William C Dudley: Regional economy and current trends in regional employment

Remarks by Mr William C Dudley, President and Chief Executive Officer of the Federal Reserve Bank of New York, at the Quarterly Regional Economic Press Briefing, New York, 6 May 2011.

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Good morning and welcome once again to the New York Fed's Quarterly Regional Economic Press Briefing. I am pleased to have this opportunity to talk with the journalists covering our region – and through you, to the people in our District. This morning I will discuss national and regional economic conditions, with particular attention to employment trends in the Second Federal Reserve District, which covers New York; northern New Jersey; Fairfield County, Connecticut; Puerto Rico; and the U.S. Virgin Islands. I will not comment on the outlook for monetary policy today but instead will focus on the economy itself. Following my remarks, my colleagues will provide more detail. As always, what I have to say reflects my own views and not necessarily those of the Federal Open Market Committee (FOMC) or the Federal Reserve System.

National economic conditions

I'll begin by commenting on national economic conditions. Since the recession ended in 2009, the economy has grown at a modest pace. When we met in February, the brisker pace of growth in the last quarter of 2010 appeared to be carrying over to the beginning of this year.

Since then growth has been somewhat softer than anticipated, with real gross domestic product (GDP) increasing at only a 1.8 percent annual rate in the first quarter of 2011. A number of factors contributed to the slowdown. Construction activity fell – likely reflecting the continued large supply of unsold homes – and government expenditures at the federal, state and local levels declined.

In addition, real, or inflation-adjusted, consumption growth in the first quarter was slower than in the last quarter of 2010. This occurred, in part, because of the rise in gasoline and food prices that pushed up consumer price inflation last quarter and reduced discretionary income. The rise in energy prices contributed to a fall in consumer confidence, which also may have had a negative impact on consumer spending. However, the weakness of real GDP growth in the first quarter probably will prove temporary. In particular, production and business survey indicators, including the New York Fed's own Empire State Manufacturing Survey, generally continue to signal strength. And financial conditions continue to improve. The temporary reduction in payroll taxes and other fiscal measures also are providing support to demand. In addition, demand abroad – particularly in Asia – remains robust, supporting our exports.

Most importantly, the labor market has shown further improvement, as demonstrated by today's employment report. Although payroll employment growth has been subdued during most of this recovery, the latest figures show the economy added 244,000 jobs in April – and an average of 233,000 over each of the past three months. While the unemployment rate – which is based on a different survey – ticked higher last month to 9 per cent it is nonetheless 0.8 percentage points lower than it was in November, a relatively rapid decline by historic standards. Private-sector job growth has been strong enough to more than offset government layoffs, particularly at the state and local level. A particularly encouraging sign is the rapid growth of manufacturing jobs over the past year and the recent broadening strength in services employment. While the exact pace of a jobs market recovery is always hard to predict, we were expecting the rate of job growth to pick up over the first half, and I am hopeful that job growth will continue to strengthen in the coming months. We would welcome this. Even if the economy added 300,000 jobs per month from now on, we would likely still have considerable labor market slack at the end of 2012.

Despite these clearly encouraging signs, there are still some downside risks to the growth outlook that bear watching. Let me list them for you:

- As I mentioned earlier, high oil and commodity prices have cut into household purchasing power, a difficult situation for many families that could constrain overall spending more than I anticipate.
- The renewed decline in home prices could dampen consumer spending and housing activity more than I expect.
- Finally, aggressive near-term government spending cuts or tax increases could slow economic growth at least in the short- to medium-term – although a credible plan for medium-term fiscal consolidation is sorely required and would have many economic benefits.

That said, I want to emphasize that these are risks rather than likely outcomes. In regard to inflation, on a year-over-year basis, the headline measures have increased to levels near those consistent with our objectives – which most members of the FOMC consider to be 2 percent or a bit less on the personal consumption expenditures measure. Moreover, the rise in commodity prices over the past year probably will push up headline inflation even further in coming months. It is noteworthy, however, that even with the sharp rise in oil and food prices, there has been little pass-through into broader measures of prices. In fact, most measures of underlying inflation trends – such as core inflation (which excludes volatile food and energy prices) – remain below levels consistent with our mandate.

Going forward, futures markets do not signal that investors expect rapid ongoing increases in commodity prices from current levels. Provided these prices stabilize (or indeed retreat), I would expect headline inflation to move back to a mandate-consistent rate. While this process plays out, however, it is critical that we ensure that inflation expectations do not become unmoored. It is much harder to keep inflation in check if people begin to raise their expectations of inflation. At this point, measures of inflation expectations overall remain stable. Economists at the New York Fed have examined inflation expectations using a unique survey that we sponsor. As reported in a recent post on our new Liberty Street Economics blog, they find no evidence to suggest that a wage-price inflation spiral is getting underway. However, we will continue to monitor expectations for medium-term inflation very closely.

To sum up, economic conditions have improved in the past year. Yet, the recovery remains moderate and we still have a considerable way to go to meet the Fed’s dual mandate of full employment and price stability.

Regional economic conditions

Now, how is our region doing? As attendees at previous press briefings may recall, the New York Fed produces Indexes of Coincident Economic Indicators to help monitor the performance of the region.

I am pleased to report that the latest months of data no longer suggest that the regional recovery has paused, as they indicated in February. Based on these measures:

- The recovery of activity in New York State and New York City continues at a steady and sustained pace.

- In New Jersey, activity also has begun to increase following a long period – roughly a year – where activity in the state was essentially flat.

We monitor Puerto Rico using an index produced by the Government Development Bank of Puerto Rico. The index shows that the decline in activity on the island began in 2005 and continued through late 2010. However, there are some signs that the economy has stabilized in recent months.

Regional employment trends

Now, let me turn specifically to employment trends in the region, the focus of our briefing today. In particular, we want to describe our region's experience during the recession and recovery.

Nationally, the Great Recession, which began in December 2007, has been the deepest economic downturn since World War II. At the jobs trough in February 2010 – about 7 months after the official end of the recession – the country had lost almost 6.5 percent of its jobs and the unemployment rate had more than doubled. Many people lost their jobs or saw their hours or income cut, and the duration of unemployment for jobless workers reached a historical high. For many families, this distress was compounded by losses of wealth from declining home prices and stock market losses. Since the jobs trough, unemployment has retreated by a percentage point and jobs growth has resumed, albeit at a slow pace. Today, we will review questions about jobs in our region such as: How severe was the downturn? Where are jobs returning? And, what factors affect the employment outlook?

As in other parts of the country, employment in our region declined substantially during the recession. But, New York and New Jersey and Puerto Rico had very different experiences.

Employment in much of New York State, including New York City, declined less severely than the nation. Both the state and city lost about 3.8 percent of their jobs. As we discussed at our briefing last October, part of reason for the more moderate decline in jobs in New York during the recession was a less pronounced boom-bust housing cycle. Indeed, as a percentage, the city and state lost fewer jobs during this recession than they did during either of the last two downturns.

By contrast, the downturn in employment in New Jersey in the current cycle was more severe. About 250,000 jobs were lost, or roughly 6.0 percent of total state employment – about the same as in the country as a whole. This decline is comparable to the job losses during the most severe recent recession in the state, that of 1989–1992.

Fairfield County in Connecticut, also part of our District, saw declines comparable to the nation, while Puerto Rico experienced much deeper and longer job declines than the nation. In fact, employment in Puerto Rico began declining nearly two years before the onset of the recession on the mainland.

Now, as in the nation, a labor market recovery has begun across much of the region. Over the past year, the tri-state region added roughly 100,000 private-sector jobs. Within the region, however, the recovery has been somewhat uneven. New York City, upstate New York and Fairfield County have been gaining jobs for more than a year now – at roughly the same pace as the nation.

However, employment in New Jersey has only begun to expand during the past few months. In Puerto Rico, job growth has yet to be firmly established. The recession, which began in 2005, has seen employment leveling off since last summer, but no clear reestablishment of growth.

Businesses in a variety of services sectors have contributed to the recovery of jobs in the region, including professional and business services, education and health, and leisure and hospitality, as well as finance. The overall expansion of our private sector is being partially offset by ongoing losses in manufacturing and construction, where firms in our region are not matching the modest growth seen in jobs at the national level. In addition, state and local government jobs in our district have declined sharply. After holding steady for much of the recession, state and local governments in New York and New Jersey have reduced job counts by more than 40,000. These losses effectively offset about half of the private-sector jobs created over the period. The government job declines were particularly severe in New Jersey and Puerto Rico, and considerably steeper than in the United States overall.

Looking ahead, the continued expansion of employment at the national level should have positive effects on many industries in our region. As elsewhere, state and local government will likely be a drag for some time. However, some new detailed job listing data point to an expansion of job openings in a number of key occupations in the region.

Finally, despite the overall recovery of employment across much of the region, unemployment rates remain very high. Although down from their year-ago levels, March's unemployment rate of 8.0 percent in New York State and 9.3 percent in New Jersey remain unacceptably high. And there is disappointingly little evidence of any sustained improvement in Puerto Rico's 16.1 percent unemployment rate.

Conclusion

To sum up, the national economy experienced a soft patch in activity during the first quarter of 2011, while the recovery in much of the region continued at a good pace. New York continued to expand and New Jersey has shown signs of turning the corner in the last two months. Puerto Rico may have bottomed out.

During the Great Recession, most of New York sustained less severe job losses than the nation as whole. By contrast, New Jersey's losses were comparable to the rest of the country and Puerto Rico's job losses have been more severe. As the recovery takes shape, private services are the most likely source of job growth throughout the region.

There are many reasons to believe conditions are in place for stronger growth in the coming months in the nation and the region. Nevertheless, both nationally and regionally, unemployment remains stubbornly high and is likely to remain so for many months to come.

Thank you for your kind attention. I will now ask James Orr to provide more details on regional economic conditions.