THE CONNECTICUT
ECONOMIC DIGEST

Vol.16 No.1 A joint publication of the Connecticut Department of Labor & the Connecticut Department of Economic and Community Development

JANUARY 2011

IN THIS ISSUE...

In November...

Nonfarm Employment
Connecticut 1,618,700
Change over month .... +0.15%
Change over year .... +0.5%

United States 130,539,000
Change over month .... +0.03%
Change over year .... +0.6%

Unemployment Rate
Connecticut 9.0%
United States 9.8%

Consumer Price Index
United States 218.8
Change over year 1.2%

The Connecticut Economic Outlook for 2011

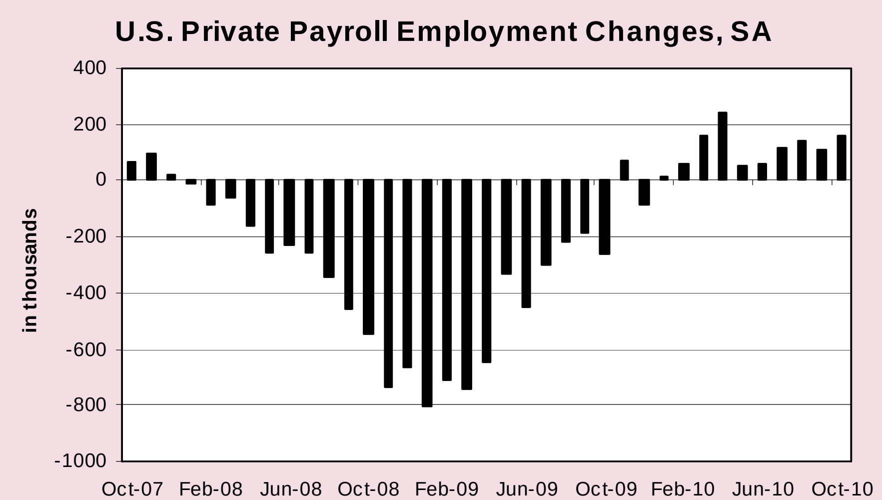
By Stan McMillen, Ph.D., Managing Economist (Stan.McMillen@ct.gov), and Mark Prisloe, Associate Economist (Mark.Prisloe@ct.gov), DECD

The Nation

We expect the modest expansion of the U.S. economy that began in the third quarter of 2009[1] will continue in 2011. The outlook for continued recovery from the longest recession since the 1930s that began in December 2007 and lasted 18 months is tempered by harsh realities - notably, unacceptably high unemployment and a weak housing market. Yet, private sector employment increased in each month last year, totaling 1.1 million jobs through October 2010.[2] Seasonally adjusted U.S. payroll employment changes appear in the figure below. Privately-owned housing starts in September were at a seasonally adjusted annual rate of 610,000 or 4.1% above the September 2009 rate of 586,000.[3] U.S. Gross Domestic Product (GDP) grew at an average rate of 2.8% each quarter since the Q3-2009 expansion began.

Forecasts of real (inflation-adjusted) GDP growth in the first six months of 2011 range from 1.4% to 1.6%, with an 80% chance the growth rate will be between 2.3% and 3.1%, according to the Financial Forecast Center (FFC).[4] The FFC forecast proved accurate in that U.S. real GDP growth in the first three quarter-over-quarter periods last year averaged 2.5%, exactly at the upper range of their forecast of 2.5% for 2010. For 2011, the National Association of Business Economists (NABE) forecasts GDP growth of 2.6%[5] while Moody's Economy.com foresees a 2.5% to 3.0% gain[6] and the New England Economic Partnership (NEEP) projects real GDP to grow 3.1%.[7]

There are encouraging signs for 2011. The Conference Board Leading Economic Index™ (LEI) for the U.S., except for slight declines in April and June 2010, exhibited



Source: Bureau of Labor Statistics

THE CONNECTICUT ECONOMIC DIGEST

The Connecticut Economic Digest is published monthly by the Connecticut Department of Labor, Office of Research, and the Connecticut Department of Economic and Community Development. Its purpose is to regularly provide users with a comprehensive source for the most current, up-to-date data available on the workforce and economy of the state, within perspectives of the region and nation.

The annual subscription is $50. Send subscription requests to: ***The Connecticut Economic Digest***, Connecticut Department of Labor, Office of Research, 200 Folly Brook Boulevard, Wethersfield, CT 06109-1114. Make checks payable to the Connecticut Department of Labor. Back issues are $4 per copy. The Digest can be accessed free of charge from the DOL Web site. Articles from ***The Connecticut Economic Digest*** may be reprinted if the source is credited. Please send copies of the reprinted material to the Managing Editor. The views expressed by the authors are theirs alone and may not reflect those of the DOL or DECD.

Managing Editor: Jungmin Charles Joo

Associate Editor: Sarah C. York

We would like to acknowledge the contributions of many DOL Research and DECD staff and Rob Damroth (CCT) to the publication of the Digest.

Connecticut Department of Labor
Linda L. Agnew, Acting Commissioner

Andrew Condon, Ph.D., Director
Office of Research
200 Folly Brook Boulevard
Wethersfield, CT 06109-1114
Phone: (860) 263-6275
Fax: (860) 263-6263
E-Mail: dol.econdigest@ct.gov
Website: http://www.ctdol.state.ct.us/lmi

Connecticut Department of Economic and Community Development
Joan McDonald, Commissioner
Ronald Angelo, Deputy Commissioner

Stan McMillen, Ph.D., Managing Economist
505 Hudson Street
Hartford, CT 06106-2502
Phone: (860) 270-8000
Fax: (860) 270-8200
E-Mail: decd@ct.gov
Website: http://www.decd.org

steady increases, offering "no indication of a relapse into another downturn through the end of the year [2010]."[8] Ken Goldstein, economist at The Conference Board said: "The economy is slow, but the latest data on the U.S. LEI suggest that change may be around the corner."[9] Moreover, Ataman Ozyildirim of the Conference Board said, "The LEI remains on an upward trend, suggesting the modest economic expansion will continue in the near term."[10]

Growth prospects are positive, for example, in that U.S. automakers, after restructuring, are profitable for the first time in six years.[11] September 2010 auto sales were up 19% from September 2009 and retail sales in general increased 7.3% in September 2010 from September 2009.[12] The National Association of Realtors expects home prices to rise in 2011.[13] The Federal Open Market Committee (FOMC) is buying treasuries to maintain low interest rates while inflation is nonexistent. Business spending on plant and equipment, Gross Private Domestic Investment (GPDI), as predicted last year, is up sharply on a quarterly basis from the preceding quarter by an average of 21.3% since Q3-2009.[14] Tax cuts, if enacted and/or extended will help stimulate personal consumption expenditures. The "National Export Initiative" to double U.S. exports in five years noted an increase in the first half of 2010 of 18% above export levels in the first half of 2009.[15]

Connecticut

Connecticut's economy should experience modest growth in 2011. Connecticut's real state gross domestic product (SGDP), the broadest measure of the state's economic health, declined 3.1% in 2009[16] and when reported for 2010 may be small and positive. According to NEEP, Connecticut may see real SGDP growth in 2011 in the range of 3.5% while personal income that dropped 2.8% in 2009, not adjusted for inflation, is expected to improve by 2.5% in 2011 relative to 2010. NEEP forecasts Connecticut will gain about 6,000 jobs or 0.4% in 2011.[17]

The state's unemployment rate will remain steady in 2011 at approximately 9.1% (footnote 7). Connecticut's unemployment rate has remained consistently below the national rate, notwithstanding that since March 2008 Connecticut nonfarm employment declined by 103,400 (-6.0%). Initial claims for unemployment insurance peaked at 32,415 in March 2009, but have since declined to 23,963 (-26.0%) in September 2010. Through September there were job gains in six of nine months ranging from 500 (April) to 6,600 (May) in 2010.

Among significant challenges facing Connecticut and most other states in 2011 are severe state budget deficits. State budget cuts for the 2011 fiscal year (which began on July 1, 2010 in most states) have already been steeper than those over the past two fiscal years. For example, Connecticut made changes to its Medicaid program on June 1, 2010, affecting pregnant women, parents, caretaker relatives and disabled and elderly adults who lost coverage for over-the-counter medications and nutritional supplements (with certain exceptions).[18] State education grants to school districts and educational programs have been reduced. Mandatory furloughs for certain state workers and state agency budget cuts have been imposed. There have been budget cuts to programs that help prevent child abuse and provide legal services for foster children (see note 18).

The Connecticut legislature's Office of Fiscal Analysis (OFA) projects deficits exceeding $10 billion in Fiscal Years (FY) 2011 through FY 2014, as shown in the table below.

The projected deficit based on "consensus revenues" in FY 2012 is $3.7 billion.[19] The adjustment to the deficit will include spending cuts, tax increases or a combination of these measures because reserves, borrowing and federal stimulus

($ - millions)	FY 11	FY 12	FY 13	FY 14
Est. Expenditures	$18,017.80	$20,065.90	$20,741.40	$21,539.60
Est. Revenue	17,934.80	16,392.60	17,254.80	18,221.80
Est. (Deficit)/Surplus	**($83.00)**	**($3,673.30)**	**($3,486.60)**	**($3,317.80)**
% of Est. Expenditures	0.50%	18.30%	16.80%	15.40%

funds will not be available options. The state's response to this crisis will have an economic impact as well on state residents' disposable income and their willingness to make purchases that may further erode income and sales taxes. Unexpected economic growth may reduce the impacts, but the seriousness of the fiscal crisis cannot be overstated.

The 2011 outlook for Connecticut's personal income is improved over last year. As forecasted by the Connecticut Department of Labor, personal income for Q1-2011 will increase by 1.7% from Q1-2010.[20] NEEP projects personal income to increase by 2.5% in 2011. By comparison, U.S. personal income rose on average 0.2% from the preceding month in calendar year 2010 through September. Growth in personal income, wealth (e.g., home and financial portfolio values) and expectations strongly influence consumption and consequently sales taxes that represent almost 27% of the state's domestic revenue.[21]

We expect Connecticut's housing market prospects to improve in 2011. On a year-to-date basis new permit authorizations through September in 2010 increased 18.2% compared to the same period in 2009 when permits declined 40.2%. Connecticut housing prices were among the top five states for appreciation, rising 2.5% in Q3-2010. Both trends bode well for the coming year.[22] New housing permits peaked at 12,269 in Q3-2005 and NEEP expects them to rise from a projected 3,986 in 2010 to 4,571 in 2011. According to NEEP, existing Connecticut single family median home prices dropped in Q3-2010 from their Q2-2007 peak of $326,800 to $260,300 and may drop to a low of $237,300 in Q3-2011. However, existing home sales should show a gain from 40,000 in 2010 to 49,000 in 2011. Meanwhile, NEEP expects the median sale price for an existing home to fall to $239,000 for 2011(see note 7, p. 11).

NEEP projects Connecticut total employment to increase by 6,000 in 2011 (0.4%). Goods producing sector employment, which declined by 26,100 (-10.3%) in 2009 and by 7,700 (-3.4%) in 2010, will decrease by 2,300 (-1.1%) in 2011. Manufacturing employment in Connecticut, which declined by 15,500 (-0.3%) in 2009 and by 3,600 (-2.1%) in 2010, will increase by 1,200 (+0.07%) in 2011. Manufacturing is a component of the goods producing sector. Private service providing employment, which shrank by 41,300 (-3.5%) in 2009 and increased by 500 (0.04%) in 2010, is expected to increase by 10,600 (0.9%) in 2011. NEEP projects total government employment (federal, state, and local) in Connecticut to decrease by 2,200 (-0.9%) in 2011.

We conclude that 2011 will likely be a better year than 2010 for employment, SGDP, investment in plant and equipment, personal income, housing, consumer confidence and retail sales, while inflation should remain insignificant. However, significant downside risks are the national and state budget deficits. As the U.S., Connecticut and other states struggle to achieve fiscal sustainability, there are likely to be programmatic cuts, reductions in the public sector workforce and tax structure changes that will play out over several years. These may be disruptive with substantial negative impacts on an otherwise cautiously optimistic forecast.

According to NEEP, "…looming federal and state fiscal crises make a difficult road to recovery in the region even more difficult, both short- and long-term."[23] NEEP projects the direct impact in the government sector could result in a more than 2% decline in employment from now until mid-2011, representing a loss of more than 21,000 jobs in the six state region. Connecticut's loss of more than 100,000 jobs to date would be compounded by additional job cuts in the public sector. Balanced budget measures, such as tax increases and expenditure reductions, will ripple through the regional economy with "multiplier" effects that will further restrain business and consumer confidence and their spending with commensurate reductions in personal income and sales tax revenues. The downside risks for rapid recovery are formidable.

As we mentioned last year, demographic and structural changes will shape the pace and form of the recovery. These include the continued decline of manufacturing and construction as a share of the state's employment and the increasing dependency ratio as workers leave the workforce for retirement. The latter biological trend may be exacerbated by the current, long-term unemployment of workers over the age of 50 who find it increasingly difficult to find suitably equivalent employment to what they lost. They will begin collecting Social Security sooner than we expected. As Connecticut's aging population retires, it will spend less as it receives lower total compensation and it will have increased demands for smaller and more affordable and efficient housing. And some retirees will leave the state. This portends lower state tax revenue and shifting housing demands.

Structural changes include the changing nature of work: companies discovered in this recession that they could achieve more with less and they did. They became profitable and invested in additional plant and equipment. They found they could dismiss payroll employees and hire them as contract labor, reducing their costs and increasing their flexibility. Companies have discovered they do not need their entire workforce in the same location at the same time, thus, the changing nature of work portends lower corporate footprints in urban areas, and increased telecommuting that will lower costs and increase worker satisfaction.

Connecticut and the nation's recovery are affected by large uncertainties that were distant visions a year ago. The fiscal and economic effects of financial reform, health care reform, immigration reform as well as the sovereign debt crisis in the Eurozone and China's recalcitrance in floating its currency and the United States' newfound dependence on exports to lift us out of the recession place great uncertainty on our future. These uncertainties in turn retard investment and consumption. Moreover, the states are engaged in a third "civil war" — an allegory promulgated by Professor Barry Bluestone of Northeastern University. The 19th century Civil War was fought between the North and South to resolve slavery and was followed by the 20th century civil war in which the North and South

--Continued on page 5--

--Continued from page 3--

'battled' for manufacturing jobs. Today we are engaged in a 21st century civil war to determine which regions, states, cities and towns will be able to retain and attract young working families to fill our labor force and revenue gaps.

As we examine the factors that are most important in winning this civil war, we are drawn to regional solutions, smaller and more effective government and the highest quality educational, housing and transportation systems we can imagine. Harnessing our formidable, innovative capacity, our Yankee ingenuity, to achieve the excellence we need to compete successfully is the key to the state's future prosperity. ■

[1] The Business Cycle Dating Committee of the National Bureau of Economic Research (NBER) determined that a trough in business activity occurred in the U.S. economy in June 2009 in a September 20, 2010 report. The trough marked the end of the recession that began in December 2007 and the beginning of an expansion.
[2] Bureau of Labor Statistics: "The Employment Situation - October 2010," November 5, 2010.
[3] U.S. Census Bureau, U.S. Department of Housing and Urban Development and U.S. Department of Commerce Joint Release: "New Residential Construction in September," October 19, 2010.
[4] The Financial Forecast Center is a small, independent, privately-owned corporation located in Houston that has produced and published economic and financial market forecasts since 1997 exclusively on the Internet. See www.forecasts.org/gdprealgrowth.htm.
[5] NABE Outlook, October 2010, "Growth Projections Marked Down: Higher Unemployment and Lower Inflation," http://www.nabe.com/publib/macsum.html.
[6] Mark Zandi, Moody's Economy.com, "U.S. Macro Outlook: Easing Past the Darkness," November 17, 2010.
[7] NEEP Outlook Conference/Moody's Analytics, "Deficits as far as the Eye Can See: Seeking Solutions to Our National and State Fiscal Crises," November 17, 2010, p. 18.
[8] Ataman Ozyildirim, The Conference Board, October 21, 2010. http://www.conference-board.org/data/bcicountry.cfm?cid=1.
[9] Ken Goldstein, The Conference Board, "October leading economic indicators up 0.5%," November 18, 2010.
[10] See Note 9.
[11] Christina D. Romer, "Not My Father's Recession: The Extraordinary Challenges and Policy Responses of the First Twenty Months of the Obama Administration," Sept. 1, 2010.
[12] U.S. Census Bureau, "Advance Monthly Sales for Retail and Food Purchases September 2010," Oct. 15, 2010.
[13] National Association of Realtors, "Pending Home Sales Slip but Modest Recovery Expected in 2011," Nov. 5, 2010.
[14] Bureau of Economic Analysis, October 29, 2010.
[15] *Report to the President on the National Export Initiative*. Sept. 16, 2010. http://www.whitehouse.gov/sites/default/files/nei_report_091510_short.pdf.
[16] BEA, News Release GDP by State: "Economic Downturn Widespread among States in 2009," November 18, 2010.
[17] See note 7.
[18] Nicholas Johnson, Phil Oliff, and Erica Williams, Center on Budget and Policy Priorities, "An Update on State Budget Cuts At Least 46 States Have Imposed Cuts That Hurt Vulnerable Residents and the Economy," November 5, 2010
[19] "Consensus revenues" are those jointly agreed upon by the OFA, Office of Policy and Management (OPM), and the Office of the State Comptroller. Table extracted from OFA, "Fiscal Accountability Report to the Appropriations and Finance Committees as required by C.G.S. 2-36b," November 15, 2010, p. 2.
[20] *The Connecticut Economic Digest*, Vol. 15, No. 11, November 2010, p. 6.
[21] DRS Annual Report, FY2009.
[22] CoreLogic, "CoreLogic Home Price Index Declined For the First Time This Year," October 25, 2010.
[23] Ross Gittell, NEEP, "Deficits as far as the Eye Can See: Seeking Solutions to our National and State Fiscal Crises," November 17, 2010, p. 8.

GENERAL ECONOMIC INDICATORS

(Seasonally adjusted)	3Q 2010	3Q 2009	CHANGE NO.	CHANGE %	2Q 2010
Employment Indexes (1992=100)*					
Leading	116.1	113.1	3.0	2.7	115.5
Coincident	101.8	102.2	-0.4	-0.4	102.4
General Drift Indicator (1986=100)*					
Leading	104.5	100.8	3.7	3.7	104.8
Coincident	106.6	106.9	-0.3	-0.3	107.1
Farmington Bank Business Barometer (1992=100)**	119.4	119.5	-0.1	-0.1	119.7
Philadelphia Fed's Coincident Index (July 1992=100)***	**NOV**	**NOV**			**OCT**
(Not seasonally adjusted)	**2010**	**2009**			**2010**
Connecticut	153.9	150.3	3.6	2.4	153.5
United States	150.4	147.6	2.8	1.9	150.2

*Sources: *The Connecticut Economy, University of Connecticut **Farmington Bank ***Federal Reserve Bank of Philadelphia*

The Connecticut Economy's **General Drift Indicators** are composite measures of the four-quarter change in three coincident (Connecticut Manufacturing Production Index, nonfarm employment, and real personal income) and four leading (housing permits, manufacturing average weekly hours, Hartford help-wanted advertising, and initial unemployment claims) economic variables, and are indexed so 1986 = 100.

The **Farmington Bank Business Barometer** is a measure of overall economic growth in the state of Connecticut that is derived from non-manufacturing employment, real disposable personal income, and manufacturing production.

The **Philadelphia Fed's Coincident Index** summarizes current economic condition by using four coincident variables: nonfarm payroll employment, average hours worked in manufacturing, the unemployment rate, and wage and salary disbursements deflated by the consumer price index (U.S. city average).