William C Dudley: The national and regional economic outlook

Remarks by Mr William C Dudley, President and Chief Executive Officer of the Federal Reserve Bank of New York, at the New Jersey Performing Arts Center, Newark, New Jersey, 18 August 2011.

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Good morning. I am pleased to be in Newark this morning and to speak to the members of the Newark Regional Business Partnership.

In the aftermath of the financial crisis, as we wound down our emergency meetings, I asked my staff to develop an ambitious outreach program so I could visit the different parts of my District. Over time, I plan to visit all parts of the region.

Each trip gives me a chance to deepen relationships with the people I represent. As you may know, the New York Fed's District includes 12 counties here in northern New Jersey; all of New York State; Fairfield County, Connecticut; Puerto Rico; and the U.S. Virgin Islands. In June, I met with community leaders, businesses and elected officials in Brooklyn, and in May I travelled to several cities in the mid-Hudson Valley north of New York City to meet with the leadership of those communities. Today and tomorrow I will meet with a wide range of people and organizations here in northern New Jersey to talk about what I do and to learn firsthand about the economic and financial issues important to you. These conversations will help me to represent all of my constituents in my work at the Fed as I consider how best to manage interest rates and make other monetary policy decisions.

Northern New Jersey is important to me not just because it is a large and important part of the New York Fed's District but also because it is my home. My wife and I have made our home in Cranford – her home town where she can be near her mother.

While my colleagues and I are pleased to work with the business community – and I know that Jason Bram and Rae Rosen of the Fed have addressed this group in the past – we also have a number of initiatives specifically targeted to help low- and moderate-income groups, particularly here in Newark.

For the past three years we have provided the Newark/Essex County Foreclosure Taskforce with data and analyses on the latest mortgage conditions and trends through a range of outlets including round tables, presentations and newsletters. This Taskforce was formed in response to the rise in foreclosures in Newark and surrounding towns in late 2007. The Taskforce is comprised of representatives of over 40 community development corporations, nonprofit housing counseling and legal service providers, government and community development officials and advocacy organizations working to address this serious issue.

Over the past two years we have partnered with Bank on Newark. Bank on Newark is a private/public partnership developed to bring unbanked populations into the financial mainstream by providing assistance in establishing bank accounts and receiving financial education. The New York Fed serves as an advisor and data monitor for Bank on Newark and its sister program, Bank on Manhattan, as well.

This fall, we will launch our Financial Awareness Video Competition in Newark and Essex County in partnership with the City of Newark. The goal of this video competition is to promote financial awareness in the Greater Newark community. The video competition invites university- and college-level students to produce original videos that encourage young adults to practice sound personal financial decisionmaking. We have successfully launched similar video competitions in Puerto Rico and New York City. Last year's videos were judged by a panel of professional film makers and leading advertising agencies. The winning videos ran for two weeks as "shorts" in major movie theaters in Manhattan and Queens.

I thank the Newark Regional Business Partnership, PNC Bank and NJ PAC for inviting me here to speak to you today. I would also like to thank the SGA Group PC for sponsoring this breakfast. Over the next two days I look forward to meeting with your elected officials in Newark, visiting Newark Now, sitting down with the Episcopal Community Development Housing Counselors, as well as meeting with New Jersey community bankers and credit union officials, visiting the manufacturer Accurate Box, touring Jersey City and learning more about the pharmaceutical industry – my staff has booked a packed schedule.

The role of the New York fed

By way of introduction, let me briefly review what the New York Fed does and what makes my job so interesting. As always, what I have to say reflects my own views and not necessarily those of the Federal Reserve System or the Federal Open Market Committee, also known as the FOMC. I am vice chair of the committee and we meet eight times a year in Washington, D.C., to set interest rates and make other decisions about monetary policy.

At every meeting of the FOMC, each committee member presents his or her current outlook for their region and for the overall economy. For these assessments, we augment input from our research departments with critical information about local economic conditions supplied by our board of directors, regional advisory councils and conversations with local stakeholders, such as the feedback I will get from you today.

At the regional level, we continually track economic conditions in our District, and we have created a number of tools for this purpose. For example, to fill a void in timely measures of regional economic output my staff produces monthly indexes of economic activity for New Jersey, as well as for New York State and New York City. These measures are similar in concept to measures of gross domestic product (GDP). We have also initiated a consumer credit panel so we can monitor local household credit conditions, including the amount of debt being carried per person and the composition and payment status of that debt.

Furthermore, we have a new survey to track credit and financing issues for small businesses, which create a lot of jobs. The poll takes a fresh look at borrower demand by asking firms not only about credit applications but also about reasons for not seeking credit. In all, 876 small businesses from the tri-state area responded to our May 2011 poll, and 14 percent of these were from New Jersey.

To share the information that we gather and produce about our diverse District, we have created a rich website with localized current data and maps on conditions in the region. I invite you to visit us at newyorkfed.org to explore the highly detailed information on small business, credit and housing conditions that we provide.

Finally, and crucially, in the aftermath of the financial crisis, we are working with our colleagues in Washington and at other agencies in the United States and abroad to help put the nation's financial system on a firmer footing. Yet, much remains to be done and we are determined to keep at it. I recognize fully that there can be no return to pre-crisis business as usual – whether on the part of the financial sector or on the part of regulators like ourselves.

All in all, there is a lot to keep my colleagues busy even in normal times.

Macro conditions

The statement issued by the Federal Open Market Committee earlier last week presents a sober assessment of the state of the U.S. economy. Economic growth so far in 2011 has been quite a bit slower than we expected earlier in the year. While jobs growth picked up early in the year, in the last few months conditions in the labor market have deteriorated again and the unemployment rate has edged up. Household spending has flattened out, and the housing sector is depressed. Business investment in equipment and software is expanding, but investment in corporate offices and other commercial buildings is weak.

Some of the weakness in economic activity in the first half of the year was due to temporary factors such as the hit to household income from higher food and energy prices, and supply chain disruptions following the tragic earthquake in Japan. These restraining forces have abated and thus, we should see stronger growth in the second half. But it is clear that not all of the weakness was due to these one-time factors – and in light of this, I have revised down my expectations for the pace of recovery going forward.

On the inflation front, the committee noted that inflation has moderated recently as energy and commodity prices have declined from their peaks – having picked up earlier in the year, mainly reflecting higher prices for commodities and imported goods, as well as the supply disruptions from Japan. Longer term inflation expectations remain stable, and the committee now expects inflation to settle over the coming quarters at levels at or below those consistent with our mandate to promote full employment and price stability.

In light of the current outlook, the FOMC in its statement noted that we now anticipate that we are likely to keep short-term interest rates exceptionally low at least through mid-2013. We also discussed the range of policy tools available to promote a stronger economic recovery in a context of price stability. Further details on the discussion at the meeting will be available when the minutes are published later this month. I will not comment on monetary policy any further today.

Following the release of the FOMC's statement, market interest rates generally moved lower, which should help provide some additional support for economic activity and jobs. I would note, however, that conditions remain unsettled and the equity market in particular has been quite volatile recently.

Regional economic conditions

So how is our region doing? Let me start by saying that New Jersey is well-positioned for growth. The state has a population of 8.8 million, the 11th largest state, and despite the fact that this is a fairly mature region, the state's population expanded by 4.5 percent over the past decade. More than 40 percent of the population 25 years of age and older in the state have a college degree, a full 5 percentage points higher than the national average. Our population is quite ethnically diverse: roughly 20 percent of the state's residents were born abroad, and that share is even higher in Essex and Bergen counties. Significant numbers of the foreign born residents in the state come from India, Mexico, the Philippines, the Dominican Republic and Korea.

The state's economy is also quite diverse, and its industry mix mirrors that of the national economy. A sizeable number of jobs in the state are in the healthcare, professional and business service, wholesale and retail trade, and leisure and hospitality categories. When we look at the northern part of the state, we see a somewhat greater concentration of jobs in finance, particularly in Hudson County, in goods distribution, related to the ports, rail lines and trucking and warehousing activities that are prominent here, in pharmaceuticals manufacturing and research and development, and in the private education sector.

The area also has important links to New York City. For example, the data centers here in the state serve many of the city's financial firms. In addition, a large number of residents, including myself, commute each day into the city. A smaller but still sizeable number of New Yorkers commute into this state.

Now, how did the state fare during the downturn and how is the recovery proceeding? As I mentioned, the New York Fed produces indexes of economic activity to help monitor the performance of the region.[1] Based on our index, the downturn in activity in New Jersey began about the same time as the Great Recession was beginning nationwide – that is, around December 2007. While activity in the state is no longer declining, and there has been a slight pickup this year in the level of activity, to date there is still no sign that a strong recovery has taken hold. Quite frankly, this modest recovery in New Jersey contrasts with the relatively sturdy recovery in activity in New York City over the past 18 months.

Employment in our region also declined substantially during the Great Recession. Job losses in New Jersey totaled about 250,000 – on par with the roughly 6 percent loss nationwide. The pattern of job losses here in northern New Jersey was very similar. In New York City, job losses were also large but somewhat less severe, with employment in the city down a little over 4 percent.

The jobs recovery in New Jersey to date has been sluggish. The private sector has seen moderate gains, with growth in some of the key sectors I mentioned earlier, particularly professional and business services, education and health, and leisure and hospitality. Businesses in these sectors, on balance, expanded jobs at a faster rate than in the nation. But the state continues to shed jobs in manufacturing and residential construction. Notably, overall employment in the state has been weighed down by declines in public sector employment. Like many states, New Jersey faced large projected state budget deficits during the downturn, and, as in many states, the adjustment to those gaps included job cuts through a reduction in state government jobs and cuts in state funding for local government programs.

Because the jobs recovery has been weak, there has been little progress in reducing unemployment. The unemployment rate among New Jersey residents currently stands at 9.5 percent, the same rate as a year ago, and slightly above the national rate.

Underneath the slow overall job growth, however, there is a considerable amount of churning in the labor market. Taking a closer look at the patterns of job gains and losses during the recession and recovery reveals some interesting facts about the labor market in New Jersey. Of particular interest is that job creation in the state and the nation since the recession ended has been closely balanced between hiring into industries that lost jobs lost during the recession and jobs in expanding industries. Thus, many unemployed workers may be returning to work without needing to retrain or look far afield from the job they lost. However, an equal number may need to search outside the industry they know best and this may require retraining in some cases. Thus, the need for job search assistance and training opportunities is likely to be high in New Jersey and the nation in the near term.[2]

Now let's look at the situation of New Jersey households. Here, too, there is room for improvement. While the median household income among New Jersey families is the second highest in the nation – at about $68,000 in 2009 – about 9 percent of residents are in families with incomes below the poverty line. This rate compares favorably with the national rate of 13.6 percent, but varies by city across the state: here in Newark that share is 24 percent. Reducing poverty is a major challenge for policymakers. Local organizations like Newark Now are working hard to create greater economic independence for low- to moderate-income residents.

More broadly, how are the state's families doing in restoring their finances? During the recession, all across the nation, the number of debt delinquencies soared and many families had to reduce their debt to more sustainable levels. The New York Fed keeps track of credit conditions in the region – including the average debt carried per person and whether they are

[1] Regional Indexes of Coincident Economic Indicators

[2] See, for additional discussion of this topic, William Dudley. 2011. "Job Creation in the Region." Remarks at the Quarterly Regional Economic Press Briefing, New York City. August 12.

current with their payments – using the special consumer credit panel we developed. The report for the second quarter of this year was just released on Monday.[3]

Families in New Jersey are reducing their debt levels. As of the second quarter of this year, for those people with a credit report, average debt per person was about $60,400 down from $63,000 three years ago. But the crisis has taken its toll. Delinquency rates on the debt are high: 7.4 percent of all debt in the state is seriously delinquent, roughly the same rate as the nation. The comparable figure for the state just three years ago was 4.1 percent, so, like the nation, households in the state still appear to have a considerable way to go before they reach more comfortable debt levels.

While there have been indications that home prices in the area have been firming in the past few months, the mortgage crisis continues to take a toll on New Jersey homeowners. As of March of this year, 10 percent of all borrowers in the state were either 90-plus days delinquent on their mortgages or their homes were in foreclosure – above the national rate of 7.7 percent. In Essex County, that rate had reached 16 percent, and in Newark it was 30 percent.

In our recent small business survey, which we conducted in May, we asked firms to report on their first quarter sales and their future outlook. The results were encouraging. Over two-thirds of firms told us they had stable or increased sales in Q1, up from 50 percent last year. When asked about their future outlook, while the majority of business owners, 56 percent, were neutral – many more said they were optimistic than pessimistic – 37 percent compared with only 7 percent.

Conclusion

These debt and delinquency figures, together with the weak jobs picture, suggest that New Jersey faces a number of challenges. In the near term, the key issue will be to expand jobs and reduce unemployment. At this point it is difficult to say when the pace of recovery in the state will pick up, but several factors appear encouraging.

A continued expansion of output and employment nationally would clearly help to expand activity and employment in a number of industries in the state, including professional and business services and the goods distribution industries. Also, the pace of contraction in public sector jobs in the state has slowed from the sharp declines that occurred last year, and has thus become less of a drag on job growth. Further, continued job growth in New York City should create opportunities for New Jersey residents, particularly in this part of the state.

Longer term, one of the key challenges will be for the state to build upon and expand the human capital – by which I mean the education and skills – of its workforce. A region’s human capital determines a large part of its economic success. Even though it already has one of the most educated workforces in the country, New Jersey needs to continue to attract and train workers who can do a range of tasks that an advanced economy demands, such as start innovative firms, operate sophisticated capital equipment and design websites. In addition, a broad expansion of education and skills goes a long way to broaden participation in the economy to all residents of the state.

Thank you for your kind attention.

[3] Quarterly Report on Household Debt and Credit, August 2011.