

THE CONNECTICUT Economy



A University of Connecticut Quarterly Review

Summer 2000

Waiting for Electric
Power Competition

Gas Tax Cuts...
At What Cost?

Green Acres:
Taking Stock of
Connecticut's Open
Space



Throwing Light on Energy and the Environment

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CONNECTICUT ECONOMIC INDICATORS

(Percent change: 1999-Q2 to 2000-Q2)

Indicators of Current Economic Activity

Total Nonfarm Jobs	+1.4%
Number Unemployed	-28.9%
Labor Force	+1.0%
Manufacturing	
Jobs	-1.7%
Avg. Weekly Hours	-0.6%
CT Mfg. Prod. Index	+0.2%
Avg. Hourly Earnings	+3.0%
New Auto Registrations	-1.6%
Travel and Tourism Index	+4.1%
Bradley Airport	
Passengers	+21.6%
Freight	-7.6%
State Taxes:	
Sales	+8.1%
Income	+17.0%
Real Estate Conveyance	0.0%
Normalized Electricity Use	+2.4%
State Exports ('99-Q1 to '00-Q1)	+11.4%
Confidence in Current Economy	+11.9%
Coincident GDI	+1.7%

Indicators of Future Economic Activity

Help-Wanted Ads	
<i>Hartford Courant</i>	-3.8%
<i>The Advocate of Stamford</i>	+6.0%
Job Orders	+0.5%
Avg. Initial Unemp. Claims	-13.0%
Housing Permits	-21.1%
Net New Business Starts	+13.1%
Confidence in Future	+5.2%
Leading GDI	+0.1%

Clouds on the Horizon?

OpSail 2000's fleet of tall ships breathed new economic life into New London and brightened an unusually dreary summer. Connecticut, like other New England states, has chalked up one of the coolest and dampest summers on record. We can blame the rain for hurting the tourist trade a bit—an increasingly important part of the Connecticut economy—but some other sectors showed signs of slower growth that can't be pinned entirely on bad weather.

Key indicators still signal a generally healthy state economy. Job growth continued, up another 22,800 or about 1.4% since the second quarter of 1999. This was only slightly below the 1.5% gain of 24,600 jobs between the first quarters of 1999 and 2000. And Connecticut kept its position as the state with the highest per capita income, now 37.3% above the national average.

So what's the concern? Maybe none. But numbers for some of Connecticut's most important sectors point to a softening economy—we hope it's just the rain. Second quarter job totals for finance, insurance and real estate (FIRE) topped 1999-Q2 figures by only half a percent. Between 1999-Q1 and 2000-Q1, FIRE jobs grew 1.1%, so new hiring in this sector has apparently slowed. Transportation, communications and utilities (TCU)

experienced an even sharper slowdown in job growth, from 2.0% between the first quarters of 1999 and 2000, to only 0.4% between the second quarters. Growth was stronger in construction (3.5%) and services (2.9%), but again both sectors registered even faster growth between the first quarters of 1999 and 2000.

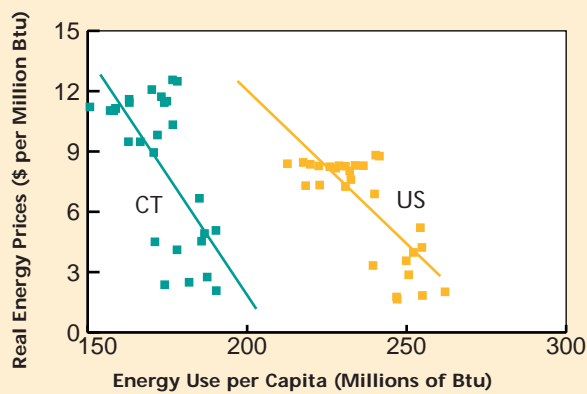
Job growth accelerated in a few sectors, including wholesale and retail trade (1.2%) and government (3.2%). [But don't forget that 2000-Q2 was a big period for temporary census workers and that "government" employment now includes tribal nations' gaming operations.] The other "positive" was a slowdown in the long-term decline in manufacturing jobs—down 1.7% compared with a 2.1% decline between the first quarters of 1999 and 2000. Unfortunately, at least for manufacturing workers, growth in average weekly earnings also slowed, from 5.7% to 3.0%, due to a drop in average weekly hours and a slowdown in the growth of average hourly earnings.

Overall, the labor market continues to be very tight, with sub-2% unemployment rates in four of the state's ten labor market areas and a statewide average of only 2.4%. In the second quarter, the number unemployed fell to 41,300. It's easy to lose sight of just how far we've come, but back in early 1993, when we launched *The Connecticut Economy* and the state was beginning its long recovery, there were 129,500 unemployed persons, more than *three* times the current figure.

Yet despite the impressive progress, there's an uneasiness about the future, reflected in the unsteady path of financial markets and the search for yet another "soft landing" that might allow the expansion to hang around a bit longer. When the economy starts to soften, it's easy to set aside other concerns. For this reason, we think the current issue's focus on energy and environmental policies is timely.

Connecticut's high energy prices have forced it to become a relatively efficient energy user (see above graph and pp. 6-7), but regulatory obstacles have delayed cleaner energy production (pp. 4-5). Market-based policies for trimming utility emissions may help the environment (p. 6), but the state also needs to reassess gasoline taxes in relation to auto emissions and road congestion (pp. 12-13). And the preservation of open space for environmental and recreational purposes (pp. 9-11) could boost Connecticut tourism. Still, as a source of clean energy and a welcome environmental amenity, we could sure use a bit more sunshine around here.

Connecticut's High Energy Prices Encourage More Efficient Use, 1970-1997



Good news

+11.9%
Confidence in
Current Economy



Bad news

-21.1%
Housing Permits

Competition in Electric Power: Not There Yet

By Brian T. Kench* and Arthur W. Wright

The day of choosing our own electric generating company may have arrived, but truly competitive power markets are still a long way off. One reason is that electric rates can't come down much until we work off utilities' "stranded costs", the legacy of past investments made under a different market regime. More important for the long haul, a congested and mismanaged transmission system will, until corrected, prevent us from realizing the full benefits of competition.

Effective July 1, 2000, Connecticut consumers joined many other Americans in being able to choose who generates the electric power they buy. United Illuminating (UI) and Connecticut Light and Power (CL&P) will still add shipping and handling charges for getting the power to your business or home. But the days of the vertically-integrated power company doing it all are fast disappearing. [See chart]

State regulators at the Department of Public Utility Control (DPUC) have heralded the coming of competition to electric power markets. Unfortunately, the label applies only to the generation segment of the business. No matter how competitive generation is, we won't see real competition until some complex issues in retail distribution and especially in long-distance transmission of power are resolved.

What would real competition mean? In narrow terms: open entry into and exit from the market; rates set by the marginal costs of the last units sold; transmission priced properly—variably—in real time; and investment decisions subject mainly to health-and-safety, not price, regulation. More broadly, electric rates would be lower than otherwise and, paradoxically, despite the increased power use with lower rates, the installation of cheaper but cleaner generating capacity could eventually reduce total emissions of CO₂, NO_x, and SO₂. This would be an excellent example of the profound efficiency gains to be had from deregulating markets.

Can we get there from here? To answer "yes" we'll have to get past a nagging transition problem and a much tougher restructuring problem. We can't deregulate electric power markets simply by closing down the DPUC and locking the door as the regulators leave. Too many assets based on past good-faith commitments are still in place, and existing asset owners must be compensated. More important, electricity markets

are made, not born: To make competition work, it is essential to maintain the integrity of what is a complex physical system. That will mean designing and installing suitable institutions to govern wholesale power transmission—the heart and head of any market for power. In New England, we're still in the design phase, and some of the key decisions aren't entirely within Nutmeggers' control.

Backdrop

The impetus to restructure electric power markets—like those in airlines, natural gas, banking, and telecommunications since the late 1970s—came from a disappointing performance under existing regulation, and from new technologies. The old edifice, erected early in the 20th century, of state-regulated franchise monopolies that controlled generation and distribution within designated service areas had grown progressively creaky. There were a few useful adaptations, such as regional power pools or grids that centralized the dispatch of generation and thus economized on back-up capacity, but not until 1992 were independent generators of power permitted to sell bulk power, wholesale, across state lines. What prompted that change was new technology—gas-turbine generators—that had emerged as the silver lining in the clouds of the "energy crisis" in the 1970s and 1980s. Gas-turbine technology is both cheaper and cleaner than the old-fashioned boiler technology that runs on oil, coal or nuclear fuel.

In a case of "winner's regret", CL&P and UI are stuck with a lot of long-lived boiler generating capacity, built over decades and state-of-the-art or "prudent" in regulator-speak at the time it was installed, but which is not yet fully depreciated. State regulators approved the outlays and thus are obligated to give the utilities the chance to recover their "stranded costs"—the undepreciated past investments that would have to be written off if cheaper power were granted unrestricted access to the power market. Electric rates must remain above long-run competitive levels for awhile, until UI and CL&P can work off stranded costs of some \$725 million and \$3.5 billion, respectively. (While the infamous "Filthy Five" plants are in the stranded-cost totals, they pale in comparison with nukes and other cleaner generating plants.)

Fortunately, stranded costs are only a temporary obstacle to realizing the benefits of competition in electric power. Tougher to surmount will be obstacles in the transmission of wholesale power in New England and beyond—e.g., in New York and even in the New Jersey-Pennsylvania-Maryland grid.

Making A Market For Electric Power

Market makers on the floor of the New York Stock Exchange stand ready to buy or sell shares of the stocks they specialize in, using inventories to balance their trading. Making a market in electric power, however, is a more delicate, complicated task because of the physical laws that

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govern the safe generation, shipment and use of electricity. Moment to moment, instantaneous reliability is at stake. When, how much, and on what terms an individual power generator puts power into the transmission grid is heavily dependent on conditions in the grid, which in turn depend on the actions of the other generators and customers using it.

Congress, in 1992, responded to the advent of gas-turbine generators by opening up interstate shipments of bulk power, exempting an entire class of wholesale power producers, Exempt Wholesale Generators or EWGs, from the 1935 ban on interstate trafficking in electricity. Inevitably, a political spat erupted over whether utilities were giving preference to their own power over that offered by other suppliers. In 1996, the Federal Energy Regulatory Commission or FERC, in its Order 888, mandated that utilities offer non-discriminatory or “open” access to their power lines to all potential suppliers, and also mandated that transmission be functionally independent from generation and local distribution. In regions like New England, FERC also urged re-forming power pools into arms-length Regional Transmission Organizations or RTOs, which would be responsible for coordinating regional shipments and selecting bids to ship power in order of lowest cost first.

Two years later, in 1998, the General Assembly put Order 888 into effect in Connecticut by passing RB 505. Besides mandating a headline-grabbing, 10-percent rate cut, this law:

- Y allows for up to 35 percent penetration of the Connecticut power market by EWGs;

- Y establishes a procedure for licensing generating-suppliers who wish to sell to state customers; and

- Y requires Connecticut utilities to join the New England RTO, the successor to the old New England Power Pool.

To date, only a few suppliers besides UI and CL&P have won sales licenses, but the numbers should rise with time, especially as the two utilities sell off their generating capacity. Both companies participate in the private, non-profit RTO known as ISO-New England (ISO stands for “Independent System Operator”), which manages the regional transmission network.

The Big Hurdle: Transmission Capacity

With strong economic growth and mounting competition in generation, the transmission network is now being used much more intensively than the region’s regulated utilities ever imagined or planned for when it was built. On especially cold or hot days, the New England system is hard pressed to meet peak demands. Present capacity is stretched thin; worse, the existing arrangements for its use allocate that capacity inefficiently. Those same arrangements, plus uncertainty about how they may change over time, are thwarting investment in new capacity.

The core problem is that FERC bases rates in the nation’s power transmission networks on average historical construction costs and current operating

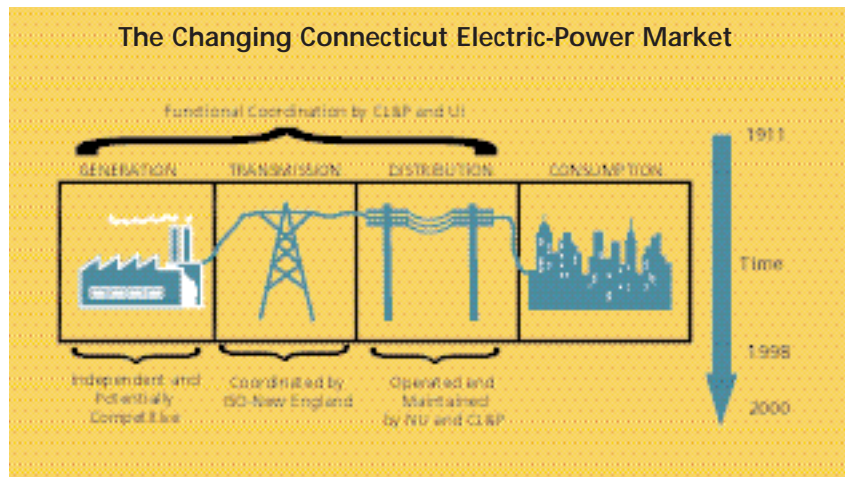
costs. Thus, anyone willing to pay the flat regulated rate may bid to use the system run by ISO-New England. As a result, those willing to pay the most for transmission services can’t gain access to them by paying more, no matter how overburdened the system is.

ISO-New England, living daily with intense pressure on its system, is struggling to find legal substitutes for the price flexibility that would, if permitted, alleviate congestion. Proposed measures include (1) permitting locational price variations, like those now used in Pennsylvania-New Jersey-Maryland (PJM); and (2) creating tradeable financial rights to transmission capacity. The PJM mechanism allows rates to rise temporarily when excess demand crops up at particular points in the transmission network; the downside is that divergent prices fuel consumer discontent and spawn political criticism.

Alternatively, granting valuable financial rights to builders of new capacity would provide a surrogate investment incentive now missing under flat regulated rates. Trading financial rights would also insulate shippers of power against money losses caused by network congestion. Some critics of the financial-rights approach advocate creation of *physical* rights to transmission capacity, in effect allowing it to be traded (like grain or natural gas) in futures as well as spot or forward markets.

In the shorter term, it may be possible to relieve transmission congestion by building new generating capacity at strategic points. (If nothing else, installing widely scattered gas-turbine generators may pose fewer siting obstacles than stringing more high-tension wires.) Obviously, ISO-New England would need to play a central role in decisions about new generation, even though its charge is to manage the region’s transmission network.

It may be some comfort that New England’s power predicament is *not* the result of the emperor fiddling while the region burns, or freezes. But curing the problems will require an unusual amalgam of enlightened flexibility and foresight on the part of FERC, state regulators, and power-industry leaders. Wish them well—the benefits of jump-starting investments in transmission capacity and, ultimately, achieving fully competitive power markets will be substantial.



Markets to the Rescue?

By Fred V. Carstensen

On May 17th, Governor Rowland issued Executive Order 19, designed to curb emissions of sulfur dioxide (SO₂) and nitrogen oxides (NO_x)—prime causes of acid rain and smog—in Connecticut. He ordered the Department of Environmental Protection to develop rules that would permit the state's 61 fossil fuel power plants and large industrial sources to trade emission "credits" or "allowances" among themselves to reduce the overall level of pollution. The objective is to cut SO₂ emissions 30% and NO_x emissions 20% by 2003.

The Governor is building on the experience of a strikingly successful national program. The U.S. Environmental Protection Agency (EPA) estimates that, since 1989, creation of a market in tradeable emission allowances has reduced SO₂ emissions by 30 to 35%, with 90% of the reduction coming in the nine high-emissions states in the Midwest. With prevailing winds moving west to east, SO₂ levels in Connecticut have dropped by nearly half, even though emissions originating in the state itself have changed little.

The market in the right to pollute originated in the 1990 Amendments to Title IV of the Clean Air Act. Those amendments set up the first large-scale environmental program that relied on tradeable property rights in SO₂ emissions. The hope was that, by creating a defined property right, competitive market forces would reduce emissions more efficiently than would administrative fiat.

Beginning in 1995, the EPA gave the 243 dirtiest plants in the country allowances that were proportional to their existing pollution levels, but which in aggregate cut total permitted annual emissions. Plants that cut emissions enough could sell their excess allowances or hold them for future use. Plants that could not reduce emissions enough had to buy allowances. New plants also had to buy allowances from the existing pool. And at the annual EPA auction of allowances on the Chicago Board of Trade, non-industry groups and individuals could buy allowances and simply retire them, reducing total permissible emissions. Environmental groups and school children have actually done so. This year, all fossil-fuel burning electrical generating facilities in the country came under the requirement to own allowances, with an even tighter cap on total emissions.

Without any meaningful market information available, no one knew at what price the allowances would trade. Projections ran as high as \$1,500 per ton when the law was passed, but prices actually started at around \$300 per ton and fell at one point to a low of \$64 a ton. With all plants now covered and the emissions cap lower, the current price is up to about \$135 per ton.

The real value of the market for SO₂ emissions is that it has provided utility managers critical information about potential trade-offs among adopting new technologies, switching to lower-sulfur coal or natural gas, or buying and selling allowances. It has also given producers and engineering firms a handy test of the profitability of improved technology: Do proposed innovations save enough in allowance costs to justify their price? With better information and the right to trade allowances, economists estimate that the market Title IV created has reduced emissions nearly a third more than traditional top-down, "command-and-control" policies could have achieved.

The success of the SO₂ program led the Clinton administration to advocate creating a similar market in world-wide emissions of carbon dioxide, the principal greenhouse gas. And here in Connecticut we will soon see if a similar market initiative can generate significant environmental benefits.

Fueled by High Prices, Connecticut Leads in Energy Efficiency

By Steven P. Lanza

After a winter of historically high heating oil prices and a summer driving season that sees gasoline near the \$2.00 mark, energy prices are making news for the first time in nearly a generation. If Connecticut residents feel especially beleaguered, they have reason. Connecticut is poorly positioned in the country's energy distribution network, and faces energy prices that are among the highest in the country. But Connecticut Yankees are an industrious lot, and they've made a virtue of necessity. Prices may be high, but the state's energy use per capita is among the nation's lowest, and its output per dollar of energy input is among the nation's highest. Over time and across industries Connecticut has proven to be an efficient energy user.

Paying Through the Hose

Connecticut residents pay more for energy than do residents in virtually any other state. According to data from a just released U.S. Department of Energy study, the state ranked among the top three states and the District of Columbia in cost per unit of energy for the period 1990-1997; sharing the dubious distinction were Washington D.C., Hawaii, Arizona, and Vermont. What's more, the state's energy price gap has widened. Connecticut energy prices exceeded U.S. prices by 31% in the 1970s, 33% in the 1980s, and 41% in the 1990s.

The recent spike in energy prices has turned heads, as heating oil and gasoline prices climbed by half in a matter of months. But even this price hike pales compared with those of the infamous embargo days. Between 1973 and 1981, a period punctuated by two OPEC-orchestrated energy crunches, energy prices quadrupled in both Connecticut and the U.S. Connecticut gasoline prices soared from 41¢ to \$1.42 per gallon, and electricity rates climbed from 2.8¢ to 8.1¢ per kwh. By 1981, the worst was over. Between that year and 1997, energy prices rose only modestly—just 10% in the U.S. and 13% in Connecticut over that entire 16-year period.

Though nominal energy prices in the late 1990s were much higher than they were in the 1970s, real prices, after adjusting for inflation, saw a protracted decline, at least until recently. In real terms, Connecticut energy prices climbed 98% between 1973 and 1981, but dropped 36% between 1981 and 1997. Similarly, U.S. energy prices rose 94% and then fell 38% over these same periods. So in both Connecticut and the U.S., energy prices in 1997 were at about same level as they were in 1978. And even at \$2.00 per gallon, the real cost of gasoline is lower today than it was in 1979.

Making Do With Less

A fundamental maxim of economics is that quantity demanded is inversely related to price. So it should come as little surprise that with energy prices among the highest in the nation, Connecticut's energy consumption per capita should rank among the lowest. (For a graphic comparing the state's energy use with the nation's, see page 3.) In 1997, Connecticut ranked 46th in energy use per capita among the 50 states and the District of Columbia. Throughout the 1990s, the state's rank never rose above 44th. Compared with the U.S. as a whole, the state's energy use is about 28% below average.

With below-average consumption helping to offset above-average prices, Connecticut's energy expenditure per person is, in a word, average. In 1997, Connecticut residents spent an average

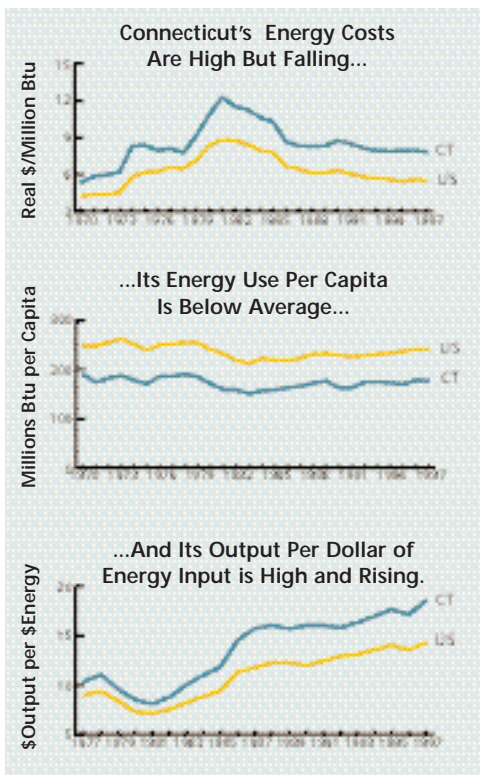
of \$2,218 per person on energy consumption, ranking the state 20 out of 51. The average U.S. resident spent \$2,119. Real energy expenditure per person in the state declined between 1981 and 1997, from \$2,051 in 1982-84 dollars to \$1,320—a drop of 33%. Real U.S. spending on energy dropped 32% over the same period.

Connecticut residents not only use much less energy than average, they use that energy more efficiently. As measured by gross state product per dollar of energy spending, Connecticut ranked 5th in 1997 for the fifth year running—behind D.C., New York, California and Delaware—producing \$18.56 in output per dollar of energy input. The U.S. average was \$14.28. Connecticut's energy efficiency is therefore about 30% higher than the U.S. as a whole. In both the U.S. and Connecticut, energy efficiency has improved over the years, but Connecticut's performance has outpaced the nation's. U.S. efficiency grew by about 4.4% per year between 1981 and 1997. Connecticut efficiency, by comparison, grew 5.3% per year over the same period.

Changing Patterns of Use

Energy price gyrations and structural economic changes have transformed state and national energy profiles. *First*, conservation has gained strength. Between 1970 and 1997, energy prices rose faster than prices overall, giving energy users everywhere reason to conserve. And with prices rising even faster in Connecticut, the drive to conserve was all the greater. Per capita energy consumption in the U.S. over this period dropped 2.8% to 240 million Btu per person in 1997. In Connecticut per capita consumption dropped 6.8% to 177 million Btu.

Second, alternatives to oil have gained favor. Energy prices have not all risen at the same rate, and where prices increased more quickly, consumption dropped apace. Nationally, natural gas prices rose the fastest, followed by oil and then electricity. Consequently, natural gas consumption fell from 29% to 26% of total energy use while electricity consumption rose from 9% to 16%. Oil use stayed constant at 52%. In Connecticut, oil prices rose the fastest, followed by electricity and then by natural gas.



As a result, Connecticut oil use dropped from 77% to 60% of total energy consumption, while natural gas use rose from 11% to 21%, and electricity use from 10% to 17%.

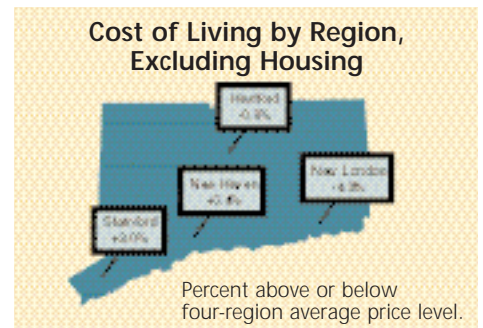
Third, industry's share of energy use has dropped. Increased mobility and the rise of the service economy have increased energy demands in transportation and commerce. For Connecticut in particular, the

shift from industry to commerce was especially pronounced. Nationally, industry's share fell from 39% to 34%, transportation use rose from 31% to 38%, and business use rose from 11% to 12%. In Connecticut, industry's share fell from 32% to 15%, transportation's share rose from 32% to 37%, while business use rose from 11% to 19%.

Fourth, rising home and business energy use has given electricity a more prominent position in consumers' budgets, particularly in Connecticut. Of the three most common forms of energy available to end users—electricity, natural gas and oil—electricity is by far the most convenient, but because of its high transmission costs, unfortunately the most expensive. And Connecticut residents pay an especially high premium for its use. In 1997, when natural gas cost 46% more than the U.S. average and oil cost 5% more than average, Connecticut electricity prices were 53% above the U.S. average.

Electricity supplies only about one-sixth of our total energy needs, but its high cost means that it commands a disproportionate and increasing share of our energy budgets. In 1970, electricity consumed 29¢ of every energy dollar spent in Connecticut; by 1997 it ate up 41¢. The comparable U.S. rates were 28¢ and 38¢. Oil, by contrast, has become less of a budget buster. In Connecticut, its bite eased from 63¢ to 47¢, while in the U.S. the comparable figures were 56¢ and 46¢. Connecticut residents thus have an abiding interest in the outcome of electricity deregulation. (For a look at the economics of electricity deregulation, see pages 4 and 5)

Over time and across sectors, Connecticut residents have adapted to higher energy costs by becoming more efficient energy consumers. Prices may be high, but the state's energy use per capita is among the nation's lowest, and its output per dollar of energy input is among the nation's highest. So, regardless of how OPEC manages its production quotas, or how the state handles the shift to electricity deregulation, Connecticut residents are likely to adjust to the new circumstances with equanimity.



Connecticut Price Changes

Percent Change 1999-Q2 to 2000-Q2

	Food	H 8.1%
	Housing	H 10.6%
	Apparel	H 1.7%
	Transportation	H 7.0%
	Medical	H 8.9%
	Entertainment	H 0.8%
	Miscellaneous	H 5.2%
	Overall	H 8.1%

GDI Enters A Summer Slump

By Steven P. Lanza

The GDI may have gotten off to a promising start in 2000-Q1, but second-quarter statistics show the index in a summer slump. The coincident index grew at the slowest rate in 16 quarters; and the leading index headed south once again after a brief, first-quarter flirtation with positive territory. The GDI is a composite measure of the four-quarter change in three coincident and four leading economic variables, and is indexed so 1986= 100.

The coincident GDI climbed from a revised 113.9 in 2000-Q1 to 114.3 in 2000-Q2, reaching a new high once again. On an annualized basis, the coincident GDI is up 1.3%—the smallest such increase since 1996-Q3. Manufacturing output, the star performer last quarter, held the index back in 2000-Q2. Between the second quarters of 1999 and 2000, output increased just 0.2% compared with a 2.1% jump in 2000-Q1. Income and job

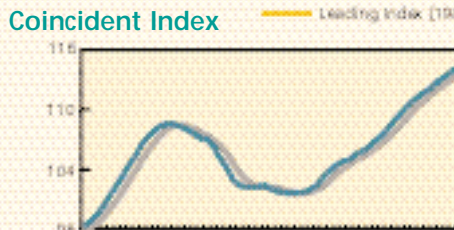
growth tried to rally but came up short. Jobs posted a respectable 1.4% advance, which is about average for the current expansion, while real income grew 2.2%—0.5% below its normal pace.

The real heartbreaker this quarter, however, was the disappointing set of numbers posted by the leading index. The leading GDI dropped from a revised 96.6 in 2000-Q1 to 96.5 in 2000-Q2, for an annualized decline of 1.0%. Three of the four economic variables in the index flagged. Average weekly manufacturing hours, which had jumped 1.6% between 1999-Q1 and 2000-Q1, dropped 0.6% between 1999-Q2 and 2000-Q2. Help wanted ads, a perennial under-achiever, shrank 3.9%. Worst of all, housing permits dropped 21.1% for their poorest showing since 1991-Q1. Only initial unemployment claims boasted any improvement, declining 8.2% between 1999-Q2 and 2000-Q2, but that was off from the previous 12% decline.

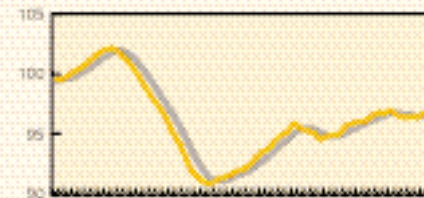
As the tally this quarter shows, the GDI is missing some muscle; still, it's too soon to say the index is headed back to the minors.

GDI Components

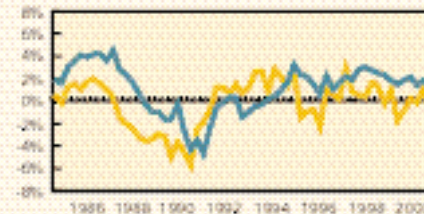
Four-Quarter Moving Average
Coincident Index (1986=100)
Leading Index (1986=100)



Leading Index



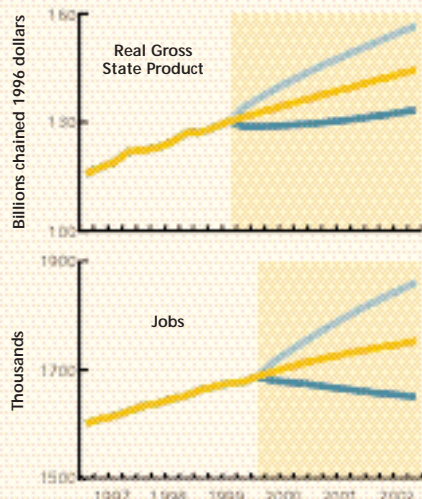
GDI Momentum



Economic Forecast

Higher prices and interest rates have dampened real gross state product (RGSP) growth in the second quarter. RGSP grew by 3.2% and is expected to post increases of around 3.4% this time next year. We anticipate the economy will add 22,000 jobs in that same period.

Where the lines branch off, the yellow line shows the predicted values for RGSP and jobs, and the green lines show a one-standard deviation margin of error around the forecast.



The Economy Booms... But for How Long?

By Kathryn Parr

With record low unemployment, slow job growth, rising prices and interest rate hikes, the Connecticut economy is showing signs of a maturing business cycle.

Our estimates of Real Gross State Product (RGSP) show the economy is still strong but slowing. RGSP grew by 3.2% between 1999-Q2 and 2000-Q2, off a bit from a revised 3.4% last quarter. Our forecast suggests growth will slow through the end of 2000 but pick up the pace in early 2001. By 2001-Q2, we expect increases in RGSP to be about 3.4%.

The number of jobs in Connecticut grew by approximately 22,800 from the second quarter last year, a drop of 1,800 from the first quarter's increase of 24,600. This slowing trend in job growth reflects labor scarcity from a booming economy rather than slowing economic activity. Connecticut continues to have one of the lowest unemployment rates in the country, with only Minnesota and Iowa reporting lower rates for the month of June. We project employment will continue to

expand, although more slowly, adding 6,500 new jobs between 2000-Q2 and 2000-Q3 and a total of about 22,000 new jobs by 2001-Q2.

Connecticut's growth occurs in an environment of strong national economic performance. Preliminary 2000-Q2 data show U.S. real GDP advancing by nearly six percent. GDP growth has seldom been faster in the current expansion.

Connecticut housing permits, although strong in the first quarter, fell both on a year-over-year and an annualized basis this quarter. This decline follows a national drop in the pace of consumption spending. While personal income, in nominal terms, remains strong, growth in real personal income is slowing as inflation, fueled by volatile energy prices, heats up.

Interest rates are another key influence on the number of new housing permits issued. Slowing housing permit activity suggests that the recent series of rate hikes is beginning to filter through the economy. We will be watching carefully as Greenspan tries to slow inflation and engineer the economy's soft landing.

Despite these warning signs of a future slowdown, gross economic measures remain strong, and for the time being the economy continues to boom.

Support for Open Spaces Strong, But Other Issues Have Funding Priority

By Chase H. Harrison
Center for Survey Research and Analysis

Connecticut residents are concerned about the amount of open space in Connecticut, and they generally support efforts to preserve rural areas of the state. But when state spending is involved, support for open lands takes a back seat to other issues.

In a recent survey sponsored by *The Connecticut Economy*, Connecticut residents listed water pollution ahead of open space as an area of immediate environmental concern. From a list of six environmental problems, nearly one-fourth (24%) of respondents reported that water pollution was the chief environmental problem in their area, followed by the destruction of open space (17%), air pollution (16%), and hazardous waste disposal (15%). Fewer Connecticut residents mentioned litter (8%) and household garbage (7%).

When asked their feelings about the sufficiency of actively used open space such as parks and passively used space such as state forests, 40% of respondents supported acquiring at least some additional open space for either active or passive use, while 28% thought the current amount of open space in the state was sufficient. At least 6% thought the state needed less total open space than it currently has. About one Connecticut resident in five (21%) would redistribute the amount of open space currently available, with most favoring greater recreational use. As the centerfold map shows (pages 10-11), Connecticut open space is more concentrated East of the River and in the Northwest Hills, and less concentrated along the Connecticut River and in Fairfield County. Survey responses, however, were not significantly different across regions.

Overall, residents seem moderately willing to pay for additional public lands, but see this as a lower priority than other possible uses of tax dollars. Forty percent of residents strongly support the pub-

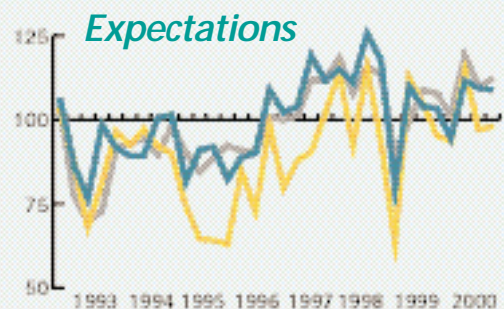
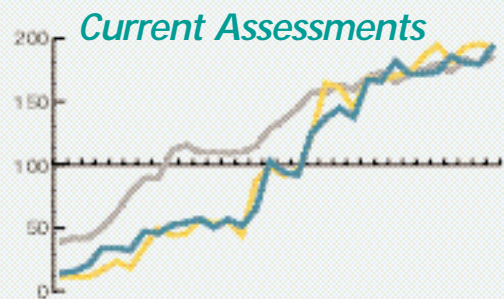
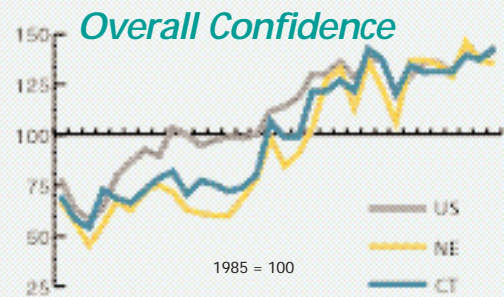
lic purchase of open space and 34% are somewhat supportive. But when given a choice for the use of tax dollars, residents assign only a moderate priority to spending on public lands. A separate CSRA survey conducted in February found residents less supportive of funding for open space preservation and more supportive of spending to reduce air pollution, and to clean up inland and coastal waterways. Interestingly, that survey found substantially less support for funding state parks than for preserving open space such as forests and farms. And a May poll for the *Hartford Courant* found spending on open space ranked seventh in overall importance for state spending, behind funding for schools and highways, and behind income and gasoline tax cuts, but ahead of business tax reductions and urban development.

Still, Connecticut residents believe that protecting the environment may require sacrificing economic growth and many are willing to make the sacrifice. Three-fourths of residents surveyed (76%) reported that the statement "We must sacrifice economic growth in order to preserve and protect the environment" was closer to their opinion than the statement "We must be prepared to sacrifice environmental quality for economic growth."

A more immediate measure of the willingness to make environmental sacrifices is to test specific environmental policies against prospective costs. One proposal for reducing air pollution is to place a tax on fossil fuels such as oil, coal, and natural gas. Advocates argue this would help prevent the greenhouse effect—the potential destruction of the earth's ozone layer—by encouraging alternative energy technologies. Connecticut residents are split on whether this tax increase would be a good idea, with approximately equal proportions supporting (41%) and opposing (43%) this policy idea.



Consumer Confidence Survey



Source: National and New England data are from the Conference Board, Inc.

July Consumer Confidence Hits New High

Connecticut consumer confidence hit a new high in July 2000, driven primarily by improved assessments of current conditions. Nationally, confidence also increased and in New England it remained stable at relatively high levels.

Overall consumer confidence in Connecticut is slightly above its previous high set in April 1998. After a sudden drop in 1998, the overall confidence measure has slowly worked its way back to its present position. Throughout the period, current assessments have generally stood above the April 1998 measure, while future expectations have stayed below the levels recorded then. This summer's reading repeats this pattern, but the record high assessment that Connecticut consumers give to current economic conditions has driven the overall measure of consumer confidence to a new high.

The survey was conducted by CSRA among 501 Connecticut residents from July 15 to 28, 2000.

Bridgeport LMA

Ansonia	7.9%	0.01	0.02
Beacon Falls	22.2	0.25	0.25
Bridgeport	8.4	0.00	0.01
Derby	17.7	0.04	0.05
Easton	1.2	0.03	0.03
Fairfield	15.3	0.04	0.06
Milford	6.3	0.02	0.02
Monroe	7.6	0.04	0.07
Oxford	7.8	0.12	0.18
Seymour	3.7	0.02	0.02
Shelton	5.7	0.02	0.03
Stratford	2.4	0.00	0.01
Trumbull	12.2	0.05	0.05

Danbury LMA

Bethel	5.6%	0.02	0.03
Bridgewater	14.0	0.68	0.83
Brookfield	4.8	0.03	0.04
Danbury	7.2	0.02	0.03
New Fairfield	17.5	0.15	0.17
New Milford	5.3	0.06	0.08
Newtown	11.3	0.14	0.18
Redding	14.8	0.32	0.37
Ridgefield	19.1	0.16	0.19
Roxbury	3.2	0.26	0.27
Sherman	7.9	0.26	0.37
Washington	11.2	0.47	0.67

Danielson LMA

Brooklyn	3.0%	0.02	0.08
Eastford	47.4	5.69	6.09
Hampton	25.1	1.93	2.52
Killingly	5.4	0.08	0.10
Pomfret	14.1	0.82	1.07
Putnam	4.6	0.03	0.07
Scotland	19.5	1.11	1.61
Sterling	20.0	0.89	1.24
Thompson	7.7	0.11	0.26
Union	50.7	13.32	13.58
Voluntown	59.0	6.37	6.42
Woodstock	6.7	0.28	0.40

Hartford LMA

Andover	14.5%	0.43	0.51
Ashford	25.7	1.26	1.62
Avon	15.6	0.13	0.17
Barkhamsted	22.1	1.44	1.45
Berlin	14.8	0.11	0.14
Bloomfield	18.9	0.13	0.17
Bolton	8.6	0.12	0.17
Bristol	7.5	0.01	0.02
Burlington	11.3	0.26	0.27
Canton	3.6	0.07	0.07
Chaplin	33.6	1.52	1.86
Colchester	11.0	0.25	0.26
Columbia	2.9	0.07	0.08
Coventry	7.4	0.09	0.16
Cromwell	11.4	0.05	0.07
Durham	21.8	0.39	0.50
East Granby	8.7	0.16	0.22
East Haddam	17.0	0.52	0.79
East Hampton	20.5	0.40	0.42

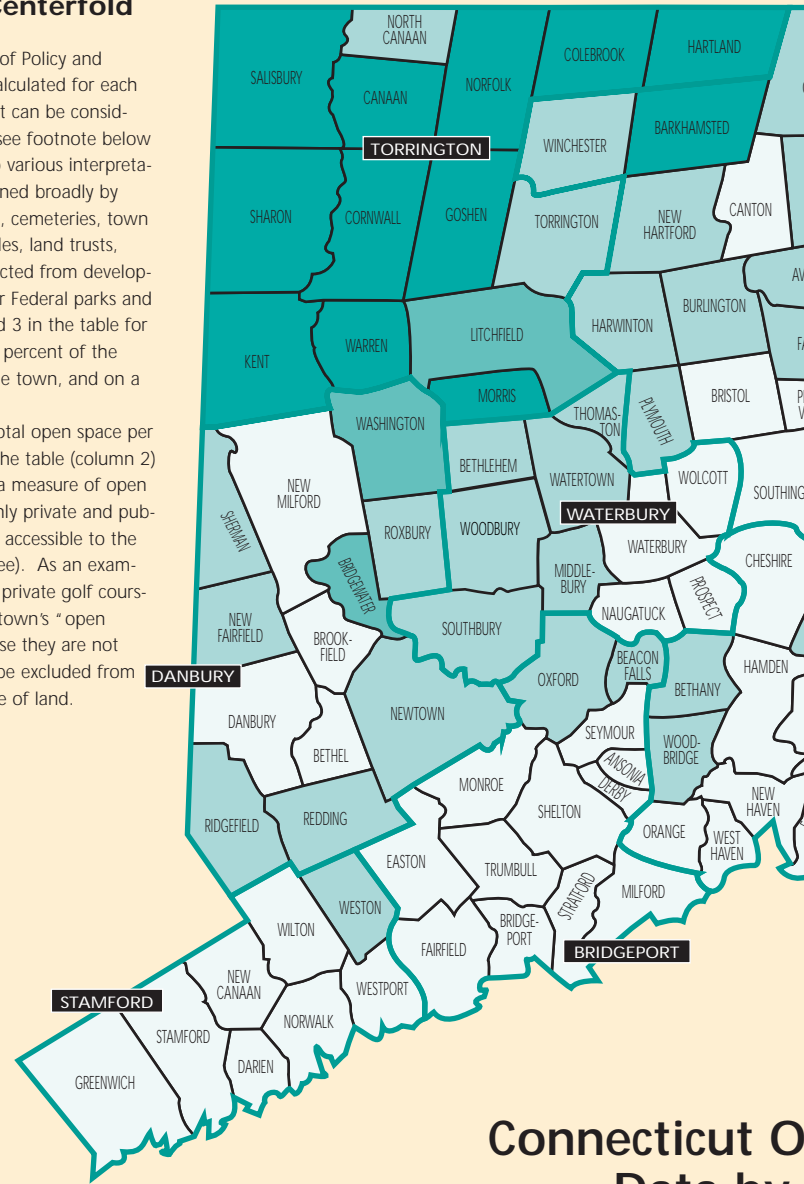
East Hartford	6.8%	0.01	0.02
East Windsor	7.6	0.08	0.13
Ellington	11.5	0.15	0.21
Enfield	10.4	0.02	0.05
Farmington	27.9	0.21	0.24
Glastonbury	11.6	0.11	0.13
Granby	16.6	0.44	0.45
Haddam	24.7	0.92	0.96
Hartford	15.2	0.01	0.01
Harwinton	12.7	0.41	0.47
Hebron	18.7	0.40	0.54
Lebanon	13.1	0.35	0.70
Manchester	8.0	0.02	0.03
Mansfield	20.5	0.20	0.33
Marlborough	16.9	0.44	0.44
Middlefield	17.0	0.25	0.34

Middletown	5.4%	0.02	0.03
New Britain	14.8	0.01	0.02
New Hartford	10.6	0.29	0.41
Newington	8.0	0.01	0.02
Plainville	4.7	0.01	0.02
Plymouth	11.6	0.07	0.13
Portland	30.0	0.47	0.51
Rocky Hill	7.2	0.03	0.04
Simsbury	23.1	0.20	0.23
Somers	13.8	0.08	0.27
South Windsor	6.9	0.04	0.05
Southington	5.9	0.02	0.04
Stafford	19.8	0.59	0.63
Suffield	5.5	0.05	0.13
Tolland	9.9	0.15	0.20
Vernon	10.3	0.03	0.04

Reading the Centerfold

The Connecticut Office of Policy and Management (OPM) has calculated for each town the total acreage that can be considered "open," as of 1998 (see footnote below map). Although subject to various interpretations, "open space" is defined broadly by OPM to include local parks, cemeteries, town greens, subdivision set-asides, land trusts, easements, farmland protected from development, schools, and State or Federal parks and forests. (See columns 1 and 3 in the table for open space presented as a percent of the total geographic area of the town, and on a per capita basis.)

While the map shows total open space per capita, we also include in the table (column 2) a more restricted per capita measure of open space that encompasses only private and public lands that are open and accessible to the public (with or without a fee). As an example, protected farmland or private golf courses would be included in a town's "open space" acreage, but because they are not publicly accessible, would be excluded from the "open access" measure of land.



Connecticut O Data by

Source: Developed by *The Connecticut Economy* based on data from the Connecticut Office of Policy and Management. The classification of land as "open" is subject to various interpretations. In addition, the accuracy of the data is somewhat diminished by the low response rate of towns in furnishing land data as well as some imprecision in the data.

West Hartford	13.7%	0.02	0.03
Wethersfield	15.2	0.02	0.05
Willington	3.6	0.11	0.12
Winchester	5.5	0.09	0.10
Windham	11.5	0.04	0.09
Windsor	9.9	0.12	0.16
Windsor Locks	5.3	0.01	0.01

Lower River LMA

Chester	38.8%	1.01	1.03
Deep River	29.5	0.38	0.58
Essex	10.1	0.09	0.11
Lyme	18.5	1.49	1.85
Westbrook	9.7	0.11	0.17

New Haven LMA

Bethany	6.5%	0.17	0.18
Branford	1.5	0.01	0.01
Cheshire	5.9	0.03	0.05
Clinton	10.4	0.06	0.08
East Haven	7.3	0.01	0.02
Guilford	9.7	0.13	0.15
Hamden	23.8	0.09	0.09
Killingworth	18.9	0.50	0.76
Madison	15.9	0.15	0.23
Meriden	13.6	0.03	0.04
New Haven	20.5	0.02	0.02
North Branford	4.2	0.02	0.05
North Haven	5.3	0.03	0.03
Orange	8.7	0.03	0.08
Wallingford	17.0	0.07	0.10

West Haven	6.4%	0.00	0.01
Woodbridge	9.4	0.08	0.14

New London LMA

Bozrah	12.0%	0.29	0.65
Canterbury	3.0	0.14	0.16
East Lyme	21.4	0.28	0.29
Franklin	17.1	0.49	1.17
Griswold	24.7	0.44	0.51
Groton	14.7	0.05	0.07
Ledyard	21.2	0.14	0.35
Lisbon	2.4	0.04	0.06
Montville	5.5	0.06	0.09
New London	14.1	0.01	0.02
North Stonington	15.7	0.72	1.09
Norwich	4.8	0.02	0.02
Old Lyme	8.4	0.19	0.12
Old Saybrook	11.6	0.10	0.11
Plainfield	8.6	0.14	0.16
Preston	3.0	0.09	0.12
Salem	7.5	0.37	0.38
Sprague	4.1	0.05	0.12
Stonington	10.0	0.11	0.14
Waterford	8.8	0.06	0.10

Stamford LMA

Darien	11.0%	0.01	0.05
Greenwich	16.2	0.04	0.09
New Canaan	6.4	0.04	0.05
Norwalk	10.8	0.01	0.02
Stamford	9.0	0.01	0.02
Weston	14.4	0.17	0.21
Westport	8.6	0.03	0.05
Wilton	8.8	0.06	0.09

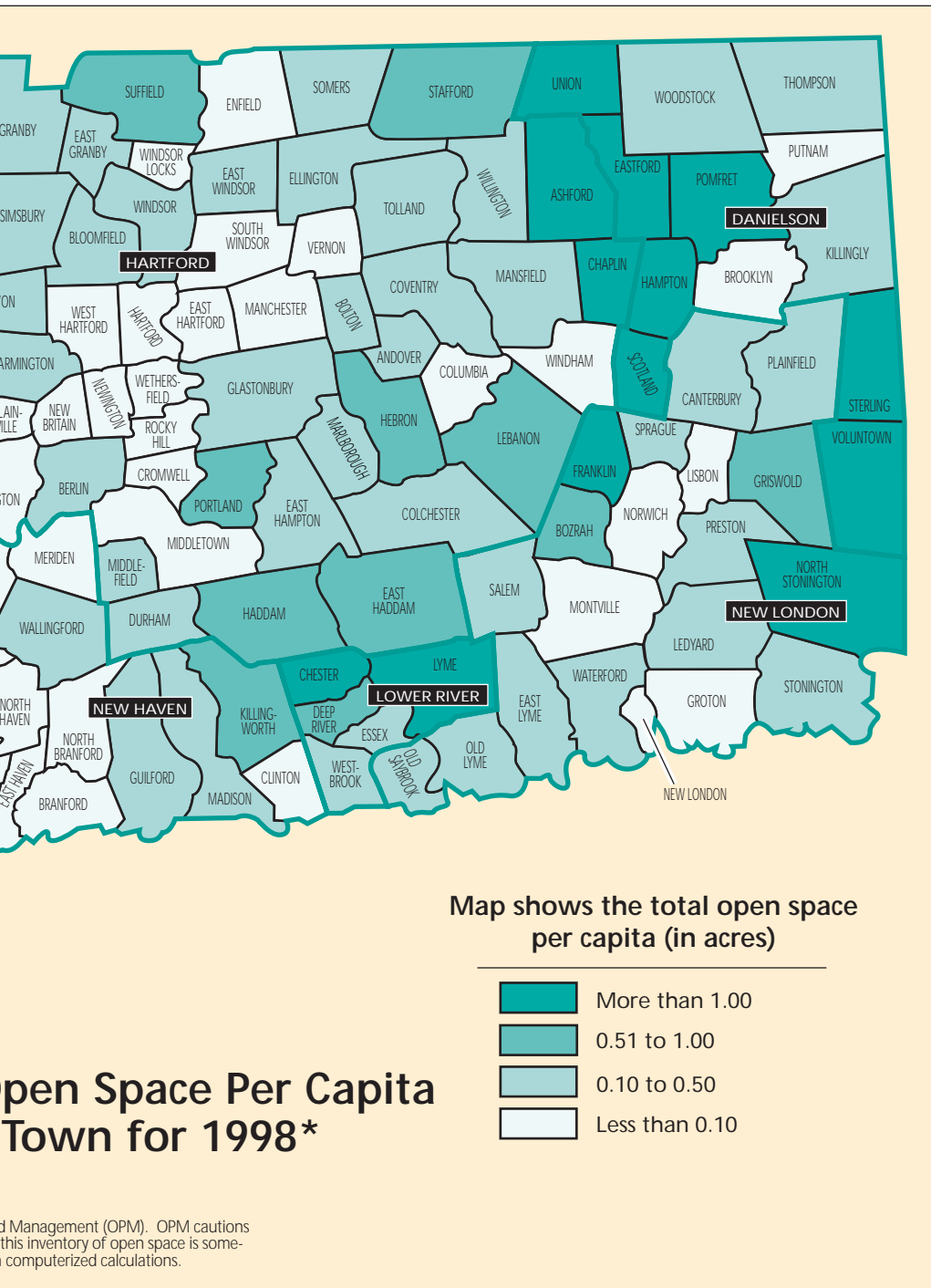
Torrington LMA

Canaan	34.1%	4.76	6.84
Colebrook	23.5	1.82	3.32
Cornwall	25.5	4.46	4.99
Goshen	11.8	0.81	1.34
Hartland	43.6	4.67	4.71
Kent	23.8	1.55	2.39
Litchfield	17.9	0.65	0.74
Morris	28.3	0.92	1.47
Norfolk	14.7	1.03	2.10
North Canaan	11.0	0.29	0.39
Salisbury	31.3	0.37	2.78
Sharon	24.1	2.00	3.04
Torrington	18.4	0.10	0.13
Warren	8.6	1.03	1.10

Waterbury LMA

Bethlehem	4.3%	0.06	0.16
Middlebury	10.4	0.16	0.20
Naugatuck	11.7	0.03	0.04
Prospect	0.5	0.01	0.01
Southbury	11.0	0.15	0.17
Thomaston	18.2	0.12	0.19
Waterbury	12.8	0.01	0.02
Watertown	13.7	0.10	0.12
Wolcott	5.2	0.02	0.05
Woodbury	3.6	0.08	0.10

Town Average 14.1% 0.10 0.13



Falling Bridges, Rising Prices, and the Connecticut Motor Fuel Tax

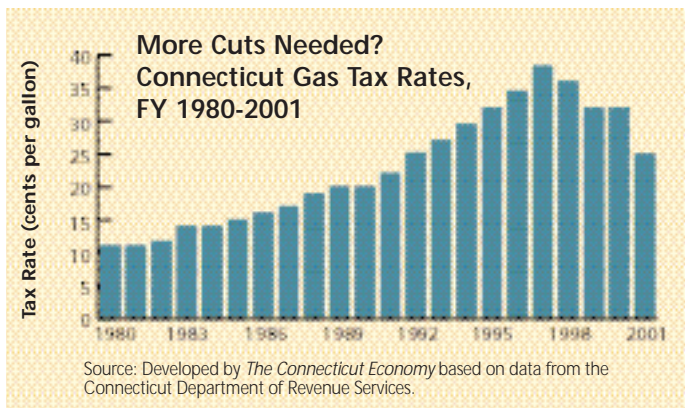
By Dennis Heffley

Connecticut's gasoline tax policy is a mix of local history, market conditions, and state politics. Spurred by a local tragedy in the early 1980s, political leaders boosted the gas tax to fund road improvements. Now, with better roads and higher prices at the pump, the gas tax has been cut 14 cents a gallon, nearly 36%, since 1997. Will further cuts benefit consumers?

In June 1983, a chunk of I-95 fell 75 feet into Fairfield County's Mianus River, killing three and injuring as many. A decaying road network suddenly became more than a nuisance. An earlier issue (Fall 1999) described the response—a multi-billion dollar program to upgrade Connecticut's roads and bridges. By 2000, roughly \$11.5 billion had been invested.

How did the state finance these improvements? Federal subsidies eased the way, but Connecticut still had to ante up its share. Back then, the state had no broad-based personal income tax, so it relied heavily on the general sales tax. Further increasing the 7.5% sales tax—then among the nation's highest—might have added little revenue if consumers responded by purchasing goods in states with lower sales taxes.

Gasoline taxes faced similar potential problems. But evidence that gasoline demand was not very responsive to price increases, at least in the short-run, may have reduced border-crossing worries. Besides, many viewed the gas tax as a "user fee" and thus the best source of highway funds. So legislators initiated a series of gas tax increases, as shown below.



During the early 1980s, when Connecticut's gas tax was flat, at 11 cents a gallon, revenue also remained flat—about \$150 million per year. Subsequent rate hikes continued through FY97, boosting yearly collections to \$542 million. Cuts in the tax, from a peak of 39 cents in FY97 to 32 cents in FY99, quickly trimmed revenue to \$490 million in FY99. Final figures for FY00 are not yet available, but revenue will likely fall below FY99 levels. On July 1, 2000, the tax dropped further, to 25 cents. Based on past data, \$360-365 million would be a reasonable revenue projection for FY01, assuming the new rate holds until next July.

But just how essential are gas taxes? Given past limitations on using general fund revenue for transportation, higher gas taxes may have been necessary to jump-start major highway improvements. Yet, in relative terms, gas taxes have dwindled. In FY80, they accounted for 9.1% of total state taxes. Despite increases in both the rate and associated revenue, the share fell to 6.7% in FY97. Subsequent reductions in the rate and revenue

have further cut the share to 5.4%. The gas tax is visible to consumers, especially when it causes conspicuous price gaps with bordering states, but it has faded as a revenue source in an economy where income, retail sales, and other taxable transactions have outpaced the volume of gasoline pumped. Still, there may be other reasons to tax gasoline.

Other Motives

Some officials advocate further cutting or even repealing the Connecticut Motor Fuels Tax. National leaders have discussed doing the same to the 18.4-cent per gallon federal tax. If enacted, such cuts would please many consumers: a national poll last March indicated that nearly 60% favored eliminating the federal gas tax. Combine the popular appeal of lower prices at the pump with the declining revenue importance of gas taxes, and you have an issue that is equally popular with politicians.

But gas taxes are more than a revenue source. By affecting market prices, gas taxes influence the volume of travel and its unwanted by-products. Market conditions shape these outcomes. In particular, the less buyers and sellers react to gas price changes, the more a tax cut will reduce prices without greatly increasing consumption, road congestion, and emissions. We might hope for these conditions, where tax cuts would trim consumers' fuel costs without clogging our roads or seriously damaging air quality. But such conditions exist more in the short-run than in the long-run.

Time Matters

Ever wonder why Europeans own fewer vehicles, drive smaller cars, ride more trains, and commute shorter distances than Americans? It's not simply a matter of lower incomes, different tastes, or mass-transit subsidies, though all play a role. Often paying prices of \$5 per gallon—mostly due to higher taxes—Europeans have made long-run adjustments in the number, types and fuel-efficiency of vehicles, car-pooling habits, available modes of travel, and even homesites and worksites.

Studies of the price-sensitivity of gasoline buyers and sellers generally ignore such long-run adjustments, concluding that "prices don't greatly affect how much we drive" and that gasoline inventories limit supply responses to price changes. Again, these are the conditions that make gas tax cuts sensible, but they exist primarily in the short-run. Greater long-run price responsiveness, on the part of sellers and buyers, means that large tax cuts might barely trim gas prices, while significantly raising gas consumption, emissions, and road congestion by encouraging wasteful driving habits, oversized and overpowered vehicles, and inefficient location patterns. With Southwest Connecticut's road congestion and emissions problems, and the State's desire to attract more tourists, this environmental "downside" of gas tax cuts warrants consideration.

Is Less Better?

Establishing sound gas tax policy in a small, densely populated state can be complex. Tax rate changes trigger changes in prices, fuel use, tax collections, environmental conditions, and even the tax policies of neighboring states. Connecticut's decision to boost gas taxes in the wake of the Mianus River Bridge collapse was the quickest way to launch a massive road improvement program. Today, with a more stable mix of general taxes, a robust economy, and a healthy budget surplus, the need to retain high gas taxes is being questioned. But, taking into account long-run responses, gas taxes may yield environmental benefits that should enter into policy discussions of the appropriate tax rate.

Was the Gas Tax Cut Good News? Well, Yes, But...

By Stanley McMillen

On July 1, 2000, Connecticut cut its gasoline tax by 7 cents a gallon, a move Governor Rowland had been advocating for some time. The cut was doubtless good news, if meager relief, for motorists facing this year's sky-high prices at the pump. But that's not all there is to the story.

Economists, the dismal scientists, can find a dark cloud on the brightest day—think of Alan Greenspan wringing his hands over rapid economic growth. Say “gas tax cut” to an economist and the party-pooper immediately asks how it will affect the rest of the government’s budget: Losing \$75-100 million in gas tax revenue requires that something else has to give, whether government spending or taxes or both. The grinch will also probably want to know how the cut will alter the tax structure and possibly whether revenues previously lost across state borders will be recaptured.

The Connecticut Center for Economic Analysis (CCEA) calculated and compared the overall impacts of the gas tax cut on the state’s economy under three different “what if?” scenarios. The first one—the current policy—blends spending cuts (“reallocations”) in the current budget with some deferred payments. The second scenario uses matching cuts in State spending in this budget to offset the loss of gas tax revenue. The third scenario re-balances the budget with a hike in the Connecticut income tax.

Which plan is best? All three boost the economy. The first scenario has the largest impact on economic performance, as well as on the size of the state’s population. Scenario three comes in second on these measures, and, because State income taxes are deductible in calculating Federal taxable income, also lessens the overall tax burden in Connecticut and makes the distribution of after-tax income more equal. Scenario two—just cutting State spending—comes in dead last on both counts.

The CCEA began by computing exactly how much revenue was at stake. That depends on how responsive gasoline use in Connecticut is to changes in price and income. Lowering the tax of course cuts prices at the pump. But it will also give consumers a *de facto* increase in their incomes, enhancing their abilities to buy *all* goods and services. Using data for 1993-2000 on state personal income, monthly gasoline use (from the Department of Revenue Services), and prices (from the Hartford office of the American Automobile Association), the CCEA found

that, when the price of gasoline drops by 4% (\$0.07/\$1.75), consumption increases by only 2%. Further, an income increase of 1% raises gasoline use by about 0.35%. The residents of Connecticut, as elsewhere, don’t vary their gasoline use much when either its price or

their incomes change. Using these “elasticities,” we calculate the net loss in revenues from the Rowland gas tax cut to be \$86.9 million a year.

Knowing the extent of the damage to the budget, we can then compare the effects on our economy of different kinds of repairs. The CCEA used the baseline forecast of a dynamic model of the

Three Options For Filling the Gas Tax Gap

Scenario	Jobs	Real GSP	Real Income	Population
1	+1,530	+\$72.1 Mil	+44.7 Mil	+2,800
2	+580	+\$32.8 Mil	+4.1 Mil	+1,980
3	+740	+\$35.5 Mil	+16.1 Mil	+1,100

Connecticut economy, assuming no tax cut, to compare the impacts through 2010 of the three scenarios outlined earlier. In all three cases, cutting the gas tax yields economic gains for the state, which reflects the increased economic activity resulting from lower costs for gasoline and for goods and services produced with gasoline. But the gains vary quite a bit in magnitude. And they have quite different impacts (not captured in the model) on Connecticut’s overall tax burden and the distribution of after-tax income.

The table shows the effect of the gas tax cut on four variables: jobs; real gross state product or GSP; real personal income; and population. All figures are yearly averages over the period 2000-2010.

The table shows clearly the extra “oomph” imparted to the state’s economy under the first scenario—double or more than realized under the third. But the third scenario would cost Connecticut taxpayers only \$61.7 million in higher State income taxes—obtained by raising the top rate from 4.5% to 4.59%—to replace the \$86.7 million in lost gas taxes. That’s because for every additional dollar of income taxes the State collects, taxpayers fork over only 71 cents, net, owing to increased deductions under the Federal income tax. (See *The Connecticut Economy*, Spring 1999.)

The third scenario would also likely improve the “fairness” of the overall tax burden. Gasoline taxes, because demand is so unresponsive to income changes, as noted above, are “regressive”: Less well-off taxpayers tend to pay a higher percentage of their incomes in gas taxes than do wealthier taxpayers. In contrast, the Connecticut income tax is quite progressive—the well-off pay a higher percentage of total State income tax revenues than their percentage of total income. One qualifier is that better-off residents are more likely to itemize deductions on their Federal returns, and a good proportion of the reduced tax burden under the third scenario would go to them.

Reducing the gas tax is likely to have effects beyond those detailed here. It may bring back some folks who’ve been buying their gas in neighboring states. It may induce some convenience stores—which sell revenue generators like gas, cigarettes, and lottery tickets—to move back across the border. Effects like those are hard to capture in a dynamic model, but to the extent they occur, the revenue impact of cutting the gas tax would be smaller than reported above. Also, our estimates of the effects on state employment, GSP, personal income and population would be too low.



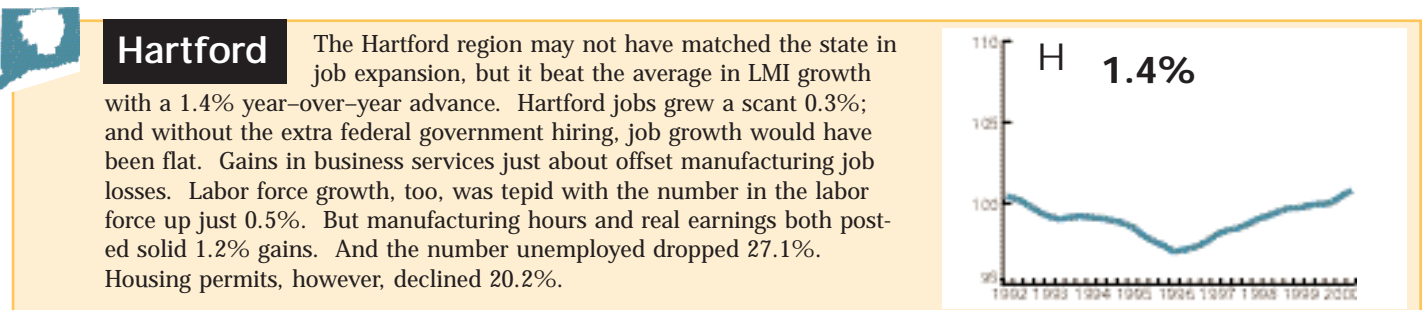
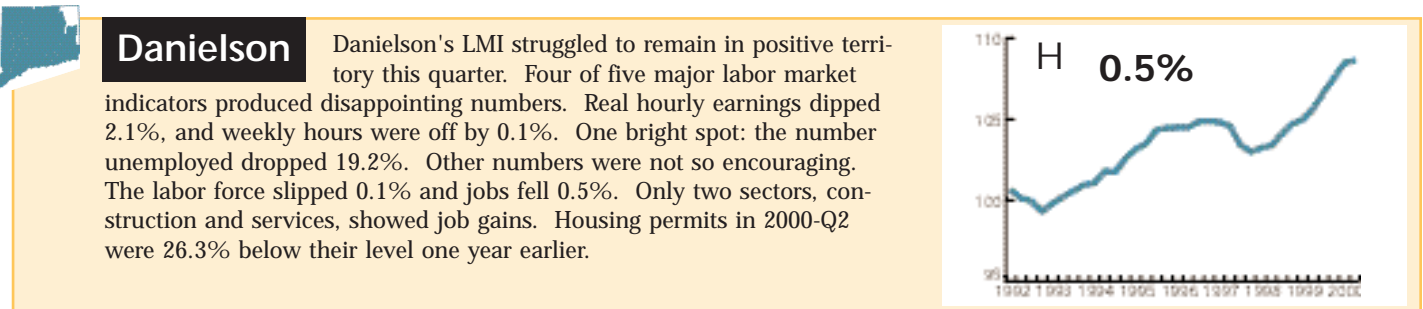
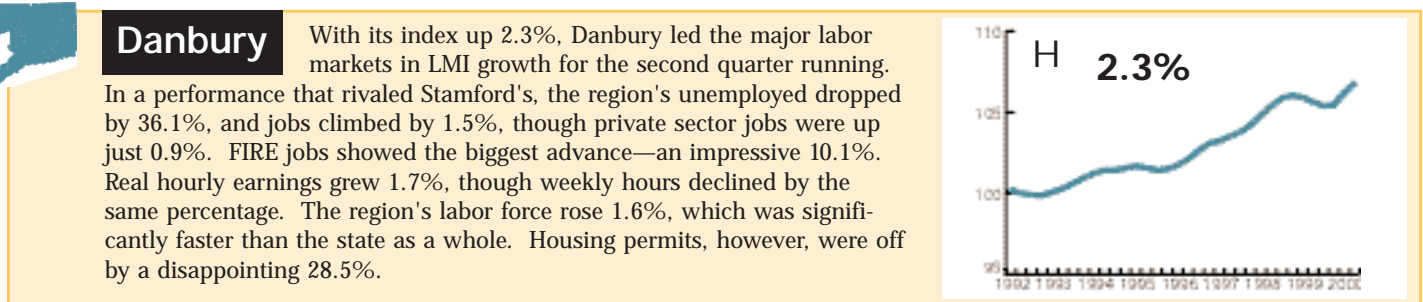
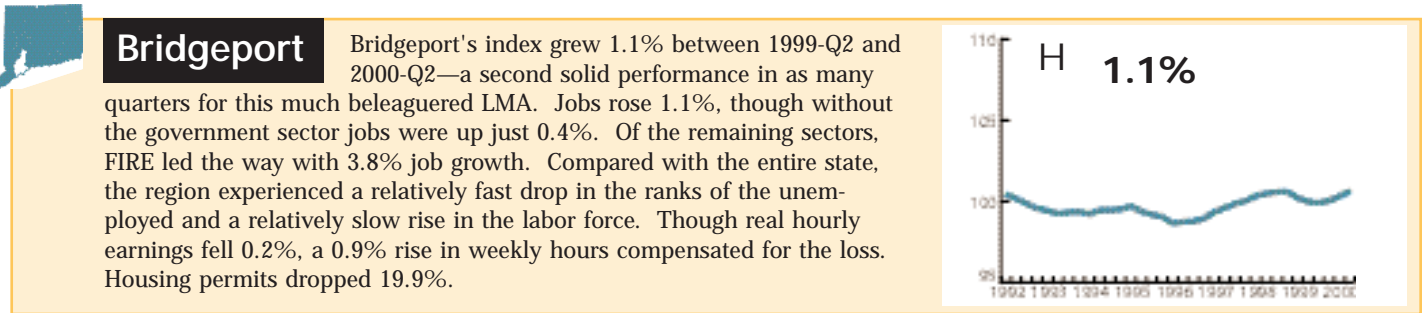
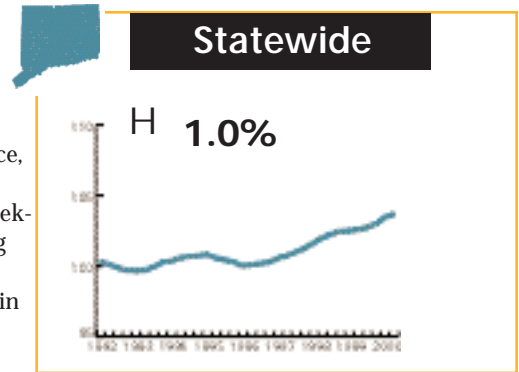
Labor Markets Take a Breather

By Steven P. Lanza

The statewide labor market activity index, or LMI, advanced 1.0% between 1999-Q2 and 2000-Q2. That's significantly off the pace set last quarter but faster than the norm for the current recovery. Each of the ten regions took a breather this quarter, and two, Danielson and Waterbury, strained to show any improvement. Jobs moved up by 1.4%, though the addition of temporary Federal government Census workers overstated the real gain. Government jobs aside, four regions—Hartford, Waterbury, Torrington and Danielson—realized no net increase in jobs. Other signs the regions are keeping their cool this summer: real manufacturing earnings are down in as many regions as they are up, and weekly hours are once again on the decline. Still, it's hard to keep a strong economy down, and 2000-Q2 saw another stunning drop in the number unemployed, which plunged statewide by 28.9%. The smallest decline, a mere 22%,

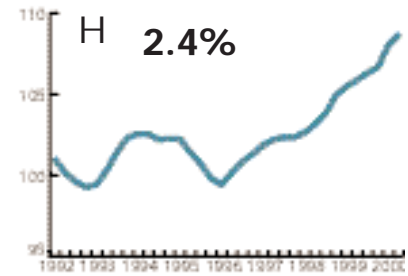
came in Danielson. Rising interest rates, however, are putting a heavy burden on the market for new homes. New housing permits tumbled 21.1% statewide—the worst showing in 32 quarters. Only two regions—Waterbury and Stamford—reported any increased housing permit activity.

The LMI, indexed so 1992 = 100, measures year-to-year changes in five key variables for each labor market region of the state and for the state as a whole: labor force, jobs, number unemployed, weekly manufacturing hours, and real hourly earnings in manufacturing.



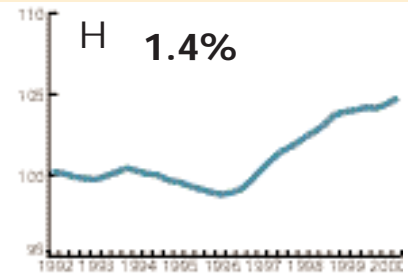
Lower River

Lower River's LMI rose by 2.4% this quarter, the same rate at which the area added jobs, for the best showing of the minor labor market regions. Though the job gains came principally in FIRE, government and the services, Lower River was one of only three regions to add manufacturing jobs. Lower River led the ten labor markets with a 3.0% jump in its labor force and was also a leader in reducing the number unemployed, which dropped by 33.3%. Housing permits, though, were off by 18.4%.



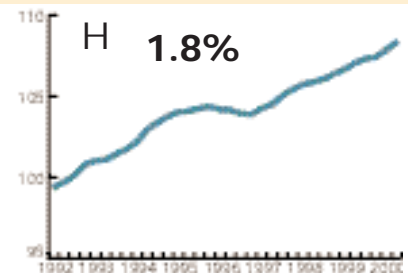
New Haven

New Haven was one of only two regions whose second quarter LMI performance outshone its first. Jobs grew by 0.9%, compared with a 0.5% increase in 2000-Q1, and the labor force gained 1.4% compared with a 0.7% increase in the quarter before. The number unemployed dropped 24.9%. Though New Haven owed half its jobs gains to federal government hires, it also added both manufacturing and service jobs. Despite the additions in manufacturing, real earnings dropped 0.1%, and weekly hours declined 0.4%. New Haven also lost steam in the housing market, with permits down 34.9%.



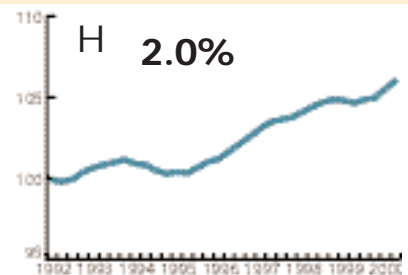
New London

Like New Haven, New London swam against the tide this quarter, as its LMI grew faster in 2000-Q2 than in 2000-Q1. With increases in trade, services, and especially government, jobs rose 1.3%. Manufacturing jobs, though, suffered some casualties. New London enjoyed a strong 1.7% year-over-year growth in the labor force and a 25.8% drop in the number unemployed. Though manufacturing hours fell 0.9%, the region enjoyed the largest advance in real hourly earnings among the major labor market areas. Although New London was a leader in housing permit activity in 2000-Q1, new permits declined 19.3% in 2000-Q2.



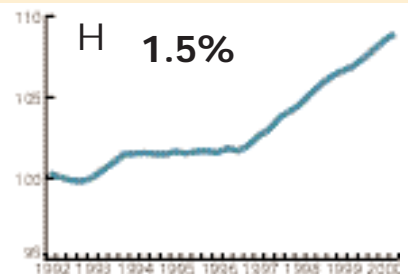
Stamford

Except for real earnings, all of Stamford's economic indicators contributed to an impressive quarter for the region. Jobs rose 1.7%, and the number unemployed declined 36.3%, making Stamford tops in unemployment reduction. Manufacturing and transportation suffered some job losses, but FIRE and services posted strong gains. The labor force increased 2.0%, outpacing all other major labor markets, but barely keeping up with jobs. Stamford's 5.1% drop in real earnings was high but not unusual—the region hasn't registered real earnings growth in 15 quarters. Housing permits inched up 2.9%.



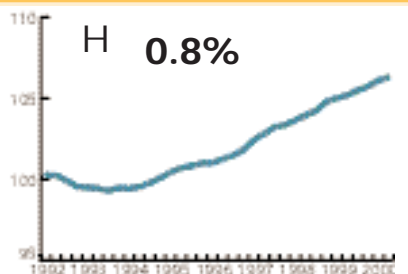
Torrington

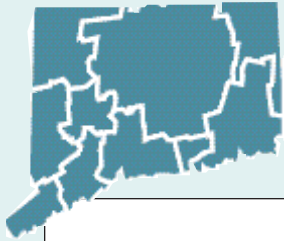
A big drop in the number unemployed contributed much to the 1.5% increase in Torrington's LMI between 1999-Q2 and 2000-Q2. As the ranks of Torrington's unemployed thinned by 30.0%, the region added 1.0% to its labor force. Jobs managed a modest 0.7% increase, though without new Federal government hiring, the region's job totals would have been flat. A 0.1% increase in real hourly earnings did little to offset a 0.5% fall in weekly hours. Torrington's housing permits suffered the worst drop among the regions—35.5%.



Waterbury

Waterbury was the laggard among the major regions this quarter, with its LMI inching up just 0.8%. One of the region's best statistics was its 29.7% drop in the number unemployed, but that figure was only about average for the ten labor market areas. And while total nonfarm jobs grew at a modest 0.6% rate, total private jobs actually fell 0.2%. Weekly manufacturing hours increased 0.8%, but real hourly earnings slipped 1.5%. Waterbury's 2000-Q2 distinction?—a 12.5% jump in new housing permit activity.





Labor Market Data

Labor Market Area	Labor Force		Nonfarm Jobs		Manufacturing Jobs	
	2000-Q2 (000)	% Change Year Ago	2000-Q2 (000)	% Change Year Ago	2000-Q2 (000)	% Change Year Ago
Bridgeport	216.4	0.7	190.3	1.1	36.9	-2.7
Danbury	109.8	1.6	90.4	1.5	19.1	-0.7
Danielson	32.8	-0.1	21.0	-0.5	5.2	-5.4
Hartford	578.2	0.5	615.9	0.3	89.7	-3.0
Lower River	12.5	3.0	10.1	2.4	2.8	1.2
New Haven-Meriden	272.8	1.3	261.1	0.9	40.3	1.3
New London-Norwich	154.0	1.7	142.9	1.3	23.5	-1.5
Stamford	196.2	2.0	213.9	1.7	25.1	-2.8
Torrington	39.9	1.0	30.7	0.7	6.1	-1.1
Waterbury	116.0	0.5	88.9	0.6	18.4	1.5
Statewide	1,711.3	1.0	1,698.0	1.4	265.7	-1.7

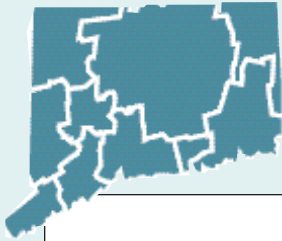
Labor Market Area	Construction Jobs		Trade Jobs		FIRE* Jobs	
	2000-Q2 (000)	% Change Year Ago	2000-Q2 (000)	% Change Year Ago	2000-Q2 (000)	% Change Year Ago
Bridgeport	6.7	1.0	42.4	1.7	11.8	3.8
Danbury	4.1	2.5	20.8	-2.0	5.8	10.1
Danielson	1.0	11.1	5.3	-1.9	0.6	0.0
Hartford	22.5	5.0	122.7	-0.7	72.7	-0.2
Lower River	0.4	0.0	2.0	-3.2	0.4	20.0
New Haven-Meriden	10.1	1.7	54.0	-0.7	12.5	-3.3
New London-Norwich	5.0	2.7	28.7	1.5	3.8	0.9
Stamford	6.7	5.2	44.6	0.2	28.2	6.1
Torrington	2.2	3.1	6.6	0.5	1.0	11.1
Waterbury	3.7	5.8	18.3	0.5	4.0	2.6
Statewide	64.2	3.5	362.6	1.2	141.0	0.5

* Finance, Insurance & Real Estate

Labor Market Area	Service Jobs		Government Jobs		TCU* Jobs	
	2000-Q2 (000)	% Change Year Ago	2000-Q2 (000)	% Change Year Ago	2000-Q2 (000)	% Change Year Ago
Bridgeport	62.4	0.9	22.9	6.4	7.3	-0.9
Danbury	26.2	2.6	11.5	5.2	2.9	0.0
Danielson	5.2	4.7	3.2	-1.0	0.5	0.0
Hartford	182.8	1.7	98.5	1.6	27.1	-1.6
Lower River	3.1	5.6	1.0	7.4	0.4	-7.7
New Haven-Meriden	93.8	1.3	34.1	4.3	16.4	-0.4
New London-Norwich	36.8	2.0	37.7	2.5	7.3	-0.5
Stamford	79.8	2.4	19.1	3.1	10.4	-1.0
Torrington	10.5	0.6	3.8	5.6	0.5	-28.6
Waterbury	26.3	-2.8	14.0	5.0	4.2	-0.8
Statewide	540.5	2.3	245.4	3.2	78.6	0.4

*Transportation, Communications, and Utilities

Sources: Quarterly figures developed by *The Connecticut Economy* based on monthly estimates from the Connecticut Department of Labor. Figures are not seasonally adjusted. Statewide totals are not necessarily the sums of individual labor market areas.



L a b o r M a r k e t D a t a

Labor Market Area	Number Unemployed		Unemployment Rate (%)		Initial Unemployment Claims	
	2000-Q2 (000)	% Change Year Ago	2000-Q2	1999-Q2	2000-Q2	% Change Year Ago
Bridgeport	6.3	-31.2	2.9	4.3	1103	-16.6
Danbury	1.8	-36.1	1.6	2.6	337	+19.2
Danielson	1.1	-22.0	3.3	4.2	212	-11.9
Hartford	14.6	-27.1	2.5	3.5	2,885	-14.9
Lower River	0.2	-33.3	1.6	2.5	*	*
New Haven-Meriden	6.9	-25.3	2.5	3.4	1,218	+0.6
New London-Norwich	3.8	-25.8	2.5	3.4	612	-13.7
Stamford	2.9	-36.3	1.5	2.3	433	-23.3
Torrington	0.7	-30.0	1.8	2.5	249	-41.4
Waterbury	3.5	-29.7	3.0	4.3	654	-8.4
Statewide	41.3	-28.9	2.4	3.4	7,702	-13.0

* Lower River included in Hartford LMA.

Labor Market Area	Average Weekly Earnings		Average Weekly Hours		Average Hourly Earnings	
	2000-Q2	% Change Year Ago	2000-Q2	% Change Year Ago	2000-Q2	% Change Year Ago
Bridgeport	\$661.00	3.9	41.8	0.9	\$15.81	3.0
Danbury	637.41	3.3	40.8	-1.7	15.61	5.0
Danielson	506.58	1.0	41.2	-0.1	12.29	1.1
Hartford	731.59	5.7	43.4	1.2	16.87	4.5
Lower River	556.05	-0.6	40.4	-3.7	13.76	3.2
New Haven-Meriden	652.09	2.7	42.6	-0.4	15.31	3.1
New London-Norwich	700.98	5.2	42.0	-0.9	16.69	6.1
Stamford	523.34	-0.7	39.9	1.3	13.13	-2.0
Torrington	581.88	2.8	41.7	-0.5	13.95	3.3
Waterbury	646.77	2.4	44.4	0.8	14.57	1.7
Statewide	\$661.80	2.4	42.2	-0.6	\$15.67	3.0

Labor Market Area	State Job Service Postings		Housing Prices*		Housing Permits	
	2000-Q2	% Change Year Ago	2000-Q2 (000)	% Change Year Ago	2000-Q2	% Change Year Ago
Bridgeport	1,357	15.3	233.8	9.6	222	-19.9
Danbury	592	41.0	296.6	10.0	228	-28.5
Danielson	319	24.6	★	★	73	-26.3
Hartford	3,775	-11.3	138.4	8.3	949	-20.2
Lower River	F	F	★	★	40	-18.4
New Haven-Meriden	1,755	-8.9	138.3	7.0	340	-34.9
New London-Norwich	1,152	32.7	164.1	3.3	201	-19.3
Stamford	605	-16.0	544.1	8.2	176	2.9
Torrington	277	-27.9	112.2	1.3	69	-35.5
Waterbury	1,611	17.2	169.8	7.2	180	12.5
Statewide	11,443	0.5	\$221.4	8.1	2,478	-21.1

* Current period's housing prices are a four-quarter moving average of the selling price of a typical home.

F Lower River included in Hartford LMA. ★Markets are too small for reliable estimates.

Sources: Quarterly figures developed by *The Connecticut Economy* based on monthly estimates from the Connecticut Department of Labor. Figures are not seasonally adjusted. Statewide totals are not necessarily the sums of individual labor market areas. Housing permits are quarterly averages based on monthly figures from the Connecticut Department of Economic and Community Development and are not seasonally adjusted. Housing prices, from UConn's Center for Real Estate and Urban Economic Studies, are preliminary.



Income Still Tops, But Poverty Increases

Recently released data for 1999 show that Connecticut maintained its top spot in per capita income, 37.3% above the national average. According to revised figures, that's the same lead the state enjoyed in 1998. Back in 1991, the darkest year of Connecticut's Great Recession, the state's lead stood at only 33.7%.

Unfortunately, the rising tide of income during the 1990s did not lift all boats. While the state's income picture brightened, the poverty rate worsened.

Using the Census Bureau's three-year averages at the state level, Connecticut's poverty rate rose from 8.1% in 1990-1992 to 9.9% in 1996-1998, the most recent data available. Over the same period, the national rate dropped from 14.2% to 13.2%. Thus, at the outset of the decade, the state's poverty rate was 6.1 percentage points below the national average (and third lowest in the country), but most recently it was only 3.3 percentage points below the national average (and eleventh lowest).

Why has poverty worsened in Connecticut in the midst of an economic boom? One possible answer has to do with births to unwed mothers, especially teenagers.

Teenagers Having Children

Social scientist James Q. Wilson notes that children born to mothers who finish high school, get married, and give birth after reaching age 20 are ten times less likely to be poor than children born to mothers who fail to do these things. Children pay the price of teenage motherhood. U.S. data for 1998 indicate that mothers under the age of 20 are less likely than those 20 and over to seek health care during the first trimester, and are more likely to smoke during pregnancy. Because of these health risks and the general economic risks of poverty, babies born to teenagers face a higher risk of low birthweight, of premature birth, and of dying in the first year of life.

Children account for a disproportionate share of America's poor—the poverty rate among children is double that of adults. Children born to unmarried mothers are more likely to be poor than are children born to married mothers. And four of five teenage mothers are unmarried. Thus, when predicting the poverty rate, a leading indicator is the teenage birth rate.

Connecticut's teen rate in 1998 was 36 births per 1000 female teenagers. The national average for this group was 51 births per 1000. Hence Connecticut's teenage birth rate most recently was about 30% below the national average.

Connecticut's 1998 teen birth rate was also 11% below its own 1991 rate of 40 births per 1000. But the national rate in 1998 was 18% below its 1991 rate of 62 births per 1000. Thus, the rate has declined less rapidly here since 1991 than in the nation; in fact, only two states, Arkansas and Rhode Island, experienced less of a decline. Connecticut's slower than average decline in teen births may help explain why the state lagged the nation in alleviating poverty during the decade.

Declines in teen birth rates here and nationally could be traced to several developments. Programs aimed at reducing teen pregnancies plus growing concern about sexually transmitted diseases resulted in more abstinence and in greater use of contraceptives. The proportion of teenagers with sexual experience stopped growing in the mid-1990s, halting a two-decade-long increase. Finally, welfare reforms and a sunnier job market made teen motherhood relatively less attractive.

Teen Birth Demographics

There are substantial differences in childbearing patterns across demographic lines. While these differences across groups may relate more to income and education than to race or place of origin, federal reports do not provide birth rate information based on income.

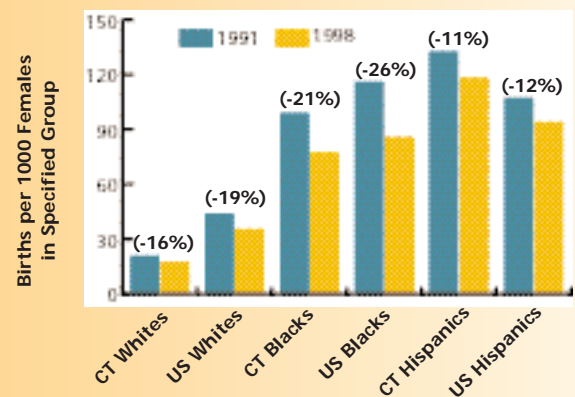
Non-Hispanic white teenage females in Connecticut experienced a rate of 17 births per 1000 in 1998, less than half the national average of 35 for this group. Only two states had lower birth rates than Connecticut. Since 1991, Connecticut's rate has declined 16% and the national average has fallen 19%, with all states showing a drop.

Black teenage females in Connecticut had a 1998 rate of 77 births per 1000—9% below the national average for black teens but more than four times the rate among the state's non-Hispanic white teens. Connecticut's birth rate among

black teens ranked 36th highest nationally. Between 1991 and 1998, Connecticut's birth rate among black teens declined by 21%. The national average fell 26%; no state showed an increase.

Hispanic teens in Connecticut had a 1998 rate of 118 births per 1000—26% above the national rate for this group, nearly seven times the rate for the state's non-Hispanic white teens, and 52% above the state's black teen rate. Connecticut's birth rate among Hispanic teens ranked seventh highest nationally. Since 1991, the rate has declined 11% in the state; the national average has declined 12%, but a

Birth Rates Among Teenagers Declined More in U.S. than in Connecticut During the 1990s



Source: Developed by *The Connecticut Economy* using the national Vital Statistics Report, Vol. 48, No. 6, April 24, 2000. Whites are non-Hispanic whites. Teenagers are females 15 to 19.

dozen states showed an increase. The accompanying chart summarizes state and national teenage birth rates for each group in 1991 and 1998.

The net effect of Connecticut's falling birth rate on the total number of teen births depends on relative population shifts among female teens between 1991 and 1998. According to Census Bureau estimates, Connecticut's population of non-Hispanic white teenage females slipped 1% between 1991 and 1998; the population of black teen females rose 8%; and the population of Hispanic teen females jumped 18%. Therefore, among non-Hispanic white teens, a declining population reinforced the falling birth rate to cut the number of teen births. Among blacks, a growing population of female teens partly offset the falling birth rate; consequently, the number of such births still declined but not as fast as the birth rate. And among Hispanic teens, rapid growth in numbers more than offset the falling birth rate, resulting in more Hispanic teen births in 1998 than in 1991.

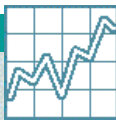
Mothers of All Ages

Finally, let's turn to mothers of all ages. About 31% of all Connecticut births in 1998 were to unmarried women, a figure slightly below the national average of 33%. The national average has been rising for decades and is nearly double its 1980 level of 18% (historical trends at the state level are not readily available).

Connecticut's 13,676 births to all unmarried women in 1998 included 5,301 to non-Hispanic whites, 3,753 to blacks, and 3,987 to Hispanics. In 1998, births to unmarried women in Connecticut accounted for 18% of all births to non-Hispanic whites, 69% of those to blacks, and 64% of those to Hispanics. Nationally, comparable figures were 22% for non-Hispanic whites, 69% for blacks, and 42% for Hispanics. The share of births to unmarried women ranked Connecticut 45th highest nationally among non-Hispanic whites, 22nd among blacks, and first among Hispanics.

Between 1991 and 1998, Connecticut's total non-Hispanic white population declined 4%, the black population increased 6%, and the Hispanic population increased 21%. Thus, the state's population grew among groups with a higher share of births to unmarried mothers, and this likely contributed to the state's rising poverty rate.

No question, there have been numerous success stories among families headed by unmarried mothers. Many have gotten jobs, and an extended family can provide financial, moral, and child-care support. But on average the odds are still stacked against children born to unmarried mothers, particularly teenage mothers.

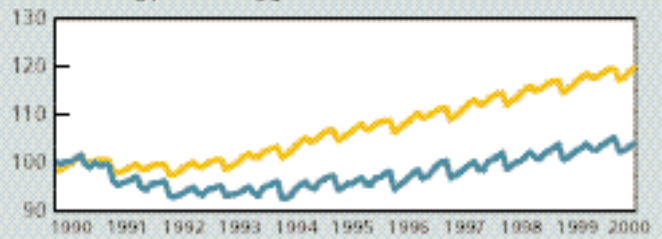


INDEX OF ECONOMIC INDICATORS

Indexed so 1990 = 100

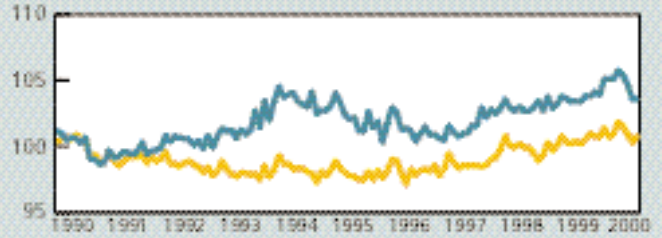
Job Totals

(not seasonally adjusted)



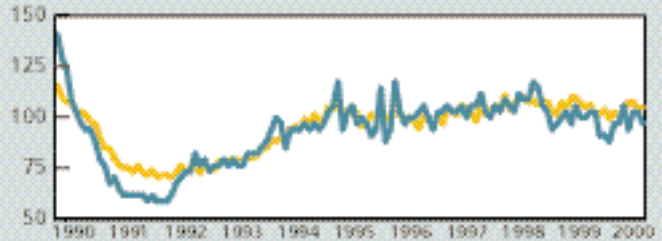
Average Real Hourly Earnings in Manufacturing

(not seasonally adjusted)



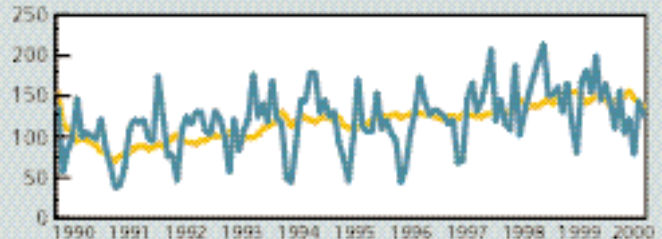
Help-Wanted Ads

(seasonally adjusted)



New Housing Permits

(not seasonally adjusted)



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Connecticut Travel and Tourism Index

The overall index increased 4.1% in the second quarter compared to the same quarter the year before. The index consists of hotel-motel revenues, hotel-motel occupancy rates, attendance at six major tourist attractions, and traffic on five tourist roads.

Hotel/Motel Rev.	H	14.1%
Occupancy Rate	H	2.3%
Attendance	H	-1.0%
Traffic	H	0.9%
Overall	H	4.1%

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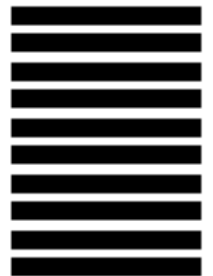
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By Mike Morris
Chairman, President and CEO
Northeast Utilities (left)

By Gene McGrath
Chairman, President and CEO
Consolidated Edison, Inc. (right)



Focused on Reliability, Poised for Growth

Late last fall, we announced the proposed merger of Northeast Utilities and Consolidated Edison. We believe this is a business combination that will benefit our customers, our employees, and our shareholders.

A Dramatic Transformation

Our industry is in the early stages of a dramatic transformation, and we are on the fast track to reinvent ourselves and leverage our capabilities in this dynamic, competitive arena. Across the country, utilities are looking at what is happening and deciding what they want to be in this new market environment. Some have decided to be bulk power suppliers. Others have decided to develop an international portfolio. Some—like us—have decided to stick closer to home and concentrate on what they know best. We know the energy distribution business and we will stick close to that. To the extent that we diversify, it will be very closely tied to our core competencies. To that end, we expect to have a vibrant presence in our region's wholesale and retail marketing business.

While we are experienced in providing safe, reliable and cost-effective energy and related products and services, our combined company must continue to perform at the levels that customers have come to expect of us and that we demand of ourselves. To that end, our merger transition team is assessing our strengths and identifying ways to improve service and save customers money on their electric bills.

Rewards and Challenges

Mergers—particularly large-scale combinations such as ours—are both rewarding and challenging. We understand the critical importance of remaining focused on our customers' requirements. Here in Connecticut we all know how much we depend on The Connecticut Light & Power Company to "keep the lights on." When it comes to meeting New York City's electric energy needs, the goal is 100% system reliability. And, even though Con Edison already has the highest level of distribution system reliability in the nation, we take that commitment to excellence seriously.

The Con Edison/NU merger challenges us to learn about each other's customers and their expectations, and return that knowledge as even better customer service. This is a much larger responsibility than either company has had before, and we relish the opportunity to learn together and to grow in order to better serve our customers' needs.

Our shareholders have enthusiastically supported this strategic combination—an alliance that builds upon our strong regional presence, financial resources and technical expertise. We will continue to work with our regulators and customers, addressing their questions and responding to their concerns, and we look forward to contributing to the economic vitality of Connecticut and the northeast.

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