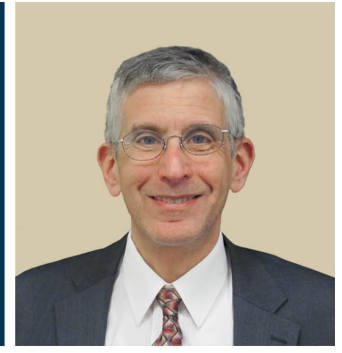


New Jersey Economic Insights



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Outlook New Jersey Scattered Signs of Strength in the National and New Jersey Economies Give Reason for Optimism

New Jersey

Despite a dearth of fresh data on the state’s economy in recent weeks, two regional surveys suggest that economic activity in the area is growing.

The Federal Reserve Bank of New York’s monthly survey of New York State manufacturers was quite positive in February. Respondents’ assessment of general business conditions was at its highest level since June 2010. The reading on conditions expected in six months slipped a bit from January’s extraordinarily high level, but in both January and February it was at higher levels than the average reading for any year since 2004.

Closer to home, the comparable survey by the Federal Reserve Bank of Philadelphia also shows that local manufacturers have very positive perceptions. Its index of general business conditions moved to a four month high in February. The Philadelphia survey includes firms located in South Jersey, so it is likely somewhat more indicative of New Jersey developments than the New York poll.

There has also been a marked pickup in the life science business cluster in the central part of the state that has recently received national media attention (http://www.nytimes.com/2012/02/01/realestate/commercial/life-sciences-development-rebounds-in-central-new-jersey.html?_r=1&ref=business). We described the state’s Pharma/Biotech sector in NJ Economic Insights

last March: http://www.state.nj.us/treasury/pdf/Economics-Newsletter_mar11.pdf, where we noted that “the traditional view that pharma/biotech is and will remain a major driver of the state’s economy, remains not just defensible, but clearly the view most supported by the available facts.”

There is a shortage of fresh statistical data on the New Jersey economy at the moment because the U.S. Bureau

of Labor Statistics and our Department of Labor won’t be releasing January job numbers until early March, several weeks later than normal. This delay, which happens every year, allows the agencies to incorporate routine annual revisions in the job count. *Due to the lack of updated New Jersey employment data, we are not including updates to the Garden State Activity Index — which depends heavily on the job information — or the usual charts on employment trends and the table on changes in employment by major industries in this issue.*

• *There are scattered indications that the state’s economy continues to improve.*

• *The national signs are highly encouraging*

U.S. Economic Outlook

The national economy continues to show somewhat surprising strength. The unemployment rate has continued to decline and stood at 8.3% in January. That compares with a rate as high as 9.1% last August. The last five months have seen the largest drop in unemployment over such a time span since 1984. Hiring

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has picked up along with the drop in unemployment. January saw net job creation of 253,000, which was the highest increase since last May. The annual revisions for national data — although as noted above New Jersey data are not yet available — showed that job growth over the last two years was somewhat higher than earlier reported. The figures now show that about 2 million jobs were created over the last 12 months — including well over 2 million in the private sector alone — which is more than enough to put some downward pressure on unemployment, although not rapid enough to bring the nation back to full employment anytime soon.

There appears to be some continuing forward momentum in the labor market. New claims for unemployment insurance have dropped from an average of around 425,000 a week in the middle of last year to less than 375,000 more recently. New claims at this lower level have traditionally been associated with fairly strong job growth. Also, there were more than 3 million private sector job openings at the end of December, the highest number since the summer of 2008 just before the economic collapse hit.

Spending and production measures continue to advance. Retail sales figures for January suggest the upswing is

continuing, following some softer numbers in December. Auto sales were quite strong last month. Housing starts appear to be moving up from rock bottom levels, and manufacturing output growth is ongoing. Inflation remains well-contained.

Despite the improvements in the national economy and upbeat sentiments in a consumer and business polls, a full economic recovery is not yet baked into the cake.

The European crisis continues to loom over the world economy. In

this election year, only limited moves are likely from Capitol Hill and the White House. However the recent agreement on the payroll tax cut and extended unemployment insurance benefits suggests that the paralysis is not complete. The Federal Reserve continues to express its concern about the underlying strength of the economy. Finally, some recent gains could merely reflect the exceptionally mild winter's bringing forward some activity, especially in construction, from the spring. Still and all, the recent information has been upbeat.

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New Jersey Housing: Will the Corner be Turned in 2012?

New Jersey, like the nation at large, has seen seismic movements in the key indicators of the housing market over the last few years. These include the number of units being built, total sales and median prices. Last year, these measures stayed at essentially rock-bottom levels. Employment levels and income for businesses in this sector remain quite depressed, and foreclosure rates are high. Nonetheless, the economic fundamentals appear to be turning in a direction favorable for housing, and there is a reasonable chance that recovery, at least in some parts of the market, could begin this year.

Although New Jersey was spared some of the worst excesses of the subprime lending bubble, our housing crash was dramatic. Permits granted for the construction of new single-family homes in the state declined from over 20,000 a year in the middle of the last decade to less than 6,300 in 2011. The Federal Housing Finance Agency reports that the median home sales price in New Jersey, taken from properties with repeat sales, dropped from just over \$350,000 in the middle of 2006 to less than \$270,000 five years later.

The New Jersey data from the National Association of Realtors shows a drop from around \$360,000 to about \$305,000 in their figure for median sales prices over the same period. The Association also reports the number of home resales fell from over 180,000 in 2004-2005 to about 110,000 in 2010 and remained at roughly that same low pace over the first three quarters of 2011. Employment at homebuilders dropped from almost 30,000 in 2006 to 17,000 in 2011. Employment at “specialty trade contractors”—plumbers, electricians, and the like, many of whom work on nonresidential projects—has fallen from 114,000 in 2006 to 83,000 in 2011.

New Jersey members in the Realtors’ Association fell from over 58,000 in December 2006 to fewer than 48,000 in December 2011. A bit more than 8 percent of all home mortgages in New Jersey were in foreclosure at the end of 2011. That number may overstate the

prevalence of foreclosure, since fewer than half of all New Jersey families own a home with a mortgage. Still, the number of foreclosures in the state exceeded 100,000, and was more than ten times higher than the 2005 figure.

Given the current bleak situation, why would there be any reason for optimism

about housing? The simple answer is that houses now appear to be highly affordable — home prices have fallen much more than incomes, and mortgage rates are at record lows. Nationwide, the Realtors’ Association

reports that a household earning the median income makes about twice as much as the amount needed to service a mortgage on a median-priced house. The corresponding calculation for New Jersey isn’t quite as favorable, but even so, the New Jersey median household income is about 50 percent higher than the amount that can qualify for a mortgage on our median-priced home.

The alternative to buying a home is renting. The nation has produced few new rental properties in recent years, and with many households choosing to stay in the rental market rather than buy, rents have been rising fairly strongly. In January, rents nationwide were about 2½ percent higher than a year earlier and it is likely that such growth will continue. The combination of affordable housing and rising rents seems likely to spur growth in home purchases and eventually encourage new construction.

Of course, many of the fundamentals favoring housing have been falling into place over the last few years. Households have been reluctant to take the plunge and

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buy because the weak economy has fueled uncertainty and has made it more difficult to save a down payment for a purchase. The large number of foreclosed properties also creates a risk of more downward pressure on home prices as these are sold at fire-sale prices, and since the 2008-09 financial crisis banks have tightened their lending rules and down payment requirements while ramping up paperwork.

Nonetheless, it seems certain that at some point the dam will break and the housing market will start to recover. The fundamentals — employment, income relative to housing prices, interest rates — are continuing to improve. Indeed, home resale's showed some signs of revival around the turn of the year both nationwide and in the Northeast. In December and January housing starts nationwide showed double-digit gains compared to the same months a year earlier. It's plausible to think some of that momentum will continue, with New Jersey sharing in the recovery. The federal government's recently announced settlement with major mortgage servicers includes New Jersey and other states and should help alleviate the uncertainty around the foreclosure process that has weighed on the housing market.

Even if sales and construction remain lackluster, other industries connected to housing could revive. In particular, the longer people stay in their homes, the more likely they are to do major renovations. National data show a marked increase in spending on home improvements in the fourth quarter of 2011. Indeed, the increase was so strong that it offset weakness in new construction and led to an increase in overall investment in housing. In other words, it is quite probable that 2012 will see some encouraging gains in housing. The major issue could be how they divide between real estate brokers' offices and the home improvement stores.

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New Jersey Business Pulse Survey

Tilting More to Optimism

New Jersey businesses report somewhat more upbeat assessments of current economic conditions and the outlook in January. These findings come from a survey administered by the New Jersey Department of the Treasury.

The New Jersey Business Pulse Survey looks beyond conventional economic data and gathers views in real time from a diverse group of businesses in the state. More than 100 firms spanning a wide spectrum of industries and sizes responded to the January survey. It included 14 questions about current and perspective conditions and gave respondents an opportunity to share their views on other topics of their choice. Detailed results may be found at <http://www.state.nj.us/treasury/pdf/jan12surveyresults.xls>

General Conditions: Current Situation Moving Toward Optimism While the Outlook Is Strongly Positive

The overall assessment of current conditions continues to improve. While about 60 percent of the panel sees little change in current conditions inside and outside New Jersey, one-fourth see ongoing improvement outside the state, with a smaller portion seeing deterioration. Roughly equal numbers of respondents see conditions inside the Garden State as either improving or deteriorating. As was the case in December, respondents to January's survey questions on conditions anticipated over the next year were quite optimistic, with only small fractions expecting deterioration inside or outside New Jersey.

Revenues, Hiring and Capital Spending: Outlook is Broadly Positive

Turning to the outlook for their own companies, responses were heavily weighted toward anticipated gains in their revenues, both world-wide and in their

New Jersey operations. While about 70 percent of the panel expects to see little change in their payroll count, those that do plan to make adjustments generally expect to add to head count, both inside and outside New Jersey. Capital spending plans are modestly less upbeat, with the mix of answers less positive not as positive as those for the revenue and employment questions.

Firms are still experiencing difficulty finding qualified workers for open positions in New Jersey. As was the case in December, roughly one-fourth of the panel reports moderate or significant problems filling open slots in the state. In contrast, few respondents reported problems filling positions outside New Jersey.

Product Price Increases Slightly More Evident as Input Cost Pressures Are Sustained

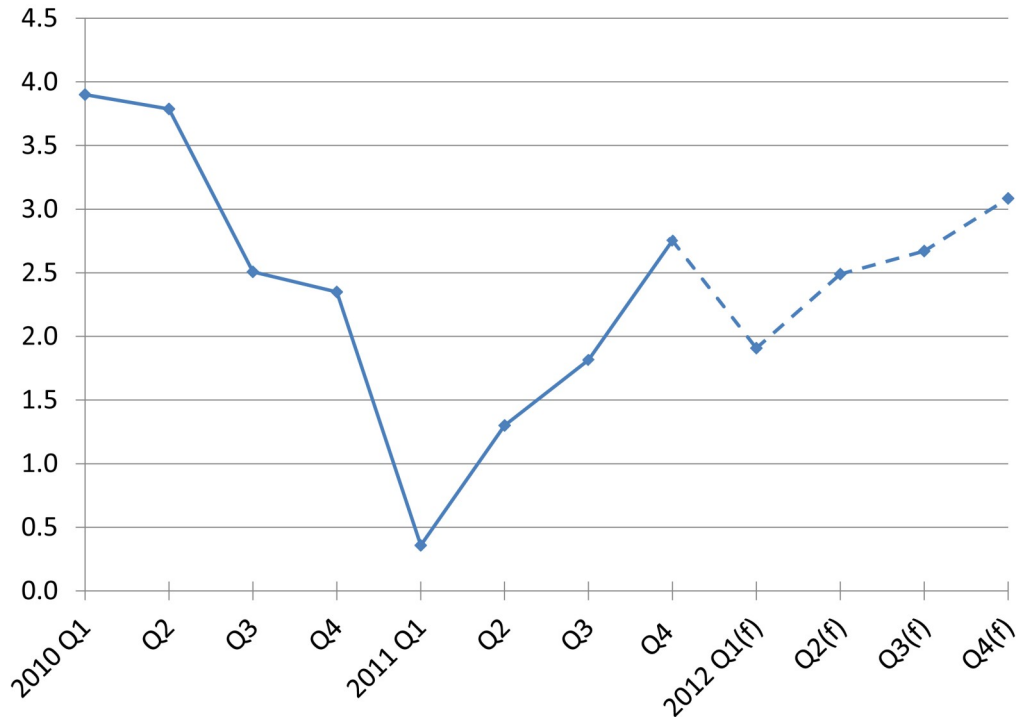
A bit more than one-fourth of respondents report recent increases in any prices that they charge. This is slightly higher than the fraction reporting increases in both November and December. As was the case in December, more than 70 percent of the panel have seen recent increases in input costs.

Conclusion

The January results appear to be broadly consistent with the general sense that the economy is improving. Nonetheless, the optimism appears to be fairly constrained; the most common response to most questions continues to be "no significant change," and relatively few firms anticipate substantial improvement in any category. Still, in general, the positive responses outweighed the negative ones. In the open-ended responses concerns continued to be expressed over regulatory issues, with some respondents commenting on energy policies.

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.

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



(f) - forecast

Data source: U.S. Bureau of Economic Analysis

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