

New Jersey Economic Insights



Dr. Charles Steindel,
Chief Economist
March 2013



Outlook New Jersey 2012 Turned Out to Be a Very Good Year for New Jersey Job Growth

New Jersey

New Jersey's labor market was even better in 2012 than we had thought. New information shows that the state added 66,400 jobs from December 2011 to December 2012, a notable upward revision from the previous figure of 48,000. The result is that 2012 was far and away the best year for job growth in New Jersey since 2000.

The unemployment rate for 2012 as a whole was unrevised at 9.5 percent, but very important details relating to unemployment were revised in a positive direction. First, the new numbers show less monthly variation in unemployment than was reported during the year. We had seen a 0.9 percentage point increase in the unemployment rate in the first half of the year, to a peak of 9.9 percent. The new figures show a less steep rise of 0.5 percentage point to a peak of 9.7 percent. More importantly, the new numbers now show that resident employment was growing steadily throughout the year. The initial figures had shown something very odd — a sharp drop in the middle of 2012 that was completely at odds with the job numbers. With the revisions, it's clear that New Jersey's higher than national average unemployment rate is directly related to the increase in our labor force participation rate. New Jersey's participation rate — the part of the population that is working or actively looking for work — has been

rising while the nation's has been falling. This discrepancy has resulted in our labor force growing much more rapidly than the nation's, which has kept our unemployment rate elevated compared to the nation. Job and employment growth in New Jersey has been comparable to the nation, which means our relatively high unemployment rate is not due to any particular problem in job formation.

- *New Jersey's economy continues to move forward, while revisions show 2012 was better than initially thought.*
- *National economy is demonstrating some surprising strength in the face of higher taxes and spending cuts.*

In early 2013 a fairly large increase in New Jersey jobs in February — they were up by 12,900 total and 7,100 private sector jobs — more than reversed a small decline in January. February also saw a drop in the unemployment rate to 9.3 percent from January's 9.5 percent. That mainly reflected a retreat in the state's labor force participation rate from its recent unusually elevated levels — resident employment growth in February was less than growth in the

number of jobs — but it's still the case that over the last year employment and jobs have been moving forward at a well-sustained pace.

Other state indicators have also firmed. The coincident economic indicators compiled by the Philadelphia and New York Federal Reserve Banks, which rely heavily on the job numbers, show that activity in the state was accelerating through January. The Philadelphia Federal

(Continued on page 2)

Reserve's manufacturing survey, which includes South Jersey firms, turned positive in March and New Jersey's personal income rose a sharp 1.9 percent, to another new record high, in the fourth quarter of last year. This was due in part to early payments of financial industry bonuses and stepped-up distributions of dividends. New housing permits in the first two months of 2013 were more than 25 percent higher than in the same months of 2012.

As winter ends the state's economy seems to be in a fairly favorable position. The recent positive developments as yet appear to owe little to rebuilding from Sandy; that factor should become more evident as the year goes on. There are still questions about the strength of the summer vacation season on the shore, but, currently, given the national outlook, the overall outlook for the state is good.

U.S. Economic Outlook

National economic growth appears to have picked up in early 2013 after some lackluster numbers in the fourth quarter. Retail sales continue to grow at a healthy pace, home building and sales are expanding, capital goods orders are up and manufacturing production is on the rise again after a flat period in mid-2012. More than 200,000 jobs were added in three of the last four months, with February seeing a gain of 236,000. The national unemployment rate fell to 7.7 percent in February, partly due to weakness in the labor force, but also reflecting growth in household employment.

The magnitude of the recent uptick in the national economy has been a bit unexpected. Analysts had felt that the January 1 Federal tax increases, especially the rise in the payroll tax, would bite into consumer spending. Furthermore, continuing policy stalemates in Washington were supposed to erode household and business confidence and hold back demand. On top of all that, the looming "sequester" of a substantial amount of federal spending

for the balance of the fiscal year, which ends on Sept. 30, was also reckoned to cast its shadow on the economy. The resiliency of the monthly indicators at the start of the year suggests that underlying strength may be more robust than was previously thought.

That said, the "sequester," unless modified, will result in substantial cuts in federal spending during the second and third quarters of 2013, so it's possible growth will ease off a bit in this period. New Jersey, however, should see only a very small portion of the direct cuts in spending due to the sequester. As is well known, there is little federal spending in New Jersey, especially compared to the federal taxes paid by our residents and businesses, so there's not much to cut! Still, the underlying trend in the economy looks somewhat improved.

Financial commentators have been busy speculating about the future path of Federal Reserve policy. Realistically, this is idle Wall Street chatter. Institutionally, the Fed is committed to keeping short-term interest rates near zero until the economy is in a *dramatically* better condition than is currently the case, or inflation shows it is moving higher. The Fed has indicated it is likely to slow down its massive purchases of government and agency securities, prior to boosting rates, at a time when the economy is showing solid improvement. But it has also emphatically said "not now." From the Fed's vantage point, the economy is convalescent, but not cured, and inflation — except for month-to-month noise resulting from moves in gasoline prices — is quite low. Some Fed officials have, indeed, aired their belief that current policy is too easy, but they are in a small minority.

“Currently...the overall outlook for the state is good.”

Economic Analysis

New Jersey Housing: Finally Turning the Corner?

The last recession began as a major collapse in home sales and construction, both in the nation as a whole and in New Jersey. Measures of housing activity were mired at extremely low levels year after year, posing a formidable barrier to more rapid growth. Typically, housing leads the economy out of recession, but it just did not happen in the early years of this recovery.

Nationwide, housing starts dropped from 1.8 million in 2006 to 1.3 million in 2007 to 900,000 in 2008 to a truly dreadful 554,000 in 2009. In the first half of 2011, starts were still very near their low. Similarly, sales of existing homes skidded from more than 7 million in 2005 to barely over 4 million in 2008-2010. The housing collapse led to massive job losses in industries such as construction and real estate brokerage. The associated slump in home prices contributed to massive losses in household wealth, working to depress consumer spending. Furthermore, the decline in home prices fueled the massive wave of foreclosures.

New Jersey's trends mirrored those of the nation. Housing

“New Jersey’s housing sector has also seen pronounced gains from very low levels.”

permits in the state sank from 38,481 in 2005 to a mere 12,235 in 2009. In the thirty-plus year history of the permits series, 2009 was the worst year on record. There was little improvement in 2010 and 2011. Additionally, the New Jersey Association of Realtors reported that sales of existing homes in the state fell by nearly half from 2004-2005 to 2011, with prices also tumbling. And, as in the nation at large, foreclosures moved up in New Jersey.

Housing statistics have been turning around since the middle of 2011. Nationwide, 2012 as a whole saw some solid gains, with starts up 27.6 percent from 2011 and existing home sales up almost 9 percent. Nearly all the

many measures of home prices showed gains in 2012. The forward momentum continued into the first months of 2013. The annual rate of housing starts in each month from December 2012 to February 2013 was over 900,000, a far cry from the 2009 low. Sales of new and existing homes have also continued to advance, though month-to-month moves in these series are quite erratic.

New Jersey's housing sector has also seen pronounced gains from very low levels. There were nearly 18,000 housing permits granted in the state in 2012, and January and February figures show continued advances with total permits more than 25 percent higher than in January and February 2012. According to The Realtors Association, existing home sales increased 11.7 percent in 2012.

Housing prices are one area where the turnaround in New Jersey has seemed to lag the national recovery a bit. Still, even here the Realtors report that transaction prices in the fourth quarter of 2012 were 3 percent higher than those in the fourth quarter of 2011. This was one of the few times in recent years that home sales prices have increased in New Jersey and it was the largest gain in at least six years — a very encouraging signal.

It's also encouraging that recent increases in permits are not merely the result of Sandy rebuilding. In fact, growth in permitting has been centered in the northern part of the state, not the Shore. To put it another way, recent gains are not the result of a post-Sandy rebound, but probably reflect more enduring forces. The inevitable pickup in activity at the Shore as rebuilding takes hold will be an addition to the favorable trend.

Why is it that we see the housing recovery continuing and gaining strength, both in the nation at large, as well as in New Jersey? The answer is simple. The fundamentals behind housing demand have turned decisively favorable. Household income is recovering, mortgage rates

(Continued on page 4)

remain extremely low, and home prices — while off the floor — remain well below pre-recession peaks. Furthermore, the lack of construction in recent years has undoubtedly created some shortages of housing, as the population has continued to grow. Finally, increases in rents have spurred both apartment building and increased demand for owner-occupied housing.

These favorable developments have been at work for some time, and it's simply been a matter of waiting until they have spilled over into improvements in housing indicators. Some continuing reluctance of banks to offer mortgages on favorable terms had hampered the recovery in housing, but that situation appears to have eased, and the housing turnaround looks now to be well underway.

To give an idea of how favorable the market remains for home buyers — which means it will also be favorable for builders — the New Jersey Association of Realtors reports that the state's "affordability index" in the fourth quarter of 2012 stood at 174.4. That means families earning the median household income in New Jersey can

afford the principal and interest payments on a standard mortgage nearly 75 percent higher than the payments needed to service a mortgage on the median-priced house in the state. Another way of looking at this is a household earning the median income can afford to service a mortgage on a house costing about 75 percent more than the median price. Half the households in the state earn at least the median income; half the houses in the state cost less than the median. In other words, half the households in the state can service a mortgage on more than half the houses in the state. This is a remarkably favorable situation for potential homebuyers who have the resources to afford a down payment.

Given the recent positive news, and the continuing favorable fundamentals, it looks like 2013 is shaping up to be another year of solid gains in New Jersey's housing markets. We are not likely to get back to pre-recession levels of activity this year, or maybe even next year, but we are going in the right direction.

—*Charles Steindel*



New Jersey Business Pulse Survey

Optimism Returns for New Jersey's Business Owners

Fifty-six firms responded to the January survey and forty-nine responded to the February survey. The survey includes 14 questions about current and perspective conditions in New Jersey and the nation and allows respondents to give their views on other topics of their choice. Detailed results may be found at <http://www.state.nj.us/treasury/economics/> This page also contains charts and tables summarizing the results, as well as an explanation on how indexes were constructed from the answers to the questions.

General Conditions: The Economy is Improving

In both January and February, New Jersey business owners characterized the general economic conditions in the U.S. as improving slightly while the state's business climate remained unchanged; however, expected near future conditions in New Jersey became even more optimistic than reported in recent months with 43 percent believing conditions will improve — the highest percentage since August 2012. Returning to an optimistic view, survey respondents also predict growth in revenue generated from business within the state as well as from outside the state.

Growth in Employment and Investments Signaled

More good news for New Jersey as businesses reported plans to expand employment in the near term. The state has been reporting one of the highest unemployment rates in the country despite seven months of continuous job growth, indicating that growth in the labor pool is chiefly driving the rate — a likely sign that New Jerseyans are becoming more optimistic about finding a job. Further supporting that claim is the fact that two thirds of business owners who expressed plans to hire in the

near future did not report having difficulty finding qualified candidates for open positions, suggesting that the pool of applicants is improving.

Plans to increase capital spending in New Jersey also turned positive in January — a change of attitude after surveys in November and December suggested plans to cut spending. In February, capital spending plans in the state remained slightly positive while plans to invest outside of New Jersey turned negative. This may indicate that New Jersey is seen as having greater investment potential than outside of the state, but since not all respondents have out of state operations this is not completely certain.

Input and Selling Prices

Breaking the long held trend, respondents in January reported recently increasing the price they charged for products/services as well as paying more for input costs themselves. February's survey returned to the pattern of firms claiming to pay more for input costs while not raising their own prices.

Conclusion

The general sentiment in the first two months of the year is a positive one where firms showed their optimism about the economy with expectations for growth in the near future in revenue and hiring, and an opinion that New Jersey is a good place to invest in business expansion through capital spending.—*Joseph Mengedoth*

The New Jersey Business Pulse Survey has been created to look beyond conventional economic data and gather views in real time directly from a diverse group of businesses in the state. If your New Jersey firm is interested in participating in this monthly survey, please contact Mary Filipowicz at 609-633-6781.

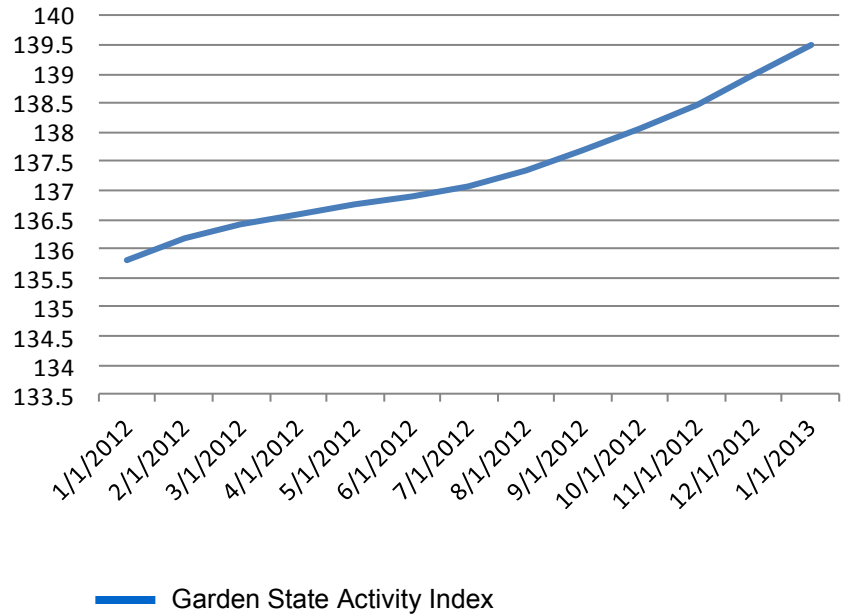
Garden State Activity Index

The *Garden State Activity Index* is our broad measure of monthly economic activity in the state of New Jersey. The index incorporates information from three sources: the Federal Reserve Bank of New York's coincident index, the Federal Reserve Bank of Philadelphia's coincident index, and the Philadelphia Fed's South Jersey Business Survey.

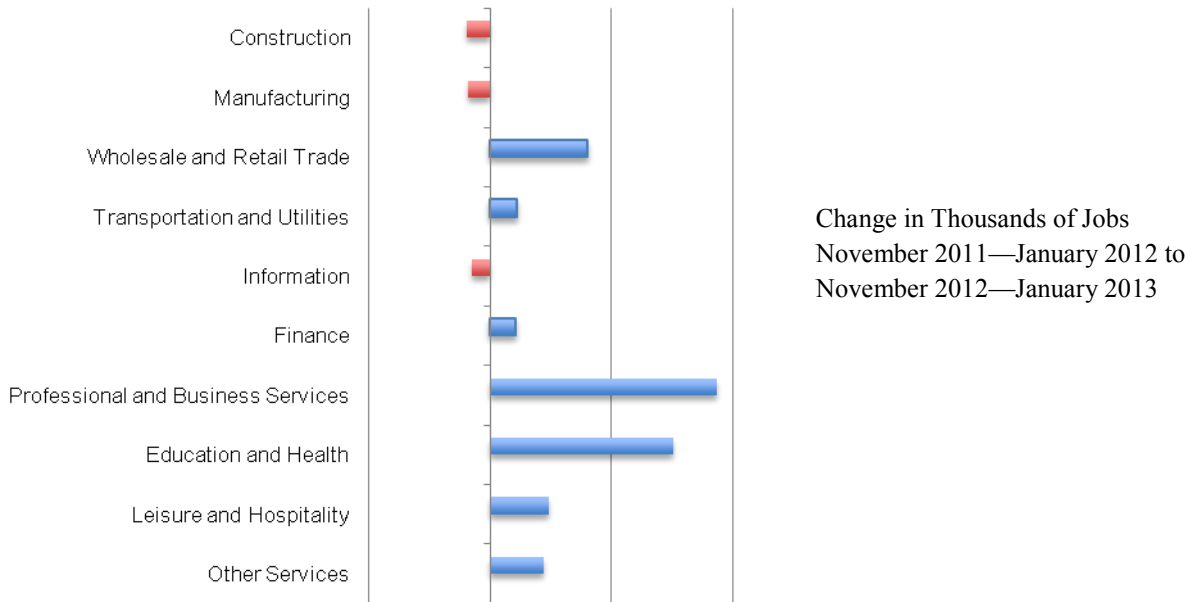
To construct the *Activity Index* we use principal components analysis, which takes a weighted average of the three Fed indicators. The composite index reflects the current state of the New Jersey economy.

Based on the most current monthly data, New Jersey's economic growth has noticeably picked up over the last 12 months. This past January, the state's economy reached an index level 2.7 percent higher than the level in January 2012.

—Andrew Lai

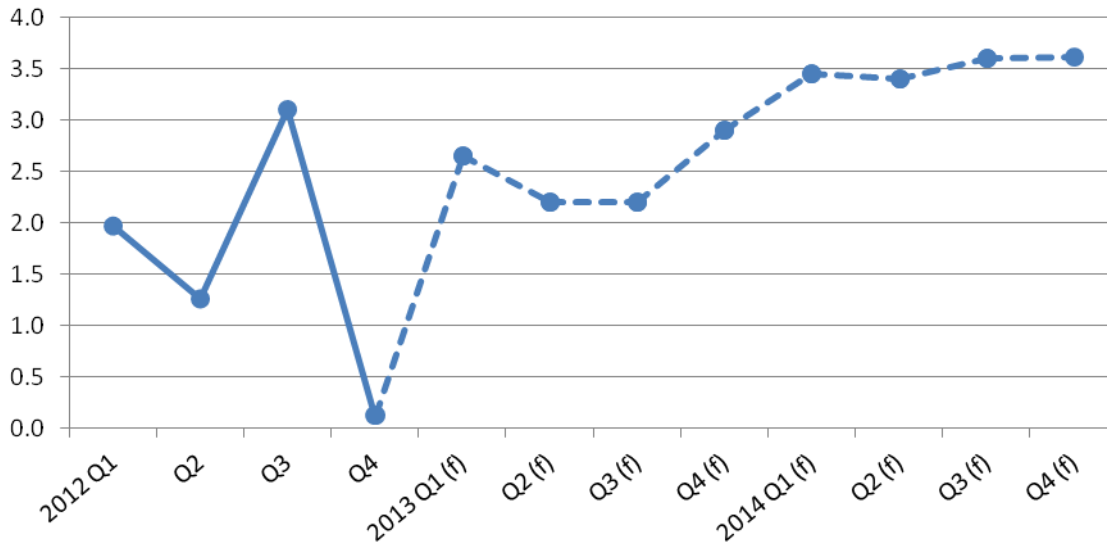


Private Industry Employment Trends



Data source: New Jersey Department of Labor

Real U.S. GDP Growth



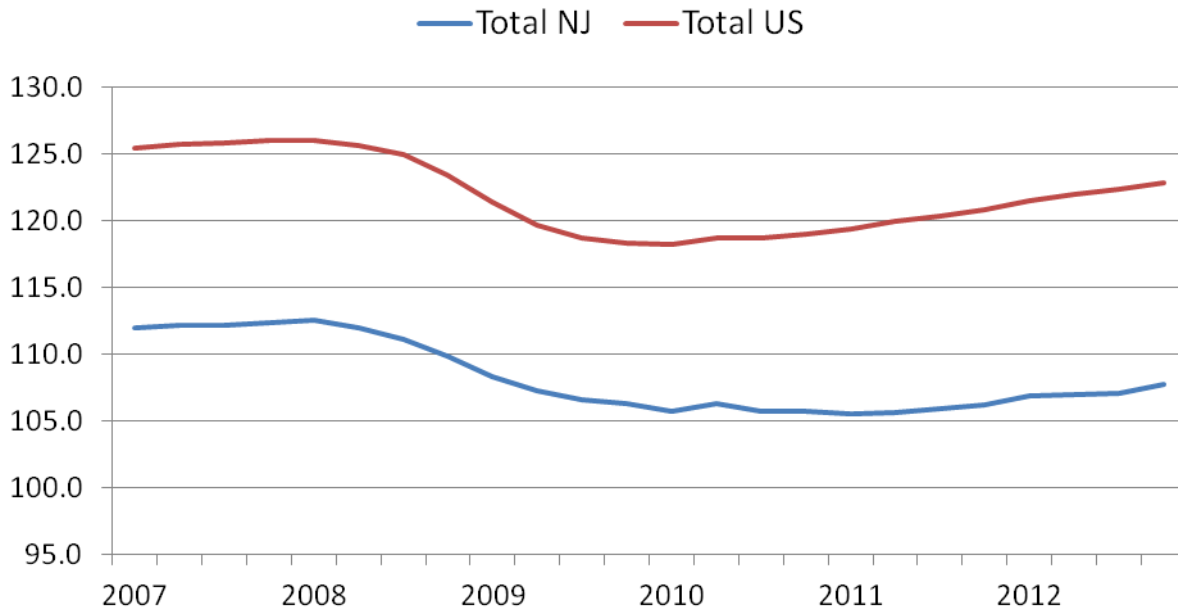
(f) - forecast

Data source: U.S. Bureau of Economic Analysis

State & National Job Trends

Total Employment (Relative Employment 1990=100)

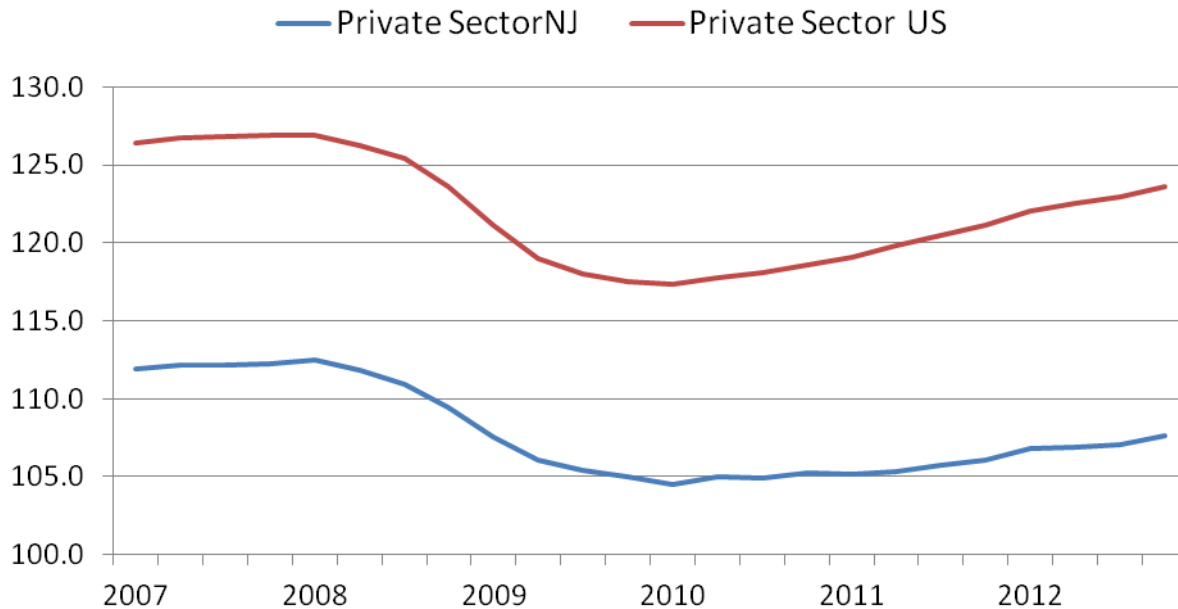
This chart compares the number of employed workers to the base year of 1990. The number 100 represents employment in 1990.



State & National Job Trends

Private Sector Jobs (Relative Employment 1990=100)

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



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

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

Disclaimer

This communication is for informational purposes only and is not an offer, solicitation or recommendation regarding the purchase of any security of the State of New Jersey or any governmental authority of the State of New Jersey. The views expressed herein are solely those of Dr. Steindel and do not necessarily represent the views of the State Treasurer or any other official of the State of New Jersey.