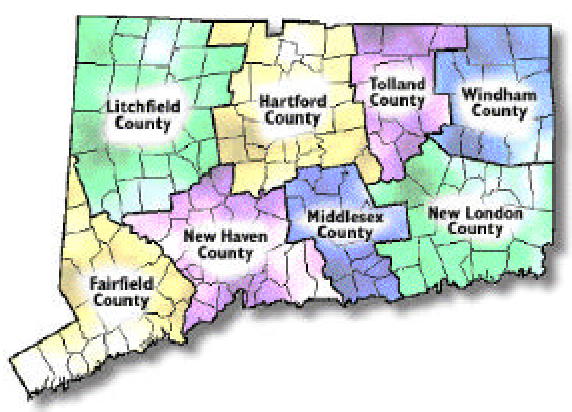
CONNECTICUT

CONNECTICUT ECONOMIC CONFERENCE BOARD

Report to the Governor and General Assembly

2000



The Connecticut Economic Conference Board
Annual Report 2000

Table of Contents

Connecticut Economic Conference Board
Executive Summary

In order to fulfill its legislative mandate, the Connecticut Economic Conference Board held a public hearing on November 19, 1999. Economic experts and representatives of the public and private sectors provided analysis and comment. The following is a summary highlighting major issues raised during the course of the day.

Connecticut's Economy

Jobs-Currently the state unemployment rate is at 2.7 percent. Unemployment should be approximately 3 percent for the coming year. The state faces a very tight labor market. Although the problem of out-migration has slowed somewhat, we are still experiencing negative net migration. In addition, slow population growth is leading to slow growth in the labor force. Going forward, the rate of job growth will continue to exceed the growth rate of the labor force. The resulting shortage of workers will hamper the state economy's ability to grow.

A number of major corporate restructurings and job cuts are currently underway. Connecticut added 32,000 jobs in 1998 and will add approximately 22,000 in 1999. That number is expected to decline to 12,000, however, in 2000. Factors affecting job growth include the effect of higher interest rates and a shortage of qualified workers.

High Incomes-Job income and output will continue to rise but more slowly. The vast majority of economists do not anticipate a recession in the coming year. Currently, per capita income in Connecticut is roughly $40,000, the highest in the nation. Labor productivity is high and increasing.

Interest Rates-The Federal Reserve raised interest rates three times in 1999. The Fed continues to be very concerned about low unemployment nationwide and its possible inflationary effect on wages. The Fed also feels that the current national growth rate in excess of 3 percent is not sustainable long term. Thus, it is very likely that we will see continued interest rate increases in the New Year. This will affect corporate profits and may trigger a long anticipated stock market correction.

E-commerce-The rise of e-commerce will have an effect on retail jobs and on state tax collections. Estimates of tax losses to e-commerce in 1998 range from $6.5 million to $100 million. Currently a national commission is addressing the problem of the state sales tax exemption on internet sales.

Loss of a Congressional Seat-After the next census, Connecticut, like several other Northeastern states, will probably lose a Congressional seat due to the combined effects of negative net migration and slow population growth. This will reduce our ability to influence policy and the allocation of resources at the national level.

The U.S. Economy

Monetary Policy-The Federal Reserve is concerned that the national economy is expanding in excess of its growth potential. The pool of available workers has declined relative to jobs, a trend that may lead to inflationary imbalances. If the Fed continues to raise interest rates in the coming year as anticipated, it will eventually lead to higher unemployment thereby reducing upward pressure on wages.

The Stock Market-The stock market, and particularly technology-driven stocks, has reached historically high levels of valuation. This carries with it the risk of a correction. At present foreign capital attracted to the U.S. stock market is financing our trade deficit. If the market drops, that capital will move to other markets making the trade deficit a more pressing concern.

The International Economy

Global Markets-1997 and 1998 were turbulent years in world markets, particularly in Asia and South America. 1999 has been a year of healing, and it appears that we are moving toward faster growth worldwide. Continued growth in most world markets for the coming year will place pressure on prices in the United States. In recent years the prices of imported goods has fallen at a rate of 2 percent per year. As other nations begin to grow more rapidly, we will be competing with them for goods leading to price increases.

The fact that the U.S. has been growing faster than other parts of the world has also helped us to attract capital from other countries. This has allowed our economy to grow while simultaneously keeping interest rates low. As growth accelerates in other countries, we will face a more competitive capital market.

Oil Prices-The price of oil has doubled within the last year. This increase has been caused by two factors. First, the oil producing countries have constrained supply. Second, the recovery in Asia has led to an increase in world demand. Since constraints on supply and increasing demand are expected to continue, it is very likely that we will experience further price increases. This can lead to general inflation and is particularly problematic for the Northeast which is heavily dependent on oil.

Instability-The international environment has been unstable for some time. Problems in Asia have not been fully resolved, and conditions there remain uncertain. There is also uncertainty surrounding the nature of China's participation in the World Trade Organization. If there are threats or surprises on the economic horizon, they are most likely to occur in the international arena.

Dr. Ed Deak
Fairfield University
The New England Economic Project's Connecticut Outlook

Overall-Connecticut is doing "marvelously". The economy is strong and growing with continued, but somewhat slower, growth expected through 2000 and beyond.

Gross State Product-Real GSP is increasing, although not as rapidly as in the past. Incomes are strong, roughly $40,000 per person; the highest in the nation. Output per worker or labor productivity is also high and increasing. The problem of out-migration has slowed somewhat, but we are still experiencing negative net migration. After the next census, Connecticut, along with several other states in the Northeast, will probably be forced to surrender a Congressional seat due to slow population growth.

Jobs-Currently the state unemployment rate is at 2.7 percent. Unemployment should be around 3 percent for the coming year. The state faces a very tight labor market; only about 35,000 eligible workers are unemployed. Slow population growth leads to slow growth in the labor force. Going forward, the rate of job growth will continue to exceed the growth rate of the labor force, and a shortage of available workers will hamper the state economy's ability to grow.

Another factor affecting jobs will be a major restructuring of United Technologies Corporation which employs 26,000 in Connecticut. UTC is cutting back by about 1100 employees at the Sikorsky division in Stratford and West Haven. Half of these cuts took place in 1999 with the balance anticipated in 2000.

Pratt and Whitney Aircraft, another division of UTC, is also going through a major reorganization which will move some work out of the state. At the same time, however, engineering activities currently located in West Palm Beach to will move to East Hartford. The net effect of these changes is difficult to gauge.

The merger of UTC's Hamilton Sundstrom will cost the state about 600 jobs. Changes are also underway at the Carrier Division and Otis Elevator, both of which have headquarters operations in Connecticut.

Employment growth will begin to slow in the coming year. The state added 32,000 jobs in 1998 and will add about 22,000 in 1999. That number is expected to decline to 12,000 in 2000. Major factors affecting job growth will include the effect of higher interest rates and the shortage of qualified workers.

Overall, continued job losses are anticipated in manufacturing. The state will lose around 8,000 manufacturing jobs between 1999 and 2003. Construction employment will grow modestly. The transportation and utility sector which includes SNET, recently acquired by SBC, and Northeast Utilities, currently in merger talks, will experience a slight decline. Wholesale and retail trade will add about 20,000 job through 2003. This figure may be higher if the Galleria Mall in New Haven becomes a reality and adds an anticipated 3,000 retail jobs. The government sector, which includes Indian reservation employment, is expected to add about 8,000 jobs. Three thousand of these will come from an $800 million addition at the Mohegan Sun Casino. Foxwoods has also recently completed an addition that will result in additional jobs. Our major job gains will again come from the services sector, particularly health services and business services, both of which have become increasingly important to the state.

In terms of net job gains and losses, we have reached the point in the economic recovery where recent announcements of job cuts are beginning to outnumber announcements of job gains. Bayer, SNET, and Peoples' Banks are among the companies that have announced anticipated job gains. Lincoln National, Automatic Rolls, Citibank, Pfizer, and Rainbow Growers are also in the process of filling jobs.

The Torrington Company, Ensign Bickford, Oxford Health, Mass Mututal, EIS Brake, Wyman Gordan, the Pequot Shipyard, the UCONN Health Center, Colt Manufacturing, A.C. Molding, and Napier Jewelry have all announced or experienced job reductions. Further anticipated cuts may come from Electric Boat, Emhart, Stanley, Lego, Relistar, C.R. Gibson, and Hartford Hospital.

Housing-Housing permits will decline slightly but will remain strong. This is a good sign in light of the anticipated trend of rising interest rates. Housing has benefited from the wealth effect created by good job opportunities, high incomes, and strong asset growth. Driven by strong demand, housing prices have increased noticeably over the last 18 months to two years.

Interest Rates-The Fed will not raise rates at the end of 1999 due to Y2K concerns. It is very likely, however, that rates will be increased in the first quarter of the New Year. The Fed is increasingly concerned with the speculative nature of the stock market and by the possible inflationary effects of very low unemployment rates. In addition, the current national growth rate in excess of 3 percent is not sustainable long term.

The Stock Market-In all likelihood, rising interest rates will trigger a stock market correction. Corporate profits will not be as strong due to higher rates and increasing foreign competition.

E-commerce-The rise of e-commerce will have an effect on retail jobs and also on state tax collections. Estimates of sales tax losses to e-commerce in 1998 approximate $ 6.5 million. If electronic retailing explodes, as is anticipated, the tax loss to the state could be substantial going forward. In 1998, the U.S. Congress passed the Internet Tax Freedom Act, which placed a ban on the collection of Internet related sales taxes for a three- year period. Currently, a commission is working at the national level to try to deal with the problem of the federal exemption of state sales tax on interstate sales of goods electronically. There should be some resolution to this issue within the next few years that will close the tax loophole for people buying goods electronically.

The longer term impact of e-commerce is immense. Electronic retailing is growing rapidly, but business-to-business sales are five times retail sales and growing at even a faster pace. It is estimated that business-to-business sales will reach $180 billion per year by 2001.

Risks-Domestic and global disruptions associated with Y2K represent a threat to this forecast. Although domestic problems have been identified and addressed for the most part, individual companies may experience various types of problems. Globally, the issue is larger. Less developed countries are much more likely to experience significant problems.

A second risk, particularly for Connecticut, is slow population growth and continued negative net migration. Every one of Connecticut's ten labor markets has an unemployment rate below 3 percent. The lack of qualified workers will hamper the state's ability to grow.

The price of oil is a threat. Currently, oil is about $26 per barrel, double what it was last year. Connecticut is a very oil dependent state that uses oil for both home heating and manufacturing. Thus, price increases in this area will affect the affordability of housing and the cost of manufactured goods.

There is the risk of employment cutbacks at major state employers, particularly Electric Boat which has fewer orders and Pratt and Whitney as orders for Boeing planes subside. It is also unclear whether the two Indian casinos will be able to maintain the monopoly on gaming they have had in the Northeast.

Mall construction in New Haven may add to further highway congestion in that area creating further bottlenecks on I-95.

Rising interest rates, likely in the New Year, pose a threat to Connecticut's financial services industry, a major source of employment, particularly in Hartford and Fairfield counties. In addition, Connecticut residents are heavily dependent on income from the stock market. We are also a state with heavy debt exposure on the part of individuals. Rising interest rates will reduce income from the stock market and at the same time make it more difficult to service debt.

Summary-Job income and output will continue to rise but more slowly. No cyclical downturn is anticipated in the United States. In the coming year it is very likely that rising interest rates will have an impact on corporate profits, the stock market, and the housing industry. In Connecticut, the lack of available workers due to slow population growth and negative net migration is a particular concern. Faster growth in the labor force is required for continued economic growth. The loss of a Congressional seat, combined with similar losses in other Northeastern states, will lead to a reduction in the Northeast's ability to influence policy and the allocation of resources at the national level.

Mr. Frederick S. Briemyer
Senior Vice President and Chief Economist
State Street Corporation
Boston, Massachusetts
The International Economy

Monetary Policy-The Fed recently raised interest rates. It has expressed concern that the economy is expanding in excess of its growth potential. Thus, the pool of available workers has declined relative to jobs, a trend that may lead to inflationary imbalances.

The economy has been growing at a rate of 4 percent for the last four quarters. The Fed would like to notch it down to 3 to 3 1/2 percent by the end of 1999 and to 2 1/2 to 3 percent by the end of the year 2000. Based upon third quarter actual and fourth quarter anticipated performance for 1999, the economy will exceed these goals.

If the Fed continues to raise interest rates, it will eventually lead to higher unemployment rates. The current national rate of unemployment is at about 4 percent. Tightening on the part of the Fed could raise the rate to 4 1/4 or 4 1/2 percent. This will help to avoid additional wage pressures.

Further tightening would also have the effect of slowing growth from its current rate of 4 percent to a more sustainable level.

Global Markets-1997 and 1998 were turbulent years in world markets, particularly Asia and South America. 1999 has been a year of healing. It appears that the worst is behind us that we are moving toward faster growth worldwide. Although conditions are improving globally, however, there continue to be vulnerabilities, particularly in Japan where a combination of monetary and fiscal policy is producing deficits of about 20 percent of GDP.

We will see continued growth in most world markets for the coming year that will pose some interesting challenges for the U. S. economy. In recent years we have been importing deflation, or lower prices, which has played a role in keeping inflation in this country at bay. Since 1995, prices of imported goods, excluding oil, fell at an average rate of 2 percent per year. Going forward, however, as other countries begin to grow more rapidly, we will begin importing inflation. We are already seeing this in the form of higher oil prices.

The fact that the U.S. has been growing faster than in other parts of the world has helped us to attract capital from other countries. This ample supply of capital has enabled us to fund the growth of our economy while simultaneously keeping interest rates low. As growth accelerates in other countries, we will find ourselves in a more competitive capital market. In all likelihood, capital will be reapportioned to some extent, and it probably should be.

Oil Prices-In the Northeast we are particularly vulnerable to increases in the price of oil. There are two components to these price increases. First, reductions by oil producing nations have constrained supply. Second, the recovery in Asia has placed additional demands on available supply. Thus, oil demand has been increasing in the face of constrained supply leading to a run-up of prices to the high end of the normal range.

Going forward, we will continue to see more rapid growth in other parts of the world accompanied by constrained oil supplies. It seems reasonable to anticipate, therefore, that oil prices will increase further. This is a source of concern because price increases can contribute to general inflation.

Risks-One of the risks on the policy front is that the Fed will not do enough. This is not an aggressive Fed, and the tendency is to do the least possible amount to avoid harming the economy. If the Fed gets behind the curve in slowing the economy, there is the threat of greater inflation.

A second risk is the stock market where technology-driven stocks appear to be overvalued. This carries with it the risk of a correction. Currently, our trade deficit is being financed foreign capital attracted to our stock market. If the market drops, foreign capital will move to other markets, and the trade deficit will become a more pressing concern.

The final risk is the international environment that has been unstable for some time. The problems and issues in Asia have not been fully resolved, and conditions there remain uncertain. China's signing of the World Trade Organization deal will add to the complexity since the nature of their participation in the WTO has not been determined. If there are surprises ahead, they are most likely to occur in the international arena.

Yearly Report of Industry Clusters
James F. Abromaitis, Commissioner
Department of Community and Economic Development

The industry cluster initiative is now almost three years old. It has become a way of doing business in the state. Within the next two weeks, the Connecticut Economic Conference Board will be provided with a copy of the latest progress report for the entire initiative. The report will provide an in-depth look at all the activities as well as some of the highlights and successes.

Initially, the cluster initiative started with six groups, but new clusters are starting to emerge and organize. The Governor's Council on Economic Competitiveness is leading the cluster effort.

Michael J. Werle
Manufacturing

The goal of the cluster initiative is to identify and nurture clusters. At the present time three formal clusters have moved into the organizational stage. An additional five to six clusters are in various stages of study and deliberation. The oldest cluster is bioscience which has completed a year of activity. A bioscience facility financing initiative went through the legislature last year. This provided about $40 million in financing to help develop lab and facility space in Connecticut. To date, approximately $12 million of that funding has been committed.

The second oldest cluster is aerospace components manufacturing. This cluster currently includes around 20 member companies with the plan to grow to 40 by the end of 2000 and 60 by the following year.

Aerospace components manufacturing is one of the clusters within manufacturing, originally identified as one of the important megaclusters. The Manufacturing Resource Center was created by the Governor's Council last year to support the growth of small and medium sized companies in the state. The CONNSTEP program, Connecticut's version of a manufacturing extension program, is the major vehicle for achieving this. Support has focused heavily in the area of adopting lean manufacturing practices that allow companies to drive down costs and become more competitive.

The third formal cluster is the software cluster, administered by the Connecticut Technology Council. This cluster has put together several initiatives and is beginning work on those.

There are other clusters in various stages of formation. These include photonics, marine, agriculture, seafood, plastics, and advanced materials and materials manufacturing.

Patricia Downs
Workforce Development

The issue of workforce development cuts across all the clusters. Two recommendations pertaining to workforce development in the manufacturing industry have already emerged from work within the clusters. The first of these is the Secondary School Pilot Program. The clusters recommended that manufacturing training be improved in the vocational/technical schools by establishing pilot programs. The pilot programs would entail extensive cluster involvement to create a strong curriculum, company exposure, closer links between businesses and public high schools, and a positive social environment.

As a result of this recommendation, DECD issued a request for proposal last year to solicit proposals from schools to participate in the pilot. Four of the ten proposals submitted were funded. These included proposals from the Northeastern Connecticut Manufacturing Initiative, the Manufacturing Advanced Placement Program in Middlesex County, the Manufacturing Technology Cooperative Program in Waterbury, and a proposal from Windsor Public High School.

The second recommendation emerging from the clusters was to fund the work being done in the area of precision machine training at the Greater Hartford Community Technical Colleges. That was done using a combination of federal, state, and private funds for a total of $1.6 million. The three colleges involved, Asnuntuck, Capital, and Manchester, have implemented the program. Classes began in February and March of 1998. The first cycle of training produced 93 students who are now in employment with area manufacturers. The second cycle of training was completed in October.

Andrea M. Scott
Connecticut Inner City Business Strategy Initiative

In the spring of 1999 the Governor's Council together with DECD launched the Connecticut Inner City Business Strategy Initiative. We worked in conjunction with Michael Porter, a professor from the Harvard Business School, who is a leading authority on global competitiveness. Professor Porter has a unique methodology for economic development in urban areas.

As a part of this initiative, we set up teams in five cities: New Haven, Hartford, Waterbury, Bridgeport, and New Britain. The teams include a city champion who is a CEO from a major corporation and an advisory board. The advisory board includes representatives from the private sector and corporations, minority entrepreneurs, and individuals from the community. A business team was set up to do local research on demographics and economic activities. We also interviewed businesses to determine the advantages and disadvantages of being located in an inner city.

To date, approximately 250 individuals have been involved. There is a corporate champion for each city, and the advisory boards have been meeting. We have interviewed about 220 inner city businesses.   Currently we are looking for themes to emerge from this research. We would like to have a final report on our work thus far for the Governor's Council by December 15.

Lauren Kyle
Marketing Connecticut

The Market Advisory Committee of the Governor's Council was asked to develop a plan to position Connecticut to facilitate business recruitment and retention and to support that plan with ad campaigns. To achieve that goal, marketing, advertising, and media experts were brought together to create an umbrella theme, "You Belong in Connecticut."   We have already run one ad campaign using this tag line.

The theme, "You Belong in Connecticut," is particularly targeted to youth, because Connecticut loses a lot of young people when students go out of state to college and fail to return. At the same time, we have more than 45 colleges and universities in Connecticut. We would like to convince some of those students to stay here by communicating that Connecticut is a good state for young people with a wealth cultural and entertainment activities.

The ad campaign includes radio advertising, billboards, buses, fly-overs, a website, and cooperation with the state colleges to run college fairs and concerts. Thus far, the campaign has resulted in a lot of media coverage; radio, television, newspapers, and business publications. The results of an awareness study will be available in December.

Judith K. Resnick
Business Training Networks Program

Through the cluster initiative, business leaders have agreed that the single most important determinant of long-term competitiveness is the ability to attract and retain a qualified workforce. The Connecticut Business Training Networks Program was developed to support the cluster initiative. Research has shown that companies that invest the most in training actually achieve higher sales and profits.

The goal of the Business Training Networks Program is to create a demand-driven system of education and training that responds directly to the needs of business rather than the other way around.

The Business Training Networks Program is a grant program with specific objectives. First, it is intended to help companies identify specific employment and training needs. If a group of companies shares similar needs, they can collaborate to obtain training thereby making it more targeted and more affordable. Second, we want to help member groups identify training and educational resources to help them with their particular requirements. By partnering with educational institutions, groups of companies can better design training suited to their needs.

There are four different phases to the grant program, each carrying a different level of funding. The objective of the program is to have participant groups become self sufficient in identifying and addressing their training needs. Participation in the program should help them lower their training costs while simultaneously improving quality. Companies with a reputation for investing in their employees will become employers of choice, thereby making it easier for them to attract and retain employees.

To date we have awarded three grants. The first was awarded to a group of spring manufacturers in Bristol, the second to a group of electronic manufacturers in Danbury, and the third to a group of metal manufacturers in the Bridgeport area.

Roger F. Therrien, Research Director
Department of Labor
Connecticut Labor Force and Unemployment:
"How They Are Measured"

The U.S. Bureau of Labor Statistics has developed a program called the Local Area Unemployment Statistics Program. This program produces data on employed and unemployed workers at the state level as well as for metropolitan areas, labor market areas, counties, cities, and towns. Employed workers are those who work at least one hour for money or those who are self-employed or working for a family business for at least 15 hours during the week for which the data is collected. Unemployed include those individuals who are not working but are able and available to work and looking for work during the week for which the data is collected. Discouraged workers, or those who are not seeking work, are not included in the labor force. Full time students, retired individuals, members of the Armed Services, prison inmates, and patients in various types of hospitals are also not included.

State level estimates are produced for the ratio of employment to population and the unemployment rate. The estimates are based on a time-series model that includes trend and seasonal components. There are three inputs to the model: non-farm employment, claimant data from unemployment insurance, and the current population survey. The model is designed to minimize monthly fluctuations that can lead to larger year-end revisions. The current population survey, in particular, is subject to variation which can lead to changes in the state's unemployment rate.

Results of the model indicate that the winter months, January and February, are the peak unemployment months. Construction workers, agricultural workers, and seasonal employees hired during the holiday season are all out of work. Unemployment rises again during the summer months when schools are out.

A description of the methodology for calculating the state's unemployment rate should be accompanied by the reminder that labor force data are estimates. They are not based on a complete headcount and, thus, are subject to variability as all sample-based estimates are. This is certainly true of the consumer population survey. This variability can cause the unemployment rate to fluctuate. We should not, therefore, read too much into one month's estimates but should rather look at the series over time. For Connecticut, the average unemployment rate for the last twelve months was 3 percent. This is equal to the lowest unemployment point of the 80s that occurred in 1988.

Factors leading to low unemployment include out-migration which was high in the early part of the decade and slow growth in the state's population. During the recession, many workers, including those in construction, left the labor force and sometimes the state. Managers restructured out of companies often retired and also left.

Those workers are now being replaced by a somewhat smaller youth population now entering the workforce. In 1990 Connecticut's labor force included approximately 420,000 16 to 24-year olds. In 1998 that number had declined to about 345,000. There has also been a decline in labor force participation due to the increase in the number of prison inmates. From 1990 to 1998 the number of persons incarcerated in Connecticut almost doubled. This has taken approximately 6,000 people out of the labor force. Temporary help has also declined, further reducing the pool of available workers. Many of these individuals are now employed.

Although out-migration has slowed considerably, Connecticut continues to face the problem of slow population growth. A comparison of the Northeast to other parts of the country reveals that most of the population growth has occurred in the South and the West. The population of the Northeast grew by just under 2 percent from 1990 through 1998. During that timeframe, Connecticut's labor force grew by less than 1 percent.