anticipation of even higher rates in the future. Another factor to consider is the effect of higher mortgage rates on housing affordability. A housing affordability index is published by National Association of Realtors, (an index of 100 means that a family with a median income has exactly enough income to qualify for a mortgage on a median priced home.) In January 2017, the Affordability Index stood at 162 and has been in the 160-170 area since the summer of 2015. Moreover with emerging signs of income improvement, it could sustain affordability at decent levels for some time.

As stated in the minutes of the mid-March FOMC meeting," *It is well understood that the impact of Federal Reserve policy on the economy operates with a significant lag sometimes up to 18 months. And because of that lag, policy actions to achieve certain employment and inflation objectives are often overshot."* When assessing the current reading on employment and inflation in relation to the Fed's objectives, it would appear that the inflation target would be of most concern, particularly because once ignited, inflation has been extremely difficult to reign in.

While the unemployment rate is at a low 4.8% rate, the labor force participation rate remains extremely low, suggesting little near term threat of wage push inflation on the horizon. The Fed's preferred inflation target, the personal consumption expenditure rate less food and energy, has been edging up from 1.5% a year earlier to 1.7% this January. At the same time, the core consumer price index excluding food and energy rose at 2.2% over a year ago and has been above 2.0% for 15 months while the all items consumer price index was up 2.7% from a year earlier, its highest reading since early 2012.

The FOMC minutes concluded that economic conditions will evolve in a manner that will warrant gradual increases in the federal funds rate. The timing of the increases is to be determined on economic conditions as reflected by incoming data. Currently, the median forecast of Federal Reserve Board members and Federal Reserve Bank presidents for the years 2017, 2018, and 2019 are: the unemployment rate 4.5% for each year; PCE inflation sequentially 1.9%, 2.0% and 2.0%; real GDP 2.1%, 2.1%, and 1.9% respectively. Under these conditions, the federal funds rate would be 1.4% this year, 2.1% next year, and 3.0% in 2019.

INDICATORS OF ILLINOIS ECONOMIC ACTIVITY

INDICATORS *	February 2017	January 2017	February 2016
Unemployment Rate (Average)	5.4%	5.7%	6.1%
Annual Rate of Inflation (Chicago)	0.1%	-0.5%	2.2%

	LATEST MONTH	% CHANGE OVER PRIOR MONTH	% CHANGE OVER A YEAR AGO
Civilian Labor Force (thousands) (Feb)	6,528.4	0.1%	-0.5%
Employment (thousands) (Feb)	6,176.1	0.4%	-0.2%
NonFarm Payroll Employment (Feb)	6,055.0	25,600	47,000
New Car & Truck Registration (Feb)	40,716	-21.8%	1.3%
Single Family Housing Permits (Feb)	558	12.2%	0.0%
Total Exports ($ mil) (Jan)	5,111.5	0.18%	2.5%
Chicago Purchasing Managers Index (M)	57.7	0.7%	7.6%

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

REVENUE
March Posts Modest Gain on Mixed Results

Jim Muschinske, Revenue Manager

Overall base revenues grew $139 million in March. More than half of the gain was generated from an uptick in federal sources, while the remaining increase reflected mixed results from the economically-related sources. Strong individual tax receipts in large part were erased by significant falloffs in corporate income taxes and weak sales tax receipts. March had the same number of receipting days as the same period last year.

The IDOR has indicated that a significant amount of "in-transit" withholdings [approximately $200 million] slipped from February into March. As a result, gross personal income tax receipts increased $379 million or $327 million net of refunds and diversions to the Fund for Advancement of Education and Commitment to Human Services Fund. In addition, pass-through withholding is now accounted for in individual rather than corporate income taxes. Public utility receipts benefited from the timing of receipts and grew $25 million in March. Inheritance taxes were up $6 million, other sources grew $4 million, and interest income eked out a $1 million gain.

Gross corporate income taxes dropped precipitously for the month, falling $263 million, or $227 million net of refunds. A large reason for the drop was the aforementioned reclassification of pass-through withholding, which is now receipted under the personal income tax designation, but timing related to the IDOR's accounting system also contributed. After posting gains in Dec/Jan, sales tax is again underperforming and in March fell $58 million. Insurance taxes and fees were off by $11 million, cigarette taxes were down $6 million, and corporate franchise taxes dipped $2 million.

Overall transfers grew $1 million in March. Riverboat transfers gained $3 million and lottery transfers $1 million, but declines in other miscellaneous transfers offset most of those upticks, falling $3 million. While federal sources actually posted decent gains for the month, rising $79 million, the increase was due to an extremely weak month one year earlier rather than any meaningful strength. In fact, the outlook for federal sources continues to be bleak, constrained by the reimbursable spending pressure.

Year To Date

Through the first three-fourths of the fiscal year, base receipts are off $1.315 billion, or 5.9%. Weakness is widespread, and resulted in year-over-year losses in key areas such as income taxes and federal sources. As mentioned in earlier briefings, with renewed weakness in sales tax performance, and with only three months left in FY 2017, it will be very difficult to alter the trajectory of what has turned into a disappointing year for revenues.

To date, gross corporate income taxes are off $749 million, or $652 million net of refunds. With the boost in March receipts, gross personal income taxes are up by $5 million, however, on a net basis they are actually down $126 million. Inheritance tax receipts are off $52 million, while public utility taxes are behind last year's pace by $43 million. Cigarette taxes are down $9 million, while sales tax weakness has manifested in a $6 million decline through March.

Other sources leads those revenue areas which have posted gains thus far in the fiscal year as receipts are up $129 million, in large part to a one-time $84 million deposit of an SERS repayment. Interest income has grown $8 million, insurance taxes is ahead by $7 million, corporate franchise is up $4 million, and liquor taxes have managed to grow $3 million.

Overall transfers are down $89 million, while federal sources continue to struggle, falling $486 million behind last year's pace.

MARCH REVISION

The Commission met on March 7th to discuss updated FY 2017 revenue estimates as well as the FY 2018 forecast. In addition, the same information was presented to various Senate and House committees.

The table on page 8 presents the latest forecasts. The estimate of FY 2017 revenues has been revised down $674 million to $30.209 billion. The FY 2018 outlook calls for base growth of $938 million, and a forecast of $31.147 billion. For a detailed presentation of the forecasts, including comparisons to the GOMB forecasts as outlined in the Governor's proposed FY 2018 budget, please view the documents on the Commission's website.

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MARCH

FY 2017 vs. FY 2016

($ million)

Revenue Sources	**March FY 2017**	**March FY 2016**	**$ CHANGE**	**% CHANGE**
State Taxes				
Personal Income Tax	$1,635	$1,256	$379	30.2%
Corporate Income Tax (regular)	170	433	($263)	-60.7%
Sales Taxes	583	641	($58)	-9.0%
Public Utility Taxes (regular)	110	85	$25	29.4%
Cigarette Tax	24	30	($6)	-20.0%
Liquor Gallonage Taxes	12	12	$0	0.0%
Vehicle Use Tax	3	3	$0	0.0%
Inheritance Tax	23	17	$6	35.3%
Insurance Taxes and Fees	38	49	($11)	-22.4%
Corporate Franchise Tax & Fees	16	18	($2)	-11.1%
Interest on State Funds & Investments	4	3	$1	33.3%
Cook County IGT	0	0	$0	N/A
Other Sources	38	34	$4	11.8%
Subtotal	$2,656	$2,581	$75	2.9%
Transfers				
Lottery	71	70	$1	1.4%
Riverboat transfers & receipts	29	26	$3	11.5%
Proceeds from Sale of 10th license	10	10	$0	N/A
Refund Fund transfer	0	0	$0	N/A
Fund sweeps	0	0	$0	N/A
Other	32	35	($3)	-8.6%
Total State Sources	$2,798	$2,722	$76	2.8%
Federal Sources	$290	$211	$79	37.4%
Total Federal & State Sources	$3,088	$2,933	$155	5.3%
Nongeneral Funds Distribution:				
Refund Fund				
Personal Income Tax	($182)	($122)	($60)	49.2%
Corporate Income Tax	($30)	(66)	$36	-54.5%
Fund for Advancement of Education	($28)	(32)	$4	-12.5%
Commitment to Human Services Fund	($28)	(32)	$4	-12.5%
Subtotal General Funds	$2,820	$2,681	$139	5.2%
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	$2,820	$2,681	$139	5.2%

CGFA SOURCE: Office of the Comptroller: Some totals may not equal, due to rounding 4-Apr-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	$10,923	$10,918	$5	0.0%
Corporate Income Tax (regular)	787	1,536	($749)	-48.8%
Sales Taxes	6,010	6,016	($6)	-0.1%
Public Utility Taxes (regular)	666	709	($43)	-6.1%
Cigarette Tax	256	265	($9)	-3.4%
Liquor Gallonage Taxes	130	127	$3	2.4%
Vehicle Use Tax	22	25	($3)	-12.0%
Inheritance Tax	203	255	($52)	-20.4%
Insurance Taxes and Fees	256	249	$7	2.8%
Corporate Franchise Tax & Fees	162	158	$4	2.5%
Interest on State Funds & Investments	25	17	$8	47.1%
Cook County IGT	150	150	$0	0.0%
Other Sources	424	295	$129	43.7%
Subtotal	$20,014	$20,720	($706)	-3.4%
Transfers				
Lottery	511	487	$24	4.9%
Riverboat transfers & receipts	228	237	($9)	-3.8%
Proceeds from Sale of 10th license	10	10	$0	N/A
Refund Fund transfer	4	77	($73)	-94.8%
Fund sweeps	0	0	$0	N/A
Other	386	417	($31)	-7.4%
Total State Sources	$21,153	$21,948	($795)	-3.6%
Federal Sources	$1,666	$2,152	($486)	-22.6%
Total Federal & State Sources	$22,819	$24,100	($1,281)	-5.3%
Nongeneral Funds Distribution:				
Refund Fund				
Personal Income Tax	($1,223)	($1,064)	($159)	14.9%
Corporate Income Tax	($136)	($233)	$97	-41.6%
Fund for Advancement of Education	($321)	($335)	$14	N/A
Commitment to Human Services Fund	($321)	($335)	$14	N/A
Subtotal General Funds	$20,818	$22,133	($1,315)	-5.9%
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	$20,818	$22,258	($1,440)	-6.5%

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

CGFA 4-Apr-17

FY 2018 and Revised FY 2017 Estimates
CGFA
(millions)

Revenue Sources	FY 2018 CGFA Mar-17	FY 2017 CGFA Mar-17	$ Difference
State Taxes			
Personal Income Tax	$15,688	$15,300	$388
Corporate Income Tax (regular)	$1,900	$1,750	$150
Sales Taxes	$8,380	$8,215	$165
Public Utility (regular)	$898	$883	$15
Cigarette Tax	$353	$353	$0
Liquor Gallonage Taxes	$173	$171	$2
Vehicle Use Tax	$30	$30	$0
Inheritance Tax	$280	$285	($5)
Insurance Taxes & Fees	$410	$405	$5
Corporate Franchise Tax & Fees	$203	$205	($2)
Interest on State Funds & Investments	$32	$28	$4
Cook County Intergovernmental Transfer	$244	$244	$0
Other Sources	$599	$647	($48)
Subtotal	**$29,190**	**$28,516**	**$674**
Transfers			
Lottery	$719	$719	$0
Riverboat transfers and receipts	$262	$265	($3)
Proceeds from sale of 10th license	$10	$10	$0
Interfund Borrowing	$0	$0	$0
Other	$699	$621	$78
Total State Sources	**$30,880**	**$30,131**	**$749**
Federal Sources	**$3,111**	**$3,000**	**$111**
Total Federal & State Sources	**$33,991**	**$33,131**	**$860**
Nongeneral Funds Distribution:			
Refund Fund			
Personal Income Tax [11.2% '17; 10% '18]	($1,569)	($1,714)	$145
Corporate Income Tax [17.25% '17; 17.5% '18]	($333)	($302)	($31)
Fund for Advancement of Education	($471)	($453)	($18)
Commitment to Human Services Fund	($471)	($453)	($18)
Subtotal General Funds	**$31,147**	**$30,209**	**$938**
Including Key GOMB Assumptions in Budget Book			
Proceeds from sale of Thompson Center	**$300**	**$0**	**$300**
Includes FAE/CHSF in Gen Funds Definition	**$942**	**$906**	**$36**
Total GOMB Assumptions	**$1,242**	**$906**	**$336**
Total General Funds	**$32,389**	**$31,115**	**$1,274**

State Employees Group Insurance Program Status Update
Anthony Bolton, Revenue Analyst

Over the past fiscal year, the lack of an enacted budget has resulted in the State Employee Group Insurance Program (SEGIP) building up a large backlog of unpaid claims. As of the end of March, approximately $4.36 billion in SEGIP claims were being held by the state from various insurers, organizations, and companies. Of this total, the largest portion was approximately $2.2 billion of HMO/Medicare Advantage claims. The second largest portion, Open Access Plans, totaled $839 million. The third largest portion of the overall claims hold came from CIGNA, which had $658 million in claims currently held by the state. Concurrently, the estimated time for claims to be held was 309-675 days for Managed Care/Medicare Advantage, 499-555 days for Open Access Plans, and 630-707 days for CIGNA. This information and other pertinent data is displayed on the chart on the next page. Without additional funding, claims will continue to build up and estimated claims hold times will increase due to no appropriation for Group Insurance.

As a result of the State Employees Group Insurance Program (SEGIP) building up a large backlog of unpaid claims from health care vendors, alternative options for payment have been explored. One option that has arisen in recent years is a program called the Vendor Payment Program (VPP), which is organized through the Department of Central Management Services (CMS).

Under the VPP, vendors for the state of Illinois who would otherwise receive prompt payment interest would instead partner with a "qualified purchaser" who would purchase the voucher from them. The vendor would receive approximately 90% of the total invoice owed to them with the other 10% paid to them once the qualified purchaser is paid by the state. The qualified purchaser would keep any interest paid out by the state on the voucher. However, the State has not been able to pay out vouchers without appropriation, so CMS has switched to the Vendor Support Initiative program (VSI), which is procedurally similar to the Vendor Payment Program, but does not require a voucher to receive payment.

At the Commission's State Employee Group Insurance Hearing on April 4, 2017, CMS presented a new plan for FY 2018 to change the Group Insurance Program by expanding existing plans into four "metal" tiers: Platinum, Gold, Silver, and Bronze. These tiers would be used by existing HMOs, OAPs, and the Quality Care Health Plan. The "metal" tiers would range from having the same copayments / deductibles / etc. but (on average) 120% higher premiums for the Platinum plan compared to the same premiums but higher copayments / deductibles / etc. for the Silver plan. The Bronze plan would have no premiums, but have much higher copayments / deductibles / etc. As a result of these plan changes and increased premiums, CMS anticipated that the State would save approximately $520 million.

This plan has been challenged by state employee unions in state court and is currently blocked from being imposed by the State as of the date of this publication. As a result CMS has indicated that they would keep the existing plan designs and employee contributions until otherwise instructed by the courts. As this case is currently in the Appellate Court and likely to be taken to the Illinois Supreme Court eventually, it is uncertain whether CMS will be able to implement the aforementioned plan changes in the 2018 fiscal year.

Claims Hold Data for SEGIP (as of March 31, 2017)			
Company	**Claims Hold**	**Length of Claims Hold (in days)**	**Interest Owed (Including Past Due Interest)**
CIGNA - PPO (and Member)	$621,384,476	630	$46,825,229
CIGNA - Non-PPO	$36,224,689	707	$3,079,099
Dental Claims Hold – PPO	$90,384,331	450	$7,615,191
Dental - Non-PPO	$45,448,873	618	$5,436,384
Magellan (Mental Health) Claims	$4,928,109	240	$131,318
Aetna HMO	$68,252,724	309	$4,819,998
Health Alliance HMO	$1,089,312,805	734	$106,589,045
HMO Illinois	$610,979,951	675	$54,116,391
Blue Advantage	$101,084,918	675	$7,673,150
HealthLink OAP	$697,643,767	555	$46,091,467
Coventry OAP	$141,440,349	499	$8,320,308
Medco	$46,994,345	378	$46,492,453
CVS/Caremark	$377,445,266	546	$25,064,633
Aetna Medicare Advantage (MA)	$13,782,381	553	$1,076,796
Health Alliance MA	$2,732,382	614	$203,297
Humana Benefit Plan MA	$441,959	584	$48,113
Humana Health Plan MA	$8,877,868	584	$936,303
United Healthcare MA	$301,681,201	362	$33,017,650
Fidelity (Vision)	$11,607,926	369	$763,376
Minnesota Life	$37,054,376	89	$85,290
Other Fees (ASC/etc.)	$54,954,061	431-492	$6,256,894
Total	**$4,362,656,756**	**275-734**	**$404,642,386**

The current interest owed on these claims is also noted in the above chart. The interest on held claims is reflective of the 9 to 12 percent interest rates mentioned in previous monthly reports and is not included in the total claims hold figure of $4.36 billion.