

A PRAYER FOR THE U.S. ECONOMY

RAISE THE
DEBT CEILING...

LOWER THE
DEFICIT...

LEFT-WING
POLITICS...

RIGHT-WING
POLITICS...

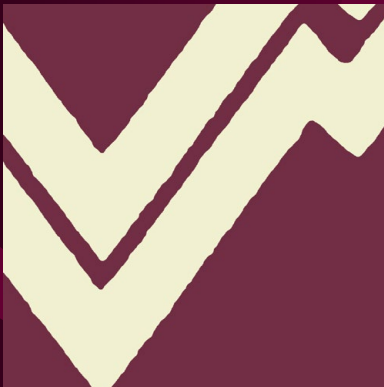
GOD HELP
US!



Economic and Revenue Review for the Vermont State Legislature

December 1, 2023

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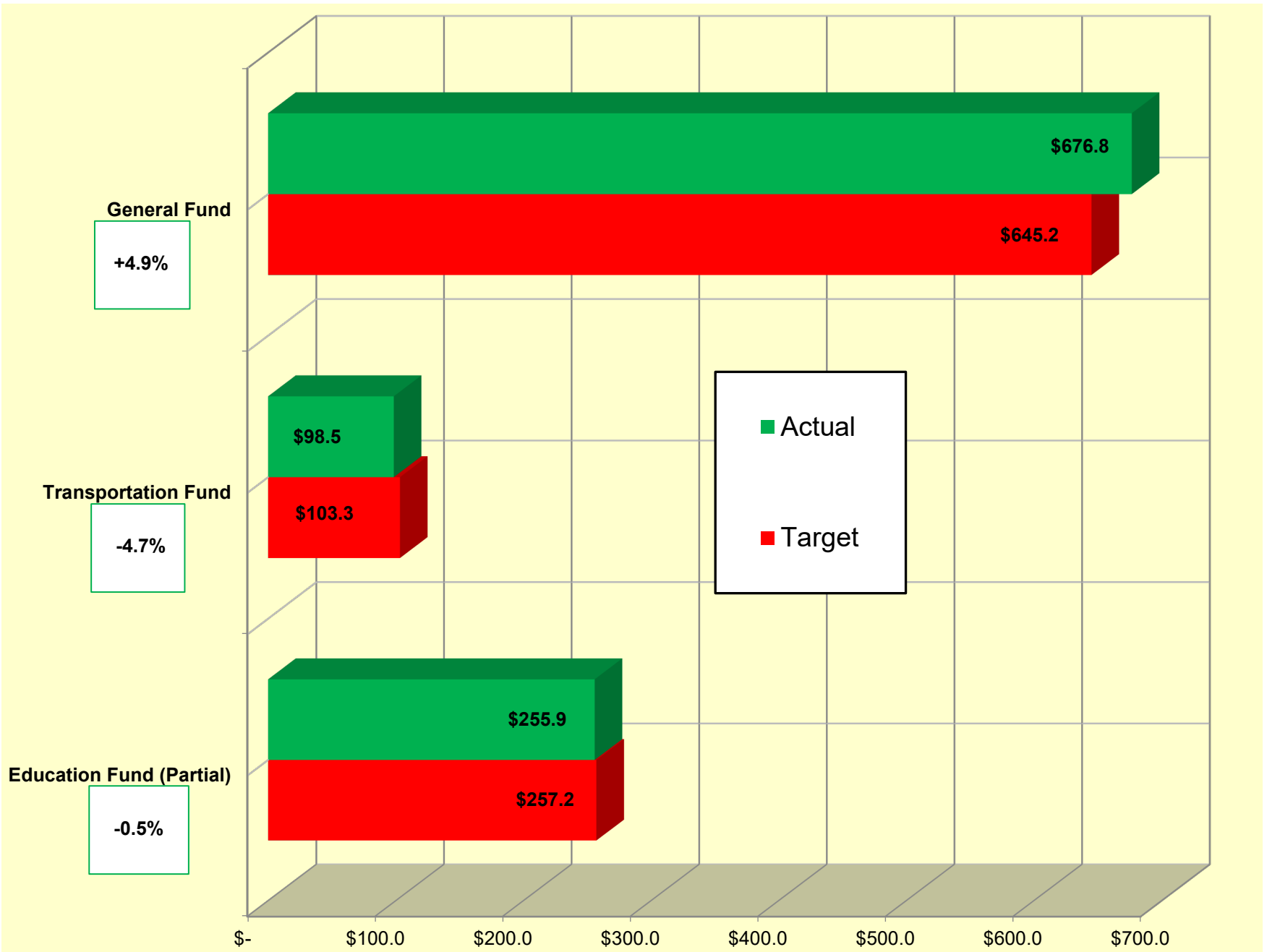
Despite Widespread Pessimism About the State of the Economy, Growth has been Solid, Inflation is Down and Unemployment is Low

- This has slightly lowered the risks of recession, raising the possibility that a rare “soft landing” may be achievable
- Interest rates remain high, however, and are taking an ever-increasing toll on the economy, especially in credit-sensitive sectors
- Despite shrinking savings, consumer spending remains intact, especially with spending on services
- Credit card debt and defaults, however, have risen significantly, with alarming implications amidst 24.6% average credit card interest rates

The Second Half of FY24, However, Will Present Mounting Headwinds that Will Likely Slow Economic and Revenue Growth

FY24 Revenues by Fund Through October 2023

Actual Revenues (Green) vs. Targets (Red), Percent Variance by Fund in Box, Source: VT Joint Fiscal Office



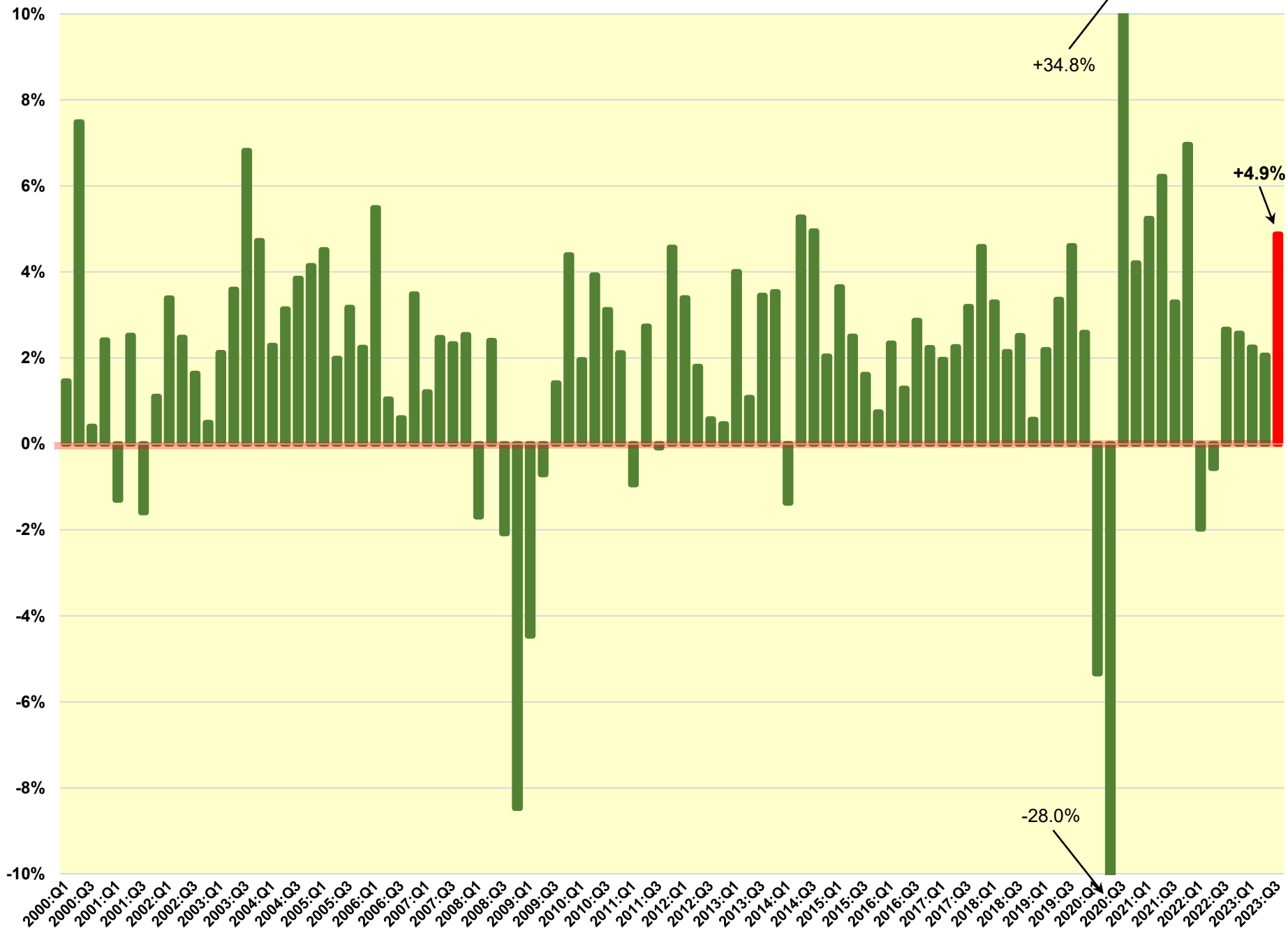
Mirroring Economic Conditions, Revenues (YTD thru October) Are Slightly Above Expectations

- Total Revenues through October (General, Transportation and partial Education Funds) are about 2.5% above targets (about \$25M on a base of about \$1B), due mostly to strength in Personal Income receipts (which are down 6.6% from last year but are about 12% above target) and despite weakness in Corporate Income revenues. Lower than expected negative tax collection effects associated with forbearance from the severe July flooding also added to the over-target performance through October, some of which is likely to be reversed in November.
- Besides Personal Income taxes, revenue categories that were stronger than expected in the first four months of the fiscal year also included Estate, Interest and Lottery revenues. Most other revenue categories were running slightly below target, including the Property Transfer tax and every T-Fund category.
- Impacts from tax payment forbearance in Meals & Rooms appears to be the only category that may have been more affected than anticipated in July. Through October, Meals & Rooms receipts were running about 4% lower than projected. Early November data, however, suggests that most of this may be made up via delayed payments. The other two large consumption taxes were mixed through October, with Sales & Use spot on at only 0.8% above target and Motor Vehicle Purchase & Use receipts 4.8% below expectations. Both high borrowing costs and continued scarce supply, which will be further exacerbated by the UAW strikes, contributed to the weak MVP&U performance. These consumption taxes will be tested throughout the balance of FY24 and into FY25 by continued high interest rates, weaker consumer spending and higher unemployment rates.
- Unfortunately, at this writing (and speaking) final November revenue data are not yet in. This year, in particular, November will be a critical month, since disaster forbearance was extended to November. Early returns indicate November will be slightly weaker than expected, reducing cumulative revenues by at least \$10M, but still closing slightly above cumulative aggregate targets. Much of this weakness will be in Personal Income, which was not as impacted by forbearance as expected. Corporate income continues to be beset by higher refunding and lower current liabilities, as sales slow.
- There continues to be considerable uncertainty affecting both the general economy and State revenues. While direct pandemic health effects have receded from prominence, their legacy of vast federal spending, shifting consumer preferences, supply chain disruptions, remote work prevalence, reduced labor force participation and higher inflation continue to resonate. The July flooding demonstrates the growing impact and unpredictability of extreme weather events associated with broader climate change and war in Europe and now the Middle East demonstrates the same unpredictability of events that can severely impact the economic conditions in a short period of time.
- When the dust settles from November revenue data, it is likely that total revenues across all three major funds will be about 1%-2% above targets - essentially a rounding error. The second half of the year, however, will be more challenging, with a slowing economy and larger downside risks.

Third Quarter 2023 GDP Shows Impressive Growth at 4.9%

(Annualized Quarterly Growth in U.S. GDP, Source: U.S. BEA)

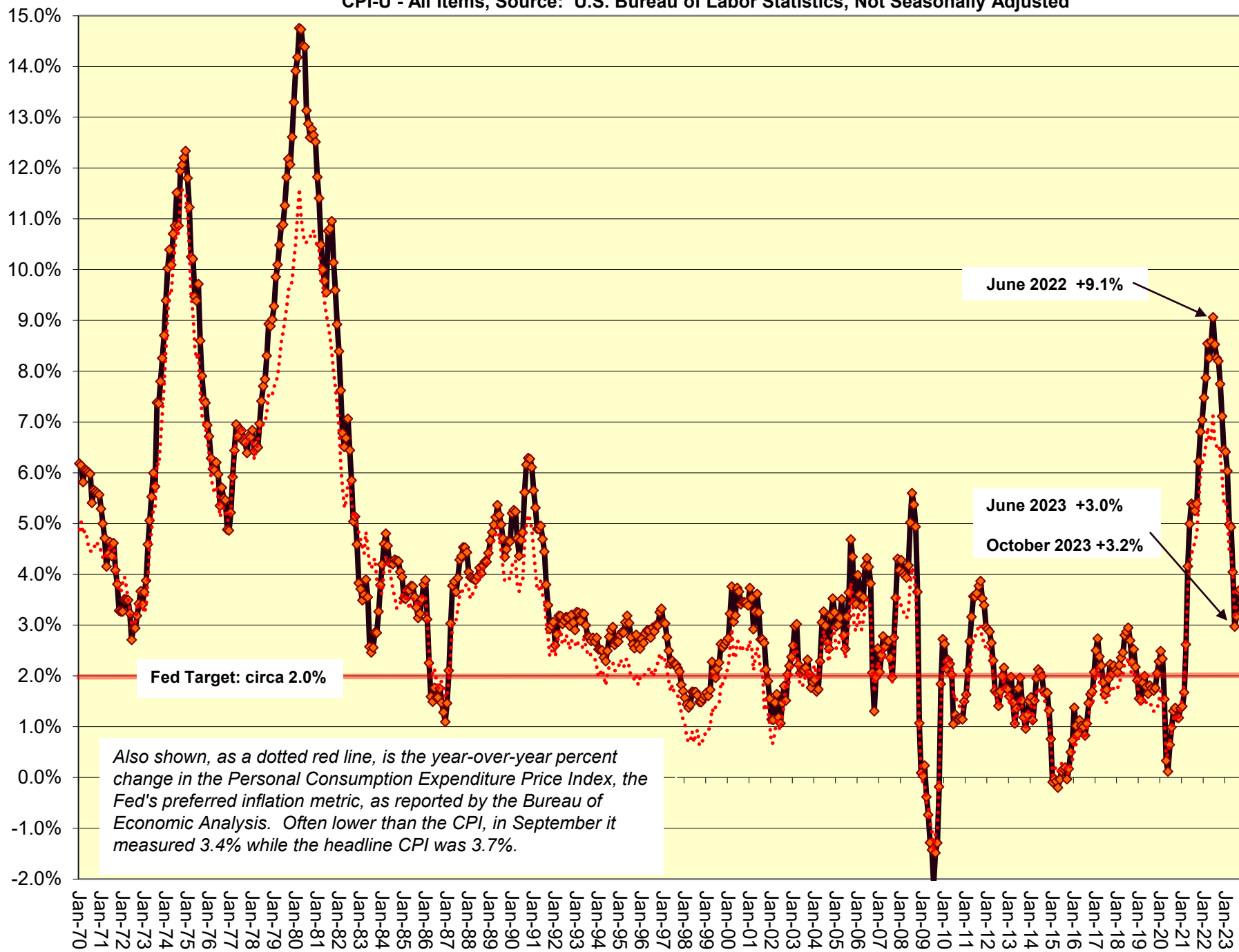
Annualized Compounded Quarterly Growth Rate



Inflation Drops Significantly in the Past Year, But Remains Above the Fed Target Rate

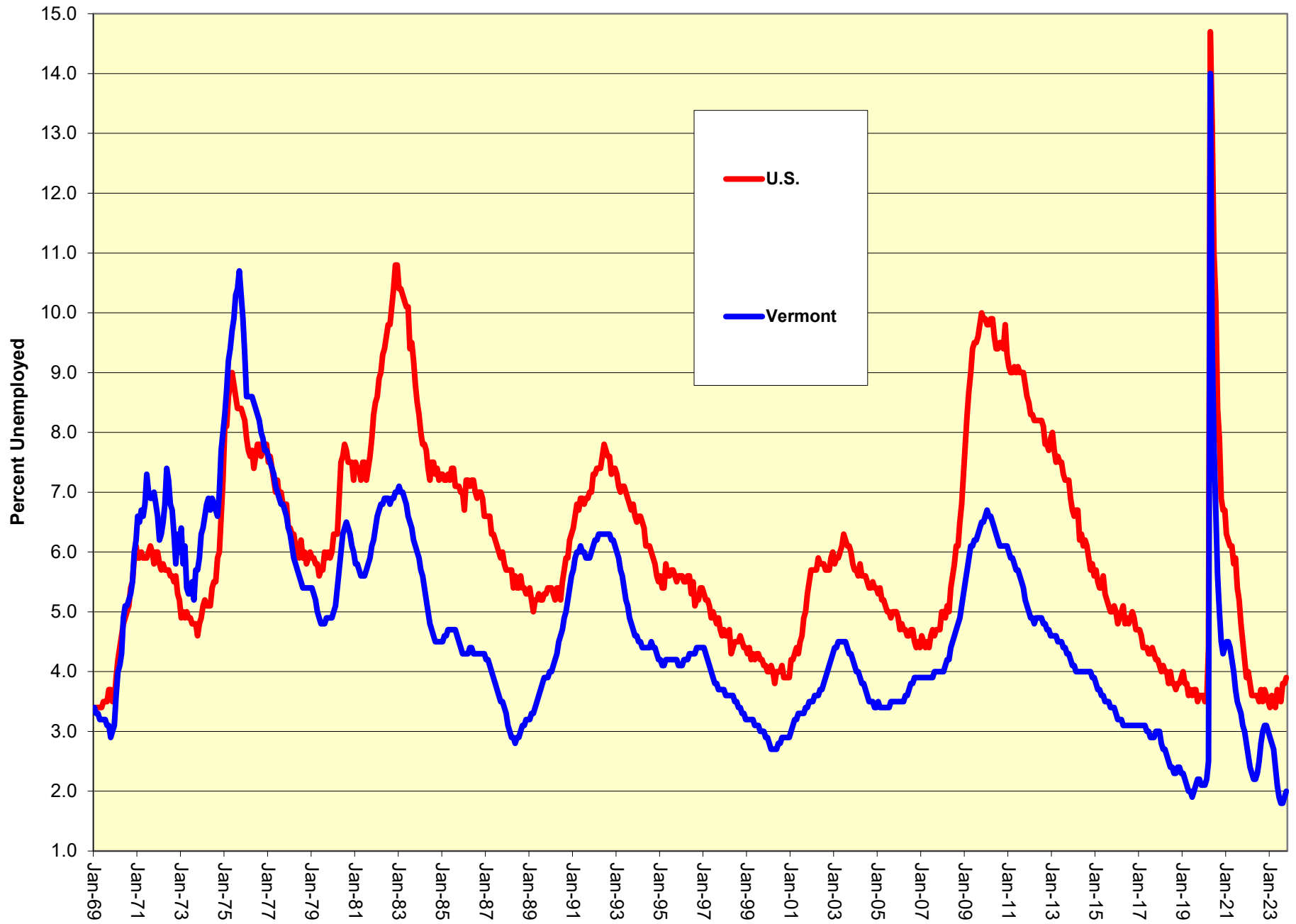
CPI-U - All Items, Source: U.S. Bureau of Labor Statistics, Not Seasonally Adjusted

Percent Change vs. Year Ago



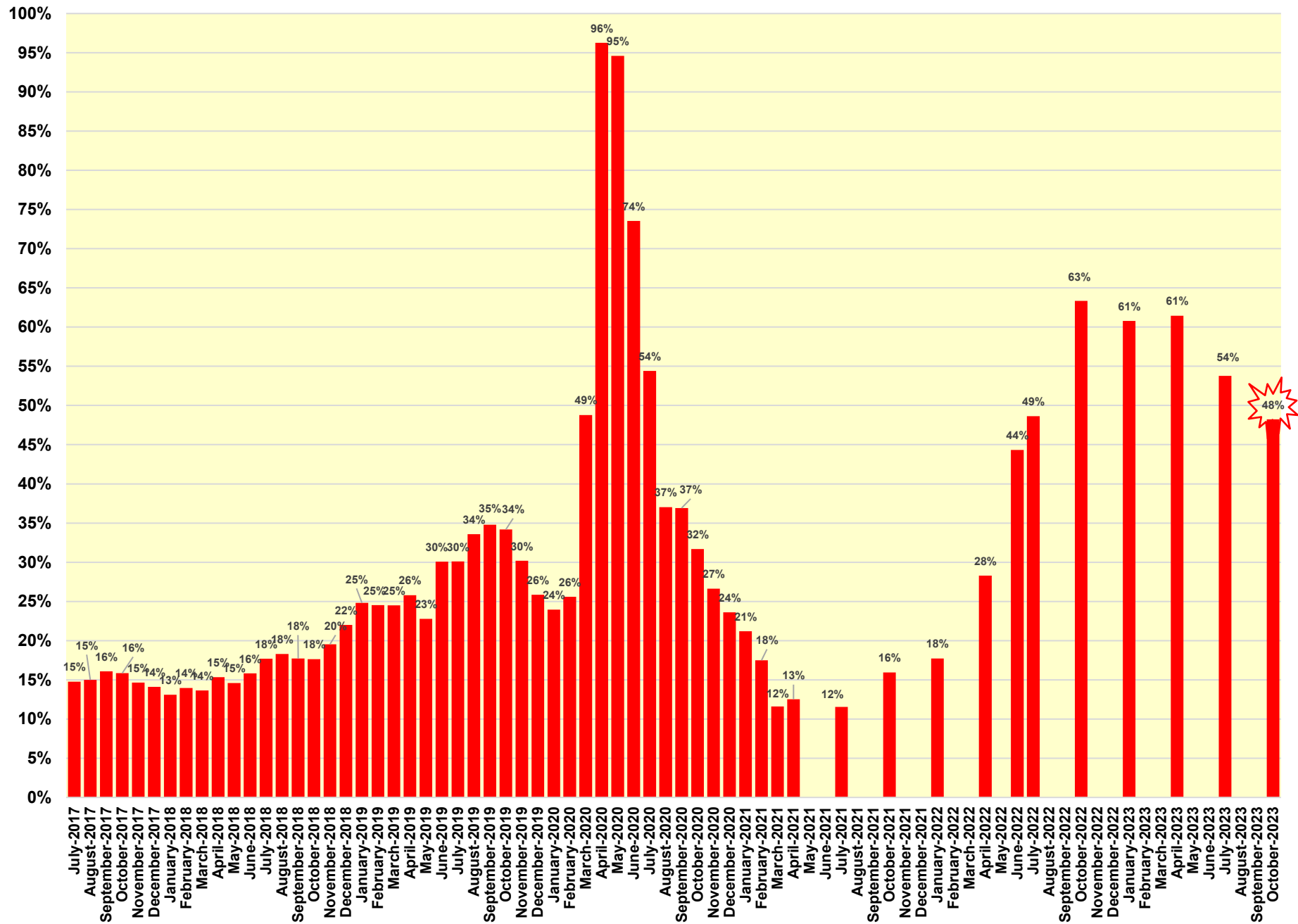
Unemployment Rates Begin to Rise After Reaching Historic Lows

(Seasonally adjusted data, Source: Bureau of Labor Statistics, U.S. Department of Labor)

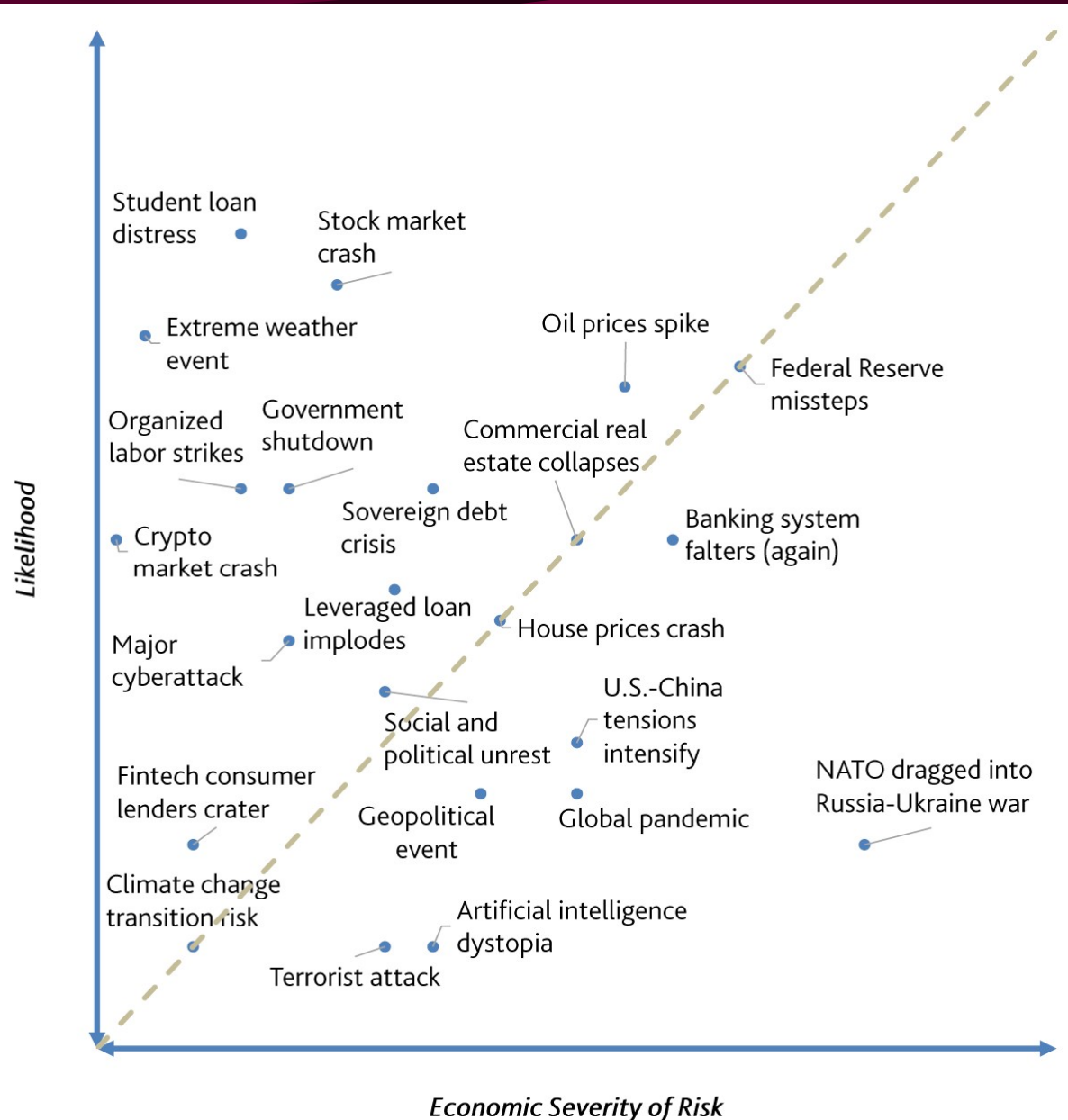


Near-Term Recession Risks Recede Slightly - Though Still a Coin Toss...

(Risk of Recession In the Next 12 Months - Source: Wall Street Journal Survey of 75 Economists)

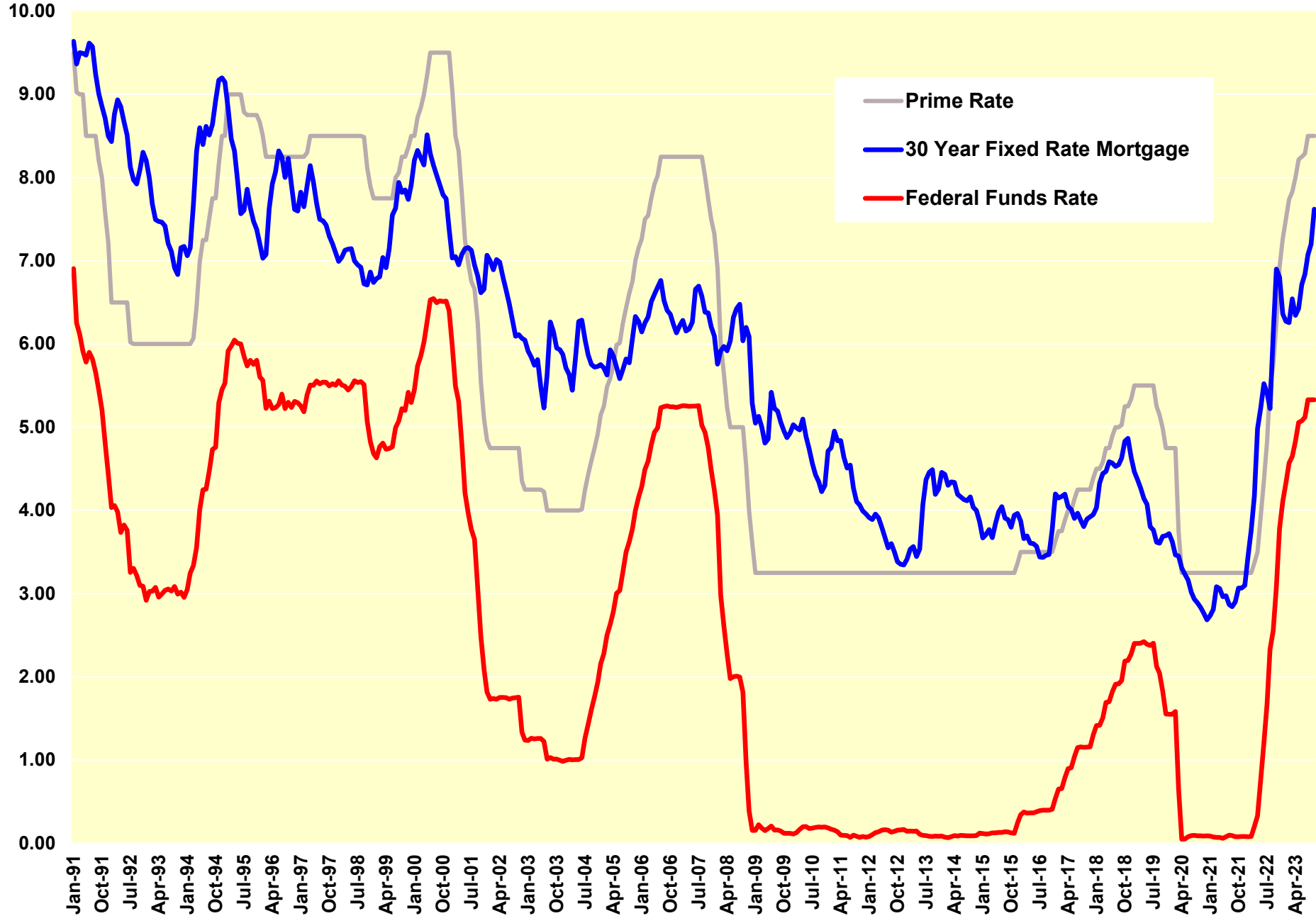


Moody's Matrix Outlines Some of the Forecast Risks



Fed Interest Rate Increases Choke Credit-Sensitive Sectors to Slow Economy and Tame Inflation

(Sources: Board of Governors of the Federal Reserve System, Freddie Mac)



High Interest Rates Impact Credit-Sensitive Sectors Dependent Upon Lending - Like Real Estate, Construction, Auto Purchases, Etc.

- While the initial effect of broad asset price appreciation, plentiful money and growing remote work has been to drive housing prices to record levels, the dependency of housing on lending has made it especially vulnerable to interest rate hikes. This has depressed home sales, new construction starts and pushed rental housing prices markedly higher.
- After some of the fastest growth on record over the past two years, house prices have slowed and are beginning to decline in some of the fastest growing states. New England (esp. northern) prices, which were slower to show gains in this cycle are now also lagging as price growth slows and declines, and have experienced some of the highest increases in the U.S. in the past few quarters. Vermont registered its highest year-over-year growth ever in the past four quarters, and growth in the second quarter of 2023 was the highest in the nation at 10.9%.
- Vehicle purchases have been dented by high borrowing costs, since 80% of new vehicle purchases and 40% of used vehicle purchases are financed. The APR rose to 7.4% for new vehicles in the 3rd quarter of this year and 11.2% for used vehicles. Average monthly payments reached a record \$736, as did the share of customers with a monthly payment of more than \$1,000 (17.5%).

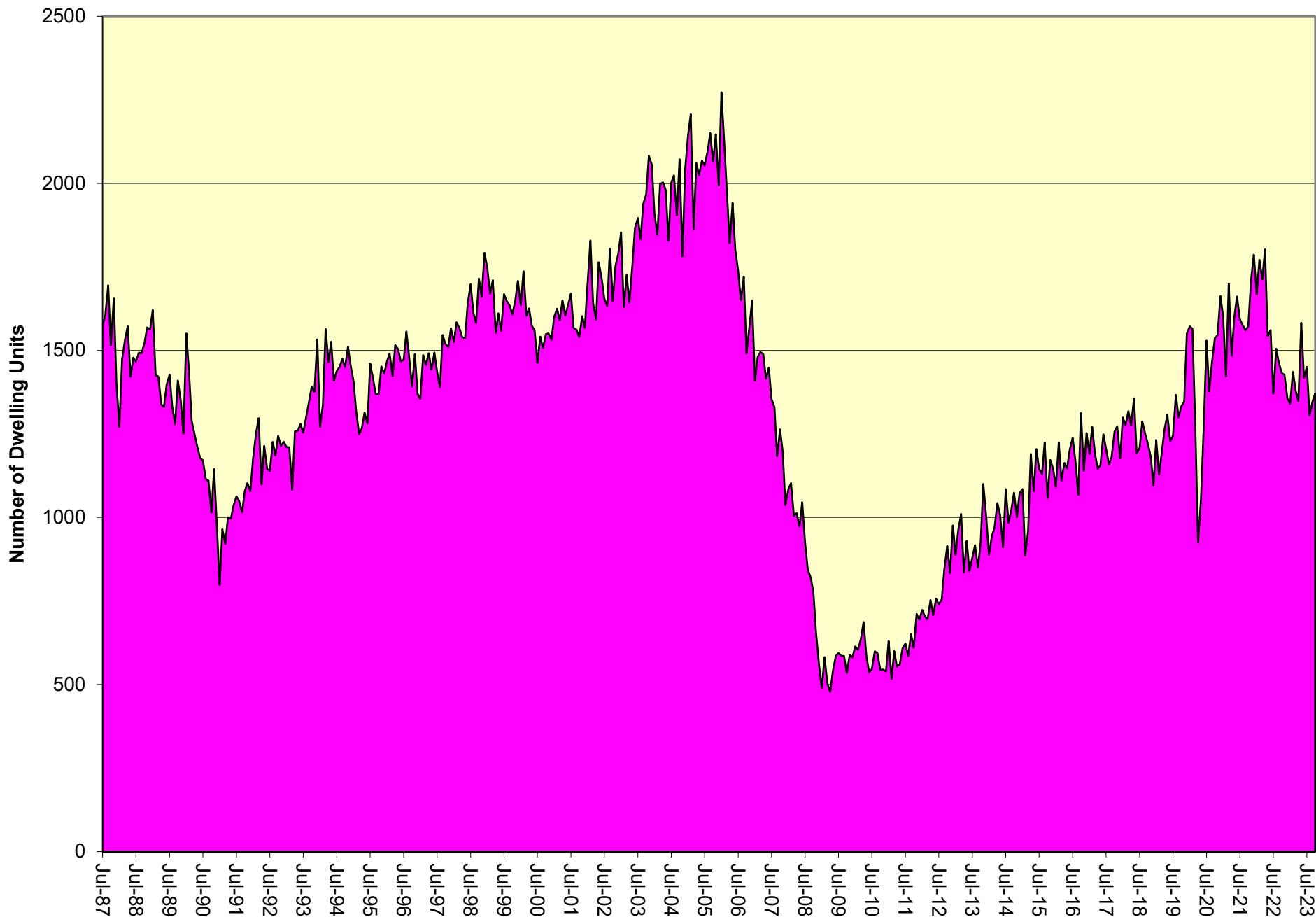
Low Inventories and High Interest Rates Still Limit Vehicle Sales and Related Revenues

(Domestic Auto Inventories, Source: U.S. Bureau of Economic Analysis)



U.S. Housing Starts Drop 27% From April 2022 as Soaring Mortgage Interest Rates Begin to Bite

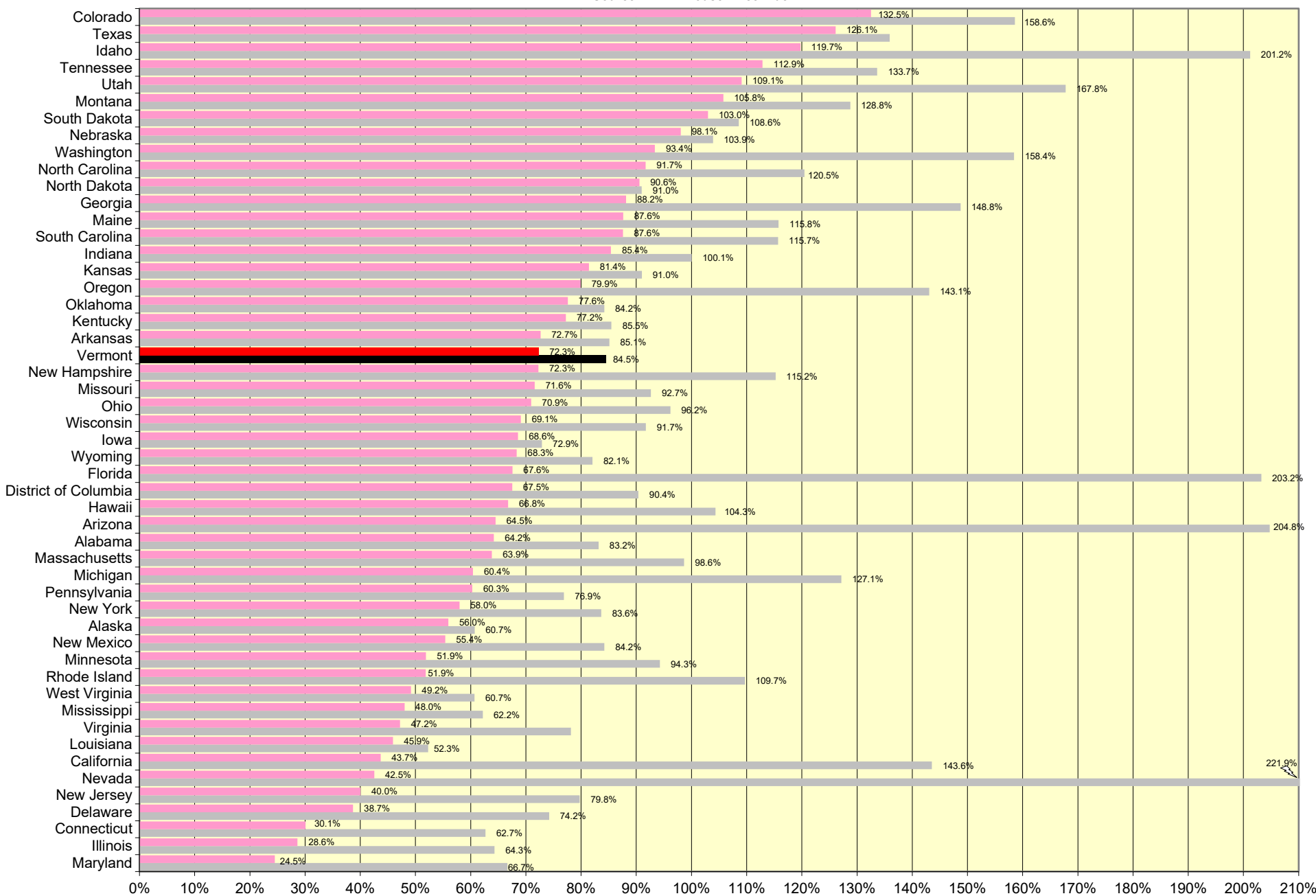
New Privately-Owned Housing Units Started, Source: U.S. Census Bureau)



Real Estate Update: Housing Values Relative to Last Peak (pink) and Trough (grey)

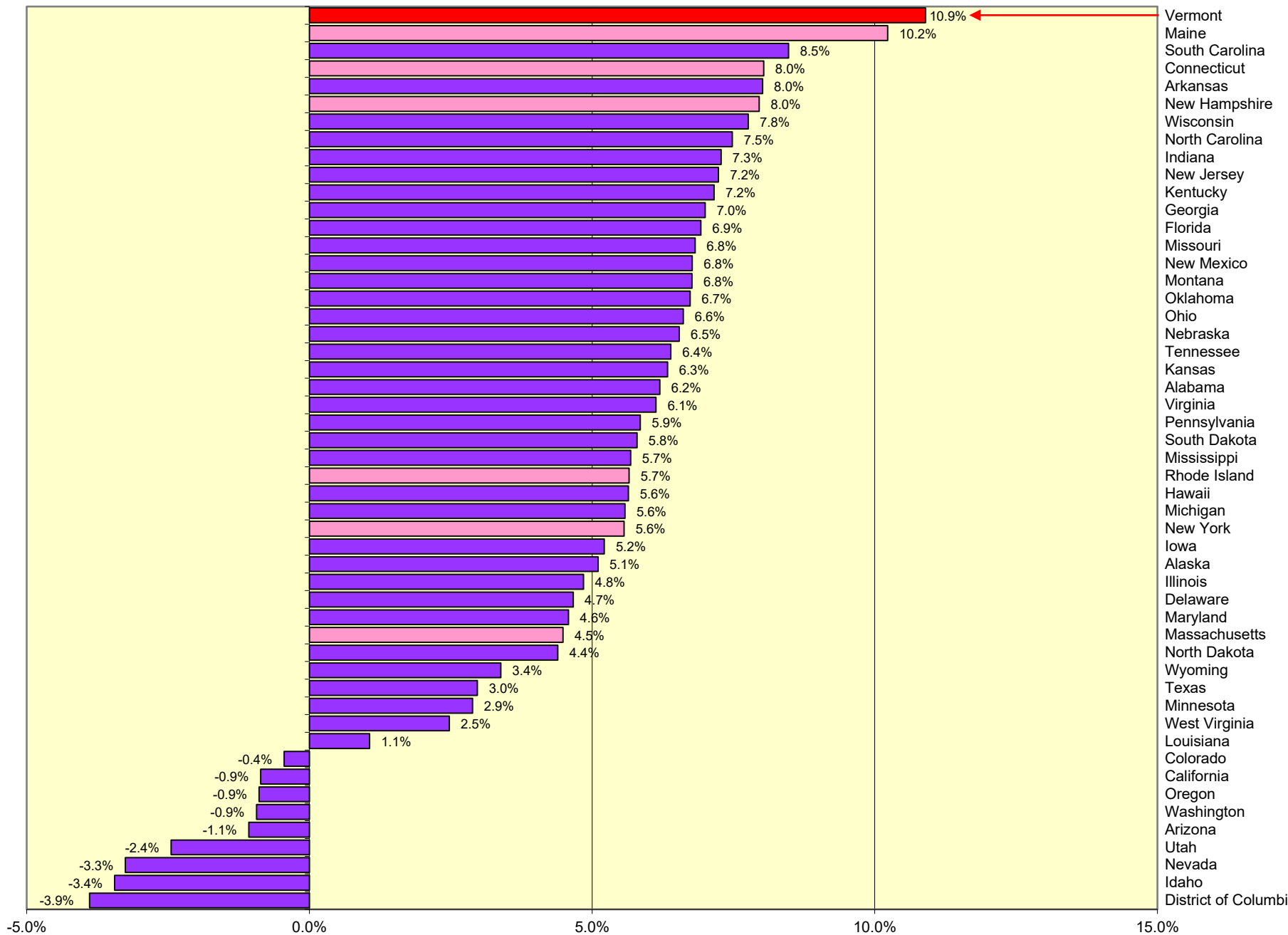
Percent Change, 2023Q3 vs. Peak Price by State Between 2005Q3 and 2009Q3 (Pink) and 2023Q3 vs. Trough Price Between 2009Q3 and 2014Q1 (Grey)

Source: FHFA House Price Index

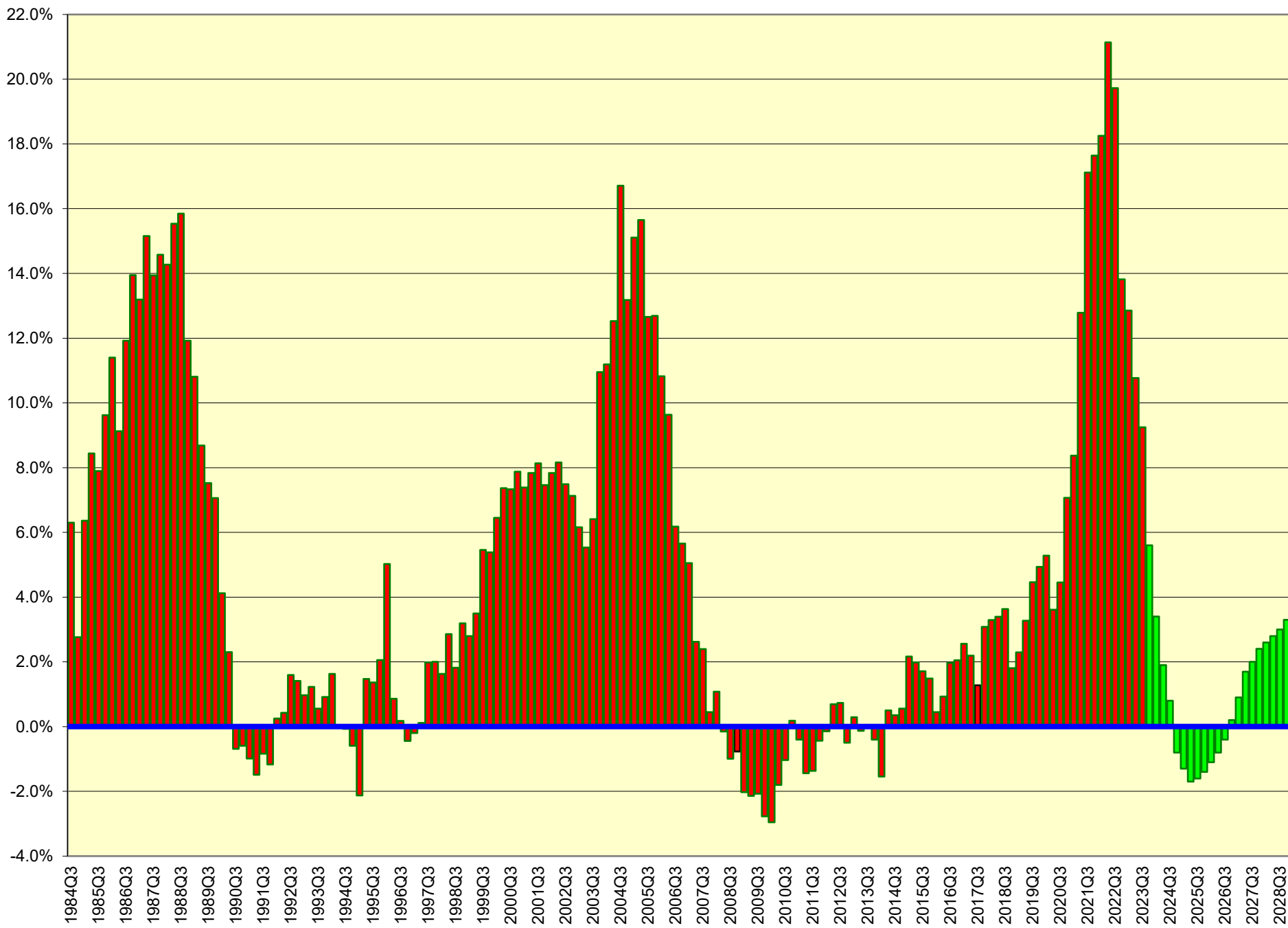


Northern NE Home Price Growth is Now Among the Strongest in the Nation

Percent Change, Second Quarter of 2023 vs. Second Quarter of 2022, Source: FHFA House Price Index



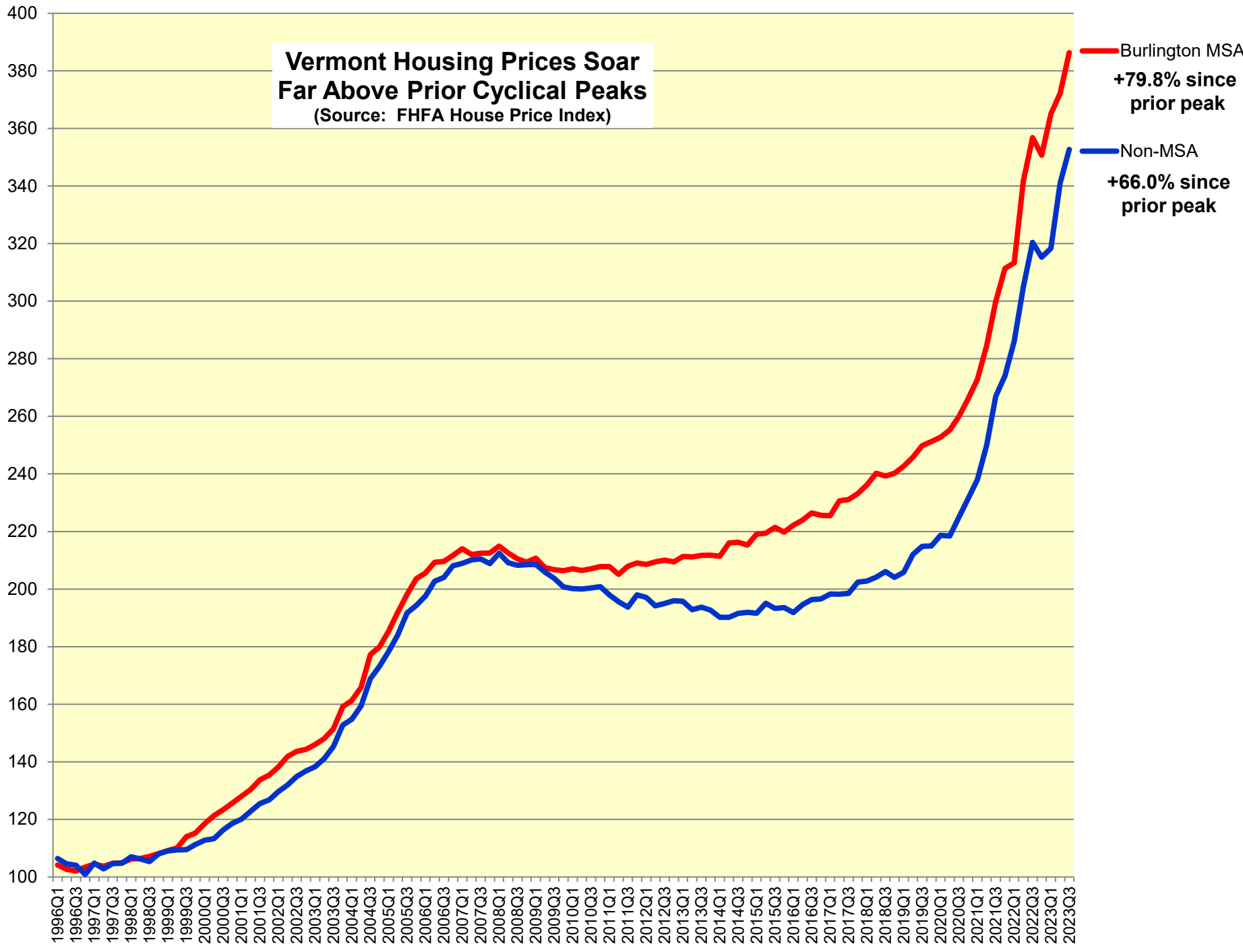
Vermont Home Price Growth Recedes from its Highest Rates Ever
(FHFA Vermont Housing Price Index Percent Change Vs. Year Ago, Historical Data - Red, JFO Forecast Data - Green)



FHFA Home Price Index, 1995Q1 = 100

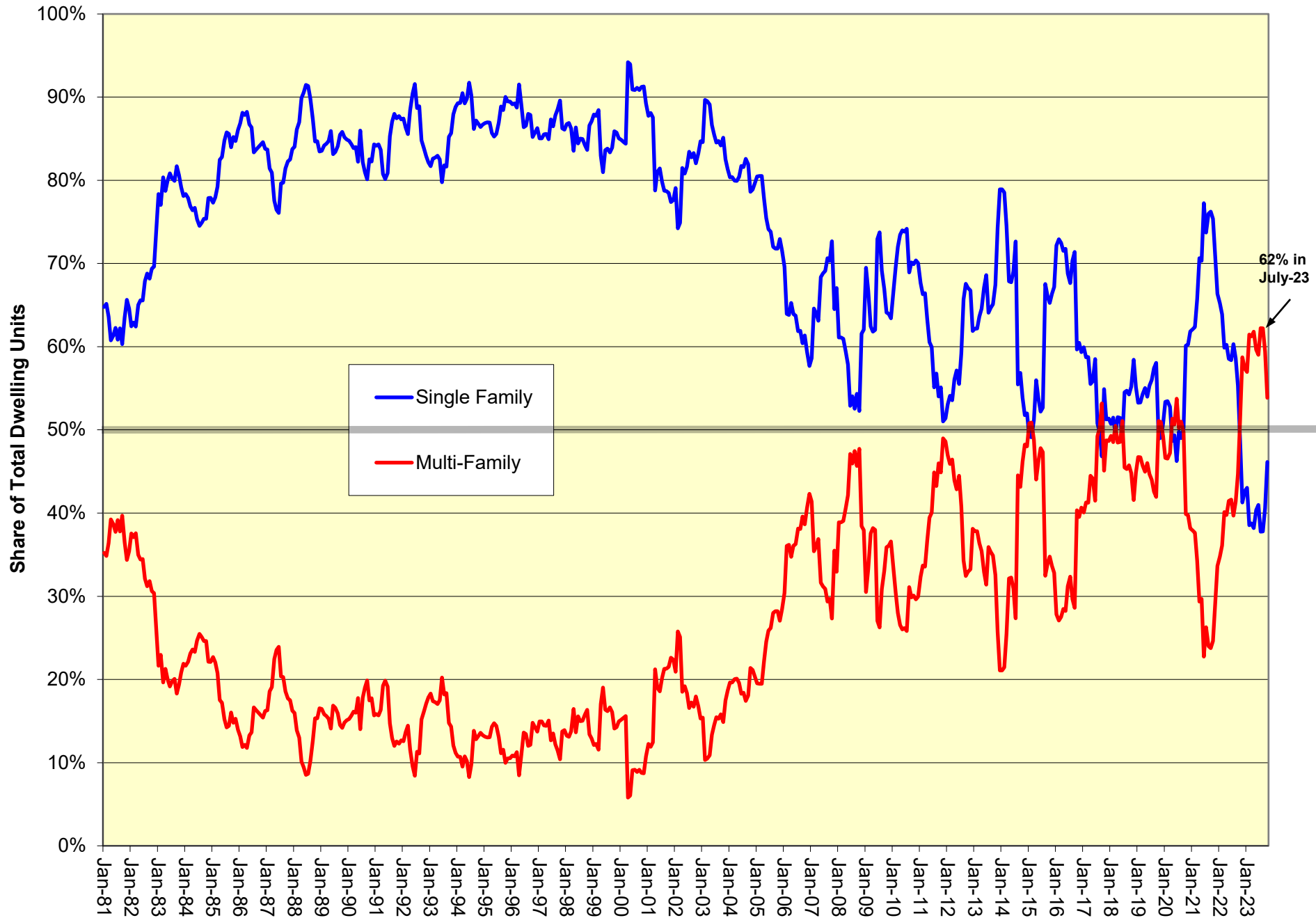
Vermont Housing Prices Soar Far Above Prior Cyclical Peaks

(Source: FHFA House Price Index)



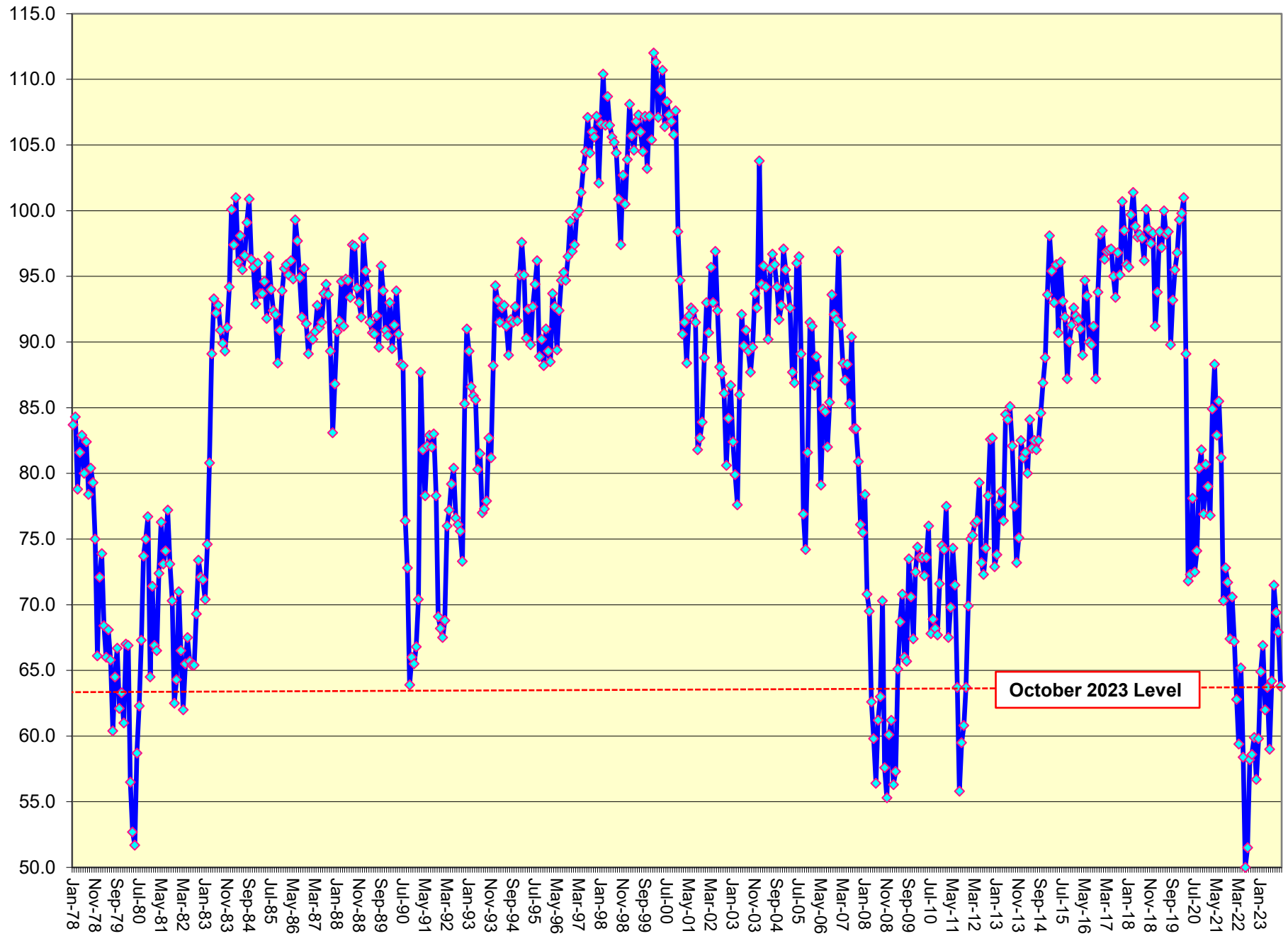
Most New Vermont Residential Construction is Now Apartments, Not Single Family Housing

(Vermont Residential Housing Starts, Shares of Dwelling Units, 12 Month Moving Totals, Source: Dodge Data and Analytics)



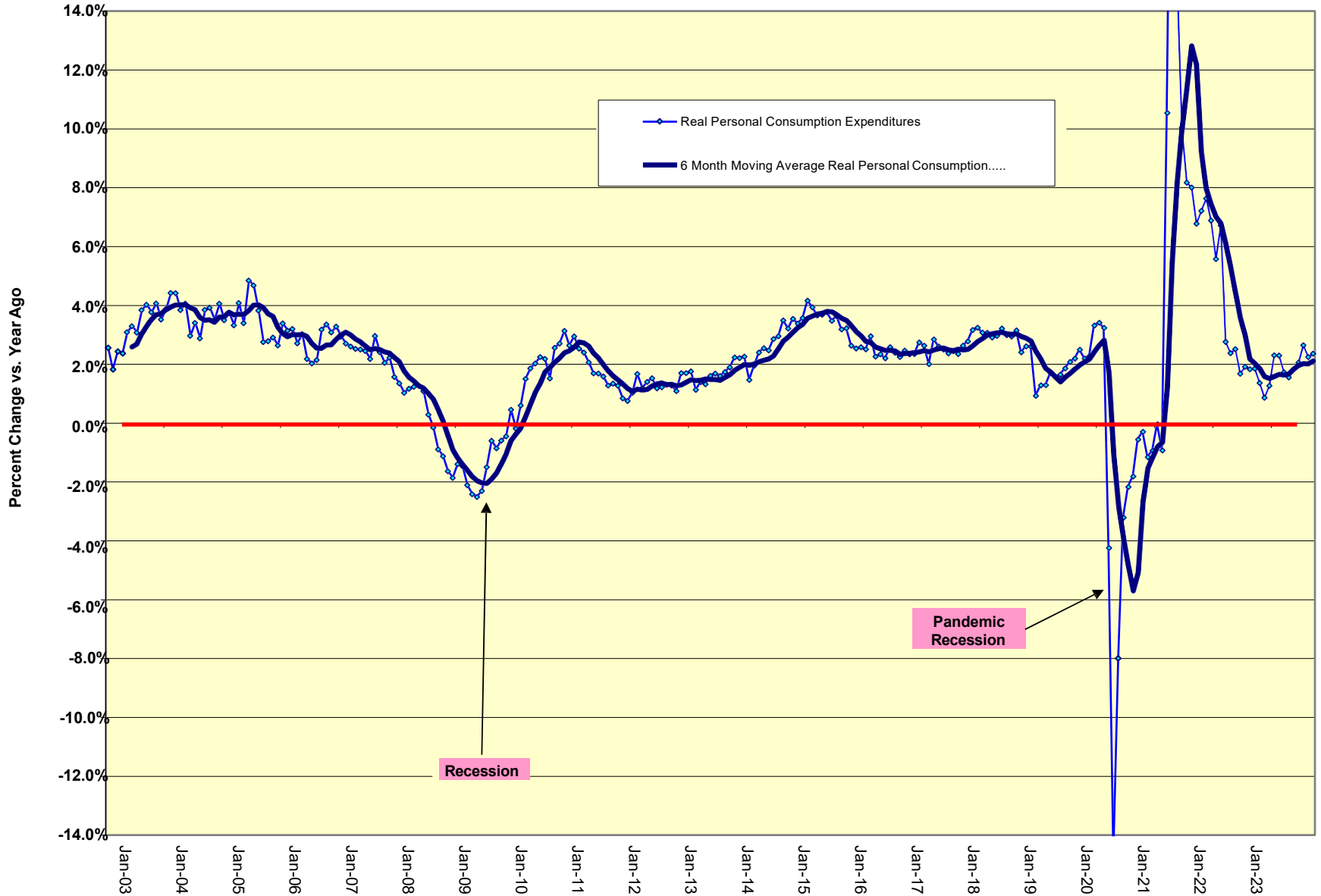
Consumers Report Extreme Pessimism, But It Doesn't Show in Their Spending

(University of Michigan Survey, Index of Consumer Sentiment)



Despite High Inflation and Widespread Pessimism, Consumers Keep Spending

Total Constant Dollar Personal Consumption Expenditures - Percent Change from Year Ago, Source: U.S. Census Bureau



ECONOMIC NEWS

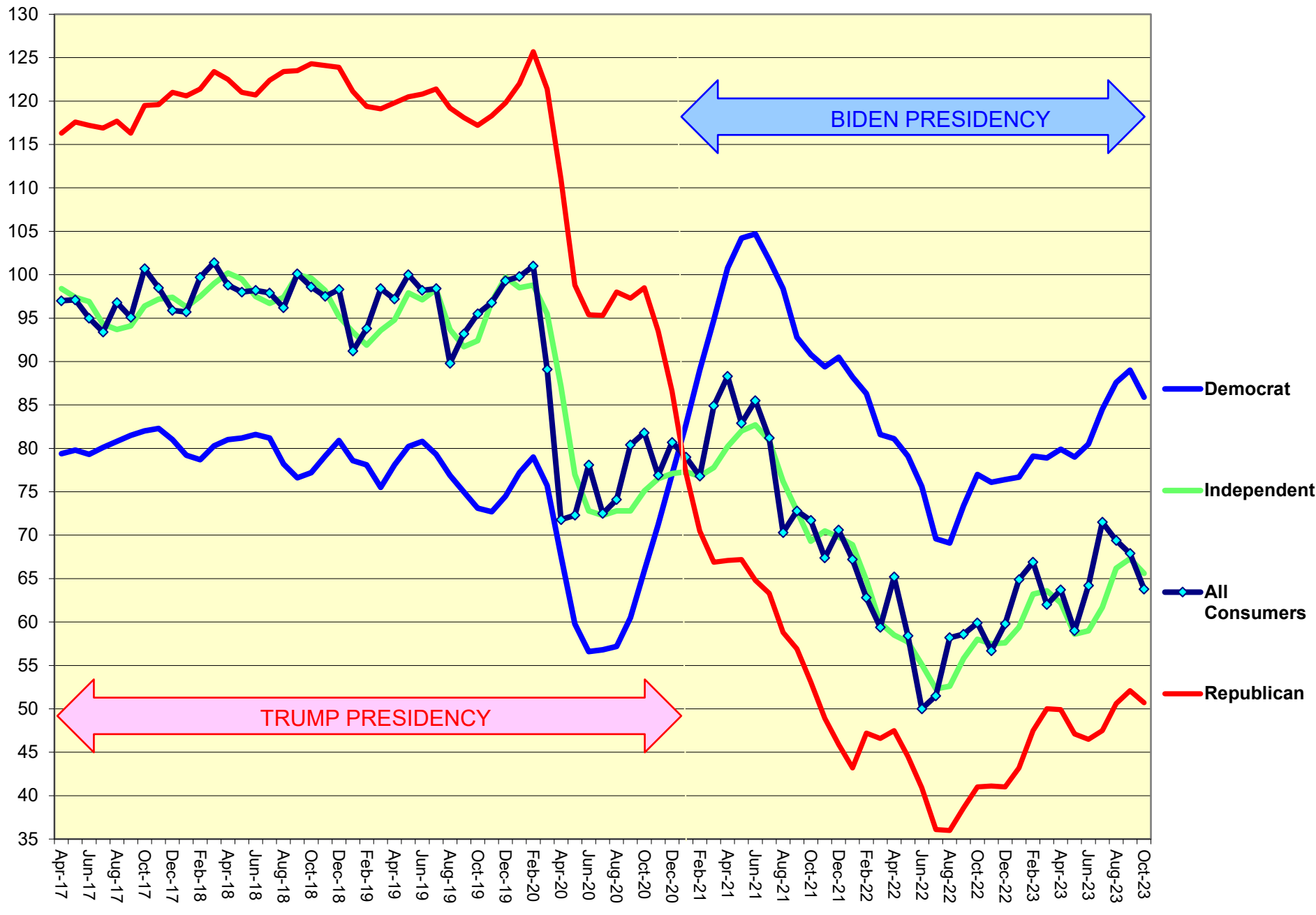
- FALLING INFLATION
- BOOMING LABOR MARKET
- RAPID GROWTH

BUT THE ECONOMY STILL STINKS!



Party Affiliation Now Controls Consumer Sentiment More Than Economic Fact

(University of Michigan Consumer Sentiment Survey)

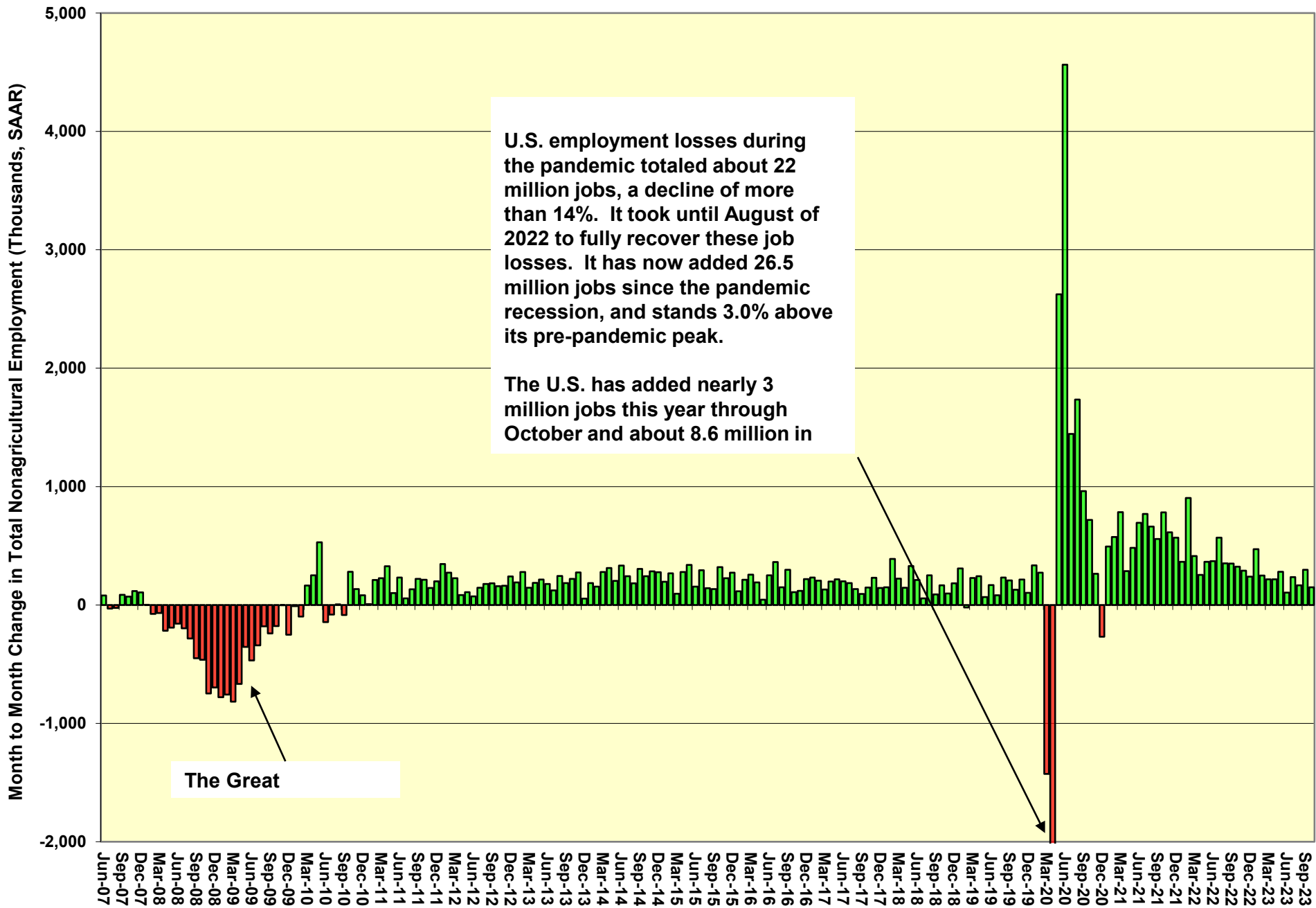


Despite Slowing Job Growth, Labor Markets Remain Tight, Shifting Power to Workers and Raising Concerns About Wage-Price Spirals

- Job growth has appreciably slowed, but has landed in a “Goldilocks” spot where growth is still solid, though not so strong as to motivate further Fed interest rate increases.
- Unemployment rates have ticked up, but are still at historically low levels – especially given persistently high interest rates and declining inflation
- Labor force participation has been rising, but is still well below pre-pandemic levels, especially among older workers.
- Although narrowing over the past 9 months, there are still substantially more job openings than unemployed persons at both the Vermont State and Federal levels
- Wage growth has been slightly above headline inflation, but unionized sectors of the economy have been successful in extracting much larger multi-year compensation gains through strikes and other labor actions

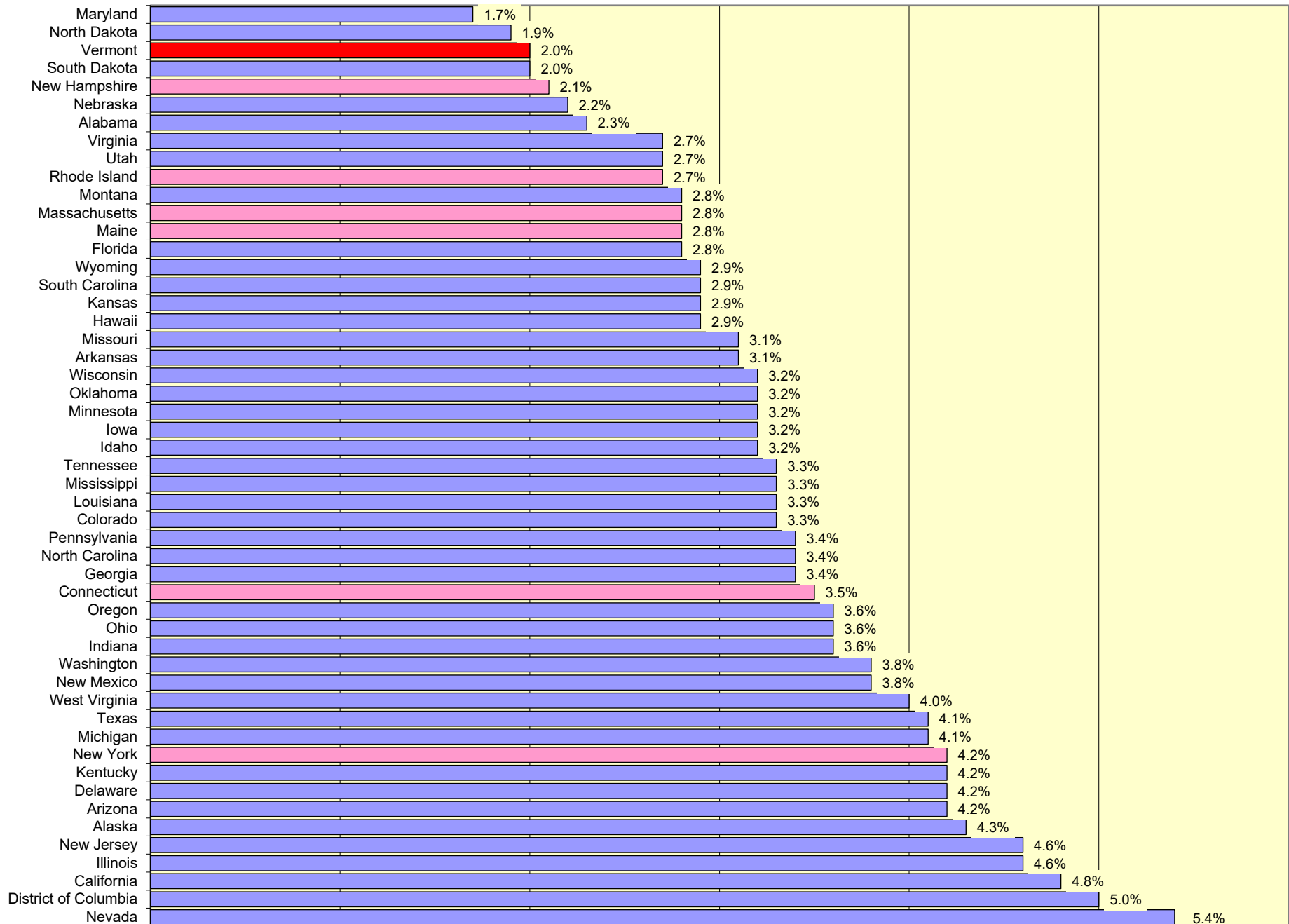
U.S. Employment Continues Steady Growth Despite Interest Rate Headwinds

Monthly Change in Total U.S. Payroll Employment, Seasonally-Adjusted, Source: U.S. Bureau of Labor Statistics



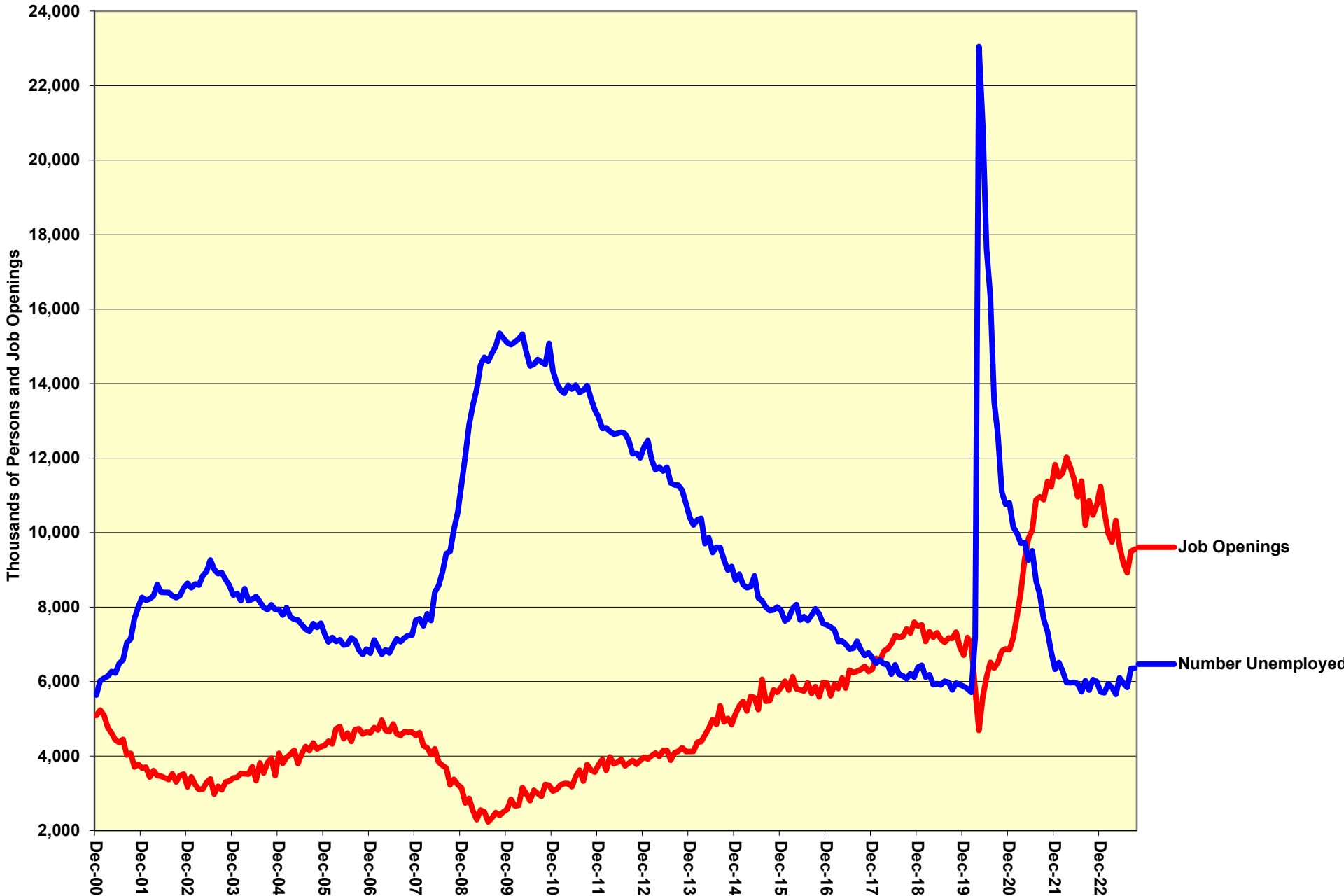
Unemployment Rate by State - October 2023

Seasonally Adjusted Data, Source: U.S. Bureau of Labor Statistics



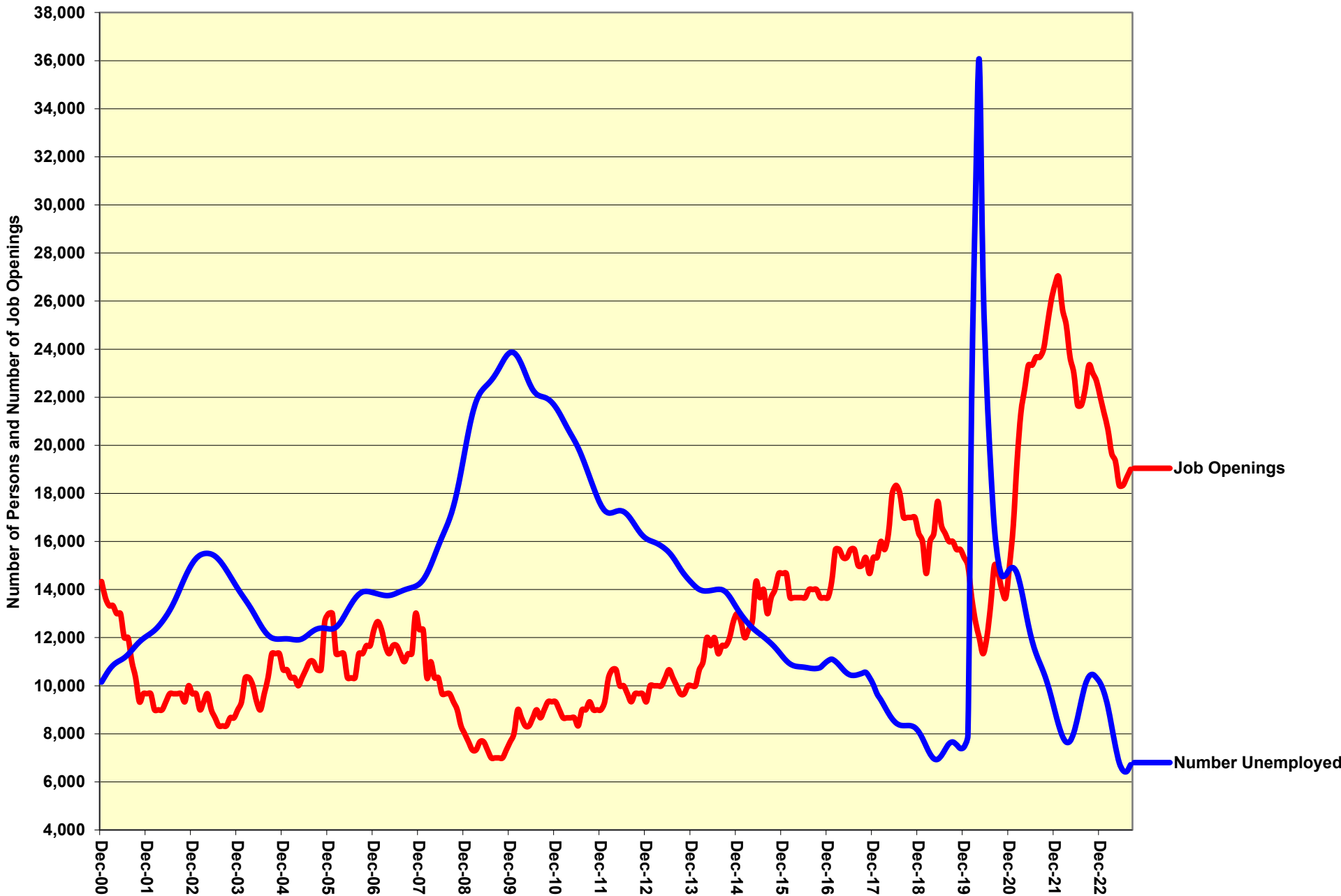
Labor Markets Remain Tight, With More Job Openings Than Unemployed Workers

(Seasonally adjusted data, Source: Bureau of Labor Statistics, U.S. Department of Labor)



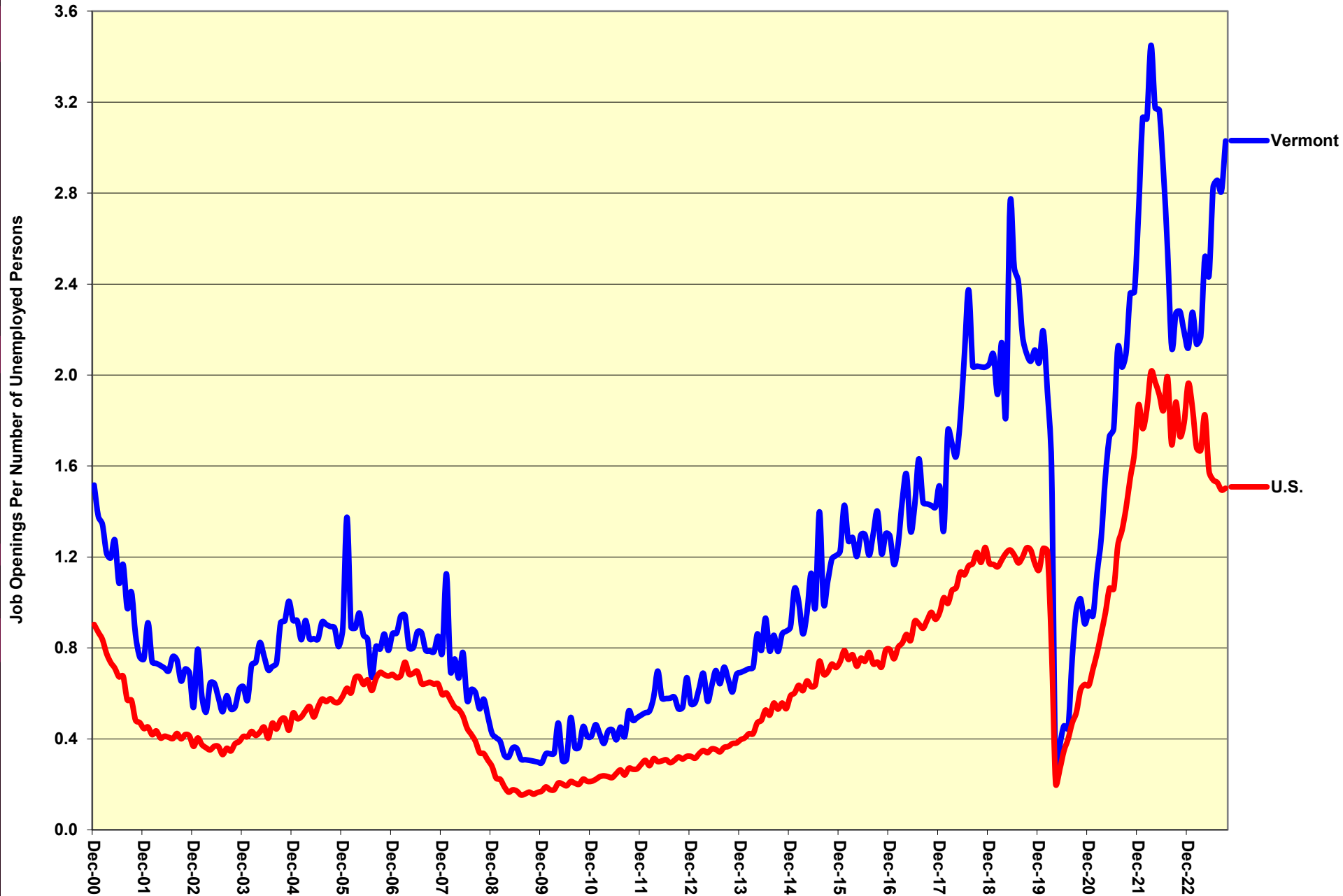
Yawning Gap Between Job Openings and Unemployed Workers Persists in Vermont

(Seasonally adjusted data, Source: Bureau of Labor Statistics, U.S. Department of Labor)



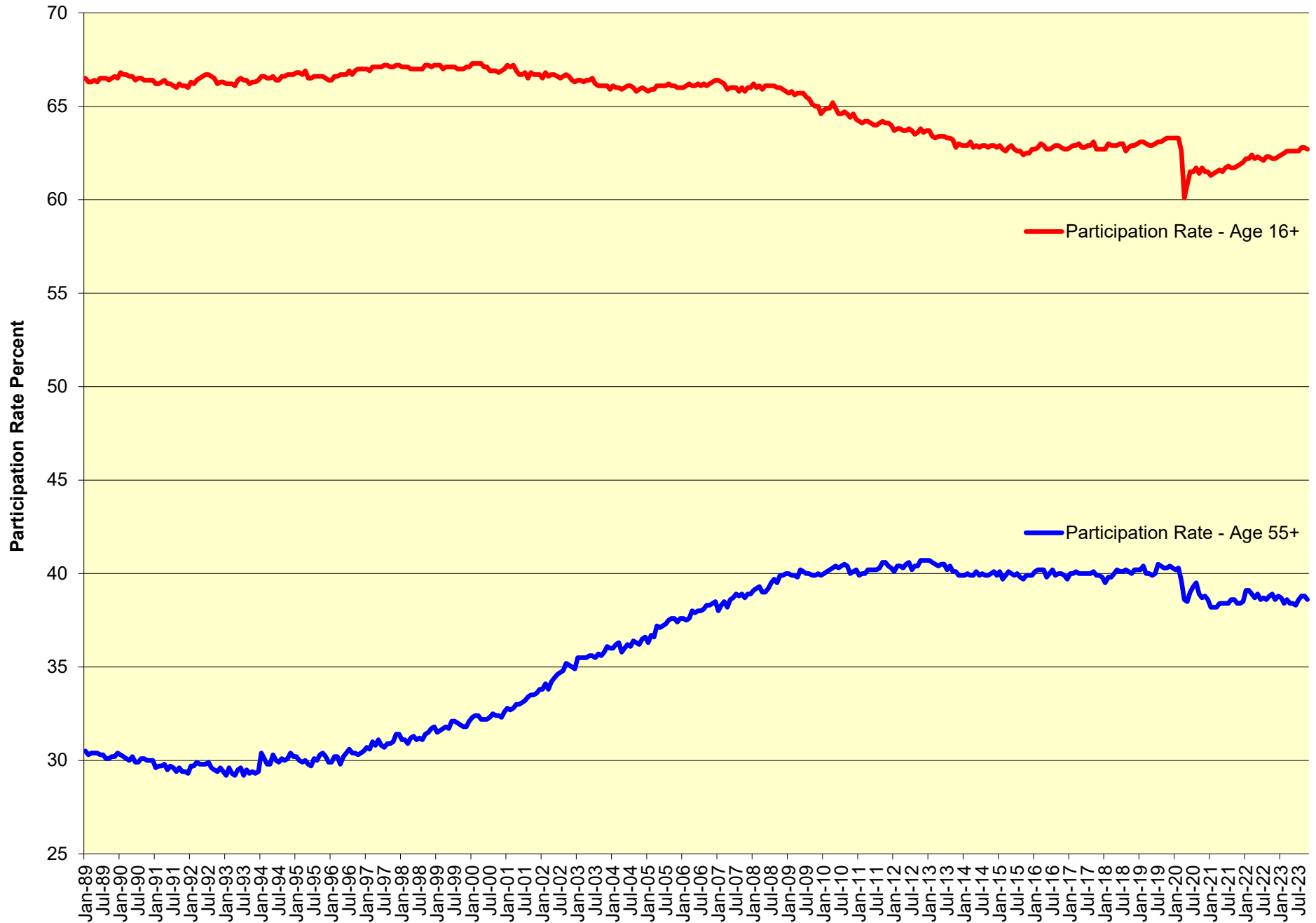
With Three Job Openings for Every Unemployed Worker, Vermont Far Exceeds U.S. Ratio

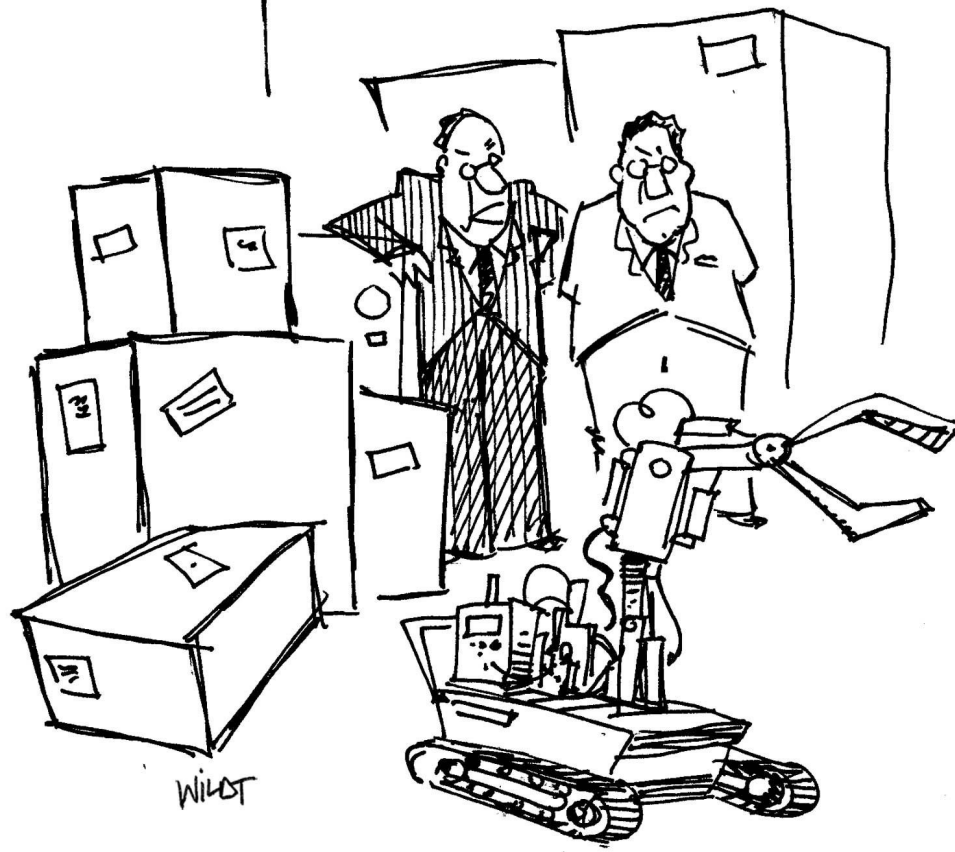
(Seasonally adjusted data, Source: Bureau of Labor Statistics, U.S. Department of Labor)



Post-Pandemic Loss of Older Workers Dampens Overall Labor Force Participation Rate

(Source: U.S. Bureau of Labor Statistics)





"We use intelligent robots, but not too intelligent because they'd want a union."

Recent Boston Fed Study Could Help Focus State Efforts to Enhance Population Growth

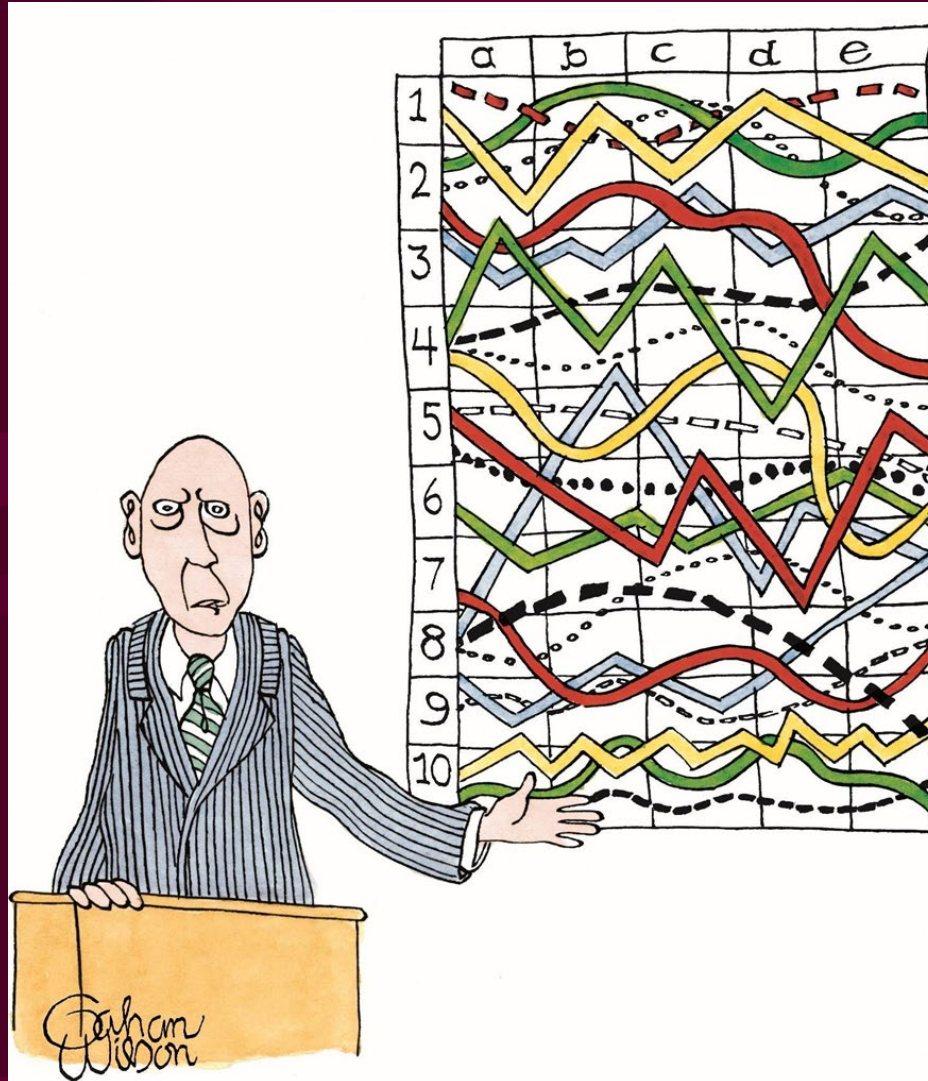
Regional Brief | 2023-1 Recent Migration and Visa Trends in New England and Implications for the Labor Market

Table 1: Population Changes by Nativity
United States and New England states, 2010–2021

	Total Population		Foreign-born Population		Population Change Excluding Foreign-born Residents	Share of Total Population Growth from Foreign-born Residents
	2010	2021	2010	2021		
US	309,349,689	331,893,745	39,955,854	45,270,103	6.4%	24%
NE	14,457,499	15,092,739	1,747,987	2,101,631	2.2%	56%
CT	3,577,073	3,605,597	487,120	549,441	−1.1%	218%
ME	1,327,567	1,372,247	45,666	56,068	2.7%	23%
MA	6,557,254	6,984,723	983,564	1,227,488	3.3%	57%
NH	1,316,759	1,388,992	69,742	82,127	4.8%	17%
RI	1,052,886	1,095,610	134,335	159,304	1.9%	58%
VT	625,960	645,570	27,560	27,203	3.3%	−2%

Source(s): Author's calculations using American Community Survey: 1-year data, 2011–2021.

Questions?



*"I'll pause for a moment so you can
let this information sink in."*

For Further Information, Contact The Vermont Joint Fiscal Office or:

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