# Recent Developments in New York City's Economy

## by Rae D. Rosen

Four years of painful economic contraction appear to be drawing to a close in New York City. The severity of the recession eliminated virtually all of the job growth of the 1983-89 expansion. If employment is the economic yardstick, the city's economy reached a cyclical low in September 1992 and has since barely begun to inch forward. How will the local economy fare now against a background of widespread expectations of slower than normal growth in the national economy? This article examines the cyclical sources of strength as well as the lingering excesses[1] of the 1983-89 boom period, the long-standing structural impediments that could dampen growth, and the positive factors and anomalies that could argue for a more optimistic outlook.

On balance, this analysis finds that there are some signs of good-to-vigorous growth in incomes. By implication, given the job losses during the recession, productivity has risen significantly, suggesting that several key sectors are indeed healthy. The prospects for growth in employment are less robust, however. The overall employment trend appears to be nearly flat. Given time, an improving economy should push operating rates to capacity and the workforce will expand, but the process will be somewhat slow.

### Signs of a recovery

*Employment growth*

At the local level, employment data are the broadest and most timely indicators of economic activity. Measures of gross production, personal income, and industrial production, all of which exist for the nation or state, are generally unavailable or woefully out of date at the city and county level. The latest labor market data indicate that the trough in the city's labor market occurred in September 1992 (Chart 1). Since then, employment has been almost flat, with only 6,000 jobs added to the city's payrolls, a gain that could easily be erased in a statistical revision. Nevertheless, it is significant that employment has apparently stopped declining for the first time since April 1989.

Job growth has developed in two broad areas. First, Service[2] employment is expanding, boosted by growth in health and social services as well as gains in engineering and management services. Second, retail trade employment is growing at restaurants and at discount outlets as major chains finally breach the New York City market. Although the aggregate FIRE sector (finance, insurance, and real estate) remains in decline, a small but critical FIRE subgroup—securities—has added several thousand jobs since September 1992. The gains in these sectors, combined with the moderating declines in construction, manufacturing, government, and transportation and utilities, produced some employment growth, albeit at an annualized rate of a mere 0.3

[1]In "The New York City Recession," Federal Reserve Bank of New York *Quarterly Review*, Spring 1992, David Brauer and Mark Flaherty identify the onset of the recession in New York City and analyze some of the excesses that led to it

[2]This article adopts (except where noted) the narrow definition of Services used by the Bureau of Labor Statistics The category comprises business, legal, and personal services, health services, engineering and management services, hotels, amusements, museums, and private education It excludes the services provided by other sectors such as FIRE (finance, insurance, and real estate), retail trade, and utilities because useful information is obscured if these sectors are consolidated into a single generic group

percent, from the fall of 1992 through the spring of 1993.

The source of the recent job growth, however, underscores the weakness of the local recovery Job gains in health care and social services do not establish the strongest nucleus for future growth; these sectors rely heavily on federal, state, and local funding that may or may not be renewed from year to year. To narrow a persistent budget gap, city administrators have in fact proposed closing or reducing funding for some day care centers for children and the homeless in fiscal 1994 In contrast, more widespread and substantial gains in retail trade and the financial industry or an expansion in business services, construction, or hotel employment would be more suggestive of a robust, self-sustaining recovery.

The recovery in employment has also been unusually slow compared with earlier recoveries in New York City. Measuring from the trough of the U.S. recessions, the top panel in Chart 2 shows that the post-1991 pattern of job growth in New York City has been far slower than in the prior four recoveries. The lower panel of Chart 2 compares the current local recovery with the current national recovery Here, the glacial pace of the local recovery even trails the atypically slow national recovery[3]

Even if the national economy should begin to accelerate, however, faster national growth might not produce the same amount of local growth that earlier relationships would suggest. If, as some management surveys have suggested, corporations are flattening and reducing their managerial staff, then economic acceleration at the national level could lead to more decentralized hiring throughout the nation rather than additional staffing of corporate headquarters in New York City In this way, recovery at the national level could generate less stimulus for the city than it has in the past.

[3]For a further discussion of national developments since the trough, see David Brauer, "A Historical Perspective on the 1989-92 Slow Growth Period," in this issue of the *Quarterly Review*

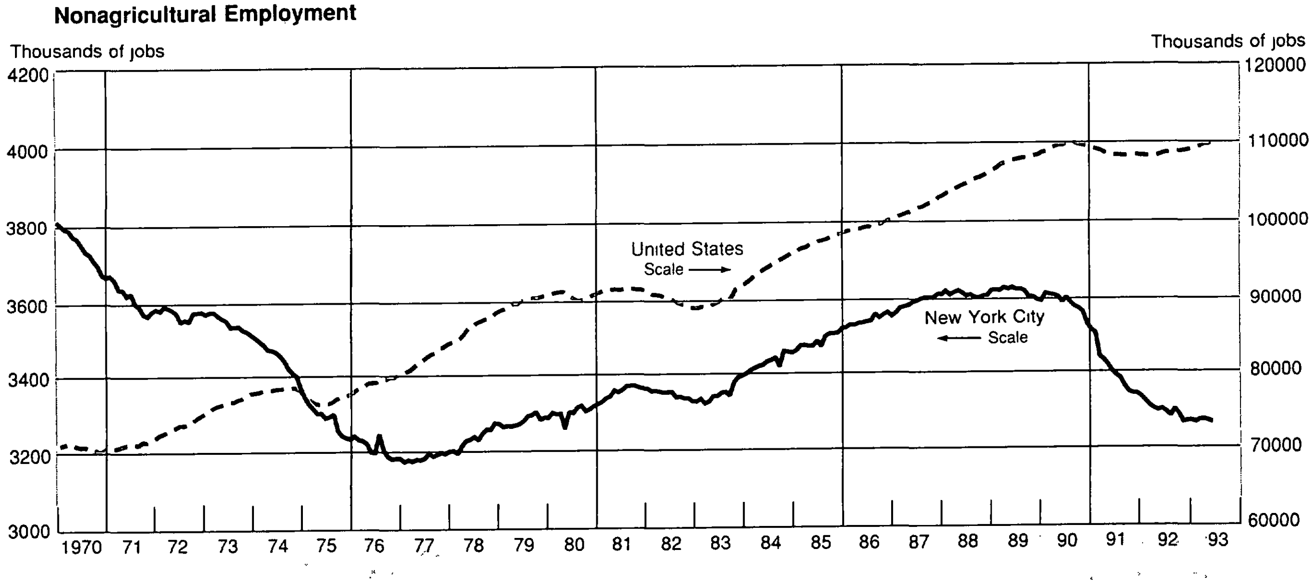
*Other indicators of cyclical recovery*

Fortunately, in addition to the marginally expanding employment data, there are supplementary indicators that suggest a more widespread economic upturn. The pattern of growth in wages and salaries, city tax collections, and retail sales all provide evidence of a nascent recovery.

*Personal income tax collections and wages*. Personal income data for New York City are usually released only with a two-year lag. However, because state and local tax collection agencies generally require personal income tax payments within the month or quarter that the income was earned, personal income tax collections are likely to give an early indication of the trends in the income data. As Chart 3 shows, the growth rates in personal income tax collections reached a turning point in the third quarter of 1990 and

Chart 1

**Nonagricultural Employment**




Sources Bureau of Labor Statistics, Federal Reserve Bank of New York increased on average 10 to 25 percent throughout 1992 and early 1993. Although the rates dropped in April and May of this year, the decline probably resulted from extremely rapid growth a year earlier In general, such growth over the past several quarters is somewhat unexpected given that the unemployment rate rose sharply during this period, peaking at over 12 percent in July 1992 and remaining above 10 percent through the first quarter of 1993 (Chart 4).

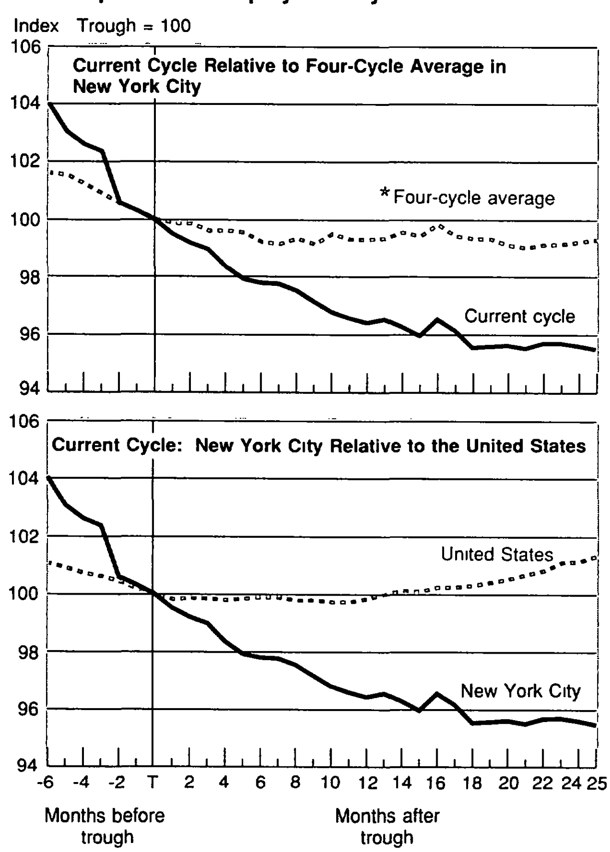
The gains in personal income tax collections are being driven by wage and salary growth that has occurred *notwithstanding* the high rate of local unemployment. At the state level, the composition of personal income shows no outsized increases in the nonwage and salary components of personal income, such as proprietors' income or dividend income, that would account for the strong growth in total personal income and personal income tax collections. Hence, in the state at least, wage and salary gains do seem to account for the strength in total income. Since the city accounts for close to 60 percent of the state totals of each of these components of state personal income, local wage and salary growth is likely to be the source of growth in local personal income and local personal income tax collections as well Thus, somewhat surprisingly, given the large numbers of unemployed in New York City, personal income tax collections strongly suggest that those people who *are* employed are making substantial gains in income.

Additional information about the source of personal income gains can be gleaned from the local wage and salary data, which account for about 60 percent of total personal income in New York City In the third quarter of 1992, the latest quarter for which data are available, New York City wages and salaries were up 4.2 percent on a year-over-year basis[4] The driving industry was brokerage and securities, whose payroll jumped 25 percent, or $550 million, and accounted for nearly half of the gain in the city's total payroll. Because 1992 was the second consecutive year of record pretax profits for the industry, Wall Street bonuses undoubtedly boosted

[4]New York State Department of Labor

Chart 2

**Comparison of Employment Cycles**



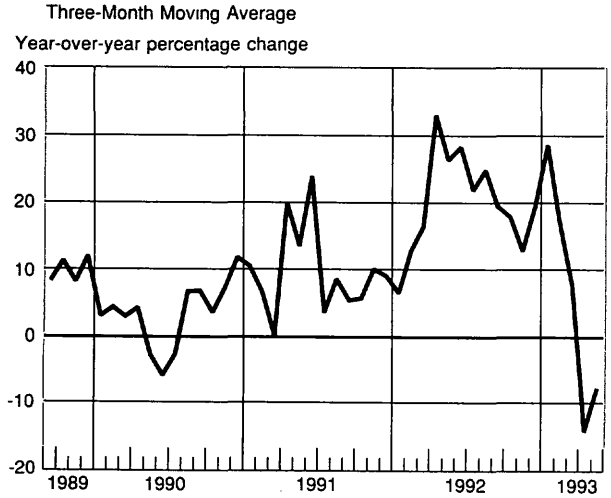

Source Bureau of Labor Statistics

* Average of 1960-61, 1969-70, 1973-75, and 1981-82 recessions

Chart 3

**Monthly Collections of New York City Personal Income Tax**

Three-Month Moving Average




Source New York City Office of Tax Policy wages and salaries in the fourth quarter of 1992 and the first quarter of 1993 well beyond the growth rates registered through the first three quarters of 1992.[5] Indeed, although the actual income and wage data will not be available for several months, the city's personal income tax collections do show a sharp spike in December 1992 and an even higher spike in January 1993

Benefiting from both the gains in the securities payroll and the modest growth in the banking payroll, the FIRE sector has accounted for about half the growth in wages and salaries in the city in recent quarters Nationally, wages and salaries in the FIRE sector contributed just 10 percent of the growth in aggregate wages and salaries in the third quarter of 1992. The importance of the FIRE sector at the local level is not adequately reflected by the number of jobs (which constitute only 15 percent of the local economy, or a mere 4 percent if limited to securities). Consideration must also be given to the high level of wages and salaries in the industry, which averaged more than $63,000 ($84,000 in the securities industry) in the first three quarters of 1992, compared with an average wage of $39,680 in New York State and $32,687 in the United States

Wages and salaries paid in the Service sector have also begun to accelerate Unlike the FIRE sector, the Service sector has been gaining in *both* payroll figures and jobs Although the general salary level in the Service sector is sharply below that of the FIRE sector, the job base is considerably broader and represents about 34 percent of the total employment in New York City. The moderate 5 6 percent growth in third-quarter 1992 Service payroll wages accounts for most of the remaining gain in the aggregate payroll in New York City; importantly, it has accrued to a substantial portion of the working population

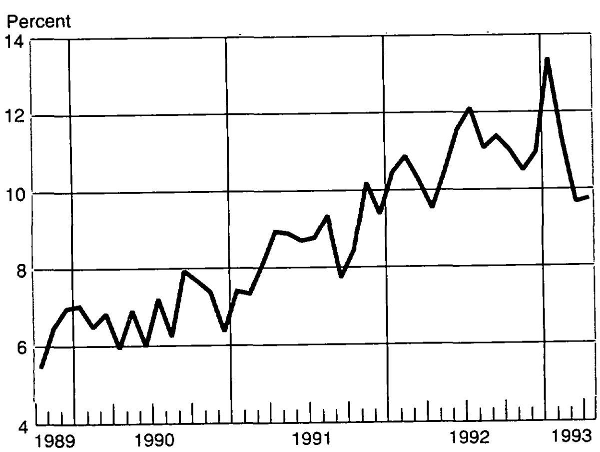
*Retail sales* The improvement in wages and salaries, evident in payroll data and tax collections, is also reflected in retail sales. Six consecutive years of annual sales declines appear to have ended when retail sales rose sharply in the second half of 1992 (Chart 5). Although the pace faltered in the relatively harsh winter months of early 1993, growth seems likely to resume with better weather and further advances in income. The generally brighter sales picture suggests that the earlier gains in wages and salaries have begun to flow into the retail market. Moreover, the improvement is fairly diffuse, leading to increased spending in areas such as apparel, restaurants, services, and other nondurable goods. The city retail sales tax collection confirms the increases in retail spending As Chart 6 indicates, the rate of decline in tax collections began to diminish in the third quarter of 1991, and by the first quarter of 1993, collections were running year-over-year gains of 3 percent

[5]The bonuses in "good" years are substantial, ranging from three to five months' salary for clerical staff to several million dollars for senior executives and traders

Chart 4

**New York City Unemployment Rate**

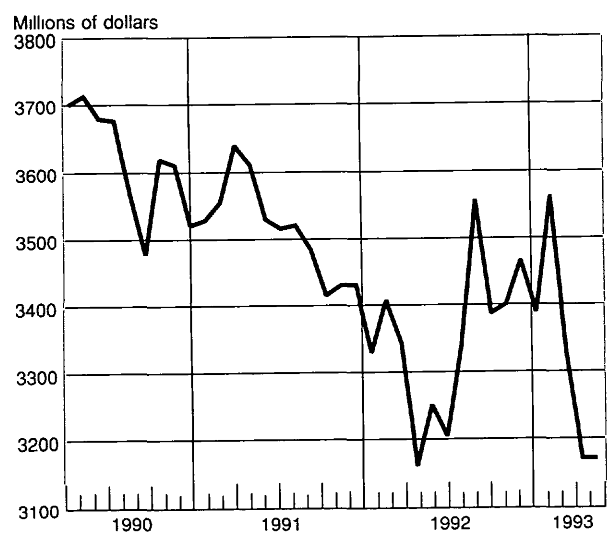
Not Seasonally Adjusted




Source Bureau of Labor Statistics

Chart 5

**Retail Sales**




Source Bureau of the Census

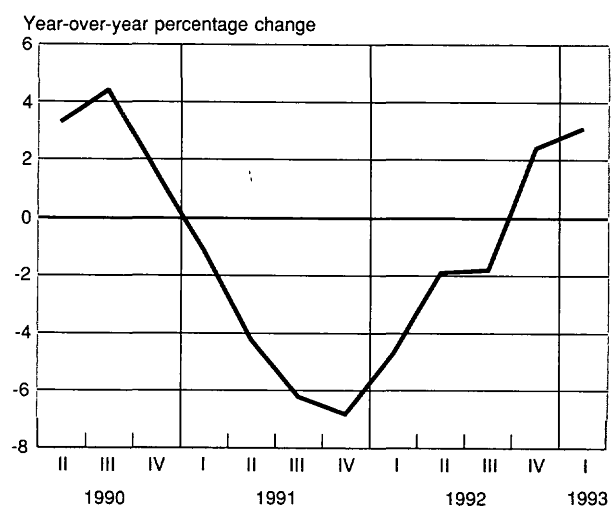
*Real estate*. In the housing sector, recovery has moved forward in fits and starts since the first quarter of 1991, when the decline in interest rates sparked a pickup in sales of existing homes throughout New York State Reasonably reliable measures of the local housing market consist of the median price of existing single-family homes and the permits for construction of one-to-four-family homes Both of these measures, however, cover the housing market in the greater metropolitan area, including Westchester, Long Island, and lower Connecticut, an aggregation well beyond the more narrow focus of New York City Anecdotal evidence suggests, however, that unit sales in the city have picked up even as prices remain weak Permits for construction of multifamily housing within the city are also rising for the first time in several years, a testament to builders' expectations of an improving market

In the nonresidential market, vacancy rates for prime commercial space appear to have peaked in 1992 Absorption rates, the rate at which vacant space is leased, are rising, though at a glacial pace However, the rate increases are driven by tenant upgrades from secondary to primary space rather than by an expansion in the workforce Midtown vacancy rates for prime space declined nominally from a peak of 16 3 percent in the fourth quarter of 1992 to 16 1 percent in the spring of 1993, but at the same time, the vacancy rate for secondary space climbed to 19 8 percent [6] In the downtown area, corporate consolidations, mergers, and closures have kept the pressure on vacancy rates, permitting only minimal absorption of space Downtown primary vacancy rates have dropped slightly to 18.2 percent in the first quarter of 1993 from a peak of 18.7 percent in the fourth quarter of 1992, but the vacancy rate for secondary space has soared to more than 26 percent

Chart 6

**Quarterly Collections of New York City Sales Tax**

Four-Quarter Moving Average




Source New York City Office of Tax Policy

*Business costs* Another sign of firming demand in the city's economy is the stabilization of major business costs following several years of decline Lofty vacancy rates clearly lowered rental costs for commercial office space well below their 1987-88 peak rates Published estimates of rental costs indicate that rates declined at least 15 percent from their peak Anecdotal evidence suggests that landlord "givebacks" in the form of decorating allowances, move-in bonuses, and free rent for the first few months or even a year combined to drop first year rental rates at least 30 percent below the peak As of first-quarter 1993, asking rates for primary office space in midtown Manhattan averaged about $34 a square foot compared with a peak 1988 rate of $39 50, while rates in downtown Manhattan averaged close to $33 per square foot compared with a 1987 peak of $38 Since then, rental rates have begun to inch up in some areas of the city, suggesting some modest improvement in demand.

Although the level of rental rates is still higher in New York City than in many office areas elsewhere in the nation, the rise in rates in many other major cities coupled with the overall decline in rates in New York has improved the city's relative position During the 1988-92 period, asking rates *rose* $1 to $5 per square foot in the central business districts of Atlanta, Houston, Tampa, and Chicago [7] New York City's relative position improved even in relation to Northern New Jersey, where average asking rates fell to $23 per square foot—a significant drop but not as sharp as in New York City. Meanwhile, increases in construction costs have also moderated in New York City the rate has dropped to about 4 3 percent from an average annual increase of 5 6 percent in the 1983-89 period.[8]

### Prospects for growth

*Similarities and differences between city and nation*

To a significant extent, many of the local excesses of

[6]Data obtained from Cushman and Wakefield, "Marketrend," various issues

[7]As of 1992, asking rates averaged $22 50 in Atlanta, $16 50 in Houston, $23 50 in Tampa, $29 00 in Chicago, and $28 in Los Angeles

[8]R H Means Company, Inc

the 1980s have been eliminated or are well on their way toward correction, setting the framework for future growth. However, the city does share some lingering problems with the nation For example, the commercial office building boom of the 1980s has left not only New York but also most parts of the nation with extensive excess office space. As we have seen, this situation has some positive implications. With the vacancy rates in New York City estimated at 15 to 26 percent inclusive of both prime and secondary office space, asking rental rates are unlikely to rise sharply and should remain attractively priced for tenant upgrades and business retention for some time to come. But the disadvantage of the lingering supply of office space is that no new boom in construction and construction employment is likely to develop during this period.

The excesses in New York City's residential market, however, appear to be close to correction The local supply of single-family housing, cooperatives, and condominiums appears to be returning rapidly to historic price/income ratios (Chart 7) In the 1982-88 period, home prices in the greater metropolitan area more than doubled, compared with a national average increase of 32 percent,[9] while personal incomes rose just 60 percent. During these years, affordability became a limiting factor as incomes failed to keep pace with home prices Since then, several years of price declines or minimal price advances, combined with moderate income gains, have narrowed the gap, and the cyclical correction is largely finished. Moreover, a repeat of the 1983-87 boom in housing prices is unlikely in this decade because employment is expected to grow more slowly and lending standards have tightened Note, too, that because local home prices are appreciating more slowly than elsewhere in the nation, the resulting *relative* improvement in housing costs may enhance the city's ability to attract and retain businesses and their employees in the coming years

Unemployment rates are gradually receding for both the nation and the city In the spring of 1993, the U S. unemployment rate was about 7 percent while the city figure was close to 10 percent Nevertheless, although the national and local rates are moving in the same direction, the difference between the two is understated because of the relatively low labor force participation rate in New York City The fraction of the local working-age population that is working or looking for work in the city is substantially smaller (by 10 percentage points) than the national average. The employment and unemployment figures count only the number of people who claim that they are working or seeking work Because of the poor participation rate, the city's official unemployment numbers are based on a labor pool that is significantly smaller than is typical elsewhere in the nation. As a result, the local unemployment rate seriously underestimates the number of working-age people who are not working Accordingly, comparisons of the city's unemployment rate with the rate in other major cities or the nation are somewhat misleading.

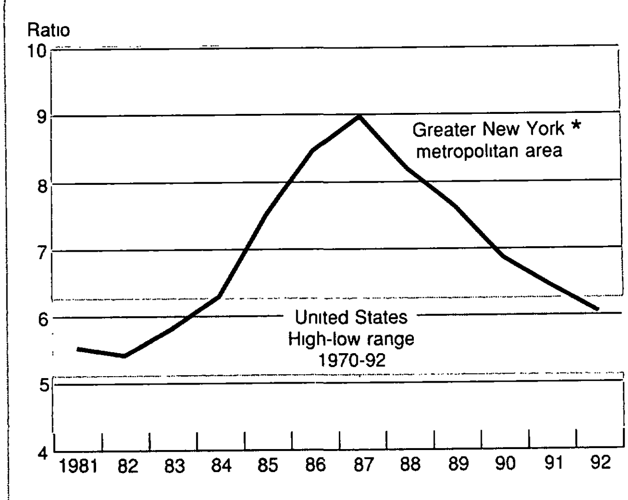
Moderate growth in income is a hallmark of both the city's and the nation's recovery, but nearly half the gains in income in the city have been tightly concentrated in the securities subsector, which accounts for just 4 percent of the jobs In contrast, the national recovery has proceeded with gains in both wages *and* jobs in construction, trade, FIRE, and Services. The city's more recent and narrow gains stand in stark contrast to the broader national expansion

On the positive side, two major differences in the local economic base could work to the comparative advantage of the city First, New York City was never a major recipient of defense spending programs, so the defense build-down that is adversely affecting employment in other parts of the country is not a critical detriment to the city's economy The closing of the Staten Island home port, for example, may cost New York City 2,600 jobs—less than 1/10 of 1 percent of the city's 3 3 million job base. Second, the composition of

Chart 7

**Income and Home Prices**

Ratio of Existing Single-Family Home Prices to Per Capita Personal Income




Sources Bureau of Economic Analysis, National Association of Realtors

*Comprises New York City, northern New Jersey, Long Island, and Westchester

[9]Data obtained from the National Association of Realtors

the city's economy is heavily oriented toward service employment in its broadest sense—that is, all sectors except manufacturing and construction. Seventy percent of the jobs in the city fall within the scope of the broadly defined service sector—utilities, FIRE, wholesale and retail trade, and other services—compared with about 60 percent for the nation. These are the sectors that are projected by most analysts to be the nation's growth areas in the 1990s. In its occupational structure, therefore, New York City is well positioned to participate in any national surge of economic growth.

*Lingering cyclical difficulties in the Service and FIRE sectors*

When the focus shifts from the most inclusive grouping of services to Services in the more specific sense used by the Bureau of Labor Statistics (defined in footnote 2 above), then both opportunities for future growth in the city's economy and some possible impediments become evident. Restructuring, mergers, and closures are thinning the ranks of both Service and FIRE corporations in the local economy. As the Service and FIRE sectors evolve, their sensitivity to national and international economic cycles also appears to be increasing. In addition, New York City's Service and FIRE sectors may be particularly susceptible to the staffing cutbacks occasioned by any trend in corporate management toward a flattened and leaner corporate hierarchy. And because Service and FIRE corporations include some of the largest employers in New York City, the cyclical expansion of staff is likely to be more limited than in earlier recoveries.

*Contraction in the FIRE sector.* Within the FIRE sector, employment for two key subsectors has been contracting. In just the last two years, over 23,000 jobs have been eliminated from the banking sector as the rationalization of the industry continues. At the same time, there has been some outmigration from the city of the securities industry, which has historically been heavily concentrated in the city in terms of both revenues and employment. In recent years, several prominent securities firms have relocated whole departments to other states such as Florida, Connecticut, and New Jersey. While the city lost 34,100 securities jobs (a decline of over 20 percent) during 1988-92 and minor declines were recorded for the nation as a whole (2.6 percent), securities employment in New Jersey rose each year, boosting the state's economy with a net addition of 8,600 jobs. Although local business cost differentials may have narrowed, New Jersey (like other states outside the Federal Reserve System's Second District) has the advantage of generally lower labor and other major costs, and can continue to attract segments of New York City's financial sector.

*The Service sector.* Similar forces of consolidation and restructuring are at work in the Service sector, suggesting that job growth in the current expansion is likely to be somewhat slower than in prior recoveries. As detailed in the accompanying box, the recent contraction in the city's Service sector was the first serious decline in Service employment in the city in the postwar period. Elsewhere in both the nation and New York State, Service employment continued to expand throughout the recession, and the recession itself was comparatively less severe than in New York City. Now, the hitherto inelastic response of the city's Service sector to an economic downturn has given way to increasing sensitivity to cyclical downturns.

Employment in two subgroups—business and health services—fueled the growth in aggregate Service employment during the expansion of the 1980s. In the recent recession, however, employment in business services fell 18 percent in New York City as against a 2.6 percent decline for the nation. The magnitude of the local decline suggests that city employment in this subsector can be highly sensitive to the business cycle. In a recession, the corporate market for business services may require less outside work because of generally weak business conditions. In addition, corporations may redirect some work to internal staff as budgets tighten during a downturn. Thus, an important source of growth in Service employment during the earlier expansion was also the source of extensive cyclical decline in the recent downturn. The data on business service employment are available from 1975 forward, so earlier patterns of business service employment during New York City recessions cannot be determined. However, the data on aggregate Services does suggest that the sensitivity of the Service sector to overall economic conditions is increasing, and that the future may therefore see cyclical variations in contrast to earlier patterns of stability.

Health and social services employment, the other major contributor to the growth of the Service sector, continued to expand throughout the 1989-92 recession, albeit at a slower pace than in the prior expansion. These services depend heavily on federal, state, and local funding, which of course is subject to change up or down in the coming years. The sustained expansion of health and social services in 1989-92 helped to blunt the effects of the recession in both an economic and a social sense, but it should be noted that on a per capita basis, the gross production per employee has been markedly below that of most other sectors of the economy (Chart 8 inset). In narrow economic terms, therefore, these jobs contribute less to the economy than do jobs in most other industries.

In sum, the one- to two-year prospects for job growth in the FIRE and Service sectors are apparently subject to some limiting forces Over the longer term, however, the prospects may well be stronger Because many of the FIRE and Service jobs are in knowledge-based industries, these sectors carry the potential to "reinvent" themselves and become forceful engines of growth at some future time For example, the securities sector has periodically devised new products and new markets physicists now apply their mathematical knowledge to the financial derivatives market. Business services offered by system analysts, data base managers, biomedical researchers, health care managers, and paralegal and mass-market personal financial consultants are of relatively recent evolution, the increasingly sophisticated equipment used by these professionals also requires the engineering and maintenance skills of

**Box: The City's Service Sector**

Although total city employment has historically been subject to cyclical decline, the local Service sector (excluding finance, insurance, and real estate) has been largely recession-proof Breaking with this pattern, Service employment fell 5 0 percent in the 1989-92 recession—compared with an average decline of 1 0 percent during the four prior recessions. This most recent drop is a potentially destabilizing development because Service employment accounts for about one-third of the city's work force During the prior expansion period, first-quarter 1983 through third-quarter 1989, the job gains in the Service sector were driven by two subsectors 1) business services and 2) health and social services The business subsector, comprising such groups as advertising, public relations, marketing, legal, accounting, consulting, and engineering and management services, is heavily utilized by large corporations responding to national and international markets Such demand and its multiplier effects are generated more by national and international business than by local business The weakness in all three markets contributed to the 18 percent decline in business service employment

Health and social services employment, the other major contributor to the growth of the Service sector, continued to expand throughout the 1989-92 recession, albeit at a slower pace This subsector encompasses hospitals, doctors, and nurses, as well as home attendants, hotlines, outreach, job skills workshops, and senior citizens' centers Such institutions and programs receive significant government funding, which could slow in the coming years with changes in health care programs

Although the Service sector ranks first in employment, it ranks second in output. In New York State, Services account for 22 percent of nominal gross production, the FIRE sector ranks first, producing about 23 percent of the state's gross output This structure of economic output differs markedly from the nation's At the national level, manufacturing ranks first in contribution to gross domestic production, whereas in New York State, manufacturing accounts for about 14 percent of nominal gross production In the city, over 15 percent of the work force is employed in FIRE and another 36 percent in the Service sector. If the state-level employment/production relationships are applied to the city data, the two sectors together appear to account for 55 to 60 percent of the city's gross production The unusual dominance of these two sectors underscores their critical importance to the city's growth prospects †

†The Bureau of Labor Statistics estimates real gross production for major industrial sectors in both the state and the nation Although the Bureau makes no estimates of gross city production, the proportion of state personal income earned in New York City strongly suggests that the trends attributed to the state are at least equally attributable to the city

**Increasing Sensitivity in Service Employment**

| Cycle Dates | Percent Change in Total Employment | Percent Change in Services Employment | Service Employment as a Share of Total |
|---|---|---|---|
| Four-cycle average[1] | −6 1 | 1 0 | 20 8 |
| April 1989-September 1992 | −9 8 | −5 0 | 31 6 |

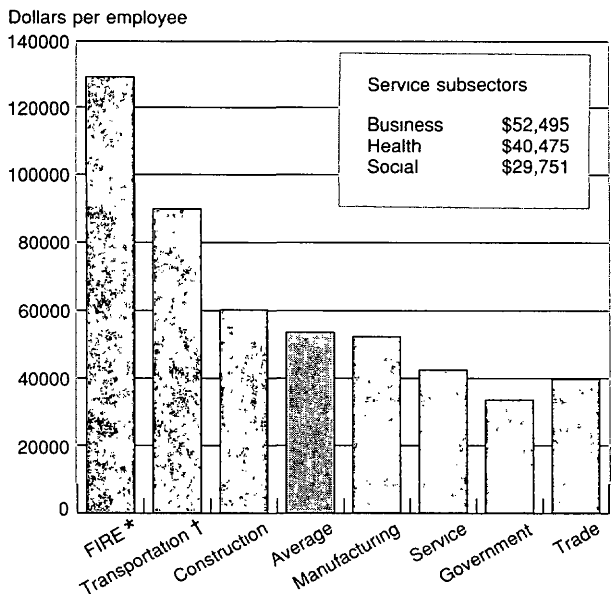
Sources For data, Bureau of Labor Statistics, calculations by Federal Reserve Bank of New York staff
[1]Average of the following cycles December 1952-June 1954, April 1962-January 1963, August 1969-March 1977, September 1981-February 1983

numerous technicians Social change and scientific advances continually raise new issues requiring legal expertise. The common factor among all these jobs is that they are knowledge-based, they carry the potential for further evolution.

Moreover, recent trends in wages and salaries suggest that the prospects for growth in personal income in New York City remain reasonably good. As noted earlier, despite the large decline in FIRE employment, the growth in wages and salaries in the FIRE sector has been so large that it has boosted aggregate wages and salaries in the city In the future, the city may continue to benefit from faster growth in income even if aggregate job growth is flat or remains slow. This outcome is possible because although the FIRE sector dominates gross production, accounting for roughly 30 percent of total output, it requires only 15 percent of the work force. On a per capita basis, each job in the FIRE sector generates *2 4 times as much output as all other sectors.* The wages and salaries that are paid in the FIRE sector reflect this degree of productivity Indeed, as mentioned earlier, income gains in the FIRE sector appear to be leading the recovery in personal income Therefore, even if the contraction in jobs in the FIRE sector continues, it may well be possible to sustain moderate growth in total personal income. Additional support for income growth may also develop in several other sectors Declines in banking employment and the general paring of jobs in a wide range of industries throughout New York City suggest that productivity could increase significantly as demand begins to revive. Such gains in productivity would also support moderate growth in income.

Chart 8

**New York State Nominal Gross Product**




Sources For data, Bureau of Economic Analysis and U S Department of Labor, calculations by Federal Reserve Bank of New York staff

*Finance, insurance, and real estate

† Transportation, public utilities, and communications

*Other constraints and opportunities*

The cyclical and longer term prospects for New York City will be affected by the city's ability to deal with long-standing structural problems such as high costs and taxes and the comparatively large fraction of the population that is out of the labor force These prospects will also depend on the city's ability to capitalize on the opportunities created by the improvement in relative business costs and the ongoing surge in immigration

*Inflation—prices and costs.* The costs of housing and commercial rents, two of the largest components in consumer and business budgets, have already been discussed. Taxes are another major factor in the local economy New York City taxes, at $2063 per person in fiscal 1990, are the highest in the nation on a per capita basis This figure is nearly twice that for San Francisco, which ranked second at $1185.[10] Not only is New York City one of the few cities that taxes personal income, it also imposes several other taxes that are unusual or unusually high, such as the tax on commercial rent or the luxury hotel room tax (city and state tax combined) that applies to most hotel rooms in the city Unfortunately, the effects of myriad local taxes are compounded by state taxes, which are also among the highest in the nation.

Taxes aside, other local costs of goods and services have risen more rapidly in the city than in most other areas in the nation over the past ten years. The consumer price index covers the largest sector of the real economy, consumer spending. Over the postwar period, the rate of consumer price inflation in the greater New York metropolitan area has outpaced the national rate of inflation for prolonged periods of time, including 1958-74 and 1983-92 (Chart 9) As a result, the greater New York metropolitan area has become increasingly more expensive relative to other areas of the country. In the last ten years, the consumer price index has risen 50 percent in New York City in contrast to a national

[10]U S Bureau of the Census, City Government Finances, series GF, no 4, annual

average gain of 40 percent. Housing was the primary contributor to the adverse local inflation differential during the 1980s, accounting for 75 percent of the local premium. The costs of food and personal items in the city also increased significantly faster than their national counterparts, accounting for 22 percent of the premium. Similarly, local wages and salaries also rose somewhat faster than the national averages. Today, the near absence of inflation in the local housing market should prove a positive factor, helping the city attract and retain new businesses and their employees. However, although the overall rate of local inflation has slowed in recent months, the national average (and the rate in other major cities as well) has shown a more pronounced decline, so that the relative position of the city has failed to improve.

*Local government.* Local government jobs were a prime contributor to the employment gains during the 1983-89 expansion, accounting for 88,000 jobs or 30 percent of the job growth. In the subsequent recession, the relative stability of local government employment was a moderating factor for the economy. Whereas total employment in the city declined about 10 percent, peak to trough, this sector fell only a moderate 3.6 percent. Today, the local government payroll accounts for about 14 percent of all employment in New York City, the national average is 10.4 percent.[11]

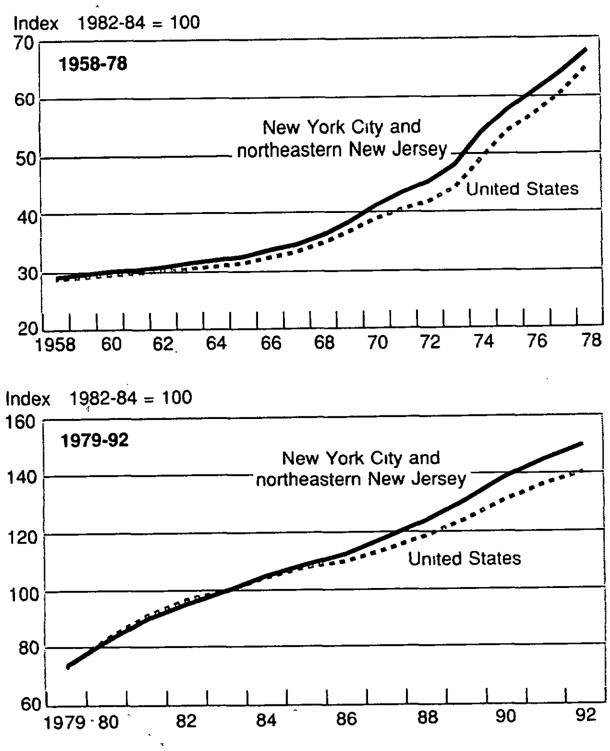
As the recovery proceeds, local government employment may continue to behave countercyclically and act as a drag on the city's economy. To maintain the sizable local government payroll in the face of a lackluster economic environment, the city must now either increase its revenue stream through additional taxes, licenses, and fees or cut back its services. These budget constraints make it difficult for the city to reduce unusual taxes, improve basic services, and enhance the general business climate.

*Labor: Composition and participation.* The second structural factor that has inhibited the city's underlying growth potential has been the unusual composition of the labor force and the low labor force participation rate. The population declines of the 1950s and the 1970s have yielded to slow growth of 0.35 percent per year in the 1980s. The recent population movements, however, appear to have occurred alongside some decline in the average education and skill levels of the resident (noncommuting) work force. Several hundred thousand people, many of them highly skilled, left the city during the 1980s. Their numbers were more than fully replaced through the arrival of 1 million new immigrants during the decade.[12] The immigrants, in many cases, brought to the city energy, youth, and innovation, but they have also placed additional demands upon New York's social services. Moreover, the growth areas of employment in the city tend to be in knowledge-based industries. At least initially, many immigrants from other countries lack the language or skills to fully replace the workers who have left the city. Language barriers make it very difficult for some highly skilled and educated groups to obtain employment, while other groups lack both skills and education. This settlement problem may be nearly as old as the city itself, but the city's heavy expenditures on social safety nets are of more recent vintage. Although Congress sets the laws governing the volume of legal immigration for the United States as a whole, the costs of settlement fall disproportionately on a few large cities such as Los Angeles and New York.

Of course, many of those who left the city in the

Chart 9

**Consumer Price Index**




Source: Bureau of Labor Statistics

[11]Although local government accounts for 10.5 percent of total employment in Los Angeles, it averages about 9 percent of total employment in most other major cities such as Chicago, Philadelphia, Detroit, Dallas, Houston, and Atlanta.

[12]Decennial Census 1990, Bureau of the Census.

1980s moved to the suburbs and now commute to their jobs in New York, so their skills are not lost to the city's work force. Their tax revenue, however, is substantially reduced because the city's personal income tax rate drops significantly for nonresidents. In addition, commuters may require services such as police, fire, transportation, and water—and at levels not much below those required by city residents. Thus the revenue losses stemming from the emigration of workers to the suburbs may not have been matched by an equivalent decline in the cost of city services to these people.

Low labor force participation rates are another problem for the city's economy. As mentioned earlier, a smaller portion of the population in New York City is working or looking for work than in many other major cities in the United States. In 1992, the participation rate in New York City was 56.3 percent, significantly below the 66.0 percent participation rate of the nation. This means that nearly an additional 10 percent of the city's population would be working or looking for work if the city's participation rate matched that of the country at large. New York City ranks midway among major cities in its poor participation rate, and the low rates generally cross the lines of sex and race. That is, if the participation rates are compared across aging industrial cities, the New York City rates fall below those of many other major cities, *regardless* of sex or race (see table).

Some popular explanations of the comparatively low participation rate in New York City suggest an undercount of the work force. A large number of people employed in the arts may work outside established, record-keeping organizations; similarly, a large number of people may be employed in an undocumented, underground economy. This last factor, however, would depress the city's relative participation rate only if the city's underground economy were significantly larger than that of aging industrial cities that have higher participation rates. The arts community in New York *is* a large and possibly undermeasured sector of the local economy, and it could account for some of the difference in participation rates. Other than the arts, however, there seems little evidence to suggest that the city has an undocumentated economy proportionately larger than that of other major industrial cities.

Whatever the cause of the city's low participation rate, the result is a double-edged problem. First, the tax burden for both New York State and its major metropolitan area is spread over a proportionately smaller work force. Second, the low participation rate suggests increased public assistance, a relationship that is borne out by the data: fully 13.3 percent of the city's population receives public assistance, whereas the national average is 5.3 percent.[13] Thus, low labor force participation rates tend to raise the demands on the city's budget for social services because more people require assistance. (In addition, the cost of such services to the city is further inflated because the eligibility requirements for public assistance are less restrictive and the programs of assistance generally more comprehensive than in many other metropolitan areas.) Raising the participation rate will require a more robust economy.

[13]New York State Department of Social Services and Family Support Administration, Fiscal 1992.

**Labor Force Participation Rates in Major Cities**

| | **New York** | Baltimore | Chicago | Detroit | Los Angeles | Philadelphia | Washington D.C. |
|---|---|---|---|---|---|---|---|
| Total | **56.4** | 59.3 | 61.4 | 51.7 | 66.4 | 55.8 | 65.7 |
| Men | **68.1** | 65.3 | 72.2 | 61.3 | 78.4 | 64.5 | 70.3 |
| Women | **46.5** | 53.7 | 51.8 | 43.9 | 54.7 | 48.5 | 61.6 |
| Both sexes, 16-19 years | **22.5** | N.A. | 36.5 | 41.1 | 37.9 | 42.3 | N.A. |
| White | **55.8** | 54.0 | 66.8 | 45.6 | 67.9 | 56.1 | 79.2 |
| Men | **69.3** | 61.0 | 79.2 | 54.9 | 80.6 | 68.3 | 85.5 |
| Women | **44.3** | 47.0 | 54.6 | 36.6 | 54.8 | 46.4 | 72.6 |
| Both sexes, 16-19 years | **26.3** | N.A. | 49.3 | N.A. | 40.4 | N.A. | N.A. |
| Black | **55.7** | 62.7 | 53.7 | 53.1 | 58.0 | 55.7 | 58.3 |
| Men | **63.3** | 68.6 | 60.8 | 62.8 | 66.8 | 60.0 | 61.3 |
| Women | **49.8** | 57.6 | 48.4 | 45.6 | 50.8 | 51.8 | 55.8 |
| Both sexes, 16-19 years | **15.2** | N.A. | N.A. | 41.7 | N.A. | N.A. | N.A. |
| Hispanic Origin | **50.7** | N.A. | 70.4 | N.A. | 68.4 | N.A. | 83.7 |
| Men | **67.1** | N.A. | 83.8 | N.A. | 84.1 | N.A. | 92.7 |
| Women | **38.3** | N.A. | 54.7 | N.A. | 51.8 | N.A. | 75.7 |
| Both sexes, 16-19 years | **20.0** | N.A. | N.A. | N.A. | 36.5 | N.A. | N.A. |

Source: Bureau of Labor Statistics, *Geographic Profile of Employment and Unemployment*, 1991.

From 1983 to 1989, relatively strong local growth, albeit below national growth rates, did raise the city's labor force participation rate, but only by about 1.5 percentage points. Moreover, much of that gain was reversed during the recession.

The low participation rate and the steady flow of immigrants are not really new issues for the city; nor are the concurrent "quality of life" issues that have been raised since at least the late 1800s. New York City is a magnet precisely because it remains the city of opportunity, and the cyclical economic downturn may actually constitute a widened window of opportunity. Even now at the trough of the economic cycle, when painful city budget decisions are being made, lower business costs are attracting new enterprises to the city and there are increased reports of companies reviewing their plans to leave the city and opting instead to stay. With little or no expenditure, the city can streamline some regulations, enlarge the job market, and increase job opportunities. For example, major discounters that have served the rest of the nation for years are finally entering the New York City market because retail space is available at an attractive price *and* city zoning regulations have been changed to permit such large-scale operations. These stores will require clerks, sales staff, and stockroom workers—jobs that require some skill but not highly advanced training. Proposals have also been made to decrease the tax that small businesses pay on their rent in order to spur new business development and hiring. In effect, the city's financial difficulties and the sluggish economic environment have created the impetus to seek such low-budget changes. The city's problems are old, but the changing economic cycle has made all parties more willing to seek solutions.

### Conclusion

Total private employment in New York City declined 10.9 percent, in aggregate, from the first quarter of 1989 to the third quarter of 1992, but the drop seems to have come to an end. Some cyclical and structural forces will tend to dampen the overall economic expansion in New York, impeding the recovery in construction and slowing employment growth in several sectors of the city's economy. In the absence of any major new external stimulus, the current slow trend of recovery appears likely to continue. However, the city's budget difficulties have also prompted many new efforts to seek solutions to the problems, so the opportunity for change is particularly strong at this point in the cycle. Because the city continued to shed jobs well into the third quarter of 1992, productivity in New York City may be poised to rise significantly as demand improves. Potential gains in real production per worker could boost the competitiveness of several industries in the city, thus partially offsetting the high-cost operating environment. In addition, productivity gains should support moderate growth in personal income and output, coincident with slow growth in employment.