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SECOND DISTRICT HIGHLIGHTS

Job Declines in New York–New Jersey Region to Slow in 2003; Modest Growth Seen for 2004

James Orr and Rae Rosen

Employment in the New York–New Jersey region will decline in 2003—but only slightly—and the region's economy is poised to rebound in 2004 with 1 percent growth, or a gain of 128,000 jobs. Continued expansion in the national economy and sustained vigor in the financial markets, however, will be essential to a favorable employment outlook.

Employment in the New York–New Jersey region fell for a second straight year in 2002. By February 2003, private sector employment was down nearly 390,000 jobs, or about 3.6 percent, from its peak at the end of 2000. This drop was just slightly more than half the size of the region's job decline during the 1989-92 downturn, but as a share of total employment, it exceeded the comparable nationwide decline by almost a percentage point. And while employment levels have edged up in recent months, the job count remains substantially below its cyclical peak.

The downturn in regional employment has occurred in several distinct phases. Many of the job losses took place during 2001, when the area met with a series of adverse developments. Failing dot-coms, the weakening stock market, and a slowing volume of initial public stock offerings began to weigh down growth both directly and through their impact on the professional and business services supporting these activities. The national recession that began in March 2001 compounded this weakness, and growth turned negative around midyear. The pace of decline picked up in the fourth quarter of the year and into early 2002 as a result of job losses associated with the 9/11 attack on the World Trade Center. However, during 2002, that pace slowed considerably in New York and New Jersey and, for the past year, job losses on a year-over-year basis have moved more or less in step with the nation's moderate pace of decline.

Within the region, major job losses were concentrated in New York City. After expanding at a rate substantially higher than the national rate in 1999 and 2000, employment in the city fell sharply in 2001, reflecting New York City's position at the center of the financial markets, the dot-com demise, and the disruptions owing to 9/11. Although the city's job declines were still much less severe than they were during the 1989-92 downturn, employment as of February 2003 had fallen by roughly 225,000 from its cyclical peak at the end of 2000. Job losses in New York State as a whole were much less dramatic during this downturn because New York City's suburbs fared relatively well. Despite the recession, several suburban areas continued to generate modest job gains through 2001 and then declined only negligibly in 2002. In New Jersey, employment decreased only modestly in 2001, and levels have remained essentially unchanged for much of the past two years.

Looking ahead, we expect that the level of employment will continue to edge up over the remainder of 2003 and that the region will post a modest 0.3 percent decline in jobs for the year overall. This relative improvement takes into account the Blue Chip Consensus forecast that the national growth rate of real, or inflation-adjusted, GDP in 2003 will not slow from the 2.4 percent rate achieved in 2002,[1] and assumes that broad stock market measures such as the S&P 500 will at a minimum not fall below their June 2003 averages. A forecasted further pickup in the national growth rate of real GDP to 3.6 percent in 2004 and some acceleration in financial market activity are projected to push regional job growth to 1.0 percent next year.

In this edition of *Second District Highlights*, we analyze employment trends in the New York–New Jersey region over the past two years and present our forecast for job growth in New York City, New York State as a whole, and New Jersey in 2003 and 2004. In addition, we describe the structure of employment in the region according to the new North American Industry Classification System (NAICS) introduced by the U.S. Department of Labor's Bureau of Labor Statistics (see box). This new system reorganizes the previous industry classification sectors and introduces several new classifications, including an information sector and a leisure and hospitality (tourism) sector, that capture job trends in industries that are key forces in the evolution of the region's employment. Some risks to the region that could affect our employment outlook are also considered.

Review of Regional Employment Developments

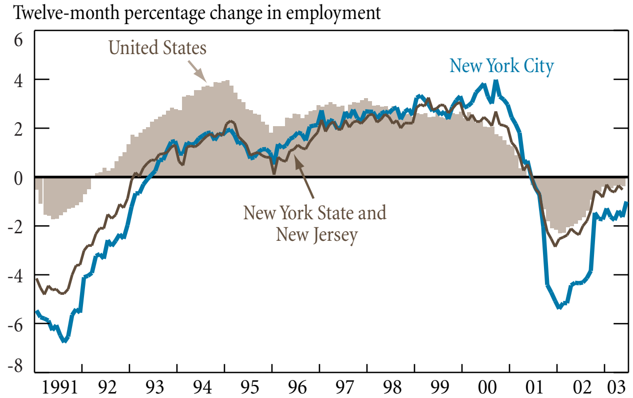
The level of private sector employment in the New York–New Jersey region peaked in December 2000, and job growth on a year-over-year basis began to slow (Chart 1). Between January and September 2001, private sector jobs in the region fell by almost 210,000. A number of adverse developments contributed to this decline. The slowing initially reflected weakness in several industries that had been key drivers of job growth for much of the second half of the 1990s. The drop in stock prices from September 2000 through March 2001—approximately 17 percent as measured by the S&P 500 and 33 percent as measured by the NASDAQ—contributed to the subsequent weakening of employment in the finance sector, as financial employment in New York City alone fell by 30,000 jobs in the first nine months of 2001. Moreover, employment in professional and business services—one of the region's largest sectors and one whose performance is closely linked to that of the finance sector—decreased by almost 100,000 jobs, or 6 percent; around the same time, a significant number of dot-coms failed and 10,000 or so jobs were lost in the information sector.[2] Adding to the pressure, the nation entered a recession in March 2001 that was associated with a broader based weakening in job growth throughout the region. Construction employment, which had experienced heady gains for several years, began to drop in mid-2001, and the pace of employment declines in manufacturing accelerated.

The region's job losses resulting from the attack on 9/11 compounded the national downturn's impact on employment. Between October and December 2001, jobs diminished by 75,000 in New York City, with losses occurring largely in industries directly and indirectly affected by the attack, such as finance, hotels, transportation, and segments of the retail trade sector.[3] At the end of 2001, these declines had contributed to a 3.0 percent reduction in the region's private sector employment from the year-earlier level, compared with a 1.8 percent drop nationwide. Among the major industries, only education and health care added jobs in significant numbers. In the public sector, a modest acceleration in the growth of state and local government employment gave limited support to overall employment.

During 2002 and through May 2003, the pace of year-over-year employment declines in the region moderated considerably as the losses associated with 9/11 receded gradually over 2002 and the national economy strengthened.[4] Employment in the region's finance sector generally stabilized, but losses in professional and business services employment continued, although at a sharply reduced pace. Construction

Chart 1
Private Sector Job Growth in the United States and the New York–New Jersey Region

Twelve-month percentage change in employment



Sources: New York State Department of Labor; New Jersey Department of Labor; U.S. Department of Labor, Bureau of Labor Statistics.

The North American Industry Classification System

In January 2003, the U. S. Department of Labor's Bureau of Labor Statistics introduced the North American Industry Classification System (NAICS) to identify establishments by industry and to enhance the reporting of monthly employment data. NAICS replaces the Standard Industrial Classification system, which provided richly detailed information on employment in the manufacturing sector but offered considerably less data on services.

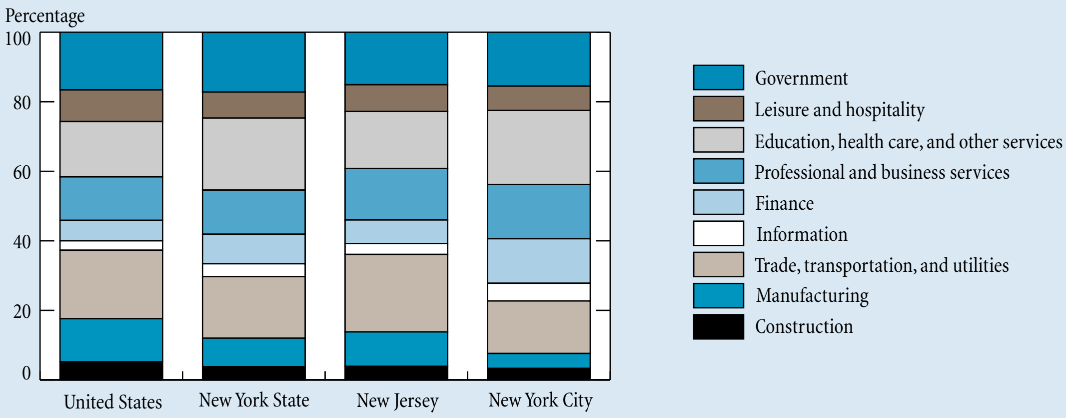
Several of the NAICS changes to industry definitions are relevant to our analysis of employment trends in the New York–New Jersey region. First, NAICS restricts the definition of a manufacturing establishment; specifically, it excludes the administrative headquarters of a manufacturing firm, reclassifying those establishments in a new sector: *professional and business services*. Employees directly engaged in the production of goods continue to be classified in manufacturing. The sector accounts for only 4.3 percent of employment in New York City, but it represents 8.2 percent in New York State as a whole, 9.9 percent in New Jersey, and 12.4 percent nationwide (see chart).

Second, the new professional and business services sector clarifies the makeup of the old services category by establishing two key subsectors. One is professional, scientific, and technical services, a group that encompasses computer systems and design, architectural services, engineering services, environmental services, management consulting, advertising and marketing, and veterinary services. The second subsector is the administrative, support, waste management, and remediation industry, which includes temporary workers. Through these two subsectors, NAICS adds important details to several of the services supplied by firms in the region.

Third, a new *information* sector was created by NAICS that includes, among many other industries, newspaper publishers and motion picture producers, sound-recording studios, broadcasting, cable programming and TV broadcasting, data processing, satellite telecommunications, wireless communications, Internet service companies, and news syndicates. Although the sector represents only a relatively small share of jobs—5.1 percent in New York City, 3.7 percent in New York State as a whole, and 3.1 percent in New Jersey—it consolidates into a coherent sector a number of industries that used to be scattered throughout various sectors.

Finally, another new sector, *leisure and hospitality*, was created to accommodate restaurants, hotels, fast-food franchises, museums, and other forms of entertainment that make up a set of establishments closely linked to tourism. This sector accounts for 7.0 percent of employment in New York City, 7.5 percent in New York State, and 7.7 percent in New Jersey.

Share of Total Employment by Sector
2001-02 Average



Source: U.S. Department of Labor, Bureau of Labor Statistics, North American Industry Classification System.

employment picked up modestly, and although manufacturing continued its well-established trend of contraction and relocation, the pace of losses in this sector moderated substantially. Transportation and utilities saw job losses bottom out while retail trade saw solid job gains. Education and health care jobs continued to expand in 2002, although at a modestly slower pace. Employment growth in the public sector stalled.

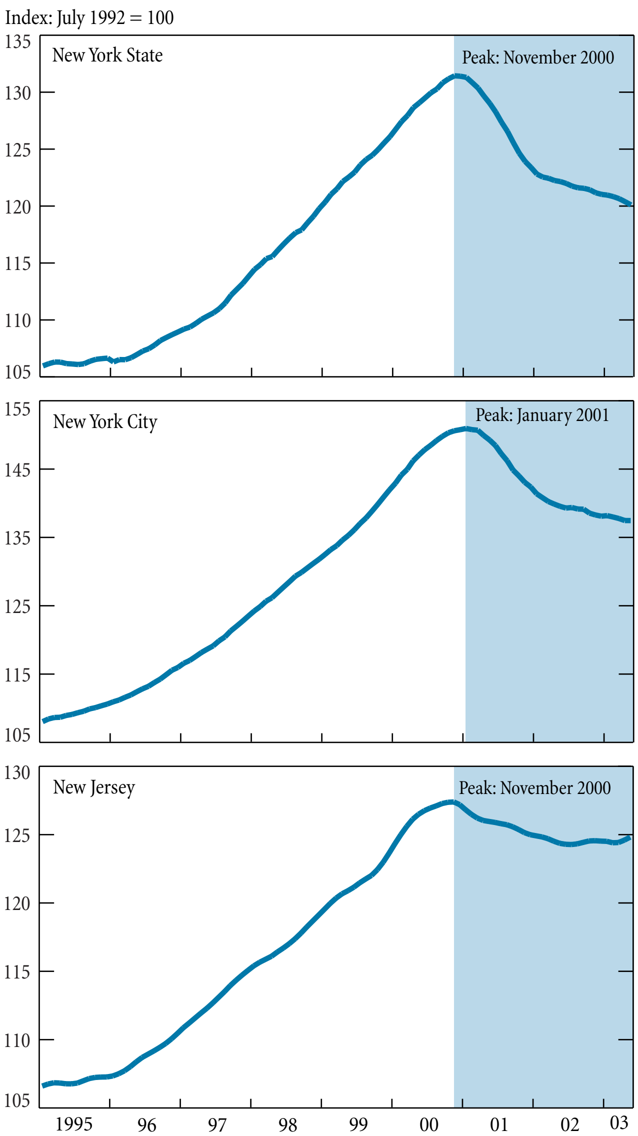
New York State

According to our index of coincident economic indicators (CEI), economic activity in New York State peaked in November 2000, almost a year before the attack on the World Trade Center and four months before national economic activity reached its peak (Chart 2).[5]

Employment weakness appeared initially in finance, particularly among commercial and investment banks and securities firms, and in computer-related services; much of the weakness was concentrated in New York City. At the time of the attack, employment in New York State had already fallen 1.0 percent from its year-earlier level. In the quarter following 9/11, private sector employment fell by 3.2 percent, or 235,000 jobs, from its level in the comparable period in 2000. The declines persisted into early 2002, but began to lessen significantly as the year progressed. By the end of 2002, employment in the state was just 0.9 percent below the year-earlier level. As of May 2003, the decline had lessened to just 0.6 percent below the year-ago level, buoyed by sustained vigor in health care and social services employment; a modest pickup in trade, transportation, and utilities jobs; and the stabilization of finance sector employment.

Chart 2

Indexes of Coincident Economic Indicators for New York State, New York City, and New Jersey



Source: Federal Reserve Bank of New York staff calculations.

This relative improvement in 2003 masks a wide variation in job growth trends across the state. New York City accounted for fully two-thirds of the state's job losses in the current downturn—more than its share of employment. Its suburbs, however, benefited from the robust growth enjoyed by the city in the late 1990s, and they lost proportionately fewer jobs to the recession and the 9/11 attack.[6] Job declines in western New York were relatively mild, although the area continues to be weighed down by the ongoing contraction in manufacturing jobs and the struggle to attract new industries.[7]

New York City

Shortly after our CEI signaled a peak in the city's economic activity in January 2001, employment growth, which had risen steadily at an accelerating pace for eight years, began to slow. By July 2001, the deceleration had given way to decline.

The attack on the World Trade Center further undermined the city's employment growth; the ensuing job losses were widespread and included significant hits to leisure and hospitality; trade, transportation, and utilities; airlines; professional and business services; and finance.

The rate of decline in manufacturing spiked from 5.4 percent in 2000 to more than 12.0 percent in 2001. That year, manufacturers in the city gave up more than 20,000 jobs. By year-end 2001, the city had lost nearly 5.0 percent of its job base. The rate of loss slowed in 2002; by May 2003, the year-over-year decline in jobs had decelerated further, to 1.6 percent. The slowing rate of decline is an improvement in the economic picture, but the level of employment remains well below its prior peak and has yet to show any sustained rise.

Two recent indicators of improvement in the city's finance sector are worth noting. The first comes from a report on domestic pretax profits in the securities industry.[8] According to the report, securities firms tripled their pretax profits to \$3.5 billion in the first quarter of 2003 from \$1.1 billion in the fourth quarter of 2002. The improvement was narrowly based on strong revenue growth from their fixed-income and energy-related trading businesses. A broader revenue recovery may be necessary to spur job growth in this sector, but this advance suggests that incentives for layoffs are lessening. Significantly, preliminary data for the second quarter suggest that a broader based recovery has begun, with revenue growth spreading to most business lines while volume-related wages rise for some lines. The second indicator of finance sector improvement comes from reports by several major commercial banks that strong revenue growth had generated healthy profits.[9] Layoffs due to restructurings, mergers, and acquisitions among commercial banks were responsible for significant job losses over the past two years, but such profit strength may signal an end to these layoffs.

New Jersey

Our New Jersey index of coincident economic indicators points to a modest expansion in activity in recent months. The index, which peaked in November 2000 and fell steadily through mid-2002, has been flat to slightly rising for the past nine months. These increases strongly suggest that the state's downturn has ended.

Private sector employment in the current cycle peaked in December 2000, then declined by 1.4 percent, or 55,000 jobs, over 2001. Employment remained relatively flat through February 2003 and has since begun to recover. This relatively mild pace of losses has matched or exceeded performance at the national level. Government jobs have continued to expand since 2001, helping to support overall employment.

Employment in the state was subject to some of the same adverse conditions affecting other parts of the region, including the new-media bust, the weakness in manufacturing, and the retrenchment in telecommunications. Although employment in these sectors continues to decline, the rate of decline has slowed and the major job losses appear to be over.

Much of the immediate impact of 9/11 on jobs in New Jersey also appears to have subsided.[10] Moreover, the state experienced only mild losses in professional and business services, and employment levels in this key sector have expanded modestly in recent months. Declines in transportation and utilities appear to have bottomed out, and growth in the leisure and hospitality sector, which had stalled in 2002, is again picking up. Jobs in education and health care expanded throughout the downturn and are growing at a month-to-month annualized pace of roughly 4.0 percent. Employment in retail trade has bounced back and is expanding at an annualized clip of 2.0 percent; jobs in construction, although off their healthy pace of previous years, are showing mild gains.

Forecast for 2003 and 2004

Employment in the New York–New Jersey region is projected to decrease by 0.3 percent, or roughly 36,000 jobs, in 2003 (see table). This decline, however, still represents an improvement over the preceding year's relatively sharp fall of 1.2 percent.

Employment in the New York–New Jersey Region: Past and Projected Growth

Annual Percentage Change

	2001	2002	2003	2004
New York and New Jersey	-0.3	-1.2	-0.3	1.0
New York State	-0.5	-1.8	-0.6	0.8
Private sector	-0.6	-2.4	-0.8	0.9
Public sector	0.0	1.4	0.0	0.5
New York City	-0.8	-3.2	-1.6	0.6
Private sector	-0.9	-3.8	-1.5	0.6
Public sector	-0.7	0.5	-2.0	0.5
New Jersey	0.1	-0.1	0.4	1.4
Private sector	-0.3	-0.5	0.5	1.7
Public sector	2.3	2.0	0.1	0.2

Sources: New York State Department of Labor; New Jersey Department of Labor; Federal Reserve Bank of New York projections.

Note: The 2003 and 2004 figures are projections.

Underlying this projected improvement is the Blue Chip Consensus forecast of a year-over-year 2.4 percent rate of aggregate economic growth in 2003—a rate that matches the 2002 pace and signals the continuation of the national recovery. The projected improvement also reflects the assumption that financial markets will at a minimum maintain the gains of roughly 10 percent achieved by S&P 500 stocks in the first six months of this year.[11] The services sector will be the region's engine of job growth: professional and business services will see losses moderate, and education and health care services and leisure and hospitality services will continue their solid expansion. Job shrinkage in finance is expected to end and could reverse by year-end given the stabilization of the financial markets. The manufacturing and information sectors will continue to see significant job losses, yet at a moderately slower pace than in 2002.

In 2004, growth is projected to reach 1.0 percent (see table), resulting in the net creation of 128,000 jobs. The recovery in employment will be supported by the expected acceleration in national growth to 3.6 percent that year.[12] Also projected for 2004 is a modest continuation of the improvement in financial market activity that will generate some job growth in the region's finance sector and in supporting services in many other sectors. Overall, services jobs will again be the major source of growth, spurred by a relatively strong bounce-back in professional and business services. This sector will respond both to the rising demand stemming from the strengthening national economy and the improving finance sector and to gradually improving local demand. Trade, transportation, and utilities will add a significant number of jobs while construction will expand moderately. The information sector is expected to stabilize in 2004, but jobs in manufacturing will continue to contract in light of this sector's long-term structural decline. An anticipated pickup in local government jobs will add to a modest expansion of public sector employment.

New York State

Employment should benefit from the projected gradual improvement in the national economy, with increased demand fueling growth in such sectors as professional and business services, information, and leisure and hospitality. More local and regionally oriented sectors such as trade, transportation, and utilities will respond to the gradual improvement in the state and regional economies. Following an anticipated slide of about 0.6 percent in 2003—an improvement over the decline of 1.8 percent in 2002—a moderate gain of 0.8 percent is projected for 2004.

Financial employment outside New York City is likely to grow modestly in 2004 as general economic activity rises. Construction employment is projected to accelerate in 2004 with the overall economic pickup and with progress in the planning process for 9/11 reconstruction. The education and health care sector, which expanded throughout the recession, appears likely to stick to that pattern through 2003 and 2004, although the rate of job growth in health care may moderate, given state budget constraints.

New York City

Employment is expected to display moderate gains in the second half of 2003. However, the depth of job losses has been sufficiently large that year-over-year gains may not materialize until late 2003; thus, jobs are projected to fall 1.6 percent for the year overall.

For 2004, we see a 0.6 percent expansion. Professional and business services and information are the two sectors likely to emerge as the key sources of growth. Professional and business services—a sector that includes computer analysts and systems developers and that served as a wellspring of the city's job growth in the 1990s—should see an intensification of demand as the national economy picks up. Since the city has a high concentration of professional and business jobs, the increased demand will help spur overall economic growth. Much of the city's employment in the information sector is in the headquarter operations of TV broadcasting, news syndication, cable programming, newspaper publishing, and motion picture production. The demand for these services will also be sensitive to an improving national economy.

A sustained rebound in the stock market and pretax profits could lead to a broader rally in securities industry employment, since greater financial market activity has historically been associated with expanded financial employment, as well as with an increased demand for banking services, legal services, advertising and marketing services, real estate, and leisure and hospitality services.[13] Significantly, preliminary data for the second quarter of 2003 suggest that a broad-based recovery in revenues may be under way, and the securities industry now anticipates that pretax profits may nearly double to $15 billion in 2003 from $8.1 billion in 2002.[14]

Leisure and hospitality jobs have benefited from the upturn in domestic tourism in 2003, but they remain constrained by the dramatic decline in domestic business travel and international travel. However, a strengthening national economy is likely to boost demand for these services and provide an impetus for growth. Some deceleration in the growth of health care services employment may occur but, on balance, the level of employment in health care and education is still likely to advance at a moderate pace given the continued underlying demand. Manufacturing employment is expected to continue its long-term secular decline, but the construction sector and the trade, transportation, and utilities sector are likely to expand, reflecting a strengthening in regional and national demand.

New Jersey

We project that employment will expand 0.4 percent in 2003, representing about 17,000 net new jobs. Services will lead growth, particularly in the education and health care sector. Manufacturing jobs will continue to decline, although at roughly half their 2002 pace, and employment in the information sector is expected to stabilize after falling more than 8.0 percent in 2002. The trade sector is expected to undergo job expansion, but it will be offset by mild declines in transportation and utilities employment.

In 2004, job growth in the state will most likely accelerate, to 1.4 percent, with roughly 58,000 new jobs created. The rebound reflects faster paced growth in services employment, especially professional and business services, and a modest expansion in the construction sector and the trade, transportation, and utilities sector. The finance sector should see some job gains owing to the general improvement in financial market activity and a return to the sector's longer term trend of moderate growth in New Jersey.

Conclusion

After declining a modest 0.3 percent in 2003, employment in the New York–New Jersey region is expected to bounce back in 2004 with growth of 1.0 percent. We base our outlook on two key assumptions: the Blue Chip Consensus forecast will be on target with its projections of real GDP growth rates in 2003 and 2004, and the broad stock market averages will not fall far below their June 2003 levels for a sustained period. Job growth in New Jersey is expected to occur almost twice as rapidly as job growth in New York State, which is being weighed down by a more modest employment recovery in New York City.

We caution, however, that the uncertain extent of the rally in financial market activity remains an important risk to the region, particularly to New York City, and a slower than projected rebound in national growth would provide less impetus to the regional economy. In addition, the downturn experienced by the region has strained state and local government budgets, and tax increases and expenditure cuts have been imposed to balance the budgets. Should job growth be slower than projected, the fiscal stress could intensify. The challenge then facing policymakers would be to address these fiscal demands without harming the New York–New Jersey region's long-term growth potential. However, should a more rapid recovery develop in the financial markets or should the national pickup gather steam, the outlook for job growth and regional budget issues would brighten.

Notes

1. See *Blue Chip Economic Indicators* (2003).

2. "Professional and business services" and "information" are two of the new NAICS sectors. The information sector includes publishing, telecommunications, and Internet and related businesses. It represents a large segment of the new-media industry—one that had not been well defined until now.

3. See Bram, Orr, and Rapaport (2002) for details on the attack's impact on New York City employment; Bram (2003) provides estimates of the separate effects of the attack and the national recession on the city's job trends.

4. See Bram (2003).

5. The CEI is a single composite measure used to track economic activity and to date business cycles. Indexes for New York State, New York City, and New Jersey can be found at <http://www.newyorkfed.org/rmaghome/regional/cei/main.html>. See Orr, Rich, and Rosen (1999) for a discussion of the construction of the indexes.

6. For example, the Albany, Dutchess, and Nassau-Suffolk labor markets declined just 0.4 percent, to 0.6 percent, in 2002 while employment in the Newburgh area rose 0.6 percent. Jobs in the suburban counties of Rockland, Putnam, and Westchester fell about 1.0 percent in 2001 and were essentially flat in 2002.

7. See Deitz and Garcia (2001).

8. See Securities Industry Association (2003, p. 27).

9. See *American Banker* (2003) and *New York Times* (2003).

10. In the months following the attack, about 15,000 jobs in New York City's finance sector relocated to New Jersey. We estimate that about one-third of them returned to the city in 2002. The state appears to have retained the other two-thirds, and has added modestly to them over the past year.

11. See *Blue Chip Economic Indicators* (2003).

12. See *Blue Chip Economic Indicators* (2003).

13. See Bram and Orr (1999).

14. These data are publicly available from the Securities Industry Association.

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About the Authors

James Orr is a research officer and Rae Rosen an assistant vice president at the Federal Reserve Bank of New York.

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