



Commission on Government Forecasting and Accountability

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MONTHLY BRIEFING FOR THE MONTH ENDED: OCTOBER 2014

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INSIDE THIS ISSUE

PAGE 1 - **ECONOMY:** Housing
Restrains Growth

PAGE 3: Illinois Economic Indicators

PAGE 4 - **REVENUE:** Monthly Revenues
Mixed Again As Weaker Federal Sources
Offset Gains Elsewhere

PAGE 5-6: Revenue Tables

LATEST PUBLICATIONS

Illinois Public Retirement Systems: A
Report on the Financial Condition of the
Illinois Municipal, Chicago and Cook
County Pension Funds of Illinois – October
2014

ECONOMY: Housing Restrains Growth

Edward H. Boss, Jr., Chief Economist

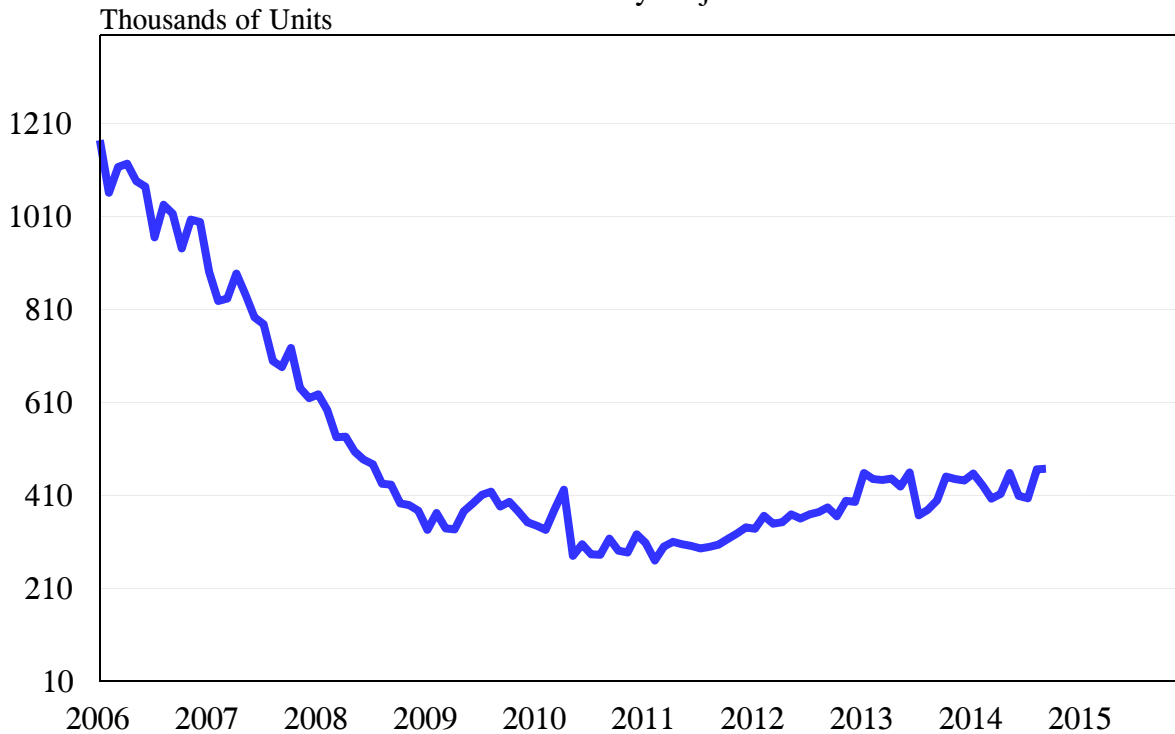
The economy grew at a 3.5% annual rate according to the Advance Estimate released for the third quarter, down from the previous quarter's 4.6% rate but an actual contraction of 2.1% in the first quarter. For the year thus far, the economy has been rising at a 2.0% rate, continuing in the 2% to 2.5% range of the previous four years and remains the weakest recovery coming out of recession in the post WWII era. Somewhat surprising in the latest report was that within the spending categories, the gains in both consumer spending and residential construction slowed while government spending, both at the federal and state and local level, rose sharply.

A turnaround in housing has been a major contributor in recent years to the recovery. Home prices had plummeted following a severe downturn from the financial crisis leaving many owners under water with their mortgages. The median price of a new home fell from a level of \$263,600 in March 2007, just prior to the recession, to \$205,100 two years later in March 2009, just prior to the recovery, a drop of 28%. Moreover, the falloff in prices varied widely by location. Those sectors mainly in the South and West, particularly in states like Nevada and Florida, which had seen prices skyrocket, fell sharply relative to those areas where price increases rose less. This led to foreclosures and walk-a-ways, driving prices even lower in those areas.

By mid-2013 median home prices had fully recovered from the sharp declines during the housing collapse, exceeding the previous high on a sustained basis. Much of the improvement in housing has come from the expansion of multi-unit housing and from investors with easy access to credit. Home sales rose sharply with more than 90% accounted for by existing homes. As shown in the accompanying chart, newly-built single family homes have shown only modest gains. And, it's only new construction that contributes to economic growth as existing home sales merely reflect a transfer of financial assets.

CHART 1

NEW SINGLE FAMILY HOMES SOLD
Seasonally-Adjusted



CGFA

This year median new home prices, while volatile, slowed their rate of advance and prices stabilized. The preliminary median priced home for September was the lowest recorded so far this year, although it followed a large gain the previous month so that the average of the two months was in line with prices seen earlier this year. Even so, the perception that housing prices always rise and, therefore, that it was a sure bet as a good investment has been shattered.

In addition to whether or not home ownership continues to be a good investment are demographic factors. According to IHS Global Insight's economic forecast...*"Newly released data on household formation was unexpectedly weak, but goes a long way to explain the current housing weakness. This reduction*

directly shaves a respective 0.1 and 0.2 percentage point of real GDP growth in each of these (2014 & 2015) two years." Even as the rise in home prices appear to have stabilized while mortgage interest rates remain at historic lows, stagnant incomes and high unemployment have begun to reduce housing affordability as measured by the affordability index - - a measure of the financial ability of U.S. families to buy a house. (An index of 100 means that families earning the national median income has just enough needed to qualify for a mortgage on a median-priced home. An index higher than 100 means they have more than enough and lower than 100 have less than enough.)

By mid-2007 just prior to the recession, the affordability index was

just slightly above 100 (107.1 in July 2007). As home prices began to decline, the affordability index began to rise reaching 160.8 in June 2009 at the start of the recovery. Affordability continued to rise and by early 2012 had risen to 200 or slightly above, more than twice that needed to purchase a median priced home. Beginning in 2013 through this year, however, affordability was reduced, reaching 157.6 in August of this year, about the same as that that existed just prior to the recovery.

While home ownership had been considered part of the American Dream, changing attitudes as to its role as an investment, increased mobility of people, and demographic and economic changes seem to have altered its role as indicated by the age of the householder. Homeownership in the U.S. dropped to 64.4% in the third quarter, the lowest

since 1995. Homeownership rates were the highest for households ages 65 and over at more than 80%, virtually unchanged from that of the previous several years. Those aged 55 to 64 had an ownership rate of 76.6%, those aged 45 to 54 at 70.1%, ownership rates for 35 to 44 year old was at 59.1%, and the lowest, at 36%, were those under the age of 35. Latest data showed overall ownership the highest in the Midwest at 68.8% and lowest in the West at 59.4%.

With the removal of the Federal Reserve's program of Quantitative Easing and its purchases of mortgage-backed securities, some stability in home prices, and slow household formation, the increase in the housing sector, while continuing to rise, is likely to be restrained. It will take somewhat faster economic growth on a sustained basis and particularly gains in income to improve significantly.

INDICATORS OF ILLINOIS ECONOMIC ACTIVITY

<u>INDICATORS *</u>	<u>Sept. 2014</u>	<u>Aug. 2014</u>	<u>Sept. 2013</u>
Unemployment Rate (Average)	6.6%	6.7%	9.1%
Annual Rate of Inflation (Chicago)	0.4%	0.6%	2.1%
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	<u>LATEST MONTH</u>	<u>% CHANGE OVER PRIOR MONTH</u>	<u>% CHANGE OVER A YEAR AGO</u>
Civilian Labor Force (thousands) (September)	6,499	0.1%	-0.5%
Employment (thousands) (September)	6,072	0.2%	2.2%
New Car & Truck Registration (September)	59,109	7.0%	16.7%
Single Family Housing Permits (September)	957	0.5%	10.8%
Total Exports (\$ mil) (August)	5,588	1.7%	0.0%
Chicago Purchasing Managers Index (October)	66.2	9.4%	0.4%

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

REVENUE
Monthly Revenues Mixed Again As Weaker Federal Sources
Offset Gains Elsewhere

Jim Muschinske, Revenue Manager

Overall base revenues declined \$24 million in October. Despite another good month for personal income and sales taxes, continued weakness in federal sources as well as corporate income taxes more than offset the positives. October had the same number of receipting days as last year.

As mentioned, gross personal income taxes continued to do quite well, growing \$100 million, or \$83 million net of refunds. Sales tax also experienced a strong month as receipts rose an impressive \$58 million. A few other sources contributed minor gains with cigarette taxes, corporate franchise taxes, and other sources each growing \$1 million for the month.

Again, gross corporate income taxes were weaker, with monthly receipts falling \$45 million, or \$40 million net of refunds. Inheritance tax dropped \$14 million, while public utility taxes declined by \$12 million. Insurance taxes weakened by \$3 million and interest income dipped by \$1 million.

Overall transfers were down \$5 million in October. While riverboat transfers increased \$2 million, all other transfers suffered a drop of \$7 million. As mentioned, it was another poor month for federal sources as receipts dropped \$93 million, reflecting reimbursable spending at this time primarily taking place from non-general funds spending.

Year to Date

Through the first one-third of the fiscal year, overall base revenues were down \$398

million. However, much of that decline was expected and was due to the much lower Refund Fund transfer into GRF. In addition, weaker federal sources to begin the year have significantly contributed to the fall off. The economically related sources were mixed as both personal income taxes and sales performed well while corporate income taxes weakened.

To date, gross personal income taxes were up \$201 million, or \$155 million net of refunds. Sales tax receipts were ahead of last year's pace by \$154 million, while other sources were up \$59 million. Inheritance tax added \$24 million, insurance taxes \$3 million, corporate franchise taxes \$2 million, interest income \$2 million, liquor taxes \$1 million, and vehicle use \$1 million.

Gross corporate income taxes were down \$122 million through October, or \$111 million net of refunds. And public utility taxes were off by \$15 million.

To date, overall transfers were down \$350 million due to the much lower Refund transfer which accounts for \$334 million of that falloff. Riverboat transfers were down \$20 million, but other transfers posted a \$1 million gain while lottery transfers contributed a \$3 million increase. Federal sources were down \$323 million thus far in the fiscal year, reflecting lower reimbursable spending from the GRF. It appears at this time, the focus on reimbursable spending has been focused in non-general funds. At some point it is believed that will shift back to GRF spending.

GENERAL FUNDS RECEIPTS: OCTOBER

FY 2015 vs. FY 2014

(\$ million)

<u>Revenue Sources</u>	<u>Oct. FY 2015</u>	<u>Oct. FY 2014</u>	<u>\$ CHANGE</u>	<u>% CHANGE</u>
State Taxes				
Personal Income Tax	\$1,379	\$1,279	\$100	7.8%
Corporate Income Tax (regular)	128	173	(\$45)	-26.0%
Sales Taxes	698	640	\$58	9.1%
Public Utility Taxes (regular)	72	84	(\$12)	-14.3%
Cigarette Tax	30	29	\$1	3.4%
Liquor Gallonage Taxes	13	13	\$0	0.0%
Vehicle Use Tax	3	3	\$0	0.0%
Inheritance Tax (Gross)	22	36	(\$14)	-38.9%
Insurance Taxes and Fees	1	4	(\$3)	-75.0%
Corporate Franchise Tax & Fees	20	19	\$1	5.3%
Interest on State Funds & Investments	1	2	(\$1)	-50.0%
Cook County IGT	0	0	\$0	N/A
Other Sources	30	29	\$1	3.4%
Subtotal	\$2,397	\$2,311	\$86	3.7%
Transfers				
Lottery	59	59	\$0	0.0%
Riverboat transfers & receipts	26	24	\$2	8.3%
Proceeds from Sale of 10th license	0	0	\$0	N/A
Refund Fund transfer	0	0	\$0	N/A
Other	37	44	(\$7)	-15.9%
Total State Sources	\$2,519	\$2,438	\$81	3.3%
Federal Sources	\$161	\$254	(\$93)	-36.6%
Total Federal & State Sources	\$2,680	\$2,692	(\$12)	-0.4%
Nongeneral Funds Distribution:				
Refund Fund				
Personal Income Tax	(\$138)	(\$121)	(\$17)	14.0%
Corporate Income Tax	(\$18)	(23)	\$5	-21.7%
Subtotal General Funds	\$2,524	\$2,548	(\$24)	-0.9%
Short-Term Borrowing	\$0	\$0	\$0	N/A
FY'13/14 Backlog Payment Fund	\$0	\$0	\$0	N/A
Budget Stabilization Fund Transfer	\$0	\$0	\$0	N/A
Total General Funds	\$2,524	\$2,548	(\$24)	-0.9%
CGFA SOURCE: Office of the Comptroller: Some totals may not equal, due to rounding				3-Nov-14

GENERAL FUNDS RECEIPTS: YEAR TO DATE

FY 2015 vs. FY 2014
(\$ million)

<u>Revenue Sources</u>	<u>FY 2015</u>	<u>FY 2014</u>	<u>CHANGE FROM FY 2014</u>	<u>% CHANGE</u>
State Taxes				
Personal Income Tax	\$5,468	\$5,267	\$201	3.8%
Corporate Income Tax (regular)	785	907	(\$122)	-13.5%
Sales Taxes	2,733	2,579	\$154	6.0%
Public Utility Taxes (regular)	308	323	(\$15)	-4.6%
Cigarette Tax	118	118	\$0	0.0%
Liquor Gallonage Taxes	57	56	\$1	1.8%
Vehicle Use Tax	12	11	\$1	9.1%
Inheritance Tax (Gross)	106	82	\$24	29.3%
Insurance Taxes and Fees	93	90	\$3	3.3%
Corporate Franchise Tax & Fees	73	71	\$2	2.8%
Interest on State Funds & Investments	8	6	\$2	33.3%
Cook County IGT	0	0	\$0	N/A
Other Sources	255	196	\$59	30.1%
Subtotal	\$10,016	\$9,706	\$310	3.2%
Transfers				
Lottery	204	201	\$3	1.5%
Riverboat transfers & receipts	112	132	(\$20)	-15.2%
Proceeds from Sale of 10th license	0	0	\$0	N/A
Refund Fund transfer	63	397	(\$334)	N/A
Other	182	181	\$1	0.6%
Total State Sources	\$10,577	\$10,617	(\$40)	-0.4%
Federal Sources	\$663	\$986	(\$323)	-32.8%
Total Federal & State Sources	\$11,240	\$11,603	(\$363)	-3.1%
Nongeneral Funds Distribution:				
Refund Fund				
Personal Income Tax	(\$547)	(\$501)	(\$46)	9.2%
Corporate Income Tax	(\$110)	(\$121)	\$11	-9.1%
Subtotal General Funds	\$10,583	\$10,981	(\$398)	-3.6%
Short-Term Borrowing	\$0	\$0	\$0	N/A
FY'13/14 Backlog Payment Fund Transfer	\$0	\$50	(\$50)	N/A
Tobacco Liquidation Proceeds	\$0	\$0	\$0	N/A
Pension Contribution Fund Transfer	\$0	\$0	\$0	N/A
Budget Stabilization Fund Transfer	\$275	\$275	\$0	0.0%
Total General Funds	\$10,858	\$11,306	(\$448)	-4.0%
SOURCE: Office of the Comptroller, State of Illinois: Some totals may not equal, due to rounding.				
CGFA				3-Nov-14