The 2015 Economic Outlook

As we begin a new year, this issue of the Digest looks at the economic prospects for 2015. As usual, this annual outlook attempts to interpret recent data and their trends, and to offer some insights about what is likely for the U.S. and Connecticut economies in the year ahead.

The Nation

The outlook for the U.S. economy in 2015 remains quite positive. A set-back in early 2014 resulting partially from weather-related factors that hampered overall growth was encouragingly offset by considerably stronger growth as the year progressed. Of note, except for a couple of minor dips, the U.S. Gross Domestic Product (GDP), or the constant dollar value of all goods and services produced by labor and capital located in the U.S., since then has averaged 2.2% at an annual rate from the preceding quarter (Figure 1). After growing 2.5% in 2010, 1.6% in 2011, 2.3% in 2012, 2.2% in 2013, and an estimated 3.9% in Q3-2014, RGDP growth near 3.0% is likely in 2015.¹ The New England Economic Partnership (NEEP), based on Moody’s Analytics underlying macroeconomic forecast, sees RGDP growth at 3.7% in 2015.² The National Association of Business Economists (NABE) outlook panel consensus is, on an average annual basis, “3.0% in 2015.”³

U.S. Employment and Unemployment

Total seasonally-adjusted nonfarm payroll employment since the end of the recession has

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¹ Real Gross Domestic Product (RGDP)
² The New England Economic Partnership (NEEP)
³ The National Association of Business Economists (NABE)
The Conference Board Leading Economic Index™ (LEI) for the U.S. in 2014 continued to post gains. Ataman Ozyildirim, Economist at The Conference Board said: “The LEI rose sharply in October, with all components gaining over the previous six months ... the LEI suggests the U.S. expansion continues to be strong.” Ken Goldstein added: “The upward trend in the LEI points to continued economic growth through the holiday season and into early 2015.”

Monetary Policy
As expected, the Federal Reserve Bank’s Open Market Committee (FOMC) began reducing its once $85 billion-per-month bond buying program in 2014. The tapering ended the program in October. The Fed has cautioned all along, however, that it would not raise interest rates “for a considerable time.” Such increases were dependent upon real improvement in the labor market and pending price stability. Indications are that such interest rate hikes will occur in 2015. Such a decision has the potential to negatively impact capital investment borrowing and home mortgages. In its October FOMC statement the likelihood of an interest rate hike was increased: “... if incoming information indicates faster progress toward the Committee’s employment and inflation objectives than the Committee now expects, then increases in the target range for the federal funds rate are likely to occur sooner than currently anticipated.” So it remains to be seen the timing and pace the FOMC will adopt, but rate hikes are surely a factor in any outlook for 2015.

Also as expected, the current Fed Chairwoman Janet Yellen’s confirmation for the post early last year meant FOMC policy was increased by 9.4 million jobs, after averaging losses of 209,500 jobs a month in Q3-Q4 2009, gains of 160,583 jobs a month in 2010-2013, and improving to 226,200 jobs per month through October in 2014 (Figure 2). Through November 2014, more jobs were created than in any year since 1999. This improved job growth trend should continue in 2015. In 2014, the U.S. unemployment rate fell to 5.8% in October from 7.2% in October a year ago, the lowest in six years, and a declining unemployment rate will likely continue in 2015.
likely to change only very gradually and given strong indications the labor and housing markets were improving. Yellen was considered the architect of the almost unprecedented original rounds of so-called “quantitative easing” (QE). Stock and bond markets have had mixed reactions to Fed policy, often rising or falling immediately after statement releases. Late in 2014, following some tumultuous selloffs and rebounds, the Dow Jones Industrial Average and the S&P Index both managed some all-time record-high closing levels.

**U.S. Growth Prospects**

The forecast embodied in this article – political confrontation aside – will assume continuation of a number of positive developments going into 2015. Growth prospects remain positive for some of the following reasons: The Manufacturing ISM Report on Business® reported the 65th consecutive monthly expansion into November 2014 of the overall economy; the ISM report noted that: “Comments from the panel generally cite positive business conditions, with growth in demand and production volumes.” Moreover, October’s PMI [Purchasing Managers Index] registered 59 percent, “an increase of 2.4 percentage points from September’s reading of 56.6 percent, indicating continued expansion in manufacturing.” A reading above 50% indicates that the manufacturing economy is generally expanding; below 50% indicates that it is generally contracting.

Consumer spending also saw gains with average monthly increases of 2.3% in 2014, up from 1.9% from the same month a year ago in 2013. The Thomson Reuters/University of Michigan final Index of Consumer Sentiment advanced to 86.9 in October 2014, the highest level since July 2007. The Conference Board Consumer Confidence Index® also reached a seven-year high of 94.5 in October 2014. The Index exceeded its same-month year-ago level throughout 2014. In November the Index stood at 88.7 (1985=100).

Real exports of U.S. goods and services increased 7.8 percent in the third quarter of 2014, compared with an increase of 11.1 percent in the second quarter. Real nonresidential fixed investment (purchases of plant and equipment) gained 5.5% in Q3-2014 and 9.7% in Q2-2014, compared with Q3 and Q2-2013.

New U.S. homes sales grew 20.6% into October from a year ago to the highest level in six years, and new housing units authorized by building permits were up 2.5% in September from a year ago; meanwhile U.S. median home sales prices rose 4.8% in the 12 months up to October. Likewise, construction spending during the first 9 months of 2014 amounted to $710.1 billion, 6.1 percent above the $669.3 billion for the same period in 2013, according to the U.S. Commerce Department.

U.S. retail sales in October were up 4.1% from the same month last year. There is also continued momentum in car sales, up 8.6% YTD through October 2014 over 2013. Meanwhile, U.S. inflation remains tame; Social Security recipients, for example, will receive a Cost of Living Adjustment (COLA) in 2015 of only 1.7%, compared to 1.5% in 2014 and less than 2% for the fifth time in six years.

**Connecticut**

Connecticut’s economy should continue to experience modest growth in 2015. Connecticut’s real state gross domestic product (SGDP), the broadest measure of the state’s economic health, increased 0.9% in 2013 (the latest year available). This growth followed a 0.9% decline in 2011, and a 1.0% growth rate in 2012. The next release of GDP by state is scheduled for the summer of 2015. The release will include revised statistics for 1997-2013 and advance statistics for 2014. When released for 2014, Connecticut should see positive growth again that should continue into 2015. Connecticut personal income grew 0.8% in Q2-2013, seasonally adjusted at quarterly rates, increased by 0.4% in Q3-2013, was unchanged in Q4-2013, but increased a further 1.2% in Q1-2014, and 1.3% in Q2-2014, all relative to the preceding quarter. As forecasted by the Connecticut Department of Labor, personal income for Q1-2015 will increase by 3.2% from Q1-2014. Increases in personal disposable income indicate stronger growth in consumer spending which can lead to additional gains throughout the economy.

The Connecticut recession from March 2008 through February 2010 saw the loss of 119,100 seasonally-adjusted non-farm jobs (Figure 3). By late November 2014, jobs regained numbered 87,900 (73.8%), or 1,570 jobs per month since February 2010 when the recovery began. The private sector has recovered somewhat faster and has regained 97,600 (87.1%, 1,743 per month) of the 112,000 private jobs that were lost during the same period. NEEP forecasts Connecticut will gain about 25,100 jobs or 1.4% in 2015. The state’s unemployment rate, after peaking at 9.4% for five consecutive months in 2010 and hovering around 8.0% for much of 2013, declined to 6.4% in October 2014. The state’s unemployment rate has not been this low since November 2008. NEEP forecasts Connecticut’s unemployment rate will be 6.4% in 2015.
average weekly initial claims for unemployment insurance peaked at 7,496 in March 2009, but declined to 4,101 (-45.3%) by November 2014. Through November, Connecticut’s total non-farm employment was up every month over the same month a year ago.

Connecticut’s Fiscal Outlook

The state’s fiscal outlook was stable in 2014 evidenced by a FY 2014 surplus of $248.5 million, based on Generally Accepted Accounting Principles (GAAP). That surplus was deposited in the Budget Reserve (“Rainy Day”) Fund bringing its balance to $519.2 million. A newly revised budget for the fiscal year ending in 2015, introduced in February 2014, is in place. However, the state potentially faces a $1.3 billion to $1.4 billion deficit in FY 2016 and FY 2017.

Connecticut’s Budget Outlook

In October 2014, the state comptroller reported the General Fund for fiscal year 2015 “anticipates a GAAP basis … balance of $0.3 million [$300,000].”16 “Consensus Revenues” for FY 2015 were estimated to be $17,398.9 million.17 The Connecticut legislature’s Office of Fiscal Analysis (OFA) projects an $89.1 million deficit for FY 2015, as shown in Table 1.18

Housing

The state’s housing market again experienced modest growth in 2014 and the U.S. Census-based residential permit data for 128 towns reported monthly by the Department of Economic and Community Development through September 2014 had grown by 23.7% compared to the same period a year ago. Moreover, the data seems to indicate “that the housing market will continue its upward trend.”19 NEEP expects Connecticut housing permits that peaked at 12,269 in Q3-2005 and reached bottom at 3,173 for all of 2011 will rebound to 6,033 in 2014, and likely reach 7,734 in 2015. According to NEEP, existing Connecticut single family median home prices peaked at $320,800 in 2007, but fell to a low of $251,100 in 2012, and are expected to average $258,600 for 2014 and $272,700 in 2015. Existing home sales might show a gain from 38,300 in 2014 to 45,600 in 2015.20

Initiatives

The Connecticut economy continued to benefit from an aggressive campaign to strengthen small businesses in recent years. The Small Business Express Program (EXP) provides loans and grants to Connecticut’s small businesses to spur job creation and growth and has seen vigorous activity since its inception. As of mid-November 2014, the state has assisted 1,207 companies with more than $171 million in loans and grants. With this much-needed capital, up to 4,485 jobs are expected to be created and 12,679 retained. Likewise the state’s “First Five” and “Next Five” job initiatives have promised substantial growth in employment and capital investment in Connecticut. At year’s end (2014), eleven business deals had been announced as part of the ongoing expansion program, which leveraged nearly $1.3 billion in private investment. Among the eleven companies — Cigna, ESPN, NBC, Alexion Pharmaceuticals, CareCentrix, Sustainable Building Systems LLC, Deloitte, Bridgewater Associates, Charter Communications, Navigators Group, Inc., and Pitney Bowes — up to 5,248 jobs were expected to be created and 12,690 retained.

Conclusion

Connecticut and the nation’s recovery are affected by constant uncertainties. Many of the issues are the same as in past years:
financial and healthcare reform, immigration reform, Eurozone debt, and China, as well as other geopolitical risks to the global economy, particularly the Middle East and Ukraine. Europe and Japan are likely to continue to have an impact on the outlook for the U.S. However, recent easing actions of their central banks indicate 2015 building on the progress of 2014: continued growth and gradual improvement in the unemployment rate. The housing market saw improvement in sales and permits that should continue in 2015. The state’s efforts in economic development as well as housing capital investments should continue to improve the state’s business climate.

Connecticut’s growth in total output that initially put it behind 49 other states in 2011 (-0.9%) was turned around in 2012 (+1.0%) and 2013 (+0.9%). The “Connecticut Bioscience” initiative and opening of Jackson Labs last year is one measure of success. On balance, therefore, we should expect continued positive economic growth in 2015.

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6 See Note 5.
8 Note 7.
18 Table extracted from OFA, “Fiscal Accountability Report to the Appropriations and Finance Committees as required by CGS Sec. 2-36b,” November 14, 2014, p. 2.
20 NEEP, See Note 2, p. 12.