

ECONOMIC NOTES

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NYC's Economic Growth Slowed During Second Half of 2006; New Year Promises Steady Gains

Overview: The City's economy is not growing as rapidly as a year ago, but no significant impediments to continued growth have emerged. A tentative housing market should be reassured by steady job and income growth. A banner year for Wall Street provides a boost for the new year.

- Real Gross City Product (GCP), a measure of the overall City economy, grew 2.4 percent in 3Q06, somewhat above the 2.0 percent U.S. rate (final estimate). The City's growth rate has been decelerating since 1Q06, but a recession does not appear imminent. Of five key economic indicators, two declined in NYC and one declined in the U.S. during 3Q06.

- NYC payroll jobs grew at a seasonally adjusted annualized rate of 1.9 percent or by 16,800 jobs in 3Q06, after adding 14,300 jobs in 2Q06. Job gains have been slowing since June and payroll employment has been declining since September. U.S. payroll jobs grew 1.4 percent in 3Q06, but finished the year on a strong note.

- Personal income taxes withheld from paychecks rose 1.3 percent in 3Q06, on a year-over-year basis. Estimated tax payments, primarily on interest income, rental income, and capital gains, rose 9.4 percent on a year-over-year basis, after a 25.9 percent gain in the second quarter.

- NYC's inflation rate dropped to 4.3 percent in 3Q06, after spiking to 4.7 percent in the second quarter. Core

inflation, which excludes food and energy prices, rose to a 14-year high of 4 percent in 3Q06. The City's inflation rate surpassed the nation's in every category except apparel, transportation, and energy.

- Unemployment fell to 4.1 percent in October, its lowest rate in almost 40 years. For the full 3Q06, it averaged 5.1 percent, the lowest quarterly average in almost 20 years. However, the labor-force-participation rate fell to 59.9 percent, compared to 60.3 percent in 2Q06. U.S. unemployment was steady at 4.7 percent.

- Retail sales in the City rebounded after a soft summer.

General sales tax collections declined slightly in 3Q06 compared to the corresponding quarter of the previous year, but grew briskly in October and November. Retail employment also grew rapidly late in the year.

- Big Wall Street firms noted record revenues and earnings for FY2006, portending a large injection of bonus money into the NYC economy in early

2007. The four large publicly held investment banking firms reporting before year's end recorded a collective 33-percent increase in net revenue and a nearly 50-percent increase in net income. A fifth reported a 38-percent rise in net earnings in its first three quarters.

- The Manhattan office vacancy rate fell to 7 percent in the third quarter, the lowest since 2001. Midtown South had the lowest vacancy rate at 6.1 percent, followed by Midtown (6.5 percent) and Downtown (9.1 percent). The average commercial asking rent in Manhattan rose to \$45.84 per square foot in the third quarter, led by Midtown, where asking rents topped \$53 per square foot.

INSIDE FOCUS:

New York City's Self-Employment Boom

Summary Table. Five Key Economic Indicators, NYC and U.S., 3Q06 vs. 2Q06

		1. GCP/GDP Growth, SAAR	2. Payroll-Jobs Growth, SAAR	3. PIT Withheld, Growth, NSA	4. Inflation Rate, NSA	5. Unemployment Rate, SA
3Q06 vs. 2Q06	NYC	2.4% Worse	1.9% Better	1.3% Worse	4.3% Better	5.1% Better
	U.S.	2.0% Worse	1.4% Better	6.4% Better	3.5% Better	4.7% No Change

NSA means Not Seasonally Adjusted. SA means Seasonally Adjusted. SAAR means SA Annualized Rate. PIT means Personal Income Tax. Comparisons for "Better" or "Worse" are with the prior quarter.

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Self-Employment Boom Fuels City's Job Growth

Summary: Wage and salary jobs in the five boroughs remain below the peak level reached in December, 2000. Nevertheless, more City residents report that they are employed today than ever before. One important reason for the apparent discrepancy is that a growing portion of the City's workforce is self-employed. Although many self-employed New Yorkers are in traditional trades, an increasing proportion are educated workers engaged in the information economy and less-educated workers providing personal services.

The job count is one of the most important indicators of the City's economic health. More jobs mean greater household incomes, more consumer spending, more prosperous local businesses, and a better fiscal picture for the City. For analysts and forecasters, employment data are particularly important because they provide a relatively current picture of what is happening in the local economy.

The two most widely watched employment series are the Current Employment Statistics (CES), and the Local Area Unemployment Statistics (LAUS). The former is tabulated from employer reports while the latter is compiled from a monthly telephone survey of households. Employment measured by the CES is, for New York City, typically higher than that measured by the LAUS, because more workers commute into the City than out. Also, multiple jobs held by the same worker would be counted separately by the CES, but the LAUS would count the worker once.

Usually, the two series track one another, telling the same story from slightly different points of view. During the past few years, however, they have displayed very different trends, suggesting that there are some fundamental changes occurring in the city's job markets. According to the CES series, which measures wage and salary jobs located within the City regardless of where the job-holder resides, payroll employment in the five boroughs plunged during the recession of 2001. Through October 2006, the job total was still 137,000 less than the previous peak number. In contrast, the LAUS data, which measures the number of New Yorkers who hold jobs regardless of their place of employment, show a much less severe job decline early in the decade. Further, by October 2006 almost 110,000 more New Yorkers held jobs than at the previous cyclical peak.

It is possible for the two employment series to show different trends if, for example, a growing number of City residents are working outside of the City, or if a growing

proportion of jobs within the City are held by City residents. However, neither of those explanations are plausible, since a similar discrepancy is displayed in the jobs trends in other parts of the metropolitan region as well. At the regional level, the number of jobs and the number of job-holders must roughly match.

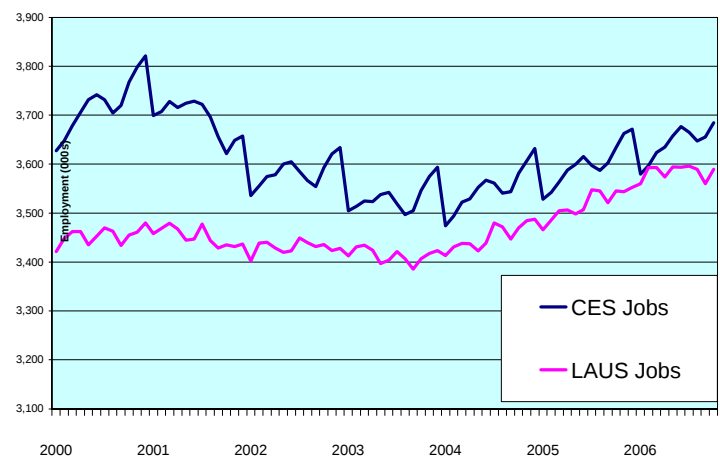
A more likely cause of the puzzling divergence in the two employment measures is self-employment. Self-employed workers are generally detected by the household employment and unemployment survey, but are missed by the survey of businesses, which polls only firms that have wage and salary employees.

Data published by the U. S. Bureau of Economic Analysis¹ (BEA) confirm that self-employment is a growing factor in our City's labor market and needs to be accounted for when evaluating the City's economic well-being. The BEA data indicate that the City's overall job base is actually nearing 4.5 million, rather than the 3.7 million figure often cited. Since 1975, the job base has grown by about 700,000, and self-employment has accounted for nearly two-thirds of the increase.

Cyclical or Structural?

In both our City and nation, self-employment declined for many decades. As late as 1948, nearly 19 percent of working Americans were self-employed, primarily because there were still many family farms. The rate in non-agricultural industries had already fallen to 12 percent, not a great deal higher than it is today. Self-employment in non-agricultural industries stabilized at about 10 percent of the work force in the 1960s, and has remained at that level since.²

Chart 1: CES and LAUS Employment Trends, New York City 2001-2006



Source: Bureau of Labor Statistics

¹ Local Area Income and Product Accounts, US Bureau of Economic Analysis.

² Steven Hipple, "Self-Employment in the United States: An Update." *Monthly Labor Review*, US Department of Labor, July 2004.

The demographic characteristics of self-employed workers are well-documented for the nation as a whole. Self-employment rates are higher for men than for women, and higher among whites than among blacks, Hispanics and Asians.³ Overall, native-born workers are more likely to be self-employed than the foreign born, although foreign-born citizens of the U.S. have higher rates of self-employment than native-born citizens. Among all groups the rate increases with age. More than one-third of working men aged 65 or older are self-employed. The self-employment rate also increases with educational attainment: 19 percent of men and 11 percent of women with advanced degrees are self-employed.⁴

Several economists have studied self-employment in recent years. Robert Farlie and Bruce Meyer found that since 1970, declining rates of male self-employment within industries have been counterbalanced by more rapid growth in industries in which self-employment is common.⁵ Finance, professional and business services, and construction are industries in which self-employment rates are relatively high.

Ellen Rissman of the Federal Reserve Bank of Chicago, along with her colleagues Daniel Aaronson and Daniel Sullivan, have analyzed how self-employment varies with the condition of the economy.⁶ They argue that self-employment is counter-cyclical; workers enter self-employment when the labor market is slack and attractive wage and salary job openings are scarce. Their econometric analysis indicates that a 40 percent increase in a state's unemployment rate increases the state's unincorporated self-employment rate by .08 to .13 percentage points.

Rissman also used data from the National Longitudinal Survey of Youth to follow a panel of 6,175 men over the period 1979-2002. She found that over one-quarter of those who ever worked spent some time self-employed, but for most self-employment was a transitory state. From one year to the next, about 35 percent of the self-employed men left self-employment for wage work. She also found that many first spells of self-employment end within a year, but that the longer a worker has been self-employed, the less likely he is to leave self-employment. Somewhat contradictorily, she found that strong growth in national GDP encourages workers to exit self-

employment for wage work, but so does a rising local unemployment rate.⁷

It is not clear that self-employment in New York City follows a cyclical pattern. Over the past 30 years, changes in the number of self-employed workers display a weak positive correlation with changes in real gross domestic product and a weak negative correlation with the local unemployment rate. Such patterns suggest that self-employment in the City is, if anything, somewhat encouraged by growth in the national and local economies.

Notwithstanding large annual fluctuations in the rate of increase, the number of self-employment jobs has grown dramatically. The number of self-employed workers in the City hit a low-point in 1976, and since then has grown at an average annual rate of 3.3 percent. According to the BEA, the City had 720,000 self-employed workers in 2004, an increase of 430,000 since 1976. Wage and salary jobs increased by only 230,000 during the same period, so the proportion of all City jobs represented by self-employment rose from 8 to 16 percent.

Self-Employment Job Niches

Since the vast majority of the self-employed employ no paid workers of their own,⁸ data on "non-employer" firms compiled by the Census Bureau can be used to gain insight into the activities of self-employed workers. The data are tabulated from IRS records and represent principally sole proprietorship businesses reported on Schedule C of form 1040 for individuals' federal income tax returns. They are supplemented with data from partnership and corporate tax returns that report no paid employees. Some filers reporting Schedule C income may have other sources of income, including full-time or part-time wage jobs, so these data are not entirely comparable to the figures cited above. Nevertheless, they show similar trends and are considered highly accurate.

The Census Bureau's figures on non-employer businesses show 677,000 in New York City in 2004 (the last year for which data are available), compared to the 720,000 self-employed reported in the BEA's series.⁹ Considering the definitional differences, these are highly compatible figures. Moreover, between 1997 and 2004, the two series show a nearly identical rate of increase.

³ Self-employment rates are defined as the proportion of all employed people who are self-employed.

⁴ Hipple, "Self-employment in the United States."

⁵ Robert W. Farlie and Bruce D. Meyer, "Trends in Self-Employment Among White and Black Men During the Twentieth Century," *Journal of Human Resources*, Fall 2000.

⁶ Daniel Aaronson, Ellen Rissman, and Daniel Sullivan, "Assessing the jobless recovery," *Economic Perspectives*, Federal Reserve Bank of Chicago, 2Q/2004.

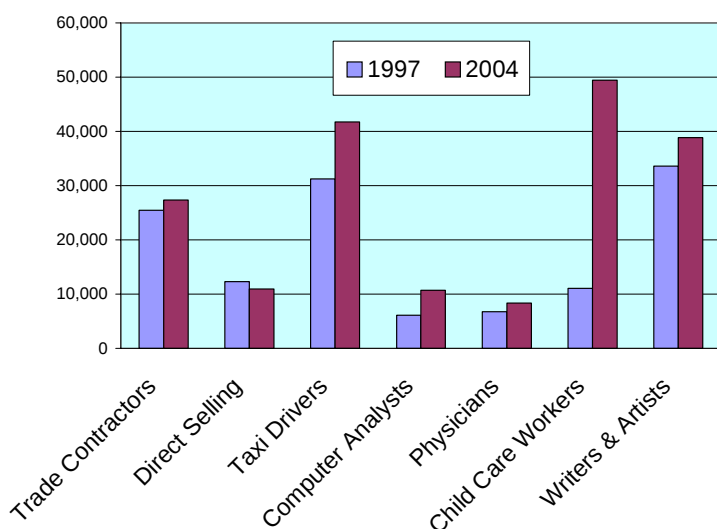
⁷ Ellen Rissman, "The self-employment duration of younger men over the business cycle," *Economic Perspectives*, Federal Reserve Bank of Chicago, 3Q/2006.

⁸ Nationally, over 80 percent of the unincorporated self-employed employ no paid workers.

⁹ Census Bureau data on non-employer businesses are geographically coded according to the mailing address on the Schedule C form. For most non-employer businesses, that is identical to the filer's home address.

Until recently, Professional, Technical and Scientific services workers represented the largest group of (non-employer) self-employed workers. The category includes some professions such as law, accounting and architecture, which traditionally have had a high rate of self-employment. It also includes a variety of consultants in management, engineering, computer systems, landscaping, design, advertising, and related fields, as well as photographers and veterinarians. The number of self-employed in the traditional professions has been increasing at a steady rate. For example, the number of self-employed vendors of legal services (with no paid employees) has been growing at about 1.8 percent per year, while the number providing accounting services has been growing at 2.5 percent annually.

Chart 2: Number of NYC Non-Employer Businesses, Selected Occupations, 1997-2004



Source: Census Bureau

There also are many self-employed engaged in traditional trades. For example, 27,341 non-employer specialty trade construction contractors filed tax forms in 2004, up from 25,483 in 1997. These self-employed contractors include plumbers, electricians, painters and a host of other tradespersons. A strong housing market and a surge in home alterations allowed this group of independent contractors to increase their average receipts by nearly 50 percent between 1997 and 2004.

Growth in traditional trades and professions has been overshadowed by that in fields associated with information and technology. One of the fastest growing categories of self-employed workers is providers of computer systems services, including software design and systems maintenance. In 2004, there were 10,704 such self-employed consultants in the City, a 76- percent increase from 1997. Their average reported income from such independent employment was \$35,900. Likewise,

the number employed in information industries, including traditional and internet publishing, broadcasting, and motion pictures and video services, increased from 8,745 in 1997 to 15,508 in 2004. On average, they reported earnings of about \$38,000 in 2004.

The arts is another field where self-employment has long been common. Nationally, the rate of self-employment for artists and musicians is 47 percent, and for writers and authors, 43 percent. In 2004, 38,810 independent writers, artists and musicians reported business profits or losses in the City, an increase of over 5,000 from 1997. They earned, on average, \$34,000 from such activities. The fastest growth in non-employer businesses, however, has not been in the technology or creative sectors. Rather, it has come in personal service occupations, the demand for which reflects the changing demographics and lifestyles of the City's population. For example, the number of home health care workers increased by 130 percent, to 7,688, between 1997 and 2004. Even more remarkable was the growth in the number of self-employed child care workers, which soared from 11,085 to 49,393. During that same time, the number of wage and salary child care workers also increased, from 17,500 to 22,600.

Who Are The Self-Employed?

The diversity of job categories in which the self-employed are represented suggests that the demographic profile of the City's self-employed workforce is equally diverse. The Census Bureau's 2005 American Community Survey, which provides a one-percent sample of the City's population, permits us to construct a general profile of self-employed New Yorkers.

Self-employment patterns in the City parallel those of the nation in many respects. Men are more likely to be self-employed than women, and self-employment rates tend to increase with age. Men comprise 53 percent of the City's resident workforce, but 65 percent of the self-employed workforce. The self-employment rate for working New Yorkers rises from 3 percent for those under 25 years old to 22 percent for those 65 and older. The rate for workers in the peak earning ages of 45-64 is about 14 percent.

Immigrants (including naturalized citizens) appear to be more likely to be self-employed than New Yorkers born in the U.S., although the difference is slight. Nevertheless, it appears to be true for each age group except those 65 or older.

The U.S.-born self-employed workforce has attained higher levels of formal education than the U.S.-born wage and salary workforce. About 63 percent of U.S.-born self-

employed workers residing in the City have four years of college or more, compared to 44 percent of U.S.-born wage and salary workers. Almost 30 percent have graduate or professional degrees, compared to 18 percent of employees. These educational differences reflect the heavy concentration of U.S.-born self-employed in the professions, in information industries, and in the arts.

In contrast, there is little difference in the educational attainment of foreign-born self-employed workers and foreign-born wage and salary workers. In both cases about half have some college background and a third have four or more years of college education. Interestingly, foreign-born residents who hold graduate or professional degrees are less likely to be self-employed than are their U.S.-born counterparts. This may be due to immigration laws, or to a greater preference for the security of salaried employment among first-generation immigrants.

Table 1: Profile of NYC's Self-Employed Workforce

	Self-Employed	Wage & Salary
Male	64.6%	51.5%
Female	35.4%	48.5%
Less than 45 years old	47.8%	63.8%
65 years old or over	6.7%	3.8%
Foreign born	49.8%	45.8%
4+ years of college	48.0%	37.7%
Graduate or prof. Degree	21.5%	15.0%
Works at home	20.7%	1.3%
Mean personal earnings	\$59,390	\$47,669
Median personal earnings	\$30,560	\$33,616
Mean household earnings	\$108,722	\$90,241
Median household earnings	\$70,288	\$67,028

Source: NYC Comptroller from ACS microdata

The average self-employed worker in the City earns more than the average wage and salary worker. Our tabulations of ACS data indicate self-employed workers earned, on average, \$59,400 in 2004, compared to \$47,700 for wage and salary workers. However, the dispersion of incomes is much wider among the self-employed. A greater proportion earn under \$25,000 annually and over \$75,000 annually than do wage and salary workers. Their median earnings are about \$5,000 lower.

Nevertheless, the households of self-employed workers have a median total income slightly greater than the households of wage and salary workers, and an average income significantly greater. In part, that is because of the higher average earnings of self-employed workers.

While self-employed workers appear to be somewhat less likely to live in households in which there are other earners, when they do, their spouses or partners appear to earn significantly more, on average, than the spouses and partners of wage and salary workers.

Even a survey as large as the ACS doesn't provide enough observations to draw reliable conclusions about the economic well-being of self-employed workers in specific occupations compared to their wage and salary counterparts. However, there are several occupations that provide sample sizes large enough to observe general patterns. Among attorneys, for example, the median earnings of the self-employed is lower than of those who are salaried, but the earnings dispersion is wider. More of the self-employed attorneys earn over \$100,000 annually. They are significantly older on average than salaried attorneys and work fewer hours.

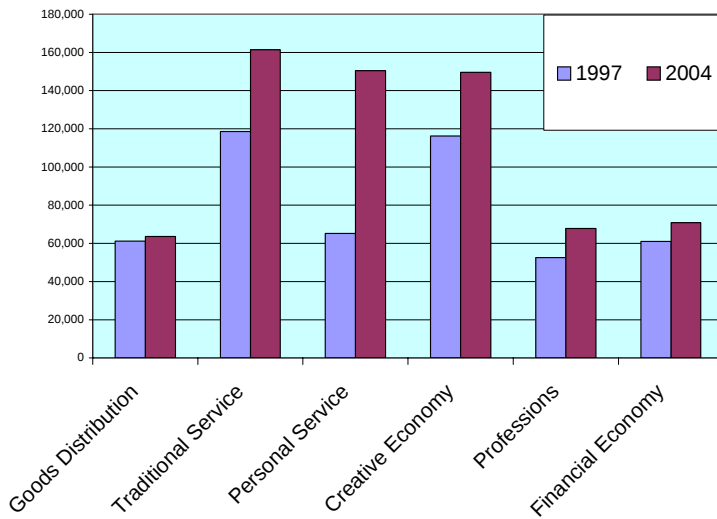
At the other end of the income spectrum are child care workers. Self-employed child care workers report, on average, lower earnings and more hours worked per week than their wage and salary counterparts. However, approximately half of the self-employed work at home, and that may be a convenience that offers transportation savings and non-monetary advantages.

New Economy, New Risks

There appear to be several factors driving the rapid increase in the self-employed workforce in New York City. Clearly, industries and occupations in which self-employment is more common have been growing faster than the overall job base. As the City's economy has become more geared to finance and real estate, the ranks of independent providers of legal services, accounting services and other professional services have grown. The information and technology sectors have also contributed to the trend, and some of today's self-employed computer systems consultants and web-based publishers may become tomorrow's growth firms. Those who worry that the City is becoming too dependent on finance and business services can take heart that the number of independent writers, artists and musicians has been growing rapidly as well.

Despite the steady growth in self-employment in the professional, technology, and creative sectors, it has been overshadowed by the startling increases in self-employed personal service workers and other lesser-paying occupations. In many cases, those modest-paying jobs provide families an important cushion between decent living conditions and poverty. For example, while self-employed child care workers earn, on average, only \$13,500 annually, they live in households that earn an average of \$50,000 per year. That indicates that many such workers are second earners whose income is vital to the family's well-being.

Chart 3: Growth of NYC Non-Employer Business By Sector, 1997-2004



Source: Census Bureau; NYC Comptroller

While rapidly growing demand for personal service workers provides welcome job opportunities for underemployed groups, it may also reflect a growing income polarization within the City. If demand is strong enough it may eventually boost the relative earnings of personal service workers and thereby reduce household income inequality, but thus far there is little evidence of that happening.

Moreover, some of the growth in self-employment, among service workers, tradespersons, and professionals alike, may be due to a reluctance of employers to absorb the costs of employee health care and other fringe benefits. The number of self-employed taxi and limousine drivers, for example, increased from 31,000 in 1997 to 41,700 in 2004. That increase is largely attributable to the continued shift away from paid taxi fleet drivers to leased fleets, whereby the independent driver assumes much of the business risk, as well as the costs of health insurance, retirement savings and the like. A similar shift may be going on in other industries, as firms find it more economical to rely on independent contractors than on in-house staff to provide certain services.

Almost 60 percent of self-employed New Yorkers have at least one other earner in the household, so many of them presumably obtain health insurance coverage through a spouse or partner. In fact, access to such family coverage may enable some workers who wish to form a business or forge a freelance career to exit wage and salary work to begin with. However, almost two-thirds of the self-employed who live in households with no other earners have total incomes under \$50,000, and for those independent workers it may be very difficult to obtain affordable health coverage. Moreover, publicly provided

disability insurance and unemployment insurance programs do not cover self-employed workers. For these reasons, as well as the inherent volatility of self-employment income, the trend toward self-employment may augur an economy in which the financial security of the typical family is diminishing.

Those concerns notwithstanding, there are positives to self-employment. Many people enjoy the independence associated with self-employment and are challenged by the prospects of entrepreneurial success. From the City's viewpoint, the economic vitality and creative energy provided by its rapidly growing, self-employed workforce should be cultivated. Public policy, however, needs to take account of the growing risks and family vulnerabilities associated with an increasingly independent workforce.