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**Inter-Departmental Memo**

To: Hon. Lisanne Altmann, Chairperson  
Members of the Budget Review Committee

From: Eric C. Naughton, Director  
Legislative Budget Review

A handwritten signature in black ink, appearing to be "EN", written over the printed name of Eric C. Naughton.

Date: July 20, 2007

Re: Second Quarter 2007 Regional Economic Forecast

Attached is a copy of the Office of Legislative Budget Review's Second Quarter 2007 Regional Economic Forecast. This report is intended to assist the Legislature in making policy decisions and in assessing budgetary forecasts. The data presented are the most current as of the date of circulation and are the most geographically relevant.

cc: Hon. Howard Weitzman, County Comptroller  
Mark Young, Budget Director  
Evan Cohen, Acting Executive Director, NIFA  
Dan McCloy, Special Assistant Minority  
Tom Stokes, Deputy County Executive  
Roseann D'Alleva, Majority Finance  
Fran Evans, Director of Policy



# SECOND QUARTER 2007 REGIONAL ECONOMIC FORECAST

## NASSAU COUNTY OFFICE OF LEGISLATIVE BUDGET REVIEW

This report seeks to provide a forecast of several regional and national economic variables. The forecast should assist the County with its budgetary projections for several major revenue and expense categories. The forecast was obtained from Moody's Economy.com. Moody's Economy.com is a leading independent provider of economic, financial, country, and industry research. This report is arranged in six sections: personal consumption, consumer prices, residential housing, commercial real estate, employment and tourism. Each section provides a summary of the current conditions in that area, a forecast of where the variables in that area will end up in 2007 and a projection of the trends anticipated in 2008. In each section the connections between the economic variables and County revenue and expense categories will be highlighted.

### Quarterly Personal Consumption Forecast

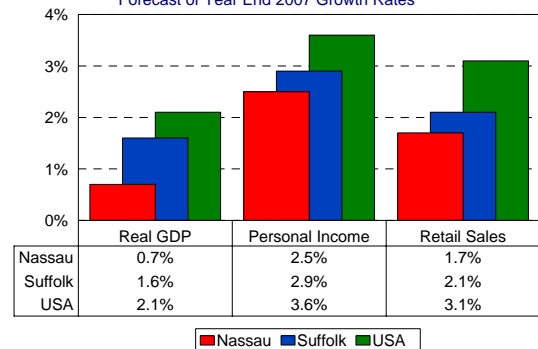
Currently, the economy is moving forward at a slow rate. According to the Commerce Department, first quarter national real gross domestic product, GDP, was 0.7%. Consumers have been credited with keeping the economy afloat since business spending has been cautious.<sup>1</sup> The Federal Reserve is expecting economic growth to expand at a moderate pace

over the second half of 2007 and continue to strengthen in 2008. They are projecting year-end 2007 real GDP growth to be in the 2.25% to 2.5% range and annual 2008 real GDP growth to be in the 2.5% to 2.75% range.<sup>2</sup>

Regionally, Moody's is forecasting Nassau real GDP to rise an additional 0.7% through the rest of 2007. In 2008, Moody's is expecting Nassau County real GDP to expand 1.3%, slightly above Moody's 2007 annual real GDP forecast of 0.9%. Suffolk is forecast to experience stronger economic growth both for the rest of 2007 and in 2008. Chart 1 details the previously discussed growth rates.

**Chart 1**

**Consumption Indicators**  
Forecast of Year End 2007 Growth Rates



Source: Moody's Economy.com

<sup>1</sup> Aversa, Jeannine, "Economic Growth Slows to 0.7 Pct. Pace", [Newsday.com](http://www.newsday.com), June 28, 2007.

<sup>2</sup> "Bernanke Says Economy to Gain Steam", [CNN/Money.com](http://www.cnn.com), July 18, 2007.

Several factors may be seen as contributing to the projection of Nassau's sluggish economic growth. Although Nassau is expected to experience a 2.5% increase in personal income, which will enable retail sales to grow 1.7%, when consumer price increases are factored in, real personal income is projected to be flat throughout the remainder of 2007. Moreover, housing wealth and employment gains will not contribute to Nassau's economic growth since both are forecast to decrease through the remainder of 2007.

The sluggish economic growth rates may be seen as contributing to the slow growth rates recorded in Nassau's sales tax collections. Year to date, Nassau County has collected \$451.0 million in sales tax. That represents an increase of 1.9% compared to this time last year.

Retail sales have historically represented 63.0% of Nassau County sales tax collections, projected Nassau County retail sales may be used as a gauge for future County sales tax collections. Since individuals require income to make purchases, as personal income grows so should County sales tax collections.

According to the forecast, all areas surveyed will record marginal, positive growth through the end of 2007 in retail sales and personal income. The nation is forecast to experience stronger real GDP, personal income and retail sales growth than that seen throughout the region.

### **Outlook for Consumer Prices**

Through May 2007, regional consumer prices have risen 2.5% and national consumer prices have escalated 2.7%. Medical, Housing, Education and Food costs propelled the all-items index up. The recent focus on gas prices remaining above \$3.00 a gallon has diverted attention away from the recent appreciation seen in food prices. Throughout the metropolitan region in May 2007 gasoline

prices fell 0.3% from the prior year. Over the same time period, regional food prices have risen 4.2%. If current food price trends continue, experts expect national food prices to rise 7% in 2007.

While all food prices have risen, those connected to corn have experienced the greatest price appreciation. This is a result of the increasing demand for ethanol, a byproduct of corn. High corn prices push farmers to devote more acreage to corn, thereby leaving other crops in short supply. Additionally, higher labor, packaging and fuel costs have also contributed to the escalation seen in food prices. In some areas, inclement weather has resulted in price spikes for citrus fruits and some vegetables.

Agricultural economist Michael Swanson opines that there is no end in sight to food inflation. In fact the full extent of the wholesale price increase has not filtered down to the consumer yet. Until now, retail establishments have absorbed part of the wholesale price increase. More of the increase is expected to be passed onto the consumer in the future.<sup>3</sup> Additional international forces should result in continued, heightened food prices. Droughts in Australia and New Zealand coupled with lower food subsidies in the European Union will diminish global food supply. Simultaneously, greater personal income levels in the booming Asian countries will increase food demand globally.<sup>4</sup> Since food purchases are largely untaxed, this price escalation will not result in greater County sales tax collections.

Currently, Moody's is forecasting a 3.4% growth rate for annual 2007 regional consumer price escalation. Nationally, Moody's expects consumer prices to rise 3.3% in 2007. In 2008 they are expecting 2.0% regional consumer

<sup>3</sup> Mc Guire, Kara, "Consumers Feel the Heat from Rising Food Prices", [StarTribune.com](http://StarTribune.com), June 3, 2007.

<sup>4</sup> Cox, Jeff, "Corn and Milk: A 1-2 Inflation Combo", [CNN/Money.com](http://CNN/Money.com), June 19, 2007.

price growth and 2.1% national consumer price growth.

### Quarterly Residential Housing Forecast

Nassau’s residential housing market moved forward at a slow pace in April 2007. Using Multiple Listing Service of Long Island statistics, from an annual perspective, average closed sale prices increased 0.3% and median closed sale prices rose 0.81%. Inventory levels were up roughly 19% from the prior year and the number of closed transactions increased 0.97% from April 2006. The housing market slowdown will negatively impact County Clerk fee revenues, of which roughly 70% are attributable to housing market transactions.

By year-end, the region is expected to experience a decline in home prices, mortgage originations and mortgage refinancings. The declines are expected to continue throughout 2008. The forecast housing market decline is supported by recent Nassau County mortgage recording tax collections which year-to-date are down 8.3% compared to this time last year.

According to the PMI Mortgage Insurance Company, the Nassau-Suffolk region has a 44.5% chance that home prices will drop in the next two years. Table 1 records the risk score, which measures the chance that home prices will decline over the next two years, for the top 18 riskiest metropolitan regions.

“If [home] prices drop, consumers might trim spending by as much as 9¢ for each dollar of wealth lost.”

“Bernanke: Subprime Hit Could Top \$100B”, [CNN/Money.com](http://CNN/Money.com), July 19, 2007.

**Table 1**

	Metropolitan Statistical Area	Risk score
1	Riverside-San Bernardino-Ontario, Calif.	652
2	Phoenix-Mesa-Scottsdale, Ariz.	646
3	Las Vegas-Paradise, Nev.	614
4	West Palm Beach-Boca Raton-Boynton Beach, Fla.	607
5	Los Angeles-Long Beach-Glendale, Calif.	586
6	Santa Ana-Anaheim-Irvine, Calif.	577
7	Oakland-Fremont-Hayward, Calif.	572
8	Orlando-Kissimmee, Fla.	563
9	Sacramento-Arden-Arcade-Roseville, Calif.	560
10	San Diego-Carlsbad-San Marcos, Calif.	555
11	Fort Lauderdale-Pompano Beach-Deerfield Beach, Fla.	542
12	Miami-Miami Beach-Kendall, Fla.	524
13	Tampa-St. Petersburg-Clearwater, Fla.	506
14	Boston-Quincy, Mass.	501
15	Washington-Arlington-Alexandria, D.C.-Va.-Md.-W.Va.	500
16	San Jose-Sunnyvale-Santa Clara, Calif.	491
17	Virginia Beach-Norfolk-Newport News, Va.-N.C.	476
18	Nassau-Suffolk, N.Y.	445

Source: PMI Mortgage Insurance Co.

Moody’s has a similar forecast for Nassau’s residential housing market. They see mortgage originations declining 10.4%, mortgage refinancings falling 12.7% and home sale prices decreasing 3.7% over the remainder of 2007. In 2008 Nassau is projected to record a 5.3% decrease in originations, a 29.6% fall in refinancings and a 4.9% decline in home sale prices. Chart 2 depicts these projected growth rates.

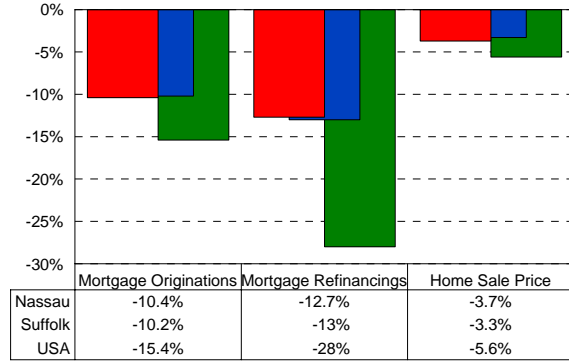
As mentioned previously, the forecasted declines will have an immediate and direct impact on Nassau County Clerk fee revenues which are closely aligned with mortgage refinancings and the number of closed transactions. The current housing slowdown is already impacting 2007 County Clerk fee revenues. OLBR is currently forecasting 2007 County Clerk fee revenue to come in at \$13.3 million, 4.7% million less than 2006 actual collections.

The forecasted mortgage refinancing decline is also expected to have an impact on County

sales tax collections. Residents have been utilizing their home equity to finance major purchases. As home equity declines individuals will make fewer purchases and the County will collect less sales tax revenue.

**Chart 2**

**Residential Housing Market Forecast**  
Forecast of Year End 2007 Growth Rates



Source: Moody's Economy.com

**Forecast for the Commercial Real Estate Market**

The Long Island office market is expected to be a source of strength for the regional economy for the remainder of 2007 and in 2008. According to Cushman & Wakefield second-quarter 2007 statistics, island-wide rental rates averaged \$30.94 per square foot. That represents a 1.8% increase from the first quarter 2007. The first quarter average rental rate of \$30.39, was the first time their index crossed the \$30 mark. According to Herb Agin, chief executive for Sutton & Edwards, a Long Island business real estate service organization, limited availability and barriers to new construction should keep rents rising steadily in Nassau and Suffolk.<sup>5</sup>

Contributing to the strong demand for regional office space is the fact that the Manhattan commercial real estate market continues to skyrocket. According to Kraig Silver, senior vice president with the Treeline Companies, "Long Island has gained a reputation as a leading alternative to Manhattan and the

<sup>5</sup> Wagner, Daniel, "Long Island Office Rents Rise in 2<sup>nd</sup> Quarter", [Newsday.com](#), July 3, 2007.

boroughs for top-tier office space attracting legal, finance, non-profit and other firms".<sup>6</sup> This trend towards eastward relocation is expected to continue. According to Bill Wilkes Jr, executive vice president with CLK/H-P, this is a noticeable trend which will continue as time goes on.<sup>7</sup>

**Quarterly Employment Forecast**

May 2007 was a negative month for employment growth. All areas surveyed witnessed annual declines in labor force and employment figures. On Long Island, the monthly increase in resident employment was not sufficient to eradicate the losses made over the prior twelve months. In New York City, resident employment fell from both a monthly and an annual perspective.

According to Moody's, the decline in resident employment is expected to continue throughout 2007 in Nassau. They are not projecting any resident employment growth for 2008 in Nassau County. Additionally, Moody's is expecting the number of unemployed Nassau residents to grow by 2.5% and the unemployment rate to average 3.8% for the remainder of 2007.

Suffolk County is forecast to lose fewer employed residents than Nassau. Suffolk is expected to shed 0.4% of its employed residents, to increase its unemployed residents by 3.0% and to record an average unemployment rate of roughly 4.0% for the remainder of 2007.

Chart 3 details the projected changes in the number of employed residents for the remainder of 2007 and in 2008.

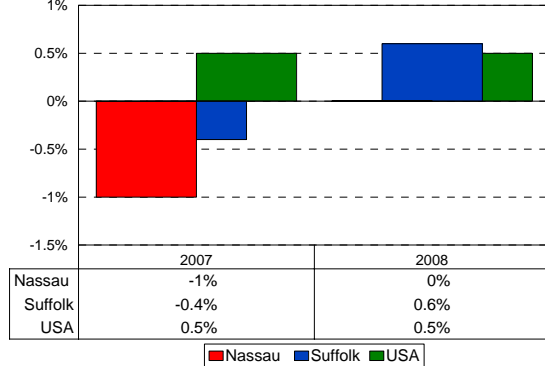
<sup>6</sup> Wagner, Daniel, "New York City Rents Pushing Offices to Long Island", [Newsday.com](#), July 17, 2007.

<sup>7</sup> Same as above.

**Chart 3**

**Resident Employment Indicators**

Forecast of Year End 2007 and Annual 2008 Growth Rates



Source: Moody's Economy.com

On the job front, the May 2007 non-agricultural employment figures reveal positive growth. The region saw an influx of 13,900 jobs from a monthly perspective and 8,500 jobs from an annual perspective. The monthly job growth was sufficient to enable the region to meet the 1.0% mark indicative of a healthy economy. The healthy job growth was well-diversified with nine of the twelve industries surveyed experiencing positive monthly job growth. Annually, ten of the twelve sectors surveyed recorded positive job growth.

Looking forward, the non-agricultural employment figures for the Long Island region should remain positive, with slow growth rates. According to Manpower's most recent hiring survey, 58.0% of employers in the US have no plan to change their hiring pace. Moreover, in the Northeast, only 27.0% of employers expect to add workers at a faster rate.<sup>8</sup>

**Forecast for the Tourism Industry**

Nassau's lodging/tourism industry has been and is expected to continue to be a source of strength for the regional economy. May 2007 occupancy rates rose 7.4% from May 2006. The occupancy rate increase is indicative of robust demand since the increase was accomplished alongside an increase in rental rates and room supply. May 2007 average

rental rates were up 3.0% from the prior month and 3.2% from the prior year. Moreover, the Long Island region has absorbed 20 new hotels since 1999.

Looking forward, Governor Eliot Spitzer announced plans to expand the "I Love New York" tourism campaign. This investment is not expected to generate immediate heightened demand on Long Island, but it is forecast to raise future occupancy levels. According to Moke McGowan, President of the Long Island Convention and Visitors Bureau, strengthening State-wide tourism will eventually benefit Long Island. However, the increased demand may not be sufficient to keep pace with current hotel inventory expansion. According to Mr. McGowan, tourism demand is growing 3 to 5 percent, but 10 percent is needed to keep pace with the hotel rooms that Long Island is producing.<sup>9</sup>

**Conclusion**

The Long Island economy appears to be stagnating. For the remainder of 2007 and throughout 2008, the region is forecast to experience negative real income growth, declining home sale prices, and no growth in resident employment. Only the commercial real estate and lodging industries can expect to witness positive growth. From a County fiscal perspective, this economic forecast implies that it would be prudent for the County to be conservative with the growth rates that it budgets for 2008 sales tax and County Clerk fee revenues.

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<sup>8</sup> "Employers Cautious on Summer Hiring", [CNN/Money.com](http://CNN/Money.com), June 12, 2007.

<sup>9</sup> Wagner, Daniel, "LI Tourism Chief Details Plans", [Newsday.com](http://Newsday.com), June 18, 2007.