

LIA Monthly Economic Report

A Research Report for Directors and Members of the Long Island Association, Inc.

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Consumer spending was robust in July, fueled by a labor market that continues to expand. Business activity declined slightly from the previous month, but remained in positive territory. Both, consumer and producer price indexes remained low and average hourly earnings exceeded inflation.

But some have argued that uncertainty continues to hang over the economy like a dark cloud. Whether and to what extent this is true will have important implications for financial markets and the real economy. This issue is addressed more fully in the *Focus On* section of this report.

The National Economy



The labor market rebounded strongly in July. Average hourly earnings rose by 3.2 percent year-over-year and the July unemployment rate remained low at 3.7 percent. There were just 209,000 jobless claims during the week ending August 17th, a number consistent with strong growth in the labor market.

The manufacturing sector again declined modestly compared to the previous month according to the Institute for Supply Management's (ISM) Manufacturing Survey. However, it remained at a level consistent with expansion. The ISM Non-manufacturing Survey also declined slightly from the previous month.

Inflation remained well in check. The Consumer Price Index rose by 2.2 percent year-over-year in July while the Producer Price Index grew by a modest 1.7 percent.

Retail sales rose at a robust pace of 0.7 percent in July, well in excess of expectations. Although, consumer confidence declined slightly in August, it exceeded expectations and remained at a high level. July durable goods orders rose by 2.1 percent, well in excess of expectations.

Existing home sales rose in July but new home sales declined.

The stock market remained choppy, possibly the result of uncertainty over a trade war with China and growing concerns of a global economic slowdown.

The Long Island Economy

Labor Market



Long Island's labor market continued its extended run. The July unemployment rate was 3.6 percent, the lowest rate for July in almost 20 years. However, both labor force participation and the number of persons employed declined compared to the previous year. When people leave the labor force, they are no longer counted as unemployed.

Long Island's private sector job count increased by 2,500 between June and July, compared to an average loss of 4,500. Hiring in the leisure and hospitality sector hit record highs for the second consecutive month. In July, strength was concentrated in arts, entertainment, and recreation which added 6,900 jobs, more than double the average gain of 3,400.

The largest year-over-year jobs gains in July were in:

- Education and Health Services (+8,600)
- Natural Resources, Mining and Construction (+8,500)
- Leisure and Hospitality (+3,900)

Wage growth increased at a relatively sluggish pace in July.

In New York State, private sector hourly earnings rose by 2.0 percent year-over-year in July.

The largest gains were seen in:

- Other Services (+4.9%)
- Trade, Transportation and Utilities (+4.3%)
- Leisure and Hospitality (+4.3%)

The continued strong growth in leisure and hospitality wages is a positive sign for the tourism season.

Business Conditions



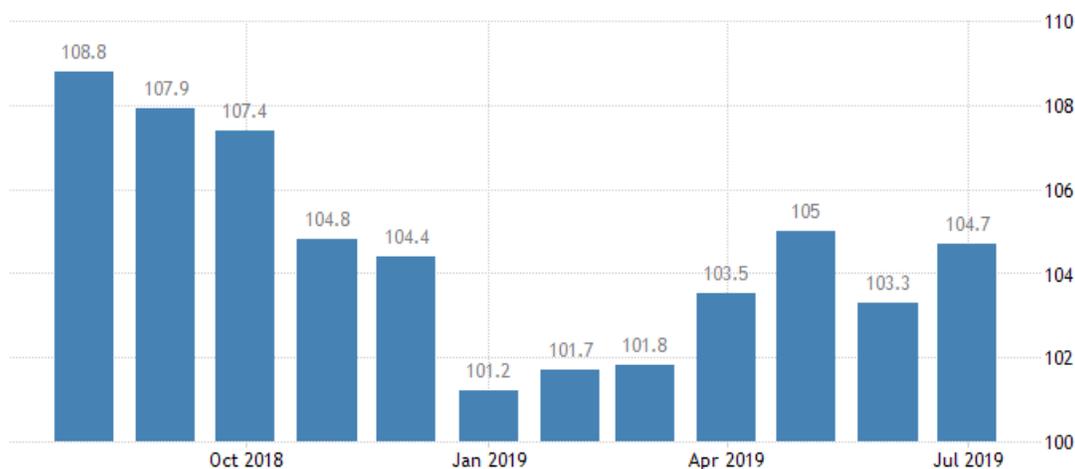
With small businesses comprising almost 90 percent of commercial establishments on Long Island, this is a key sector for economic growth.

The NFIB Small Business Optimism Index remained in positive territory, rising by 1.4 points from the previous month to 104.7 in

July 2019, Expectations for better business conditions rose by five points while those reporting the current period as a good time to expand increased by two points. The percent of owners who anticipate higher sales volumes rose five points, to 22 percent of owners. Additionally, plans to create new jobs and make capital outlays increased and earnings trends improved, supported by a solid improvement in sales trends. So the overall picture for small business is favorable.

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NFIB Small Business Optimism Index



SOURCE: TRADINGECONOMICS.COM | NATIONAL FEDERATION OF INDEPENDENT BUSINESS

Business activity showed modest improvement, according to firms responding to the August 2019 Empire State Manufacturing Survey. New orders increased after declining for the prior two months, and shipments continued to expand. Still, as may be seen in the chart below, growth in manufacturing has been slower relative to the fall of 2018.

Empire State Manufacturing Survey



Activity in the region’s service sector continued to expand, according to firms responding to the Federal Reserve Bank of New York’s August 2019 Business Leaders Survey. The business climate index held slightly above zero, indicating that on balance, firms regarded the business climate as better than normal.

Consumer Sector



Consumer spending, as indicated by sales tax collections, rose by 3.18 percent in Nassau County. Spending rose more rapidly in Suffolk County, increasing by 5.18 percent. Given the increase in Internet sales over time, these year-over-year sales tax revenue comparisons may understate actual consumer spending because proportionately fewer purchases incur local sales taxes in later years. Adjusting for this change, estimated year-over-year spending may have risen by 4.14 percent in Nassau County and by 5.14 percent in Suffolk.

Residential Real Estate



The real estate sector continued its sluggish performance. In Nassau County, July prices rose from \$537,000 in 2018 to \$546,400, an increase of just 1.7 percent. And sales declined from 1,302 to 1,258 units sold, a drop of 3.4 percent. Suffolk County fared somewhat better. July prices rose by 6.7 percent year-over-year, from \$390,000 to \$416,000. But sales rose only modestly, from 1,630 to 1,660 units sold, an increase of 1.8 percent.

The total number of Long Island residential inventory in July 2019 was 19,144 representing an 8.1% increase over last year.

Commercial Real Estate – Office Space



The Long Island office market is comprised of 43.2 million square feet in five geographic concentrations ranging in size from the 10.4 million square foot East Nassau submarket to the Southwest Nassau submarket, which accounts for 7.1 million square feet. In the ten-year period beginning with the third quarter of 2009, the Northwest Nassau submarket has experienced the greatest introduction of new inventory, 233,000 square feet, amounting to 50.2% of all new competitive stock added to the market.

The average vacancy rate for office space on Long Island is the 10th lowest among metropolitan areas national and the fourth lowest in the Northeast Census Region. The mean vacancy rate as of July was 13.5 percent, with a range of 0.0 to 60.6 percent.

VACANCY RATES – Office Space

Low	25 th Percentile	Mean	75 th Percentile	High
0.0%	3.7%	13.5%	18.1%	60.6%

As of July 2019. Source: Reis Reports: www.reisreports.com.

The mean asking rent was \$27.58 per square foot as of July. This varied from a low of \$16.75 to a high of \$39.12.

ASKING RENTS – Office Space

Low	25 th Percentile	Mean	75 th Percentile	High
\$16.75	\$23.80	\$27.58	\$33.00	\$39.12

As of July 2019. Source: Reis Reports: www.reisreports.com.

Long Island's Economic Outlook



While the labor market remained quite strong in terms of jobs, wage growth appears to have decelerated. Business activity continued to expand, but at a slower pace than in previous months. The overall economy still appears to be robust, but is showing signs of weakening. Is growing uncertainty a cause of this apparent slow down. This issue is discussed more fully in the *Focus On* section of this report.

Focus On... The Uncertainty Principle in Economics

Consumers, investors, and business owners make decisions in a world of uncertainty. And as in physics, economics has its own *uncertainty principle*. This is not to be confused with Heisenberg's uncertainty principle that measuring one variable more precisely leads one to measure a related variable less precisely. But it is just as powerful in its own way.

In economics, the uncertainty principle may be stated as: *uncertainty causes stagnation*. Nobel Laureate Professor Paul Krugman illustrated this well in a recent *New York Times* article. He argued for example that uncertainty over trade policy is causing more harm to the economy than the actual effects of the trade policy itself.

So, what is the evidence on trends in uncertainty? A convenient real-time measure of uncertainty is the so-called Volatility Index or VIX. The VIX is a quantitative measure of the market's expectations for future volatility that is calculated from the prices of options on the S&P 500 index. It is an estimate of variability in the S&P 500. Higher values of this index indicate greater uncertainty.

The table below shows the annual average value of the VIX since 2000 (see column 2). Columns 3 and 4 show, respectively, the actual volatility in the S&P 500 index and the average difference between the VIX and the S&P measures. Casual inspection reveals that the year-to-date value for the VIX is well in line with historical norms and certainly not on the high side.

YEAR	AVERAGE VIX LEVEL	AVERAGE OF S&P 500 21-DAY REALIZED VOLATILITY (%)	AVERAGE IMPLIED/REALIZED VOLATILITY SPREAD
2000	23.32	21.16	2.16
2001	25.75	20.95	4.80
2002	27.29	24.41	2.88
2003	21.98	16.75	5.24
2004	15.48	11.04	4.44
2005	12.81	10.12	2.68
2006	12.81	9.80	3.01
2007	17.54	14.71	2.82
2008	32.69	34.43	-1.73
2009	31.48	25.97	5.51
2010	22.55	16.97	5.58
2011	24.20	20.46	3.75
2012	17.80	12.68	5.12
2013	14.23	11.04	3.19
2014	14.18	10.54	3.63
2015	16.67	14.64	2.03
2016	15.83	12.43	3.40
2017	11.09	6.66	4.43
2018	16.64	14.37	2.27
YTD 2019	15.78	13.32	2.46

Source: S&P Dow Jones Indices LLC, Bloomberg. Data as of Aug. 22, 2019. Past performance is no guarantee of future results. Table is provided for illustrative purposes.

Some have nevertheless argued that uncertainty is rising and over brief periods of time, one may find some evidence of this. But, even then, the recent spikes in the VIX are just not unusually high. And even if this does signal an increase in uncertainty, it is certainly at an early stage. And that means there is ample time for policymakers to tame uncertainty, most importantly perhaps by ending the trade war. Or at least by providing consistent guidance on what will happen going forward with tariffs.

The greater problem may be the *perception* that uncertainty is increasing, even though it is not high by historical standards. And by objective measures of uncertainty such as the VIX, there is little evidence that *actual* uncertainty is rising. In this view, it may be the case that we have nothing to fear but fear itself.