# The New York City Recession

*by David Brauer and Mark Flaherty*

The New York City economy is now mired in its deepest slump since the mid-1970s. In the first quarter the city unemployment rate reached 10.5 percent, the highest rate in fifteen years, and substantially above the national average. Between April 1989 and March 1992, payroll employment declined by 9.9 percent, reversing all of the progress made during the 1980s.[1] This article examines the origins, scope, and sectoral profile of the New York City recession. In addition, we document the buildup of imbalances in the economy before the downturn and discuss the extent to which these imbalances have been alleviated.

Although the city's recession originated in the finance, insurance, and real estate (FIRE) sector, it subsequently spread to every major sector except health care. The local recession began in the spring of 1989 and intensified when the national economy slipped into recession in July 1990. After city employment lagged significantly behind both suburban and national employment even during the period of expansion, job losses during the recession greatly exceeded those experienced by the rest of the nation but were only slightly worse than those of the suburbs. Our analysis suggests that roughly two-thirds of New York's employment loss in the recession reflects city- and area-specific factors, with the national recession accounting for the remaining one-third. Finally, we find that imbalances generated during the expansion of the 1980s, including high and rising labor costs and excess office capacity, were only partially corrected as of the end of 1991.

[1]All employment figures in this article are seasonally adjusted by the authors See the appendix for details

**The scope of the current recession**

To understand the origins and scope of the New York City recession, one must examine developments in the preceding decade. Between 1977 and 1987, employment in the city grew at an average annual rate of 1.2 percent, with much of this growth fueled by expansion in the financial sector. The recessions of the early 1980s had only minor and short-lived effects on employment in the city. Until 1987, it appeared that the boom would continue indefinitely.

The city's prospects, however, changed dramatically with the October 1987 stock market crash. The subsequent slump can be divided into four phases (Chart 1). Employment grew very slowly for a year and a half following the crash. In the second phase, beginning in April 1989, employment in the city turned down, falling by 1.5 percent. The downturn reflected declines in construction, FIRE, trade, and manufacturing. The decline in the New York City economy, however, was somewhat milder than that of the surrounding region. The third phase is defined by the national recession, which began in the summer of 1990 and apparently ended in the spring of 1991. During this period, employment in the city fell a further 4.7 percent. The most recent phase is characterized by a continuing slide in city employment despite a stabilization in national employment. Overall, since April 1989, total employment in the city has fallen 9.9 percent, with weakness in every major sector except health services (Table 1).

Notwithstanding the sharp decline in employment during the current recession, at this time comparisons with the recession of the mid-1970s are overdrawn. Between 1973 and 1976, employment fell by roughly the same amount as in the current recession, but in 1973 employment was already about 7 percent below its 1969 peak. Thus the total decline during the city's long slump in the 1970s was nearly twice as large as in the current recession to date Nevertheless, while the earlier recession was indeed much longer and deeper, the *rate* of job loss has been significantly faster in the current recession.

*Sectoral effects*

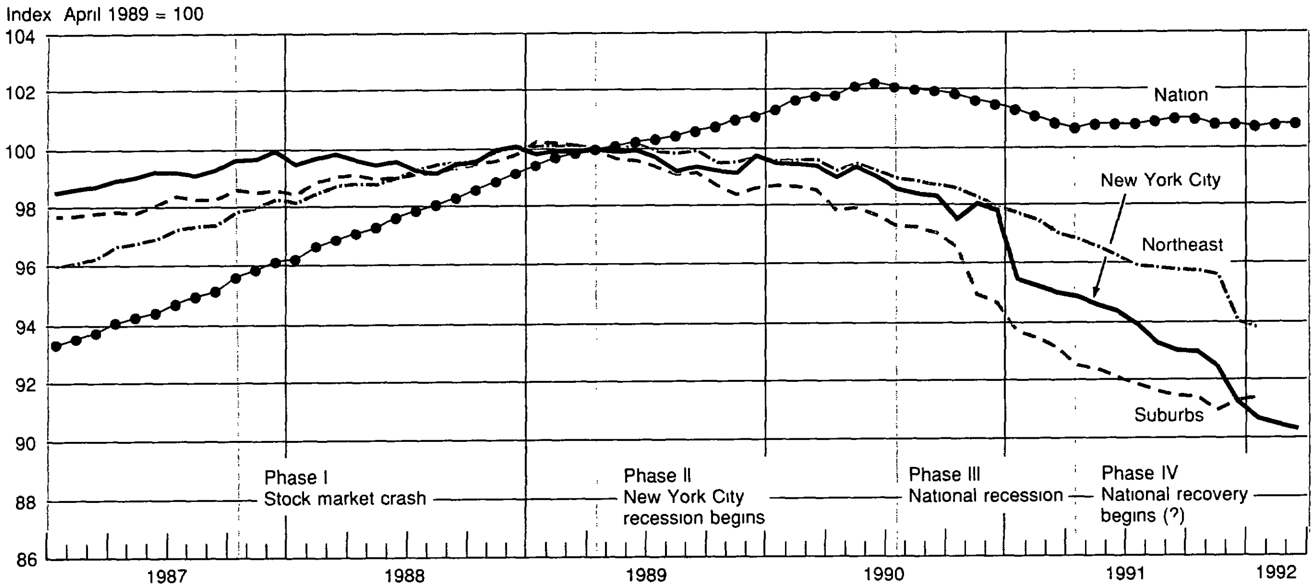
A look at the recession's impact on employment by sector is instructive. In the 1969-77 downturn, manufacturing accounted for nearly half of New York City's employment losses, while in the current recession it is responsible for only about 20 percent of the decline in employment. This difference reflects not only a smaller percentage decline in manufacturing output in the current period, but also the much smaller role of manufacturing in the local economy. Manufacturing's current share of total New York City employment is less than half that of 1969, with only printing and publishing and apparel maintaining a significant local presence (Table 2). The decline in manufacturing's importance mirrors broad national trends, but the structural changes in the New York City economy are also related to such city- and region-specific factors as high taxes, land and labor costs, and a deteriorating infrastructure

Another significant difference between the current and earlier downturns concerns the performance of the service sector Total service employment (excluding financial services) in the city has fallen by 5 4 percent since April 1989, with business services accounting for virtually all of the decline Compared with other sectors, services have declined modestly in percentage terms, but because services now account for nearly a third of total employment in New York City, the weakness in this sector has been an important contributor to the overall employment decline. By contrast, during the 1970s recession, services were the only pocket of strength. between 1969 and 1977, services employment was virtually unchanged

The FIRE sector accounts for about 15 percent of city employment, a figure more than double the national share. FIRE's overall role in the New York City economy, however, is even greater Financial services accounted for about a third of the 400,000 new jobs created in the city between 1977 and 1987 In addition, growth in the financial sector indirectly boosted city employment in several ways. Business and other services catering to the financial sector benefited Incomes generated in the financial sector also spilled over into consumer spend-

Chart 1

**Employment Trends since the Stock Market Crash**




Sources New York State Department of Labor and Bureau of Labor Statistics

Note All data are seasonally adjusted

ing, helping to arrest a long decline in retail trade employment. Likewise, much of the revival of construction activity can be linked directly or indirectly to financial services.

The close relationship between financial services and the health of the New York City economy explains why the October 1987 stock market crash was such a critical turning point. Over the next year and a half, FIRE employment fell sharply, the growth of business and related services and retail trade slowed significantly, and no major new construction projects were undertaken. Even though the pace of layoffs on Wall Street slowed by 1989, these ripple effects, together with the slowdown in national economic growth, helped push the local economy into recession.

*Industrial composition and employment growth*

Despite the local recession's severity, there is no evidence that the city suffers from a mix of industries that have experienced weaker than average long-term growth. On the contrary, a favorable industrial composition partially explains the city's strong performance between 1977 and 1987 In particular, services and FIRE, which during this period grew more rapidly than other sectors nationally, constituted more than a third of 1977 city employment, compared with only a fourth of national employment. At the same time, the shrinking manufacturing sector represented a much smaller fraction of employment locally than nationally. In fact, had the 1977 New York City economy shown the same employment shares as the national economy, city employment during this period would have grown at an annual rate of only 0.7 percent, a figure just over half the actual 1.2 percent growth rate.[2] Furthermore, the underrepresentation of cyclically sensitive industries in the New York City economy suggests that sectoral composition alone cannot explain the city's recession.

Table 3 provides a rough accounting of the employment declines during the New York City recession. Since the start of the local recession, employment in the city has declined at a 3.5 percent annual rate, representing a 4.7 percentage point decline in growth relative to the 1977-87 expansion. The suburbs have also suffered a great deal, with employment falling at a 3.2 percent rate since April 1989. Thus, unlike the 1969-77 downturn, when the suburbs grew during the city's recession, the current downturn seems to reflect regional rather than purely city-specific difficulties Because growth in both the city and the region has fallen roughly 3 percent more than at the national level, we infer that region-specific problems account for about two-thirds of New York City's employment decline The national slowdown is also partly responsible: employment growth nationally (excluding the New York metropolitan area) has slowed 1 7 percentage points, accounting for roughly a third of the city's employment losses relative to the 1977-87 trend.

## Continuing economic imbalances

The city's rapid growth during the 1980s brought with it

[2]The exact calculation is $\sum_{i=1}^{13} w_i e_i$, where $w_i$ is defined as the proportion of the nation's employment accounted for by sector i in 1977, and $e_i$ is the rate of employment growth in sector i in New York City between 1977 and 1987 The calculation includes the sectors shown in Table 1 as well as mining Trade is divided into wholesale and retail, and manufacturing is divided into apparel, printing and publishing, and all other

Table 1

**Employment Growth by Sector, New York City**

Percent Change

| | 1969-77 | 1977-87 | April 1989-March 1992† |
|---|---|---|---|
| Total‡ | −16 1 | 12 6 | −9 9 |
| Construction | −39 3 | 85 0 | −28 4 |
| Manufacturing | −34 8 | −29 5 | −18 9 |
| FIRE§ | −10 8 | 32 7 | −9 0 |
| Services | 0 4 | 41 5 | −5 3 |
| Business | N A | 52 6 | −22 6 |
| Health | N A | 26 8 | 10 8 |
| Trade | −17 2 | 2 8 | −16 6 |
| Transport and utilities | −20 3 | −16 7 | −7 8 |
| Government | −7 1 | 14 3 | −3 6 |

†Values are seasonally adjusted, except for business and health services

‡Total employment in New York City declined by 610 thousand between 1969 and 1977, increased by 402 thousand between 1977 and 1987, and declined by 357 thousand between April 1989 and March 1992

§Finance, insurance, and real estate

Table 2

**Employment Shares**

Percent

| | New York City | | Nation | |
|---|---|---|---|---|
| | 1977 | 1991 | 1977 | 1991 |
| Construction | 2 0 | 2 9 | 4 7 | 4 3 |
| Manufacturing | 16 9 | 9 1 | 23 9 | 16 9 |
| FIRE† | 13 0 | 14 7 | 5 4 | 6 2 |
| Services | 24 6 | 32 6 | 18 6 | 26 4 |
| Business | 6 1 | 6 5 | 2 4 | 4 9 |
| Health | 5 8 | 7 9 | 5 6 | 7 6 |
| Trade | 19 5 | 16 6 | 22 5 | 23 3 |
| Transport and utilities | 8 1 | 6 5 | 5 7 | 5 3 |
| Government | 15 9 | 17 5 | 18 3 | 16 9 |

†Finance, insurance, and real estate

high rates of price and wage inflation and a buildup of overcapacity in the real estate sector. These side effects of prosperity helped put a brake on the expansion and contributed to the length and severity of the current recession. As of the end of 1991, these imbalances appeared to have been only partially corrected, thus impeding a quick resumption of income and employment growth.

Table 3
**Accounting for the Decline in New York City Employment Growth**
Percent Change, Annual Rate

| | 1977-87 | April 1989-Jan. 1992 | Difference |
|---|---|---|---|
| (A) New York City | 1.2 | −3.5 | −4.7 |
| (B) Suburbs† | 2.2 | −3.2 | −5.4 |
| (C) Rest of nation | 2.2 | 0.5 | −1.7 |
| (D) = (A)-(C) City versus nation | −1.0 | −4.0 | −3.0 |
| (E) = (B)-(C) Suburbs versus nation | 0 | −3.7 | −3.7 |
| Memo: New York City compositional advantage | 0.5 | 0.8‡ | 0.3 |

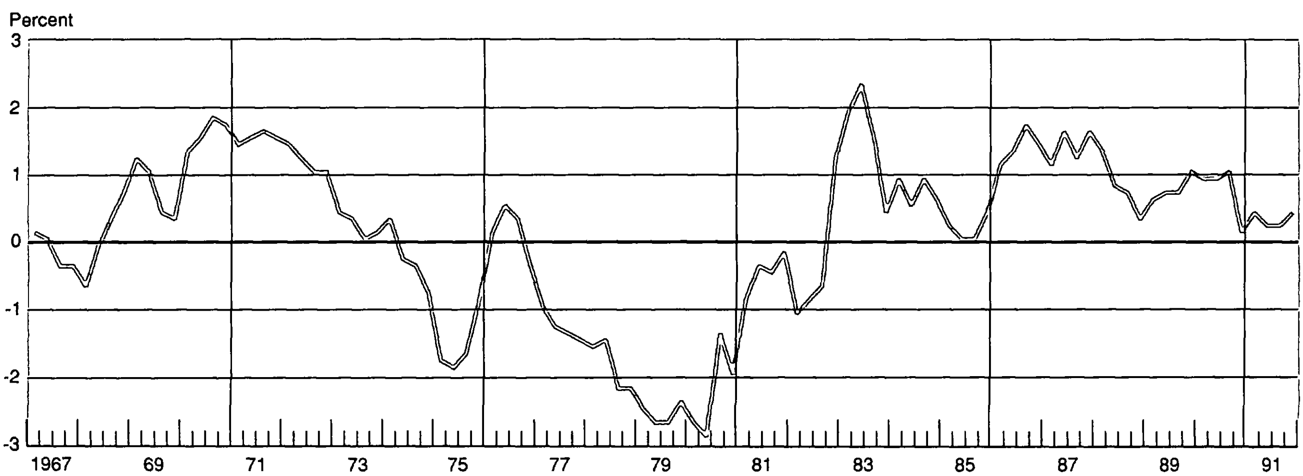
†Includes Nassau, Suffolk, Putnam, Rockland, and Westchester Counties in New York State; and Bergen, Essex, Hudson, Morris, Passaic, Sussex, and Union Counties in New Jersey.
‡1989-91 full year.

*Wages and the cost of living*

Despite the longer, deeper recession in the New York area, wage and price inflation here has not eased to the extent that it has nationally. In the past two decades, inflation in New York has exhibited two distinct trends (Chart 2). From 1972 to 1982, the area's slower than average growth was accompanied by a rate of inflation lower than that of the rest of the nation. After 1982, the trend was reversed. As the New York economy grew, inflation was consistently higher locally than nationally. Although the city entered the most recent recession earlier and fell deeper, its inflation has remained stubbornly higher. There are signs, however, that this trend may be ending. The gap in rates has narrowed from a high of 1.4 percentage points in 1987 to only 0.3 percentage points in the fourth quarter of 1991.

The link between wage and cost-of-living inflation has been evident in the pattern of local wages. Wages in New York City have for a long time been higher than those paid to comparable workers in the rest of the country. During the expansion of the 1980s, local wages rose even further relative to national averages. Between 1981 and 1991, manufacturing workers' average hourly earnings rose at an annual rate of 4.6 percent, compared with the national average of 3.4 percent. To be sure, the annual growth in local manufacturing wages has slowed to 2.8 percent, as against 3.1 percent nationally, since the end of the city's boom in 1987. But available data on various white-collar occupations in nonmanufacturing industries show no slowdown in labor

Chart 2
**Consumer Price Inflation Differential: New York Area Compared with the United States**




Source: Bureau of Labor Statistics.

cost inflation. For example, from 1987 to 1991, New York computer operators' wages grew 5 5 percent annually Wages for clerical positions, including file clerks, word processors, and secretaries, rose even faster, at annual rates above 8 percent.[3]

*Real estate markets*

The real estate market clearly illustrates the boom and bust experience of New York. Home prices, commercial rents, and construction costs rose at rates considerably above the national average during the 1980s. Although significant progress has been made in unwinding the excesses caused by the boom, imbalances persist.

Residential home prices exploded during the early 1980s. The median single-family home in the New York metropolitan area sold for as much as $194,000 in 1988, more than double the national average and almost triple the median price in 1981 (Chart 3). Since then, prices have fallen considerably, dropping to $170,800 in the fourth quarter of 1991 Still, despite rising prices nationally, New York home prices remain about 70 percent above the national average As a consequence, in the fourth quarter of 1991 the median family income in the New York area was only 64 3 percent of the income necessary to afford the mortgage on a median-priced home in the area. Although this "affordability index" shows an improvement over the mid-1990 level of 44 5, it remains far below the national average of 122 5.

After reaching high levels in 1988, commercial rents, too, have moderated. As of the fourth quarter of 1991, asking rents in the downtown and midtown areas have dropped 16 percent and 7 percent, respectively, since early 1988. Anecdotal evidence on effective rental rates, moreover, suggests even more marked drops in rental costs Official statistics on rental rates likely mask the pattern of newly negotiated contracts, which would be expected to show a greater response to the depressed market Despite falling rents, the vacancy rate for downtown office space has grown from just over 10 percent in 1987 to over 20 percent in the last quarter of 1991 (Chart 4) Such high and increasing levels point to excess capacity that has yet to be worked off

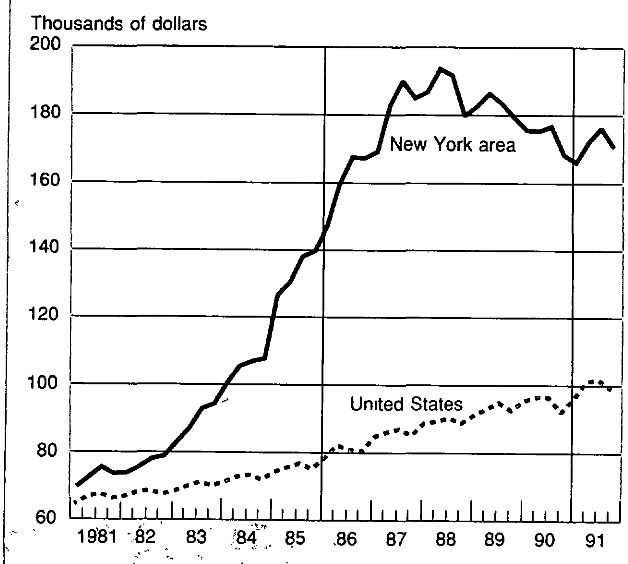
The boom in building during the 1980s was accompanied by accelerating construction costs. From 1977 to 1987, city construction costs rose at an annual rate of 6 8 percent.[4] Although construction cost inflation has slowed to a 4 5 percent rate since 1987, this deceleration has not matched the slowdown in the rest of the country. During 1991, city construction costs rose 3.0 percent, compared with 2 3 percent nationally, leaving the city's cost index 31 percent above the national average

[3]Manufacturing wage data come from the New York State Department of Labor The source of occupational wage data is the U S Department of Labor's Area Wage Survey

[4]The cost measure is a weighted average of material costs, labor rates, and equipment rental rates indexed to a thirty-city average calculated by R S Means Inc , a private engineering consulting firm

Chart 3

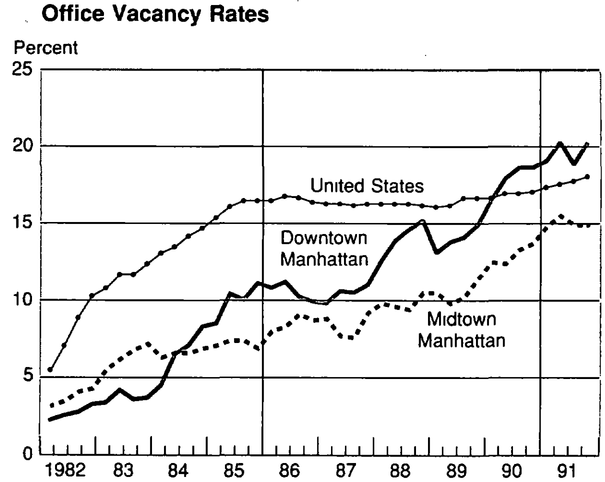
**Median Home Prices**




Source National Association of Realtors

Chart 4

**Office Vacancy Rates**




Source Coldwell Banker

## Conclusion

Because FIRE sector firms are heavily represented in New York, the city benefited greatly from explosive growth in that sector during the 1980s The stock market crash of 1987 sapped this sector of much of its strength and signaled coming economic difficulties. Financial sector weakness subsequently spread throughout the local economy. The local downturn has been exacerbated by the national recession and by the continuing decline in manufacturing employment

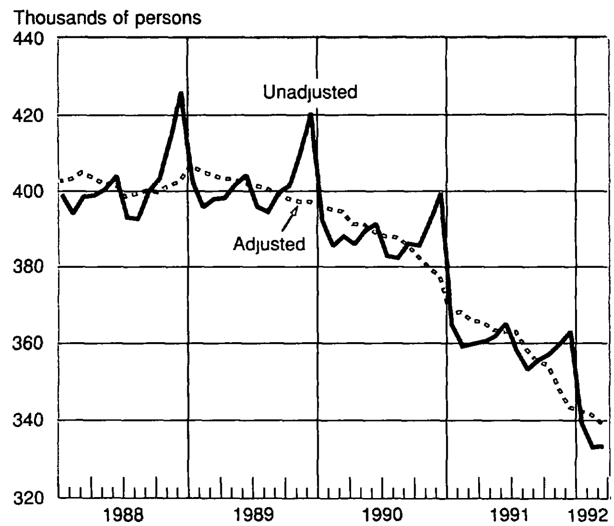
The boom brought on economic imbalances such as high cost inflation and speculative real estate markets. These imbalances have aggravated the recession and posed obstacles to recovery. Although the downturn to date has not matched the recession of the 1970s in its duration or severity, ongoing job losses and persistent economic imbalances mean that New York City's economic recovery is likely to be gradual.

### Appendix: The Use of Seasonally Adjusted Data

Seasonal adjustment removes from a data series the effects of events that follow a regular seasonal pattern This correction makes underlying trends and cyclical fluctuations in the data more apparent In this article, we use the X-11 method, which assumes that the unadjusted series is the product of trend/cycle, seasonal, and irregular components [†] The procedure is applied to employment totals to determine seasonal adjustment factors. The adjusted series is then calculated by dividing each month's unadjusted figure by the adjustment factor For New York City and its suburbs, total employment is calculated by seasonally adjusting employment separately by industry and then aggregating [‡]

To understand the value of such adjustments, consider New York City employment in retail trade Employment tends to peak in December, then drop sharply in January, with a smaller dip typically taking place in July and August (see chart) Without seasonal adjustment, only comparisons between identical months in separate years would be meaningful But by correcting for seasonal patterns, we can identify cyclical fluctuations or changes in the trend much more quickly. For instance, the adjusted data reveal that retail employment began to decline in the spring of 1989, but with unadjusted data a clear change in the trend cannot be detected until the fall of that year

**The Effect of Seasonal Adjustment on Retail Trade Employment**




Sources New York State Department of Labor (unadjusted data), authors' calculations (adjusted data)

†For most of its seasonally adjusted series, such as the national unemployment rate and payroll employment, the Bureau of Labor Statistics applies the slightly more sophisticated X-11 ARIMA (autoregressive integrated moving average) model

‡The industries are construction, manufacturing, transportation and utilities, wholesale trade, retail trade, FIRE, services, and government Wholesale and retail trade are combined in the suburbs