# Current Trends in the New York City Economy

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**Report 6-2005** **September 2004**

New York City's economy is now recovering after being adversely affected by the national recession, the financial market downturn, and the terrorist attacks of September 11, 2001. These three events had a greater impact on the City than on the rest of the metropolitan area or the State.

The loss of jobs during the economic downturn was heavily concentrated in higher-paying sectors, and caused a significant downturn in income that resulted in serious fiscal pressures on the City. However, the City's economy began to revive in the summer of 2003, and as 2004 has progressed there have been additional signs of recovery. While the City's fiscal health has improved, near-term economic growth in the City will be significantly lower than during the late 1990s.

Employment is increasing, commercial real estate markets are improving, and the residential real estate market is continuing to boom. Tourism is rebounding, with higher leisure and hospitality employment, increasing hotel occupancy, and growth in the number of domestic tourists who visit the City.

Though Wall Street profits rose in 2003, they fell by 68.1 percent in the second quarter of 2004 compared with the same period last year. This unexpected shortfall occurred after the industry reported strong profits in the first quarter, and now raises concerns about whether 2004 profits will meet the level of 2003 profits.

Growth in consumer spending essentially carried the national economy from late 2001 into 2003, as rising home values and record-low interest rates allowed consumers to tap into their home equity. Tax cuts also fueled consumer spending, contributing to a rising federal deficit that was exacerbated by military expenditures.

The national economy shifted into higher growth in the summer of 2003. As business spending surged and job creation finally began, the City's economy also experienced a lift, and has been slowly adding jobs since that time. The City's economic health is closely linked to the nation's because a large part of the City's economy is tied to meeting the professional and business service needs of major corporations.

Economic growth in the nation slowed in the second quarter of 2004, with the gain in the gross domestic product (GDP) falling to 2.8 percent from 4.5 percent in the first quarter. Also, growth in national employment has slowed recently compared with the early months of 2004. While forecasters expect gains in GDP and jobs in the coming months, the unevenness of growth highlights some of the risks that lie ahead.

Crude oil futures, which had settled back to about $30 per barrel after the Iraq invasion in early 2003, recently peaked at nearly $50 per barrel in the face of rising worldwide demand for oil and the possibility of supply disruptions in Iraq, Russia, and Venezuela. While prices have since eased, continued high oil prices would divert business and consumer spending from more growth-oriented uses.

The continued emphasis on productivity gains—through technology, outsourcing, or other measures—could dampen job growth. Strong productivity gains allowed the national economy to expand without creating jobs in the early phase of the recovery.

Rising interest rates will place pressure on heightened debt levels throughout the economy. Locally, high housing costs will limit the ability to attract and retain a skilled labor force. Finally, the performance of the financial markets has recently stumbled in the face of various uncertainties.

While none of these risks are serious enough at this point to bring the expansion in the City or the nation to a halt, they are likely to hamper future economic growth.

Among the findings highlighted in this report:

- Wall Street profits fell to $6.8 billion in the first half of 2004, a decline of 23.9 percent compared to the same period last year.
- Seasonally adjusted employment levels in the City began to rise again in July 2003, and since then 34,300 jobs have been created, including 32,100 jobs added so far in 2004.
- The local unemployment rate has begun to recede, averaging 7.8 percent during the first seven months of 2004.
- Wages in almost all parts of the private sector improved in the second half of 2003, and the rate of decline in the securities industry slowed as a result of better year-end bonus payments.
- In 2003, energy prices rose by 15 percent in the region and by 12.2 percent in the nation. During the first seven months of 2004, prices for both increased 9.1 percent.
- Inflation is increasing at a faster rate locally than nationally in 2004. While energy is a factor, housing and food costs are greater contributors to the rise in local inflation this year.
- Inflation is picking up steam in other cities in the nation as well. In 2003, only three of 27 cities reported an inflation rate of 3 percent or more, compared with eight cities during the first half of 2004.
- The total market value for all one-, two-, and three-family homes has increased 21.9 percent in fiscal year 2005, marking the fifth consecutive year that total market values have increased in excess of 10 percent.
- Given the rising levels of personal debt and its burden, personal bankruptcies are also increasing. Nationally, these rose by 6 percent in 2002 and 5.6 percent in 2003. In New York City, personal bankruptcies rose faster—by 7.4 percent in 2002 and 8.4 percent in 2003.
- The number of tourists visiting New York City in 2003 increased 7.2 percent to a record 37.8 million. Hotel occupancy rates for the first half of 2004 are almost 10 percentage points higher than one year earlier.

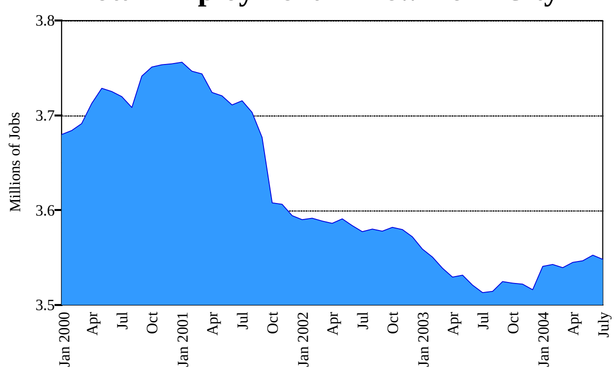
## Employment

Employment in New York City, on a seasonally adjusted basis, has begun to rise again after nearly three years of decline—and the loss of 243,100 jobs. The turn began in July 2003 (see Graph 1), and since then 35,200 jobs have been created. Of these jobs, 32,100 have been added so far in 2004.[1]

Employment in export-oriented sectors, which generally conduct business outside of the city and serve national and international customers, increased by 28,300 jobs through July 2004 (on a seasonally adjusted basis), after losing 37,900 jobs in 2003. While this year's gains occurred primarily in the professional and business services sector and the culture and media sector, the losses in the remaining export-oriented sectors (notably manufacturing and securities) were lower than they had been in 2003.

**Graph 1**

**Total Employment in New York City**




Source: NYS Department of Labor; seasonally adjusted by OSDC

Employment gains in local market–oriented sectors (which include education and health services, construction, retail and wholesale trade, transportation and warehousing, utilities and telecommunications, and eating and drinking services) were slower than in the export-oriented sectors. Between December 2003 and July 2004, over 18,100 jobs were created in the local market–oriented sectors, after a loss of 3,900 jobs in 2003. Jobs were added in more than half of these sectors.

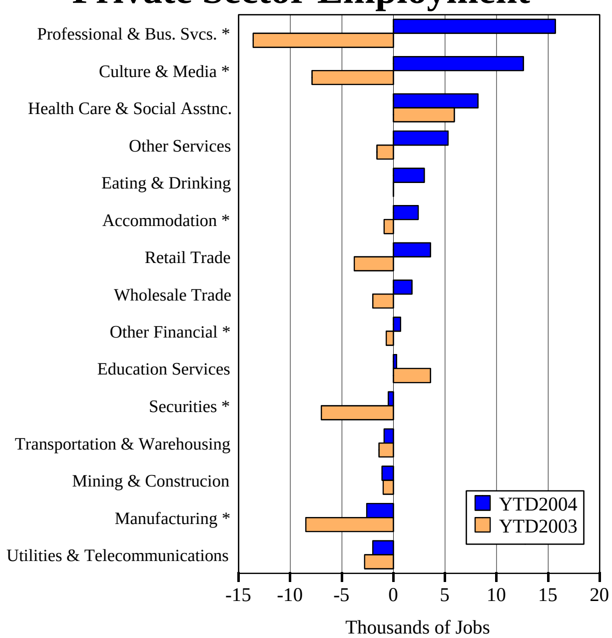
[1] All employment data in this report reflects the North American Industrial Classification System (NAICS) introduced into reporting in early 2003. Analyses in this report are therefore incompatible with numbers in reports issued prior to early 2003.

The resumption of job growth in the export-oriented sectors is good for the City's economy, as export-oriented jobs generally pay higher salaries than local market–oriented jobs. Because of their higher income levels, export-oriented jobs have a greater impact on the local economy. Higher incomes mean more spending, which generates greater demand for goods and services.

Unfortunately, the average salary across industries that are losing jobs this year ($69,701) is still higher than in industries where jobs are being created ($51,117). This is primarily because the securities industry is still shedding its high-paying jobs, thereby boosting the average for the declining industries. Nonetheless, overall income is rising because more jobs are being created than are being lost.

**Graph 2**

**Changes in New York City Private Sector Employment**




* Export-oriented; all others are local market-oriented.
Source: NYS Department of Labor; seasonally adjusted by OSDC

*Professional and Business Services:* Employment in this sector had the highest growth of any sector in the City, adding 15,700 jobs between December 2003 and July 2004 (see Graph 2), following a loss of 12,900 jobs last year. More than half of this year's gains occurred in the administrative and support services subsector, and included an increase of 4,100 jobs in employment services (i.e., temporary help agencies). In the professional services subsector, employment in the accounting industries increased by 3,000, while the computer system design industry added 1,700 jobs through July, with smaller increases posted in the other professional, scientific, and technical industries.

*Culture and Media:* Employment grew by 12,600 jobs through the first seven months of 2004, more than regaining the 4,100 jobs lost in 2003. Almost 2,600 jobs were created in the arts, entertainment, and recreation subsector, while the rest of the new jobs were in information, including a 4,400-job increase in the motion picture and sound recording subsector and a 1,200-job gain in the publishing subsector. The motion picture and sound recording subsectors lost over 11,000 jobs in the prior two years. Broadcasting and Internet-related businesses also reported job gains through July 2004.

The New York State budget that was recently approved by the Legislature includes both City and State tax credits to encourage the creation of jobs in film production.

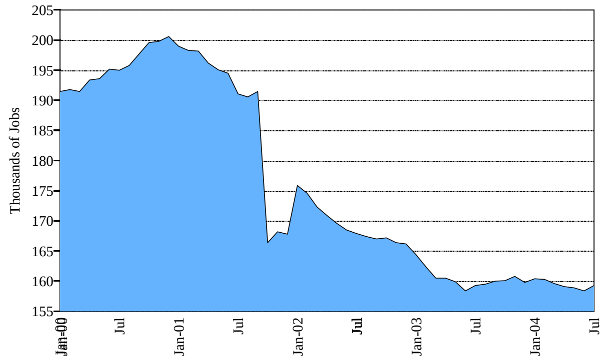
*Accommodation:* This sector gained 2,400 positions between December 2003 and July 2004, after losing 400 jobs in 2003. This area lost more than 4,000 jobs in 2001 as a result of the drop-off in tourism-related industries following the events of September 11, 2001—but recouped 1,600 jobs in 2002.

*Manufacturing:* Employment in this sector has consistently declined in the City. During the first seven months of 2004, manufacturing lost 2,600 jobs, including 2,200 jobs in the apparel manufacturing subsector. Durable goods manufacturing increased by 800 jobs, however. In the prior three years, 50,000 manufacturing jobs disappeared—a decline of almost 30 percent.

*Securities:* The high-paying securities industry, where salaries averaged $226,700 in 2003, lost 500 jobs between December 2003 and July 2004. Wall Street began slowly reducing employment early in 2001 and lost almost 25,000 jobs immediately following the events of September 11, 2001 (see Graph 3), partially as a result of relocations by firms to sites outside the City. While some of these jobs returned in subsequent months, over 40,000 jobs were lost between December 2000 and December 2003.

**Graph 3**

**Securities Industry Employment**

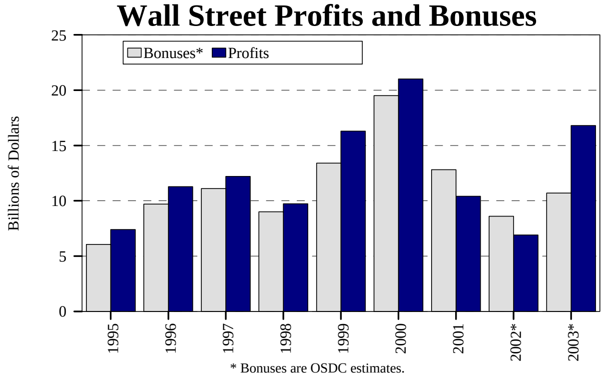



Sources: NYS Department of Labor; OSDC analysis

Securities firms continue to be cautious about hiring due to the unevenness of profitability. While profits on New York Stock Exchange member firms were $5.1 billion in the first quarter of 2004 (45 percent higher than in the same quarter last year), profits in the second quarter totaled only $1.7 billion (68.1 percent below the same quarter of 2003). This profits fall-off was due to a decline in revenues from commissions and gains generated by the firms' own trading. For the first half of 2004, profits are 23.9 percent lower than they were at this point last year. In 2003, profits had rebounded to $16.8 billion—second only to the $21 billion in profits earned in 2000 and more than double the amount of profits earned in 2002 (see Graph 4).

**Graph 4**

**Wall Street Profits and Bonuses**




* Bonuses are OSDC estimates.

Note: Bonuses are paid in the fourth quarter of the current calendar year and in the first quarter of the following calendar year.

Sources: NYS Department of Labor; New York Stock Exchange; OSDC analysis

A resumption of hiring in the securities industry would greatly benefit the New York economy. In general, every securities job created in the City results in the creation of two additional jobs in the City and one job in the suburbs.

*Other Financial:* The rest of the financial sector gained 700 jobs this year. An increase of 2,000 jobs in the real estate subsector was partially offset by job losses in all other financial industries, including a decline of 1,200 jobs at depository institutions.

*Health Care and Social Assistance:* This sector added the most jobs among the local market–oriented sectors in 2004, growing by 8,200 jobs. Health care added 8,300 jobs, while social assistance lost 100 jobs. Health care and social assistance continues to be a consistent engine of growth for the City, adding a total of 21,400 jobs between December 2000 and December 2003.

*Trade:* The recession and the events of September 11, 2001, hurt employment in the retail trade sector, which lost more than 20,000 jobs between December 2000 and December 2001. Almost one third of these jobs were regained in the following two years. Between December 2003 and July 2004, retail trade gained 3,600 jobs, including an increase of 2,100 positions in the clothing stores industry. However, losses occurred in stores in the general merchandise, food and beverages, and health and personal care industries. The wholesale trade sector grew by 1,800 jobs in 2004 after losing 9,500 jobs over the three years ending in December 2003.

*Other Private:* Employment in the food services and drinking places sector grew by 3,000 jobs during the first seven months of 2004, following gains of 3,200 jobs in 2003 and 4,300 jobs in 2002.

Job losses slowed in the utilities and telecommunications sector, to 2,000 jobs compared to 2,800 jobs during the first seven months of 2003. The construction sector lost 1,100 positions in 2004, adding to the 16,500 jobs lost in the prior three years, and experienced similar declines compared to the same period last year. The educational services sector, which was one of only three sectors to gain jobs between 2000 and 2003, gained 300 jobs during the first seven months of 2004.

The transportation and warehousing sector also had employment declines in 2004, losing 900 jobs. This followed losses of 1,500 jobs during the prior two years. Only the courier and messenger subsector showed growth in 2004.

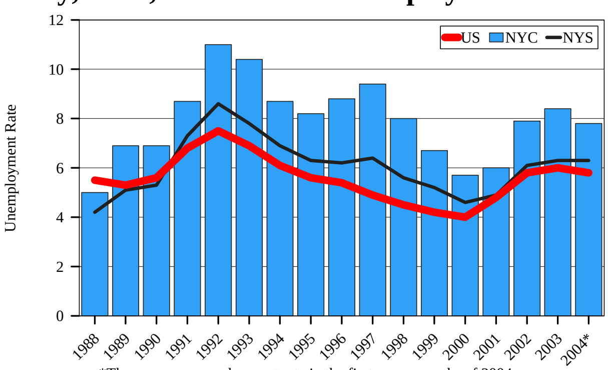
*Government:* This sector lost 14,300 jobs between December 2003 and July 2004, with job declines in federal (1,400), State (700), and local (12,300) government. During 2003, the government sector lost 14,000 jobs, of which 10,900 were in the local government subsector.

## Unemployment Rate

New York City's unemployment rate[2] has fallen slightly in the first seven months of 2004, to an average of 7.8 percent (see Graph 5). Monthly labor force statistics show that while the number of unemployed residents in New York City has declined in the first seven months of 2004 compared to the same period in 2003, the number of employed residents did not grow.[3] The City's unemployment rate has consistently been higher than the rates for both the State and the nation, and though the differences narrowed during the late 1990s, they have since begun to widen again.

**Graph 5**

**City, State, and National Unemployment Rates**




*The average unemployment rate in the first seven months of 2004.
Source: NYS Department of Labor

[2] The unemployment rate is defined as the proportion of labor force participants without jobs. The labor force consists of people who are either employed or actively seeking jobs. People not actively participating in the labor force are not counted as unemployed.

[3] The labor force data measure the number of employed based on place of residence, as opposed to employment data, which measure the number of jobs based on place of employment. Thus, a decline in the labor force—as shown by lower labor force participation rates—is a major factor in the lowering of the unemployment rate. In other words, the unemployment rate can fall not just because people are finding jobs, but also because workers are getting discouraged about not finding jobs and cease looking for work.

The City's unemployment rate hit a six-year high of 8.4 percent in 2003, rising from a decade low of 5.7 percent in 2000. The corporate scandals and the war in Iraq in early 2003 weighed down the labor market and left many people not only unemployed, but also discouraged from job hunting. The 2003 unemployment rate was still far below its peak of 11 percent, seen in 1992 during the last recession.

The U.S. Census Bureau's Current Population Survey provides additional demographic data on the City's labor market, including the following highlights.

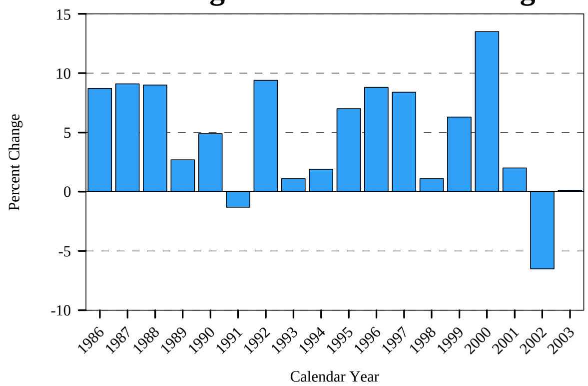
- People aged 65 and over made up the only age group that has a higher percentage of job seekers unable to find a job in the first half of 2004 compared to a year ago. During the recession, the labor force participation rate of this group increased as many retirees reentered the workforce after their pensions and savings shrank because of the collapse of the stock markets.
- Among the major racial or ethnic groups covered by the survey, the unemployment rate of Hispanics or Latinos showed the largest decline during the first half of 2004. White adults were the only group to see an increase in the percentage of people participating in the labor force and still reduce their unemployment rate. During the recession, Black or African-American adults suffered the most, with the sharpest increase in the unemployment rate and the deepest decline in the participation rate.
- Women in the workforce fared better during the recession than men, as their unemployment rate increased less and their participation rate declined less than the comparable rates for males. One of the reasons for this can be attributed to the higher concentration of women working in service industries, in particular the noncyclical educational, health, and social service areas. Almost 40 percent of female workers in the City are employed in these sectors. By contrast, about 40 percent of employed males work in the sectors hit hardest by the recession—financial activities, manufacturing, professional and business services, and transportation and warehousing.

## Wage Income

Recently released data show that although private sector wages experienced a very small gain (0.1 percent) in 2003, this represented a rebound after wages declined in 2002 by 6.5 percent, which was the first annual decline since 1991 (see Graph 6).

**Graph 6**

**Annual Change in Private Sector Wages**




Source: NYS Department of Labor

With overall job growth building in 2004, wages are expected to show an increase. In addition, the 25 percent increase in securities industry year-end bonuses for 2003, most of which was paid in the first quarter of 2004, should help boost wage growth this year. However, the continued loss of high-salary securities jobs will dilute some of the employment-related wage gain, keeping the overall wage growth this year relatively modest.

In 2003, annual wages in the local market–oriented sectors generally increased, particularly the noncyclical education and health services sector, while many export-oriented sectors, such as finance and manufacturing, still experienced declining annual wages. Indeed, the local market–oriented education and health services sector has not experienced any decline in either wages or employment throughout the recession, and last year wages in this sector increased by 6.8 percent.

When the City's economy started showing signs of recovery during the second half of 2003, wages in almost all private sectors improved compared to the same period one year earlier. Total annual wages increased by 0.3 percent in 2003 as government wages increased slightly, supplementing the small private sector wage gain.

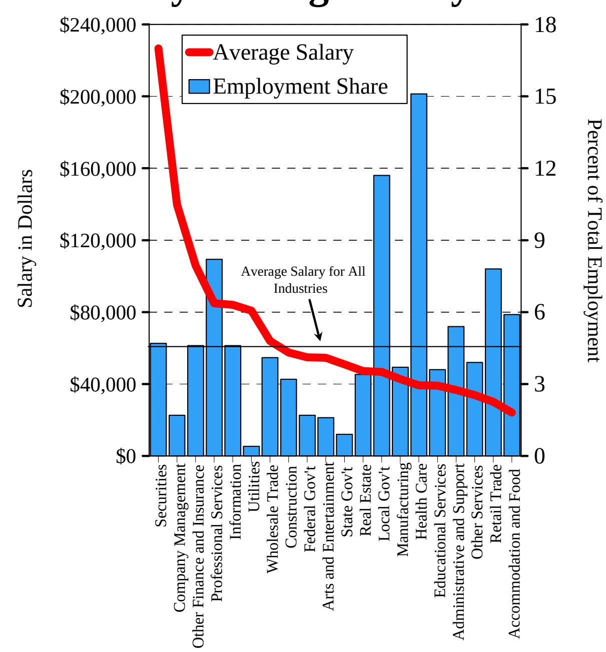
The rate of decline in securities industry wages slowed to 5.4 percent in 2003 because improved year-end bonus payments in the fourth quarter offset part of the impact of declining employment. Between 2001 and 2003, the securities industry accounted for 79 percent of total wage losses in the City. Nevertheless, the industry remained the largest contributor to City wages, representing one fifth of total wages paid in 2003.

The Citywide average salary across all industries grew by 1.5 percent to $60,343 in 2003, after falling by 2.6 percent in 2002. Because inflation rose 3.1 percent in 2003, the real (inflation-adjusted) average Citywide salary actually declined by 1.6 percent.

The relatively high Citywide average salary masks the disparity among salaries in different industries, which range from a high of $226,700 in securities to $24,131 in accommodation and food services (see Graph 7). Over 71 percent of all employment in the City occurs in industries that pay less than the Citywide average. During the recent recession, the higher-paying subsectors both lost jobs and saw wages decline, while the lower-paying subsectors experienced gains in both.

**Graph 7**

**Distribution of City Employment by Average Salary**




Sources: NYS Department of Labor; OSDC analysis

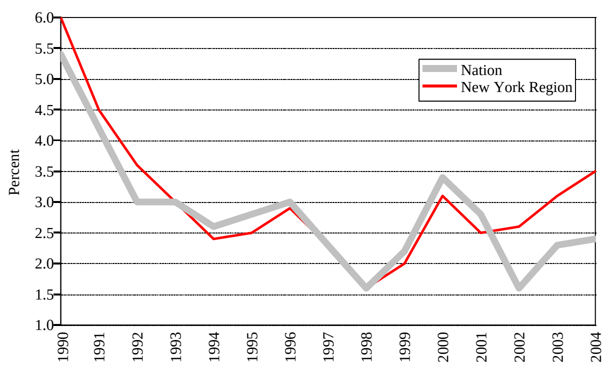
The disparity between the salaries in the securities industry and in the nonfinancial industries has sharply widened over the last decade. The divergence has only been temporarily interrupted during periods when financial market slowdowns restrained securities industry salaries. Between 1994 and 2003, the average salary in the securities industry doubled to $226,700, while the average in the nonfinancial industries increased only 38 percent to $49,462. While the average securities industry salary is currently 4.6 times that of the average nonfinancial industries salary (up from 3.2 in 1994), the multiple reached as high as 5.2 during the peak of the financial market boom in 2000.

## Inflation

Inflation in the New York City metropolitan area[4] has begun to rise, and is increasing at a faster rate than in the nation (see Graph 8). In 2003, the inflation rate was 3.1 percent in the region and 2.3 percent in the nation. During the first seven months of 2004, inflation in the region increased by 3.5 percent compared with the same period one year earlier, but the inflation rate for the nation only rose to 2.4 percent.

**Graph 8**

**Overall Inflation Rate**



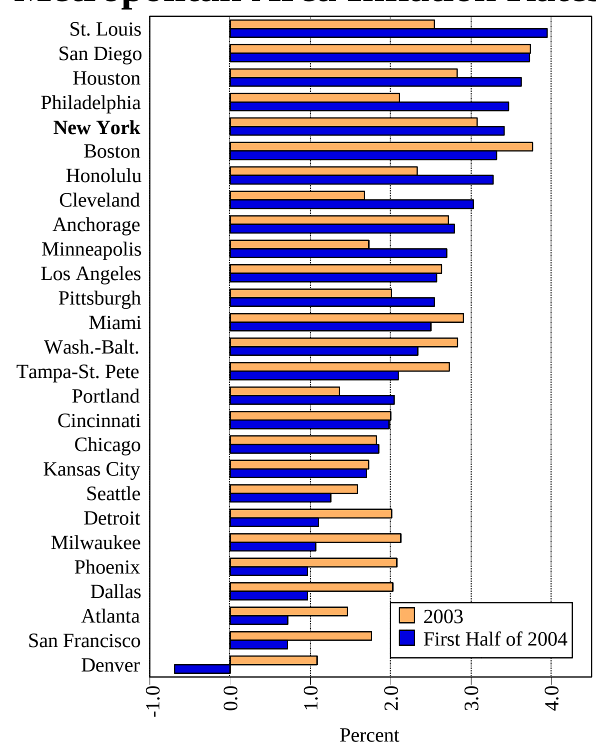

*January through July 2004 compared to the same period one year earlier.
Source: U.S. Department of Labor

Inflation is picking up steam in other cities as well. In 2003, among the 27 metropolitan areas for which inflation data are available, only three cities reported an inflation rate of 3 percent or more. During the first half of 2004, however, eight cities reported inflation at this level. New York ranked fifth during the first half of 2004, behind St. Louis, San Diego, Houston, and Philadelphia (see Graph 9). Only Boston and San Diego exceeded New York's inflation rate during 2003.

Energy costs have been very volatile in recent years. While energy is a factor in rising inflation, energy costs represent a small piece (about 7 percent) of the market basket used by the consumer price index to measure inflation.[5] Other factors play a larger part in the rise of inflation, especially for the New York region.

**Graph 9**

**Metropolitan Area Inflation Rates**




Source: U.S. Department of Labor

In 2003, energy prices rose by 15 percent in the region and by 12.2 percent in the nation. During the first seven months of 2004, the increase in both the region and the nation was 9.1 percent. While these increases are high, they are diluted within the overall inflation measure. Excluding energy, inflation in the region has risen from 2.4 percent in 2003 to 3.2 percent in the first seven months of

[4] The Bureau of Labor Statistics at the U.S. Department of Labor compiles inflation on a regional basis. The local region is comprised of New York City and its suburban areas, including Long Island and parts of the Hudson Valley, Northern New Jersey, Connecticut, and Pennsylvania.

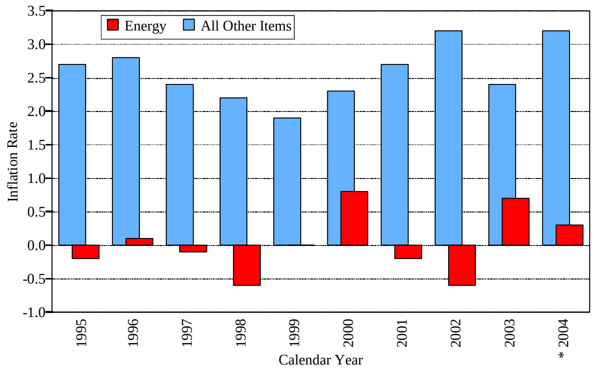
[5] Energy is initially presented in the consumer price index within other areas, notably housing and transportation, and then separately aggregated.

2004, while the national rate has increased from 1.5 percent last year to 1.9 percent so far this year (see Graph 10).

New York's higher rate of inflation (both compared to the nation and to recent years) is rooted in several components—most notably housing and, more recently, food costs.

**Graph 10**

**Contribution of Energy to New York Area Inflation**




* January through July 2004 compared to the same period one year earlier.
Source: U.S. Bureau of Labor Statistics

Housing is the largest component of the consumer price index, accounting for more than 42 percent of the national market basket used to measure inflation (a portion of energy costs are included in housing—such as home heating oil and utilities). Housing costs are also rising faster in the region than in the nation.

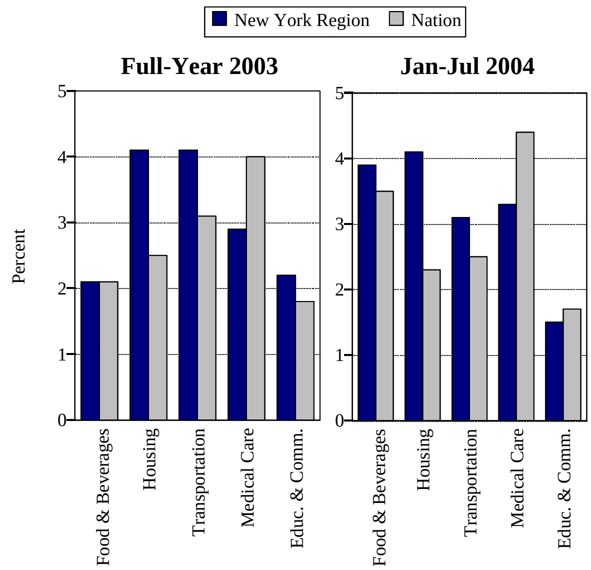
Throughout the late 1990s, the region and the nation shared a relatively close rate of increase in housing costs, but these rates began to significantly diverge in 2002. In both 2002 and 2003, housing costs in the region advanced by 1.6 percentage points more than in the nation. In the first seven months of 2004, housing costs in the region have increased by 4.1 percent, nearly double the rate of increase in the nation (see Graph 11).

Food and beverages represent more than 15 percent of the consumer price index. While food prices rose at about the same rate in both the region and the nation last year (2.1 percent), they have increased at a much faster rate in the first seven months of 2004, rising by 3.9 percent in the region and 3.5 percent nationally.

Transportation is the next largest component of the consumer price index, accounting for nearly 17 percent of the national market basket (energy costs for gasoline are included in transportation costs). Transportation costs in the region rose by 0.5 percentage points more than in the nation during 2004, after growing a full percentage point more in 2003 (when mass transit fares were raised).

**Graph 11**

**Comparison of Inflation by Major Components**




Note: Comparison is with the same period one year earlier.

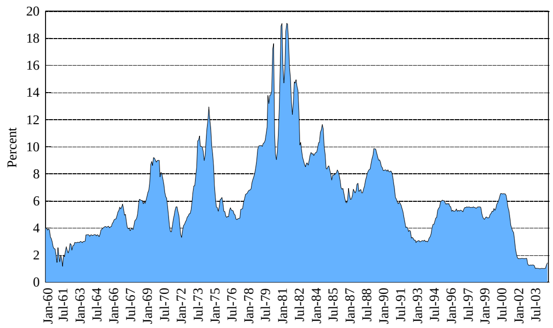
## Interest Rates and Personal Debt

Over the last few years, the Federal Reserve Board followed a very accommodative interest rate policy. Concerned with low economic growth and the possibility of deflation (based upon the recessionary experiences of the Japanese economy in the 1990s), the Federal Reserve felt it could lower rates dramatically to stimulate the economy without risking price instability. The federal funds rate was lowered to 1 percent, its lowest point in more than 40 years (see Graph 12), for an extended period.

Falling interest rates, aided by rising home values and tax reductions, contributed to the growth in consumer spending that primarily drove the national economy until business spending picked up in the summer of 2003. With interest rates at generational lows, homeowners were able to refinance their mortgages, and in many cases removed equity from their homes (at the cost of higher mortgage balances). As home prices rose quickly, adjustable rate loans often offered the lower rates necessary to make a home purchase affordable for first-time homebuyers. Low rates also made other forms of consumer credit (such as car loans) less expensive.

**Graph 12**

**The Federal Funds Rate**




Source: Federal Reserve System

Nationally, home mortgage debt rose by 12 percent in 2002, 12.7 percent in 2003, and 12.5 percent in the first quarter of 2004, reaching an annualized level of $6.9 trillion. These are the fastest rates of increase since the mid-to-late 1980s. Other forms of consumer credit grew by 4.4 percent in 2002, 4.9 percent in 2003, and 6.1 percent in the first quarter of 2004, reaching an annualized level of $2.1 trillion.

The rise in various debt levels is reflected in the Federal Reserve Board's household financial obligations ratio, which looks at household payments for items such as homes, cars (including leases), and other consumer credit as a percent of disposable income. The ratio has risen and fallen with economic cycles over the last few decades, but has been trending upward. In 2003, financial obligations equaled 18.3 percent of income.

Given the rising levels of debt and its burden, personal bankruptcies are also increasing. Nationally, these rose by 6 percent in 2002 and 5.6 percent in 2003. In New York City, personal bankruptcies rose somewhat faster—by 7.4 percent in 2002 and 8.4 percent in 2003.

As economic growth has picked up and inflation has begun to rise, the Federal Reserve Board has declared that the threat of deflation has passed. The Federal Reserve has, therefore, embarked on a policy of measured increases in interest rates, both to control the pace of economic growth and to head off the renewed threat of inflation.

As a result, the federal funds rate was raised by one-quarter of a point in June and by a similar amount in August. Additional increases are expected over the rest of 2004 and throughout 2005. By raising rates at a steady, expected pace, the Federal Reserve hopes to avoid sending the economy into another recession. Given the increased debt levels faced by consumers, rising rates may lead to a more pronounced retrenchment in consumer spending.

## Real Estate

The City's real estate market has performed well through the first half of 2004. Commercial properties have rebounded from the struggles brought on by the recession and the events of September 11, 2001. Through June 2004, asking rents have risen and vacancy rates have fallen. The residential real estate market was never adversely affected by the recession, and with low interest rates (particularly mortgage rates), demand for homes has been strong and property values have risen. This is particularly true of the condominium and cooperative markets in Manhattan, where the average selling price recently exceeded $1 million.

### *Commercial Real Estate*

The overall vacancy rate for Manhattan's office market fell gradually, from a high of 17.7 percent at the end of 1991 to a low of 4.2 percent in the second quarter of 2000. From that point, the rate steadily rose through the first quarter of 2003, when it reached 13 percent. The rate has since declined to 11.9 percent in June 2004, with the lowest vacancy rate in Midtown (11.4 percent) and the highest rate in Downtown (12.9 percent; see Graph 13). The Downtown vacancy rate has been improving over the past six months, falling 1.3 percentage points.

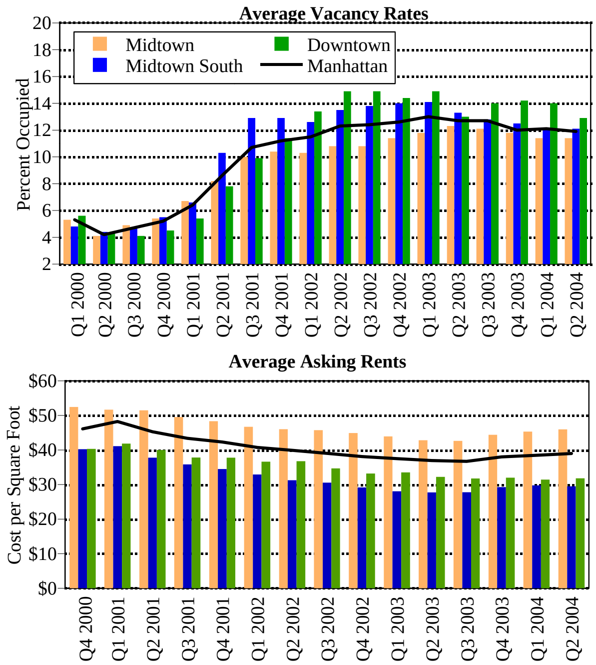
For Class A properties, the overall vacancy rate in June 2004 was 10.5 percent. Downtown had the highest vacancy rate among Class A properties, (11.8 percent) and Midtown South had the lowest rate (6.3 percent), although only 3.2 percent of all Class A property is located in Midtown South. The Midtown vacancy rate was 10.5 percent.

Following the trend in vacancy rates, Manhattan's commercial rental rates also showed improvement. Rental rates declined from the first quarter of 2001 through the third quarter of 2003, when rents were

$36.70 per square foot. Since then, rates have risen through June 2004, reaching $38.99 per square foot. Midtown had the highest average rents of all the submarkets in the second quarter of 2004, at $45.96 per square foot, compared with $31.81 per square foot in the Downtown submarket and a low of $29.76 per square foot in Midtown South.

**Graph 13**

**Manhattan's Commercial Real Estate Market**




Source: Colliers ABR

Another market indicator that points to recovery is net absorption, which is the change in available space from one period to another. Negative net absorption means that less space was occupied in the later period than in the earlier period, or that more space was returned to the market than was leased. Positive net absorption indicates that vacant space was either leased or taken off the market for other reasons.

In Manhattan, for all submarkets and all three building classes, net absorption on a year-to-date basis went from a negative 16,946 square feet in June 2003 to a positive 5,254,889 square feet in June 2004.

The most dramatic change in net absorption during this time period was in Class A properties. Through the first six months of 2003, all Class A properties had a positive net absorption of 80,666 square feet, while Midtown Class A properties had a negative net absorption of 1,388,726 square feet. During the first six months of 2004, all Class A properties had a positive net absorption of 4,288,970 square feet, with net absorption for Midtown Class A equal to 2,904,927 square feet (see Table 1).

**Table 1**

**Year-to-Date Net Absorption Positive/(Negative) Square Feet**

| | Jun-03 | Jun-04 |
|---|---|---|
| **All Manhattan** | | |
| Midtown | -2,176,466 | 3,642,959 |
| Midtown South | 605,022 | 359,781 |
| Downtown | 1,554,496 | 1,252,149 |
| **Total** | **-16,948** | **5,254,889** |
| **Class A Manhattan Property** | | |
| Midtown | -1,338,720 | 2,902,927 |
| Midtown South | 12,600 | 58,423 |
| Downtown | 1,408,792 | 1.327.620 |
| **Total** | **80,666** | **4,288,970** |

Source: Colliers ABR

Leasing was very active in June 2004, with 2.6 million square feet of new deals closed, raising the total leasing for the first six months of this year to 8.8 million square feet. This monthly leasing pace hasn't been matched since 2000, when the annual leased total was 31.5 million square feet. In 2003, 18.3 million square feet was leased, which represented an increase over each of the prior two years, but was significantly lower than the amount of space leased during the period from 1998 to 2000, when both high-tech and financial services firms were leasing enormous amounts of office space.

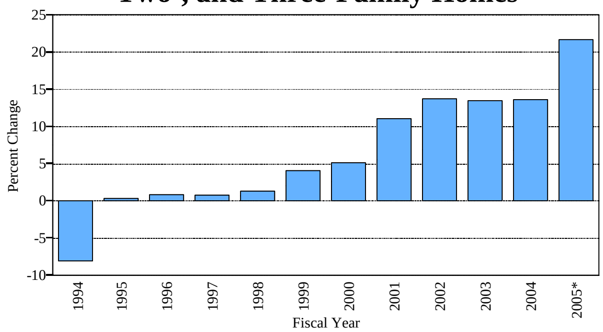
In 2003 the most active industry in leasing was the legal profession, which took almost 3 million square feet of new space for reasons that included growth, mergers, and lease expirations. The financial services industry ranked second despite slow employment growth, taking over 2.2 million square feet. The number of large transactions increased in 2003, with 19 new deals for properties larger than 100,000 square feet, compared to 8 new deals for properties of that size in 2002. Renewals or renewals and expansions of property larger than 100,000 square feet followed the same trend, with 18 in 2003, compared to just 7 in 2002.

*Residential Real Estate*

Based on preliminary data for FY 2005 from the City's Department of Finance, the total market value for all one-, two-, and three-family homes[6] has risen to $277.3 billion, an increase of 21.9 percent from the previous fiscal year. This increase is the fifth consecutive year that total market values have increased in excess of 10 percent (see Graph 14).

**Graph 14**

**Growth in Market Values for One-, Two-, and Three-Family Homes**

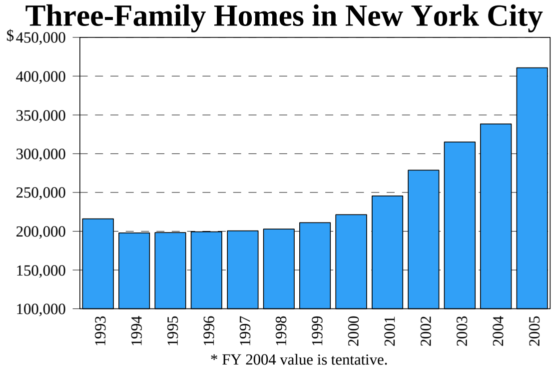



*Data for FY 2005 is tentative.
Source: NYC Department of Finance

Increasing market values have brought the average value for one-, two-, and three-family homes to $433,000 on the tentative FY 2005 tax roll (see Graph 15), compared to $221,000 in FY 2000, which is an increase of 95.6 percent.

**Graph 15**

**Average Value for One-, Two-, and Three-Family Homes in New York City**




* FY 2004 value is tentative.
Source: NYC Department of Finance

The average home value in Manhattan is now $1,853,000, far exceeding averages in the other boroughs. Brooklyn has the second-highest average value ($457,000), followed by Queens ($434,000), Staten Island ($380,000), and the Bronx ($339,000).

In Manhattan, where the cooperative and condominium markets are robust, the average sales price of apartments (as reported by the Corcoran Group) exceeded $1 million during the first quarter of 2004. This is the highest level ever, and prices have continued to increase. The Corcoran report also notes that demand continues to far exceed supply in the borough, and many properties sell on the first day they are listed.

The average sales price for a condominium through the first half of 2004 was $1.2 million, an increase of 38 percent from one year earlier, while the sales price for cooperative apartments grew by 19 percent during this period, reaching $858,000.

## Tourism

Tourism is an important part of the City's economy, contributing to employment in several areas of the leisure and hospitality, transportation, and trade sectors. Tourism also helps contribute to an improving City economy, as greater numbers of travelers fill up hotels and restaurants and partake in the City's many cultural offerings.

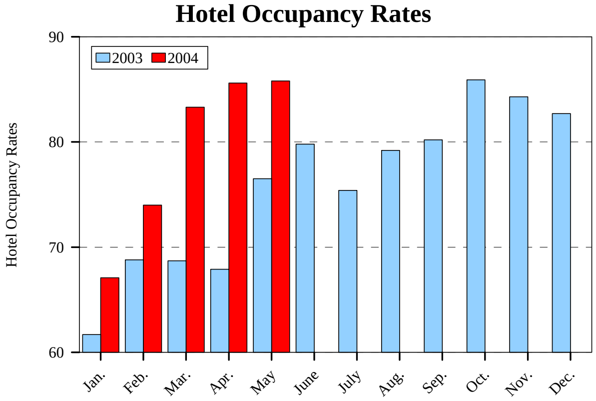
In August 2004, NYC & Company (the City's convention and visitors bureau) reported that the number of visitors to the City reached a record 37.8 million in 2003, an increase of 7.2 percent from the 2002 level. This increase is entirely due to growth in domestic visitors, as the number of foreign visitors—who usually spend more money on their trips to the City than domestic visitors do—declined. Nevertheless, the City was still the most popular U.S. destination for international visitors. NYC & Company estimates that the number of visitors to the City will reach 39.4 million in 2004, with growth expected in both domestic and international visitors.

Previously, both the recession and the 2001 terrorist attacks severely curtailed travel to New York City. Data from NYC & Company showed that a recovery began in 2002, when the number of tourists visiting the City increased by 0.3 percent, to total 35.3 million people. While domestic visitor counts grew by 2.4 percent in 2002, to 30.2 million, the number of international visitors fell by 10.5 percent.

[6] Almost all of the City's 640,000 one-, two-, and three-family homes are located outside of Manhattan. Queens and Brooklyn claim nearly three quarters of these homes (42.4 percent and 31.3 percent, respectively).

Hotel occupancy rates provided by PKF Consulting support the visitor trends reported by NYC & Company. Occupancy rates for the first six months of 2004 were almost 10 percentage points higher than one year earlier. This strength has built on a surge that began in the second half of 2003 (see Graph 16). The start of the war in Iraq held down travel in early 2003. Occupancy rates reached 76 percent for all of 2003, slightly higher than the 75.6 percent reached in 2002.

**Graph 16**
**Hotel Occupancy Rates**



Source: PKF Consulting

Average daily hotel room rates fell in the first three months of 2004, but because of significant improvements since March, they averaged $198.49 for the first six months of the year, an increase of 7.3 percent over 2003 levels. Room rates have experienced significant declines in recent years due to a falloff in tourism, especially among international travelers. Room rates fell by over 12 percent in 2001 from highs of over $230 in 2000, and fell an additional 5 percent in 2002. Average daily room rates declined again in 2003 by 2.3 percent, to $193.36, when compared to the previous year (although between September and December rates were higher than in 2002).

Attendance at Broadway shows in 2004 has grown by over 7 percent through July 4, according to the League of American Theatres and Producers. This reflects a rebound from 2003, when attendance dropped by almost 3 percent, partially due to a musicians' strike that temporarily closed Broadway—but also because of the slowdown in tourism due to the war in Iraq.

According to the Port Authority of New York and New Jersey, airplane passenger traffic at airports in the New York City region is also recovering. In 2003, domestic passenger traffic increased by 3.1 percent and international traffic by 0.2 percent when compared to 2002. As with the rest of the tourism indicators, this trend has intensified in 2004 with domestic traffic up 13.5 percent, and international travel higher by 18.1 percent through April.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