Report of the
CONSENSUS ECONOMIC FORECASTING COMMISSION
November 1, 2012

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Summary

The Maine Consensus Economic Forecasting Commission (CEFC) convened on October 25, 2012, and followed up briefly on October 29, 2012, to review and revise the February 2012 forecast. This report provides a summary of the Commission's findings.

National and state economic indicators suggest little improvement in economic conditions since the CEFC met in February 2012. Maine's coincident economic activity index was unchanged in the three months ending in August and remains below pre-recession levels. About half the states saw growth over the three months ending in August. Nationwide, consumer sentiment and small business optimism are up over year-ago levels. Personal income in Maine grew 3.0% year-over-year in the first half of 2012, while wage and salary income grew 1.3% over the same period. The Consumer Price Index was 2.0% higher in September 2012 than it was in September 2011.

The price of crude oil (West Texas Intermediate) remained fairly steady in the third quarter of 2012 around $92 per barrel. Home sales in Maine increased in six of the seven months since January 2012. Month-over-month, housing permits in Maine grew 33% in August. The median home price in the Portland Metropolitan Statistical Area (York, Cumberland, and Sagadahoc Counties) increased 3.1% year-over-year in the second quarter of 2012. Mortgage delinquency rates remain well above pre-recession levels but below peak crisis levels. The foreclosure rate in Maine increased in the second quarter of 2012 and remains well above pre-recession levels.

Uncertainty stemming from the "fiscal cliff" has continued to restrain economic growth in recent months. The "fiscal cliff" is a major fiscal tightening that includes the expiry of the Bush tax cuts, the payroll tax cut, emergency unemployment insurance benefits, and depreciation incentives as well as the sequester spending cuts, for a cliff estimated to be worth 3.0% of GDP nationally. *The CEFC assumes that there will be a constructive solution reached by the new Congress and president preventing any extensive deterioration of economic conditions.* Given the severe impact to the economy if a solution is not successfully reached, the CEFC will reevaluate their forecast in the first quarter of calendar year 2013 in response to actual policy decisions at the federal level.

Wage and salary employment growth was revised upwards slightly for 2012 and slightly downwards for 2013-2015 to reflect more robust current-year employment growth and longer-term structural workforce challenges, respectively. Personal income growth was revised upwards for 2012 in part to reflect the stronger employment growth and in 2013 to reflect increased dividends, interest and rent income, while 2014 and 2015 were revised downwards. Inflation, as measured by the Consumer Price Index (CPI), was revised upwards for 2012 and downwards for 2013-2015.

The table on the next page provides the forecast's major indicators.

Calendar Years	*2011*	2012	2013	2014	2015	2016	2017
Wage & Salary Employment (Annual Percentage Change)							
CEFC Forecast 02/2012	**0.1**	**0.1**	**0.8**	**1.3**	**1.4**		
CEFC Forecast 11/2012	***0.0***	**0.3**	**0.7**	**1.0**	**1.0**	**1.0**	**0.8**
Personal Income (Annual Percentage Change)							
CEFC Forecast 02/2012	**3.8**	**3.0**	**3.0**	**4.7**	**4.8**		
CEFC Forecast 11/2012	***4.6***	**3.5**	**3.2**	**4.1**	**3.9**	**4.2**	**3.8**
CPI (Annual Percentage Change)							
CEFC Forecast 02/2012	**3.1**	**1.3**	**1.9**	**2.3**	**2.1**		
CEFC Forecast 11/2012	***3.1***	**2.0**	**1.3**	**1.8**	**1.7**	**1.9**	**1.9**

Prior to the forecasting meeting, the CEFC held a data gathering session during which they heard from a variety of Maine industry associations. The presenters included the Maine Association of REALTORS, Maine Bankers Association, Associated Builders and Contractors of Maine, Maine Automobile Dealers Association, Manufacturers Association of Maine, Maine Hospital Association and the Maine Chamber of Commerce. The summary of this data gathering session is available in a separate report. Overall, these business perspectives helped confirm the CEFC's subsequent findings that Maine should not expect significant economic growth in the short run.

In deliberations leading to consensus, the CEFC considered information presented by several state agencies, including the Maine Department of Labor, Maine Revenue Services, and the Office of Policy and Management. The following sections summarize these reports.

Office of Policy and Management

In August 2012, the Maine Coincident Economic Activity Index, a composite of four economic indicators (three employment statistics plus real wage and salary income) that summarizes overall economic conditions, was 0.7% higher than it was in August 2011. For the three months ending in August 2012, the state coincident indexes increased in 28 states, decreased in 16, and remained unchanged in six, including Maine. In November 2011 (the data available at the last CEFC meeting) the state coincident indexes increased in 43 states, decreased in six states, and remained unchanged in one.

The State Leading Index predicts the six-month growth rate of the State Coincident Index. It uses the Coincident Index plus four other variables that lead economic activity: state-level housing permits (1 to 4 units), state initial unemployment insurance claims, delivery times from the Institute for Supply Management (ISM) manufacturing survey, and the interest rate spread between the 10-year Treasury bond and the 3-month Treasury bill. In August 2012, the State Leading Index for Maine was 0.39, meaning the State Coincident Index is expected to grow 0.39% over the six-month period from August 2012 to February 2013.

According to preliminary estimates from the Bureau of Economic Analysis, total personal income grew 3.0% year-over-year and wage and salary income grew 1.3% year-over-year in the first half of 2012.

On an annual basis, the Consumer Price Index (CPI) rose 3.2% from 2010 to 2011. The CPI rose 2.0% from September 2011 to September 2012. Core inflation, which excludes food and energy prices, also rose 2.0% over the same period, as increases in food costs offset declines in fuel and utilities costs. The CPI rose 1.9% year-over-year in the second quarter of 2012. Core CPI (all items less food and energy) rose 2.3% over the same period. The BEA National Income and

Product Accounts (NIPA) Implicit Price Deflator for Gross Domestic Product rose 1.7% over the same period.

In September 2012, the survey-based University of Michigan Consumer Sentiment Index increased 5.4% month-over-month, the highest monthly increase since January 2012. The index was up 32% from a year ago. In September 2012, the survey-based National Federation of Independent Business (NFIB) Small Business Optimism Index declined 0.1%, although it was up 4.4% from one year ago.

The price of West Texas Intermediate was $92.27 per barrel in the third quarter of 2012. The price of WTI declined 1.3% from the second quarter of 2012 to the third quarter of 2012. The price of heating oil in Maine ($3.80/gallon on October 15, 2012) is higher than it was at the same time of year in any of the past four heating seasons. The price of heating oil in Maine has increased over the course of three of the last four heating seasons. The price declined over the course of the 2008-2009 heating season, which coincided with the financial crisis and its immediate economic effects.

Single family existing-home sales in Maine were up 15.1% in August 2012 over August 2011. In August 2012, single unit housing permits in Maine increased 33% from July. Single unit housing permits in Maine in the 12-month period from September 2011 through August 2012 were 2% higher than in the previous 12-month period. The median home price in the Portland – South Portland – Biddeford metropolitan area increased 3.1% year-over-year in the second quarter of 2012. The median home price in the Portland – South Portland – Biddeford metropolitan area in the second quarter of 2012 was $226,000. The share of mortgages in Maine that are delinquent 30 days or more was 7.8% in the second quarter of 2012. That is below the recent peak of 9% in the first quarter of 2010 but well above pre-recession levels. Maine's foreclosure rate increased in the second quarter of 2012 and remains well above pre-recession levels. The rate of foreclosure starts was 0.9% in the second quarter of 2012.

Maine Department of Labor

The national unemployment rate has continued to trend lower during 2012 while Maine's unemployment rate has trended higher. However, this is not an indication that the U.S. economy has been improving while Maine's has been weakening. Maine's unemployment rate is likely to be adjusted upwards for late 2011/early 2012, resulting in a generally flat trend overall. In addition, the U.S. unemployment rate has declined due to lower labor force participation, while in Maine, labor force participation rates have seen much less of a decline. The national decline in labor force participation has resulted in approximately 5.6 million fewer people in the labor force than there would have been if not for declining participation.

A better way to compare Maine to the U.S. is to look at the employment to population ratio. Maine's employment to population ratio is higher than the national ratio: Maine has been around 60% since late 2009 (pending an expected revision for late 2011/early 2012) while the U.S. has been around 58.5% since late 2009.

Maine's September 2012 labor force participation rate is 65.0% with an official unemployment rate of 7.6% while the U.S. labor force participation rate is 63.6% with unemployment of 7.8%. If the U.S. labor force participation rate matched Maine's, the national unemployment rate would have been 9.8%. Similarly, if labor force participation in Maine was as low as in the U.S., Maine's unemployment rate would have been 5.5% in September.

Early indications from the employer payroll survey are that nonfarm payroll jobs estimates are likely to be revised up. In the 12 months through June 2012, payroll jobs reported through quarterly unemployment insurance tax filings were up 6,800. This growth is coming entirely from the private sector, while state and local government jobs continue to decline. The gradual increase in wage and salary jobs has not yet translated to a rise in total wages paid.

The likely revisions to the payroll jobs should place the CEFC's previous forecast for 2012 slightly below the actual job growth.

There was discussion around the fact that Maine is likely facing a structural skills gap. The types of jobs Maine has lost are very different from the types of jobs seeing growth. This leads to a real challenge in reemploying individuals in jobs requiring different skill sets, especially at similar levels of compensation.

Maine Revenue Services

Total general fund revenues for the month of September 2012 were under budget by $22.1 million and were under budget for the first quarter of the fiscal year by $26.9 million. About half of the total variance for the quarter came from the corporate income tax line, which was $13.2 million under budget. The reason for this is yet unclear – it may be a timing issue around refunds, or it could be an indication that corporate profits are beginning to dry up. Additionally, the estimate of the timing on the bonus depreciation tax cut may have been off. The corporate data does have a large lag, so more clarity may emerge as more data is available.

Taxable sales were up 3.1% for the three months ending in August compared to a year ago, which was somewhat slower than anticipated. Total revenues from the sales and use tax were under budget by $9.6 million for the first quarter of the fiscal year. Some of this may be due to overstating the annual accrual, whereby in June of each year, Maine Revenue Services looks out 60 days and estimates what will be collected due to activity in the current fiscal year.

Within taxable sales, auto/transportation is doing well and was up 8.4% in August over last year. Restaurant and lodging sales were also better in August, although July was worse than anticipated, perhaps due to the July 4 holiday falling in the middle of the week. Building supply sales have slowed significantly as have business operating expenses. Other northeast states have seen steady declines in sales over the summer months (excluding auto sales).

The individual income tax line was under budget by $6.2 million in September and $4.8 million for the first quarter of the fiscal year. Overall, 2011 was not a very good year for income taxes, and with the third estimated payments coming in lower than expected, it could be that 2012 is not going very well either.

The highway fund is doing okay; it was about $2 million over budget for the first quarter of the fiscal year, with gains in motor vehicle registration and fees offsetting losses from fuel taxes.

Maine Revenue Services has estimated that the "fiscal cliff" would cause Maine households to experience an increase in taxes of about $1.4 billion for the 2013 tax year if all tax credits end as expected. This would equate to a hit of about $3,000 per household. There is some question about how high income taxpayers will react to the expectation of a 2013 tax increase: whether they will pull forward as much income as possible into 2012 to avoid the higher 2013 taxes.

Macroeconomic Assumptions

Two different economic forecasts were examined at the meeting: the Moody's Analytics baseline scenario and the IHS Global Insight baseline scenario. Each forecast was based on a different set of national macroeconomic assumptions. These forecasts were then compared to this CEFC's February 2012 forecast. Overall, the CEFC felt the Global Insight assumptions and forecast better reflected their current views of the economy. The key national macroeconomic assumptions from Global Insight are outlined below.

- The U. S. economy will continue to grow slowly with a weak global economy.
- The 2 percentage point social security payroll tax cut and emergency unemployment insurance benefits will be extended for 2013 and then phased out over several years.
- The lame-duck Congress will extend the "fiscal cliff" deadlines into 2013, when the new Congress and president will come up with a package combining cuts in Medicare, Medicaid, Social Security, and nondefense discretionary spending with increases in income taxes. Most of these measures are expected to begin in January 2014.
- The Bush tax cuts are extended for 2013 but the present 50% bonus depreciation incentive is not extended for 2013.
- The Federal Reserve will hold rates near zero until mid-2015 and the QE3 program of mortgage-backed security purchases will be supplemented with renewed purchases of long-term Treasuries in 2013.
- Global growth will slow in 2012 and 2013.
- This weak global growth will keep oil prices low.
- The U.S. drought will cause consumer food price inflation to be higher in 2012 and 2013.

Consensus Forecast

The CEFC began with a general discussion of the forecasts and assumptions. CEFC members agreed that the IHS Global Insight forecast generally tended to be more in line, both in terms of assumptions and forecast, with their current views. They accepted Global Insight's national macroeconomic assumptions around the "fiscal cliff," including assumptions that the lame-duck Congress will extend the deadlines and that the new Congress and president will produce a package of spending cuts and tax increases. The CEFC assumes that there will be no significant deterioration in economic conditions due to the fiscal cliff and a constructive solution will be reached. If this does not occur, the CEFC would reconsider its forecast in light of actual events.

Given the anticipation of likely upward revisions to the 2012 wage and salary employment figures from the Bureau of Labor Statistics, the CEFC decided to deviate from the Global Insight forecast for 2012 and increase the annual growth rate from its previous forecast (from 0.1% to 0.3%). The CEFC believes long-term employment growth is likely to be slow due to structural workforce-related problems, such as the skills gap and demographic challenges. Given this assumption, the CEFC limited its annual growth forecasts to 1.0% for 2014-2016.

The CEFC accepted the Global Insight forecast for inflation, as measured by the Consumer Price Index, for all years. This was based on recognition of higher food prices in the near term followed by a decline and slower growth in energy prices due to weak global demand and a glut of natural gas.

Some modifications were made to the personal income forecast due to the changes made in the wage and salary employment line. Wage and salary income for 2012 was left at the same growth rate as the previous forecast (2.6%), which was higher than the current Global Insight forecast, while growth rates for 2015 and 2016 were reduced to match the lower employment growth rates.

The following page provides the full forecast.

Maine Consensus Economic Forecasting Commission							
November 2012 Forecast	History	Forecast					
	2011	2012	2013	2014	2015	2016	2017
CPI-U* (Annual Change)	3.1%	2.0%	1.3%	1.8%	1.7%	1.9%	1.9%
CPI for Energy Prices** (Annual Change)	15.2%	0.3%	-5.1%	1.1%	-0.9%	2.0%	2.2%
Average Price of a New Vehicle** (Annual Change)	3.3%	0.8%	0.3%	2.0%	2.9%	2.2%	2.5%
New Vehicle Registrations** (Annual Change)	2.8%	11.9%	2.9%	3.5%	2.0%	2.3%	1.2%
Personal Savings Rate**	4.3%	3.8%	3.7%	4.1%	4.5%	4.8%	4.8%
Maine Unemployment Rate**	7.6%	7.4%	7.2%	6.8%	6.3%	5.8%	5.6%
3-Month Treasury Bill Rate**	0.05%	0.09%	0.12%	0.12%	0.73%	2.66%	3.72%
10-Year Treasury Note Rate**	2.79%	1.80%	2.05%	2.74%	3.47%	4.32%	4.86%
Before-Tax Corporate Profits* (Annual Change)	2.1%	14.4%	8.1%	-1.2%	-3.2%	-4.7%	-4.4%
Maine Wage & Salary Employment* (thousands)	593.0	594.8	599.0	604.9	610.9	617.0	621.8
Natural Resources	2.6	2.6	2.6	2.7	2.7	2.7	2.7
Construction	24.8	25.2	25.5	26.1	26.9	27.8	28.1
Manufacturing	50.4	50.2	49.5	49.5	49.2	48.9	48.6
Trade/Trans./Public Utils.	117.5	117.5	118.3	119.1	120.1	121.3	122.5
Information	8.2	7.8	7.8	7.9	8.0	8.0	8.1
Financial Activities	31.6	31.5	31.8	32.0	32.2	32.3	32.4
Prof. & Business Services	56.9	57.8	58.8	60.4	62.2	63.6	64.6
Education & Health Services	120.2	121.8	123.4	125.0	126.9	128.9	130.8
Leisure & Hospitality Services	59.5	60.0	61.0	61.8	62.4	63.0	63.6
Other Services	20.1	19.5	19.8	19.9	19.9	19.9	19.9
Government	101.3	100.9	100.6	100.6	100.6	100.6	100.6
Agricultural Employment	14.0	14.0	14.0	14.0	14.0	14.0	14.0
Maine Wage & Salary Employment* (Annual Change)	0.0%	0.3%	0.7%	1.0%	1.0%	1.0%	0.8%
Natural Resources	-0.7%	0.7%	0.4%	3.1%	0.7%	0.5%	-1.2%
Construction	1.5%	1.8%	1.2%	2.3%	3.0%	3.5%	1.2%
Manufacturing	-1.0%	-0.3%	-1.3%	-0.1%	-0.6%	-0.6%	-0.7%
Trade/Trans./Public Utils.	0.5%	0.0%	0.6%	0.7%	0.9%	1.0%	1.0%
Information	-9.9%	-5.3%	0.0%	0.8%	1.7%	0.6%	0.3%
Financial Activities	1.2%	-0.4%	0.7%	0.7%	0.7%	0.4%	0.4%
Prof. & Business Services	2.2%	1.6%	1.7%	2.8%	2.9%	2.3%	1.6%
Education & Health Services	1.0%	1.4%	1.3%	1.3%	1.5%	1.6%	1.5%
Leisure & Hospitality Services	-0.7%	0.8%	1.6%	1.4%	1.0%	1.0%	0.8%
Other Services	1.6%	-2.9%	1.5%	0.5%	0.1%	0.1%	0.1%
Government	-2.0%	-0.4%	-0.3%	0.0%	0.0%	0.0%	0.0%
Agricultural Employment	-16.2%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
	2011	2012	2013	2014	2015	2016	2017
Personal Income* ($ million)	50,869	52,647	54,314	56,552	58,763	61,212	63,531
Wage & Salary Disbursements*	23,954	24,576	25,340	26,247	27,166	28,144	29,181
Supplements to Wages & Salaries*	6,201	6,285	6,504	6,793	7,120	7,475	7,820
Non-Farm Proprietors' Income*	3,913	4,112	4,276	4,534	4,806	5,006	5,170
Farm Proprietors' Income	108	154	132	110	94	88	89
Dividends, Interest, & Rent*	7,646	7,993	8,378	8,741	9,198	9,722	10,216
Dividends	2,469	2,669	2,878	2,982	3,078	3,093	2,970
Interest	3,682	3,637	3,653	3,845	4,244	4,830	5,493
Rent	1,495	1,686	1,847	1,914	1,876	1,799	1,753
Transfer Payments*	11,701	12,223	12,590	13,246	13,873	14,571	15,177
Less: Contributions to Social Ins.	3,572	3,638	3,870	4,113	4,517	4,847	5,206
Residence Adjustment	917	941	964	993	1,023	1,054	1,085
Personal Income* (Annual Change)	4.6%	3.5%	3.2%	4.1%	3.9%	4.2%	3.8%
Wage & Salary Disbursements*	2.2%	2.6%	3.1%	3.6%	3.5%	3.6%	3.7%
Supplements to Wages & Salaries*	2.4%	1.4%	3.5%	4.5%	4.8%	5.0%	4.6%
Non-Farm Proprietors' Income*	2.7%	5.1%	4.0%	6.0%	6.0%	4.2%	3.3%
Farm Proprietors' Income	0.2%	42.4%	-14.2%	-16.8%	-14.4%	-6.4%	0.4%
Dividends, Interest, & Rent*	7.6%	4.5%	4.8%	4.3%	5.2%	5.7%	5.1%
Dividends	27.3%	8.1%	7.8%	3.6%	3.2%	0.5%	-4.0%
Interest	-0.8%	-1.2%	0.4%	5.2%	10.4%	13.8%	13.7%
Rent	2.7%	12.8%	9.5%	3.6%	-1.9%	-4.1%	-2.5%
Transfer Payments*	5.3%	4.5%	3.0%	5.2%	4.7%	5.0%	4.2%
Less: Contributions to Social Ins.	-8.0%	1.9%	6.4%	6.3%	9.8%	7.3%	7.4%
Residence Adjustment	7.1%	2.6%	2.4%	3.0%	3.1%	2.9%	2.9%
*CEFC Forecast							
**From Global Insight - October 2012							
Remaining lines derived from CEFC forecast by CEFC staff and reviewed by CEFC							