THE ASSEMBLY
STATE OF NEW YORK
ALBANY

February 23, 2010

Dear Colleagues:

I am providing you with the New York State Assembly Ways and Means Committee's Economic Report for 2010. This report continues our commitment to providing clear and accurate information to the public by offering complete and detailed assessments of the national and State economies.

The Ways and Means Committee staff's assessments and projections presented in this report are reviewed by an independent panel of economists, including professionals from major financial corporations and universities, as well as respected private forecasters.

Assembly Speaker Sheldon Silver and I would like to express our appreciation to the members of this Board of Economic Advisors. Their dedication and expert judgment continue to be invaluable in helping to refine and improve our forecasts. While they have served to make the work of our staff the best in the State, they are not responsible for the numbers or views expressed in this document.

I wish to also acknowledge the dedicated and talented staff of the Assembly Ways and Means Committee and the many hours of work that went into producing this report. They play a vital role in our State's budget process.

As we continue our efforts toward enacting a timely budget that is fair and equitable for all New Yorkers during this difficult financial period, I look forward to working with each of you.

Sincerely,

Herman D. Farrell, Jr.
Chairman

NEW YORK STATE

ECONOMIC REPORT

February 2010

Sheldon Silver
Speaker
New York State Assembly

Herman D. Farrell, Jr.
Chairman
Assembly Ways and Means Committee

Prepared by the
Assembly Ways and Means Committee Staff

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EXECUTIVE SUMMARY

United States

- The NYS Assembly Ways and Means Committee staff forecast for **overall national economic growth** in 2010 is 2.9 percent. The staff forecast is lower than the Division of the Budget by 0.2 percentage point, Blue Chip Consensus and IHS Global Insight by 0.1 percentage point, and Macroeconomic Advisers by 0.8 percentage point. The staff forecast is higher than Moody's Economy.com by 0.1 percentage point.

U.S. Real GDP Forecast Comparison
(Percent Change)

	Actual 2008	Estimate 2009	Forecast 2010	Forecast 2011
Ways and Means	0.4	(2.4)	2.9	2.8
Division of the Budget	0.4	(2.4)	3.1	3.4
Blue Chip Consensus	0.4	(2.4)	3.0	3.1
Moody's Economy.com	0.4	(2.4)	2.8	3.6
Macroeconomic Advisers	0.4	(2.4)	3.7	4.2
IHS Global Insight	0.4	(2.4)	3.0	2.8

Sources: NYS Assembly Ways and Means Committee staff; Blue Chip Economic Indicators, February 2010; Division of the Budget, Executive Budget 2010-11, February 9, 2010; Moody's Economy.com, February 2010; IHS Global Insight, February 2010; Macroeconomic Advisers LLC, February 2010.

- In the midst of the 2008-09 financial market turmoil and global economic crisis, the **U.S. economy** underwent one of the sharpest declines since the 1930s. National home values declined 31.8 percent from the 2006 peak level to May 2009 and cumulative job losses reached 8.4 million in January 2010, twenty-five months after the downturn began in December 2007. Gross Domestic Product adjusted for inflation, or real GDP, declined 3.7 percent from the fourth quarter of 2007 to the second quarter of 2009. Consumer spending, which accounts for roughly two-thirds of real GDP, declined 1.9 percent during the same period. It was the sharpest such decline since 1947.

- After declining an estimated 2.4 percent in 2009, **U.S. real GDP** is forecast to increase 2.9 percent in 2010. This is well below the post-World War II average performance: on average, the U.S. economy grew 4.9 percent during the first year after all of the nine post-World War II recessions. The national economy is forecast to grow another 2.8 percent in 2011.

- **Credit conditions** still represent a concern for consumers and businesses, and play a large role in the ability of the economy to recover. What began as general concern over mortgage-backed securities spread further than anticipated, leading to a wide-spread credit crunch. Overall, credit conditions were tight throughout the recession and continue to be strained.

- U.S. **personal consumption** spending is estimated to have declined 0.6 percent in 2009 after falling 0.2 percent in 2008. This was the first back-to-back yearly falloff in consumer spending since 1932. Household wealth rebuilding will encourage consumer spending going forward. However, relatively weak growth in wages and salaries, depressed home prices, and a fragile labor market will dampen consumer spending. Thus, consumers are unlikely to resume pre-crisis spending patterns. Consumer spending grew at an annual average rate of 3.3 percent from 1992 to 2007. U.S. personal consumption spending is forecast to grow only 2.0 percent in 2010 and 2.5 percent in 2011.

- Total **U.S. business spending** declined an estimated 23.3 percent in 2009 due to weakness across all sectors of business investment activity. Spending on nonresidential structures is expected to continue to decline until early 2011 due to ongoing problems in the commercial real estate sector. However, as the housing market improves and investment in inventories, and equipment and software returns, overall business spending is forecast to experience strong growth throughout the forecast period.

- Since its peak in the second quarter of 2006, **national home prices** have declined by more than 30 percent, with the highest depreciation rate in the areas that experienced the fastest growth during the boom period. Declining home prices led to a significant drop in households' real estate assets, which fell 27.9 percent from 2006 to the third quarter of 2009. Housing starts are still at historic low levels but have increased from a monthly average of 534,000 in the first six months of 2009 to 570,000 in the second half of 2009.

- **Federal government spending** growth is estimated to have slowed to 5.2 percent in 2009 compared to 7.7 percent in 2008, due to slower growth in public investment spending and significantly lower non-compensation expenditures, Federal government spending growth will slow further to 4.2 percent in 2010 as the federal government reins in military compensation, and defense investment spending decelerates. By 2011, federal government spending is forecast to fall 0.3 percent as the government restrains spending on compensation for defense and nondefense personnel as well as public investments.

- State and local government spending tends to lag overall economic growth. As a result, as tax collections remain depressed due to a fragile labor market, weak consumer spending, and falling property taxes, **state and local government spending** fell an estimated 0.1 percent in 2009, and is forecast to grow only 0.2 percent in 2010 even with a boost from the American Recovery and Reinvestment Act of 2009 (ARRA). As the fiscal stimulus abates, state and local government spending is forecast to decline 0.3 percent in 2011.

- U.S. **exports** are estimated to have declined 9.9 percent in 2009. Global economic recovery and a weak U.S. dollar will help U.S. exports to grow 9.0 percent in 2010 and 6.9 percent in 2011.

- Faced with the deepest recession in decades, U.S. **imports** declined for the second consecutive year in 2009, falling 14.2 percent. As the U.S. economy recovers, imports are forecast to grow 8.4 percent in 2010 and another 7.5 percent in 2011.

- Between December 2007 and January 2010, the U.S. economy lost 8.4 million payroll jobs. **National employment** declined by 0.6 percent in 2008 and 4.3 percent in 2009, much more than in previous recessions. For comparison, national employment declined 1.1 percent in 2002. Employment is forecast to gain gradually throughout 2010 but will remain below the 2009 level on an annual average basis.

- **Personal income** is estimated to have fallen 1.4 percent in 2009, the first decline since 1949, primarily from a decline in wages and salaries. Growth in personal income is expected to be 3.7 percent in 2010 as the labor market continues to be strained by a slow economic recovery. Personal income is anticipated to grow a modest 4.0 percent in 2011 due to an improving labor market with higher wage and salary expectations, and increases from dividend and interest income.

- **Wages and salaries** grew 2.1 percent year-over-year in 2008, after growing 5.6 percent in 2007. In 2009, wages and salaries declined an estimated 3.3 percent as hourly wages slowed and average hours worked fell. This was the first yearly decline in wages and salaries since 1954, and the largest since 1946. Wages and salaries are forecast to grow a mere 3.2 percent in 2010, as employment, hourly wages, and hours worked improve at a measured pace. In 2011, wages and salaries are expected to increase another 3.7 percent due to gradual improvements of the labor market and other economic conditions.

- Consumer **prices** grew 3.8 percent in 2008 as a direct result of pricing pressures—namely from record high energy prices. As energy prices in 2009 were considerably lower than in 2008 and as overall economic growth fell sharply in 2009, consumer prices are estimated to have declined 0.3 percent year-over-year in 2009, the first decline since 1955. Consumer prices are expected to increase 2.3 percent in 2010 as the economy continues to recover and energy prices remain above the 2009 annual average level. In 2011, prices are forecast to increase 2.1 percent.

- As output growth slowed and production costs rose sharply, **corporate profits** declined 4.1 percent in 2007, ending five consecutive years of double-digit growth. With further weakening in the economy throughout 2008 and 2009, corporate profits continued to suffer, falling 11.8 percent and an estimated 3.7 percent, respectively. With economic growth resuming in the second half of 2009 and expected to continue through the forecast period, corporate profits are forecast to rebound by 10.3 percent in 2010 and 10.4 percent in 2011.

- The **federal funds rate**, which averaged 0.16 percent in 2009, is predicted to average 0.24 percent in 2010 and rise further to 1.7 percent in 2011. Similarly, the **three-month Treasury bill rate** averaged 0.15 percent in 2009, and is forecast to average 0.27 percent in 2010 and 1.8 percent in 2011.

- The **10-year Treasury note yield** averaged 3.3 percent in 2009. As the world economy is expected to rebound in 2010, investors may shift their investment from Treasuries to stocks and corporate bonds to seek higher returns. The 10-year Treasury rate is forecast to average 3.6 percent in 2010 and rise to 4.4 percent in 2011.

- The **S&P 500 stock price index**, or S&P 500, gained over 50 percent since March 2009 but is still more than 30 percent below its 2007 peak. Overall economic activity and corporate profitability remained weak during 2009; the annual average level of the S&P 500 stock price index was lower than the 2008 level. On an annual basis, the S&P 500 declined 22.5 percent in 2009. With movement towards global economic recovery coupled with the most enticing equity valuation levels in decades, the S&P 500 is forecast to increase 21.1 percent in 2010 and continue to grow further by 7.9 percent in 2011.

- Several **risks** to the economic outlook of the nation remain. The housing market appears to be stabilizing but significant downside risks remain. Problems in commercial real estate are expected to be a drag on the economy. Personal consumption spending remains restrained in the face of high unemployment and stagnant wages and salaries, and the economy continues to be hampered by credit and liquidity issues. Energy prices also present significant concern to the nation as a spike could curtail or derail economic recovery.

New York

- The NYS Assembly Ways and Means Committee staff's forecast for 2010 nonfarm payroll employment growth in **New York State** is negative 0.4 percent. The staff forecast is 0.2 percentage point higher than the Division of the Budget and 0.4 percentage point above Moody's Economy.com. The Committee staff's forecast for 2010 wage growth in **New York State** is 5.2 percent. The staff forecast is 1.7 percentage points above the Division of the Budget and 2.5 percentage points above Moody's Economy.com.

New York State Forecast Comparison
(Percent Change)

	Actual 2008	Estimate 2009	Forecast 2010	Forecast 2011
Employment				
Ways and Means	0.5	(2.8)	(0.4)	0.9
Division of the Budget	0.6	(2.9)	(0.6)	0.8
Moody's Economy.com	0.7	(2.1)	(0.8)	1.1
Wages (Calendar Year)				
Ways and Means	2.0	(7.4)	5.2	0.5
Division of the Budget	2.0	(7.0)	3.5	3.1
Moody's Economy.com	2.2	(5.4)	2.7	2.2
Wages (Fiscal Year)	**2008-09**	**2009-10**	**2010-11**	**2011-12**
Ways and Means	(3.1)	(2.2)	4.1	5.1
Division of the Budget	(3.1)	(2.5)	3.9	4.9

Note: Calendar year wage numbers are affected by a shift of wages from the first quarter of 2011 to the fourth quarter of 2010, as a result of the expiration of federal tax cuts. Differences in the amounts assumed for the shift may account for some of the difference between calendar year numbers. The fiscal year wage numbers are little affected by this shift.

Sources: NYS Assembly Ways and Means Committee staff; Division of the Budget, Executive Budget 2010-11, February 9, 2010; Moody's Economy.com, January 2010.

- In 2008, total **nonfarm payroll employment** in New York State grew 0.5 percent, significantly lower than 2007, while national employment declined by 0.6 percent. As the overall economy weakened further in 2009, nonfarm payroll employment in the State is estimated to have declined by 2.8 percent, the worst decline in more than a decade. As State employment lags the overall recovery of the economy, nonfarm payroll employment in New York State is forecast to fall another 0.4 percent year-over-year in 2010, before growing 0.9 percent in 2011.

- National **job losses** during the recent recession have been spread throughout many sectors. However, New York fared better than many other states in terms of job loss in the hardest hit sectors such as construction and manufacturing. The nation lost 8.4 million jobs between December 2007 and December 2009. For New York State, the comparable job loss is 231,000.

- After six years of growth, most of it vigorous, **wages** in New York State fell an estimated 7.4 percent in 2009. Wages are expected to grow in 2010 and 2011; however, the growth rates will be much lower than in 2006 and 2007, with growth of 5.2 percent in 2010 and 0.5 percent in 2011.

- The lower **wage growth** in 2011 is a result of firms shifting wage payments, particularly bonuses, from the beginning of 2011 to the end of 2010 in anticipation of the expiration of certain federal tax cuts. A similar shift took place in 1992 and 1993 as the federal tax rate was expected to increase in 1993. Without the shift, the growth rates would be more evenly spread. Growth in 2010 would be 2.9 percent and growth in 2011 would be 4.8 percent. On a state fiscal year basis, the growth rates are little affected by the shift.

- The NYS Assembly Ways and Means Committee staff estimates that **New York State total variable compensation**, which was $73.4 billion in 2007, fell 4.6 percent to $70.1 billion in 2008 as financial services companies began to cut back. Total variable compensation is estimated to have declined by 31.6 percent or $22.1 billion in 2009. This is the largest decline since estimates of the series began in 1975.

- On a fiscal year basis, **New York State securities industry variable compensation** fell 46.8 percent in State Fiscal Year (SFY) 2008-09 to $19.1 billion, while total variable compensation fell 32.2 percent. Securities industry variable compensation is expected to rise by 7.6 percent to $20.6 billion in SFY 2009-10, before rising further to $25.3 billion in SFY 2010-11.

- Central to the overall wage and variable compensation outlook for New York State is the performance of Wall Street. The average wage in the **finance and insurance sector** is over three times that of the overall average wage in the State. This sector accounted for 22.3 percent of total New York State wages in 2007, the highest share since the series started in 1975, whereas employment in the industry was only 6.4 percent of total nonfarm payroll employment in the State. In 2009, the share of total finance and insurance employment is estimated to have fallen to 6.0 percent while the wage share fell to 18.0 percent.

- The **New York State housing market** performed better than the nation in both the housing boom and during the correction. As of September 2009, New York State had the second lowest rate of mortgage holders in negative equity at 6.2 percent. However, the State has a higher percentage of subprime loans with adjustable rate mortgages that are scheduled to have interest rates reset in the next twelve months than the nation.

- The overall decline in economic growth, coupled with the deterioration in the housing market and the significant falloff in corporate equity prices, led to an estimated 54.6 percent decline in taxable **capital gains** in 2008. Taxable capital gains is estimated to have fallen 27.2 percent in 2009 to $38.1 billion as home prices remained depressed and investors faced stock prices that were lower than in prior years. In 2010, taxable capital gains are forecast to increase 45.0 percent to $55.2 billion, partly reflecting a continued recovery in equity markets and investors' response to the anticipated rise in capital gains taxes in 2011.

- The New York State economy is quite susceptible to changes in the securities industry, especially the variability in bonuses from year to year, as the bonuses paid by the securities industry are a major driver of State variable wages. The economic crisis that began in December 2007 has resulted in calls for reforms to Wall Street's pay structure that are meant to discourage the high-risk/high-gains culture leading up to the financial crisis. Drastic cuts in Wall Street compensation or movement towards non-cash-based bonuses will have significant implications for the State, which is particularly dependent on Wall Street's compensation practices for tax revenues. However, a faster turnaround than expected in Wall Street activities offers some upside potential for the forecast.

UNITED STATES FORECAST

In the midst of the 2008-09 financial market turmoil and global economic crisis the U.S. economy underwent one of the sharpest declines since the 1930s. National home values declined 31.8 percent from the 2006 peak level to May 2009. Cumulative job losses reached 8.4 million in January 2010, twenty-five months after the downturn began in December 2007 (see Figure 1). Gross Domestic Product adjusted for inflation, or real GDP, declined 3.7 percent from the fourth quarter of 2007 to the second quarter of 2009. Consumer spending, which accounts for more than two-thirds of real GDP, declined an estimated 0.6 percent in 2009 after falling 0.2 percent in 2008. It was the first back-to-back yearly decline since 1932.

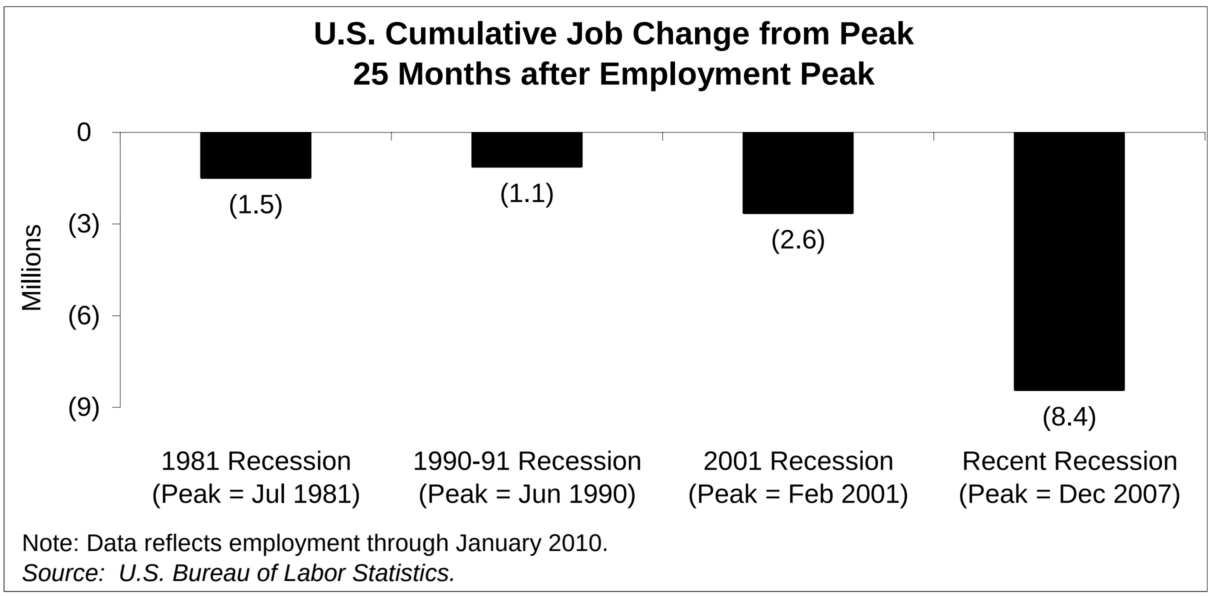
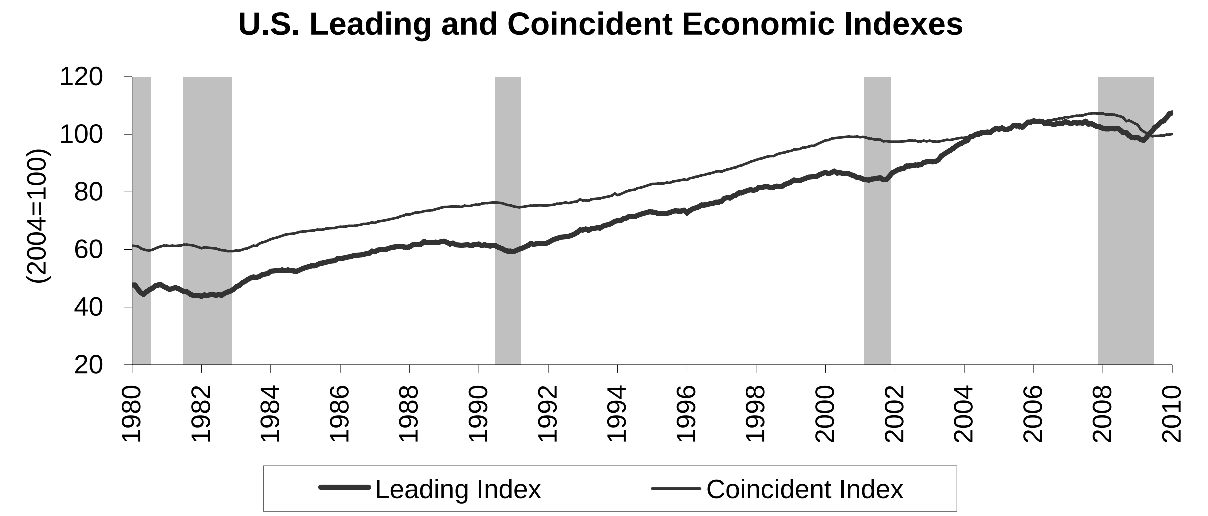


Figure 1

Although weaknesses remain in many parts of the economy, there are signs of stabilization and recovery under way. U.S. real GDP increased by an annualized 2.2 percent in the third quarter of 2009 following the fourth consecutive quarterly decline. It increased further by an estimated 6.1 percent in the fourth quarter. Employment losses declined sharply from an average of 753,000 per month in the first quarter of 2009 to 103,000 per month in the fourth quarter. The Chicago Fed National Activity Index (CFNAI), a coincident indicator of the business cycle as a weighted average of 85 monthly indicators of national economic activity, improved in September 2009 on a three-month moving average basis to a level greater than negative 0.7 for the first time since January 2008.[1] The Conference Board's coincident economic indicator index has been on an upward trend since June 2009.[2] The leading indicator index has gained for ten months in a row, also pointing to further recovery in the near future (see Figure 2).



Note: Data is monthly through January 2010. The shaded areas represent recessions.
Source: The Conference Board, Inc.

Figure 2

The Federal Reserve's aggressive easing and direct lending programs have helped improve financial market conditions in general. With uncertainties being lifted and investor confidence returning, the S&P 500 stock price index has gained more than 300 points since early March 2009 after falling almost 900 points or 56.8 percent from the 2007 peak. The risk premium required on lower quality corporate bonds has been steadily falling, as risk and uncertainty perceived by investors have receded (see Figure 3).

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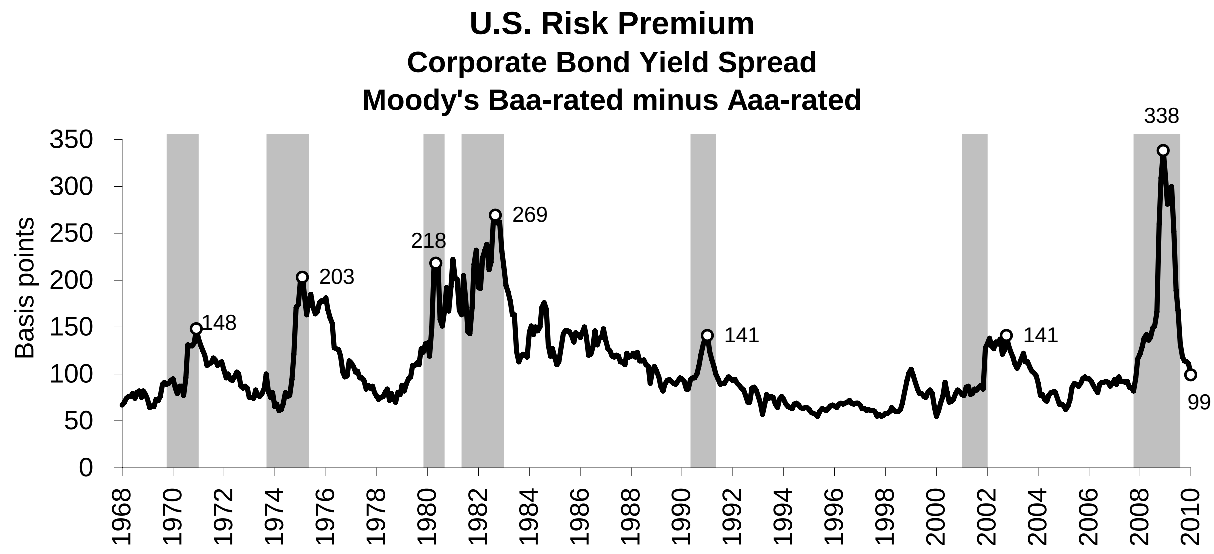
[1] In the previous recessions, the first month when the three-month average value of CFNAI was above negative 0.7 coincided closely with the end of each recession as eventually determined by the National Bureau of Economic Research. Although the index retreated below the threshold in October due to weakness in production and housing-related indicators, the overall trend during recent months still remains positive. For more details, see "Chicago Fed National Activity Index News Release," Federal Reserve Bank of Chicago, November 23, 2009, http://www.chicagofed.org/economic_research_and_data/files/cfnai_november2009.pdf.

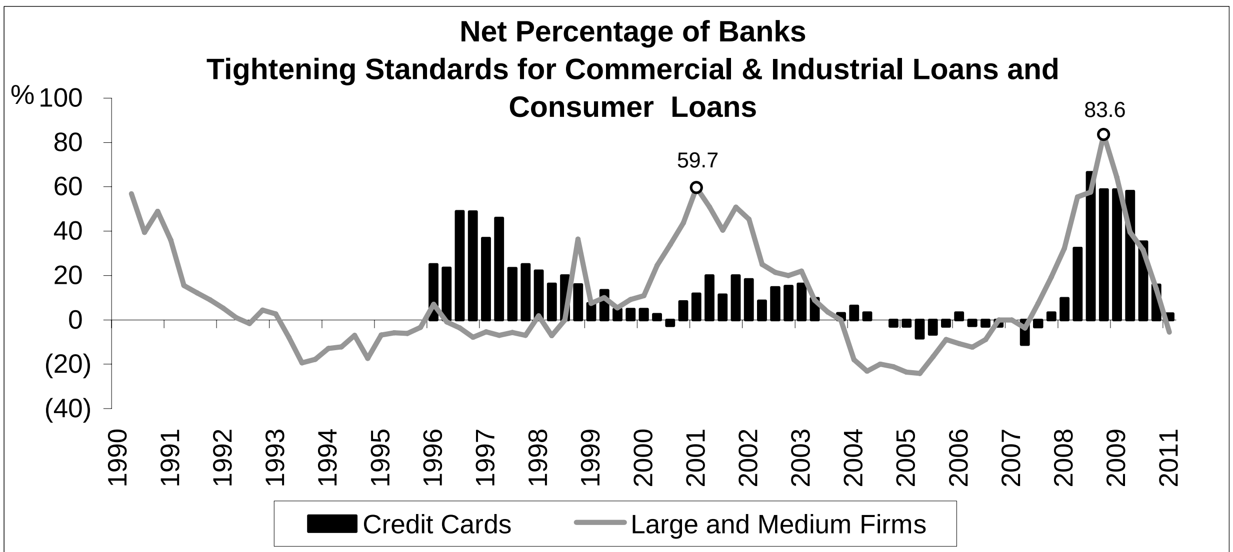
[2] Based on these two coincident indicators and other information, the NYS Assembly Ways and Means Committee staff projects that the national recession that began in December 2007 probably ended some time in the summer of 2009.



Note: Data is monthly through January 2010. The shaded areas represent recessions.
Source: Federal Reserve.

Figure 3

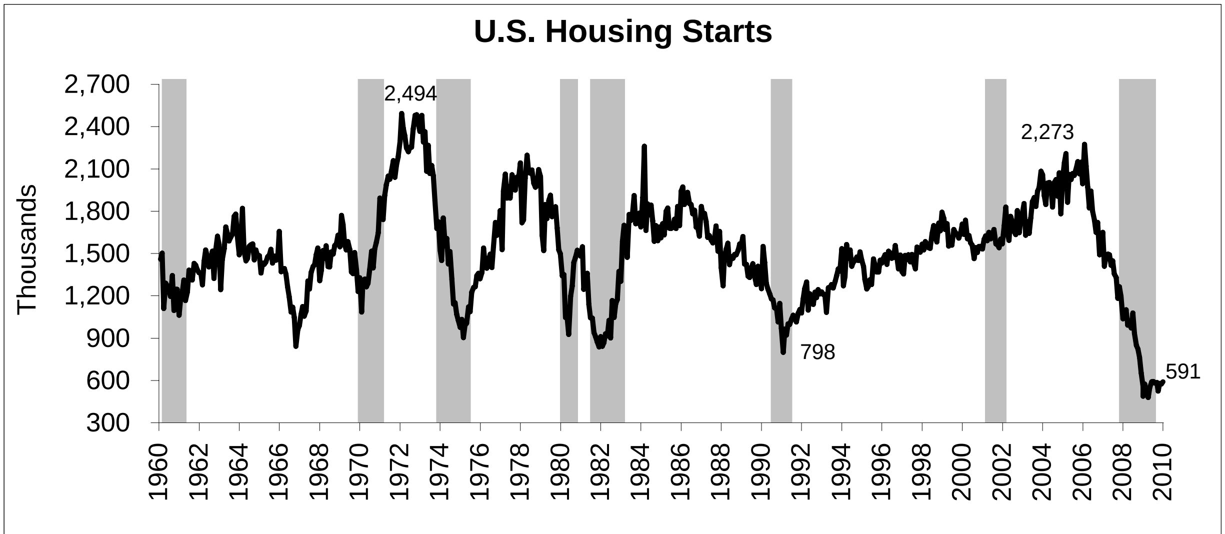
The Treasury bond market also has regained stability after a shaky performance in the early summer of 2009 and asset-backed commercial paper issuance has recently started increasing. Bank lending practices also show improvement: the number of banks tightening lending standards has declined and willingness to lend has improved (see Figure 4).



Note: Data is quarterly through 2010:Q1. Data for each quarter corresponds to information collected in the previous quarter. Bank data taken from a survey of approximately sixty large domestic banks and twenty-four U.S. branches and agencies of foreign banks. The credit card series starts in 1996:Q1.
Source: Board of Governors of the Federal Reserve System: Senior Loan Officer Opinion Survey on Bank Lending Practices, January 2010.

Figure 4

The housing sector also shows signs of some improvement. Home sales have been steadily increasing and inventories of unsold homes have continued to decline in recent months. The federal housing tax credit program (up to $8,000 for first-time homebuyers and up to $6,500 for existing home owners) appears to have helped stimulate home sales; both new and existing home sales have picked up in recent months.[3] Housing starts are still at historic low levels but have increased from a monthly average of 534,000 in the first six months of 2009 to 570,000 in the second half of 2009 (see Figure 5). More importantly, in some parts of the country home prices have been stabilizing after the national index fell over 30 percent from the 2006 peak level.



Note: Data is monthly through January 2010. The shaded areas represent recessions.
Source: U.S. Census Bureau.

Figure 5

Despite those positive signals and prospects of recovery, the upcoming recovery may not be as strong as earlier ones. Overall monthly employment losses have shrunk sharply in recent months but job growth in the private sector will remain sluggish for some time even after overall economic growth returns. Even with the recent gains in the financial market and the recent signs of stabilization in the housing market, it will take a long while for home and equity prices to return to their peak levels and for households to recuperate from wealth losses. As of the third quarter of 2009, 22.6 percent of U.S. home mortgage

[3] The federal housing tax credit program has recently been extended to April 2010. The program also has been expanded to include existing homeowners who have lived in their current home for at least five years.

holders owed more on their mortgages than their home was worth.[4] Thus, it is unlikely that consumers will resume their pre-crisis spending routines any time soon. Some fiscal stimulus programs have been particularly popular and effective in inducing consumers back to shopping, but the effects will likely be limited. For example, the Consumer Assistance to Recycle and Save (CARS) program, commonly called Cash for Clunkers, helped boost vehicle sales in the summer of 2009; and it appears that most of the gain in vehicle sales was attributed to the program. With unemployment expected to stay high, demand for office and retail space should remain weak, weighing on commercial construction activity.

Against this backdrop, after declining an estimated 2.4 percent in 2009 U.S. real GDP is forecast to increase 2.9 percent in 2010 (see Table 1). This is well below the post-

Table 1

U.S. Economic Outlook (Percent Change)	Actual 2008	Estimate 2009	Forecast 2010	Forecast 2011
Real GDP	0.4	(2.4)	2.9	2.8
Consumption	(0.2)	(0.6)	2.0	2.5
Investment	(7.3)	(23.3)	11.2	11.0
Exports	5.4	(9.9)	9.0	6.9
Imports	(3.2)	(14.2)	8.4	7.5
Government	3.1	1.9	1.7	(0.3)
Federal	7.7	5.2	4.2	(0.3)
State and Local	0.5	(0.1)	0.2	(0.3)
Personal Income	2.9	(1.4)	3.7	4.0
Wages & Salaries	2.1	(3.3)	3.2	3.7
Corporate Profits	(11.8)	(3.7)	10.3	10.4
Productivity	1.8	3.0	3.7	1.2
Employment	(0.6)	(4.3)	(0.6)	1.3
CPI-Urban	3.8	(0.3)	2.3	2.1
S&P 500 Stock Price	(17.3)	(22.5)	21.1	7.9
Treasury Bill Rate (3-month)*	1.4	0.2	0.3	1.8
Treasury Note Rate (10-year)*	3.7	3.3	3.6	4.4

* Annual average rate.

Note: Personal income and corporate profits are nominal.

Sources: U.S. Bureau of Economic Analysis; U.S. Bureau of Labor Statistics; Federal Reserve; Standard & Poor's; NYS Assembly Ways and Means Committee staff.

[4] First American CoreLogic's data report is based on 47 million properties that have a first and/or second mortgage, which account for over 80 percent of all mortgages in the U.S. See First American CoreLogic, "First American CoreLogic's Negative Equity Data Report" (as of September 2009), November 2009.

World War II average performance: on average the U.S. economy grew 4.9 percent during the first year after nine post-World War II recessions. The only other time when the first-year economic growth after the end of recession was similarly weak was 2002. That year, the U.S. economy grew only 1.8 percent in the midst of continued weakness in the labor and financial markets. The national economy is forecast to continue to expand in 2011, but at a below-trend rate of 2.8 percent.

Combined with relatively stable energy prices, the recent trend in productivity and unit labor costs indicates that inflationary pressures from the labor market are minimal. These inflation-stabilizing forces will largely remain in place in the next two years, helping to keep inflationary pressures in check. Although finding an effective exit strategy is a challenge to the Federal Reserve, the inflation outlook in the report assumes that the Fed will successfully control the unwinding of current stimulus measures in a manner that prevents the emergence of rapid inflation.[5]

U.S. payroll employment declined by an estimated 6.1 percent or 8.4 million jobs between December 2007 and January 2010, the largest such decline since the early 1930s. Compared to earlier employment cycles, the U.S. economy created payroll jobs at a much slower rate during the 2002-07 expansion and has lost jobs by a much larger magnitude during the current downturn.[6] The severity of the current downturn is such that even by the end of the third year after the 2007 peak, the U.S. economy will have 5.2 percent fewer jobs compared to the 2007 peak level.[7] U.S. payroll employment is forecast to gain 1.2 million jobs from December 2009 to December 2010 and another 2.5 million jobs during 2011.

Gross Domestic Product

The U.S. economy, as measured by real GDP, grew a mere 0.4 percent in 2008. Had it not been for the positive contribution of net exports, the national economic performance in 2008 could have been worse. U.S. real GDP is estimated to have declined

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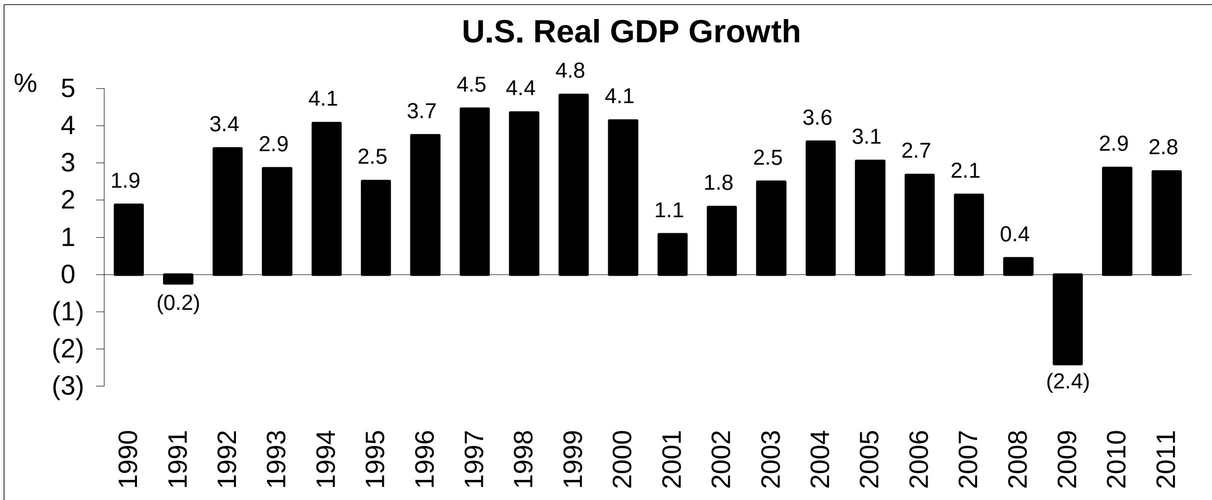
[5] There are views that are skeptical of such optimism. See, for example, Joseph E. Stiglitz, "Death Cometh for the Greenback," *National Interest online*, November/December issue, October 27, 2009, http://www.nationalinterest.org/Article.aspx?id=22348.

[6] U.S. employment grew only 4.4 percent during the three-year period leading up to the fourth quarter of 2007, whereas net job creation during the three-year period leading up to earlier employment peaks ranged from 6.2 percent to 7.9 percent.

[7] In comparison, employment grew 0.6 percent during the three-year period after the 1990 peak and 4.7 percent on average during the three-year period after earlier peaks.

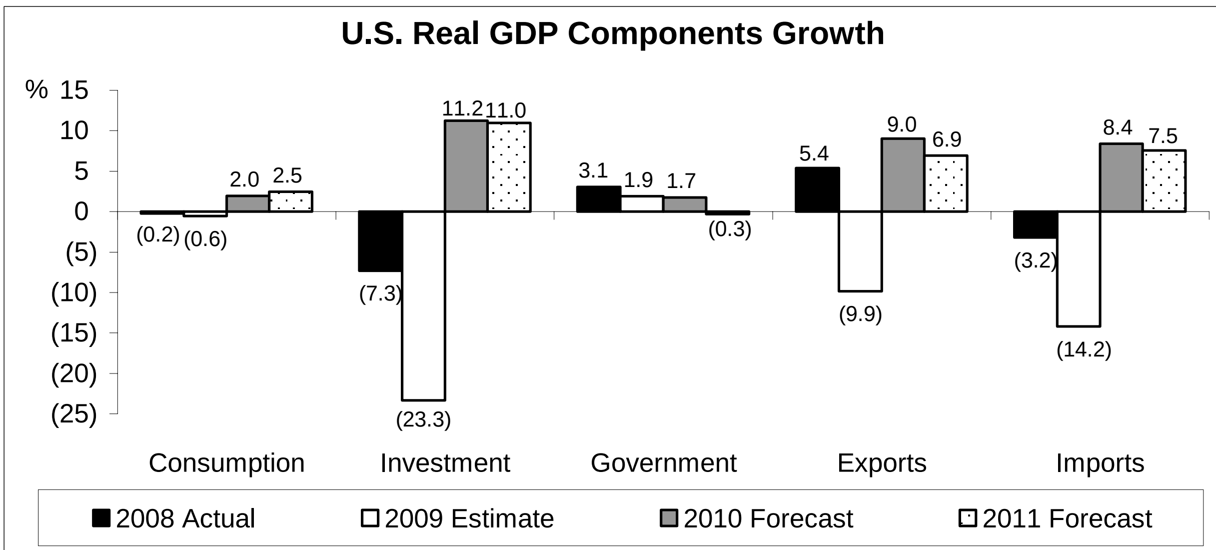
by 2.4 percent year-over-year in 2009 (see Figure 6). This is the largest yearly decline since 1946. Contraction in both consumer and business spending accounts for the sharp decline in national economic activity in 2009 (see Figure 7). The estimated 0.6 percent decrease in personal consumption spending in 2009 marks the second consecutive yearly decline, which is unprecedented since the early 1930s. Also, the estimated 23.3 percent contraction in overall business spending in 2009 is the largest yearly decline since 1949.



Note: Data for 2009 is estimated; 2010 and 2011 are forecasts.

Sources: U.S. Bureau of Economic Analysis; NYS Assembly Ways and Means Committee staff.

Figure 6



Sources: U.S. Bureau of Economic Analysis; NYS Assembly Ways and Means Committee staff.

Figure 7

U.S. real GDP is forecast to grow 2.9 percent during 2010 as corrections work their way through the economy with the Fed's vigorous easing and the large fiscal stimulus package helping to alleviate the financial and economic crisis. Personal consumption spending is expected to recover in 2010 from the back-to-back yearly decline, but growth will likely be at a measured pace, as labor market conditions remain weak and the effects of household wealth losses linger. Commercial construction activity started showing weakness in recent quarters and other business capital spending remained weak throughout the first half of 2009. However, overall business spending started recovering in the second half of 2009 and is expected to continue expanding during the forecast period aided by continued improvement in residential construction. Overall business spending should also be helped by inventory rebuilding as businesses restock their shelves and lots after a large drawdown on inventories. With a large amount of fiscal stimulus geared toward more public projects and services anticipated in 2010, the public sector as a whole is expected to help improve overall economic growth. As global economic recovery is expected to lag the U.S. economic recovery, the foreign sector will likely be more of a drag on U.S. economic growth. The national economy is forecast to expand further by 2.8 percent in 2011.

Consumption

Expenditures on consumer goods and services remain the biggest concern to overall economic recovery as personal consumption spending accounts for more than two-thirds of real GDP. Consumers continue to be thrifty as confidence about the economy is still low and sources of income that were once readily available have dwindled. Despite some improvement in recent months, consumer spending continues to be strained by lower home prices, limited access to credit, stagnant income growth, and a severely weakened labor market. These factors are expected to contribute to a consumer spending recovery that is below pre-recession levels.

In an effort to bolster consumer spending, the government appropriated funds for programs that sought to increase the discretionary income of households. The funds have been in the form of tax cuts, transfer payments such as extension of unemployment benefits, tax credits for home purchases, and other support for spending on cars and appliances. These payments have been effective to the extent that growth in disposable income has stabilized instead of plunged. In July 2009, the federal government rolled out the Consumer Assistance to Recycle and Save (CARS) program, popularly called Cash for

Clunkers, which prematurely elevated the demand for motor vehicles.[8] The program ended August 24, 2009. The CARS program boosted retail sales in August. However, because the program essentially borrowed from future consumer spending, personal consumer spending in out-years is possibly stymied.[9] Except for the boost in spending from programs associated with specific purchases, consumer spending remains restrained, as households have instead increased their savings.

In the second quarter of 2008, the tax rebates that were sent to households provided temporary support for growth in personal consumption spending.[10] As the effect of these tax rebates diminished, however, and elevated commodity prices in early to mid-2008 compared to 2007 placed additional pressure on disposable income, consumers felt the squeeze and significantly cut back on spending in the second half of 2008. As a result, personal consumption spending growth, adjusted for inflation, declined 0.2 percent in 2008, after growing 2.7 percent in 2007 (see Figure 8).

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[8] The Cash for Clunkers program is a part of the American Recovery and Reinvestment Act of 2009 (ARRA), and provided a credit of $3,500 or $4,500 for customers who purchased a qualifying new, more fuel efficient auto or light truck from a participating dealer when they traded in a qualifying less fuel efficient auto or light truck. The trade-in vehicle must have been less than 25 years old, get 18 miles per gallon or less, and must have been registered and continuously insured under the same owner for a year. The amount of credit depended on the fuel economy of the new vehicle and the trade-in vehicle. If the new vehicle had a combined fuel economy that was at least 4 but less than 10 miles per gallon higher than the trade-in vehicle, the credit was $3500. For vehicles with more than 10 miles of improved fuel efficiency, the credit was $4500. See http://www.cars.gov/ (accessed on September 4, 2009).

[9] In 2010, the number of cars, pickups, sport utility vehicles, and passenger vans projected to sell is 11.4 million, 6 million units below the 2000 peak level.

[10] For details on this fiscal stimulus package, see the Economic Stimulus Act of 2008, Public Law 110-185, 110th Congress, February 13, 2008.

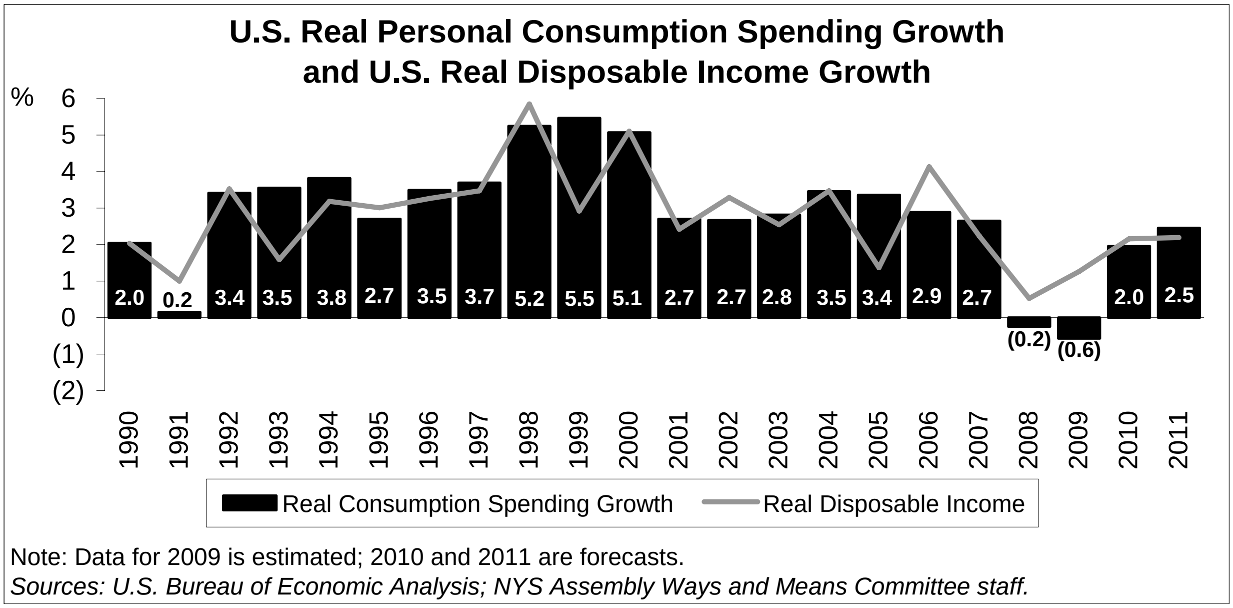
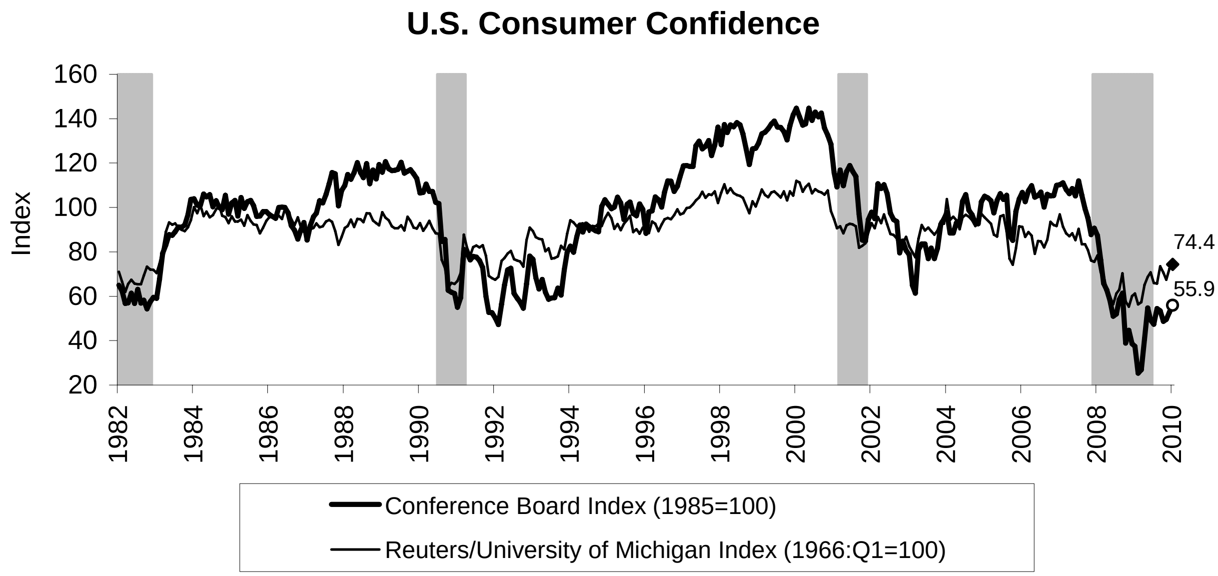


Figure 8

Lower energy prices and various stimulus programs somewhat encouraged consumer spending in 2009. However, on a yearly average basis, real personal consumption spending is estimated to have contracted in 2009 as households laden in debt struggled to balance debt obligations with other financial responsibilities. The cumulative effect of losses in household wealth, less access to credit, slower income growth, and higher unemployment has continued to weigh on consumer confidence (see Figure 9).[11] The downward pressure of these factors on consumer spending will outweigh the effects of low interest rates, tax cuts, tax credits, and other transfer income that households received through the fiscal stimulus passed by Congress in February 2009. Consequently, real personal consumption spending further declined an estimated 0.6 percent in 2009, marking the first back-to-back yearly falloff in consumer spending since 1932.

[11] Consumer confidence fell to its lowest level in January 2009 since the series started in 1978. Consumer sentiment improved slightly but remained very low in December 2009 and January 2010.



Note: Data is monthly through January 2010. The shaded areas represent recessions.
Sources: The Conference Board, Inc. CCI; Reuters/University of Michigan ICS.

Figure 9

Over time, debt reduction and higher savings will likely enhance personal consumption spending as funds once used to make debt payments become available to make purchases. In addition, consumer spending will be encouraged from households rebuilding their wealth. However, a sagging labor market, weak wage and salary growth, and a fragile housing market suggest that consumers will spend at a more deliberate pace. In addition, the expiration of the Economic Growth and Tax Relief and Reconciliation Act of 2001 (EGTRRA) and the Job and Growth Tax Relief Reconciliation Act (JGTRRA) of 2003 will increase tax rates on income of households and likely suppress consumer spending.[12] Thus, real personal consumption spending is anticipated to grow by only 2.0 percent year-over-year in 2010 and forecast to increase 2.5 percent year-over-year in 2011.

The forecast for consumer spending is consistent with the gradual recovery pattern of past recessions that were most similar in nature to the recent recession. Characteristically, the recession that began in December 2007 appears to be most comparable to the 1990-91 recession than to other recessions of the past four decades. In the 1990s, serious solvency problems arose at thrift institutions and the financial sector was

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[12] Economic Growth and Tax Relief and Reconciliation Act of 2001, Public Law 107-16, 107th Congress, June 7, 2001; and Job and Growth Tax Relief Reconciliation Act, Public Law 108-27, 108th Congress, May 28, 2003.

hit by a credit crunch. Initially the recovery in consumer spending was sluggish. On the other hand, the 1973-75 and 1980-82 recessions were caused by a disruption in oil supply. Then, consumer spending fell dramatically, however rebounded quite sharply.

Retail sales remain weak as sales in recent months have been largely driven by government programs that subsidize the purchase of specific goods. Sales of motor vehicles and housing-related goods accounted for 30.1 percent of retail sales in 2008. Sales at motor vehicles dealers fell 29.0 percent from October 2007 to March 2009, while sales at furniture, electronics, and appliance stores decreased 17.1 percent from November 2007 to October 2009, peak-to-trough. With the expiration of government programs that subsidized certain purchases, sales of these goods are expected to remain lackluster at best in 2010, given tightened credit standards and limited refinancing activity due to lower home prices.

An advantage of programs such as the Cash for Clunkers is that they allowed retailers to draw down excessive inventory by boosting consumer spending. Retailers have not replenished their stock of goods in proportion to the falloff in inventory. The significant drop in new orders of consumer goods, a leading indicator of personal consumption spending, experienced in the second half of 2008 stabilized in third quarter of 2009 and continues to improve (see Figure 10). This suggests that while retailers are keeping inventory more aligned with sales, they are doubtful that consumers will curtail spending further.

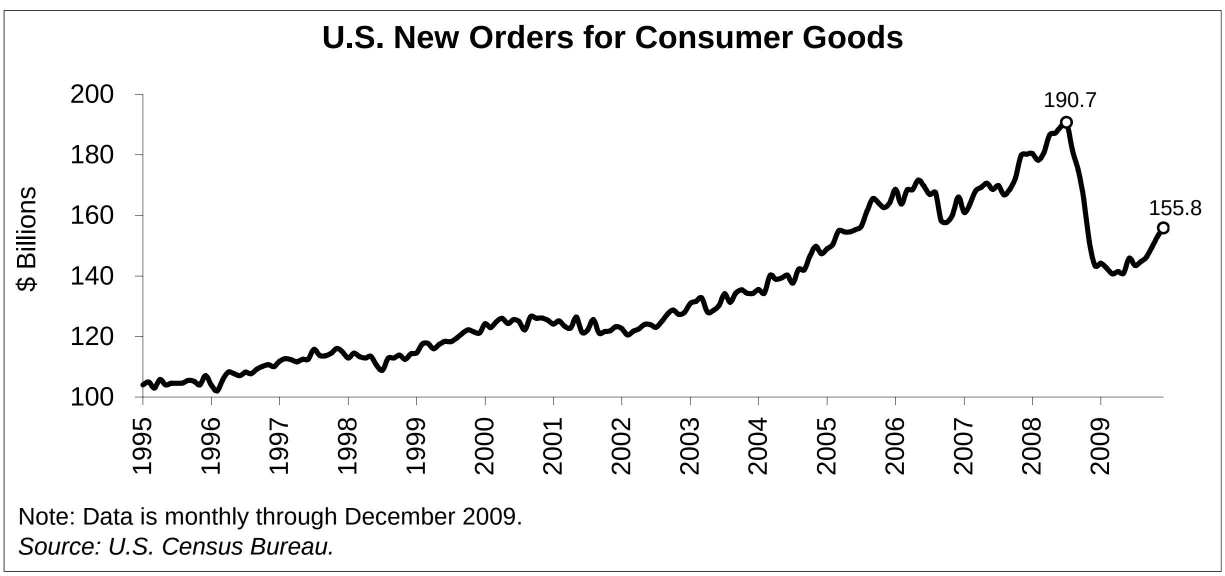
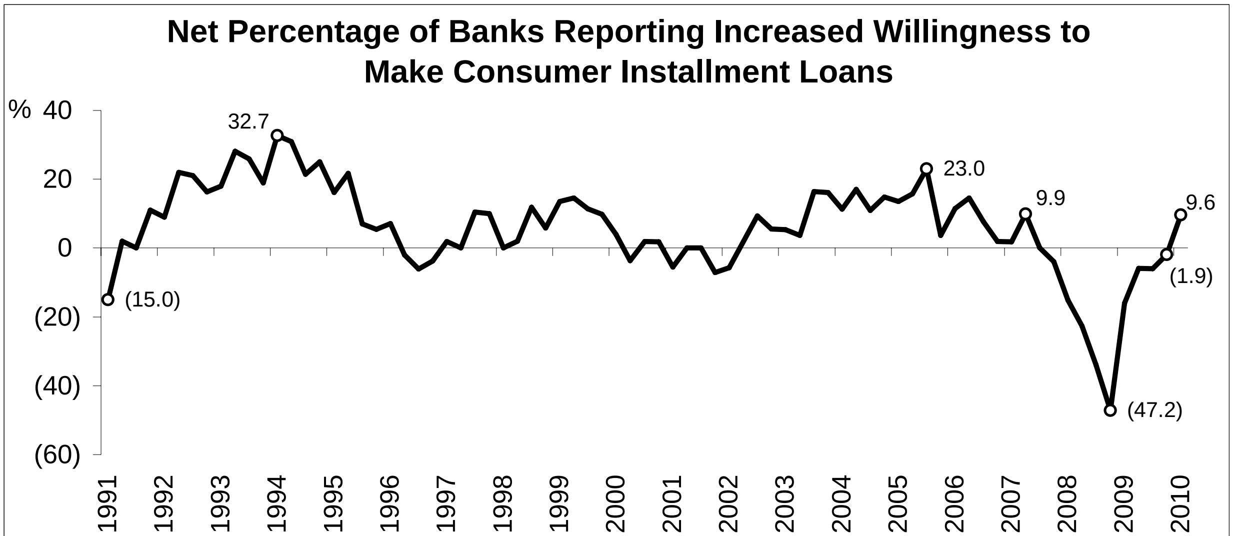


Figure 10

Though credit conditions have somewhat eased, the ripple effects of tightened credit standards continue to burden households as resources that were once readily available to finance spending activities have withered (see Figure 11).[13] The fall in home prices has limited households' ability to withdraw equity from their houses since the third quarter of 2006.



Note: Data is quarterly through 2010:Q1. Data for each quarter corresponds to information collected in the previous quarter. Bank data was taken from a survey of approximately sixty large domestic banks and twenty-four U.S. branches and agencies of foreign banks.
Source: Board of Governors of the Federal Reserve System: Senior Loan Officer Opinion Survey on Bank Lending Practices, January 2010.

Figure 11

Total home equity withdrawals by households fell $73.0 billion from its peak in the second quarter of 2006 to the fourth quarter of 2009 (see Figure 12). The $10.6 billion in home equity cashed out in the fourth quarter of 2009 was the smallest since 2000. Overall, refinance activities escalated in the fourth quarter of 2008, as homeowners who were creditworthy took advantage of lower interest rates. Homeowners continued to take advantage of lower interest rates through the fourth quarter of 2009 when 33 percent of

[13] In the fourth quarter of 2009, only 1.9 percent of the banks surveyed reported less willingness to lend. In the fourth quarter, less than 20 percent of the banks surveyed had tightened standards from the third quarter. In the first quarter of 2010, 9.6 percent of banks surveyed were more willing to lend compared to the prior quarter. According to the Federal Reserve Board, the reported net percentages equal the percentage of banks that reported tightening standards ("tightened considerably" or "tightened somewhat") minus the percentage of banks that reported easing standards ("eased considerably" or "eased somewhat"). The Senior Loan Officer Opinion Survey on Bank Lending Practices is published quarterly by the Federal Reserve Board. See http://www.federalreserve.gov/boarddocs/SnLoan survey/.

borrowers lowered their principal balance by refinancing. This was the highest "cash-in" share since the data began being tracked in 1985.[14] In the long-term, lower mortgage payments can lead to higher discretionary income. Any further easing of credit conditions and a stabilized housing market could provide support for consumption spending growth.

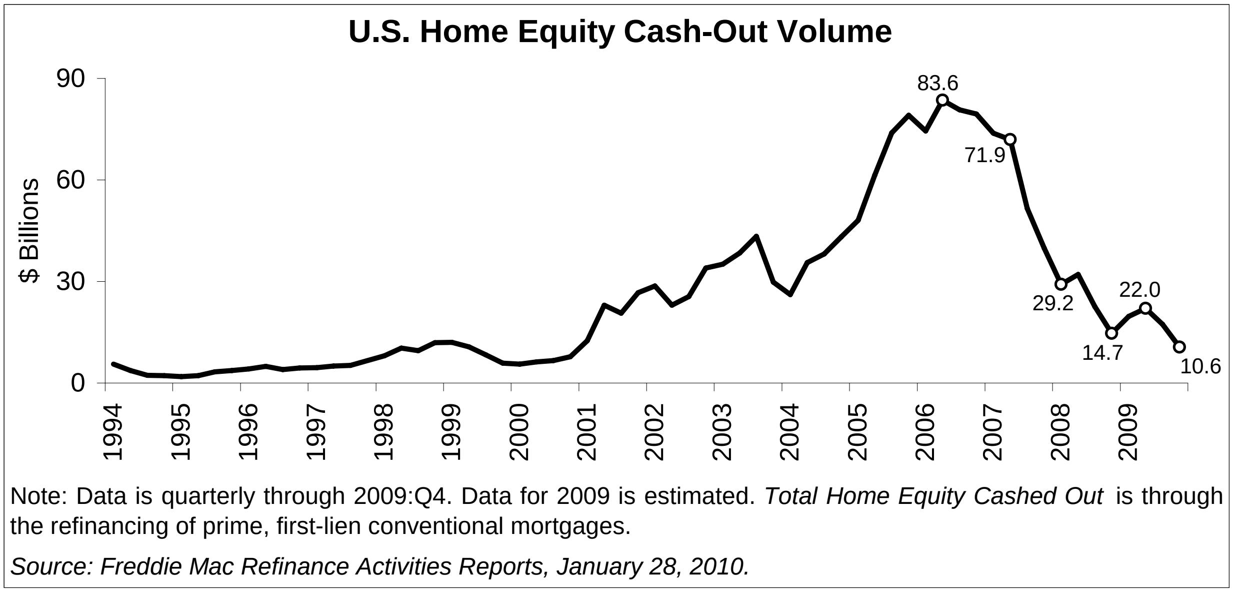


Figure 12

Findings on the effects of the Economic Stimulus Act of 2008, in which households received between $300 and $1,200, suggest that households spent 30 percent of their tax rebates.[15] Similarly, the tax credits and other cash payments to households in 2009 from the American Recovery and Reinvestment Act of 2009 (ARRA) have proved only to encourage higher savings.[16] Households tend to pay down debt during economic downturns, which also contributes to higher savings. Even though higher saving rates dampen consumer spending, savings create a financial buffer in an arduous economy. Over time, this cushion can act as an impetus to consumption spending recovery as

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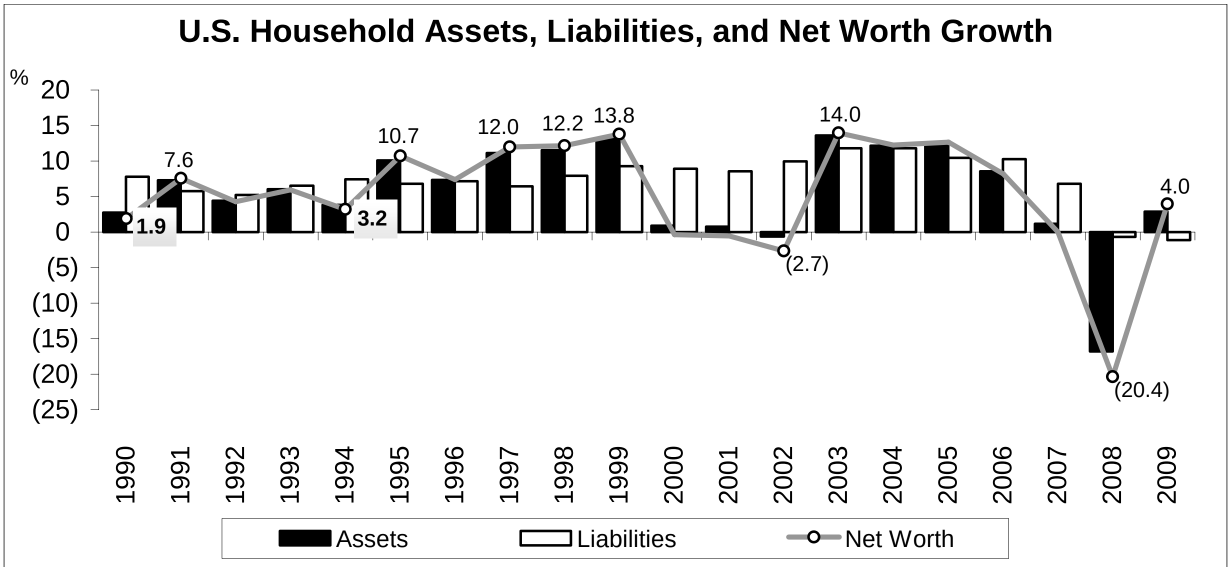
[14] Freddie Mac Refinance Activities Report, "Record High Share of Borrowers Who Refinanced in Fourth Quarter Paid Down Principal Balance, Reducing Mortgage Debt," Freddie Mac, January 28, 2010, http://www.freddiemac.com/news/archives/rates/2010/4qupb09.html.

[15] In addition, 49 percent of recipients reported using rebates to pay down debt, and 18 percent saved their rebate. See, U.S. Bureau of Labor Statistics, "Consumer Expenditure Survey Results on the 2008 Economic Stimulus Payments (Tax Rebates)," *Consumer Expenditure Survey*, (Last Modified Date: October 15, 2009), http://www.bls.gov/ces/taxrebate.htm.

[16] For 2009, the savings rate averaged 4.6 percent, compared to an average of 1.7 percent in 2007 and 2.6 percent in 2008.

consumers regain their confidence. However, consumers are not expected to spend at rates seen in the 1990s or even in the mid-2000s.

The spillover effect of the depressed housing market into the financial markets took its toll on the balance sheet of households. As asset prices spiraled downward, the net worth of households fell $13.1 trillion or 20.4 percent in 2008 compared to 2007 (see Figure 13).[17] This was the largest annual decline since the series began in 1945. Corporate equity holdings decreased as equity markets succumbed to falling corporate profits and tightened credit conditions. Households' real estate value growth turned negative in 2007 for the first time since 1945 and as of the third quarter of 2009 remained far below its 2006 peak due to considerable depreciation in home prices. Many homeowners now have mortgages that are higher than the value of their home. Though the stock markets have shown improvement, the $9.1 trillion decline in the value of financial assets will not be



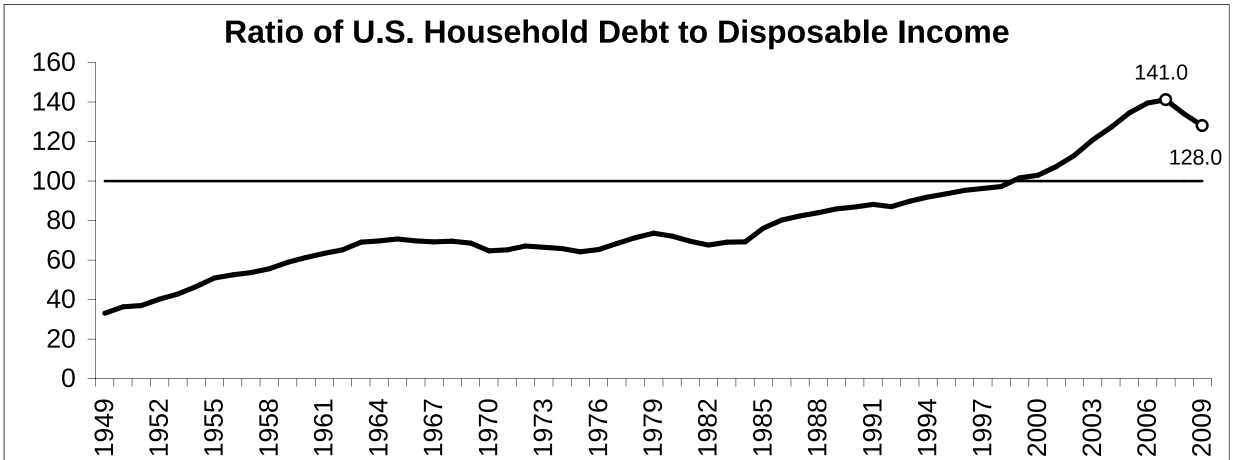
Note: Annual growth for each year is based on fourth quarter over fourth quarter percent change. Data for 2009 is based on the third quarter.
Source: Federal Reserve.

Figure 13

[17] Household net worth fell $17.5 trillion or 26.6 percent from its peak in the second quarter of 2007 to the trough in the first quarter of 2009.

easily recouped any time soon even with households changing the composition of their portfolios. The diminished wealth of households will likely exert more downward pressure on real personal consumption spending.[18]

Additional pressures on personal income from joblessness suggest more stress on the discretionary income of households. Household leverage increased consistently since 1982 and reached its peak in 2007. At its peak, household debt was 41.0 percent higher than disposable income. By 2008, the ratio of household debt to disposable income had fallen to 133.9 (see Figure 14).[19] Generally, household debt growth has outpaced disposable income on a year-over-year basis. In harsh economic times of rising unemployment coupled with a prohibitive lending environment, such debt to income ratio is hardly sustainable and leads to higher delinquency rates as an upper bound exists on the size of debt that households can service based on income. Hence, consumer spending will be hampered by households continuing to deleverage over the forecast period.



Note: Data for disposable income is annual through 2008. Data for household debt is based on the fourth quarter of each year. The ratio for 2009 is based on data for the third quarter for disposable income and household debt.
Sources: Federal Reserve; Bureau of Economic Analysis.

Figure 14

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[18] The Congressional Budget Office estimates that the wealth effect will subtract 0.75 percentage point from the growth of personal consumption spending in 2009, and reduce growth in 2008 by 1.1 percentage points. See, Congress of the United States, Congressional Budget Office Testimony: Statement of Douglas W. Elmendorf, Director, "The State of the Economy and Issues in Developing an Effective Policy Response," before the Committee on the Budget, U.S. House of Representatives, January 27, 2009.

[19] Based on 2009 third quarter data, the ratio of U.S. household debt to disposable income was 128.0.

Though overall personal consumption spending has been subpar, spending on services has fared better than spending on durable and nondurable goods. From the fourth quarter of 2007 to the third quarter of 2009, spending on consumer durable goods fell in five quarters, while spending on nondurable goods declined in four quarters, and spending on services provided to consumers fell in only two quarters.

In part, most expenditures associated with services cannot be delayed as these include spending on health care, housing, utilities, and transportation. On the other hand, consumers can economize by finding substitutes, and defer or eliminate purchasing discretionary durable and nondurable items. These shifts in household behavior are crucial to the pace at which consumer spending recovers throughout the forecast period.

In 2008, growth in spending on durable goods fell 4.5 percent primarily due to a falloff in light motor vehicle sales.[20] On average, sales of light motor vehicles fell 18.0 percent in 2008 compared to 2007. The pullback in durable goods spending was also attributed to the slowdown in spending related to home purchases. Growth in spending on furniture and household equipment slowed in 2007 from 2006, and the slowdown intensified in 2008 as the recession deepened.

After falling in the second quarter of 2009, spending on durable goods escalated in the third quarter boosted by light vehicle sales, which were supported by the Cash for Clunkers federal program. On a year-over-year basis, however, in 2009 spending on durable goods fell an estimated 4.0 percent. The back-to-back decline was the first since the recession of 1990-91. As the housing market stabilizes and credit conditions continue to ease, spending on durable goods will be below trend, and is forecast to improve 4.4 percent in 2010 and 5.8 percent in 2011 (see Figure 15). From 1992 to 2007, durable goods grew at an annual average rate of 6.7 percent.

[20] Light motor vehicles have a gross weight of up to 10,000 pounds. This includes cars, light conventional pickups, compact pickups, sport-utility vehicles, and passenger vans.

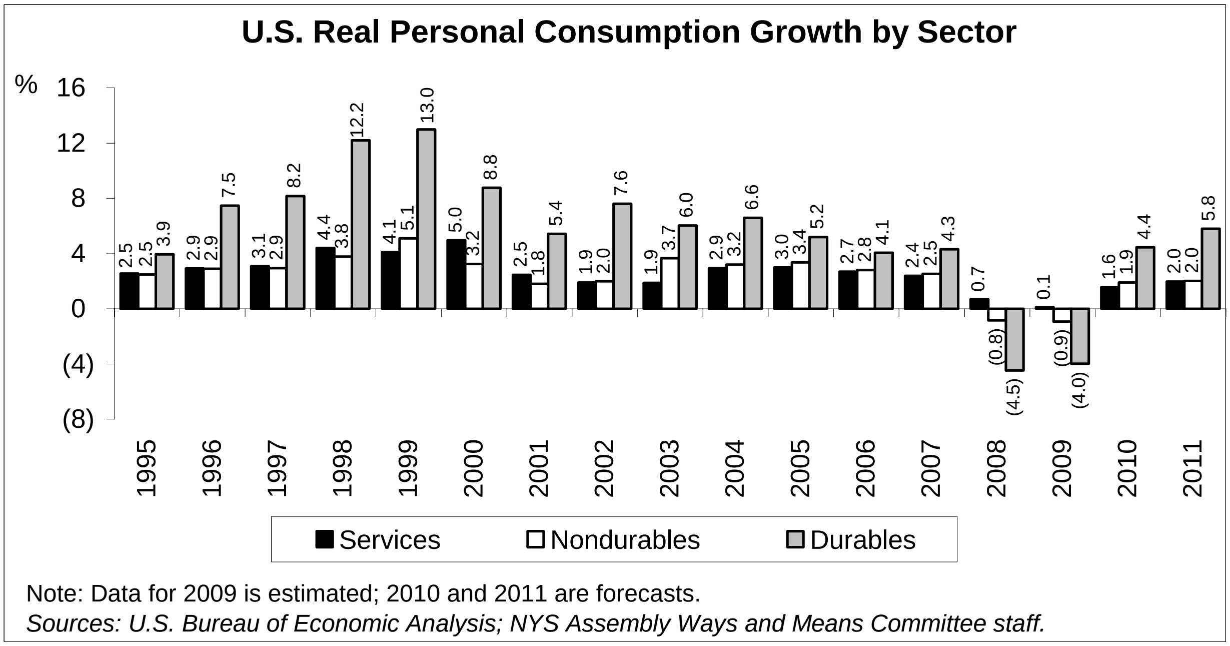

Figure 15

Elevated energy prices that were passed through to food and other nondurable goods prices in early and mid-2008 placed pressure on real disposable income, restraining consumer spending on these and other consumer items. Total personal consumption spending on nondurable goods declined 0.8 percent in 2008. Despite lower energy prices, declining income and a delay of purchases or substitution to cheaper goods led consumers to reduce spending on nondurable goods an additional 0.9 percent in 2009, the first consecutive year-to-year decline since the early 1930s. The recovery in nondurable goods spending, while more aligned to the 2001 recession, will be below the 2.9 percent annual average growth observed from 1992 to 2007. In 2010, nondurable goods spending growth is anticipated to rebound to 1.9 percent, and then 2.0 percent in 2011 as the labor market gradually improves, supporting higher discretionary income.

Consumer spending on services grew a tepid 0.7 percent in 2008 due to increases in spending on services related to housing and utilities, and health care, which mitigated cutbacks in financial services and insurance, and food services and accommodation. Spending on many of these services grew even slower, increasing only 0.1 percent in 2009, the lowest positive growth rate since 1947.[21] With personal disposable income and overall economic growth expected to steadily improve, spending on consumer services is

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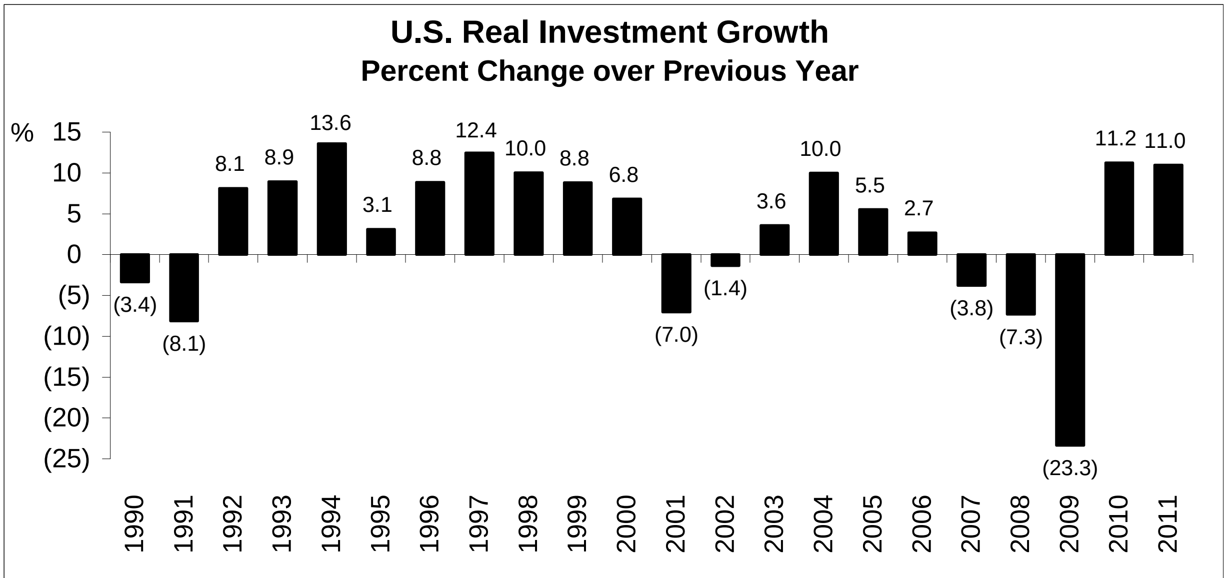
[21] The growth in spending on consumer services was 0.4 percent in 1947, the next lowest was in 1938 when spending on consumer services declined to 0.8 percent.

projected to increase by 1.6 percent in 2010 and 2.0 percent in 2011, well below the annual average of 2.8 percent between 1992 and 2007.

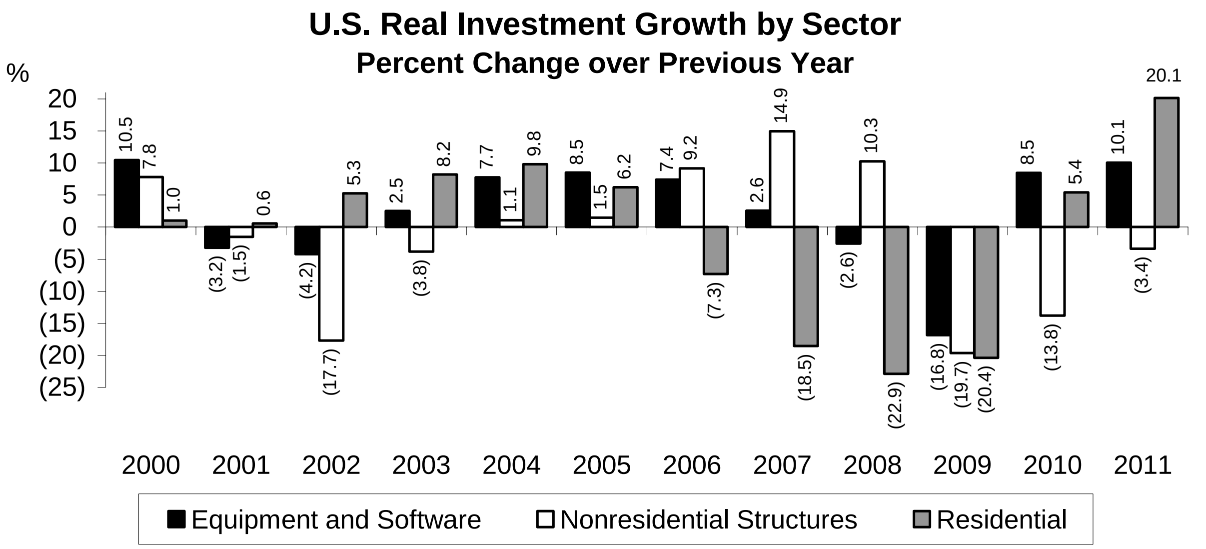
Investment

Deterioration in the residential market, waning business confidence, and a suffocating credit environment have led to the worst falloff in U.S business spending since WWII. Business spending plummeted eleven of thirteen quarters from its peak in the first quarter of 2006 to its trough in the second quarter of 2009, totaling a decline of 35.7 percent and marking the deepest and longest downturn since WWII. In previous recessions, investment declined an average of 20.1 percent over a period of 4.1 quarters (refer to Appendix B on page 96). Total U.S. business spending declined an estimated 23.3 percent in 2009 (see Figure 16) due to weaknesses across all sectors of business investment activity (see Figure 17). Business spending rebounded in the second half of 2009 and is forecast to continue to grow throughout 2010 as the housing market moderates, businesses rebuild inventories, and firms update equipment and software.



Note: Data for 2009 is estimated; 2010 and 2011 are forecasts.
Sources: U.S. Bureau of Economic Analysis; NYS Assembly Ways and Means Committee staff.

Figure 16



Note: Data for 2009 is estimated; 2010 and 2011 are forecasts.
Sources: U.S. Bureau of Economic Analysis; NYS Assembly Ways and Means Committee staff.

Figure 17

While all areas of investment have suffered, the worst declines have come from investment in residential structures, which fell 55.6 percent from the first quarter of 2006 through the second quarter of 2009. The worst of the fallout from the residential sector appears to be over, as the crescendo in defaults of subprime mortgages that caused the housing market to plummet over the last three years has abated. However, a second and smaller wave of defaults, coming from those with prime mortgages who have lost their jobs and have exhausted unemployment benefits, has further inhibited recovery in the residential market. Consequently, home prices have been slow to recover as the delinquency rate on single-family residential mortgages remains at record high levels, climbing to 9.8 percent in the third quarter of 2009 (see Figure 18).[22] In addition, new homes remain on the market for extended periods with no buyer despite the lowest inventory rates for new homes since the 1970s.[23]

[22] Federal Reserve Board, "Charge-off and Delinquency Rates on Loans and Leases at Commercial Banks," *Federal Reserve Statistical Release*; (Last updated: November 16, 2009), http://www.federalreserve.gov/releases/chargeoff/.

[23] In December 2009, the median period that a home remained on the market after completion rose to a record 13.9 months, up from a low of 3.4 months in September 2006.

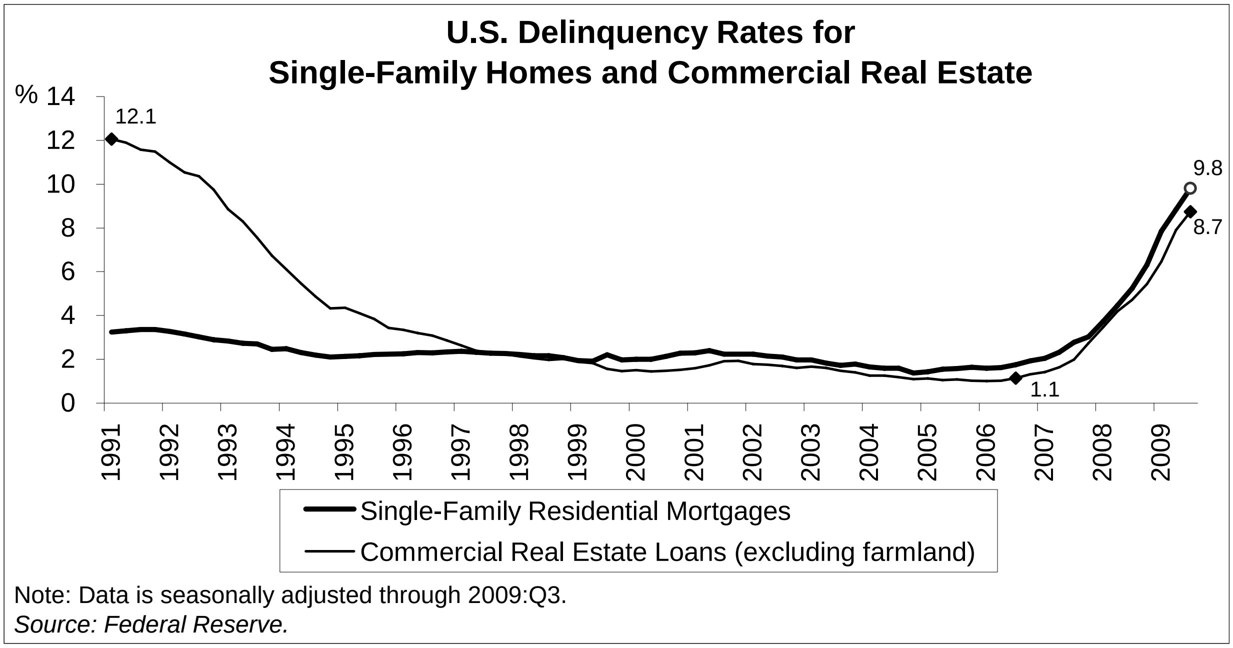


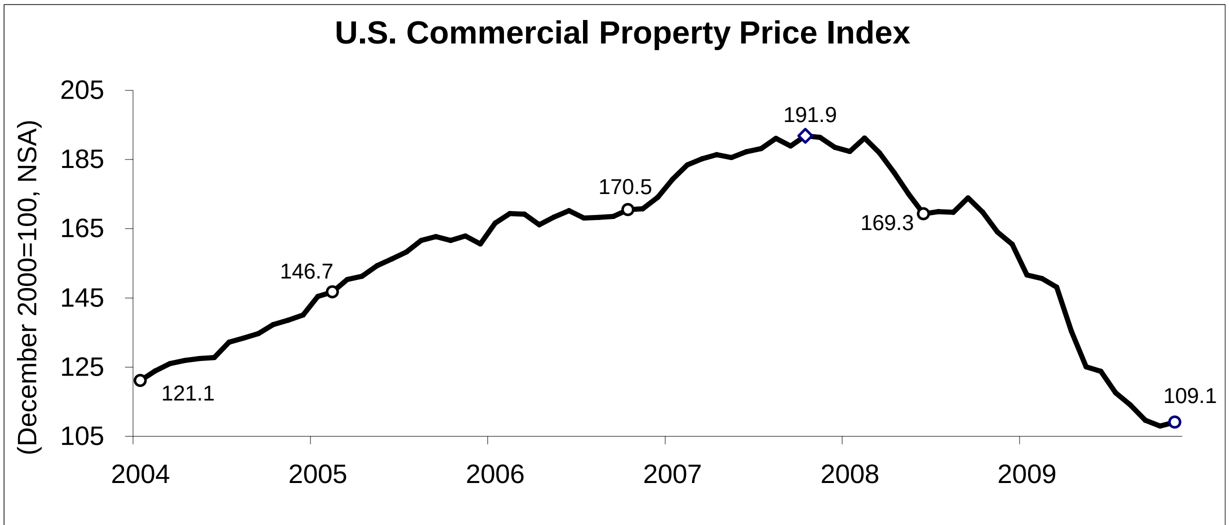
Figure 18

Though the residential market continues to be challenged by tight credit conditions and ongoing troubles in the labor market, the environment appears to be easing as depressed prices in the housing market coupled with government incentives have encouraged able renters to become homeowners. Positive activity has begun to be reflected in residential indicators; in June 2009, after forty months of contraction, construction of single-family homes, which makes up approximately 70 percent of residential construction activity, began to experience growth. Ongoing improvements in the single-family home market helped boost residential investment in the second half of 2009.[24]

While the residential market appears to be on the path to recovery, developments in the nonresidential sector threaten the overall economic recovery (see Figure 17 on page 20). Of highest concern is the extent of potential fallout in the commercial real estate market. Like the housing market, space prices in nonresidential buildings became highly inflated due to easy and cheap financing in the years preceding the recession. From its peak in October 2007 to October 2009, the commercial property price index declined

[24] As defined by the U.S. Census Bureau: New single-family homes include new houses and townhouses built to be sold or rented and units by the owner or for the owner on contract. New multi-family homes include apartments and condominiums.

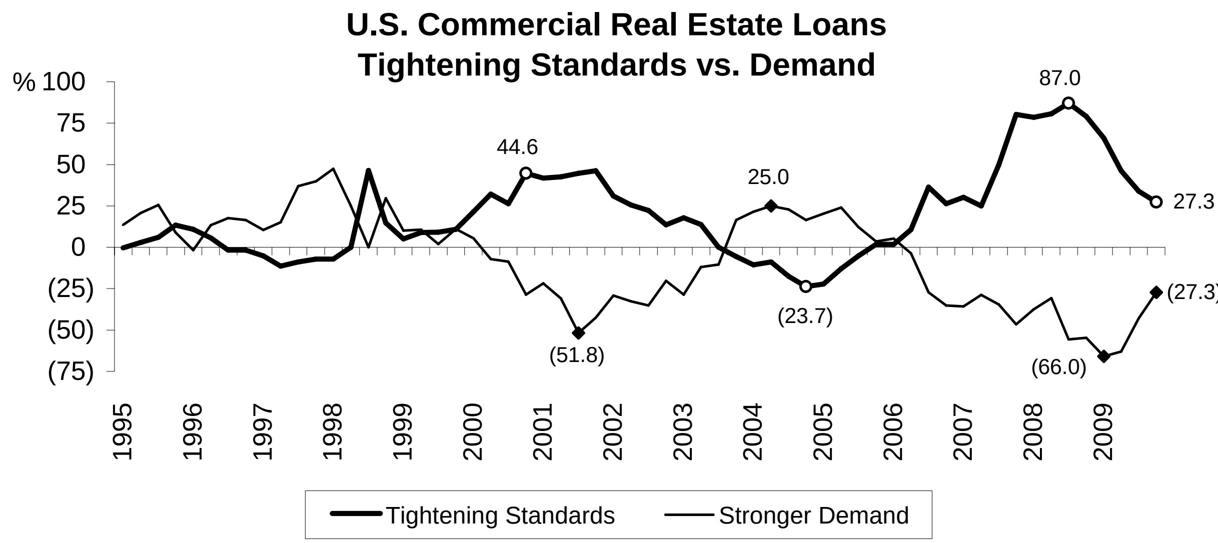
43.7 percent, losing nearly half of its value over a span of two years (see Figure 19).[25] Furthermore, tight credit conditions and waning demand for commercial real estate loans from investors continue to weigh on the health of the nonresidential sector—on net, 27.3 percent of banks surveyed in the first quarter of 2010 reported having tightened lending standards for commercial real estate (CRE) loans from the previous quarter, the same net percent of banks also reported weaker demand for CRE loans compared to the previous quarter (see Figure 20). Given declining space prices, increasing vacancy rates, and a tight credit environment, the ability of borrowers to refinance loans has been put into jeopardy and many have been forced into default and bankruptcy. Rising delinquency rates, which are already at a sixteen-year high and are expected to continue mounting, will further discourage investment in nonresidential construction in 2010.



Note: Data is monthly through November 2009.
Source: Moody's Investors Service.

Figure 19

[25] November 2009 saw the first uptick in the index in fourteen months. The index has declined in twenty-one of the last twenty-four months.



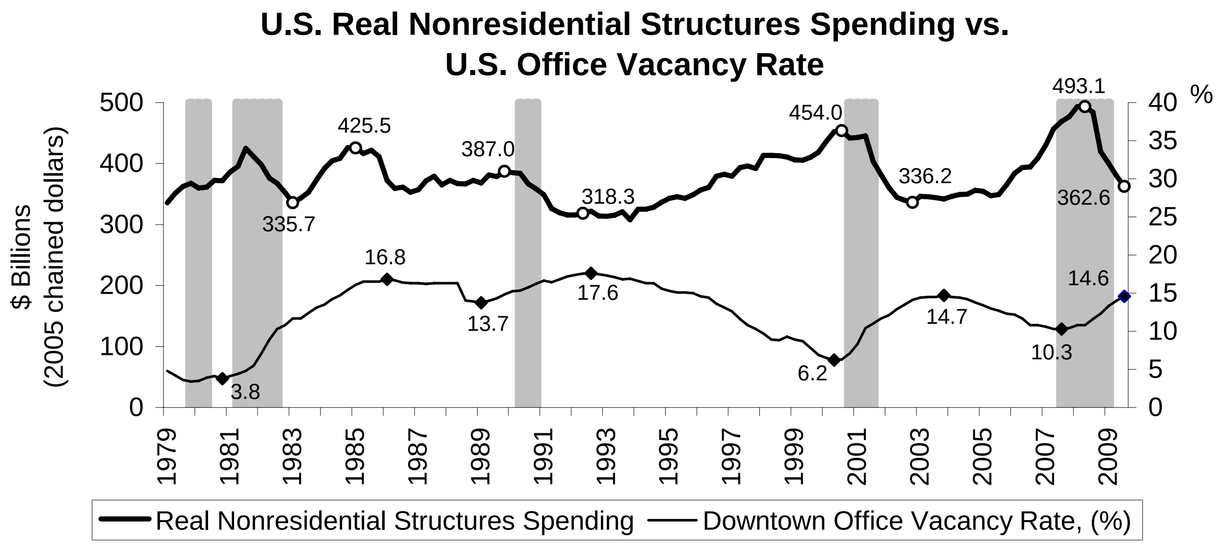
Note: Data is quarterly through 2010:Q1. Data for each quarter corresponds to information collected in the previous quarter. In regards to tightening standards on commercial real estate loans, banks are asked if they are tightening standards, loosening standards, or if loan standards have remained the same. The percent of banks loosening standards is then subtracted from the percent of banks tightening standards. A similar calculation is also performed to determine demand.

Source: Board of Governors of the Federal Reserve System: Senior Loan Officer Opinion Survey on Bank Lending Practices, January 2010.

Figure 20

Historically, downturns in the nonresidential sector are far from short-lived. Rising vacancy rates have, with an average 2.3 quarter lag, an inverse relationship with investment in nonresidential structures (see Figure 21).[26] Over the past three recessions, office vacancy rates have risen for an average of 16.3 quarters and investment in business structures has fallen for 7.7 quarters from peak to trough. As of the fourth quarter of 2009, vacancy rates had risen for eight quarters, and business spending on nonresidential structures had fallen for six quarters, indicating that the fall in nonresidential construction spending will continue at least through the first half of 2010.

[26] U.S. downtown office vacancy rate data series began in 1978:Q2.

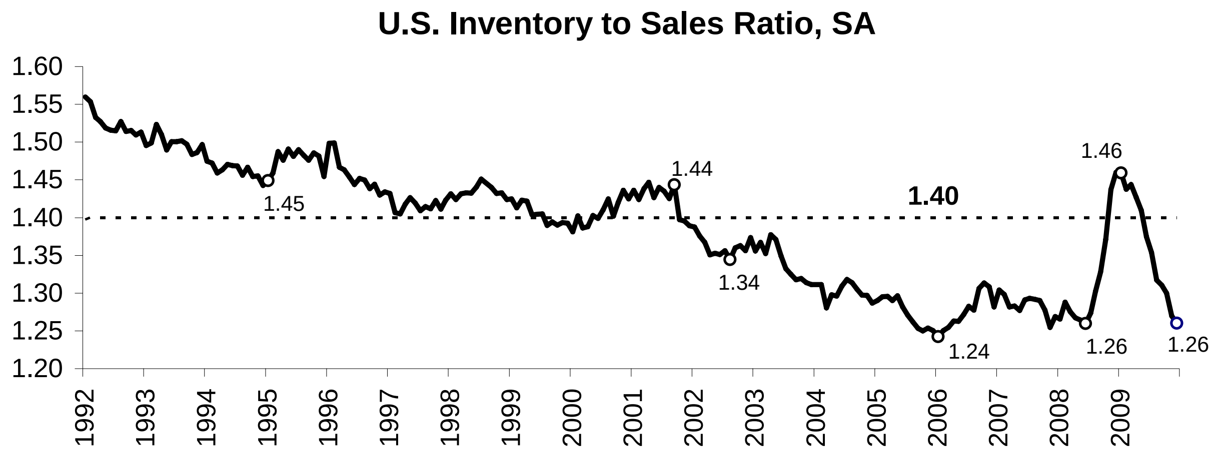


Note: Data is quarterly through 2009:Q4.
Sources: CB Commercial Real Estate Services Group, Inc.; U.S. Bureau of Economic Analysis.

Figure 21

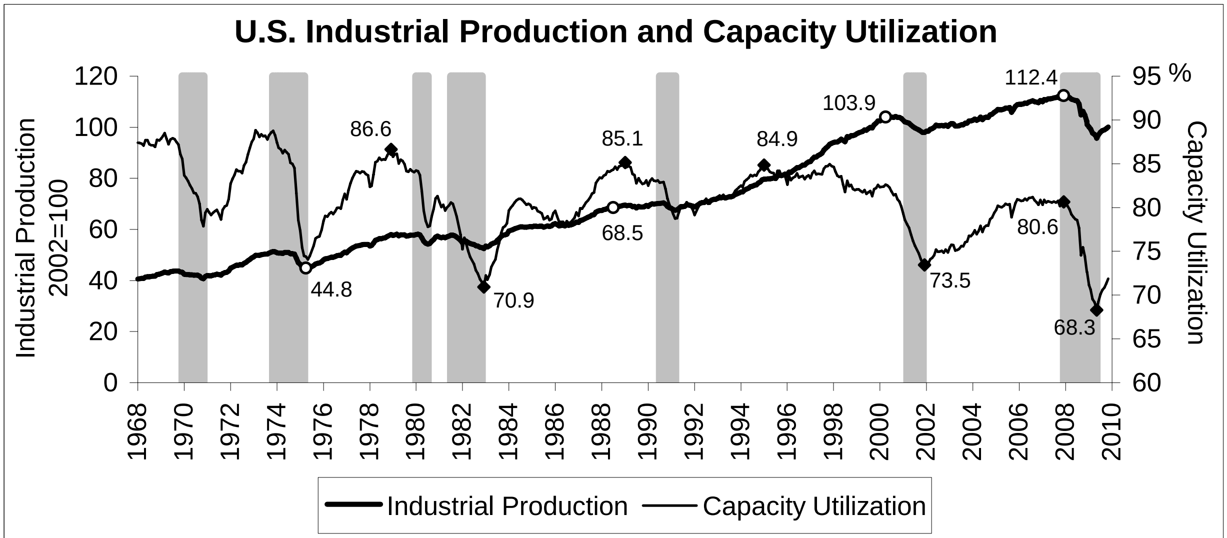
Business spending on equipment and software decreased 2.6 percent in 2008 and is estimated to have declined 16.8 percent in 2009. The decline was driven by contractions in business spending on industrial equipment, transportation equipment, and information-related equipment and software spending, and largely continued through the second quarter of 2009. The need to pull back on production was exacerbated by tight credit conditions and a jostled consumer base, which forced the inventory to sales ratio to jump from 1.26 to 1.46 (see Figure 22).[27] Consequently, capacity utilization rates fell to record lows in 2009 and industrial production dropped dramatically as companies moved to slow down production in order to realign supply with waning demand (see Figure 23).

[27] The inventory/sales ratio is commonly interpreted as the number of months it would take to deplete the present inventory stock given the correlating month's sales rate.



Note: Data is through December 2009. Dotted line represents the average inventory to sales ratio from January 1992 through December 2007.
Source: U.S. Census Bureau.

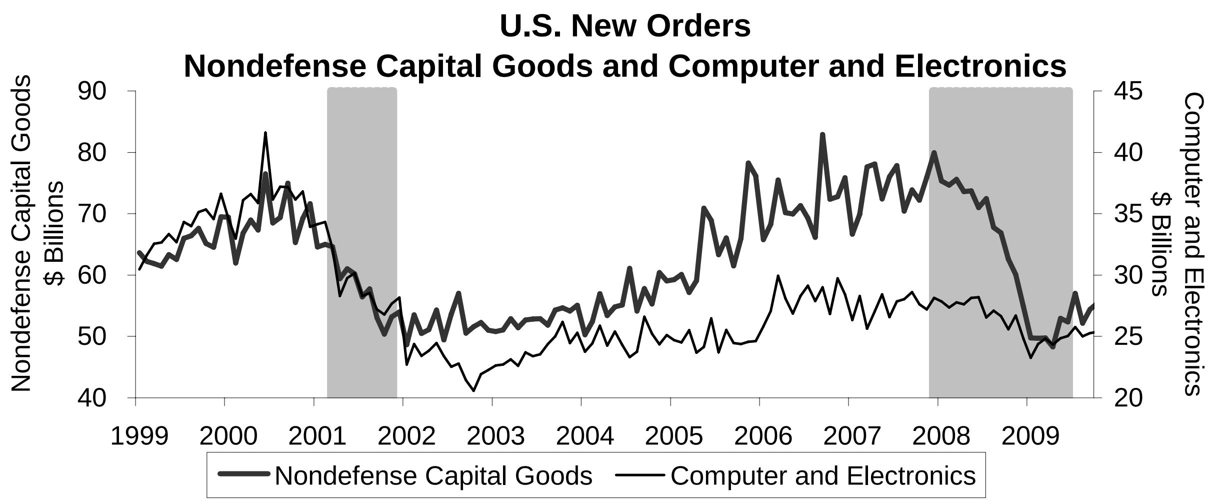
Figure 22



Note: Data is monthly through January 2010. The shaded areas represent recessions.
Source: Federal Reserve.

Figure 23

Information-related equipment and software spending gained in the third quarter of 2009 after declining for six consecutive quarters. The sector's modest growth was driven by a turnaround in spending on computer and electronic equipment, as well as growth in business spending on transportation equipment. Despite some month-to-month volatility, new orders on nonmilitary capital goods are on an upward trend, indicating further improvements in business capital spending (see Figure 24). With the recovering economy and the need for capital upgrades, business spending on equipment and software is forecast to grow 8.5 percent in 2010 and 10.1 percent in 2011.



Note: Data is monthly through December 2009. The shaded areas represent recessions.
Source: U.S. Census Bureau.

Figure 24

Developments in the inventory cycle will further contribute to business spending growth in the forecast period. Inventory adjustments contributed 0.7 percentage point to overall GDP growth in the third quarter of 2009. Further inventory adjustments are estimated to have contributed 3.5 percentage points to GDP growth in the fourth quarter of 2009 and were responsible for nearly all of the estimated 42.3 percent growth in investment for the same period. Further improvements in inventories will continue to be a positive force on total investment growth in the forecast period, though to a more moderate degree than experienced in the second half of 2009. Total investment is forecast to grow 11.2 percent in 2010 and 11.0 percent in 2011.

Housing Market

Housing accounts for the largest portion of household wealth. The housing market has emerged as one of the most important factors to influence the overall state of the economy, especially following the 2001 recession. Home prices had been steadily increasing since the end of the 1991 recession. From the second quarter of 2002 to the second quarter of 2006, national home prices appreciated by 55.3 percent. As a result, household real estate assets grew 66.7 percent from $13.8 trillion in 2002 to its peak of

$22.9 trillion in 2006. Household real estate assets dropped to $16.5 trillion in the third quarter of 2009.[28] Activities in the housing market also slowed significantly. Both new and existing home sales have continued to decline, while housing starts in April 2009 dropped to the lowest level since the series started in the late 1940s. Improving housing affordability has helped increase sales and starts in recent months (see Figure 5 on page 4).

Since its peak in the second quarter of 2006, national home prices have declined by more than 30 percent, with the highest depreciation rates in the areas that experienced the fastest growth during the boom period. The S&P/Case-Shiller home price index has been declining since the fourth quarter of 2006; however, the rate of decline has slowed in the most recent quarters (see Figure 25).

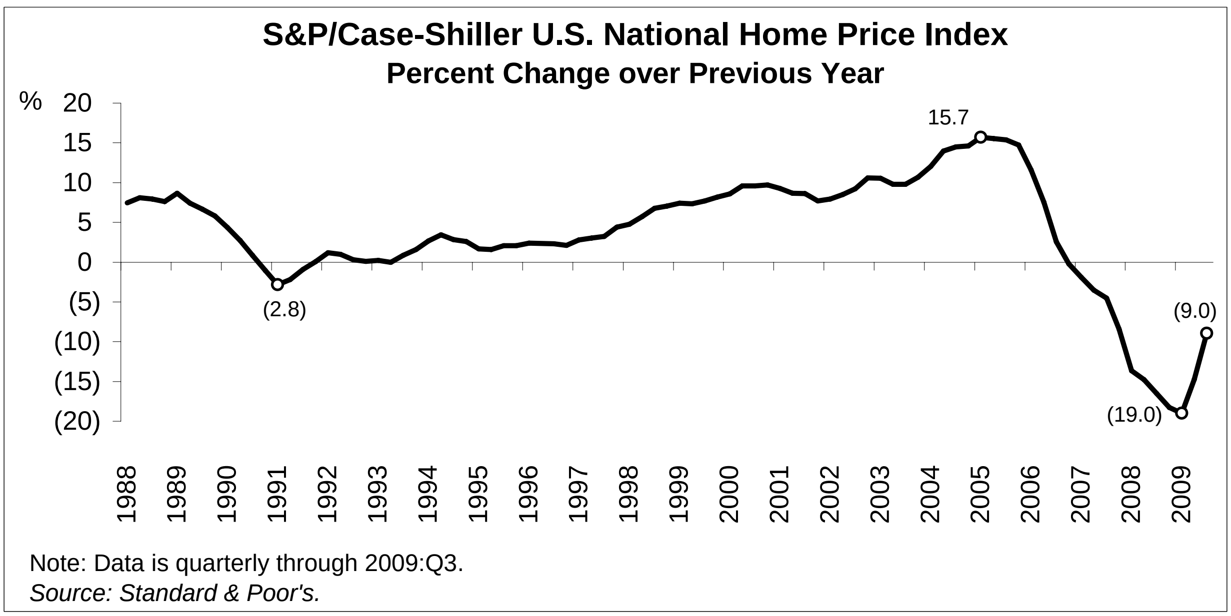


Figure 25

As the price of a home declines, the owner's equity in household real estate also declines. Owner's equity in household real estate declined from 58.8 percent in 2002 to 37.6 percent in the third quarter of 2009.[29] Declining home values have contributed to the negative equity many homeowners have on their mortgages. As of September 2009, it was estimated that more than ten million mortgages or 22.6 percent of all mortgage holders owed more on their mortgage than the properties were worth (in negative equity), with

[28] Federal Reserve Board, "Flow of Funds Account of the United States," *Federal Reserve Statistical Release*, December 6, 2007, and December 10, 2009, http://www.federalreserve.gov/releases/z1/.

[29] Ibid, Federal Reserve Board.

another 2.3 million mortgages approaching negative equity.[30] This imposes a significant downside risk to the housing market as it could create an incentive for homeowners to default on their mortgages.

During the housing boom, many households chose to finance their homes with adjustable rate mortgages (ARMs). With adjustable interest rates resetting higher and home prices falling, many households, especially those borrowers who have less than perfect credit (subprime borrowers), are having difficulty making their payments. The issues in the subprime mortgage market caused a tightening of lending standards. Tighter lending standards have made it more difficult for households to purchase a home or refinance an ARM into a traditional fixed rate mortgage (FRM). Therefore, some homeowners are forced to sell their houses below market value or default on their loans.

In 2009, a record number of almost three million properties nationwide filed for foreclosure, up 21.2 percent from 2008.[31] More foreclosures are expected as five-year ARMs that originated in 2005 are scheduled to have their rates reset in 2010. As of November 2009, about 5.5 percent of all existing first-lien owner-occupied subprime ARMs were scheduled to reset within the next twenty-three months, with an additional 20.6 percent of first-lien owner-occupied Alt-A ARMs scheduled to reset within the next twenty-three months.[32]

Rising new foreclosures and tightened lending standards have left a significant number of homes on the market. The national inventory of new homes rose from an average of 8.4 months in 2007 to 10.7 months in 2008 and continued to rise further to 12.4 months in January 2009. Similarly, the inventory of existing homes rose from an average of 8.7 months in 2007 to 10.6 months in November 2008 (see Figure 26).

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[30] First American CoreLogic's data report is based on 47 million properties that have a first and/or second mortgage, which account for over 90 percent of all mortgages in the U.S. The data was revised for the third quarter of 2009 to adjust for amortization and home equity lines of credit (HELOC). As a result, the third quarter estimates are not comparable to prior quarters. Using the old methodology, the third quarter estimate of negative equity would be 33.8 percent. See First American CoreLogic, "First American CoreLogic's Negative Equity Data Report" (as of November 2009).

[31] RealtyTrac Staff, "Year-end Report Shows Record 2.8 million U.S. Properties with Foreclosure Filing in 2009," *RealtyTrac.com* (Irvine, CA), January 14, 2009, http://www.realtytrac.com/contentmanagement/pressrelease.aspx?channelid=9&accnt =0&itemid=8333.

[32] Federal Reserve Bank of New York, "United States Credit Conditions," November 2009. http://data.newyorkfed.org/creditconditions/.

As home sales slowed and inventory rose, homebuilders pulled back on housing production. After reaching over two million starts in 2005, housing starts fell to a record low of 479,000 (annualized rate) in April 2009. As a result, new single-family homes available for sale were at record lows in December 2009 at 231,000, the lowest since April 1971. Housing starts are expected to rebound in 2010 to just under 800,000 units.

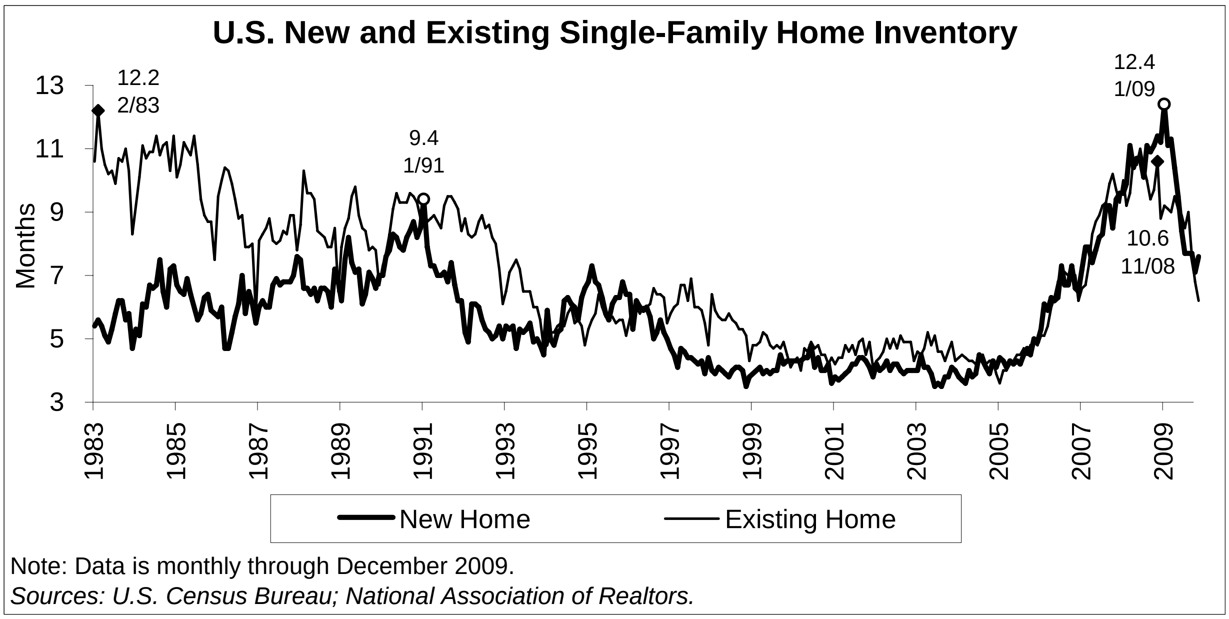

Figure 26

Low mortgage rates and declining home prices as a result of foreclosures have led to a significant improvement in housing affordability in the past year. High housing affordability along with the federal housing tax credit program, which gives a tax credit of up to $8,000 for first-time homebuyers, appears to have attracted a large number of first-time homebuyers and helped stimulate home sales. Existing home sales grew seven out of the last nine months, leading to lower home inventory in recent months. Between 1990 and 2000, new home inventory averaged only 5.5 months, while existing home inventory averaged 6.4 months. Currently, existing home inventories stand at almost seven months, while new inventory stands at about eight months.

Current improvement in the housing market has been largely driven by federal support programs. Further, improvement in the housing market will rely heavily on housing inventory as well as the condition of the labor market. Going forward, it is expected that activity in the housing market will continue to remain slow. Home sales have been increasing due to high affordability and the federal support program, and are anticipated to continue to improve. However, weak employment and income growth outlooks will likely prolong the current correction in the housing market and restrain home prices from appreciating any time soon. Home prices are expected to remain stable at least through the first half of 2010.

Government Spending

Federal government spending was the predominant driver of overall government spending growth in 2008, though state and local government spending accounted for more than 60 percent of total government spending. Federal government spending increased 7.7 percent in 2008 after growing 1.3 percent in the prior year due to significant growth in both defense and nondefense spending. Defense spending growth was mainly attributed to higher growth in the compensation of civilian and military employees, larger outlays for services related to weapons and personnel support, and more spending on equipment and software. Growth in nondefense spending arose from an increase in compensation and public investment.

Due to slower growth in public investment spending and significantly lower non-compensation expenditures, federal government spending growth in 2009 slowed to an estimated 5.2 percent. The 2010 Census will temporarily boost the federal government civilian workforce in the first half of the year augmenting nondefense payroll expenses.[33] However, slower growth in the compensation of military employees and defense investment spending will contribute to federal government spending decelerating further to 4.2 percent in 2010. Once Census workers are off the federal payroll, outlays for nondefense compensation are anticipated to decline. Hence, federal government spending is forecast to decline 0.3 percent as the government continues to restrain spending on compensation for defense and nondefense personnel as well as public investments in 2011 (see Figure 27).

[33] In January 2010, the U.S. Census Bureau had hired 9,000 temporary workers for the 2010 Census. In total, 1.2 million temporary Census workers are expected to be hired in 2010. See U.S. Department of Labor, Bureau of Labor Statistics, "The Employment Situation – January 2010," *News Release*, February 5, 2010.

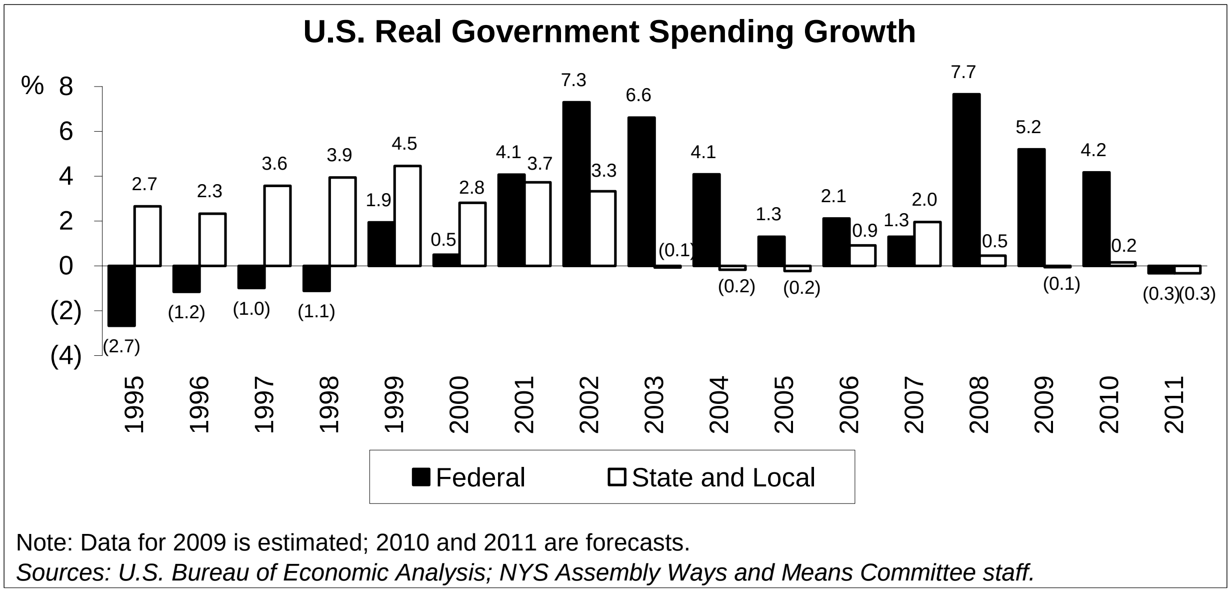

Figure 27

The federal budget deficit increased to $454.8 billion or 3.2 percent of GDP in Federal Fiscal Year (FFY) 2007-08 and grew to $1.4 trillion or 9.9 percent of GDP in FFY 2008-09 (see Figure 28). This was the largest federal deficit as a share of GDP since 1945. The considerable gap in the federal budget stemmed from declining tax receipts and substantially higher spending. Federal tax receipts declined 16.6 percent with individual income tax receipts falling 20.1 percent, and corporate income tax revenues declining even more sharply by 54.6 percent in FFY 2008-09 compared to the prior fiscal year.[34] Meanwhile, outlays by the federal government rose 18.3 percent.[35]

The Troubled Asset Relief Program (TARP), included in the Emergency Economic Stabilization Act of 2008 that contained provisions for the bailout of insolvent financial institutions, has contributed to the expansion of the budget deficit.[36] The extension of unemployment benefits due to a higher unemployment rate and an increase in the federal government's share of Medicaid costs authorized by the American Recovery and

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[34] U.S. Department of Treasury, Financial Management Service, *Final Treasury Statement of Receipts and Outlays of the United States Government*, September 2009, http://www.fms.treas.gov/mts/mts0909.pdf.

[35] For the first quarter of federal fiscal year (FFY) 2009-10, the federal budget deficit was $388.5 billion, up $56 billion from the comparable period in FFY 2008-09. However, the deficit is projected to be 9.2 percent of GDP or $1.3 trillion in FFY 2009-10. See, Congress of the United States, Congressional Budget Office, *The Budget and Economic Outlook: Fiscal Years 2010-2020*, January 2010. See also, Department of Treasury, *Monthly Statement of Receipts and Outlays of the U.S. Government, Financial Management Service*, January 2010, http://www.fms.treas.gov/mts/mts1209.pdf.

[36] Emergency Economic Stabilization Act of 2008, Public Law 110-343, 110th Congress, October 3, 2008.

Reinvestment Act of 2009 (ARRA) have expanded the federal deficit. In addition, the Making Work Pay tax credit provisions in the ARRA are partly credited for the falloff in income and payroll tax receipts. Though spending related to these fiscal policies has expanded the federal deficit, they have provided support to overall economic growth. Long-term, however, an expanding budget deficit poses certain risks to economic growth.

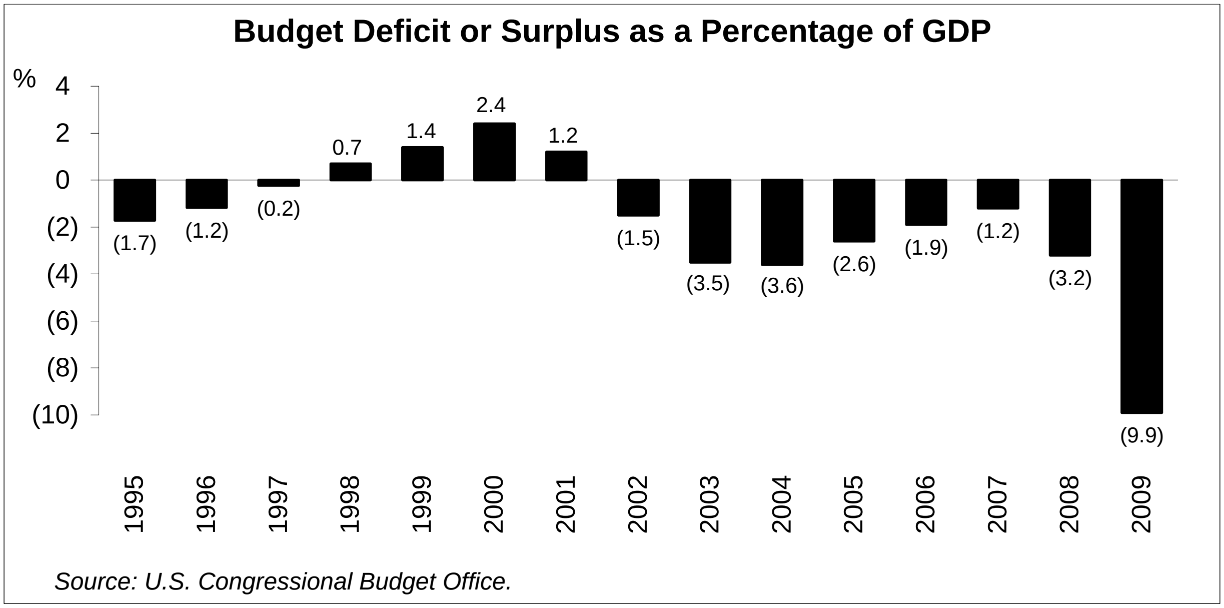

Figure 28

State and local government spending growth slowed to 0.5 percent in 2008 due to lower revenues that discouraged investment in structures, and equipment and software compared to 2007. Historically, states try to maintain spending levels in an economic downturn by initially drawing down reserve funds. However, as revenue expectations are diminished and "rainy day" funds are depleted, spending cutbacks such as a hiring freeze or layoffs, canceling or delaying of capital projects, renegotiation of debt, pension and health benefits, cuts in public safety and human services, and across-the-board cuts become necessary. Many states also raise taxes.[37] Since all states except Vermont operate under balanced budget requirements, these options are most readily used to alleviate the fiscal stress of lower revenues in a deteriorating economy.

[37] "Rainy day" funds were the equivalent of 10.5 percent of general fund budgets for states or $69 billion at the end of fiscal year 2007. See, Center on Budget and Policy Priorities, "States in Trouble Due to Economic Downturn," *Policy Points*, (Updated January 29, 2009).

Generally, state and local government spending continue to suffer even after recessions have ended. While policymakers' response to the recent recession has mirrored that of the past, though the magnitude has been unprecedented, the hardship faced by state and local governments will likely prolong into coming years given that the recent recession has been deeper and longer. In 2001, state and local government spending growth increased 0.9 percentage point from the prior year, then slowed by only 0.4 percentage point in 2002. Growth fell 3.4 percentage points in 2003 from 2002 and continued to decelerate until 2006. The falloff in state and local government spending was primarily due to a significant drop in income tax collections, which meant states and localities had to make necessary adjustments to meet budgetary requirements. As state deficits rose, Congress enacted a fiscal relief package that included $20 billion in assistance to states.[38] The decline in state and local spending from 2003 to 2005 could possibly have been higher without the fiscal relief for the states.

The national recession that began in December 2007 has taken its toll on state and local governments and triggered widespread cutbacks. Tax receipts for states declined 10.9 percent in the third quarter of 2009 from the same quarter in 2008, the third consecutive quarterly decline.[39] Lower home prices continue to put downward pressure on property taxes. Personal income tax collections have faltered dramatically due to a weak labor market, job losses, and fewer hours worked, while restrained consumer spending has lowered sales tax collections. Corporate income tax collections have dropped sharply also, due to falling corporate earnings.

States with adopted budgets for State Fiscal Year (SFY) 2009-10 have already closed gaps and are still facing more shortfalls. Over SFY 2009-10 and SFY 2010-11, these deficits are expected to be at least $350 billion.[40] Even with assistance from the federal

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[38] The fiscal relief package included $10 billion for Medicaid assistance and $10 billion in grants based on state populations. See, the Jobs and Growth Tax Relief Act Reconciliation Act of 2003, Public Law 108-27, 108th Congress, May 28, 2003.

[39] In the second quarter of 2009, tax receipts fell 16.6 percent; personal income tax collections fell another 27.5 percent after falling 17.7 percent in the first quarter; corporate income tax receipts grew 2.9 percent after declining 20.1 percent in the prior quarter; and sales tax collections dropped an additional 9.5 percent, the third quarterly decline. In the third quarter of 2009, personal income tax fell 11.8 percent, corporate tax collections declined 22.6 percent, and sales tax fell 8.9 percent. See, Lucy Dadayan and Donald J. Boyd, "State Tax Revenues Show Record Drop for Second Consecutive Quarter," *State Revenue Report*, Rockefeller Institute of Government, no. 77, October 2009; "Recession or No Recession, State Tax Revenues Remain Negative," *State Revenue Report*, Rockefeller Institute of Government, no. 78, January 2010.

[40] The $350 billion includes gaps already closed and projected deficits. See, Iris J. lav, Nicholas Johnson, and Elizabeth McNichol, "Additional Federal Fiscal Relief Needed to Help States Address Recession's Impact," Center of Budget and Policy Priorities, July 2009.

government, widening budget gaps will require additional reductions in services and programs provided by state and local governments, higher taxes, and further layoff of employees. Hence, the impact of the portion of the ARRA that has been allocated to state and local governments in the form of matching funds for Medicaid spending, block grants, and funds for public works projects, will to some extent cushion against adjustments states have to make elsewhere to combat expanding deficits.[41]

Tightened credit markets have amplified the strains on some states that rely on short-term borrowing to provide funds for day-to-day government operations. Prohibitive lending rates have led states and municipalities to delay or abandon offerings. Though the credit markets have showed signs of easing, many states have sought funding for capital projects through the Build America Bonds program authorized under the ARRA that provides financing at lower costs.[42]

State and local government spending fell an estimated 0.1 percent in 2009 and is forecast to increase only 0.2 percent in 2010, despite a boost from the ARRA. As the fiscal stimulus wanes and states continue to limit spending, state and local government spending is forecast to decline 0.3 percent in 2011.

Exports and Imports

After growing six years in a row, U.S. exports declined sharply in the midst of the global recession. Export growth slowed to 5.4 percent in 2008. The global recession caused exports to decrease sharply in 2009, falling by an estimated 9.9 percent. Global economic recovery will help U.S. export growth in 2010 and 2011. Exports are forecast to grow 9.0 percent in 2010 and rise further by 6.9 percent in 2011.

Faced with the deepest recession in decades, U.S. imports are estimated to decline in 2009, falling an estimated 14.2 percent after declining 3.2 percent in 2008. As the U.S.

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[41] The National Income and Product Account (NIPA) definition of government spending does not include transfer payments such as Medicaid. However, spending on Medicaid is a major component of state spending. NIPA's definition is used for state and local government spending in this report.

[42] Many states have seen their credit rating adversely affected because of declining revenues. Moody's has placed all municipal bonds on a negative credit watch, which may be an indicator of a future credit downgrade for many municipalities. See, Securities and Financial Markets Association, Research Report, Research Quarterly, vol. iv, no. 8, August 2009, http://www.sifma.org/research/pdf/RRVol4-9.pdf; and Peter Schroeder, "BAB Program Has Seen $17.4 billion From 34 States, Treasury Reports," *Bond Buyer*, July 21, 2009, http://www.bondbuyer.com/issues/118_138/-305515-1.html.

economy recovers from the recession, imports are forecast to grow 8.4 percent in 2010, and 7.5 percent in 2011 (see Figure 29).

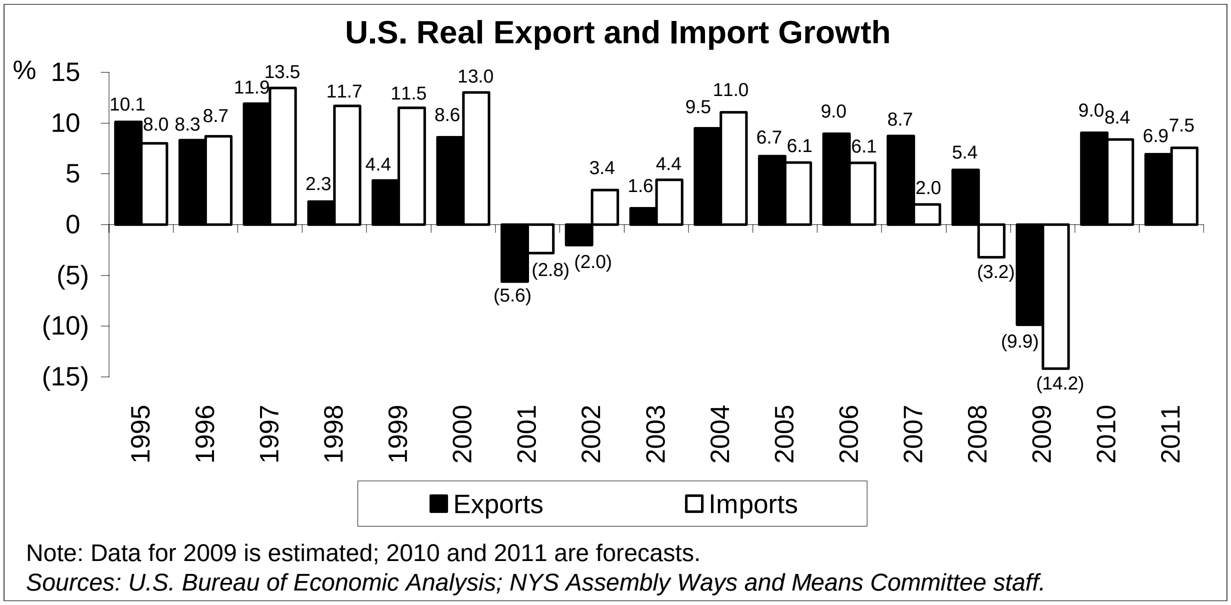


Figure 29

The U.S. dollar has depreciated for six consecutive years since 2003. This is due mainly to the worsening budget deficit and the current account deficit. Although the budget deficit improved significantly in FFY 2006-07 to the lowest level since 2002, continuing problems in the housing and credit markets and investment opportunities in emerging economies kept the dollar value from appreciating in 2008. The budget deficit deteriorated in FFY 2007-08 and worsened significantly in FFY 2008-09. This trend is expected to continue due to slow revenue growth and the associated costs of all government programs related to the economic stimulus package. As systemic risk in global financial markets rose, the dollar appreciated sharply from the second half of 2008 until early 2009.

Downward pressure from increasing worries among holders of mounting U.S. debt has caused the dollar to depreciate starting from the second quarter of 2009. As this trend is expected to continue, the U.S. dollar is forecast to depreciate in 2010 and 2011 after appreciating 4.1 percent in 2009 on a yearly average basis (see Figure 30).

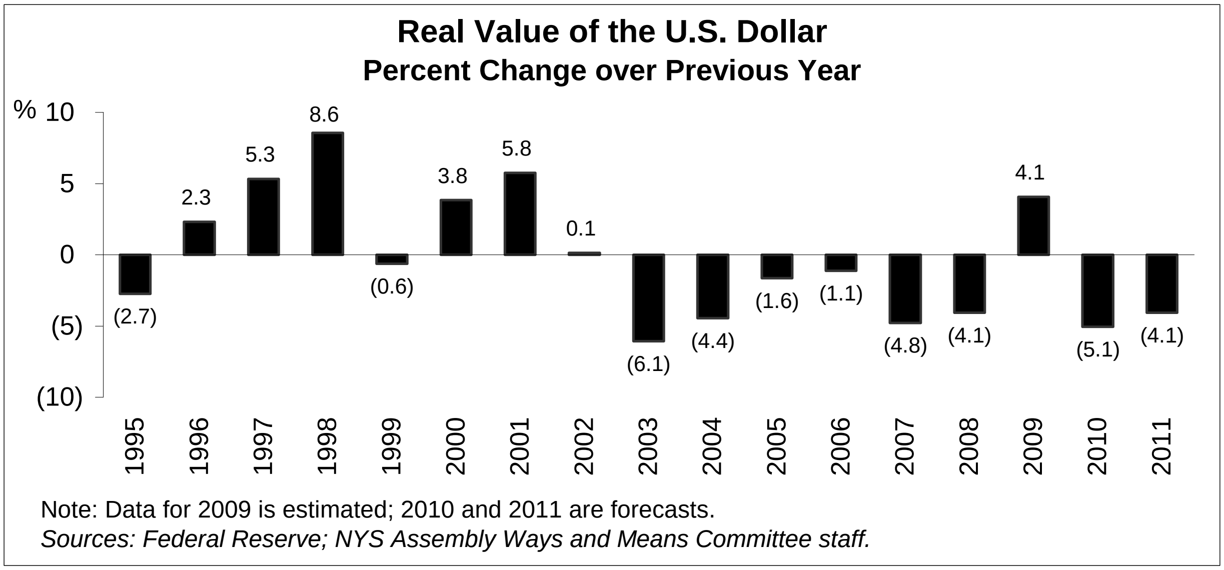


Figure 30

The declining dollar together with strong demand for U.S. goods and services, and more recently, a sharp decline in oil prices from mid-2008 through early 2009 has led to significant improvement in the U.S. trade deficit. As a result, the current account deficit declined from a record high of $859.2 billion in the third quarter of 2006 to $432.1 billion in the third quarter of 2009 (see Figure 31).

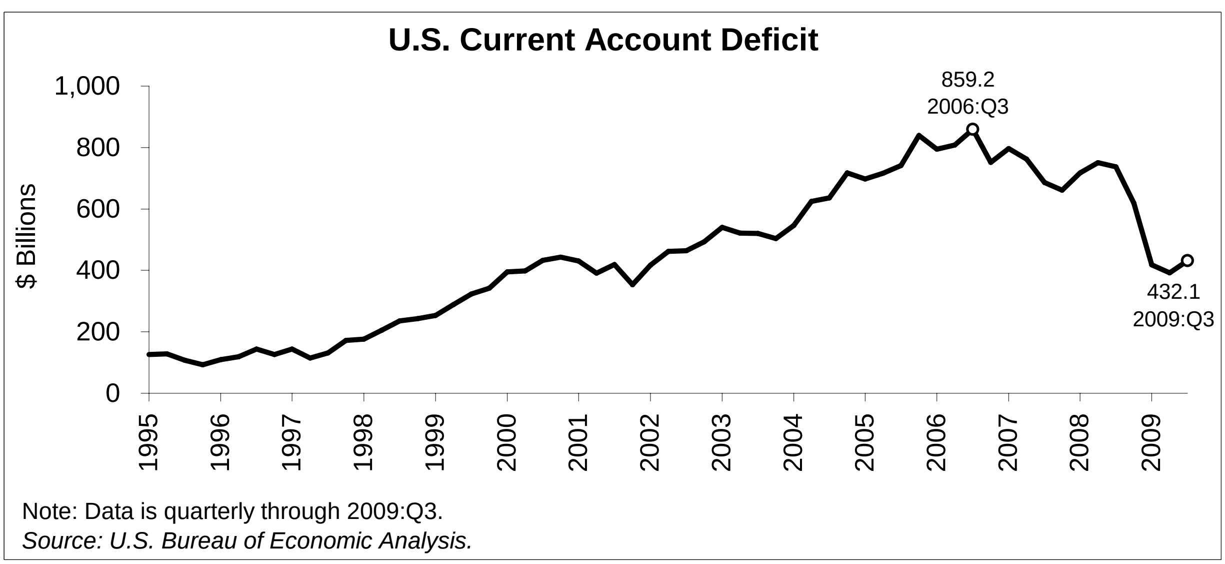


Figure 31

After years of robust growth, the world economy entered recession in 2009, with most advanced countries and a number of developing countries already in recession. Japan's economic growth is estimated to have declined sharply by 5.6 percent in 2009. The Canadian economy, the largest trade partner for the United States, is estimated to have fallen 2.4 percent in 2009. Germany's economy, the largest economy in Europe, is estimated to have declined 4.9 percent in 2009.[43] The slowdown of Germany and other major economies in Europe was a drag on the economic performance of the euro area. The euro economy is estimated to have declined 3.9 percent in 2009. The global recession led to a sharp decline in global trade in the final quarter of 2008 through the first half of 2009 (see Figure 32).

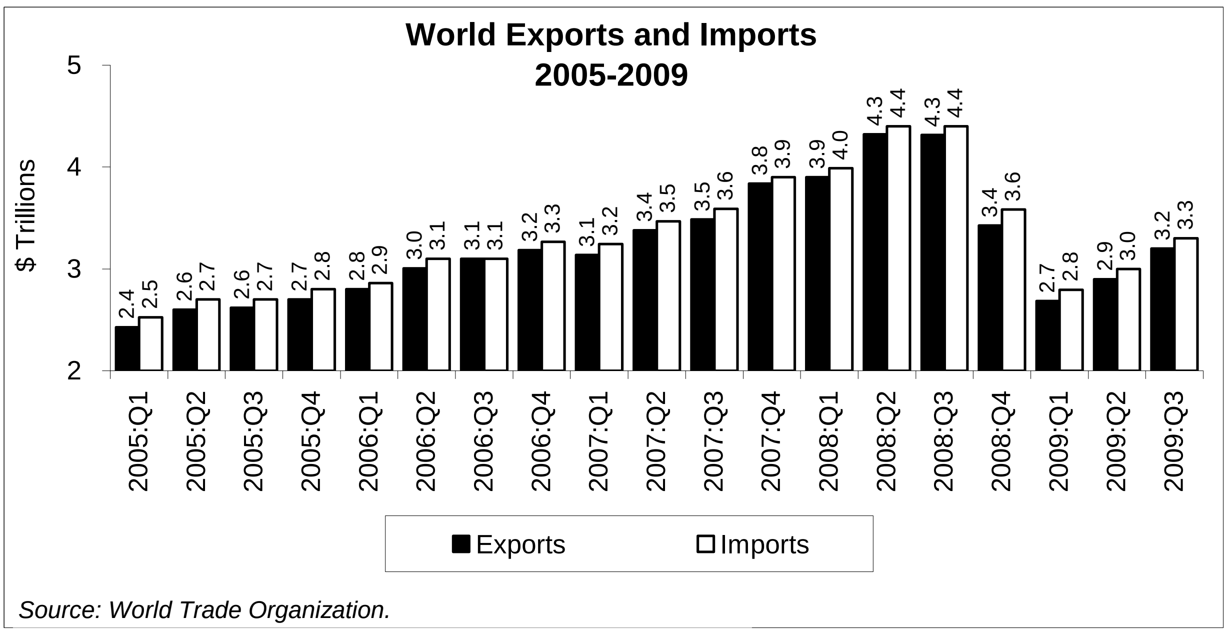


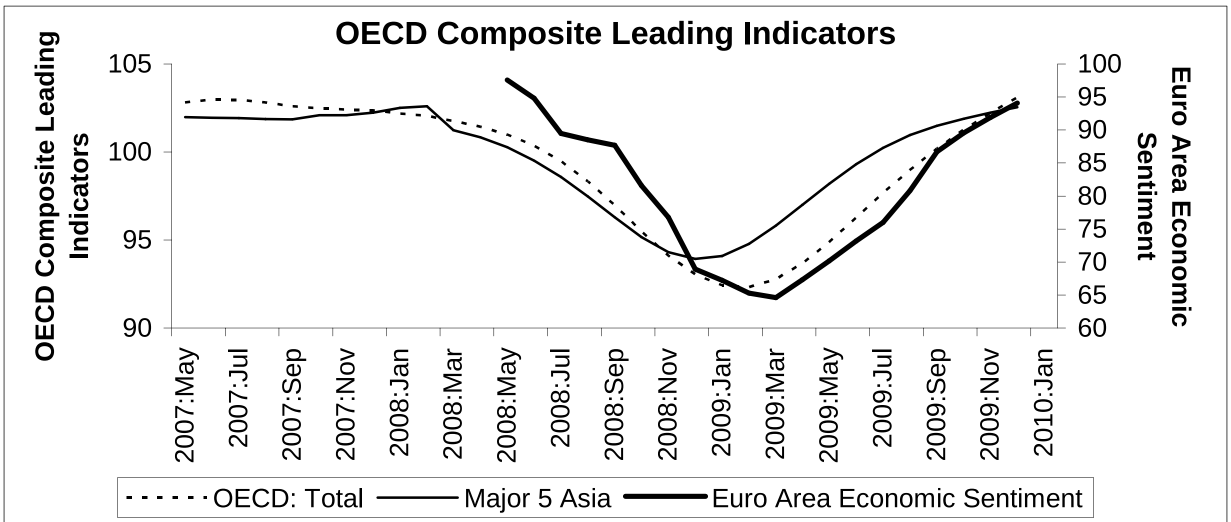
Figure 32

Hit with slow growth in demand for exports and high inflation, much of the developing world also grew slower in 2009 than 2008. China, the largest U.S. trading partner in Asia, grew an estimated 8.2 percent in 2009 and is forecast to grow 9.7 percent in 2010. Mexico's economy was hit particularly hard by the U.S. recession and is estimated to have declined sharply by 6.9 percent in 2009. Many countries in South America were also in recession. The Brazilian economy, the largest economy in South America, is

[43] "Blue Chip International Consensus Forecasts," *Blue Chip Economic Indicators*, vol. 35, no. 2, February 10, 2010.

estimated to have grown just 0.2 percent in 2009 but is forecast to grow 4.9 percent in 2010.[44]

Signs of an economic recovery have been visible globally in recent months. In Europe, euro area economic sentiment, industrial confidence, and consumer confidence have been continuously improving after falling to record lows in March 2009.[45] Similarly, the composite leading indicators (CLI) for the Organisation for Economic Co-operation and Development (OECD) countries and the Major 5 Asia have been increasing since early 2009, pointing to a global economic recovery (see Figure 33).[46] Although the recent debt crisis in Greece has raised concern about the global recovery, it is expected that the problem will be contained and will not spread to other economies. Most countries are expected to post positive and much higher growth in 2010 than in 2009.



Note: Data is monthly. Data for OECD Composite Leading Indicators is from April 2007 to December 2009; data for Euro Area Economic Sentiment is from May 2008 to January 2010.
Sources: Organisation for Economic Co-operation and Development (OECD); European Commission.

Figure 33

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[44] Ibid, Blue Chip.

[45] European Commission, "Key Indicators for the Euro Area, February 2010," Economic Databases and Indicators, Economic and Financial Affairs, February 11, 2010.

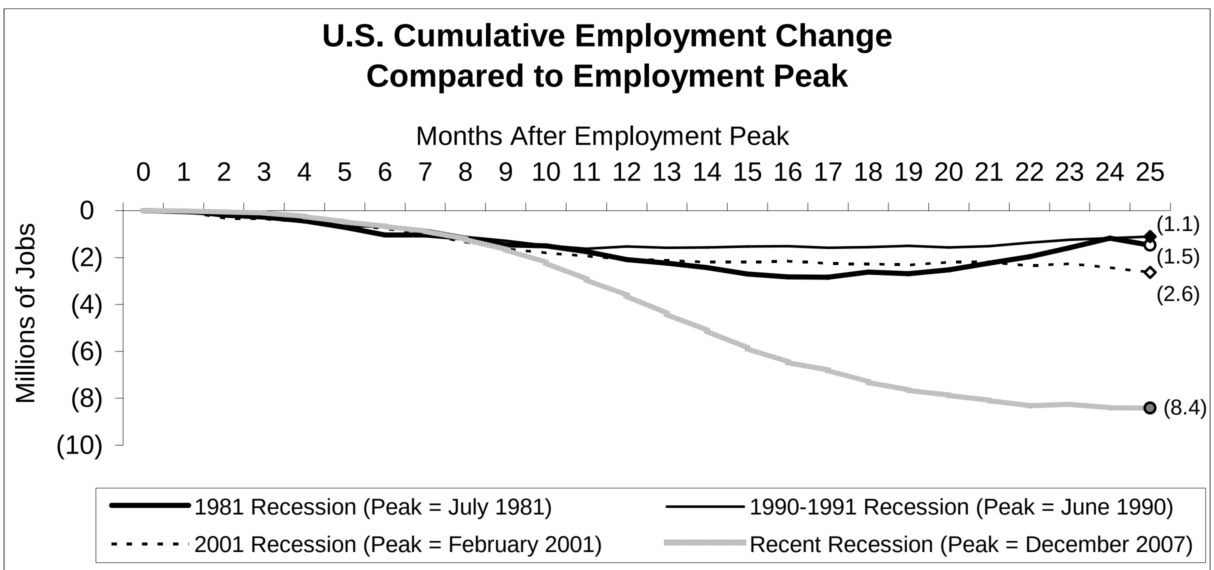
[46] The OECD composite leading indicator series includes the following twenty-nine countries: Australia, Austria, Belgium, Canada, Czech Republic, Denmark, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Japan, Korea, Luxembourg, Mexico, Netherlands, New Zealand, Norway, Poland, Portugal, Slovak Republic, Spain, Sweden, Switzerland, Turkey, United Kingdom, and United States. The Major 5 Asia includes China, India, Indonesia, Japan and Korea. See, Organisation for Economic Co-operation and Development, "Composite Leading Indicators (CLIs) for OECD Countries and Major Non-Member Economies January 2010 update," January 8, 2010.

As the U.S. and the world economies are expected to continue to recover in 2010, U.S. imports are anticipated to grow faster than exports once again in 2011. As a result, net exports will likely deteriorate throughout the forecast period and will adversely influence U.S. economic growth in 2010 and 2011.

Employment

As the recession unfolded, several factors contributed to a weak labor market, with many sectors being hit hard. Although the housing market has shown some signs of stabilization, construction and other housing-related jobs are still suffering. Finance and insurance employment succumbed to the fallout from the credit crunch and continues to be hampered even as the financial markets are starting to recover. In addition, as consumers continue to cautiously spend, employment in most of the sectors that supply everyday goods and services such as retail sales has declined.

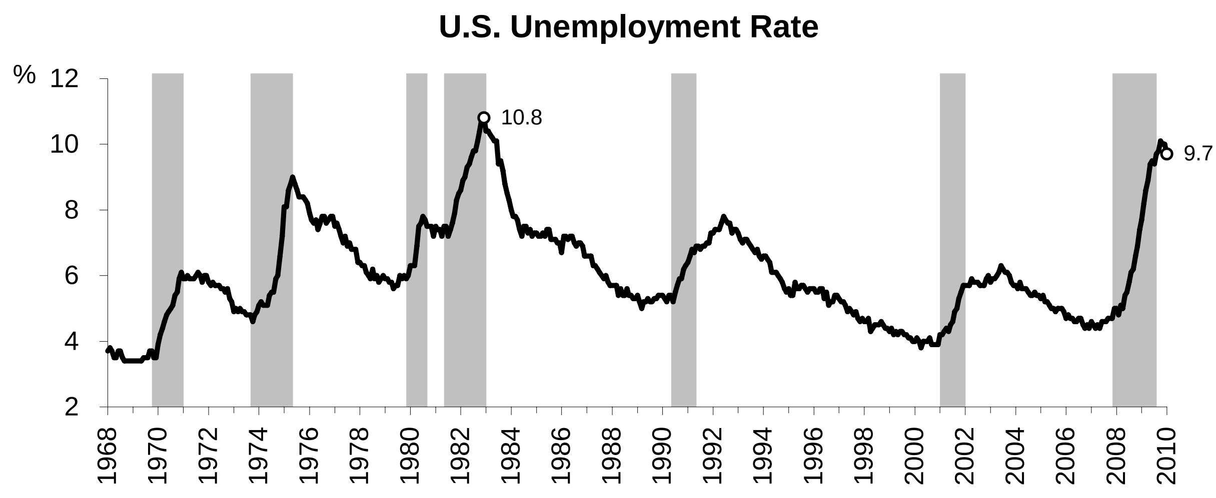
The depth of the recent recession has been especially felt in the labor market, as employment has declined much more than in some past recessions, and unemployment remains high. Between December 2007 (when employment peaked) and January 2010, the economy lost 8.4 million jobs. In the three recessions prior to the recent one, cumulative job losses did not reach 3 million before starting to recover (see Figure 34).



Note: Data is through January 2010.
Source: U.S. Bureau of Labor Statistics.

Figure 34

The unemployment rate was 9.7 percent in January 2010, after hitting 10.1 percent in October 2009 (see Figure 35). The high rate reflects the large number of workers who lost their job and remain unemployed. Due to the jobless recovery, the unemployment rate is expected to abate slowly.



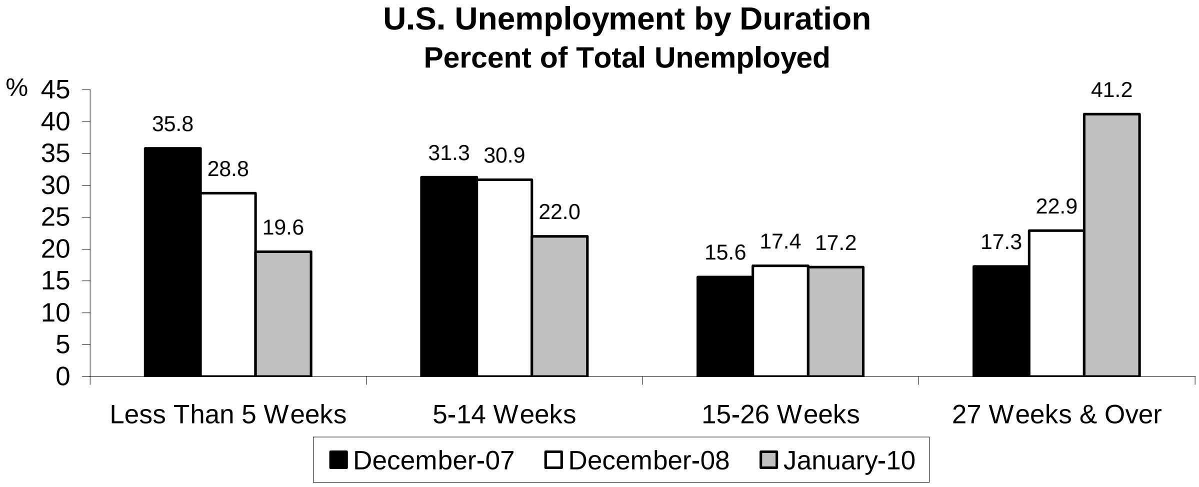
Note: Data is monthly through January 2010. The shaded areas represent recessions.
Source: U.S. Bureau of Labor Statistics.

Figure 35

In addition to larger numbers of employees being laid off, individuals are remaining out of work for a longer period. The exhaustion rate for unemployment benefits is at an all-time high since the series started in 1972. In January 2010, the exhaustions rate for regular federal benefits was 54.0 percent.[47] The percentage of unemployed persons who have been unemployed longer than twenty-seven weeks was 41.2 percent in January 2010, more than double the percentage than when employment peaked in December 2007. Historically, this number is also quite high. Before the recent recession, the month with the highest percentage of persons unemployed more than twenty-seven weeks was June 1983, when 26 percent were unemployed for that long. The longer duration of unemployment presents challenges for those out of work, as after an extended period they will exhaust state and federal extensions to unemployment benefits (see Figure 36).[48]

[47] An exhaustions rate of 50 percent can be thought of as: for each 100 people who became unemployed six months ago, 50 of them have exhausted benefits in the current month. For a more technical definition, see http://www.workforcesecurity.doleta.gov/unemploy.

[48] As of December 19, 2009, several extensions to unemployment insurance had been made by both the federal government and states. For example, in New York State those covered under unemployment insurance were eligible for 26 weeks of regular benefits, and some claimants were able to qualify for all or a



Note: The Bureau of Labor Statistics classifies people as unemployed if: they do not have a job, have actively looked for work in the prior four weeks, and are currently available for work.
Source: U.S. Bureau of Labor Statistics.

Figure 36

Initial and continuing claims have been offering somewhat of a stabilizing picture for unemployment. The four-week moving average for initial claims has been on a downward trend since April 2009, coinciding with reports of lower employment losses in the past few months compared to early 2009. However, claims still remain above the benchmark level of 400,000, indicating that the labor market recovery still has a long way to go (see Figure 37).

Continuing claims also show some signs of recovery, although the picture could be muddied by claimants who have exhausted benefits. Although volatile, continuing claims have been following an overall downward trend since July 2009, after peaking in late June (see Figure 38). It is unclear how much of the drop in continuing claims are due to claimants who have exhausted benefits. Therefore, amid the high level of claims coupled with a longer duration of unemployment than usual, the labor market will have a long road to recovery regardless of the official end date of the recession.

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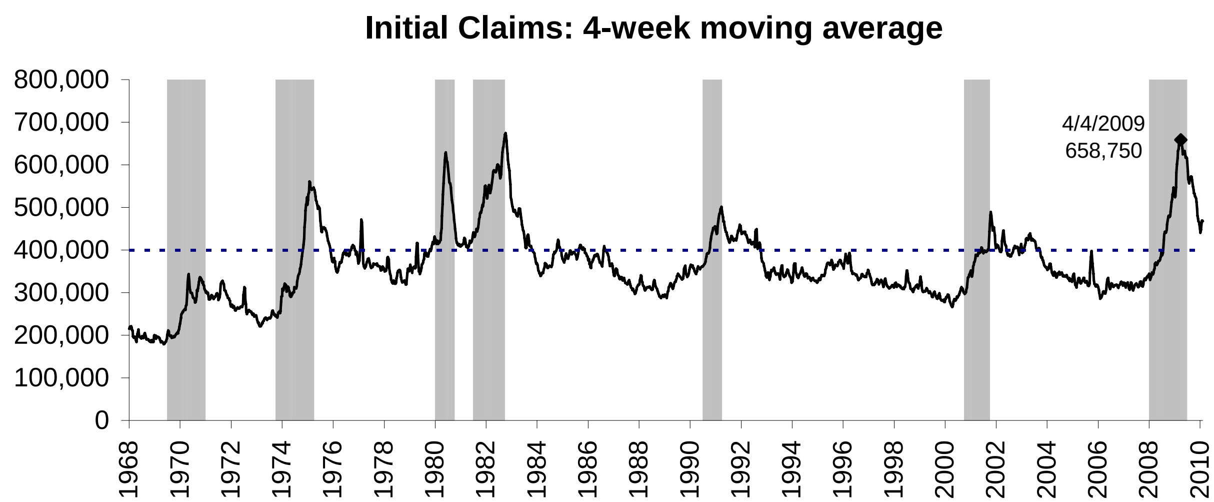
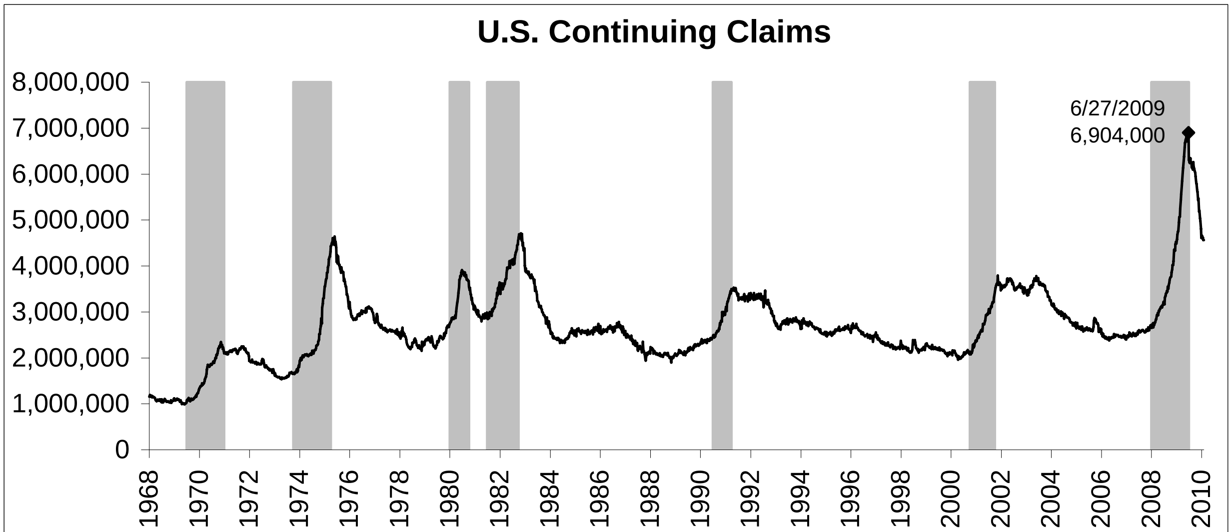
portion of 53 weeks of emergency unemployment compensation and 20 weeks of extended benefits. Some workers were also eligible to receive a $25 increase in benefits per week under the Federal Additional Compensation Program provisions in the American Recovery and Reinvestment Act of 2009, www.labor .state.ny.us and www.bls.gov.



Note: Data is weekly through February 13, 2010. Dotted line represents the benchmark level. The shaded areas represent recessions.
Source: U.S. Department of Labor.

Figure 37



Note: Data is weekly through February 6, 2010. The shaded areas represent recessions.
Source: U.S. Department of Labor, Office of Workforce Security.

Figure 38

Total national payroll employment declined by 0.6 percent in 2008 and fell 4.3 percent in 2009. For comparison, employment fell 1.1 percent in 2002. Employment is expected to decline another 0.6 percent year-over-year in 2010 as hiring remains sluggish (see Figure 39). Near-term, employment will be helped by the hiring of temporary Census workers by the federal government. In 2011, employment is expected to grow 1.3 percent.

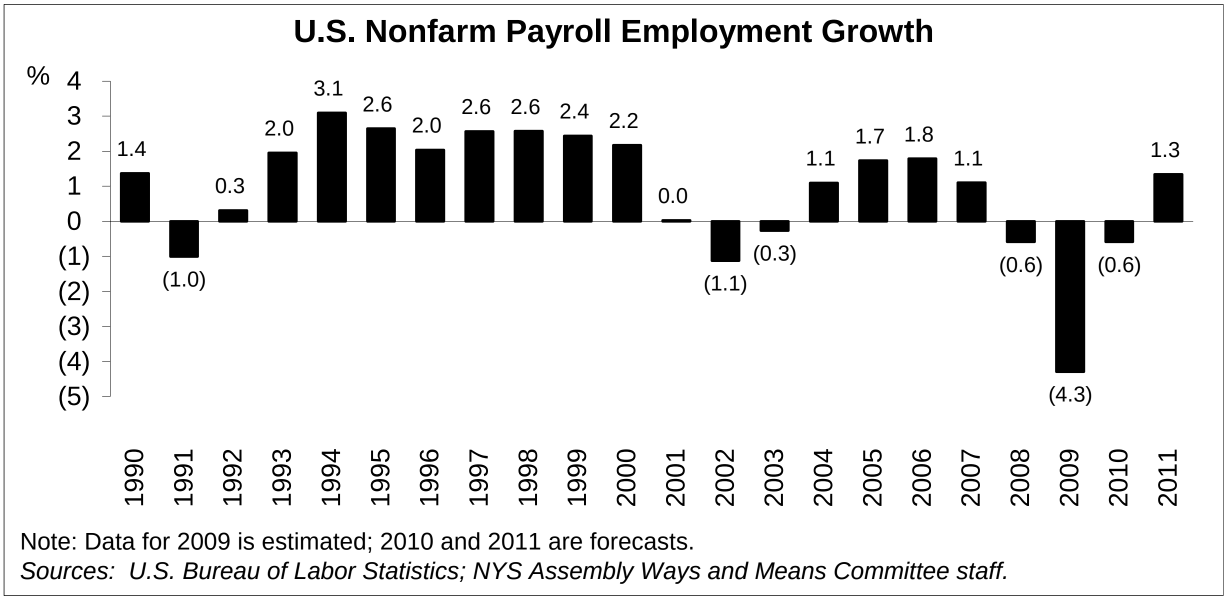


Figure 39

In addition to the reasons previously discussed in this report, employment may not reverse course as fast as in previous recoveries due to fundamental differences in the economy. Some of these factors may also be attributed to the jobless recovery seen after the 2001 recession. Productivity gains have made it possible for companies to do more with less labor input, and technological gains that may not have been possible during past recoveries are available to businesses today. In addition, global competition has forced companies to cut costs, and labor costs are a natural place for firms to try to streamline.

Employment losses have been widespread throughout many sectors of the economy (see Table 2). While some sectors still added jobs in 2008, only two added jobs in 2009: education and health, and government. As the recession deepened in early 2009, sectors that had previously had employment growth, such as leisure and hospitality, professional services, and management of companies also began to lose jobs.

Table 2

U.S. Employment by Sector (Percent Change)	Actual 2008	Estimate 2009	Forecast 2010	Forecast 2011
Total	**(0.6)**	**(4.3)**	**(0.6)**	**1.3**
Education and Health	2.8	1.8	1.9	2.2
Government	1.3	0.2	0.6	(1.0)
Leisure & Hospitality	0.1	(2.5)	(0.9)	1.9
Mgmt. of Companies	2.0	(2.6)	(2.1)	1.9
Professional Services	1.8	(3.7)	(0.5)	2.4
Finance & Insurance	(1.9)	(4.2)	(1.3)	0.9
Retail Trade	(1.5)	(4.9)	(0.9)	0.7
Transp. & Utilities[1]	(0.5)	(5.4)	(1.2)	2.3
Wholesale Trade	(1.2)	(5.4)	(0.8)	2.2
Information	(1.6)	(5.9)	(2.6)	(1.2)
Real Estate, Rental, & Leasing	(1.9)	(6.2)	(1.5)	1.5
Other Services[2]	(2.6)	(7.2)	1.6	2.9
Manufacturing[3]	(3.0)	(11.2)	(2.7)	0.6
Construction	(6.1)	(15.7)	(8.4)	4.8

[1] Transportation, Warehousing, and Utilities.

[2] Including Administrative, Support, and Waste Management Services.

[3] Including Mining and Logging.

Sources: U.S. Bureau of Labor Statistics, Current Employment Statistics (CES); NYS Assembly Ways and Means Committee staff.

Construction employment continued to fall drastically in 2009, after declining 6.1 percent in 2008. Since July 2007, construction employment has declined every month (seasonally adjusted data). Losses accelerated in late 2008 and early 2009, with over 100,000 construction jobs lost in each of the first four months of 2009 alone. The major subsectors of construction have all been hard hit as losses that began in the residential sector spread to the nonresidential sector. Construction employment in 2010 is not expected to grow from the 2009 annual average, a reflection of the slow housing market recovery and the weakness in commercial construction activity.

In 2009, manufacturing realized double digit employment declines, following a loss of 3.0 percent in 2008. Although manufacturing employment has been declining for decades, the fall during the recent recession has been exacerbated by the problems in the automobile industry. In December 2007, motor vehicle and parts manufacturing employment was 6.9 percent of total manufacturing employment. In January 2010, it was only 5.8 percent after losing 278,000 jobs since December 2007. The Cash for Clunkers program sponsored by the federal government may have provided some relief to the industry, allowing the manufacturers to either bring workers back from temporary layoffs or avoid laying off some staff all together. Going forward, auto manufacturers may be able to keep staff or hire new workers as inventories were drawn down as a result of Cash for Clunkers and may be replenished in anticipation of a pickup in demand.

The weak labor market has also caused problems in other parts of the economy. Because of the dire state of the labor market and continuing uncertainty regarding the recovery of employment, it has been difficult for many consumers to feel financially secure enough to spend.

Some sectors that are driven by consumer activity have typically held up well in previous recessions, with only slight employment losses during past recessions. For example, in 2002, leisure and hospitality employment fell 0.4 percent and then rose 1.6 percent in 2003. In 1991, the sector lost 0.3 percent of jobs, and then grew 2.0 percent in 1992. In 2009, leisure and hospitality employment is estimated to have declined 2.5 percent, the largest decline since the data series started in 1939. This is a direct reflection of consumers cutting back on leisure activities such as traveling and dining out. Although leisure and hospitality employment is predicted to fall 0.9 percent in 2010, the outlook for the sector remains dependent on the behavior of consumers throughout the forecast period.

Personal Income

Personal income growth has been sustained by a significant increase in social benefit payments by governments to households. As the economic downturn deepened in the second half of 2008 and persisted into 2009, wages and salaries, the main component of personal income, decreased drastically. In addition, other non-transfer income components fell sharply. The worsening job market exerted downward pressure on hourly wages and average hours worked as employers adjusted their workforce to the weakened economy. In 2008, personal income grew 2.9 percent after growing 5.6 percent year-over-year in 2007. Personal income fell an estimated 1.4 percent in 2009 as the increase in transfer income was outweighed by the sharp decrease in labor, dividend, and interest income (see Figure 40). This was the first decline in personal income since 1949.

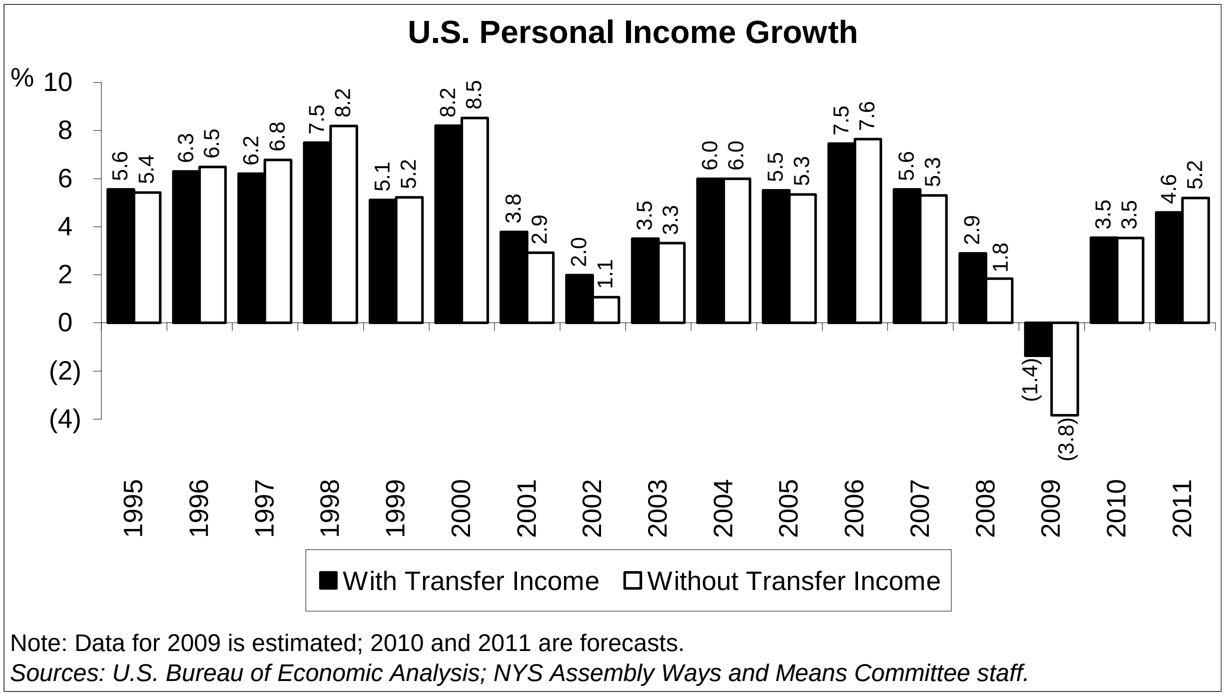


Figure 40

Growth in personal income is expected to improve only 3.7 percent in 2010 as the labor market continues to be strained by slow economic recovery. Historically, the increase in personal income predicted for 2010 is below the 4.6 percent annual average from 2002 to 2007, and almost 2 percentage points lower than the period after the 1990-91 recession to 2000. Personal income is forecast to grow a modest 4.0 percent in 2011 due to an improving labor market with higher wage and salary expectations, and increases from dividend and interest income.

Wages and salaries grew 2.1 percent year-over-year in 2008, after growing 5.6 percent in 2007. In 2009, wages and salaries declined an estimated 3.3 percent as hourly wages slowed and employment and average hours worked fell sharply (see Figure 41). The year-over-year decline in wages and salaries was the first since 1954.

Figure 41

Average weekly hours worked fell 2.9 percent from its peak in December 2006 to its lowest level in June 2009, while hourly compensation fell 1.5 percent peak to trough from October 2008 to February 2009 (see Figure 42). The deteriorating labor market has resulted in layoffs, a reduction in hours worked, and has made employers more resistant to raising wages. Furthermore, as the economy recovers and employers seek to expand their workforce, they will have a larger pool of workers from which to choose, putting more strain on wages and salaries growth.

Wages and salaries growth is forecast to be a mere 3.2 percent in 2010 as employment, hourly wages, and hours worked improve at a measured pace. In 2011, wages and salaries growth is expected to grow 3.7 percent due to gradual improvements in the labor market and other economic conditions. The expected expiration of the Economic Growth and Tax Relief and Reconciliation Act of 2001 (EGTRRA) and the Job and Growth Tax Relief Reconciliation Act of 2003 (JGTRRA) in 2011 have also impacted the forecast for 2010 and 2011.[49] In particular, certain wages and salaries that would have been paid

[49] The EGTRRA included provisions that reduced the income tax rates for most tax payers, eliminated the marriage penalty, provided greater tax deductions for education expenses and savings, increased the tax credit for tax payers with children, created a 10 percent tax bracket, and increased the amount of tax deduction that could be taken for IRA contributions. The JGTRRA included provisions that reduced the long-term capital gains tax rate and dividend income, increased tax deductions to small businesses, and extended most of the provisions in the EGTRRA, which would have been phased out prior to 2010. See Economic

out in the first quarter of 2011 are anticipated to be shifted to the fourth quarter of 2010 to take advantage of the lower tax rates.

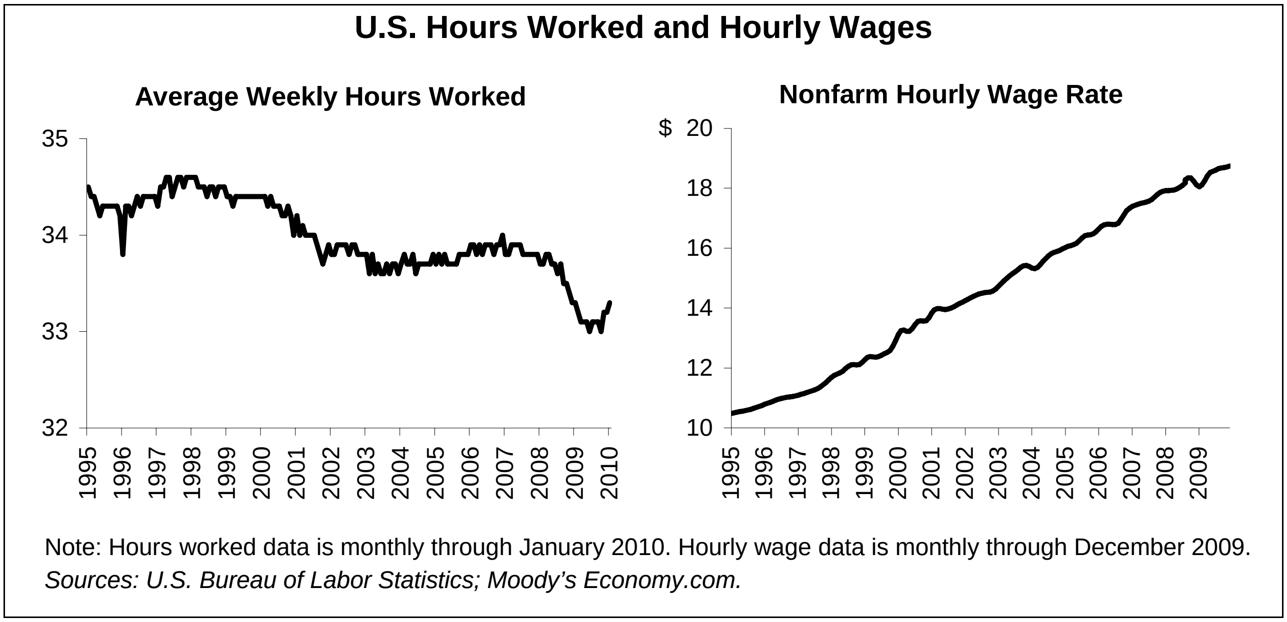


Figure 42

In 2008, transfer income growth was boosted by the tax rebates that households received as a result of the enacted Economic Stimulus Act of 2008. Growth in transfer income also reflected the extension of unemployment benefits that were provided to individuals who had exhausted their regular benefits.[50] Personal transfer income grew 9.2 percent in 2008.[51] Similarly, transfer income growth has been helped by social benefit payments associated with government programs that allocated billions of dollars in funds to households. These programs also included the extension of unemployment benefits along with additional benefits for healthcare. Personal transfer income is estimated to have grown 12.3 percent in 2009. As these benefits are exhausted, growth in personal transfer income will likely abate. Personal transfer income growth is forecast to slow to 3.6 percent in 2010 and 1.8 percent in 2011.

Growth and Tax Relief and Reconciliation Act of 2001, Public Law 107-16, 107th Congress, June 7, 2001; and Job and Growth Tax Relief Reconciliation Act, Public Law 108-27, 108th Congress, May 28, 2003

[50] The Supplemental Appropriations Act of 2008 has provisions that enact an additional thirteen weeks of unemployment compensation insurance benefits to individuals. See, the Supplemental Appropriations Act of 2008, Public Law 110-252, 110th Congress, June 30, 2008.

[51] The ARRA includes provisions that provide assistance to unemployed workers and struggling families, assistance for child support through the Temporary Assistance for Needy Families, increased medical support through Medicaid, and food assistance through the Supplemental Nutrition Assistance Program. See, the American Recovery and Reinvestment Act of 2009, Public Law 111-5, 111th Congress, February 17, 2009.

A slowing economy and deepening problems in the financial markets led to falling revenues and profits for many corporations. As a result, dividend income dropped 10.3 percent in 2008. In 2009, dividend income decreased an additional 19.2 percent as liquidity constraints coupled with challenging economic conditions led many firms to conserve cash and cut dividends to shareholders. As the economy continues to improve and firms become more profitable, dividend income is forecast to increase 5.3 percent in 2010 and 7.6 percent in 2011.

Personal interest income will continue to weigh on personal income as low interest rates have depressed interest income. Interest income growth slowed to 3.3 percent year-over-year in 2008 from 12.3 percent in 2007. As interest rates were kept low, personal interest income declined an estimated 5.4 percent in 2009. With a gradual increase expected in the federal funds rate and other interest rates starting from the second half of 2010, interest income is expected to increase 1.2 percent in 2010 and 6.9 percent in 2011.

Prices

Consumer prices grew 3.8 percent in 2008 as a direct result of pricing pressures from record high energy prices, which were eventually passed through to consumers when producers could no longer afford to absorb them (see Figure 43). Energy prices in 2009 were considerably lower than in the first half of 2008, as overall economic growth diminished significantly. Consumer prices are estimated to have declined 0.3 percent in 2009, the first decline since 1955. Consumer prices are forecast to increase 2.3 percent in 2010 and 2.1 percent in 2011 as economic growth rebounds and energy prices remain above the 2009 annual average level. Although finding an effective exit strategy is a challenge to the Federal Reserve, the inflation outlook in this report assumes that the Fed will successfully control the unwinding of current stimulus measures in a manner that prevents the emergence of rapid inflation.

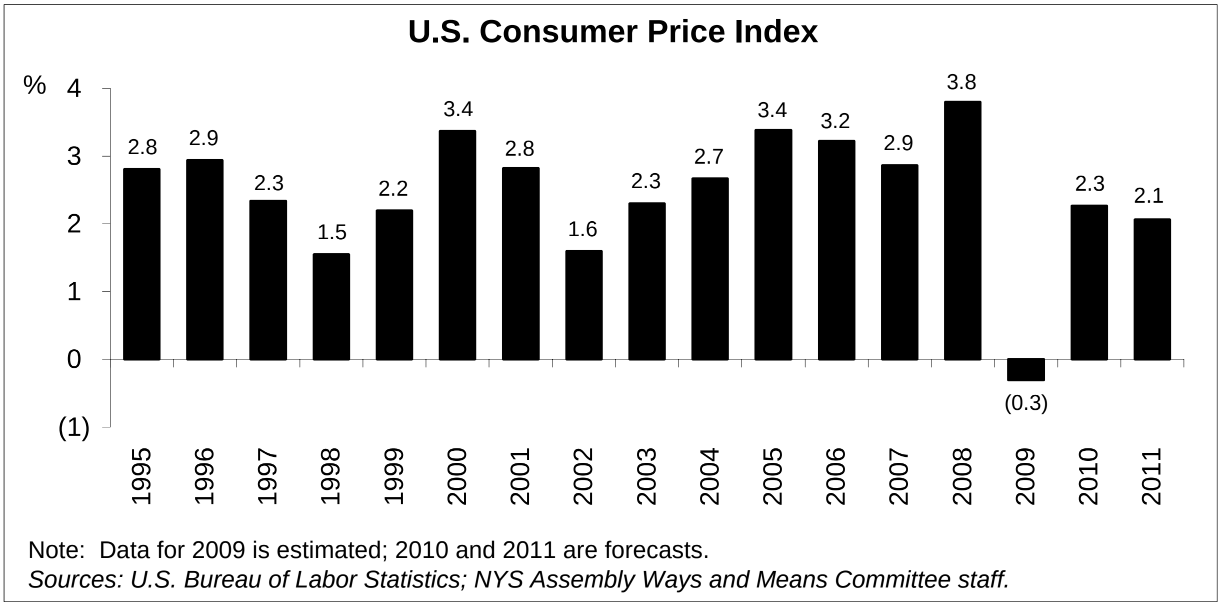


Figure 43

Falling oil prices in early 2009 largely explain lower prices in 2009, but oil prices continue to represent considerable risk to the forecast. The long-term outlook for oil prices is unclear and daily movements in prices may not necessarily reflect the true balance of supply and demand fundamentals in the long run (see following Energy Prices section).

Although a declining dollar has caused imports to become more expensive, putting upward pressure on prices, demand for imports fell during the recent recession limiting inflationary effects. In addition, other underlying fundamentals have also been working to keep core inflation in check. Productivity growth is estimated to have accelerated in 2009 to 3.0 percent from 1.8 percent in 2008. Productivity is also expected to increase in 2010, helping to keep downward pressure on inflation. Unit labor costs for the U.S. nonfarm business sector are estimated to have fallen by 0.9 percent in 2009 and are forecast to fall another 0.9 percent in 2010. This will help to put downward pressure on prices as businesses will not face an increase in labor costs, which account for a major portion of most firms' budgets. There is some risk, however, that as the economy recovers and stimulative policies continue to take hold, inflationary pressures will increase, causing prices to grow at a higher rate than expected.

Energy Prices

Energy prices, in particular the price of crude oil, continue to represent a critical risk to the overall health of the economy. Although prices are volatile on a short-term basis, long-term increases in overall energy prices present a direct hazard to both consumers and producers. Prices are affected by supply and demand fundamentals, and by other factors such as the decline of the dollar and commodities speculation. The volatility in energy prices is aided by the uncertainty of future conditions in energy markets. Some of the factors that continue to contribute to this uncertainty are weather-related phenomena such as hurricanes, geopolitical instability, and speculation.

Oil prices, as measured by the refiner acquisition cost of imported oil (RAC), averaged $92.77 in 2008, an increase of 38.4 percent from the 2007 average of $67.04 (see Table 3). As demand weakened in 2009 in response to slower economic growth, the

Table 3

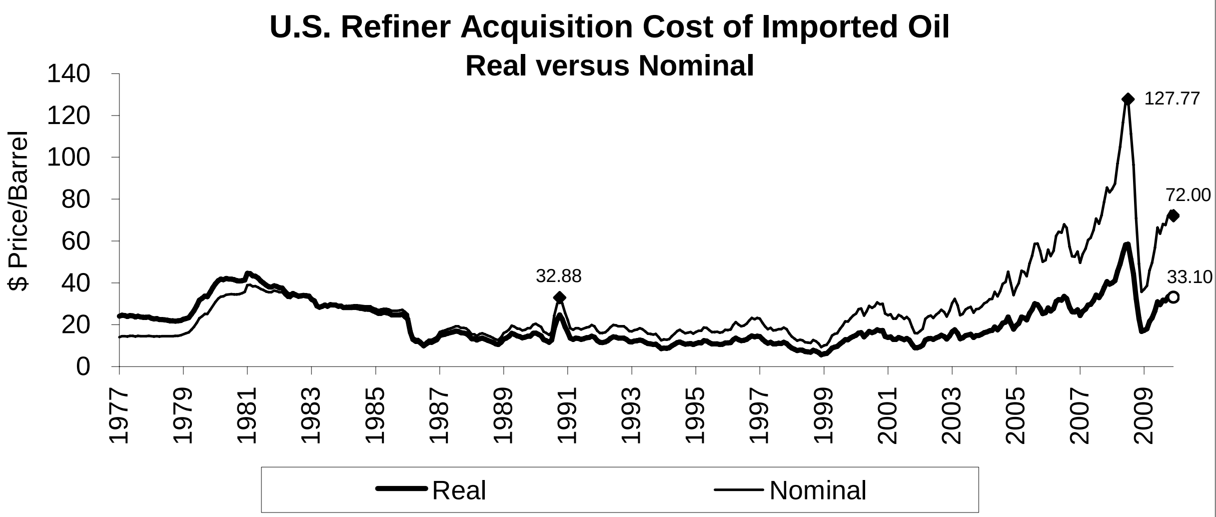
U.S. Energy Prices
Annual Average

		2005	2006	2007	2008	2009
Crude Oil - RAC	***Percent Change***	**36.1**	**20.8**	**13.6**	**38.4**	**(36.1)**
	Level	48.86	59.02	67.04	92.77	59.31
Crude Oil - WTI	***Percent Change***	**36.4**	**16.6**	**9.5**	**37.7**	**(37.8)**
	Level	56.64	66.05	72.32	99.55	61.95
Crude Oil - Brent	***Percent Change***	**42.6**	**19.4**	**11.2**	**33.8**	**(36.3)**
	Level	54.57	65.16	72.44	96.94	61.74
Natural Gas	***Percent Change***	**49.3**	**(23.4)**	**3.4**	**26.8**	**(54.1)**
	Level	8.81	6.75	6.98	8.85	4.06
Heating Oil	***Percent Change***	**45.5**	**11.1**	**12.4**	**40.4**	**(41.4)**
	Level	1.63	1.81	2.03	2.85	1.67
Electricity	***Percent Change***	**6.1**	**9.2**	**1.1**	**7.3**	**12.5**
	Level	8.7	9.5	9.6	10.3	11.59
Gasoline	***Percent Change***	**22.7**	**13.2**	**9.3**	**15.7**	**(28.0)**
	Level	2.27	2.57	2.81	3.25	2.34
NYS Gasoline	***Percent Change***	**22.1**	**14.3**	**7.4**	**22.6**	**(27.1)**
	Level	2.38	2.72	2.92	3.58	2.61
Diesel	***Percent Change***	**45.2**	**16.2**	**9.3**	**37.7**	**(43.2)**
	Level	1.67	1.94	2.12	2.92	1.66

Note: The refiner acquisition cost (RAC) of oil is a volume weighted average price of imported oils. The RAC daily spot price is generally less than the West Texas Intermediate (WTI) spot price, which is commonly reported in the media. Natural gas figures are average of monthly Henry Hub Spot Price, dollars per thousand cubic feet; heating oil figures are for No. 2 heating oil, NY Harbor Spot Price, dollars per gallon; electricity price is U.S. average for the residential sector, cents per killowatthour; gasoline prices are for retail, regular grade, dollars per gallon; diesel prices are for New York Harbor No. 2 Diesel Low Sulfur Spot Price FOB, dollars per gallon.

Source: U.S. Energy Information Administration.

RAC of oil averaged $59.31 in 2009 as prices climbed from lows of around $37 early in 2009 (see Figure 44). In 2010, the NYS Assembly Ways and Means Committee staff forecasts that the RAC of oil will be $77.00 (annual average). The potential for higher oil prices exists, as economic growth will lead to higher demand for oil, putting upward pressure on prices.



Note: Data is monthly through December 2009. Real values are inflation-adjusted using CPI (All Urban Consumers 1982-84 = 100). The refiner acquisition cost of oil is a volume weighted average price of imported oils. It is generally several dollars less than the West Texas Intermediate price, which is commonly reported in the media.
Sources: U.S. Bureau of Labor Statistics; U.S. Energy Information Administration.

Figure 44

Gasoline prices have also been highly volatile since 2007, and represent a threat to consumer spending as higher gasoline prices demand a higher portion of consumer's disposable income. In the summer of 2008, the national average price of gasoline was over $4.00, a level consumers were unaccustomed to planning for in their budgets. Since then, the price has generally been lower, decreasing to less than $2.00 in the beginning of 2009, and then increasing to $2.75 at the beginning of November 2009. Much of the future outlook for gasoline prices depends on the price path for crude oil.

Different regions in the nation are affected by different pricing pressures, and energy products are one of the areas where households in different parts of the country may face different costs. Gasoline offers an example of an energy product that is also used nationwide, but is often priced differently by region. The difference may be large at times. For example, for the week of February 15, 2010, regular gasoline cost $2.93 per gallon in

California, compared to $2.46 in Texas. New York's gasoline prices are usually slightly above the national average, which was $2.61 the same week.[52]

Corporate Profits

The weakening economy and continued write-offs have weighed on corporate profits over the past three years. As output growth slowed and production costs rose sharply, corporate profits declined 4.1 percent in 2007, ending five consecutive years of double-digit growth (see Figure 45). With further weakening in the economy throughout 2008 and 2009, corporate profits continued to suffer, falling 11.8 percent in 2008 and an estimated 3.7 percent in 2009.

Figure 45

Both nonfinancial and financial corporate profits have been challenged by the magnitude of the recent recession (see Figure 46). Operating profits were handed a large blow as corporations scurried to appropriately react to sharp contractions in aggregate demand, tightening credit conditions, and large asset depreciations over the last three years.

[52] Historical and current energy prices discussed in this section are as reported by the Energy Information Administration on their website, www.eia.doe.gov.

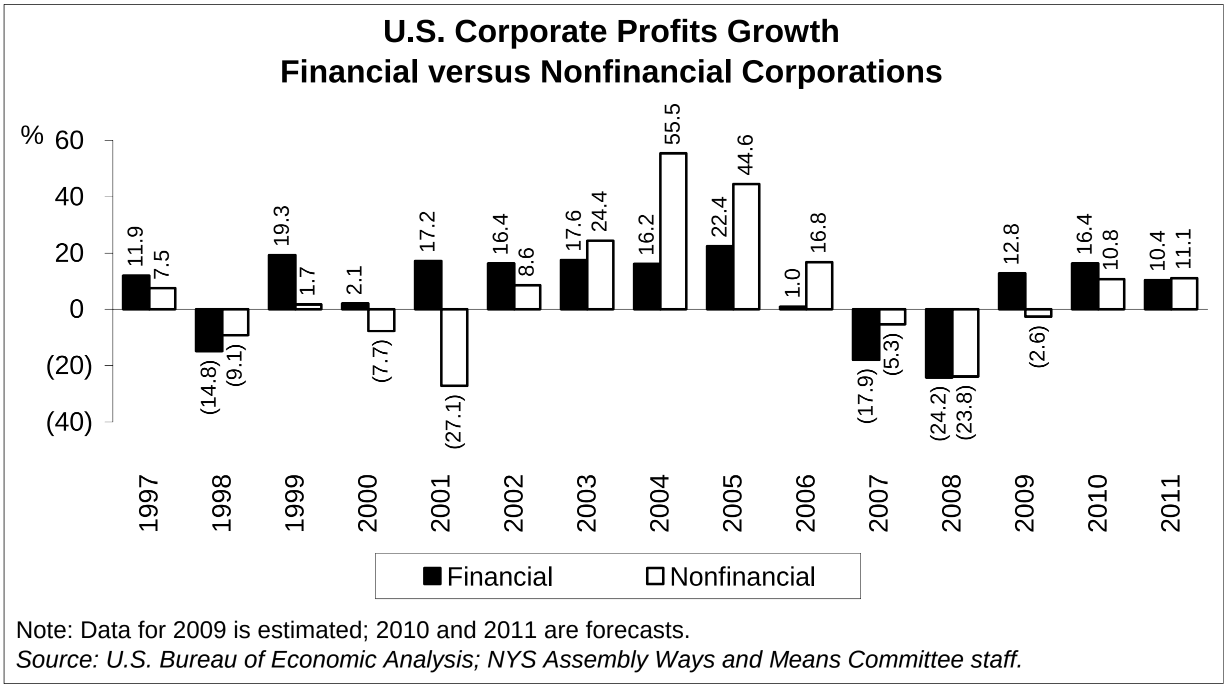


Figure 46

In the five years preceding the recession that began in 2007, aggressive financial leveraging helped boost corporate profits, as did a booming housing market and a strong consumer base. Cumulatively, these conditions spawned an environment that encouraged business and consumer spending, in effect helping prop the corporate profits share of national income to 13.7 percent by the third quarter of 2006.

When the housing bubble burst in 2006, panic ensued in the financial markets as creditors pulled back the lending reins. Problems continued to mount in 2007 and 2008, with lending and other financial institutions making large write-offs on residential mortgages and other assets while tightening consumer lending standards. Rising loan losses, continued declines in asset values, and sizeable losses in trading accounts hit the financial sector hard, causing profits in the financial sector to fall 17.9 percent in 2007 and 24.2 percent in 2008 (see Figure 46).

On the nonfinancial side, massive drops in wealth engendered consumer restraint, and demand for new homes, cars, and other items declined dramatically. Revenues were struck by the abrupt turn in conditions and fixed costs led to large erosions in operating profits. The business sector quickly responded by slowing output, running down inventories, laying off workforce, and overall pulling back on investment.

In the fourth quarter of 2008, problems coming from all sides of the economy combined to create the worst quarterly performance for corporate profits since WWII, causing them to fall an unprecedented $331.0 billion (at an annualized rate). Of the $331.0 billion decline in corporate profits, roughly two-thirds came from losses in the financial sector, which was battling with the repercussions of years of reckless leveraging activity and significant losses from a rapidly deteriorating stock market. At the same time, nonfinancial corporate profits also declined sharply in the same quarter, as producers aimed to cut back output and inventories to realign with consumer demand, which had fallen off dramatically. These factors contributed to a sharp decline in the corporate profits share of national income to 9.0 percent in the fourth quarter of 2008 (see Figure 47).

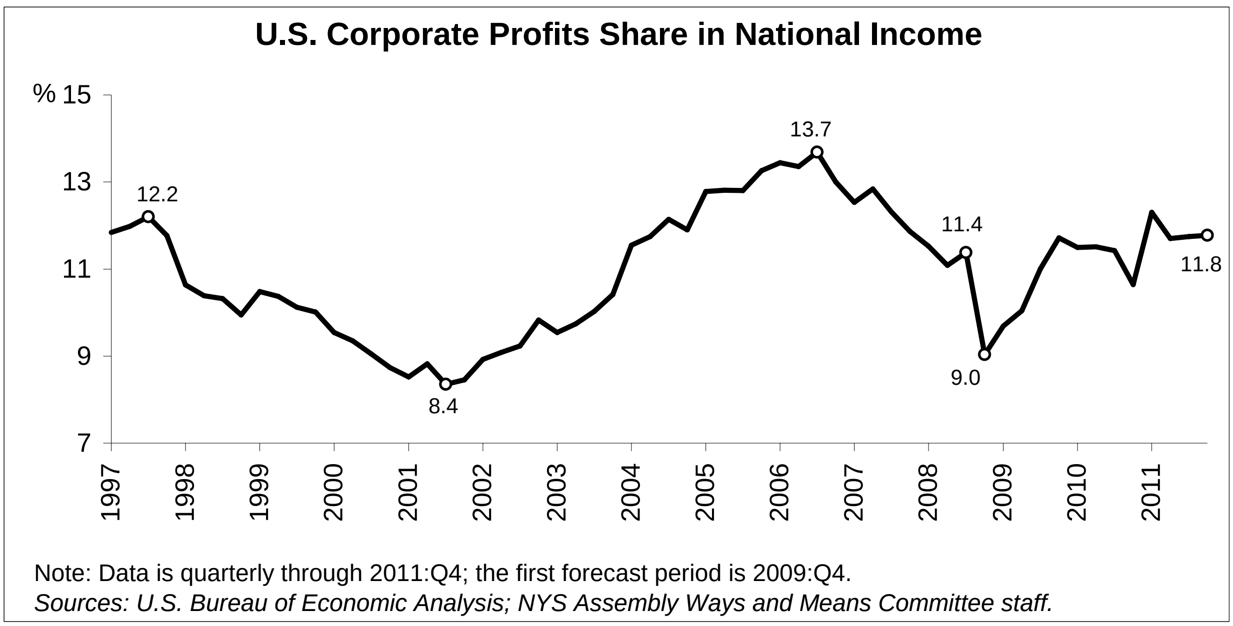


Figure 47

Corporate profits improved through the first three quarters of 2009, as productivity jumped 6.9 percent and 7.2 percent in the second and third quarter, respectively. Continued cuts in employment costs throughout the first three quarters of 2009 and improving demand have contributed to profits in the nonfinancial sector.

In 2009, the financial sector benefited from higher net interest income, gains on asset sales, increased trade revenues, and higher servicing fees. Losses from asset backed commercial paper write-downs continue to be a thorn in the sector's side, but appreciations in security values and other investments are contributing to profits.[53]

U.S. corporate profits are projected to improve further in the forecast period as output is expected to continue to grow faster than costs. Increases in the business transfer receipts and other government spending programs incorporated in the American Recovery and Reinvestment Act of 2009 will also help corporate profit growth in the forecast period. The NYS Assembly Ways and Means Committee staff forecasts corporate profits to grow 10.3 percent in 2010 and 10.4 percent in 2011.

Interest Rates

Faced with the deepest recession in decades, the Federal Reserve cut the federal funds target rate to a 0 to 0.25 percent range on December 16, 2008, the lowest level on record. As the U.S. economy is expected to recover slowly from the recent recession, the unemployment rate is expected to remain high in 2010, while inflation is expected to stay in check. Thus, the current forecast assumes that the Fed will maintain the rate within the current target range for the first half of 2010 before raising the rate gradually throughout the forecast period (see Figure 48).[54]

The federal funds rate, which averaged 1.9 percent in 2008, averaged 0.16 percent in 2009, and is predicted to average 0.24 percent in 2010 before rising to 1.7 percent in 2011. Similarly, the three-month Treasury bill rate averaged 0.15 percent in 2009, and is forecast to average 0.27 percent in 2010 and 1.8 percent in 2011.

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[53] Federal Deposit Insurance Company, "All Institutions Performance, Third Quarter 2009," *Quarterly Banking Profile*, (Last Updated 11/24/2009), www2.fdic.gov/qbp/2009sep/qbpall.html.

[54] The Federal Reserve has started to withdraw liquidity from the financial system by raising the interest rate charged for overnight loans to depository institutions (discount rates) from 0.5 percent to 0.75 percent on February 18, 2010. This will encourage depository institutions to rely more on private funding. See, Board of Governors of the Federal Reserve System, *Press Release*, February 18, 2010.

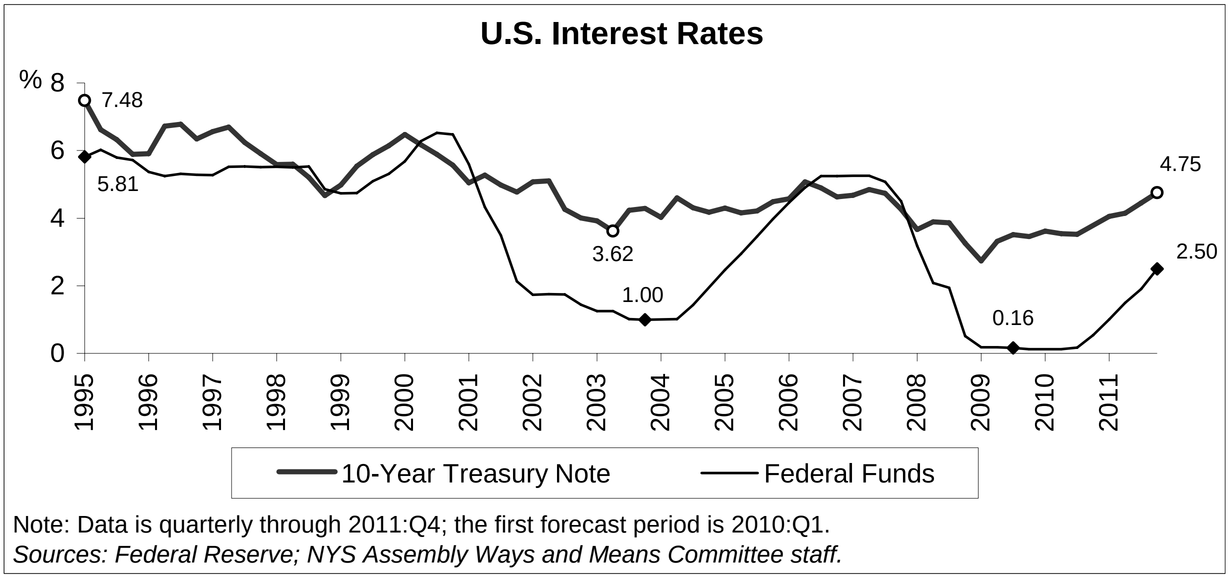


Figure 48

As the U.S. and world economies continued through the recession, the bond market became more attractive for investors who sought safer investments. Looking for safety and liquidity, investors shifted their investment from stocks to Treasury bonds. Foreign investors significantly increased their purchase of U.S. Treasury bonds in 2008 and 2009 from less than $200 billion in 2007 to $538.5 billion in 2009.

On the contrary, net purchases of U.S. corporate stocks by foreigners dropped drastically from almost $200 billion in 2007 to less than $40 billion in 2008, while net purchases of U.S. corporate and other bonds by foreigners dropped from $511 billion in 2006 to less than $100 billion in 2008 (see Figure 49).[55] This trend continued into 2009 for corporate and other bonds to a net sale (instead of purchase) of $40.7 billion. In contrast, purchases of U.S. corporate stocks increased in the past few months as investors with regained confidence in the economy sought higher returns.

[55] U.S. Department of the Treasury, Office of International Affairs, "Statistics—U.S. Financial Accounts with Foreigners (Excludes Direct Investments)," *Treasury International Capital System - Home Page,* www.treas .gov/tic/.

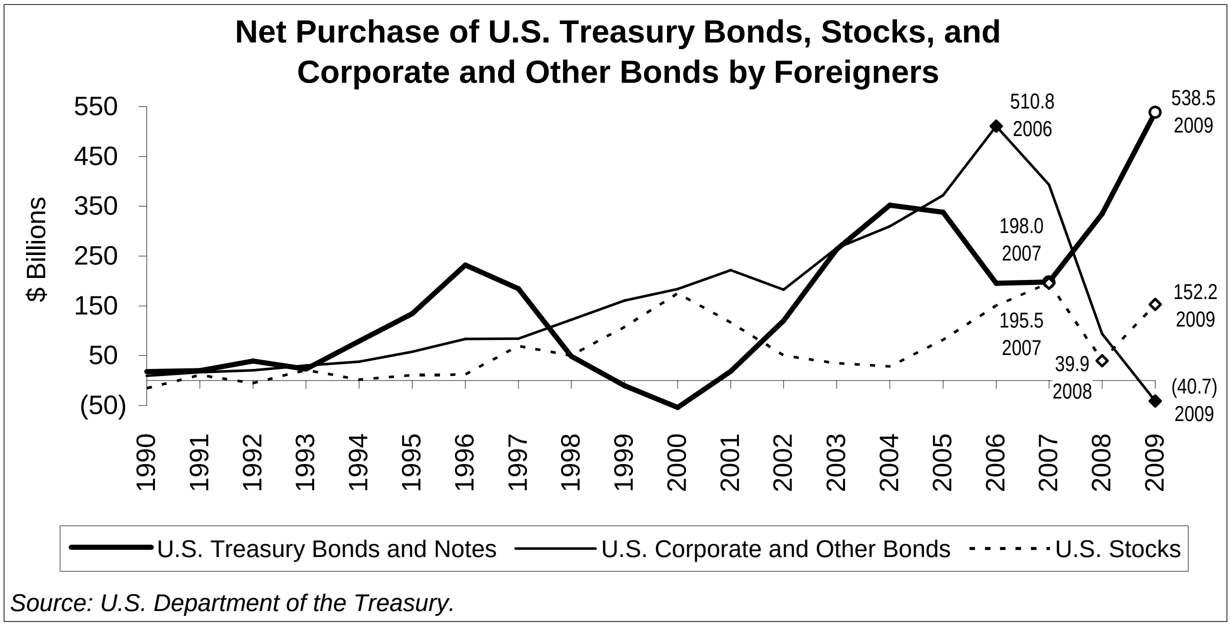


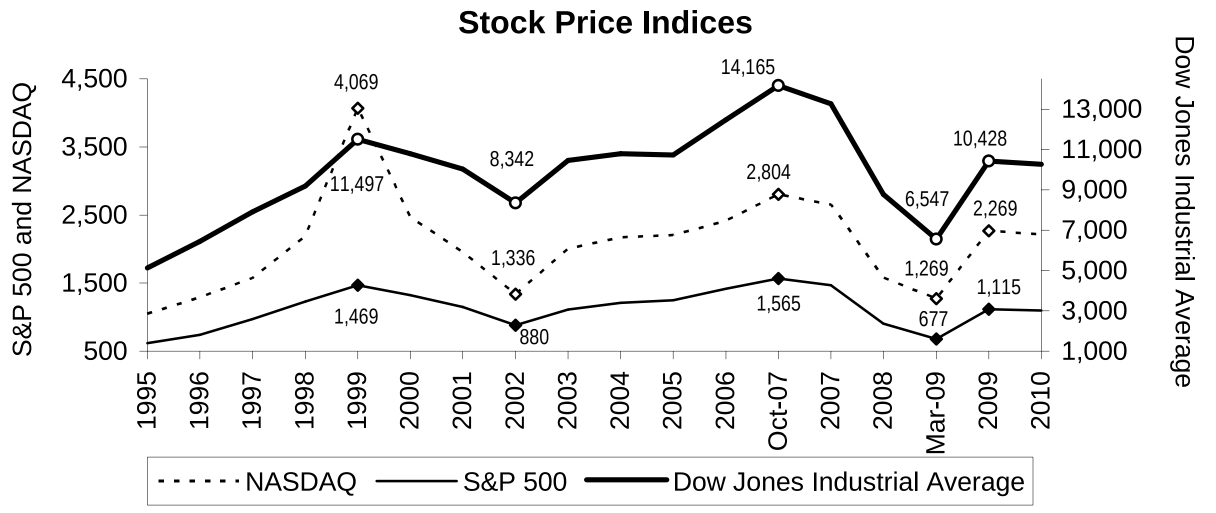
Figure 49

High demand for U.S. Treasury securities pushed bond prices up in 2008 and early 2009. As a result, the 10-year Treasury note yield dropped from an average of 3.7 percent in 2008 to 3.3 percent in 2009. Lower yield on long-term bonds has also led to a lower mortgage rate, which is typically set relative to long-term bond yield.

Increasing the supply of Treasury securities to finance the budget deficit pushed bond yields up in late 2009. The 10-year Treasury note yield averaged 3.5 percent in the fourth quarter of 2009, an increase from 2.7 percent in the first quarter. As the economy is expected to continue to rebound in 2010, investors will likely shift their investment from Treasury securities to stocks and corporate bonds to seek higher returns. The 10-year Treasury rate is forecast to average 3.6 percent in 2010 before rising to 4.4 percent in 2011.

Stock Market

The stock market plummeted to the lowest level in more than twelve years in March 2009 (see Figure 50). From its recent peak in October 2007 to its trough in March 2009, the S&P 500 stock price index, or S&P 500, was down 56.8 percent, compared to a drop of less than 50 percent from its peak in March 2000 to its trough in October 2002.[56]



Note: Data is at close of December 31 each year. The last period is February 16, 2010 value.
Sources: Securities Industry and Financial Markets Association; Wall Street Journal.

Figure 50

On a quarterly average basis, the S&P 500 surpassed its previous peak to a record high of 1,496.4 in the second quarter of 2007 (see Figure 51). After the U.S. entered recession in December 2007, activities in the stock market declined rapidly. The S&P 500 dropped 45.9 percent from the second quarter of 2007 to 809.3 in the first quarter of 2009. With the economy beginning to recover, the stock market is expected to continue to improve throughout the forecast period.

[56] Similarly, the Dow Jones Industrial Average (DJIA) dropped 53.8 percent compared to less than the 40 percent decline from its peak in January 2000 to its trough in October 2002. During the 1929 stock market crash, the DJIA dropped by more than 80 percent from its peak in September 1929 to its trough in July 1932. The DJIA did not return to pre-1929 levels until the mid-1950s.

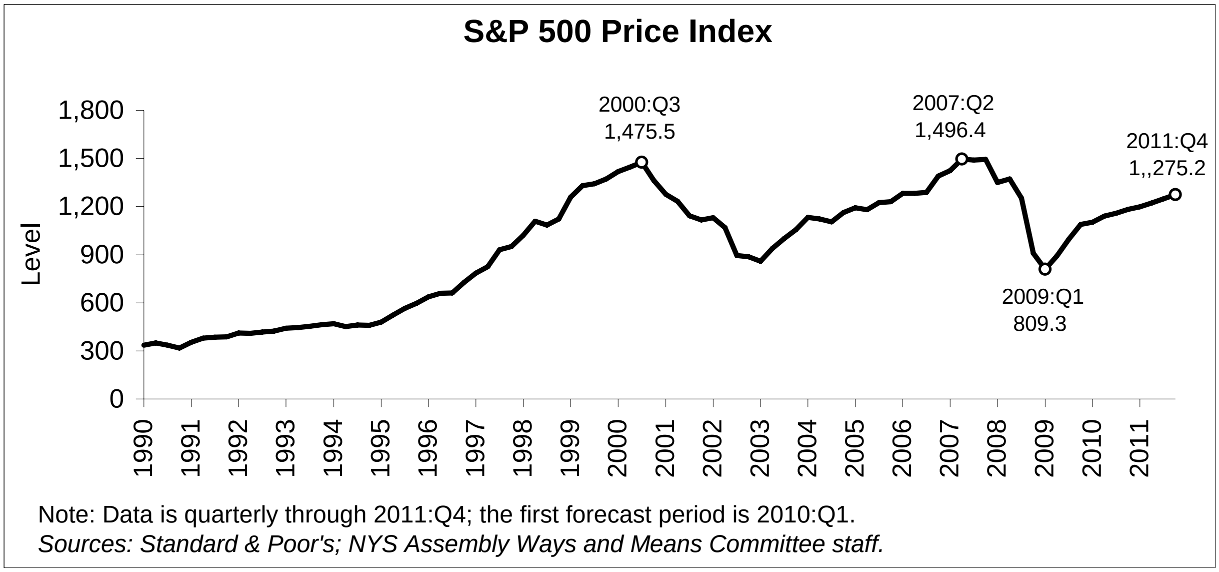


Figure 51

Improvement in economic activities has gradually lifted market uncertainty, helping to improve stock market performance in the second half of 2009. The recovery is expected to continue throughout the forecast period; however, as overall economic activity and corporate profitability remained weak during most of 2009, the annual average level of the S&P 500 was lower than the 2008 level. On an annual basis, the S&P 500 declined 22.5 percent in 2009. With improvement towards global economic recovery accompanied by the most enticing equity valuation levels in more than a decade, the S&P 500 is forecast to increase 21.1 percent in 2010 and to continue to grow further at 7.9 percent in 2011.

Although the stock market continues to improve, the gain is fragile as uncertainties still exist. Slow economic growth and high unemployment have led to a significant increase in loan defaults as reported by several major banks. More foreclosures are expected from the pool of five-year subprime ARMs mortgages which originated in 2005 that will have their rates reset in 2010. In addition, investors and investment firms have also been heavily exposed to credit derivatives such as credit default swaps (CDS). In three years, total outstanding CDS grew almost eightfold from $8.4 trillion in the second half of 2004 to $62.2 trillion in the second half of 2007. Increasing risk in equity markets has led to a reduction of outstanding CDS in the market by almost half to $31.2 trillion in the first half of 2009.[57] A recent survey indicated that more than 85 percent of banks and over 60 percent of insurers use CDS.[58] These highly speculative derivatives are lightly regulated.

United States Forecast Comparison

The NYS Assembly Ways and Means Committee staff forecast for overall national economic growth in 2010 is 2.9 percent (see Table 4). The staff forecast is lower than the Division of the Budget by 0.2 percentage point, Blue Chip Consensus and IHS Global Insight by 0.1 percentage point, and Macroeconomic Advisers by 0.8 percentage point. The staff forecast is higher than Moody's Economy.com by 0.1 percentage point.

Table 4

U.S. Real GDP Forecast Comparison
(Percent Change)

	Actual 2008	Estimate 2009	Forecast 2010	Forecast 2011
Ways and Means	0.4	(2.4)	2.9	2.8
Division of the Budget	0.4	(2.4)	3.1	3.4
Blue Chip Consensus	0.4	(2.4)	3.0	3.1
Moody's Economy.com	0.4	(2.4)	2.8	3.6
Macroeconomic Advisers	0.4	(2.4)	3.7	4.2
IHS Global Insight	0.4	(2.4)	3.0	2.8

Sources: NYS Assembly Ways and Means Committee staff; Blue Chip Economic Indicators, February 2010; Division of the Budget, Executive Budget 2010-11, February 9, 2010; Moody's Economy.com, February 2010; IHS Global Insight, February 2010; Macroeconomic Advisers LLC, February 2010.

The Assembly Ways and Means Committee staff forecast for overall national economic growth in 2011 is 2.8 percent. The staff forecast is lower than the Division of the Budget by 0.6 percentage point, Blue Chip Consensus by 0.3 percentage point, Moody's Economy.com by 0.8 percentage point, Macroeconomic Advisers by 1.4 percentage points, and is the same as IHS Global Insight.

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[57] International Swaps and Derivatives Association, Inc., "ISDA Market Survey Results, 1987-present," *Survey and Market Statistics*, http://www.isda.org/statistics/pdf/ISDA-Market-Survey-historical-data.pdf.

[58] International Swaps and Derivatives Association, Inc., "ISDA Research Notes," Number 2, 2009, http://www.scribd.com/doc/24545398/ISDA-Research-Notes2.

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NEW YORK STATE FORECAST

The NYS Assembly Ways and Means Committee staff estimates that in 2009 nonfarm payroll employment in the State declined 2.8 percent, wages declined 7.4 percent, and personal income declined 4.2 percent. In 2010, job losses will continue at an annual average rate of 0.4 percent. Personal income is forecast to gain 4.2 percent, as property income and wages and salaries recover. Employment is forecast to grow in 2011. Variable compensation is estimated to have declined 31.6 percent in 2009, and is forecast to grow 32.1 percent in 2010, then decline by 22.3 percent in 2011 (see Table 5).[59]

Table 5

New York State Economic Outlook
(Percent Change)

	Actual 2008	Estimate 2009	Forecast 2010	Forecast 2011
Employment	0.5	(2.8)	(0.4)	0.9
Personal Income	2.7	(4.2)	4.2	2.5
Total Wages	2.0	(7.4)	5.2	0.5
Base Wages	3.2	(3.6)	2.2	3.8
Variable Compensation	(4.6)	(31.6)	32.1	(22.3)
New York Area CPI	3.9	0.4	2.1	2.4

Note: Base wages and variable compensation are estimated by the NYS Assembly Ways and Means Committee staff and sum to total wages. New York area CPI is based on the New York-Northern NJ-Long Island, NY-NJ-CT-PA CPI-U series from the U.S. Bureau of Labor Statistics.

Sources: U.S. Bureau of Economic Analysis; NYS Department of Labor, QCEW; U.S. Bureau of Labor Statistics; NYS Assembly Ways and Means Committee staff.

The strong variable wage growth in 2010 and the large decline in 2011 are reflections of the assumption that although the finance industry is recovering, changes in

[59] Data based on NYS Assembly Ways and Means staff estimates. Variable compensation consists primarily of cash bonuses and exercised stock options. There is no known series of data for state or national variable compensation. The Ways and Means Committee staff estimates variable compensation based on seasonal variations in wage patterns. These seasonal patterns are analyzed at the NAICS three-digit level. The growth in this variation over time is also accounted for in the estimate. Since this estimate is based on seasonal variation, it may underestimate bonuses and commissions that come at frequent intervals throughout the year. It also may underestimate stock options to the extent that they are exercised throughout the year. On the other hand, in some cases non-variable pay may be included in variable compensation if there are regular seasonal patterns (e.g., if overtime regularly occurs in a certain quarter). Therefore, variable compensation contains high uncertainty—even in terms of the data history.

federal tax law will cause shifting of some bonus payments from 2011 to 2010.[60] This pattern of shifting is consistent with historical shifting seen from 1993 to 1992. The impact of the shift assumed in this report is significant on a calendar year basis, as without the shift total wages could be assumed to grow only 2.9 percent in 2010 compared to 5.2 percent with the shift. In 2011, wages are expected to grow 0.5 percent with the shift, compared to 4.8 percent without the shift. Since most of the shift is assumed to happen within a state fiscal year, state fiscal year growth rates are little affected.

The impact of the recent recession on New York State has differed from the effect on other states. In addition, the downturn has had a different impact on New York State compared to past recessions. While some changes in economic behavior during the recent recession are attributable to the various factors that triggered the national recession, there have been changes in the State economy over time that may account for the different impact.

The changing composition of New York's economy has led to some differences in New York State employment losses as compared to previous recessions. Historically, manufacturing employment has made up a much larger share of the State economy and was especially hard hit in the 1990-91 recession. In 2001, in the aftermath of the attack on the World Trade Center there was permanent relocation of jobs from New York to other surrounding states.

National job losses during the recent recession have been spread throughout many sectors. However, New York fared better than many other states in terms of job loss in the hardest hit sectors such as construction and manufacturing. In fact, due to New York State's relative shield from the real estate bubble, the State's employment continued to grow several months after the nation's December 2007 employment peak. Therefore, New York State has been losing jobs for a shorter time than the majority of states. For example, California employment has followed a downward trend almost every month since August 2007. Florida employment peaked in March 2007. Unlike these states and several others, payroll employment in New York State did not begin to have consecutive monthly declines until August 2008. However, due to the concentration of the financial sector on Wall Street, New York was impacted more severely by the loss of finance and insurance jobs than most other states. Only California has lost a higher number of total finance and insurance jobs since December 2007 than New York. However, New York State was

[60] Federal tax rates would rise upon the expiration of the Economic Growth and Tax Relief Reconciliation Act of 2001 and the Job and Growth Tax Relief Reconciliation Act of 2003.

relatively harder hit in the high-paying subsectors of finance and insurance such as the securities industry.

The 2008 annual average employment in the New York State finance and insurance sector was 9,515 jobs less than in 2007. As these jobs have been lost, the income associated with these positions has also been cut. Therefore, the employment decline during the recent recession was accompanied by a larger percentage drop in wages than in previous recessions. In addition, the finance sector employees who remained employed were faced with reduced compensation. Around the 2001 recession, wages dropped by 2.6 percent in 2002, then grew by 1.4 percent in 2003. For the 1990-91 recession, wages in 1991 dropped just 0.2 percent (see Figure 52). In contrast, total wages in 2009 are estimated to have dropped 7.4 percent, the largest percentage drop since the data series started in 1975. The next largest drop in New York State wages was in 2002.

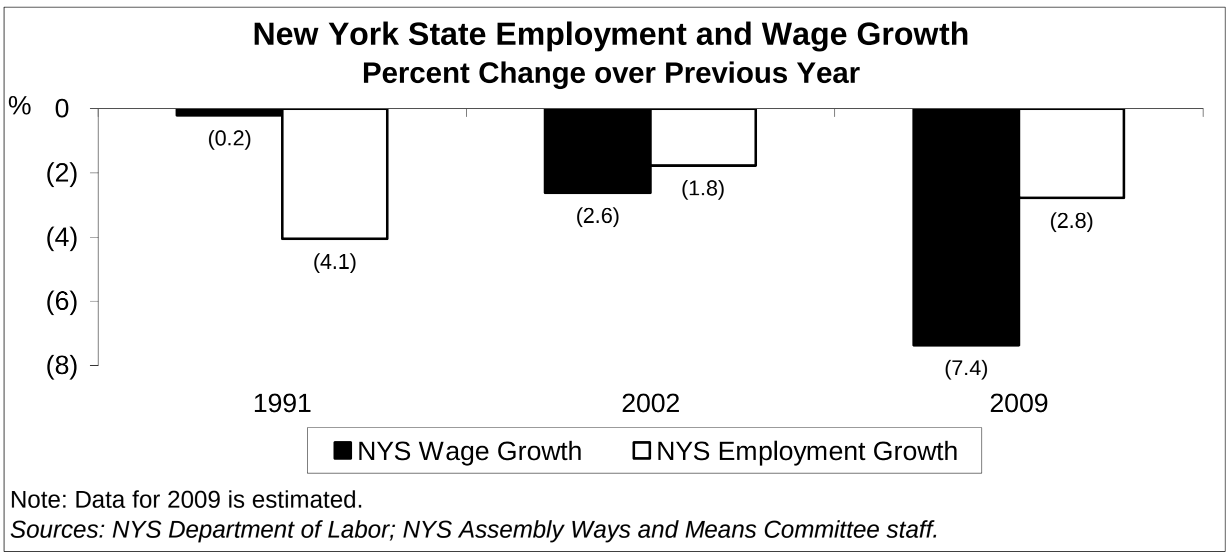
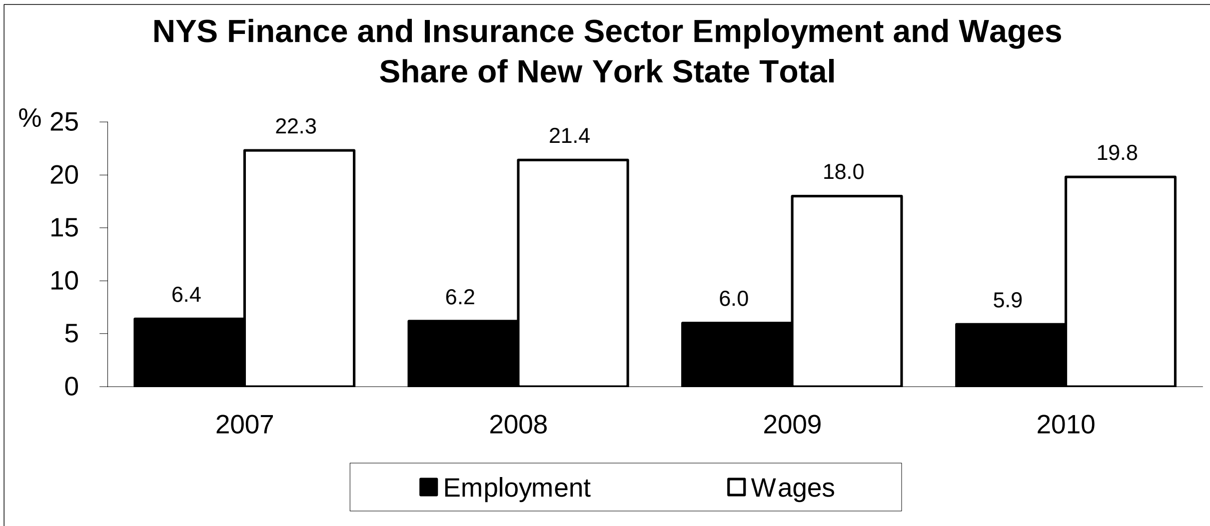


Figure 52

Central to the overall wage and variable compensation outlook for New York State is the performance of Wall Street. The average wage in the finance and insurance sector is over three times that of the overall average wage in the State. This sector accounted for 22.3 percent of total New York State wages in 2007, the highest share since the series started in 1975, whereas employment in the industry was only 6.4 percent of total nonfarm payroll employment in the State (see Figure 53). In 2009, the share of total finance and insurance employment is estimated to have fallen to 6.0 percent while wages fell to 18.0 percent. In 2010, the finance and insurance employment share is forecast to fall further to 5.9 percent, the lowest level since 1975 as employment in the sector continues to fall on an annual average basis. On the contrary, finance and insurance wage share is expected to increase to 19.8 percent in 2010, reflecting expectations that variable wages will increase going forward.



Note: Data for 2009 is estimated; 2010 is forecast.
Source: NYS Department of Labor, QCEW.

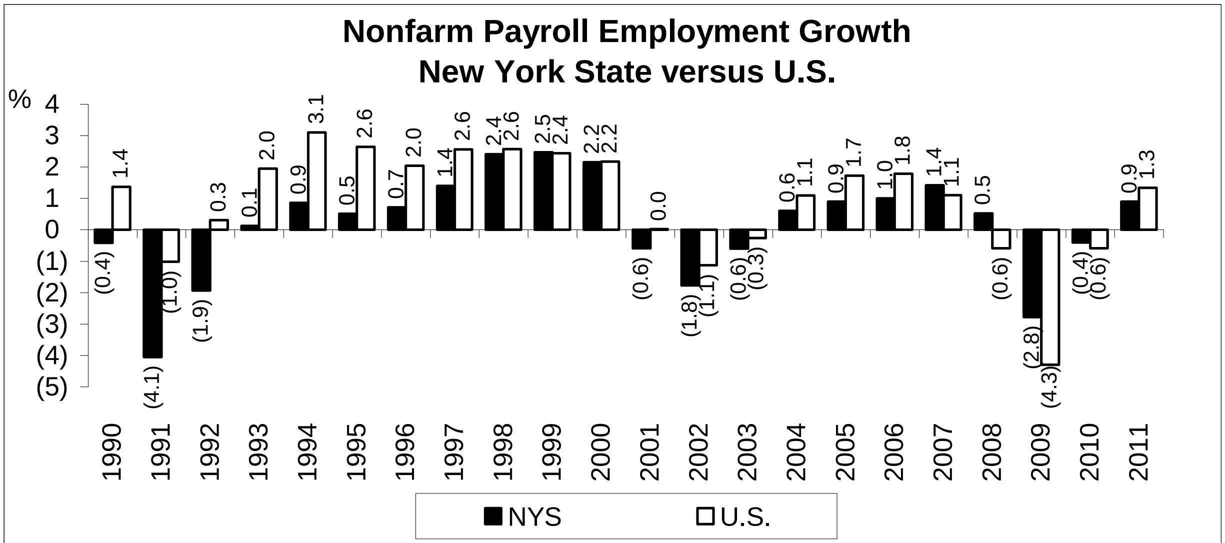
Figure 53

As states experienced different magnitudes of decline in employment and wages during the recent recession, regions within New York State have also been affected. New York City, with its heavy concentration of finance jobs, saw dramatic declines in wages and employment compared to other regions in the State. While some regions saw only small declines, their growth during the recovery may not be as fast as New York City's should the financial sector recover strongly and help drive New York City's economy to levels seen during previous expansions.

Employment

During the two decades before the recent recession, nonfarm employment growth in New York State almost always lagged national employment growth. New York was hit harder than the nation in the two prior recessions, and its employment recovered much slower than the nation. As the U.S. economy went into recession at the end of 2007, employment growth in both the State and the nation slowed sharply in 2008. In 2008, total New York State nonfarm payroll employment grew 0.5 percent, significantly lower than

2007, while national employment declined by 0.6 percent. As the overall economy weakened further in 2009, total employment in the State is estimated to have declined by 2.8 percent, the worst decline in more than a decade. New York State nonfarm employment growth is expected to be close to the nation in 2010 and 2011. Total nonfarm payroll employment in the State is forecast to decline another 0.4 percent in 2010, before growing 0.9 percent in 2011 (see Figure 54).



Note: Data for 2009 is estimated; 2010 and 2011 are forecasts.

Sources: NYS Department of Labor, QCEW; U.S. Bureau of Labor Statistics, CES; NYS Assembly Ways and Means Committee staff.

Figure 54

Unlike the 2001 recession, when the State started losing jobs earlier than the nation, New York State entered the recent downturn after the nation. New York State's total nonfarm payroll employment decline started in the third quarter of 2008, while the nation started losing jobs in the first quarter of 2008 (see Figure 55). The rate of employment loss in the State has also been lower than the nation during the national recession that began in December 2007. New York State is expected to lose 3.2 percent of total payroll jobs from peak to trough compared to 5.4 percent for the nation (annual numbers). As the New York housing market fared better than that of the nation, the percentage of employment loss in the construction sector is expected to be much less than the national construction job loss. This is a major part of why the State is expected to lose less of a percentage of total employment than the nation as a result of the recent recession. In contrast, New York lost 2.9 percent of employment from peak to trough (annual numbers), compared to a 1.4 percent loss for the nation during the 2001 recession.

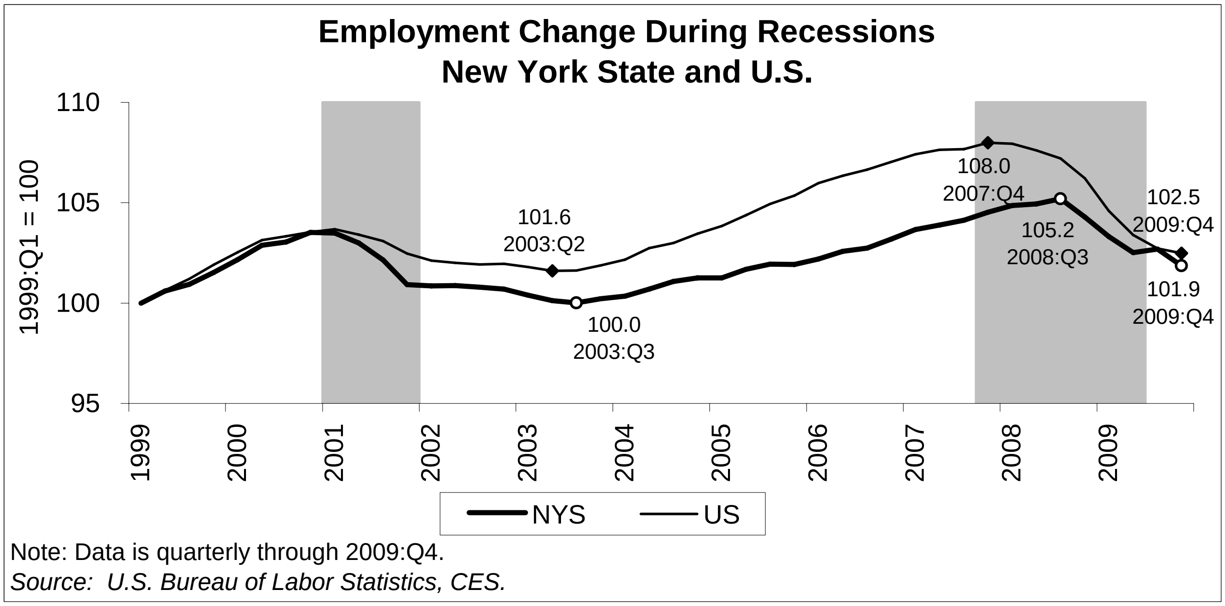


Figure 55

From 2008 to 2009, New York State is estimated to have lost approximately 2.8 percent of total jobs or about 238,400 jobs on a yearly average basis. Employment is forecast to continue to decline, with a loss of 33,200 jobs in 2010. As a result, the unemployment rate in the State has been increasing. The unemployment rate in the State was 8.8 percent in December 2009, compared to 6.8 percent in December 2008.[61] Unemployment is expected to continue to rise as those who left the labor force during the recession will return and firms remain cautious about recovery and may be reluctant to hire. The State unemployment rate peaked at 7.0 percent during the 2001 recession and reached over 9.0 percent during the 1990-91 recession.

The only employment gain in 2010 is expected to be in the education and health, management of companies, and other services sectors. Education and health accounted for the largest share of 2008 total nonfarm payroll employment in New York State at 17.8 percent. While most sectors lose jobs during economic downturns, health and education employment has been steadily increasing even through the recent recession. This trend is likely to continue as aging baby boomers create more demand for health care services. From 2009 to 2011, the education and health sector is forecast to grow at about 2.0 percent per year and generate more than 30,000 new jobs each year. As a result, the sector's share of total nonfarm payroll employment in New York State is expected to

[61] New York State Department of Labor, "Employment and Unemployment Data," Workforce and Industry Data, December 2009.

increase to 19.3 percent in 2011. The other services sector is expected to recover relatively faster than other sectors as temporary employment will increase during the early stages of the recovery.

The largest number of jobs lost will be in the manufacturing sector. Manufacturing employment, which has been continuously falling for the past few decades due to structural shifts in the economy and other economic factors, is estimated to have declined by 10.1 percent in 2009. The decline of the U.S. automobile industry has had a negative effect on national and State manufacturing employment, and is of particular concern to upstate New York, as many manufacturing firms are located in upstate. Manufacturing employment is forecast to continue to decline for both the State and the nation throughout the forecast period. In 2010 and 2011, New York State manufacturing employment is forecast to fall by 4.6 percent and 3.2 percent respectively, the fastest rate of employment loss among all sectors (see Table 6). Between 2008 and 2010, the manufacturing sector is

Table 6

New York State Employment by Sector (Percent Change)

	Actual 2008	Estimate 2009	Forecast 2010	Forecast 2011
Total Employment	**0.5**	**(2.8)**	**(0.4)**	**0.9**
Education & Health	2.1	2.0	2.0	2.0
Mgmt. of Companies	2.8	1.1	0.9	1.9
Government	0.9	(0.1)	(0.3)	(0.1)
Leisure & Hospitality	2.3	(1.5)	(0.1)	2.2
Real Estate, Rental, & Leasing	0.3	(3.6)	(2.1)	0.8
Information	(0.4)	(3.7)	(2.2)	(1.0)
Professional Services	2.3	(4.1)	(1.0)	2.0
Retail Trade	0.2	(4.2)	(0.8)	0.7
Other Services[1]	0.3	(4.2)	1.4	1.5
Transp. & Utilities[2]	0.8	(4.3)	(1.3)	0.6
Wholesale Trade	(1.3)	(5.7)	(1.0)	0.5
Finance & Insurance	(1.7)	(6.5)	(2.0)	0.6
Construction	2.1	(9.9)	(3.4)	2.9
Manufacturing[3]	(3.6)	(10.1)	(4.6)	(3.2)

Note: Rankings are based on two decimal places.
[1] Including Administrative, Support, and Waste Management Services.
[2] Transportation, Warehousing, and Utilities.
[3] Including Mining.
Sources: NYS Department of Labor, QCEW; NYS Assembly Ways and Means Committee staff.

expected to lose over 75,000 jobs, which will account for over 25.0 percent of total State nonfarm payroll jobs lost. Employment is forecast to recover in 2011 in almost all sectors, with the exception of the manufacturing, information, and government sectors.

The construction sector lost a significant number of jobs in 2009 as a result of slow activity in both commercial and residential construction. As private construction is expected to continue to slow for the next few years, employment in this sector is forecast to decline at a moderate rate in 2010.

The turmoil in the financial and housing markets has had a significant negative impact on employment and the performance of the finance and insurance sector, especially the securities industry. By 2010, the finance and insurance sector in the State is expected to lose 54,300 jobs or 10.0 percent of the overall employment from its peak in 2007 as financial firms cut jobs in order to reduce costs. This is higher than the rate of sector employment lost during the last employment downturn. The finance and insurance sector lost 8.4 percent of jobs from 2000 to 2003. Industry employment had been growing since the sharp declines in 2002 and 2003.

Within the finance and insurance sector, the securities industry was particularly hard hit and continues to be troubled by the problems in the financial system. Securities industry employment reached a record high of 865,900 jobs nationally in the second quarter 2008, but has since contracted by 10.2 percent. As of August 2009, securities industry employment in the State accounted for more than 20 percent of the nation's securities industry employment.[62] The industry currently employs almost 200,000 workers in the State, most of which are located in New York City, and accounted for 2.4 percent of total State nonfarm employment in 2008. Although there are some signs of hiring in segments of the industry, securities industry employment is estimated to have declined by 9.3 percent in 2009 and is expected to decline further by 2.2 percent in 2010 before growing 0.9 percent in 2011 (see Figure 56).

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[62] Paul Rainy, "Securities Industry Employment Update," *Research Report*, vol. 4, no. 10 (Securities Industry and Financial Markets Association), November 3, 2009, http://www.sifma.org/research/statistics/other/employment-NY-quarterly.pdf.

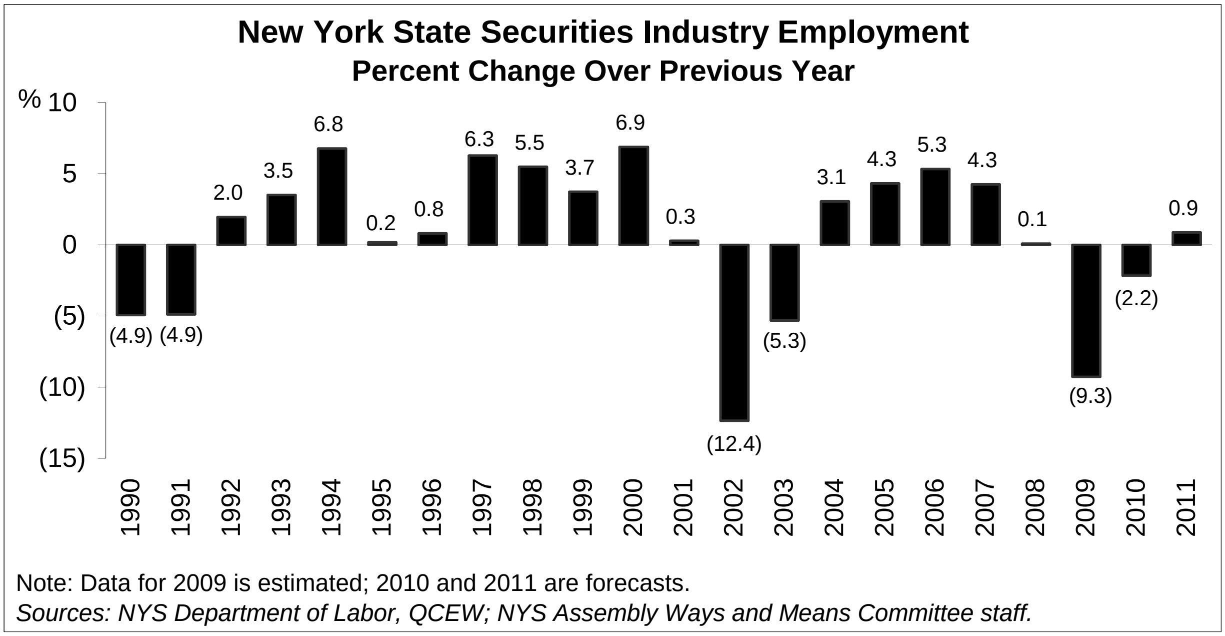


Figure 56

Between the second quarter of 2008 and the second quarter of 2009, New York State lost over 260,000 nonfarm jobs led by a 60,300 job loss in the manufacturing sector. Nonfarm employment declined in all regions during this period; however, upstate was less affected by the recent recession than downstate. The rate of job losses was distributed quite evenly across the regions with the fastest decline in the Mid-Hudson region, which lost 3.7 percent of its nonfarm jobs due to significant loss of construction, manufacturing, and retail jobs. On the contrary, the Mohawk Valley region lost the least percentage of jobs from the second quarter of 2008 to the second quarter of 2009, as the majority of jobs in this region are in the government and education and health sectors, which were least affected by the recession. New York City accounted for 43.3 percent of total State nonfarm employment in the second quarter of 2008, and accounted for 41.7 percent of total State nonfarm employment loss from the second quarter of 2008 through the second quarter of 2009 (see Table 7).

Table 7

New York State Nonfarm Employment by Region 2008:Q2 to 2009:Q2	Employment 2009:Q2 (Thousands)	Share of Total State Employment 2009:Q2 (%)	Employment 2008:Q2 (Thousands)	Share of Total State Employment 2008:Q2 (%)	2008:Q2 - 2009:Q2 (Percent Change)	Share of Total State Nonfarm Employment Change 2008:Q2 to 2009:Q2 (%)
New York State	**8,253.0**	**100.0**	**8,516.9**	**100.0**	**(3.1)**	**100.0**
Downstate	**5,643.6**	**68.4**	**5,829.8**	**68.4**	**(3.2)**	**70.5**
Mid-Hudson	869.2	10.5	903.0	10.6	(3.7)	12.8
Long Island	1,198.5	14.5	1,240.8	14.6	(3.4)	16.0
New York City	3,575.9	43.3	3,686.0	43.3	(3.0)	41.7
Upstate	**2,609.4**	**31.6**	**2,687.1**	**31.6**	**(2.9)**	**29.5**
Mohawk Valley	172.7	2.1	176.4	2.1	(2.1)	1.4
Southern Tier	292.8	3.5	303.6	3.6	(3.6)	4.1
Finger Lakes	533.2	6.5	550.2	6.5	(3.1)	6.4
Central New York	341.5	4.1	353.1	4.1	(3.3)	4.4
North Country	149.6	1.8	153.7	1.8	(2.7)	1.5
Western New York	616.6	7.5	635.2	7.5	(2.9)	7.1
Capital	502.9	6.1	514.8	6.0	(2.3)	4.5

Note: New York State total does not include unclassified data.
Source: NYS Department of Labor, QCEW.

Table 8 shows the sectoral rates of year-over-year employment growth by region for the most recent quarter for which data is available. From the second quarter of 2008 to the second quarter of 2009, employment decreased in most sectors in all regions. In all regions, the largest employment level increase in recent years was in the education and health sector, while in most regions, the largest rate of employment loss was in the manufacturing sector.

Table 8

New York State Employment Change 2008:Q2 to 2009:Q2 (Percent Change)				
	New York State	Downstate		Upstate New York
		New York City	NYC Suburbs	
Total	**(3.1)**	**(3.0)**	**(3.5)**	**(2.9)**
Education and Health	1.8	**2.0**	1.5	1.5
Government	0.2	(0.0)	0.3	**0.4**
Mgmt. of Companies	(0.3)	(2.4)	0.1	**1.8**
Leisure and Hospitality	(1.7)	**(1.0)**	(3.2)	(1.2)
Information	(3.5)	(5.0)	**(3.1)**	(4.1)
Real Estate, Rental, and Leasing	(3.9)	**(3.1)**	(5.1)	(5.1)
Retail Trade	(4.2)	(3.8)	(5.4)	**(3.6)**
Professional Services	(4.3)	(5.5)	(4.1)	**(2.1)**
Transportation and Utilities[1]	(4.9)	**(4.0)**	(4.7)	(6.5)
Other Services[2]	(5.4)	**(4.7)**	(5.7)	(6.4)
Wholesale Trade	(6.5)	(6.8)	(7.0)	**(5.0)**
Finance & Insurance	(7.2)	(8.3)	(7.5)	**(3.4)**
Construction	(10.0)	(8.3)	(13.3)	**(7.5)**
Manufacturing[3]	(11.1)	(14.5)	**(8.7)**	(11.2)

Note: Downstate employment grew 1.0 percent during this period. Rankings are based on two decimal places. Bolded numbers are largest in each sector.

[1] Transportation, Warehousing, and Utilities.

[2] Includes Administrative, Support, and Waste Management Services.

[3] Including Mining.

Source: NYS Department of Labor, QCEW.

Although the State has a lower share of manufacturing employment than the nation, manufacturing represents a larger share of total upstate employment than that of total State nonfarm employment. As of the second quarter of 2009, manufacturing employment made up 10.4 percent of upstate nonfarm employment and 3.7 percent of downstate nonfarm employment, and 5.7 percent of total State nonfarm employment. The highest concentration of manufacturing employment was in the Southern Tier and the Finger Lakes regions, where manufacturing employment accounted for 13.9 percent and 13.2 percent of the regions' nonfarm employment, respectively (see Table 9).

Table 9

New York State Manufacturing Employment by Region 2007:Q2 to 2009:Q2					
	Manufacturing Employment 2009:Q2 (Thousands)	Manufacturing Share of Nonfarm Employment 2009:Q2 (%)	Manufacturing Employment 2007:Q2 (Thousands)	Manufacturing Share of Nonfarm Employment 2007:Q2 (%)	2007:Q2-2009:Q2 (Percent Change)
U.S.	**12,621**	**9.6**	**14,658**	**10.7**	**(13.9)**
New York State	**480**	**5.7**	**559**	**6.5**	**(14.1)**
Downstate	**209**	**3.7**	**245**	**4.2**	**(14.5)**
Long Island	75	6.3	84	6.7	(9.9)
Mid-Hudson	52	6.0	60	6.6	(13.3)
New York City	82	2.3	102	2.8	(19.0)
Upstate	**271**	**10.4**	**314**	**11.7**	**(13.7)**
Southern Tier	41	13.9	46	15.1	(11.0)
Finger Lakes	70	13.2	83	15.1	(14.9)
Western New York	68	11.0	80	12.7	(15.0)
Mohawk Valley	17	9.9	20	11.2	(13.1)
Central New York	34	9.8	39	11.0	(13.4)
North Country	12	8.0	14	9.3	(16.1)
Capital	30	5.9	33	6.5	(10.6)

Note: New York State total does not include unclassified data.
Sources: U.S. Department of Labor, CES; NYS Department of Labor, QCEW.

From 1998 to 2008, New York State nonfarm payroll employment grew at an average rate of 0.6 percent per year, slower than the national average growth rate of 0.9 percent per year. This trend has, however, reversed in recent years.

In 2009, New York State accounted for 6.5 percent of total U.S. payroll employment. The State ranked third in the size of employment, behind California and Texas. The State has performed better than the nation and relatively well in terms of employment growth in recent years compared to other states, and is among the best compared to other large states. In 2009, the State's employment has declined slower than that of the nation. In the same period, total State nonfarm payroll employment declined 2.2 percent, a fall from 0.7 percent growth in 2008. Total New York State nonfarm payroll employment growth was ranked tenth in 2009, an improvement from thirteenth in 2008 and twentieth in 2007 (see Table 10).[63]

[63] These growth rates and rankings are based on Current Employment Statistics (CES) data, which is timelier than the Quarterly Census of Employment and Wages (QCEW) data but subject to significant revisions.

Table 10

Employment Growth by State 2007-2009						
	Employment Growth					
Geography	2009		2008		2007	
	Growth	Rank	Growth	Rank	Growth	Rank
United States	**(3.8)**	**-**	**(0.4)**	**-**	**1.1**	**-**
Top Five						
North Dakota	0.6	1	2.4	2	1.7	14
District Of Columbia	0.5	2	1.6	5	0.9	31
Alaska	(0.1)	3	1.4	6	0.9	30
Louisiana	(0.9)	4	1.3	7	3.4	3
South Dakota	(1.5)	5	1.2	8	2.0	10
New York	**(2.2)**	**10**	**0.7**	**13**	**1.3**	**20**
Bottom Five						
Georgia	(5.1)	47	(1.0)	43	1.4	19
Oregon	(5.3)	48	(0.6)	35	1.6	16
Nevada	(6.2)	49	(2.0)	47	1.0	27
Michigan	(7.0)	50	(2.5)	50	(1.4)	51
Arizona	(7.1)	51	(2.1)	48	1.5	17

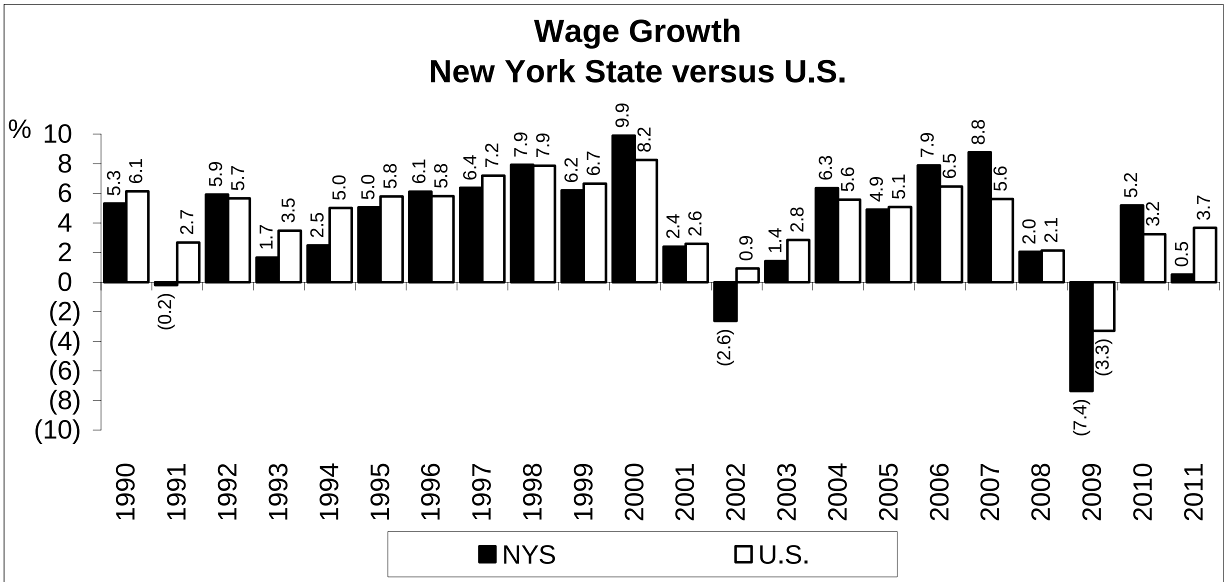
Note: The growth rates and rankings are based on Current Employment Statistics (CES) employment data. This data may differ from QCEW data usually used by the NYS Assembly Ways and Means Committee. The CES data is more timely but subject to possible significant revision. Rankings are based on two decimal places.

Source: U.S. Bureau of Labor Statistics.

Wages

After six years of growth, most of it vigorous, New York State wages fell an estimated 7.4 percent in 2009. This was a direct reflection of the nature of the recent recession, as well as the dependence of State wages on the financial sector. Wages are expected to rebound in 2010 as growth in variable and base wages is expected to recover; however, the growth rates will be much lower than in 2006 and 2007, with total growth of 5.2 percent in 2010. As in past recessions, wages in the State have fared worse than in the nation. In 2009, national wages fell, a phenomenon that did not occur during the past two recessions (see Figure 57).

Unless otherwise noted, QCEW data is the basis of statements regarding New York State employment in this section.

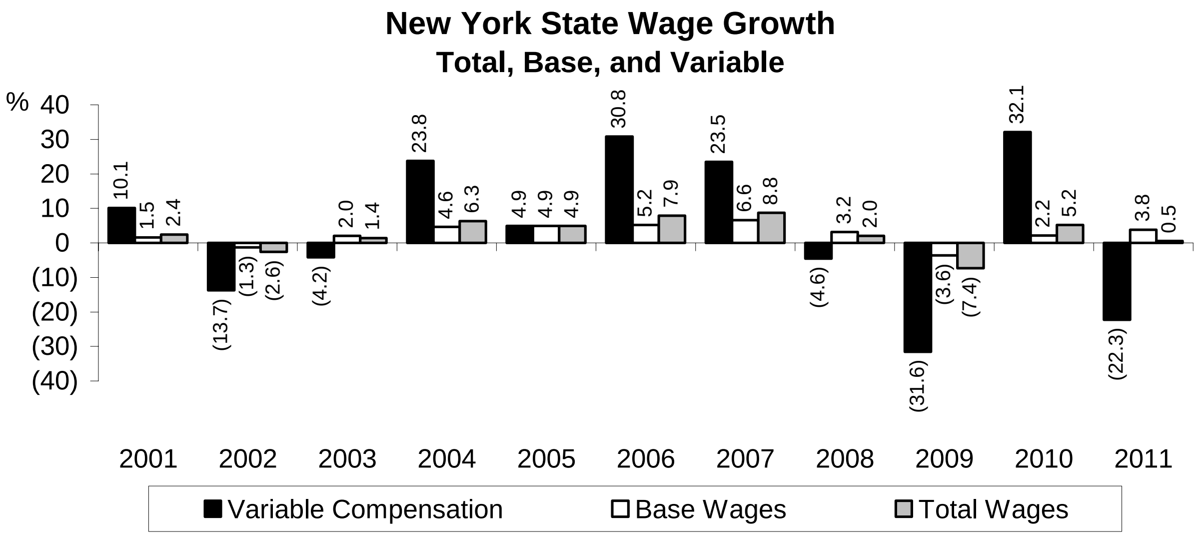


Note: Data for 2009 is estimated; 2010 and 2011 are forecasts.
Sources: NYS Department of Labor, QCEW; U.S. Bureau of Economic Analysis; NYS Assembly Ways and Means Committee staff.

Figure 57

Much of the variability in wages in New York State is due to the volatility of variable wages. Base wages have shown much more stable growth throughout history, and are estimated to have fallen 3.6 percent in 2009. Base wage growth is expected to resume throughout the forecast period as employment improves. The fall in variable wages is the major driving factor in the 2009 estimate, as shown in the NYS Assembly's series for variable wages (see Figure 58). This decline is a direct result of declines in Wall Street bonuses, which were curtailed significantly due to problems in the financial sector (see the Variable Compensation Section on Page 81).

In 2010, total New York State wages are expected to grow by 5.2 percent. This growth is a result of both positive base and variable wage growth. Base wages are expected to grow 2.2 percent in 2010 as employment losses slow. Variable wages are expected to grow 32.1 percent in 2010 and fall 22.3 percent in 2011, reflecting the possibility that financial firms will increase their cash bonuses as well as the anticipation of some wage payments shifting into late 2010 from early 2011 as a consequence of expiring federal tax cuts from the Economic Growth and Tax Relief and Reconciliation Act of 2001 and the Job and Growth Relief Act of 2003. Without the shift, the growth in 2010 and 2011 would be more evenly spread. On a state fiscal year basis, growth rates are little affected. Total variable wages are expected to grow 15.1 percent in State Fiscal Year (SFY) 2010-11 and 13.6 percent in SFY 2011-12.



Note: Total wage data for 2009 is estimated; 2010 and 2011 are forecasts. Base wages and variable compensation are estimated by the NYS Assembly Ways and Means Committee staff and sum to total wages.
Sources: NYS Department of Labor, QCEW; NYS Assembly Ways and Means Committee staff estimates.

Figure 58

Prior to the recent recession, strong overall wage growth in New York State had been helped by the State's unique concentration of the securities industry in New York City. When bonuses were strong, they had the potential to support wage growth even in the absence of other factors such as strong employment growth or gains in productivity. However, as the recent recession began, this concentration ceased to provide positive support to wages. As bonuses fell, the magnitude was not offset by changes in other fundamentals, leading to a significantly weakened wage outlook for the State. In addition, poor wage growth had a significant negative impact on State personal income growth in 2009 (see Table 11).

Table 11

Personal Income, Wages, and CPI New York State		Actual 2008	Estimate 2009	Forecast 2010	Forecast 2011
Personal Income	***Percent Change***	**2.7**	**(4.2)**	**4.2**	**2.5**
	Level	934.4	894.7	932.4	955.9
Total Wages	***Percent Change***	**2.0**	**(7.4)**	**5.2**	**0.5**
	Level	518.5	480.2	505.1	507.6
Base Wages	***Percent Change***	**3.2**	**(3.6)**	**2.2**	**3.8**
	Level	448.4	432.3	441.7	458.4
Variable Compensation	***Percent Change***	**(4.6)**	**(31.6)**	**32.1**	**(22.3)**
	Level	70.1	48.0	63.4	49.3
New York Area CPI	***Percent Change***	**3.9**	**0.4**	**2.1**	**2.4**

Note: Levels are in billions of dollars. New York area CPI is based on the New York-Nothern NJ-Long Island, NY-NJ-CT-PA CPI-U series from the U.S. Bureau of Labor Statistics.

Sources: U.S. Bureau of Economic Analysis; NYS Department of Labor, QCEW; U.S. Bureau of Labor Statistics; NYS Assembly Ways and Means Committee staff.

Regionally, the share of total New York State nonfarm wages is uneven (see Figure 59). Over half of the wages paid in the State are paid in New York City, although in 2008 the City accounted for only 42.8 percent of employment and 43 percent of total State population.[64] The share of wages outside of New York City is spread more evenly throughout the other State regions.

[64] Population data from U.S. Census Bureau, 2008, American Community Survey 1-Year estimates.

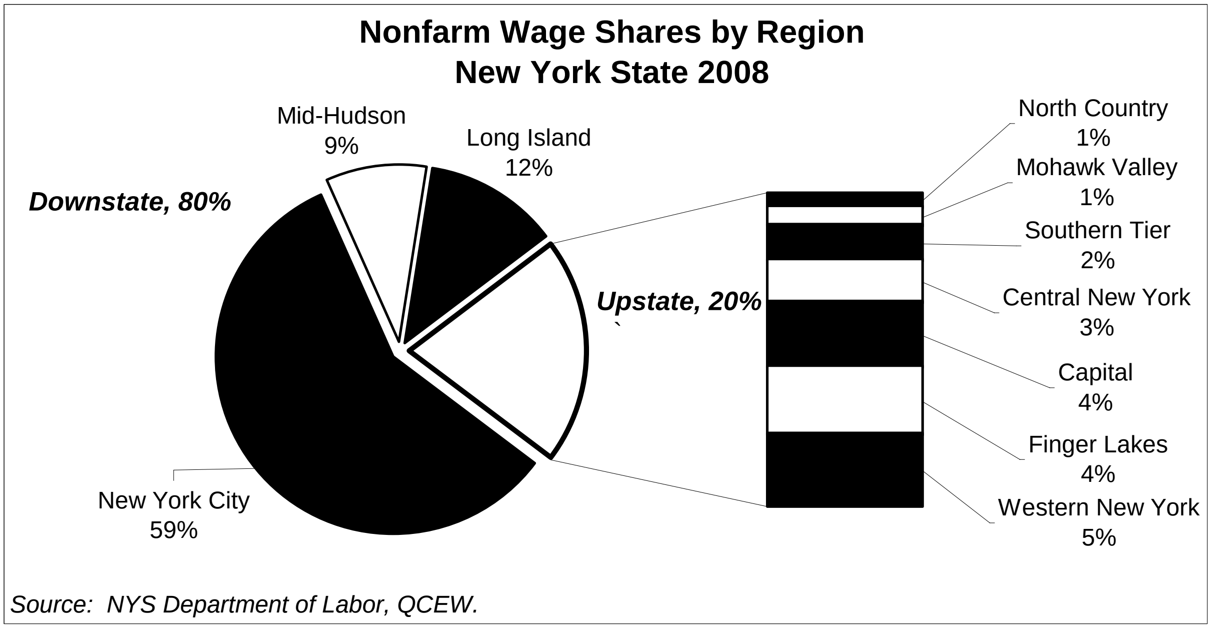


Figure 59

Wage growth across regions is also disparate, and growth in many regions has been adversely affected by the recession. In 2008, annual wage growth ranged from 1.3 percent in New York City to 4.6 percent in the Southern Tier. New York City has historically had higher wage growth compared to other regions (e.g., in 2007, NYC wages grew 12.0 percent); however, the city has been affected greatly by the downturn in the financial sector, much of which is concentrated in New York City.

The wage share of New York City is even higher in the first quarter of most years due to high bonus payments by financial firms, which mostly accrue to New York City businesses. In the first quarter of 2007, before the recent recession started, New York City accounted for 65.7 percent of State wages. By the first quarter of 2009, well into the recession, this share had fallen to 60.4 percent (see Table 12). As this share fell however, the City still maintained a majority share of wages in the State. Although some upstate regions gained in share of total New York State wages between the first quarter of 2007 and the first quarter of 2009, upstate regions accounted for relatively small shares of total State wages.

Table 12

New York State Nonfarm Wages by Region 2007:Q1 to 2009:Q1					
	Wage Level 2009:Q1 (Billions)	Total Share of State Wages 2009:Q1 (%)	Wage Level 2007:Q1 (Billions)	Total Share of State Wages 2007:Q1 (%)	2007:Q1 to 2009:Q1 (Percent Change)
NYS Total	**511.2**		**600.7**		**(14.9)**
Downstate	**411.1**	**80.4**	**500.4**	**83.3**	**(17.8)**
New York City	308.7	60.4	394.6	65.7	(21.8)
Long Island	57.6	11.3	58.3	9.7	(1.2)
Mid-Hudson	44.8	8.8	47.5	7.9	(5.7)
Upstate	**100.1**	**19.6**	**100.3**	**16.7**	**(0.2)**
Capital	20.8	4.1	20.1	3.3	3.7
Mohawk Valley	5.7	1.1	5.7	0.9	0.3
North Country	5.1	1.0	5.1	0.9	(0.8)
Central New York	13.4	2.6	13.3	2.2	0.8
Southern Tier	11.0	2.2	11.1	1.9	(1.4)
Western New York	22.9	4.5	23.3	3.9	(1.8)
Finger Lakes	21.3	4.2	21.7	3.6	(2.0)

Note: New York State total does not include unclassified data.
Source: NYS Department of Labor, QCEW.

As the share of wages distributed across regions of the State is uneven, growth rates across regions are also disparate. This reflects the diverse economic characteristics of each region in the State. These disparities contributed to how differently each region was affected by the recent recession. Although all regions in New York State experienced a drop in employment between the first quarter of 2007 and the first quarter of 2009, wages increased in some regions but fell in others.

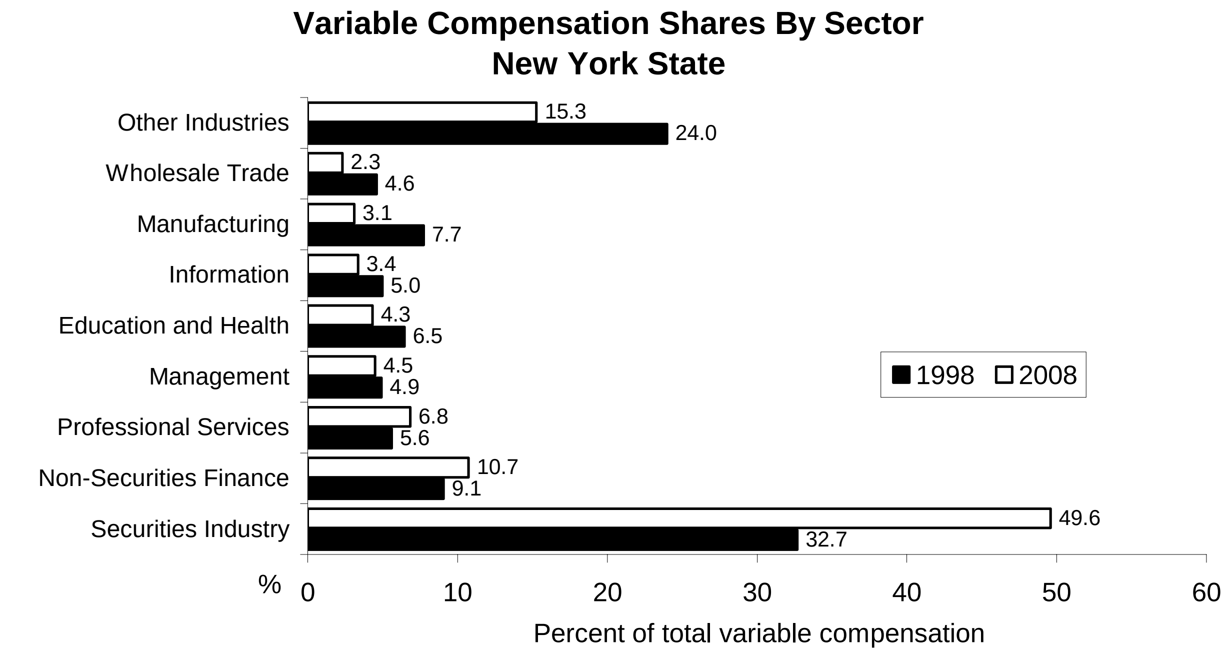
All regions in downstate experienced a loss of wages. The recent recession was led by a downturn in the financial sector. Wages in New York City were particularly hard hit because New York State's financial sector is centered in New York City. City wages fell 21.8 percent, the largest percentage drop of any region in the State, and accounted for 96 percent of total wages lost in the State.

Variable Compensation

Variable compensation is the most volatile component of New York wages and plays an important role in the forecasting of State wages. Even though the share of variable compensation in total wages is small compared to base wages, its impact on changes in total compensation cannot be ignored. Variable compensation accounted for an estimated average of 12.3 percent of total State compensation from 2004 to 2008, increasing from around 5 percent in the 1970s. The share reached a high of 14.5 percent in 2007. In 2009, however, this percentage is estimated to have fallen to 10.0 percent as financial firms drastically cut back on bonus payouts in the face of billions of dollars in losses.

The NYS Assembly Ways and Means Committee staff estimates that New York State total variable compensation, which was $73.4 billion in 2007, fell 4.6 percent to $70.1 billion in 2008 as financial services companies began to cut back. Total variable compensation is estimated to have decreased by 31.6 percent to $48.0 billion in 2009. This is the largest decline since estimates of the series began in 1975. The declines are a direct result of a major pullback in securities industry bonus payments, which are estimated to have fallen 45.3 percent. Much of this decline is accounted for in State wage data in the first quarter of 2009, when firms paid lower bonuses based on dismal company results for calendar year 2008.

The securities industry accounts for the largest portion of State variable compensation paid in New York State (see Figure 60). In 2008, the industry paid 49.6 percent of variable compensation. This share has increased significantly over the past two decades. Before 2000, the securities industry accounted for less than 40 percent of total State variable compensation. By 2007, the share had risen to 51 percent as Wall Street activities reached record levels. This share is estimated to have fallen to approximately 40 percent in 2009.



Note: The *Other Industries* category includes administrative and other services, construction, retail trade, leisure and hospitality, and transportation and utilities.
Sources: NYS Department of Labor; NYS Assembly Ways and Means Committee staff.

Figure 60

Finance and Insurance Sector

The finance and insurance sector is important to the overall health of the New York State economy, especially downstate regions as sector employment is heavily concentrated in New York City. While the sector accounted for less than 7.0 percent of total State employment in 2008, the industry comprised 21.4 percent of total State wages. As a result, the performance of the finance and insurance sector has a considerable impact on State tax revenues.

Finance and insurance variable compensation accounted for more than half of total State variable wages in 2008. It is the most volatile component of State wages and as such is a major forecast risk to the New York State forecast. Finance and insurance bonuses are related to securities industry revenues and profits. Given the recent turmoil in the industry, revenues may no longer automatically translate into strong profits as many firms take write-downs, which lead to lower profits. As problems in the housing and the credit markets continued to intensify throughout the recent recession that began in December 2007, industry revenue and profits declined. Slow activities, asset degradation, huge write-downs by many firms, as well as the closure of financial institutions contributed to the poor performance of Wall Street firms.

On a fiscal year basis, New York State finance and insurance variable compensation fell 42.9 percent in SFY 2008-09 to $24.6 billion, while total variable compensation fell 32.2 percent. As the national economy came out of recession in the second half of 2009, financial firms were expected to pay higher bonuses. However, as public pressure has risen, firms have changed their bonus payment structure from cash to more long-term stock options. As a result, finance and insurance variable compensation is expected to rise by only 6.0 percent to $26.0 billion in SFY 2009-10, before rising further to $31.6 billion in SFY 2010-11.[65]

The recent recession led to a major slowdown in Wall Street activities that had traditionally helped the securities industry attain huge profits. For example, after setting record deals in 2007, merger and acquisitions (M&A) activity slowed markedly in 2008. Announced M&A activities dropped 29.6 percent to $2.9 trillion in 2008, the lowest level since 2005. Contributing to this decline was the tight credit market, which led to a record high number of withdrawn M&A transactions as dealmakers were unable to obtain favorable financing. M&A activities remained slow in the first nine months of 2009. The volume of announced worldwide M&A in the first nine months of 2009 was down 38.2 percent from the first nine months of 2008. Similarly, the value of announced U.S. M&A deals in the first nine months of 2009 dropped 41.1 percent from the same period last year to $496.7 million.[66] As the economy emerged from recession and credit conditions improved, M&A activity increased significantly in the fourth quarter of 2009 with more than 2,000 announced deals in the U.S. valued at over $200 billion.[67] Although there is still uncertainty in the market, easing credit conditions and an improving economy should cause M&A activity to continue to improve in 2010.

Initial public offering (IPO) activities, another area that can be very lucrative for securities industry firms, have also been curtailed. The number of IPOs issued in 2008 was the lowest since Dealogic started to track the market in 1995.[68] The total value of IPOs globally was also sharply down in 2008 compared to 2007 and has still not rebounded. As

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[65] However, if firms that do not currently face bonus restrictions continue to pay a large portion of their bonuses in cash, it could spur firms to shift bonuses back towards cash in order to hold on to talented staff that may migrate towards larger cash bonuses.

[66] Thomson Reuters: "Mergers & Acquisitions Review," Financial Advisors, third quarter of 2009.

[67] Thomson Reuters: "Mergers & Acquisitions Review," Financial Advisors, fourth quarter of 2009.

[68] Lacey Rose, "NBC Universal, Vivendi's Idle Threat," *Forbes.com* (Los Angeles) October 29, 2009.

Wall Street recovers and investors regained their appetites for risk, IPO activities started to rebound in the fourth quarter of 2009 with more activity in the quarter than in the previous nine months.

Firms in the securities industry were not the only businesses in the financial sector affected during the recession. Since the financial crisis started, a record number of banks have gone bankrupt. In 2009, 140 banks failed.[69] This has placed enormous strain on the Federal Deposit Insurance Corporation (FDIC), which raised $45 billion by requiring banks to prepay the amount they would owe the FDIC in insurance premiums for the next three years in December 2009.[70] Since last year, sixteen additional banks have failed and it is expected that the prepaid fee will soon be depleted.

The finance and insurance sector profit and bonus outlook may be forever changed as major investment banks collapsed and converted to bank holding companies, and the financial system continues to face a major overhaul. More federal oversight and regulation over the sector's operation, especially over bonus payments, may occur. These payments may be more in the form of stock options instead of cash payments, which would contribute to the difficulty in determining the timing of when employees would receive income from a bonus award.

As the world economy recovers from recession, demand for financial services will likely increase. As a result, Wall Street revenue is expected to increase and the financial sector is anticipated to post improved profits in 2010. However, finance and insurance sector employment in New York State and the nation is not expected to improve on an annual average basis until 2011 as firms may be reluctant to hire until they are certain about the future of the sector.

State Housing Market

The New York State housing market performed better than the nation in both the housing boom and during the correction. More home choices, moderate prices, low mortgage interest rates, and a lower rate of job losses helped to keep the State housing market on solid ground until recently. During the six-year period from the third quarter of 2001 to the third quarter of 2007, home prices in the State grew by 66.2 percent,

[69] Federal Deposit Insurance Corporation, Failed Bank List, January 20, 2010, www.fdic.gov/bank/individual /failed/banklist.html.
[70] Binyamin Appelbaum, "Banks to Prepay FDIC for Failures," *Washington Post*, November 13, 2009.

compared to 48.9 percent in the nation. Home prices in both the State and the nation have declined since the start of the housing correction in mid-2007. From the third quarter of 2007 to the third quarter of 2009, overall State home prices declined by 6.5 percent, while national home prices declined by 7.8 percent. The fall in overall home prices in New York State is attributed to the depreciation in downstate's property prices, which inflated significantly during the housing boom. Home prices in upstate were less affected by the real estate cycle than downstate, and continued to appreciate in most metros throughout the recent recession (see Table 13).

Table 13

Home Price Change by New York State Metropolitan Area
2001:Q3 to 2009:Q3
(Percent Change)

	FHFA Existing Home Price Index	
	2001:Q3-2007:Q3	**2007:Q3-2009:Q3**
Buffalo-Niagara Falls	29.3	4.1
Rochester	21.9	3.1
Syracuse	39.1	3.0
Albany-Schenectady-Troy	72.4	(1.3)
New York-White Plains	78.6	(10.1)
Nassau-Suffolk	78.2	(10.7)
New York City (Case-Schiller)	70.9	(15.9)
New York State	**66.2**	**(6.5)**
U.S.	**48.9**	**(7.8)**

Note: The FHFA index presented herein may show different price changes from the S&P/Case-Shiller Index in Figure 25. This is because the two indices use different data. The FHFA index is based on homes with conforming loans, which have a loan limit of $417,000 for single-family homes. Therefore, the FHFA index does not reflect price changes for more expensive homes. FHFA index also included both sales and appraisal data.

Source: Federal Housing Finance Agency (FHFA).

As of September 2009, New York State had the second lowest rate of mortgage holders in negative equity at 6.2 percent. It was estimated that more than 100,000 of the State's mortgages were in negative equity, with another 41,200 mortgages in danger of entering negative equity.[71]

[71] First American CoreLogic's data report is based on 47 million properties that have a first and/or second mortgage, which account for over 90 percent of all mortgages in the U.S. See First American CoreLogic, "First American CoreLogic's Negative Equity Data Report" (as of November 2009).

Although the housing market in the State outperformed the nation, the market remains fragile. As in the nation, adjustable rate mortgages (ARMs) had become popular in recent years. In New York State, the number of subprime mortgage originations with adjustable rates rose from 3,110 loans in the third quarter of 1998 to more than 100,000 loans in the third quarter of 2007. Subprime ARMs originations dropped to less than 73,000 loans in the third quarter of 2009. Foreclosure filings in the State have been increasing rapidly since mid-2006, especially for those subprime borrowers with ARMs. As of the third quarter of 2009, foreclosure rates for subprime borrowers with ARMs were almost four times that of subprime borrowers who had fixed-rate mortgages (FRMs). The overall foreclosure rate for subprime borrowers with ARMs in the State rose from 5.8 percent in the third quarter of 2006 to 32.5 percent at the end of the third quarter of 2009. Moreover, 10.0 percent of these subprime loans with ARMs are scheduled to have their interest rates reset in the next twelve months, much higher than the national rate of 5.5 percent.[72] This imposes a significant downside risk on the New York State housing market as it could create more foreclosures if these mortgage holders cannot afford new mortgage payments at a higher interest rate and cannot refinance their mortgages.

Housing has become more affordable recently as home prices have fallen faster than income. The national housing affordability index reached a record high in early 2009 and remains near record highs, with more than 70 percent of homes sold in the third quarter of 2009 affordable to families earning the national median income, up from 56.1 percent during the third quarter of 2008. The ratio of the median home price divided by median household income in the nation dropped from 4.1 in the third quarter of 2007 to 2.8 in the third quarter of 2009. This ratio also improved in most metros of New York. For example, New York/White Plains fell from 8.8 to 6.6. As a result, the NAHB/Wells Fargo Housing Opportunity Index in the New York/White Plains area rose significantly from 7.1 percent in the third quarter of 2007 to 19.2 percent in the third quarter of 2009.[73]

Despite improvement in housing affordability, a large disparity in housing affordability exists in the State.[74] Upstate homes are much more affordable than homes in downstate areas. As of the third quarter of 2009, out of 227 metros nationwide, four of the nine upstate metros ranked in the top fifty of most affordable metros, while three of the four

[72] Federal Reserve Bank of New York, "United States Credit Conditions," November 2009. http://data.newyorkfed.org/creditconditions/.

[73] The Housing Opportunity Index is defined as the share of homes sold in the area that would have been affordable to a family earning the median income (i.e., the total monthly payment is less than 28 percent of the monthly median household income).

[74] Housing is considered affordable when it costs less than 30 percent of household's income.

downstate metros ranked in the bottom fifty (least affordable).[75] Residents in downstate face a much higher housing cost burden than those in upstate, especially those who rent. In 2008, less than 35 percent of all New York homeowners paid more than 30 percent of their income on housing, while nearly half of all renters paid more than 30 percent of their income on housing. Regionally, housing burden was highest in Long Island, where 44.3 percent of homeowners and 54.1 percent of renters paid more than 30 percent of their income on housing. On the contrary, only 22.1 percent of homeowners and 40.9 percent of renters in Binghamton paid more then 30 percent of their income on housing (see Table 14).

Table 14

Housing Cost Burden by New York State Metropolitan Area 2008

	Owner		Renter	
	Owner-Occupied Housing Units Total	**Percent with Housing Costs Over 30% of Household Income**	**Renter-Occupied Housing Units Total**	**Percent with Housing Costs Over 30% of Household Income**
Metropolitan Statistical Area				
Long Island	754,254	44.3	156,781	54.1
New York City	1,031,691	39.4	2,023,584	47.9
Poughkeepsie-Newburgh-Middletown	163,120	38.8	62,138	51.0
Kingston	48,267	35.3	20,992	46.5
Glens Falls	37,368	32.2	14,732	45.5
Ithaca	20,534	26.6	17,110	49.7
Albany-Schenectady-Troy	225,669	26.6	111,638	44.8
Rochester	277,492	25.6	122,213	51.8
Buffalo-Niagara Falls	314,396	24.3	152,778	46.4
Syracuse	171,714	23.9	78,925	46.2
Utica-Rome	78,906	22.4	37,719	42.9
Binghamton	68,528	22.1	30,739	40.9
Elmira	23,485	19.6	11,241	51.1
New York State	**3,941,790**	**34.6**	**3,158,150**	**47.6**
United States	**75,515,104**	**30.5**	**36,862,873**	**45.6**

Note: Housing costs for homeowners include mortgage payment, real estate taxes, fire hazard and flood insurance, utilities, and fuels. Housing costs for renters is gross rent.
Source: U.S. Census Bureau, 2008 American Community Survey.

[75] National Association of Home Builders, "NAHB/Wells Fargo Housing Opportunity Index (HOI)," November 19, 2009, http://www.nahb.org/fileUpload_details.aspx?contentID=535.

While residential real estate activities in the State have performed relatively well, commercial real estate, especially the office market, deteriorated in 2008 and 2009. In Manhattan, slow demand due to layoffs caused leasing activity to drop by almost 45 percent in the second quarter of 2009 compared to the same period in 2008.[76] The overall vacancy rate in Manhattan rose from 7.0 percent in the third quarter of 2008 to 9.6 percent in the third quarter of 2009, while the average rental rate dropped from $65.40 per square foot per year to $51.42 per square foot per year.[77] Looking forward, the office market will remain weak in 2010 as employment in the key office-using industries such as finance and insurance, professional services, and information are expected to continue to decline.

Capital Gains

The performance of financial markets, particularly equity markets and the real estate market, is an important indicator of capital gains realizations. In 2003, corporate equity holdings accounted for 26.1 percent of the share of total U.S. net capital gains, while real estate accounted for 31.5 percent, and pass-through gains made up 35.9 percent. Contrastingly, in 1999 gains from corporate stocks represented 42.7 percent of U.S. net capital gains, while real estate and pass-throughs comprised 11.1 percent and 25.2 percent of total U.S. net capital gains, respectively.[78]

The housing market started showing signs of weakness in 2006 when home prices in the U.S. grew only 8.2 percent after double-digit gains in the previous two years. Home prices decreased by 3.6 percent by the end of 2008. The prolonged contraction of the housing market also resulted in the decline of housing prices in the State by 1.1 percent in 2008. The turmoil in the financial markets, sparked by the distressed housing market, led to the stock markets falling significantly through the end of 2007. Accordingly, these disturbances have had a significant adverse effect on capital gains realizations in New York State.

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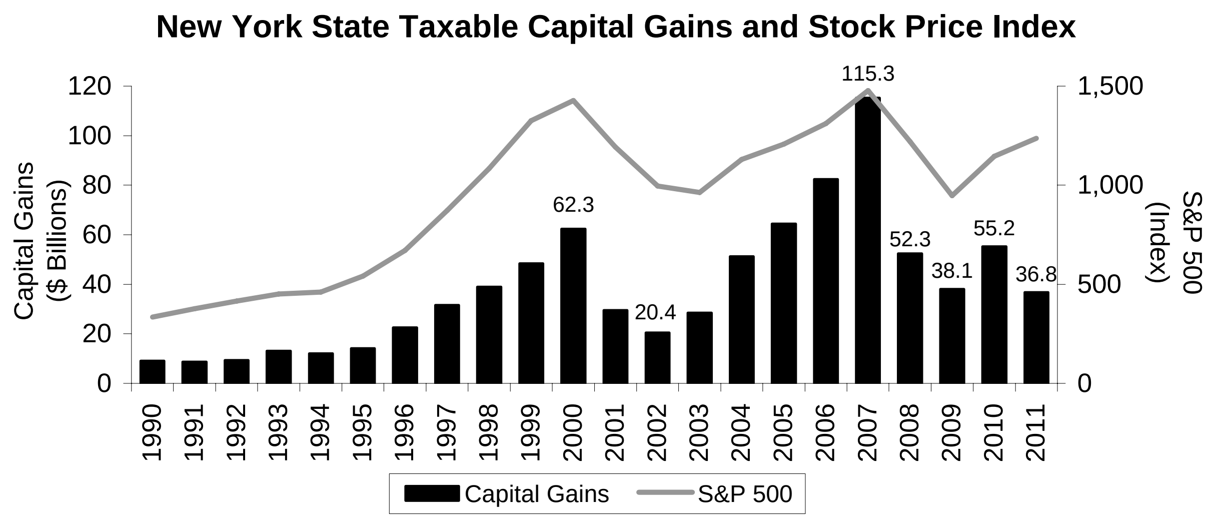
[76] Cushman & Wakefield Inc, "Manhattan Office Report 2Q09," *Local Market Reports*, Second Quarter 2009.

[77] Colliers ABR, "The Bridge to Recovery," *Barometer*, Third Quarter 2009, (New York City) http://www.colliers.com/Content/Repositories/Base/Markets/NewYork/English/Market_Report/PDFs/Barometer_3Q2009.pdf.

[78] Pass-through gains include capital gains sold by partnerships, S Corporations, estates and trusts, and distributions to be taxed at the individual partner, shareholder, and beneficiary level. See, Janette Wilson and Pearson Liddell, "Sales of Capital Assets Panel Data, Tax Years 1999-2003," *Statistics of Income Bulletin*, Internal Revenue Service, Summer 2009.

Capital gains realizations grew rapidly during the booming stock market of the late 1990s, but plummeted in 2001, triggered by the steep decline in stock prices from post-bubble corrections in the stock market and the events of September 11th.[79] After a further decline in 2002, taxable capital gains began to steadily rise in 2003 with the recovering stock market and the strengthening housing market (see Figure 61). The stock market peaked again in 2007 with record level taxable capital gains in both the U.S. and New York State.



Note: Capital gains data for 2008 is estimated; the first forecast period is 2009. The first forecast period for S&P 500 is 2010.
Sources: NYS Department of Taxation and Finance; NYS Assembly Ways and Means Committee staff.

Figure 61

Since capital gains is only realized when the sale price of assets exceeds the purchase price of assets, the disparity between current year asset prices and prior years' asset prices has important implications for capital gains realization in current and future years. If an investor purchased stocks in 2004 and sold them in 2007, capital gains were most likely realized since on average equity prices were much higher in 2007 than 2004 based on the S&P 500.

New York State posted taxable capital gains of $115.3 billion in 2007. However, the overall decline in economic growth coupled with the deterioration in the housing market and the significant falloff in corporate equity prices led to an estimated 54.6 percent

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79 New York State capital gains were more adversely affected by the events of September 11th because the equity market is one of the most important sectors in the State.

decline in taxable capital gains in 2008. Despite improvements in the stock market beginning in mid-2009, taxable capital gains are estimated to have fallen an additional 27.2 percent in 2009 to $38.1 billion as home prices remained depressed and investors faced stock prices that were lower than in prior years.

The Economic Growth and Tax Relief Reconciliation Act of 2001, which included provisions that reduced the tax rate on capital gains from 20 percent to 15 percent effective in 2002, is set to expire in 2011. Accordingly, taxable capital gains are forecast to increase 45.0 percent to $55.2 billion in 2010, partly reflecting a continued recovery in the financial market and investors' response to the anticipated rise in capital gains taxes in 2011. The selling off of certain assets to take advantage of the lower tax rate in 2010 begets a pullback in 2011. Taxable capital gains are forecast to decline 33.4 percent in 2011 to $36.8 billion.

New York State Forecast Comparison

The NYS Assembly Ways and Means Committee staff's forecast for total nonfarm payroll employment growth for the State in 2010 is negative 0.4 percent (see Table 15). The staff forecast is 0.2 percentage point above the Division of the Budget, and 0.4 percentage point higher than Moody's Economy.com. The staff's forecast for State wages for 2010 is 5.2 percent. The staff forecast is 1.7 percentage point above the Division of the Budget, and 2.5 percentage points above Moody's Economy.com.

The Assembly Ways and Means Committee staff's employment growth forecast for 2011 is 0.9 percent. The staff forecast is 0.2 percentage point below Moody's Economy.com, and 0.1 percentage point above the Division of the Budget. The staff's forecast for New York State wages for 2011 is 0.5 percent. The staff's forecast is lower than Moody's Economy.com and the Division of the Budget.

Table 15

New York State Forecast Comparison (Percent Change)	Actual 2008	Estimate 2009	Forecast 2010	Forecast 2011
Employment				
Ways and Means	0.5	(2.8)	(0.4)	0.9
Division of the Budget	0.6	(2.9)	(0.6)	0.8
Moody's Economy.com	0.7	(2.1)	(0.8)	1.1
Wages (Calendar Year)				
Ways and Means	2.0	(7.4)	5.2	0.5
Division of the Budget	2.0	(7.0)	3.5	3.1
Moody's Economy.com	2.2	(5.4)	2.7	2.2
Wages (Fiscal Year)	**2008-09**	**2009-10**	**2010-11**	**2011-12**
Ways and Means	(3.1)	(2.2)	4.1	5.1
Division of the Budget	(3.1)	(2.5)	3.9	4.9

Note: Calendar year wage numbers are affected by a shift of wages from the first quarter of 2011 to the fourth quarter of 2010, as a result of the expiration of federal tax cuts. Differences in the amounts assumed for the shift may account for some of the difference between calendar year numbers. The fiscal year wage numbers are not affected by this shift.

Sources: NYS Assembly Ways and Means Committee staff; Division of the Budget, Executive Budget 2010-11, February 9, 2010; Moody's Economy.com, January 2010.

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RISKS TO THE FORECAST

Several risks to the economic outlook of the nation and New York State remain. Problems that were central to the recent recession continue to a certain extent, including weaknesses in the housing market and uncertainty in the financial markets. If these areas were to worsen again, the impact on the outlook would be significant.

Energy prices continue to have an impact on the economic outlook, and the long-term outlook for energy prices continues to be difficult to pinpoint. Should energy prices spike for an extended period of time, economic growth could be curtailed and inflation could be a major concern. However, should energy prices decrease, growth may be stronger than forecast.

Long-term behavior of the consumer is also a risk to the outlook presented in this report, which assumes the consumer will slowly start to spend again. If consumers should curtail spending for a more extended period of time, the outlook presented in this report may be too optimistic. A return of consumer confidence also plays a strong role in the recovery. Bad news such as further write-downs, company bankruptcies, further layoffs, and investment scandals has the potential to depress confidence in the ability of the economy to continue to recover.

Actions by the government also add uncertainty to the forecast. If the economy does not become self-sustaining from the many fiscal policies implemented to spur growth, the outlook presented in this report would be less optimistic.

As the economy improves, stability in the financial markets and credit availability remain issues that can have significant impacts on the economy, and these present risks going forward. If credit conditions do not ease further, even with the help from the federal government and the Federal Reserve, it could have dismal implications for the recovery path set forth in this report.

The health of the global economy is also a concern. If the global economy was not to recover as assumed, the ability of the United States economy to grow would be impacted. Many global issues add uncertainty to the outlook, including the wars in Iraq and Afghanistan, tensions in the Middle East, and other geo-political issues.

The current economic climate presents particular challenges and risks to the New York State forecast. Since the extent to which the Wall Street landscape will be permanently changed when the economy emerges from the current crisis is still unclear, there is great ambiguity surrounding the State outlook. Wall Street and the financial markets play a central role in the State economy, and drastic cuts to or changes in the composition of Wall Street compensation (including bonuses) and the resulting reductions in Wall Street tax revenues have critical implications for the economic health of the State. However, a faster turnaround than expected for Wall Street activities offers some upside potential for the forecast.

APPENDIX A

U.S. Recessions Since World War II (Based on Series-Specific Turning Points)					
GDP			**Employment**		
Peak to Trough	**Duration (Quarters)**	**Depth**	**Peak to Trough**	**Duration (Quarters)**	**Depth**
1948:Q4-1949:Q4	4	(1.6%) ($29.5)	1948:Q3-1949:Q4	5	(4.4%) (1,973.0)
1953:Q2-1954:Q1	3	(2.7%) ($62.7)	1953:Q2-1954:Q3	5	(3.2%) (1,635.0)
1957:Q3-1958:Q1	2	(3.7%) ($97.7)	1957:Q2-1958:Q2	4	(4.1%) (2,200.7)
1960:Q1-1960:Q4	3	(1.6%) ($45.1)	1960:Q2-1961:Q1	3	(1.7%) (910.0)
1969:Q3-1970:Q4	5	(0.6%) ($26.8)	1970:Q1-1970:Q4	3	(1.0%) (737.7)
1973:Q4-1975:Q1	5	(3.2%) ($157.8)	1974:Q3-1975:Q2	3	(2.7%) (2,087.3)
1980:Q1-1980:Q3	2	(2.2%) ($131.9)	1980:Q1-1980:Q3	2	(0.9%) (847.0)
1981:Q3-1982:Q3	4	(2.7%) ($163.8)	1981:Q3-1982:Q4	5	(3.0%) (2,734.3)
Average over All Previous Recessions	3.5	(2.3%) ($89.4)	Average over All Previous Recessions	3.8	(2.6%) (1,640.6)
1990:Q2-1991:Q1	3	(1.4%) ($109.4)	1990:Q2-1991:Q3	5	(1.4%) (1,498.3)
2000:Q4-2001:Q3	3	0.0% 5.6	2001:Q1-2003:Q2	9	(2.0%) (2,657.3)
2008:Q2-2009:Q2	4	(3.8%) ($513.7)	2008:Q1-2009:Q4	7	(6.0%) (8,271.0)

Note: Depth is defined as the level change from the peak level to the trough level. GDP is in billions of chained 2005 dollars. Employment is non-farm total in thousands. The percentages are the depth divided by the peak level.

Sources: U.S. Bureau of Economic Analysis; U.S. Bureau of Labor Statistics, CES; NYS Assembly Ways and Means Committee staff.

APPENDIX B

U.S. Recessions Since World War II (Based on Series-Specific Turning Points)					
Consumption			Investment		
Peak to Trough	Duration (Quarters)	Depth	Peak to Trough	Duration (Quarters)	Depth
1948:Q4-1949:Q4	No Decline	3.4% 40.4	1948:Q3-1949:Q2	3	(31.0%) ($75.2)
1953:Q2-1953:Q4	2	(0.9%) ($12.7)	1953:Q2-1954:Q2	4	(11.1%) ($27.6)
1957:Q4-1958:Q1	1	(1.4%) ($22.3)	1957:Q3-1958:Q2	3	(17.2%) ($47.7)
1960:Q2-1960:Q3	1	(0.4%) ($7.1)	1960:Q1-1960:Q4	3	(21.7%) ($71.9)
1970:Q3-1970:Q4	1	(0.3%) ($7.5)	1969:Q3-1970:Q1	2	(8.4%) ($43.5)
1973:Q3-1974:Q1	2	(1.2%) ($37.0)	1973:Q4-1975:Q2	6	(29.4%) ($198.2)
1979:Q4-1980:Q2	2	(2.4%) ($92.8)	1978:Q4-1980:Q3	7	(19.9%) ($163.2)
1981:Q3-1981:Q4	1	(0.8%) ($29.0)	1981:Q3-1982:Q4	5	(22.5%) ($181.3)
Average over All Previous Recessions	1.4	(0.5%) ($21.0)	Average over All Previous Recessions	4.1	(20.1%) ($101.1)
1990:Q3-1991:Q1	2	(1.1%) ($56.6)	1990:Q2-1991:Q2	4	(12.7%) ($129.7)
2000:Q4-2001:Q3	No Decline	1.2% $94.2	2000:Q2-2001:Q4	6	(14.2%) ($287.3)
2007:Q4-2009:Q2	6	(1.9%) ($174.6)	2006:Q1-2009:Q2	13	(35.7%) ($808.0)

Note: Depth is defined as the level change from the peak level to the trough level. Consumption and investment are in billions of chained 2005 dollars. The percentages are the depth divided by the peak level.

Sources: U.S. Bureau of Economic Analysis; U.S. Bureau of Labor Statistics, CES; NYS Assembly Ways and Means Committee staff.

APPENDIX C

NYS Employment and Wages in NAICS Sectors

	Employment (Thousands)			Wages ($ in Billions)		
	Estimate 2009	Forecast 2010	Forecast 2011	Estimate 2009	Forecast 2010	Forecast 2011
Total	**8,335.2**	**8,302.0**	**8,377.1**	**480.2**	**505.1**	**507.6**
Education & Health	1,553.6	1,584.1	1,615.5	68.3	71.7	75.7
Government	1,443.3	1,438.5	1,436.7	75.7	77.9	80.2
Retail Trade	856.9	849.7	855.6	24.5	24.8	25.5
Other Services	728.9	739.3	750.4	27.4	28.4	29.3
Financial Activities	678.9	665.0	669.5	95.9	109.9	99.2
Leisure & Hospitality	704.6	704.0	719.2	18.4	19.0	19.9
Professional Services	561.8	556.0	567.1	49.3	51.6	53.1
Manufacturing	483.3	461.2	446.6	27.2	27.0	27.1
Construction	323.6	312.6	321.8	19.4	19.6	20.6
Wholesale Trade	331.1	328.0	329.6	22.9	23.1	23.8
Transport & Utilities	258.1	254.8	256.4	12.9	13.0	13.4
Information	252.4	247.0	244.4	21.9	22.0	22.6
Management of Companies	133.0	134.3	136.8	15.5	16.1	16.4

Note: Some NAICS sectors are grouped with others. For sector definitions, see Appendix I.

Sources: NYS Department of Labor, QCEW; NYS Assembly Ways and Means Committee staff.

NYS Employment and Wage Growth in NAICS Sectors
(Percent Change)

	Employment			Wages		
	Estimate 2009	Forecast 2010	Forecast 2011	Estimate 2009	Forecast 2010	Forecast 2011
Total	**(2.8)**	**(0.4)**	**0.9**	**(7.4)**	**5.2**	**0.5**
Construction	(9.9)	(3.4)	2.9	(8.7)	0.8	5.4
Education & Health	2.0	2.0	2.0	3.2	5.0	5.6
Government	(0.1)	(0.3)	(0.1)	1.8	2.9	3.0
Leisure & Hospitality	(1.5)	(0.1)	2.2	(2.3)	3.3	4.3
Professional Services	(4.1)	(1.0)	2.0	(4.6)	4.6	3.0
Transport & Utilities	(4.3)	(1.3)	0.6	(4.6)	1.0	3.0
Other Services	(4.2)	1.4	1.5	(4.3)	3.6	3.2
Retail Trade	(4.2)	(0.8)	0.7	(7.2)	1.3	2.7
Wholesale Trade	(5.7)	(1.0)	0.5	(6.1)	1.2	2.6
Information	(3.7)	(2.2)	(1.0)	(5.2)	0.3	2.7
Management of Companies	1.1	0.9	1.9	(11.6)	3.7	1.8
Financial Activities	(5.7)	(2.0)	0.7	(20.8)	14.6	(9.8)
Manufacturing	(10.1)	(4.6)	(3.2)	(11.6)	(0.8)	0.3

Note: Some NAICS sectors are grouped with others. For sector definitions, see Appendix I.

Sources: NYS Department of Labor, QCEW; NYS Assembly Ways and Means Committee staff.

APPENDIX E

New York State Economic Outlook State Fiscal Year		Actual 2008-09	Estimate 2009-10	Forecast 2010-11	Forecast 2011-12
Employment	***Percent Change***	(0.3)	(2.6)	0.1	1.0
	Level	8,529.9	8306.8	8316.8	8401.1
Personal Income	***Percent Change***	(1.0)	(0.9)	4.0	4.8
	Level	909.6	901.0	936.8	982.2
Total Wages	***Percent Change***	(3.1)	(2.2)	4.1	5.1
	Level	494.2	483.1	503.2	528.6
Base Wages	***Percent Change***	1.7	(2.7)	2.9	4.0
	Level	445.2	433.2	445.7	463.3
Variable Compensation	***Percent Change***	(32.2)	2.0	15.1	13.6
	Level	49.0	50.0	57.5	65.3
CPI (1982-84=100)	***Percent Change***	3.3	0.6	2.2	2.4
	Level	236.5	237.9	243.2	249.1

Note: Employment level is in thousands; wage and personal income levels are in billions of dollars.
Sources: U.S. Bureau of Economic Analysis; NYS Department of Labor, QCEW; U.S. Bureau of Labor Statistics; NYS Assembly Ways and Means Committee staff.

APPENDIX F

U.S. Economic Outlook (Levels)				
	Actual 2008	**Estimate 2009**	**Forecast 2010**	**Forecast 2011**
Real GDP*	13,312.2	12,991.6	13,364.3	13,734.9
Real Consumption*	9,290.9	9,238.2	9,419.1	9,650.2
Real Investment*	1,989.5	1,525.0	1,696.3	1,882.6
Real Exports*	1,629.3	1,468.6	1,601.3	1,712.2
Real Imports*	2,123.5	1,822.4	1,975.1	2,124.1
Real Government*	2,518.0	2,566.4	2,611.2	2,602.6
*Federal**	975.9	1,026.6	1,069.5	1,065.9
*State and Local**	1,543.7	1,542.8	1,545.1	1,540.1
Personal Income**	12,238.8	12,072.1	12,517.7	13,020.7
*Wages & Salaries***	6,545.9	6,330.6	6,535.7	6,775.5
Corporate Profits (Economic Basis)**	1,360.4	1,310.5	1,445.1	1,595.4
Productivity (1992=100)	142.6	146.8	152.3	154.1
Employment***	136.8	130.9	130.1	131.9
CPI-Urban (1982-84=100)	215.2	214.6	219.4	224.0
S&P 500 Stock Price (1941-43=10)	1,220.9	946.7	1,146.2	1,236.4
Treasury Bill Rate (3-month)****	1.4	0.2	0.3	1.8
Treasury Bond Rate (10-year)****	3.7	3.3	3.6	4.4

* In billions of chained 2005 dollars.
** In billions of dollars.
*** In millions.
**** Annual average rate.

Sources: U.S. Bureau of Economic Analysis; U.S. Bureau of Labor Statistics; Federal Reserve; Standard and Poor's; NYS Assembly Ways and Means Committee staff.

APPENDIX G

U.S. Economic Outlook (Percent Change)	Actual 2008	Estimate 2009	Forecast 2010	Forecast 2011
Real GDP	0.4	(2.4)	2.9	2.8
Real Consumption	(0.2)	(0.6)	2.0	2.5
Real Investment	(7.3)	(23.3)	11.2	11.0
Real Exports	5.4	(9.9)	9.0	6.9
Real Imports	(3.2)	(14.2)	8.4	7.5
Real Government	3.1	1.9	1.7	(0.3)
Federal	7.7	5.2	4.2	(0.3)
State and Local	0.5	(0.1)	0.2	(0.3)
Personal Income	2.9	(1.4)	3.7	4.0
Wages & Salaries	2.1	(3.3)	3.2	3.7
Corporate Profits (Economic Basis)	(11.8)	(3.7)	10.3	10.4
Productivity	1.8	3.0	3.7	1.2
Employment	(0.6)	(4.3)	(0.6)	1.3
CPI-Urban	3.8	(0.3)	2.3	2.1
S&P 500 Stock Price	(17.3)	(22.5)	21.1	7.9
Treasury Bill Rate (3-month)*	1.4	0.2	0.3	1.8
Treasury Note Rate (10-year)*	3.7	3.3	3.6	4.4

* Annual average rate.

Sources: U.S. Bureau of Economic Analysis; U.S. Bureau of Labor Statistics; Federal Reserve; Standard & Poor's; NYS Assembly Ways and Means Committee staff.

U.S. Economic Outlook
State Fiscal Year
(Percent Change)

	Actual 2008-09	Estimate 2009-10	Forecast 2010-11	Forecast 2011-12
Real GDP	(0.9)	(1.0)	2.8	3.0
Real Consumption	(0.8)	0.2	2.2	2.5
Real Investment	(12.9)	(16.7)	11.9	12.0
Real Exports	0.1	(5.1)	8.2	7.2
Real Imports	(7.1)	(9.3)	8.9	7.6
Real Government	2.7	2.2	1.1	(0.6)
Federal	7.3	5.4	2.8	(0.9)
State and Local	0.1	0.3	(0.0)	(0.3)
Personal Income	1.6	(0.3)	3.8	4.5
Wages & Salaries	0.5	(2.0)	3.4	4.6
Corporate Profits (Economic Basis)	(15.2)	6.8	7.9	7.8
Productivity	1.5	4.1	2.6	1.1
Employment	(1.6)	(4.0)	0.2	1.7
CPI-Urban (1982-84=100)	2.7	0.4	2.1	2.1
S&P 500 Stock Price (1941-43=10)	(25.5)	(6.0)	14.7	7.4
Treasury Bill Rate (3-month)*	0.9	0.1	0.5	2.3
Treasury Note Rate (10-year)*	3.4	3.5	3.7	4.6

* Fiscal year average rate.
Sources: U.S. Bureau of Economic Analysis; U.S. Bureau of Labor Statistics; Federal Reserve; Standard & Poor's; NYS Assembly Ways and Means Committee staff.

APPENDIX I

The North American Industry Classification System (NAICS)

Code	NAICS Title
11	**Agriculture, Forestry, Fishing and Hunting**
111	Crop Production
112	Animal Production
113	Forestry and Logging
114	Fishing, Hunting and Trapping
115	Support Activities for Agriculture and Forestry
21	**Mining**
211	Oil and Gas Extraction
212	Mining (except Oil and Gas)
213	Support Activities for Mining
22	**Utilities**
221	Utilities
23	**Construction**
236	Construction of Buildings
237	Heavy and Civil Engineering Construction
238	Specialty Trade Contractors
31-33	**Manufacturing**
311	Food Manufacturing
312	Beverage and Tobacco Product Manufacturing
313	Textile Mills
314	Textile Product Mills
315	Apparel Manufacturing
316	Leather and Allied Product Manufacturing
321	Wood Product Manufacturing
322	Paper Manufacturing
323	Printing and Related Support Activities
324	Petroleum and Coal Products Manufacturing
325	Chemical Manufacturing
326	Plastics and Rubber Products Manufacturing
327	Nonmetallic Mineral Product Manufacturing
331	Primary Metal Manufacturing
332	Fabricated Metal Product Manufacturing
333	Machinery Manufacturing
334	Computer and Electronic Product Manufacturing
335	Electrical Equipment, Appliance, and Component Manufacturing
336	Transportation Equipment Manufacturing
337	Furniture and Related Product Manufacturing
339	Miscellaneous Manufacturing
42	**Wholesale Trade**
423	Merchant Wholesalers, Durable Goods
424	Merchant Wholesalers, Nondurable Goods
425	Wholesale Electronic Markets and Agents and Brokers

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The North American Industry Classification System (NAICS) -- *(continued)*

Code	NAICS Title
44-45	**Retail Trade**
441	Motor Vehicle and Parts Dealers
442	Furniture and Home Furnishings Stores
443	Electronics and Appliance Stores
444	Building Material and Garden Equipment and Supplies Dealers
445	Food and Beverage Stores
446	Health and Personal Care Stores
447	Gasoline Stations
448	Clothing and Clothing Accessories Stores
451	Sporting Goods, Hobby, Book, and Music Stores
452	General Merchandise Stores
453	Miscellaneous Store Retailers
454	Nonstore Retailers
48-49	**Transportation and Warehousing**
481	Air Transportation
482	Rail Transportation
483	Water Transportation
484	Truck Transportation
485	Transit and Ground Passenger Transportation
486	Pipeline Transportation
487	Scenic and Sightseeing Transportation
488	Support Activities for Transportation
491	Postal Service
492	Couriers and Messengers
493	Warehousing and Storage
51	**Information**
511	Publishing Industries (except Internet)
512	Motion Picture and Sound Recording Industries
515	Broadcasting (except Internet)
516	Internet Publishing and Broadcasting
517	Telecommunications
518	Internet Service Providers, Web Search Portals, and Data Processing Services
519	Other Information Services
52	**Finance and Insurance**
521	Monetary Authorities - Central Bank
522	Credit Intermediation and Related Activities
523	Securities, Commodity Contracts, and Other Financial Investments and Related Activities
524	Insurance Carriers and Related Activities
525	Funds, Trusts, and Other Financial Vehicles
53	**Real Estate and Rental and Leasing**
531	Real Estate
532	Rental and Leasing Services
533	Lessors of Nonfinancial Intangible Assets (except Copyrighted Works)

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The North American Industry Classification System (NAICS) -- *(continued)*

Code	NAICS Title
54	**Professional, Scientific, and Technical Services**
541	Professional, Scientific, and Technical Services
55	**Management of Companies and Enterprises**
551	Management of Companies and Enterprises
56	**Administrative and Support and Waste Management and Remediation Services**
561	Administrative and Support Services
562	Waste Management and Remediation Services
61	**Educational Services**
611	Educational Services
62	**Health Care and Social Assistance**
621	Ambulatory Health Care Services
622	Hospitals
623	Nursing and Residential Care Facilities
624	Social Assistance
71	**Arts, Entertainment, and Recreation**
711	Performing Arts, Spectator Sports, and Related Industries
712	Museums, Historical Sites, and Similar Institutions
713	Amusement, Gambling, and Recreation Industries
72	**Accommodation and Food Services**
721	Accommodation
722	Food Services and Drinking Places
81	**Other Services - except Public Administration**
811	Repair and Maintenance
812	Personal and Laundry Services
813	Religious, Grantmaking, Civic, Professional, and Similar Organizations
814	Private Households
92	**Public Administration**
921	Executive, Legislative, and Other General Government Support
922	Justice, Public Order, and Safety Activities
923	Administration of Human Resource Programs
924	Administration of Environmental Quality Programs
925	Administration of Housing Programs, Urban Planning, and Community Development
926	Administration of Economic Programs
927	Space Research and Technology
928	National Security and International Affairs

Source: Executive Office of the President, Office of Management and Budget, North American Industry Classification System, United States, 2002.