Commission on Government Forecasting and Accountability

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MONTHLY BRIEFING FOR THE MONTH ENDED: SEPTEMBER 2015

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Wagering In Illinois: FY 2015 Update

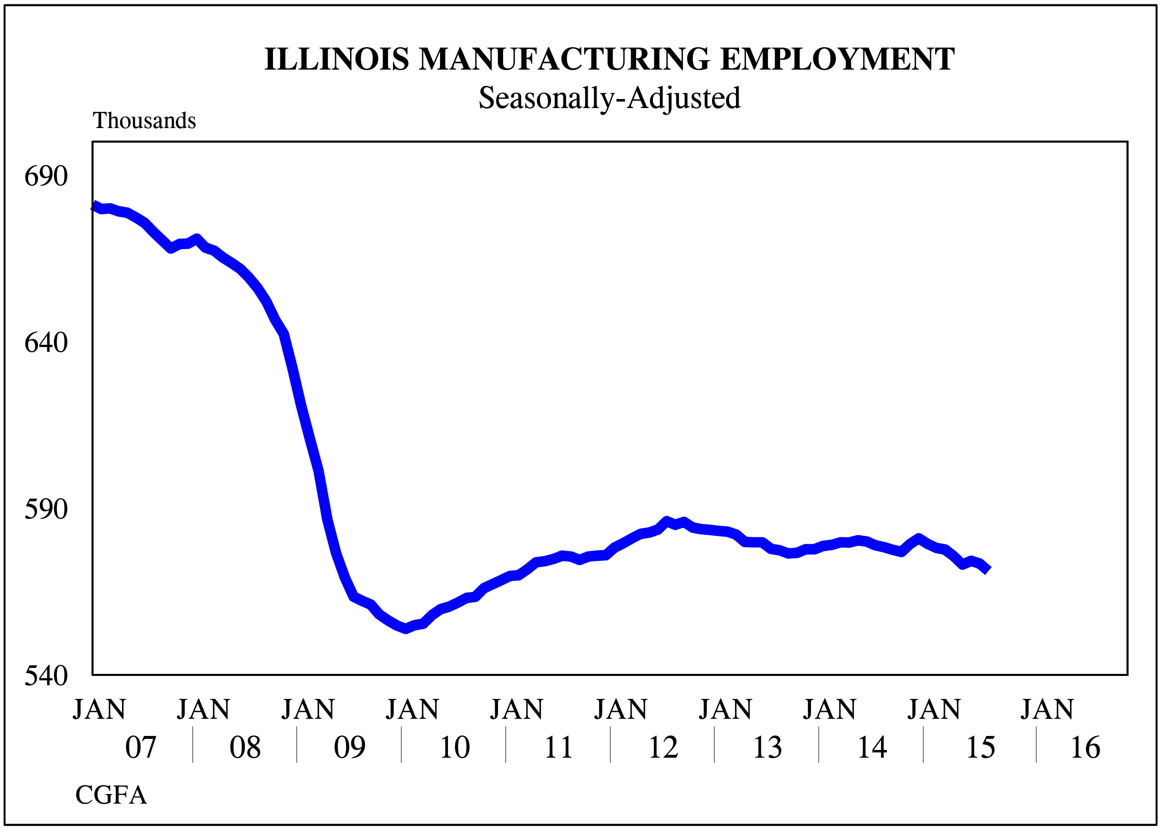
ECONOMY: Role of Manufacturing

Edward H. Boss, Jr., Chief Economist

In the first decade of the 2000's the manufacturing sector, and therefore manufacturing jobs, continued to decline as the U.S. saw it replaced by an increased share of the jobs centered in the service sector. By the start of 2005, manufacturing employment already had fallen to 14,257,000, from a level of 17,824,000 in January 2000. At the beginning of 2010 manufacturing jobs fell further, reaching a level of 11,460,000. By the start of 2015, however, the decline had been stemmed and manufacturing jobs rose to 12,318,000, an increase of 7%. By August of this year, manufacturing employment showed modest gains with preliminary data showing the level of manufacturing jobs at 12,329,000.

The loss of high-paying manufacturing jobs at the expense of generally lower-wage service jobs, not only has been a major factor behind stagnant wages overall, but also widens the disparity between income classes, particularly affecting the middle class. Stagnant wages also depress city and state tax receipts, many of which are in need of revenues to restore underfunded pension systems, handle heavy borrowing, and rescue social services from the slow pace of economic growth following the last recession.

Not only is this the slowest recovery in the post WWII era, but there appears to be little acceleration in its growth now into its 7th year. The latest data on GDP real growth for the second quarter was revised upward to show an annual increase of 3.9%, up from a rate of 3.7%. However, when combined with the modest 0.6% in the first quarter growth was at a 2.25% rate of during the first half of the year with expectations that the third quarter growth will slow. This compares to last year when real GDP rose at a 2.6% annual rate in first half of the year with rates of growth at 0.8% and 4.4%, respectively during the first two quarters.



By the beginning of this year it was clear that the continuous loss of manufacturing jobs was ending and beginning to rise. There was much hope of a brewing resurgence in the so-called rust belt centered in the Midwest. Even so, the improvement was not equally shared among the Midwestern states. As shown in the Chart, Illinois manufacturing jobs rose slightly less than 6% from the beginning of 2010 to the beginning of 2015, compared to 7% in the U.S. Moreover, while several Midwestern states were showing respectable manufacturing job growth, in the 12 months ended August 2015, Illinois manufacturing jobs increased by a modest 41,200, a gain of only seven tenths of 1% and has held virtually unchanged since May.

The turnaround in manufacturing jobs can be explained in part by the sharp drop in energy prices from increased oil and gas production in the U.S. through new discoveries and drilling techniques. The result was an increase in U.S. competitiveness although partially offset by a strengthening dollar. Ultimately, however, it will take rising demand from improved world economic growth to increase manufacturing jobs. This does not seem likely anytime soon. The economic slowdown in China has reduced its demand while parts of Europe have slowed. At the same time, the economies of Russia, Venezuela, Brazil, and other large oil producers have been sharply affected by the steep decline in energy prices. Indeed, according to press reports, Illinois' Caterpillar has seen its demand reduced for engines and equipment used on oil rigs, and mining, as well as construction equipment. As a result it announced it would lay off 10,000 or more workers with a significant number of those in Illinois while announcing it was still planning for a new headquarters in Peoria, although it has been put on hold, at least temporarily. Thus Caterpillar joins the likes of Mondelez (makers of snack foods and Oreo cookies), Walgreens, and Kraft with roots in Illinois having recently announced large layoffs.

The recent softening in manufacturing is reflected in the Institute for Supply Management's (ISM) Manufacture's Index which stood at 51.1 in August, down from 58.1 a year earlier. (Any number above 50.0 represents expansion while below that represents contraction.) The ISM September Manufacturer's Index for the Chicago area just became available and shows the index fell to 48.7, compared to 54.4 in August and the lowest since May.

The effect of recent developments in the manufacturing sector on jobs was depicted in the latest ADP National Employment Report. The Private sector employment was shown to have increased by 200,000 jobs in September, in line with those of recent months. The only sector to decline was manufacturing, which fell by 15,000 jobs but was more than made up for 35,000 new construction jobs, 39,000 in Trade/transportation /utilities, 15,000 in Financial activities, and 29,000 new jobs in Professional/business services. Thus, it appears the overall employment gains of recent months appear on track.

INDICATORS OF ILLINOIS ECONOMIC ACTIVITY

INDICATORS *	AUG. 2015	JULY 2015	AUG. 2014
Unemployment Rate (Average)	5.6%	5.8%	6.5%
Annual Rate of Inflation (Chicago)	4.9%	-1.3%	-0.1%

	LATEST MONTH	% CHANGE OVER PRIOR MONTH	% CHANGE OVER A YEAR AGO
Civilian Labor Force (thousands) (August)	6,492.8	0.0%	-0.2%
Employment (thousands) (August)	6,130.3	0.2%	0.7%
NonFarm Payroll Employment (August)	5,920,400	-900	41,200
New Car & Truck Registration (August)	56,394	-4.1%	2.1%
Single Family Housing Permits (August)	1,048	-5.5%	8.0%
Total Exports ($ mil) (July)	5,068	-6.0%	-7.8%
Chicago Purchasing Managers Index (Sept.)	48.7	-10.5%	-19.5%

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

REVENUE
Receipts Continue To Reflect Lower Income Tax Rates
Jim Muschinske, Revenue Manager

Overall base revenues fell $382 million in September. Comparatively lower income tax rates, related income tax diversions to the education and human service related funds account for the decline. The month had the same number of receipting days as last fiscal year.

Due to the lower income tax rates effective January 2015, gross personal income tax receipts fell $286 million, or $254 million net of refunds. An additional $30 million was directed from the general funds to both the Fund for Advancement of Education as well the Commitment to Human Services Fund. As result, net personal income tax receipts were comparatively lower by $314 million. Gross corporate income tax also fell due to reduced rates, with gross receipts off $134 million, or $119 net of refunds.

A number of sources suffered declines in September. Insurance taxes were down $7 million, public utility taxes $4 million, interest income $2 million, and liquor taxes $1 million.

A few sources did manage to record gains for the month. Inheritance taxes fared quite well, growing $12 million, sales tax generated a modest $6 million gain, corporate franchise grew $5 million, and both cigarette tax and vehicle use tax each managed to post a $1 million increase.

Overall transfers fell $2 million in September. For the month, riverboat transfers dropped $20 million and lottery transfers fell $1 million. Other transfers offset much of those declines, however, as receipts grew $19 million. While federal sources managed to post a $41 million gain for the month, the increase was more a function of an extremely poor month last year than actual positive performance this September.

Year To Date

Through the first quarter of the fiscal year, base receipts are down $987 million. The drop reflects comparatively lower income tax rates as well as the one-time nature of some pharmaceutical court settlements recovered by the Attorney General's Office last fiscal year.

Gross personal income taxes are down $699 million, $621 million net of refunds, or $829 million when the diversions to the education and human service funds are included. Gross corporate income taxes are behind last year's receipting by $154 million, or $138 million net of refunds. Other sources are down $117 million, reflecting the aforementioned court settlement proceeds received last fiscal year in a similar amount. Public utility taxes are off $25 million, inheritance tax by $7 million, and interest income by $3 million.

A small number of sources posted gains for the first quarter as sales tax receipts are up $18 million, corporate franchise taxes $6 million, and vehicle use tax $1 million.

Overall transfers are up by $57 million, and federal sources, despite its weakness, are up $50 million for the quarter.

GENERAL FUNDS RECEIPTS: SEPTEMBER
FY 2016 vs. FY 2015
($ million)

Revenue Sources	Sept. FY 2016	Sept. FY 2015	$ CHANGE	% CHANGE
State Taxes				
Personal Income Tax	$1,393	$1,679	($286)	-17.0%
Corporate Income Tax (regular)	392	526	($134)	-25.5%
Sales Taxes	686	680	$6	0.9%
Public Utility Taxes (regular)	79	83	($4)	-4.8%
Cigarette Tax	30	29	$1	3.4%
Liquor Gallonage Taxes	13	14	($1)	-7.1%
Vehicle Use Tax	4	3	$1	33.3%
Inheritance Tax	31	19	$12	63.2%
Insurance Taxes and Fees	61	68	($7)	-10.3%
Corporate Franchise Tax & Fees	28	23	$5	21.7%
Interest on State Funds & Investments	1	3	($2)	-66.7%
Cook County IGT	0	0	$0	N/A
Other Sources	32	31	$1	3.2%
Subtotal	$2,750	$3,158	($408)	-12.9%
Transfers				
Lottery	56	57	($1)	-1.8%
Riverboat transfers & receipts	23	43	($20)	-46.5%
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	53	34	$19	55.9%
Total State Sources	$2,882	$3,292	($410)	-12.5%
Federal Sources	$161	$120	$41	34.2%
Total Federal & State Sources	$3,043	$3,412	($369)	-10.8%
Nongeneral Funds Distribution:				
Refund Fund				
Personal Income Tax	($135)	($167)	$32	-19.2%
Corporate Income Tax	($59)	(74)	$15	-20.3%
Fund for Advancement of Education	($30)	0	($30)	N/A
Commitment to Human Services Fund	($30)	0	($30)	N/A
Subtotal General Funds	$2,789	$3,171	($382)	-12.0%
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	$2,789	$3,171	($382)	-12.0%

CGFA SOURCE: Office of the Comptroller: Some totals may not equal, due to rounding 1-Oct-15

GENERAL FUNDS RECEIPTS: YEAR TO DATE
FY 2016 vs. FY 2015
($ million)

Revenue Sources	FY 2016	FY 2015	CHANGE FROM FY 2015	% CHANGE
State Taxes				
Personal Income Tax	$3,390	$4,089	($699)	-17.1%
Corporate Income Tax (regular)	502	656	($154)	-23.5%
Sales Taxes	2,052	2,034	$18	0.9%
Public Utility Taxes (regular)	211	236	($25)	-10.6%
Cigarette Tax	88	88	$0	0.0%
Liquor Gallonage Taxes	44	44	$0	0.0%
Vehicle Use Tax	10	9	$1	11.1%
Inheritance Tax	77	84	($7)	-8.3%
Insurance Taxes and Fees	92	92	$0	0.0%
Corporate Franchise Tax & Fees	58	52	$6	11.5%
Interest on State Funds & Investments	4	7	($3)	-42.9%
Cook County IGT	0	0	$0	N/A
Other Sources	109	226	($117)	-51.8%
Subtotal	$6,637	$7,617	($980)	-12.9%
Transfers				
Lottery	136	145	($9)	-6.2%
Riverboat transfers & receipts	80	86	($6)	-7.0%
Proceeds from Sale of 10th license	0	0	$0	N/A
Refund Fund transfer	77	63	$14	22.2%
Fund sweeps	0	0	$0	N/A
Other	203	145	$58	40.0%
Total State Sources	$7,133	$8,056	($923)	-11.5%
Federal Sources	$553	$503	$50	9.9%
Total Federal & State Sources	$7,686	$8,559	($873)	-10.2%
Nongeneral Funds Distribution:				
Refund Fund				
Personal Income Tax	($330)	($408)	$78	-19.1%
Corporate Income Tax	($76)	($92)	$16	-17.4%
Fund for Advancement of Education	($104)	$0	($104)	N/A
Commitment to Human Services Fund	($104)	$0	($104)	N/A
Subtotal General Funds	$7,072	$8,059	($987)	-12.2%
Short-Term Borrowing	$0	$0	$0	N/A
Interfund Borrowing	$0	$0	$0	N/A
Budget Stabilization Fund Transfer	$125	$275	($150)	-54.5%
Total General Funds	$7,197	$8,334	($1,137)	-13.6%

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

CGFA 1-Oct-15

PENSIONS
Summary of the TRS 2015 Experience Study
Jerry Lazzara, Pension Analyst

Public Act 99-0232 requires that the Teacher's Retirement System (TRS) perform a triennial Investigation of Demographic and Economic Experience. On August 13, 2015, TRS published their investigation that covers the three-year period from July 1, 2011 to June 30, 2014. The results of this investigation are to be used in preparation of the June 30, 2015 through June 30, 2017 actuarial valuations, which will determine the funding requirements for fiscal years 2017 through 2019. After the investigation, TRS recommends that several changes be made in future actuarial assumptions, and these recommendations can be seen in the table below:

Assumption	Observed Experience Relative to Expectations	Recommendation	Impact on Costs
Termination from Active Employment	More Terminations	Increase Rates	Decrease
Disability Retirement	Fewer Disabilities	Decrease Rates	Decrease
Regular Service Retirement	More Retirements	Increase Rates	Increase
Mortality	Fewer Deaths	Decrease Rates	Increase
Utilization of Early Retirement Option (ERO)	Lower Utilization	Decrease Rates	Decrease
Optional Service and Sick Leave Service	Lower Utilization	Decrease Rates	Decrease
Salary and Severance	Lower Increases	Decrease Rates	Decrease
Tier 2 COLA and Paycap	Lower Increases	Decrease Rates	Decrease
Investment Return	N/A	Keep the Same	N/A

Summary of Recommended Changes

Termination – The assumed rates of termination from employment should be adjusted to more closely reflect the pattern of terminations by age, and to bring the combined male/female ratio of actual to expected terminations to 100% overall.

Disability Retirement – The assumed rates of disability should be reduced so that the ratios of actual to expected are increased to approximately 100% to more closely reflect recent experience.

Regular Service Retirement – The assumed rates of regular service retirement should be adjusted to better fit the actual age-and-service-related patterns observed during the experience period.

Mortality – The assumed mortality rates should be changed to reflect actual recent experience for TRS members. The proposed mortality rates are based on the RP-2014 mortality tables. TRS reflects more mortality improvements in the future which will result in a higher fiscal impact.

ERO – ERO is currently scheduled to sunset on July 1, 2016, however the investigation was performed under the assumption that it was permanent. The rates of utilization of ERO should be set to actual rates experienced during the period of the study.

Optional Service and Sick Leave Service – The pension benefit obligation for retirement benefits for active members who have not previously purchased optional service – and whose pension benefit would be improved by such a purchase – should continue to be increased to cover the employer cost of optional service purchased in the last two years prior to retirement.

Salary and Severance Pay – The age-based salary increase assumption should be replaced with a service-based assumption. The Full Time/Part Time average used to cover employment type and status changes should be combined with the rest of the assumption. The components of the salary increase assumption will maintain the 3% inflation; 0.75% real wage growth; and reduce merit/longevity increases by roughly 1% across the board. The percent of retirees from active service assumed to receive severance payments, and the amount of such severance payments, should be based on the assumption of 20% of retirees will receive severance pay and the average severance payment will be 3% of other pensionable earning in the last year of employment.

Investment Return – TRS recommends that the Board retain the current 7.5% investment return, which equates to a real return of 4.5% and inflation of 3%

The table below depicts the estimated fiscal impact of proposed revisions in actuarial assumptions. The total projected change in Actuarial Accrued Liability is a $502.9 million increase.

Change in Actuarial Accrued Liability as of June 30, 2014 ($ Millions)			
Actuarial Assumption Revision	Actuarial Accrued Liability		
	Amount	Change	Cumulative Change
June 30, 2014 Valuation	103,740.4	0.0	0.0
Termination From Active Employment	103,700.5	-39.9	-39.9
Disability Retirement	103,676.6	-23.9	-63.8
Regular Service Retirement	103,715.1	38.5	-25.3
Mortality	106,547.7	2,832.6	2,807.3
Utilization of ERO	106,476.8	-70.9	2,736.4
Optional Service and Sick Leave Service	106,264.0	-212.8	2,523.6
Salary and Severance	104,243.3	-2,020.7	502.9

The table below depicts the estimated change in total normal cost. The total projected change in normal cost is a 1.18% decrease.

Change in Total Normal Cost (Shown as a % of Covered Payroll)			
Actuarial Assumption Revision	Normal Cost		
	Amount	Change	Cumulative Change
Fiscal Year 2016	19.69%		
Termination From Active Employment	19.64%	-0.05%	-0.05%
Disability Retirement	19.61%	-0.03%	-0.08%
Regular Service Retirement	19.63%	0.02%	-0.06%
Mortality	20.05%	0.42%	0.36%
Utilization of ERO	20.01%	-0.04%	0.32%
Optional Service and Sick Leave Service	19.88%	-0.13%	0.19%
Salary and Severance	18.51%	-1.37%	-1.18%