New Jersey Economic Insights

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Outlook New Jersey

Despite Disappointing Job Numbers, Underlying Data Show Gains

New Jersey

Growth in the Garden State's job market has been choked by some of the same factors stunting the progress of the national economy. After three positive months that saw the welcome addition of 28,800 private jobs, New Jersey's private sector job count fell by 700 in May. The unemployment rate rose to 9.4 percent. These numbers are in line with the poorer national numbers that saw private employment nationwide grow by only 73,000 in May and the national unemployment rate inch up to 9.1 percent. The Federal Reserve Bank of Philadelphia's June index of local manufacturers also deteriorated.

Clearly, the near-term trajectory of the economy is cause for concern. Still, it is possible to be too pessimistic. A deeper look at the data shows greater underlying firmness than the employment figures suggest, and recently released numbers that track the overall path of the state's recovery show substantial progress.

Job losses in May were concentrated in construction and manufacturing after an employment surge in these sectors in April. Such steep rises are often the result of statistical flukes and can result in sharp corrections soon after they are released. The drop in construction and manufacturing masked New Jersey's addition of 4,200 service jobs in the private sector following April's gain of 8,900 service jobs, also in the private sector. The private service producing sector accounts for more than 85 percent of New Jersey's private employment and in both months its job-creating performance outpaced the nation's.

Indeed, since January, New Jersey businesses have created nearly 28,000 service sector jobs, about 8,000 more than if we had grown at the national rate in that period. In particular, employment in one key sector — professional and business services, an area that encompasses the jobs of tens of thousands of skilled professionals and is square in the heart of the state's economy — has grown nearly 3 percent, or by 15,000 jobs, since January, after very limited growth last year.

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It goes without saying that May's 9.4 percent unemployment rate is deeply distressing, but not clearly more so than April's 9.3 percent. The increase in the unemployment rate did not reflect fewer people working in May. It came from an increase in the number of people who said they were looking for work. Technically, an "unemployed" person is someone who is actively looking for work. The category includes everyone who is collecting unemployment insurance, but also many others.

Apparently, some people who had given up looking for work and so had no longer been counted as "unemployed" decided to resume their search in May, possibly because job conditions improved a bit. The bottom line is that a small rise in the unemployment rate like May's is not necessarily a sign that conditions are getting worse. Indeed, our Garden State Activity index continued to move up in May.

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Other data show that significant portions of the state's economy have made important strides toward recovery. The U.S. Bureau of Economic Analysis (BEA) has reported that New Jersey's Gross Domestic Product (GDP) — an encompassing measure of activity designed to be comparable to the similarly-named national statistic — rose 2.5 percent in 2010. This increase, the largest since 2006, offset about two-thirds of 2009's sharp decline. New Jersey's increase was very close to the national gain of 2.6 percent and ranked twenty third across the 50 states. Of course, while the rise in output clearly shows the state's economy has been growing, the high unemployment rate highlights how much ground lost to recession has yet to be recovered.

Further evidence on the state's recovery is provided by the numbers on incomes. BEA reports that from the fourth quarter of 2010 to the first quarter of 2011, aggregate personal income in New Jersey rose 1.8 percent, to an annual rate of $453.8 billion — a new record high. In sum, while the sluggishness in employment is quite disappointing, the ongoing gains in physical output and income seem likely to be reflected in brisker hiring.

U.S. Economic Outlook

The national numbers still reflect some of the "soft patch" effect. Most notable, the labor market stayed weak in June, with the unemployment rate reaching 9.2 percent. While private job growth has slowed, the recent weakness in the labor market has been exacerbated by cuts in government employment. There have been some signals that the private sector is improving, and, as was the case last year, we could well be setting the stage for a second half that looks substantially better than the first half. Retail sales in May were held back by a shortage of Japanese models hurting car sales. Correcting for that temporary factor, car sales were fairly solid. Manufacturing production — which was hit hard in April by the effects the disasters in Japan had on auto plants in the U.S. — rebounded in May. Commodity prices, particularly oil, have softened, taking away some of the risk of inflation. Indeed, recent declines in gasoline prices could result in some negatives for headline inflation.

It's most likely that the economy will shake off the recent headwinds and start to move forward at a faster pace. The Federal Open Market Committee's latest forecast calls for a pickup in growth in the second half of the year and for the unemployment rate to edge down. There's no doubt there are significant risks in the outlook. The continuing European debt crisis is one; not so much because the dollar amounts of items such as Greek debt are so large in the global context, but rather because of the potential risks to banks and other financial institutions, not only in Europe but in the U.S. as well.

Closer to home, housing, usually the leading edge of an economic expansion, remains in disarray. The underlying factors of demographics, incomes and interest rates all suggest that we should be now seeing a pronounced recovery in housing. Nonetheless, the surge forward is being blocked by the failure to resolve all the problems associated with foreclosures and the sluggish pace of writing new rules for mortgage lending.

New Jersey and New York: The Trans-Hudson Exchange

Anyone who has ever been stuck in a traffic jam on the George Washington Bridge, or who notices that the helmets on those home football teams in the Meadowlands Stadium have "Ys" where the "Js" should be, can appreciate that New Jersey and New York are closely connected. The linkages between the two states go much deeper than common rooting interests for baseball and football teams.

According to U.S. Census figures, in 2000 more than 350,000 New Jerseyans worked in New York State, while over 125,000 New Yorkers worked in New Jersey. Most likely, these numbers have not changed radically since then. The number of Garden State residents who work in New York — greater than the population of Newark — is larger than employment in virtually all New Jersey counties*. The reverse commute flow is considerably smaller, but in absolute terms it is still huge.**

The Port Authority of New York and New Jersey reports that in 2009 eastbound toll traffic on its six crossings averaged more than 400,000 vehicles a day. Train and ferry passengers and people travelling overland across New Jersey's northern land border with New York, swell the count of border crossings even more. All in all, the number of people who cross to and from New Jersey to New York on a typical work day is very much higher than the numbers who commute between the two states and could well be as high as one million. It is almost surely the largest volume of state-to-state travel in the nation (It could be that daily movement to and from the District of Columbia from *both* Virginia and Maryland is comparable to or larger than the New Jersey-New York flow).

For many issues, such as the balance between the demand for government services and the flow of tax revenues, the key part of the interchange between New Jersey and New York is the relative numbers commuting from home in one state to work in the other. The main point is that many more New Jerseyans commute to New York than vice-versa. The divergence is even more striking for incomes. New Jersey taxpayers who work in, or own a business in New York reported aggregate Empire State salary and business income of more than $50 billion in 2009. That's more than all 310 million Americans spend each year on movie admissions and all forms of live entertainment, including sports. New Yorkers, meanwhile, reported earning about $10 billion in New Jersey on their nonresident tax returns.

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The income divergence is reflected in taxes. New Jersey residents claimed $1.9 billion in credits in 2009 against our state income tax for taxes paid to New York State (the New York State income tax) and New York City (the city's unincorporated business tax). This is money that otherwise would have been paid to the New Jersey State Treasury and used, as our state constitution requires, for property tax relief. $1.9 billion is equal to more than one-fifth of our income tax revenue for that year, or close to one-tenth of all the residential property tax paid in New Jersey.

Of course, New Jersey income taxes paid by New Yorkers offset some of this revenue loss, but that amount totaled only about $500 million. Incidentally, New York taxes paid by New Jersey residents are much larger than the amount that can be credited against our income tax. We estimate total taxes paid by New Jersey residents to New York State and City are well above $3 billion a year.

Most government services are generally connnected to a person's residence — most notably, the public education provided to the household's children, but also police and fire protection, water and sewer service, parks, libraries and other recreational facilities. Services connected to a place of work are much more limited. Thus, at least as measured by the size of incremental service demands compared to incremental tax revenues, New York government units gain from current cross-border commuting patterns, while New Jersey governments lose. To sustain existing government services to residents, New Jersey tax rates (including, most notably, those on residential property) are, in general, higher, and New York tax rates are lower, than they would be if commuter incomes were taxed by place of residence.

This unfavorable balance of taxes is not an argument that cross-state commuting is "bad" for New Jersey. It is utterly true that the existence of job opportunities in New York and New Jersey for all residents of the region allows for higher levels of income and wealth in both states and spills over into increased activity and income for localized businesses. To give perhaps the most banal but still illustrative example, consider the dry cleaner by the train station that gets its business from commuters.

However, the realities of the cross-state flow of taxes puts constraints on New Jersey revenues that are not obvious from a simple look at the wealth and income of our residents. Put simply, a good portion of that income is not part of New Jersey's tax base — it is taxed by New York.

New Jersey and New York are inextricably linked in countless ways and personal and family connections are profound. For example, the early 1990s saw Jim Florio, a Brooklyn-born governor of New Jersey serving alongside David Dinkins, a Trenton-born mayor of New York City. As in many families, the relationship between the elder sibling — New Jersey, as determined by date of ratification of the Constitution — and the younger one is sometimes uneven but always treasured.

*Bergen is our only county that has a substantially higher number of jobs.

**The cross-Delaware work exchange between New Jersey and Pennsylvania is also substantial, involving somewhat more than 100,000 individuals traveling in each direction.

New Jersey Business Pulse Survey

Views about the State and Global Economies Hold Steady

New Jersey businesses continued to express modest optimism about the state and world economies in May. These findings come from a survey administered by the New Jersey Department of the Treasury.

The New Jersey Business Pulse Survey has been created to look beyond conventional economic data and gather views in real time directly from a diverse group of businesses in the state. Responses to this latest survey were given by 41 firms spanning a wide spectrum of industries and sizes. The survey includes 14 questions about current and prospective conditions and allows respondents to give their views on other topics of their choice. Detailed results may be found at http://www.state.nj.us/treasury/pdf/May-Business-Pulse-Survey-Results.xls .

General Conditions: Steady as you go, but better times ahead.

The firms surveyed found general conditions inside and outside New Jersey to have changed little over the past month. Looking toward next year, there continued to be a more upbeat tone, with only one-fifth seeing national or world conditions deteriorating to any extent, and less than one-fourth seeing deterioration in the state. Most of the firms see their Garden State revenues growing over the next year. However, of those firms with operations outside New Jersey, only one-fourth expect out-of-state sales to increase. Only one respondent expected them to fall.

Hiring and Capital Spending: Stability is the Word

Firms are cautious about plans to expand their workforces and plant and equipment, both in New Jersey and elsewhere. Less than one-fourth of the panel anticipates making any significant changes in their workforce, either inside or outside New Jersey. Similarly, more than one-half of the firms anticipate no change in New Jersey capital spending over the next year, and more than three-fourths of those that responded expect to make no significant changes in their firm's out-of-state spending. While these replies do not suggest that the economic expansion is likely to gain a lot of traction in the near future, neither do they suggest that a major retrenchment in the works. Our survey continues to find that firms have few problems finding qualified employees either inside or outside the state.

Input Costs Rise but Product Prices are Stable

Less than one-third of the respondents indicate that they have recently increased any of the prices they charge their customers. In contrast, more than three-fourths indicate that some of the prices they pay suppliers have recently risen. More than one-fourth strongly agree that their input costs have gone up. The upshot is that firms have generally not passed increases input costs on to customers at least not to any widespread extent.

Conclusion: Not Much Change in the Results, Outside of Prices

In general, responses to May's survey did not greatly differ from April's, in the questions covering current and future conditions as well as company plans. There was some slight shrinkage in the percentages of more optimistic responses, but no marked increase in pessimistic ones. This suggests the "soft patch" may be little more than that—firms are less upbeat, but not more gloomy. One area where there seemed to be some change is that firms reported more widespread indications of increased input costs, but even less indication that they are raising their sales prices.

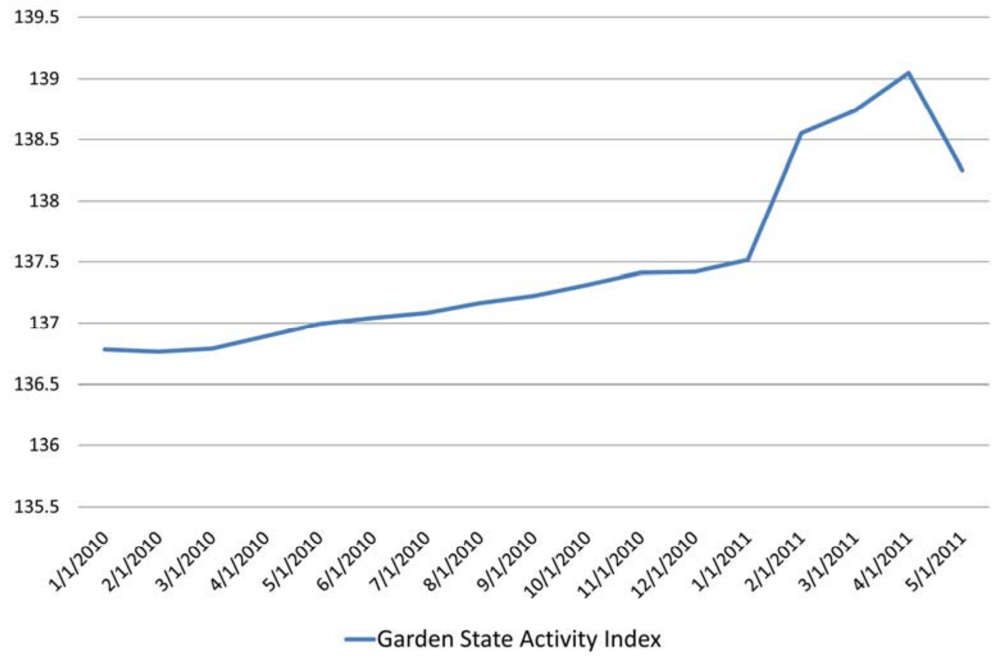
Future of the Survey

We expect to conduct this survey monthly. If your New Jersey firm is interested in participating, please contact Mary Filipowicz at 609-633-6781.

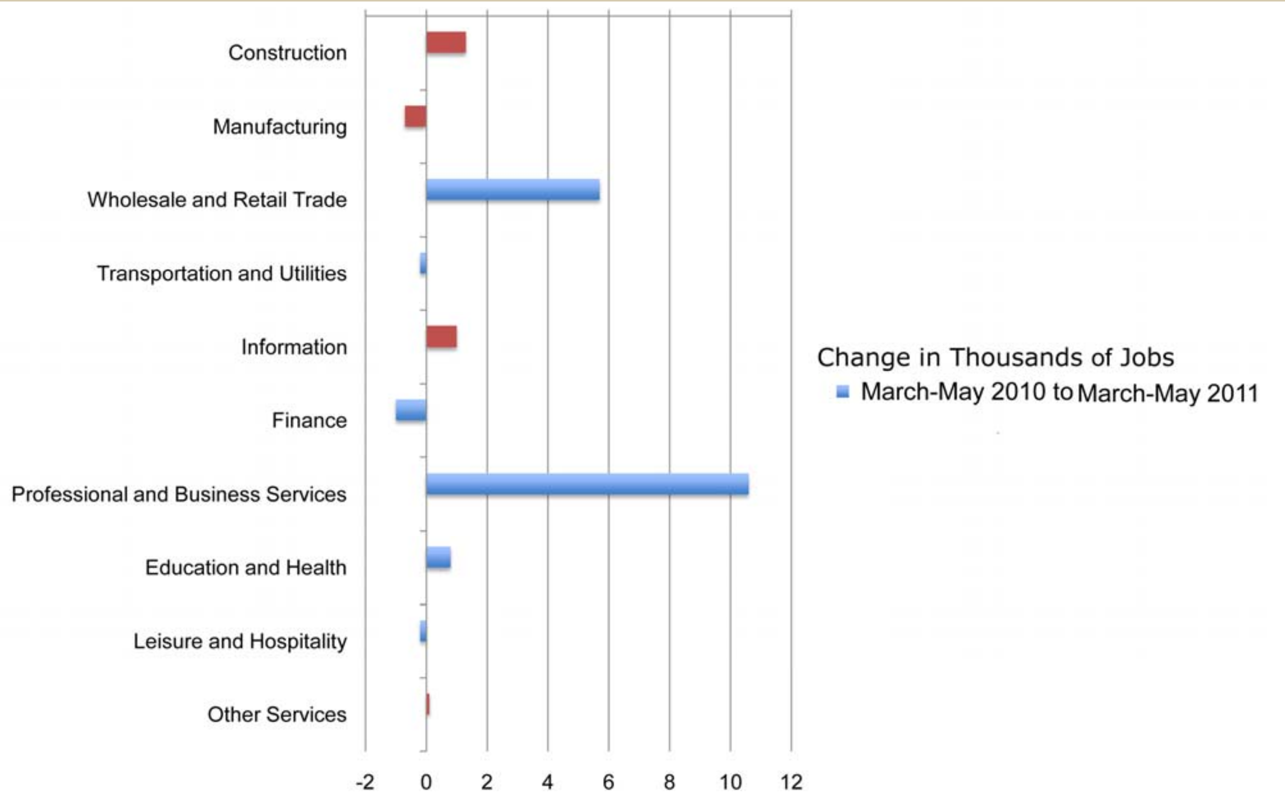
Charles Steindel

Garden State Activity Index

The *Garden State Activity Index* is a measure designed to provide a broad indicator of monthly economic activity in New Jersey. The index is an average of three other measures: the coincident economic indexes for the state produced by the Federal Reserve Banks of New York and Philadelphia and a measure derived from the Philadelphia Bank's South Jersey Business Survey. The latest reading shows that the index edged up slightly in May to a level about .9 percent higher than its May 2010 value.

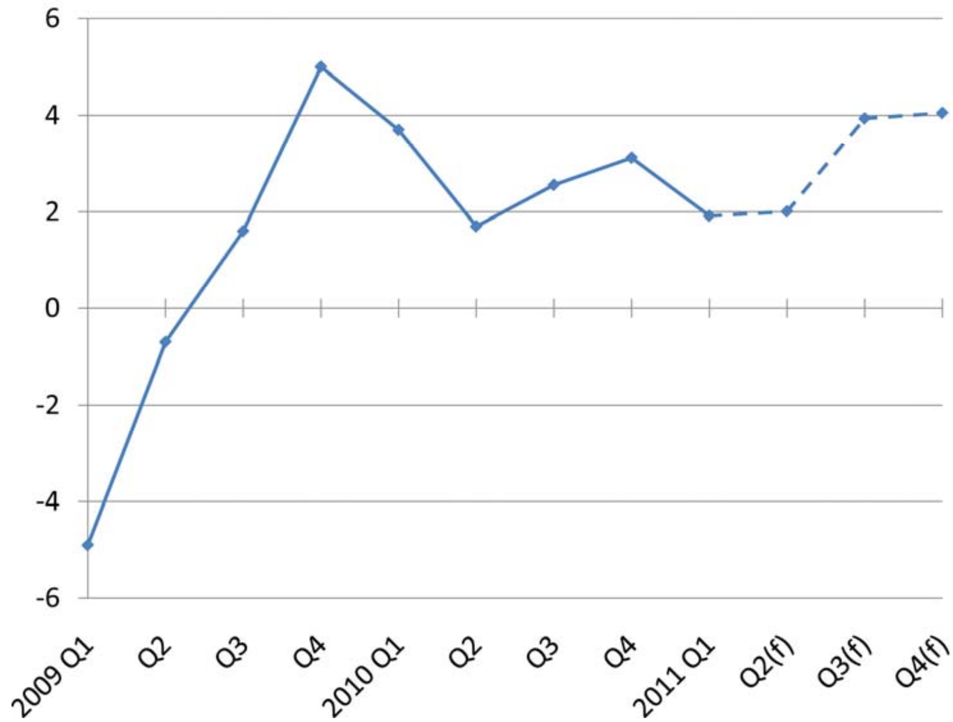


Private Industry Employment Trends



Data source: New Jersey Department of Labor

Real U.S. GDP Growth *(Percent change, compound annual rate)*



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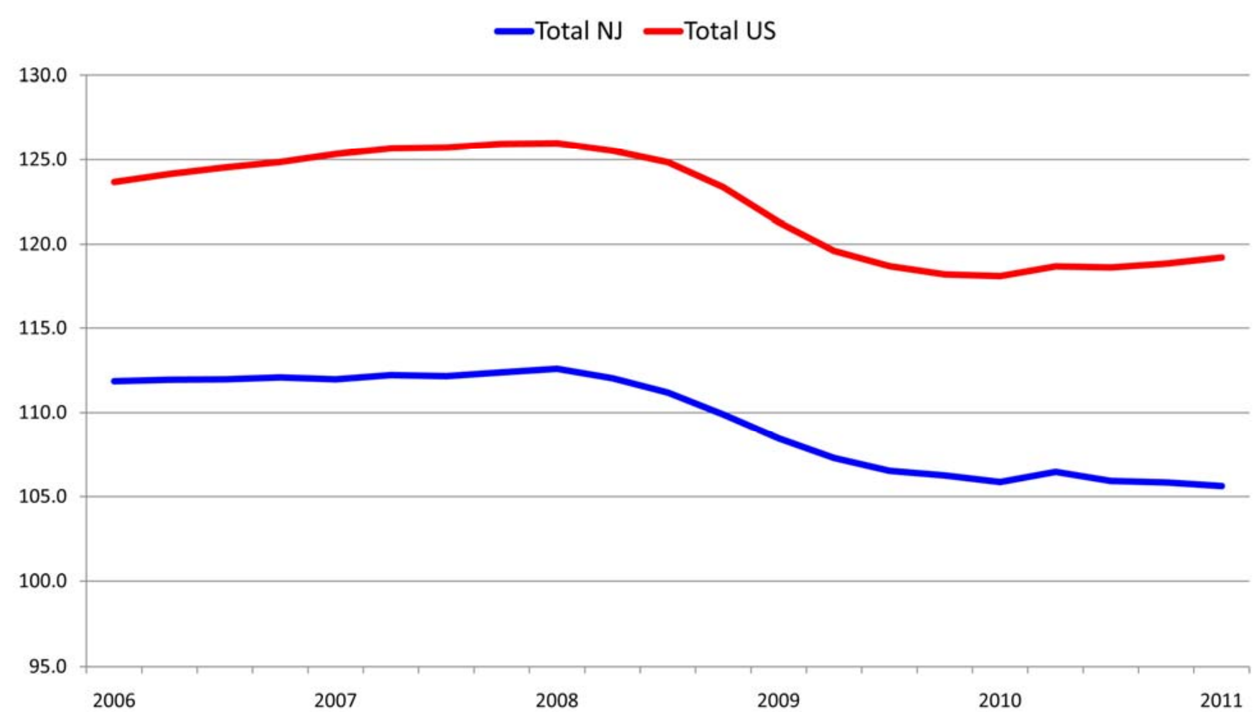
Data source: U.S. Bureau of Economic Analysis

State & National Job Trends

Total Employment *(Relative Employment 1990=100)*

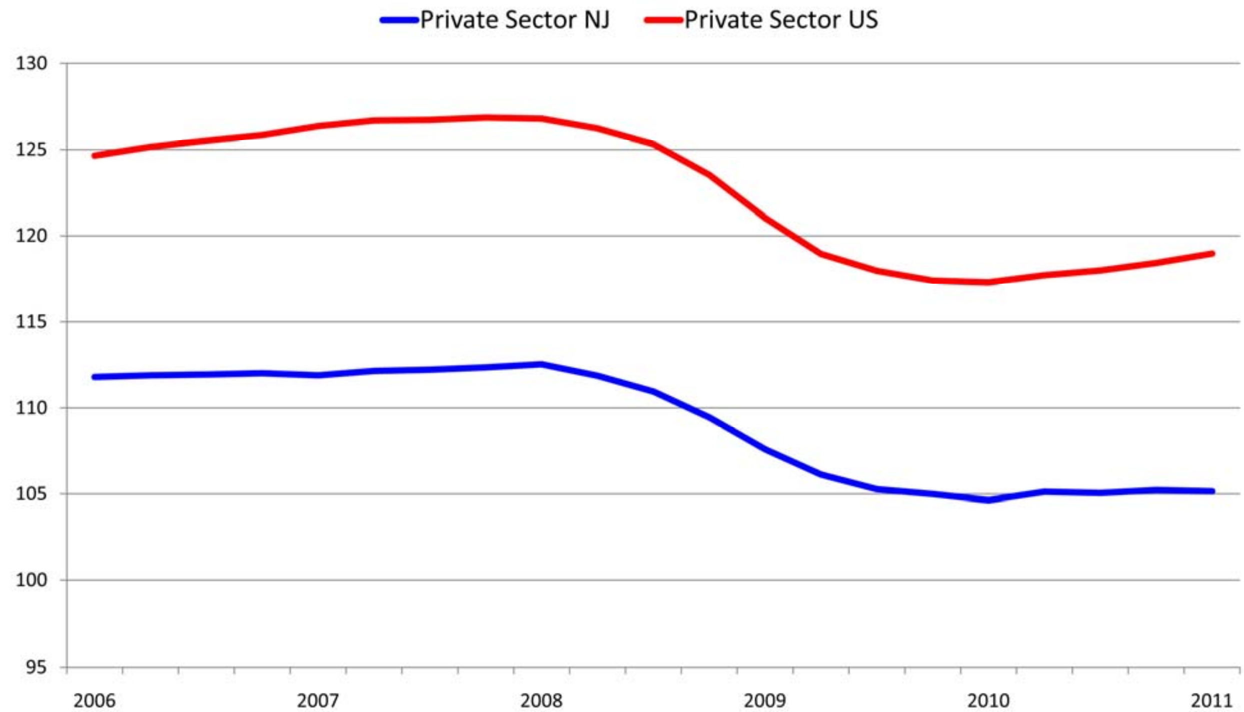
This chart compares the number of employed workers to the base year of 1990. The number 100 represents employment in 1990.



State & National Job Trends

Private Sector Jobs *(Relative Employment 1990=100)*

This chart compares the number of employed workers to the base year of 1990. The number 100 represents employment in 1990.



Data source: U.S. Bureau of Labor Statistics, New Jersey Department of Labor

Explanatory note: These charts track trends in total and private sector employment in New Jersey and compare them with those of the nation as whole measured against a 1990 baseline.