February 26, 2007

Dear Colleagues:

I am pleased to provide you with the New York State Assembly Ways and Means Committee's Economic Report for 2007. This report continues our commitment to providing clear and accurate information to the public by offering complete and detailed assessments of the national and State economies.

The Ways and Means Committee staff's assessments and projections presented in this report are reviewed by an independent panel of economists, including professionals from major financial corporations and universities, as well as respected private forecasters.

Assembly Speaker Sheldon Silver and I would like to express our appreciation to the members of this Board of Economic Advisors. Their dedication and expert judgment continue to be invaluable in helping to refine and improve our forecasts. While they have served to make the work of our staff the best in the State, they are not responsible for the numbers of views express in this document.

I wish to also acknowledge the dedicated and talented staff of the Assembly Ways and Means Committee and the many hours of work that went into producing this report. They play a vital role in our State's budget process.

As we continue our efforts toward enacting a timely budget that is fair and equitable for all New Yorkers, I look forward to working with each of you.

Sincerely,

Herman D. Farrell, Jr.
Chairman

NEW YORK STATE

ECONOMIC REPORT

February 2007

Sheldon Silver
Speaker
New York State Assembly

Herman D. Farrell, Jr.
Chairman
Assembly Ways and Means Committee

Prepared by the
Assembly Ways and Means Committee Staff

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EXECUTIVE SUMMARY

United States

- The NYS Assembly Ways and Means Committee staff forecast for ***overall national economic growth in 2007*** is 2.6 percent.

- The NYS Assembly Ways and Means Committee staff forecast for ***overall national economic growth in 2008*** is 3.1 percent.

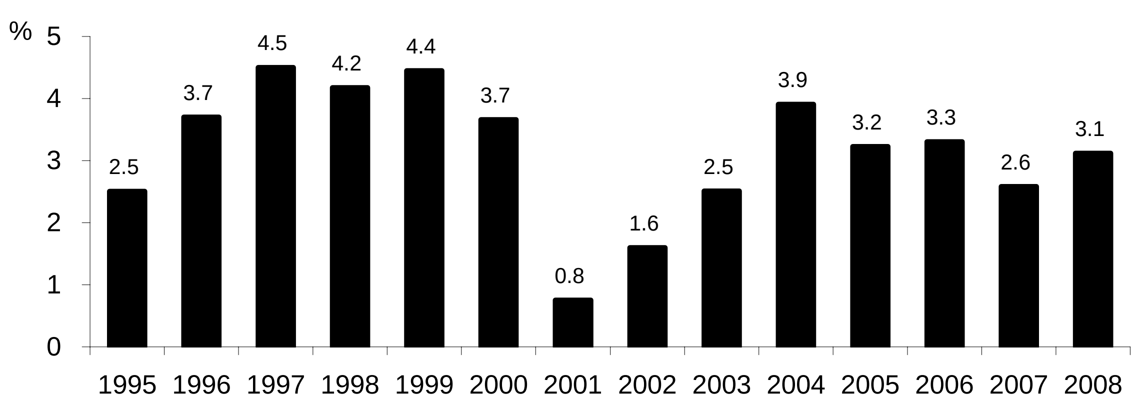
U.S. Real GDP Forecast Comparison
(Percent Change)

	Actual 2005	Estimate 2006	Forecast 2007	Forecast 2008
Ways and Means	3.2	3.3	2.6	3.1
Blue Chip Consensus	3.2	3.4	2.7	3.0
Division of the Budget	3.2	3.3	2.4	3.0
Moody's Economy.com	3.2	3.4	2.7	3.2
Macroeconomic Advisers	3.2	3.4	2.8	3.2
Global Insight	3.2	3.4	2.7	3.0

Sources: NYS Assembly Ways and Means Committee staff; Blue Chip, February 2007; New York State Financial Plan Projections, 2007-08 Executive Budget Supplemented for 21-Day Amendments, 2006-07 through 2010-11, February 21, 2007; Moody's Economy.com, February 2007; Global Insight, February 2007; Macroeconomic Advisers, February 2007.

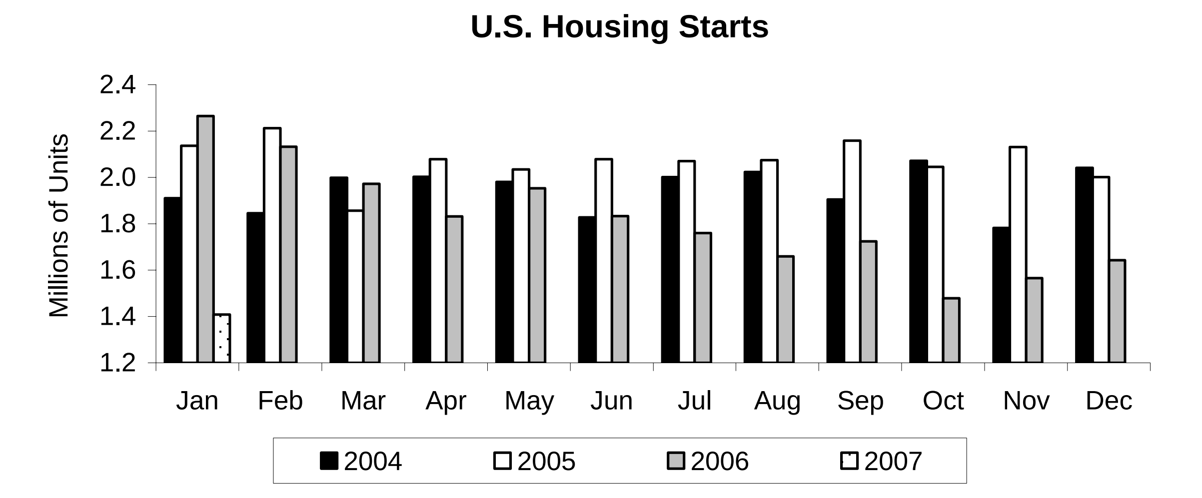
- The ***national economy***, as measured by real Gross Domestic Product (GDP), grew an estimated 3.3 percent in 2006, after growing 3.2 percent in 2005. It was the fifth consecutive yearly expansion since the end of the 2001 recession.

U.S. Real GDP Growth



Note: Data for 2006 is estimated; 2007 and 2008 are forecasts.
Sources: Bureau of Economic Analysis; NYS Assembly Ways and Means Committee staff.

➢ After surging 5.6 percent (annualized) in the first quarter of 2006, the economy has shifted into low gear, growing on average an estimated 2.2 percent per quarter during the rest of 2006. A ***sharp decline in residential construction activity*** and a slowdown in personal consumption spending growth were responsible for this recent slowdown in overall economic growth.

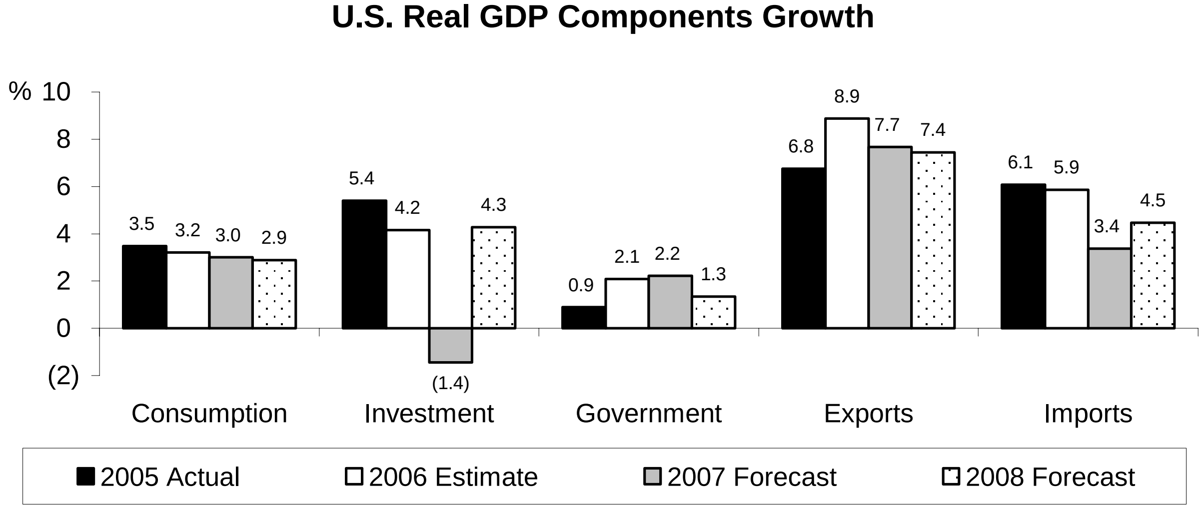


Source: U.S.Census Bureau.

➢ ***Overall economic growth*** will likely continue to soften throughout 2007, but the national economy is unlikely to slip into a recession. This optimism is based on the belief that the recent as well as near-future slowdown is a result of a shift in the sources of growth rather than the deterioration in a whole array of economic fundamentals. It appears that further growth of the economy will be powered more by business capital spending and net exports than by homebuilding and consumption financed by borrowing (including refinancing).

➢ ***Personal consumption spending*** is expected to continue to be helped by a steady increase in personal income. Employment gains, though remaining on a lower track than in previous recoveries, as well as healthier gains in hourly compensation are expected to continue to support personal income growth throughout 2008. With energy prices expected to stabilize at their current rate, this will also help sustain the consumer's purchasing power.

➢ There are factors that may negatively affect consumer spending. Housing market activity is expected to continue to decline throughout 2007. This implies that cash flow from refinancing will drop significantly, restraining overall consumer spending. In particular, outlays on consumer goods and services by lower and lower-middle income households will likely soften significantly.



Sources: Bureau of Economic Analysis; NYS Assembly Ways and Means Committee staff.

- ***Private investment spending*** will also slow in 2007, due mainly to continued weakness in residential construction activity. However, nonresidential construction spending is likely to remain robust. The projected increase in the share of nonresidential investment spending during the forecast period will be significant enough to sustain the economy's current expansion path.

- The ***housing market*** has given both the New York and national economies a big boost over the past several years. Historically low interest rates during the past few years have contributed to rapid home price appreciation; in some areas, beyond a level that can be supported by economic and demographic fundamentals.

- ***Federal government spending*** is expected to increase further in 2007 and 2008, due mainly to the expected increase in U.S. military presence in Iraq, after growing an estimated 2.0 percent in 2006. ***State and local government spending*** grew 2.2 percent in 2006 and is expected to grow 2.5 percent in 2007 and 1.7 percent in 2008. Investment spending in structures and information technology will be the main drivers of state and local government spending growth in 2007.

- ***Net exports***, defined as exports minus imports, have declined (becoming more negative) every year from 1995 through 2006, adversely affecting the exchange rate, external debt, and GDP. Net exports will likely improve in 2007 and 2008, as world economic growth remains robust and the demand for U.S. goods and services increases.

- The ***employment*** profile for the U.S. shows relatively slower growth in 2007 and 2008, due to the slowdown in overall economic growth. Employment growth will regain a bit in 2008 compared to 2007 as economic growth is expected to return to near-trend growth.

- The general price level, as measured by the ***Consumer Price Index*** (CPI), increased 3.2 percent year-over-year in 2006, after accelerating to 3.4 percent during 2005 from 2.7 percent in 2004. As energy markets are expected to stabilize and economic growth is likely to soften to below-trend to near-trend rates in the course of the current forecast period, overall consumer price inflation will likely slow to 1.9 percent during 2007 and 2.4 percent in 2008.

- ***Energy prices*** represent a critical issue for the United States economy, and remain one of the most volatile risk factors for the health of the economy. The price of oil has increased in the past several years. However, if the price of oil is adjusted for inflation, oil prices are not as high as in the early 1980s. Along with crude oil, other energy prices in the United States have also risen. While oil prices have recently declined from the high levels seen in 2005 and 2006, the movements in the price still represent a significant risk to the forecast.

- ***Corporate profits*** steadily improved at a double-digit rate for five years in a row after plummeting 6.2 percent in 2001. Robust growth in productivity, among other factors, is believed to account for much of the recent continued improvement in corporate profits. Profits are estimated to record another solid gain in 2006, thanks to a 60.8 percent (annualized) surge in the first quarter. The gain in profits was helped largely by strong economic growth in that quarter. With output growth expected to slow, corporate profit growth will likely slow to between five and six percent during 2007 and 2008.

- The Federal Reserve is unlikely to raise the ***federal funds rate*** any further due to a slowdown in overall economic growth, partly reflecting both the cooling of the housing market and signs of moderating inflation. The federal funds rate averaged 5.0 percent in 2006 and has been at the current rate of 5.25 percent since June 2006. It is expected to average 5.25 percent throughout 2007 and 2008. The 10-year Treasury note yield averaged 4.8 percent in 2006, and is expected to average 4.8 percent in 2007 and 5.1 percent in 2008.

- Using yearly average values, the ***S&P 500*** Index increased 17.3 percent in 2004 and 6.8 percent in 2005 following three annual declines in 2001, 2002, and 2003. Due to healthy corporate profits and dividend income, the S&P 500 further increased 8.6 percent in 2006. Although corporate profit growth is likely to slow in 2007 and 2008, stable inflation and the interest rate outlook will help further sustain the stock market.

- ***Risks to the forecast*** are varied. They include uncertainty associated with energy volatility, interest rate movements, the housing market, and the potential of another terrorist attack. Energy prices remain a major risk to the forecast. Changes in energy prices have both upside and downside potential. Major job cuts in the domestic automobile industry are also a threat to the economy.

New York State

- The NYS Assembly Ways and Means Committee staff's New York State ***employment growth forecasts*** for 2007 and 2008 are 0.7 percent and 0.8 percent, respectively.

- The NYS Assembly Ways and Means Committee staff's New York State ***wage growth forecast*** for 2007 is 5.9 percent.

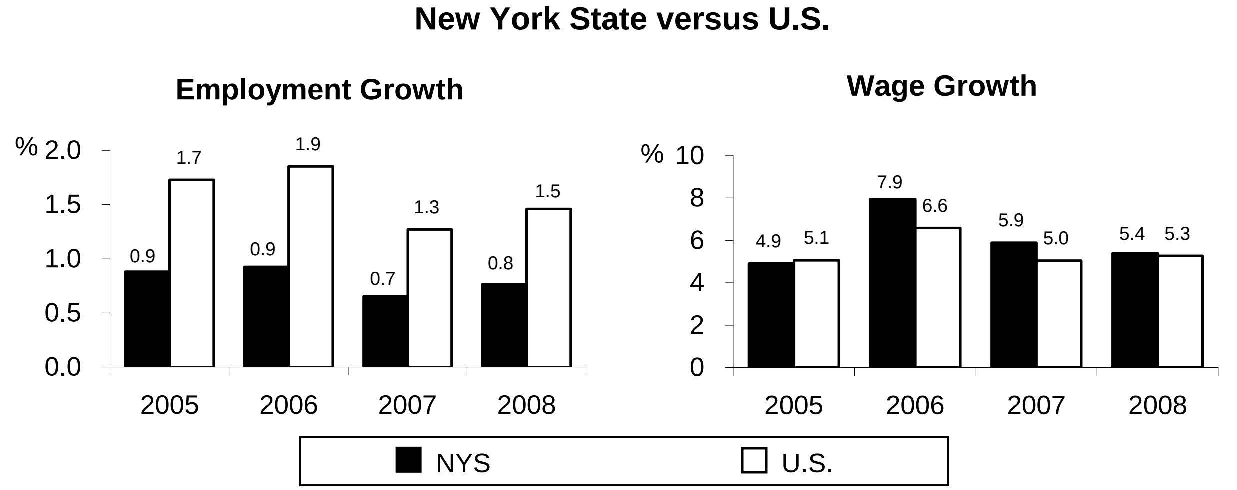
NYS Forecast Comparison
(Percent Change)

	Actual 2005	Estimate 2006	Forecast 2007	Forecast 2008
Employment				
Ways and Means	0.9	0.9	0.7	0.8
Division of the Budget	0.9	0.9	0.7	0.7
Global Insight	0.9	0.8	0.5	0.8
Moody's Economy.com	0.9	0.8	0.8	0.7
Wages				
Ways and Means	4.9	7.9	5.9	5.4
Division of the Budget	5.1	7.6	5.5	5.2
Global Insight	4.8	6.3	3.6	4.7
Moody's Economy.com	4.8	6.3	5.6	3.7

Sources: NYS Assembly Ways and Means Committee staff; New York State Financial Plan Projections, 2007-08 Executive Budget Supplemented for 21-Day Amendments, 2006-07 through 2010-11, February 21, 2007; Global Insight, Winter 2007 Short-term Forecast, January 2007; Moody's Economy.com, February 2007.

- ***The New York State coincident economic indicator index*** constructed by the NYS Assembly Ways and Means Committee staff indicates that the State economy is still expanding. The recent softening in the State leading economic indicator index hints at a possible decline in the State's economic performance in the near future. However, the Committee staff believes that the State economy is not likely to go into a recession during the forecast period.

- The ***New York State economy*** continues to lag the United States in employment growth. However, the State will benefit from the continued expansion of the national economy.



Note: Data for 2006 is estimated; 2007 and 2008 are forecasts.
Sources: NYS Department of Labor, QCEW; Bureau of Economic Analysis; NYS Assembly Ways and Means Committee staff.

- In 2007, ***New York State employment*** is expected to grow 0.7 percent compared to 0.9 percent in 2006. The steady rate of employment growth reflects both business expansion and growing consumer spending. However, the rate of New York State employment growth is expected to remain lower than that of the nation throughout the forecast period, reflecting a lower long-term rate of employment growth in the State.

- ***The sectoral composition of job gains*** in 2007 is expected to be similar to that of 2006. The largest employment gains (in levels) will be in education and health, professional services, and securities. Since 1995, the largest average annual regional job gains have been in New York City, but there have also been notable job gains in NYC suburbs. As in the State and the nation, employment gains in the New York regions were concentrated in the service sectors. Manufacturing employment in the State has declined at a faster rate than in the nation.

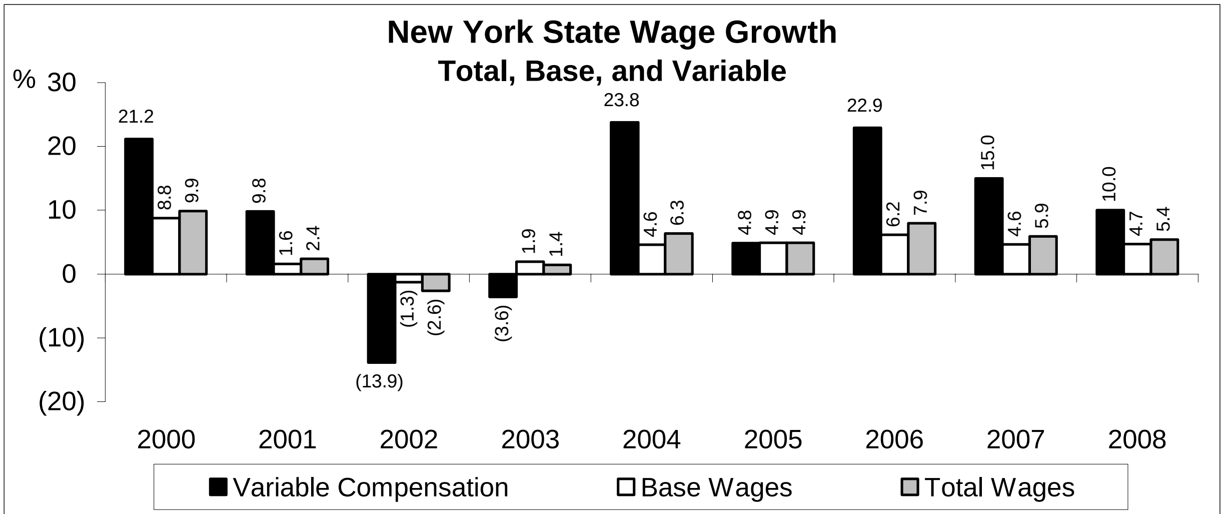
- ***New York State employment growth*** will be helped by employment growth in the New York City area. Upstate growth, however, continues to lag both the nation and the rest of the State. Overall, New York State employment growth is usually ranked around 40th when compared to other states and the District of Columbia. Upstate (if ranked as a state) frequently ranks near last.

- ***Wage growth in New York State*** is expected to be 5.9 percent in 2007 following an estimated 7.9 percent in 2006. In 2008, total wages are expected to grow 5.4 percent; a result of slower variable compensation growth in 2008 compared to 2007.

- ***Variable compensation*** is expected to continue to show stronger growth than base wages throughout the forecast period. In 2007, base wages are forecast to grow 4.6 percent, compared to 15.0 percent growth in variable compensation.

- Announced United States ***mergers and acquisitions*** were strong in 2006, helping to fuel securities industry profits. Worldwide-announced mergers and acquisitions, which exceeded $1 trillion in activity in 2005, surged 38 percent in 2006 to a record $3.8 trillion. Low interest rates, along with increasing corporate earnings, have created favorable conditions for mergers and acquisitions. In addition, both initial public offering (IPO) activity and announcements of companies going private also were strong. The outlook for IPOs, private equity, and mergers and acquisitions is positive.

- In 2005, variable wages grew in most sectors of the New York State economy. The largest level gain was seen in the securities industry. The NYS Assembly Ways and Means Committee staff estimates that New York State total variable compensation, which was $45.7 billion in 2005, increased by 22.9 percent to $56.2 billion for 2006. This will be followed by a growth of 15.0 percent year-over-year during 2007 and 10.0 percent in 2008.



Note: Total wage data for 2006 is estimated; 2007 and 2008 are forecasts. Base wages and variable compensation are estimated by the Committee staff and sum to total wages.
Sources: NYS Department of Labor, QCEW; NYS Assembly Ways and Means Committee staff estimates.

- Since 1995, ***wages in New York City*** have grown at the highest average annual rate of any region in the State. The upstate region with the largest average annual percentage increase was the Capital region, with 4.2 percent.

- ***Risks to the New York State forecast*** are both positive and negative, and include the risks to the national forecast. Among the risks is uncertainty with respect to energy price volatility, interest rate movements, and the housing market. The volatility of the securities industry also represents a significant risk to the New York State forecast.

INTRODUCTION

United States Economy

The national economy continued to expand in 2006 for the fifth year since the end of the 2001 recession. After surging 5.6 percent (annualized) in the first quarter of 2006 however, the economy has shifted into low gear. In the fourth quarter of 2006 national economic growth slowed to an estimated 2.2 percent, following 2.0 percent growth in the third quarter and 2.6 percent growth in the second quarter.[1] The recent slowdown was mainly caused by a significant decline in residential construction activity, among other factors. Residential construction spending, which accounts for about a third of total private fixed investment spending, declined an estimated 19.2 percent (annualized) in the fourth quarter of 2006. It was the largest quarterly decline since the first quarter of 1991 and also the fifth consecutive quarterly decline since the third quarter of 2005.

Various signs point to sharp cooling in the housing market.[2] Home sales and housing permits have been falling, inventories of unsold new homes rising, and housing starts plunging (see Figure 1). House prices have also been declining. Homebuilders' confidence has dropped to its lowest level in more than a decade.

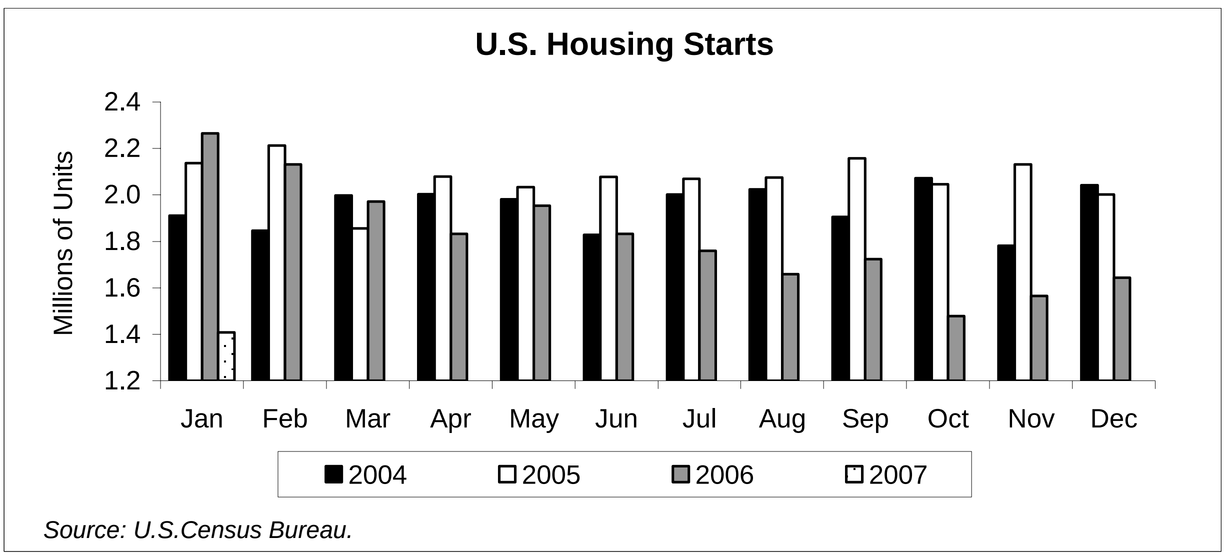


Figure 1

[1] According to an "advance" estimate by the Bureau of Economic Analysis, the U.S. economy grew 3.5 percent in the fourth quarter of 2006. However, based on several recent monthly economic indicators, the Committee staff estimates that the national economy grew only 2.2 percent in the fourth quarter.

[2] However, according to a survey by WSJ.com, economists believed by nearly a 2 to 1 margin that the worst of the housing bust was over. Nevertheless, they still predicted that the average selling price of a house would fall in 2007. See Phil Izzo, "Why the Housing Forecast is Mixed," *Wall Street Journal*, November 21, 2006, A2.

The decline in the housing market is worrisome. According to a study done by the National Association of Home Builders, housing—the production of housing as well as the value of housing services produced by the housing stock—accounts for about 14 percent of U.S. aggregate economic activity.[3] Housing not only has direct effects on the construction sector but also indirect effects on personal consumption spending through income and housing wealth effects—in particular through the so-called mortgage equity withdrawal by homeowners. Housing and housing-related activity added an estimated 35,000 payroll jobs a month during 2005, about 20 percent of total payroll jobs created during that year.[4] According to a Federal Reserve survey of homeowners, nearly a quarter of the homeowners surveyed said they refinanced in the 2001-02 refinance boom and approximately half of those cashed out some equity.[5] The average amount liquefied was $26,700, substantially larger than the corresponding amount of $18,200 from the 1999 survey. Of the cashed-out equity, 51 percent was used for consumer expenditures and home improvements; 26 percent for debt repayment; and 21 percent for financial, business or real estate investments.[6]

Payroll employment, although still steadily improving, has been growing persistently slower compared to earlier recoveries (see Figure 2). Employment gained only 5 percent in the five-year period after the end of the 2001 recession. In comparison, the gain in employment was 10 percent during the same length of period after the end of the 1991 recession, and 14 percent during the recovery period of the post-World War II average business cycle before 1991. The annual three-year revisions of the National Income and Product Accounts (NIPA) that were released in July 2006 showed a 0.2 to 0.3 percentage point slower annual growth in real GDP over the past three years, hinting at a similar downward shift in the trend growth.

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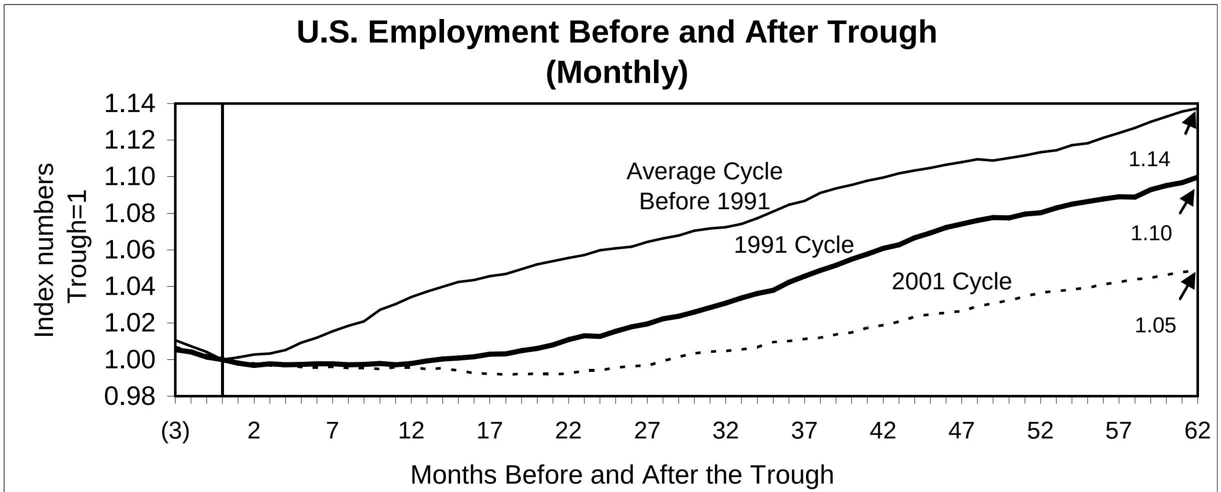
[3] National Association of Home Builders, *Housing: The Key to Economic Recovery*, 2002.

[4] Mark M. Zandi and Zoltan Pozsar, Moody's Economy.com,"MEW Matters," *Regional Financial Review*, vol. 16, no. 12, April 2006.

[5] Glenn Canner, Karen Dynan, and Wayne Passmore, "Mortgage Refinancing in 2001 and Early 2002," *Federal Reserve Bulletin*, December 2001, 469-481.

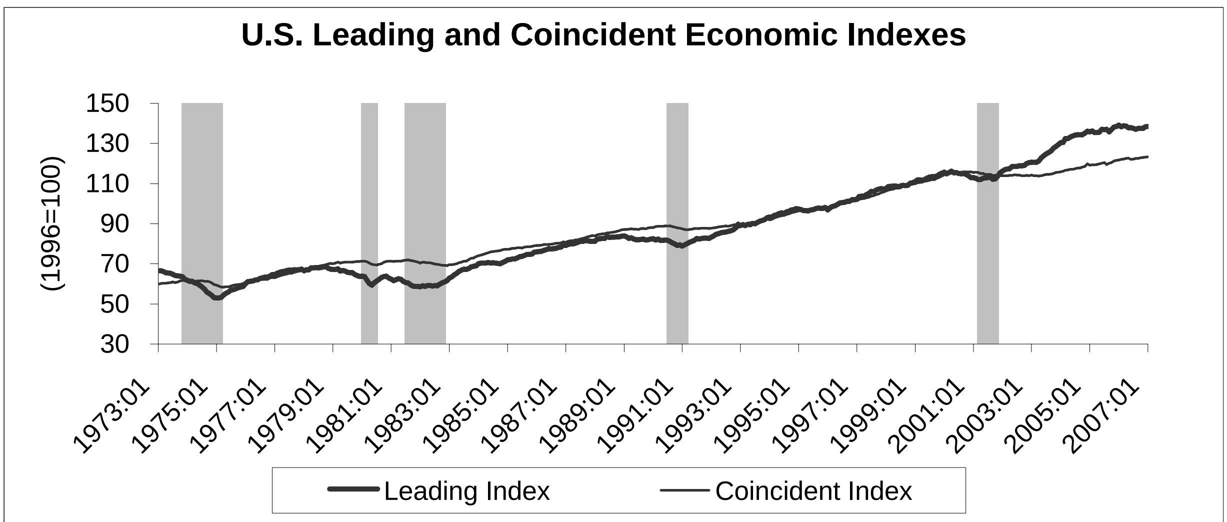
[6] The remaining 2 percent of the cashed-out equity was used for taxes. Spending on home improvements shows up in private residential construction investment in the National Income and Product Accounts (NIPA) published by the Bureau of Economic Analysis.



Note: The trough month for the 1991 cycle is March and the trough month for the 2001 cycle is November. These trough months are based on the National Bureau of Economic Research's (NBER) business cycle dates. The 62nd month after the 2001 cycle trough corresponds to January 2007.
Source: Bureau of Labor Statistics.

Figure 2

The composite index of U.S. coincident indicators, a representative gauge of current economic activity, has risen every month since July 2005, indicating the U.S. economy is still expanding (see Figure 3).[7] On the other hand, the index of U.S. leading economic



Note: Shaded areas represent recessions.
Source: The Conference Board.

Figure 3

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[7] The Conference Board's composite index of U.S. coincident indicators consists of nonfarm payroll employment, real personal income less transfer payments, real sales in the manufacturing and trade sectors, and industrial production.

indicators, a key gauge of future economic activity, fell five out of twelve months in 2006, hinting that the national economy may decline in the near future.[8] This decline in the leading economic index was ascribed to several components which include declining building permits and negative term spreads.[9]

Of particular interest is the recent negative term spread between the 10-year Treasury note yield and the federal funds rate. In the past fifty years, an inverted yield curve (i.e., the short-term interest rate rising above the long-term interest rate) has always preceded a recession, although a recession has not always followed an inverted yield curve (see Figure 4).[10] As such, it is not to be dismissed easily. However, it is important to note that the message in the recent inversion of the yield curve seems unclear. This time around, foreign investors, including those from Asia, Europe, and South America, have been large, willing buyers of U.S. long-term bonds, looking for the safety and liquidity provided by U.S. securities.[11] These global forces have helped keep the U.S. long-term interest rate relatively low, but for reasons largely independent of the bond market expectations and returns. Thus, the recent inverted yield curve appears to be a less reliable indicator of a future recession.

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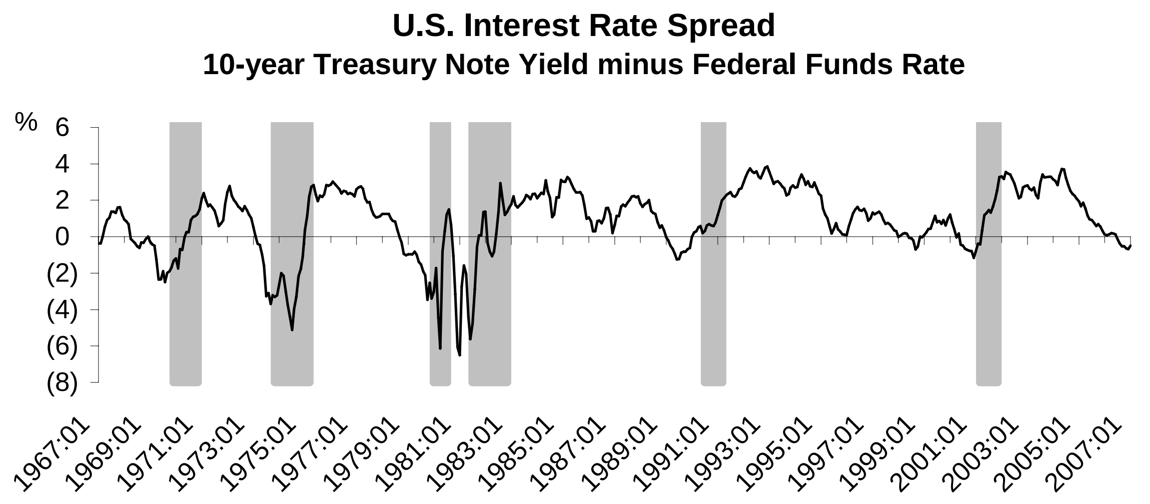
[8] The Conference Board's composite index of U.S. leading indicators consists of ten monthly time series. These include the average weekly hours worked by manufacturing workers, new orders for consumer goods, new orders for nondefense capital goods, stock prices measured by the S&P 500 composite stock price index, initial jobless claims, vendor performance, building permits, money supply measured by M2 adjusted for general price inflation, consumer expectations, and the spread between the 10-year Treasury note yield and the federal funds rate.

[9] A negative term spread occurs when the long-term interest rate falls below the short-term interest rate.

[10] One explanation for an inverted yield curve's tendency to precede a recession involves bond market expectations. As the economy nears the peak of the business cycle, economic growth starts slowing and inflation pressure begins to dissipate. This prompts bond market investors to believe a recession is on the horizon and the Fed will start lowering the short-term interest rate in the near future. As a result, demand for long-term bonds increases, pushing the long-term interest rate down, often below the current short-term interest rate, resulting in an inverted yield curve. The value of the yield curve as a cyclical indicator has recently been discussed by the Federal Reserve Bank of New York. See Arturo Estrella and Mary Turbin, "The Yield Curve as a Leading Indicator: Some Practical Issues," *Current Issues in Economics and Finance*, Federal Reserve Bank of New York, July/August 2006. For a more casual discussion, see Michael Hudson, "Grading Bonds on Inverted Curve," *Wall Street Journal*, January 8, 2007, C1.

[11] Foreign holdings of U.S. federal debt more than doubled to $2.1 trillion in June 2006 from June 2001. During the same five-year period the foreign share increased from 17 percent to 25 percent.



Note: Shaded areas represent recessions.
Source: Moody's Economy.com.

Figure 4

The New York State Assembly Ways and Means Committee staff believes that overall economic growth will likely continue to soften throughout 2007, but the national economy is unlikely to slip into a recession.[12] This optimism is based on the belief that the recent as well as near-future slowdown is a result of a shift in the sources of growth rather than the deterioration in a whole array of economic fundamentals. It appears that further growth of the economy will be powered more by business capital spending, government spending, and net exports than by homebuilding and consumption financed by borrowing (including refinancing).

As utilization of the existing production capacity increases (see Figure 5), business capital spending will likely continue to expand. This expansion will be helped by the recent improvement in corporate balance sheets as well as the big surge in business cash flow seen over the past few years. Capital goods orders have also been trending upward, indicating a further increase in business capital spending. Also encouraging is the expansion in business investment spending across a wide range of equipment, software,

[12] Although predictions based on various econometric models point to a recession ahead—the above mentioned yield curve inversion model is one such example—many economists argue that this time will be different. According to Edward Leamer, Director of the UCLA Anderson Forecasts, model predictions will be wrong this time because: 1) manufacturing is not poised to contribute much to job loss; and 2) inflation-adjusted interest rates are very low and there is no evident credit crunch, now or on the horizon. As for the housing market, he argues that this time the problems in housing will stay in housing. For more details, see Edward E. Leamer, "Is a Recession Ahead? The Models Say Yes, but the Mind Says No," *Economists' Voice*, Vol. 4, Iss. 1, Article 1, January 2007, http://www.bepress.com/ev/vol4/iss1/art1.

and structures. Healthy gains have been seen in energy-related equipment, construction of office buildings, and energy-related structures.

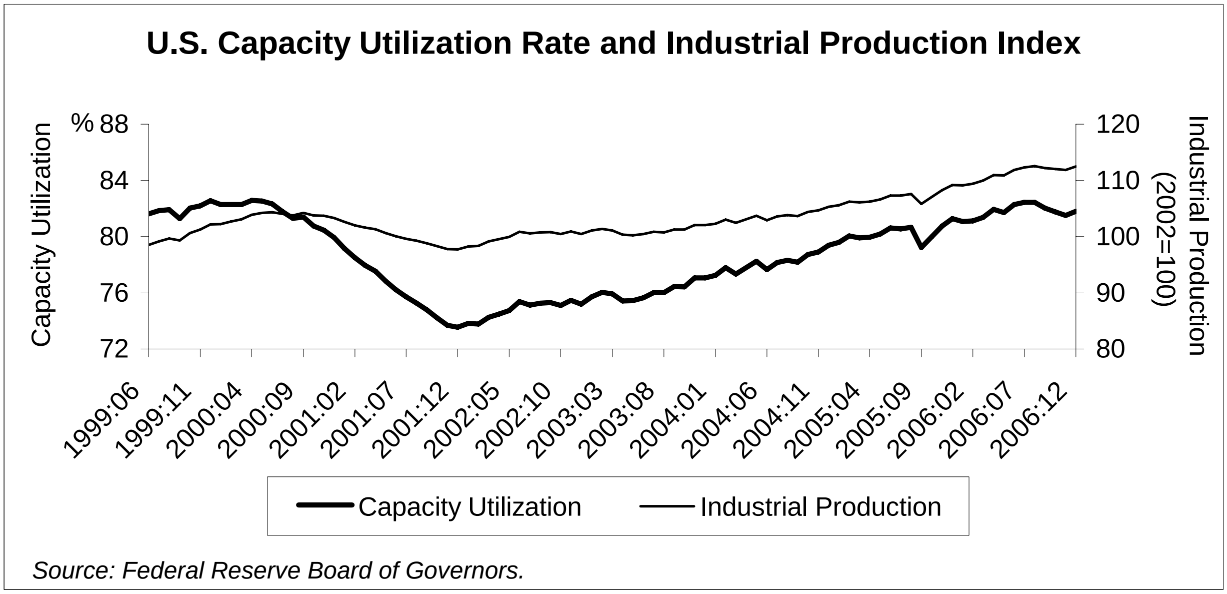


Figure 5

Although likely to be restrained by a general softening in economic growth and a decline in home prices, personal consumption spending is expected to continue to make a positive contribution to economic growth, helped by a steady increase in personal income. Employment gains, though remaining on a lower track than in previous expansions, as well as healthier gains in hourly compensation are expected to continue to support this personal income growth throughout 2007. Energy prices, which are expected to stabilize in the coming months, will help sustain consumer purchasing power. Research has shown that the relationship between home equity or mortgage-financed cash flow and personal consumption spending has not been as strong as previously thought.[13] Even when such a relationship exists, it is estimated to be biased less toward higher income and wealthier consumers than to lower income households that have spent more aggressively in response to fast appreciation in their housing values.[14] To the extent that the bulk of spending on consumer goods and services is done by higher-income and wealthier consumers, the negative wealth effects of any declining housing values on overall consumption spending will likely be limited.

[13] Joel L. Prakken, "Housing Bubble Trouble?" (presentation prepared for Macroeconomic Advisers' 15th Annual Washington Policy Seminar, December 8, 2005). Jonathan McCarthy and Charles Steindel, "Housing Activity, Home Values, and Consumer Spending," *Innovations in Real Estate Markets: Risks, Rewards, and the Role of Regulation*, Federal Reserve Bank of Chicago, 2006.

[14] Mark M. Zandi and Zoltan Pozsar, Moody's Economy.com, "MEW Matters," *Regional Financial Review,* vol. 16, no. 12, April 2006.

Net exports will be less of a drag on economic growth as the U.S. dollar is expected to continue declining during 2007 and 2008. Broad-based global economic growth, with recovery apparently well footed now even in Japan and most of the industrialized economies in Europe, will help boost foreign demand for U.S. produced goods and services, supporting U.S. economic growth.

Overall consumer price inflation remained relatively high at 3.2 percent in 2006, after accelerating to 3.4 percent during 2005 from 2.7 percent in 2004. Not only high energy prices but also a steady rise in the core Consumer Price Index (CPI) was responsible for the recent relatively high inflation. The core CPI, which excludes more volatile items such as energy and food from the overall consumer price index, increased 2.1 percent in 2005. It further increased 2.4 percent in 2006. This recent gain in core CPI was caused by underlying economic fundamentals such as decelerating productivity growth and a sharp rise in unit labor costs. Energy prices have been passed through, although not fully or in all industries, to consumers in the form of higher prices for other goods and services.[15] Higher import prices as a result of a depreciation in U.S. dollar values also contributed to increased CPI inflation. However, as energy markets are expected to stabilize and economic growth is likely to soften to below-trend to near-trend rates in the course of the current forecast period, overall price inflation will likely slow to 1.9 percent during 2007 and 2.4 percent in 2008.[16]

With productivity growth expected to slow to a more sustainable rate of around 2 percent, the nation will likely gain around 144,000 payroll jobs a month during 2007. Although the employment gain will be seen in most economic sectors, the residential construction sector will be an exception due largely to declining homebuilding.

Stock prices measured by the S&P 500 index grew solidly in 2005, increasing 6.8 percent using yearly average values. Due to healthy corporate profits and dividend income, the S&P 500 further increased 8.6 percent in 2006. Although corporate profit growth is likely to slow in 2007 and 2008, a stable inflation and interest rate outlook will help sustain the stock market.

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[15] According to a study by the Congressional Budget Office, in 2005 non-energy prices appeared to have grown by about half a percentage point more than they would have if energy prices had not risen. See U.S. Congressional Budget Office, *The Economic Effects of Recent Increases in Energy Prices*, July 2006. See also Owen F. Humpage and Eduard Pelz, "Do Energy Price Spikes Cause Inflation?" Federal Reserve Bank of Cleveland Economic Commentary, April 2003.

[16] The 2003-04 weight for energy in overall CPI is 8.7 percent. This means a direct impact of a 10 percent increase in energy prices is a 0.9 percent increase in overall CPI.

Despite the positive signs mentioned above, the economic environment remains uncertain, with many risks to the current forecast. The future course of oil prices is certainly a major risk factor. Also uncertain is how much further the housing market will decline and how long personal consumption can remain strong. Large deficits in the U.S. current account and federal budget may have very serious economic repercussions both at home and abroad. Any future terrorist attack as well as further deterioration of the situation in Iraq may have a large impact on spending and investment, in part by hindering confidence in the future performance of the economy. Major job cuts in the domestic automobile industry are also a threat to the economy, particularly if this trend spreads to other industries.

New York State Economy

The New York State coincident economic indicator index constructed by the NYS Assembly Ways and Means Committee staff indicates that the State economy is still expanding (see Figure 6).[17] The recent softening in the State leading economic indicator index hints at a possible decline in the State's economic performance in the near future. However, the Committee staff believes that the State economy is not likely to go into a recession during the forecast period.

[17] These New York State coincident and leading economic indicator indexes were constructed by NYS Assembly Ways and Means Committee staff employing the methodology that the Conference Board developed for its U.S. economic indicator indexes. The New York State coincident indicator index presented here was constructed based on two time series: the Conference Board's U.S. coincident index and New York State total nonagricultural employment. Additional time series that were tried but not included in the final selection include time series on State sales tax receipts, wages and salaries withholding receipts, and hourly average wages in the State manufacturing industry. The New York State leading indicator index presented here was constructed based on three State time series (unemployment insurance initial claims, consumer confidence expectations index, and building permits) and five U.S. time series (new orders for consumer goods, new orders for nonmilitary capital goods, stock prices measured by the S&P 500 composite stock price index, vendor performance, and the spread between the 10-year Treasury note yield and the federal funds rate). For more details on the Conference Board methodology, see "Calculating the Composite Indexes," July 10, 2006, http://www.conference-board.org. Similar economic indicator indexes were constructed using different approaches. For example, James Orr, Robert Rich, and Rae Rosen, "Leading Economic Indexes for New York State and New Jersey," *FRBNY Economic Policy Review*, March 2001, 73-94. Robert Megna and Qiang Xu, New York State Division of the Budget, *Forecasting the New York State Economy: The Coincident and Leading Indicators Approach*, (posted: http://www.budget.state.ny.us/pubs/supporting/supporting.html).

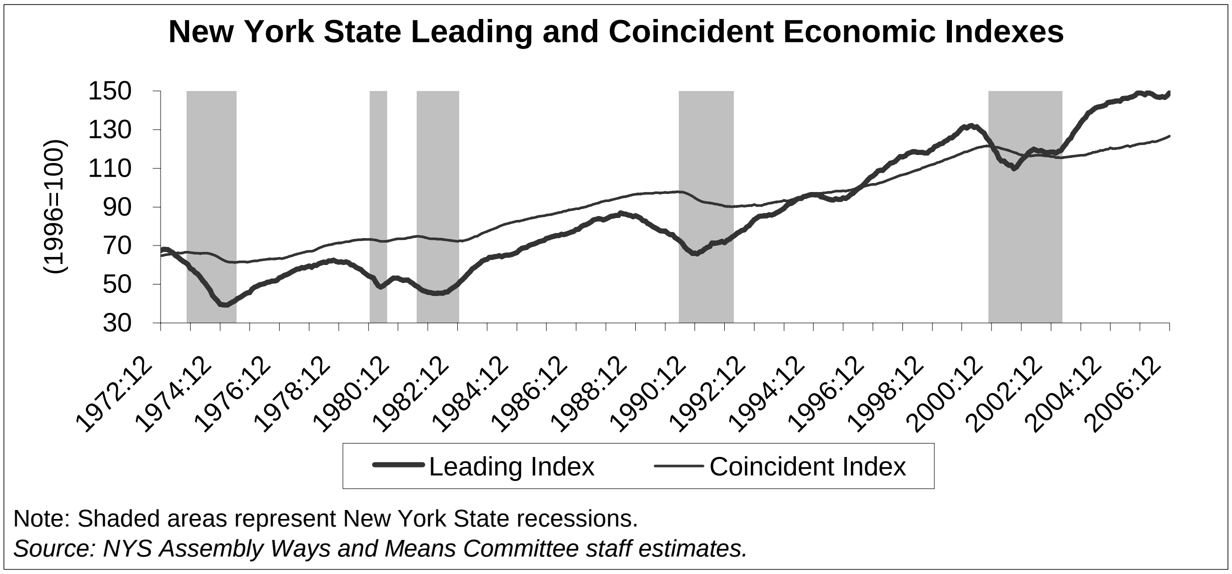


Figure 6

As the nation continues to grow, New York's economy will continue to benefit. Estimated State employment growth for 2006 was less than the nation. This is predicted to be the case throughout the forecast period. State wages are estimated to have grown faster than United States wages in 2006, a trend that is expected to continue throughout the forecast period as Wall Street economic activity is expected to remain robust in 2007 and 2008 (see Figure 7 and Figure 8).

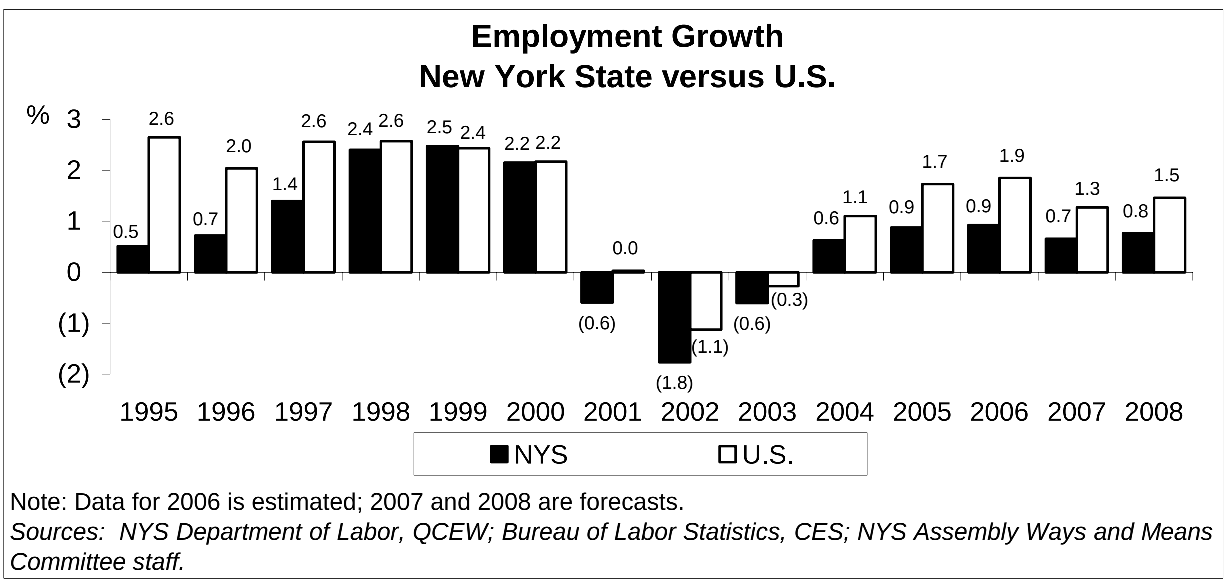
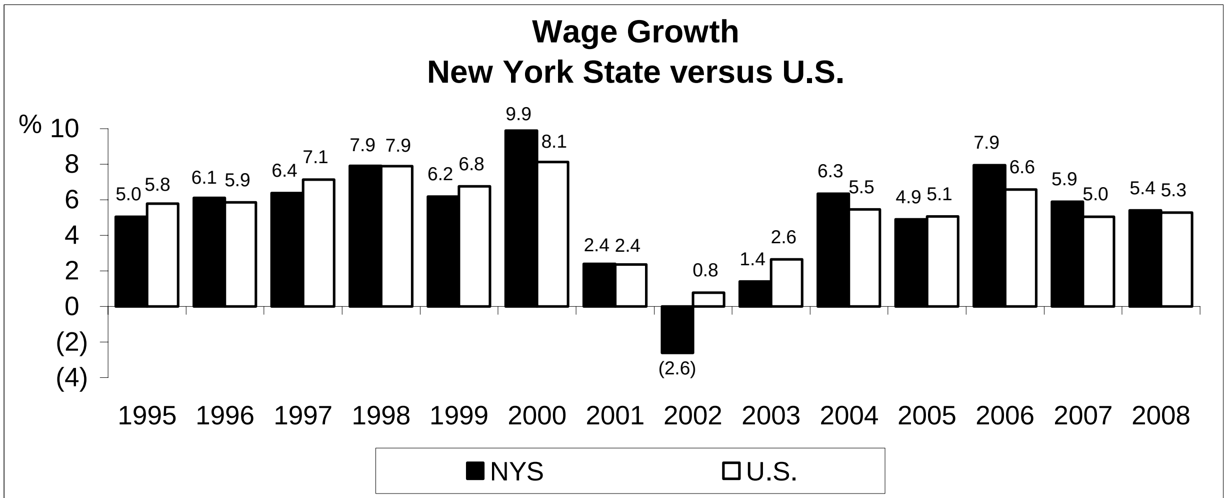


Figure 7

The gains in both national and New York State employment are expected to be bolstered throughout the forecast period by continued expansion of the service sector. The largest level gain is expected to be in the education and health sector. The manufacturing sector will likely continue to lose employment throughout the forecast period. Construction employment growth will slow to less than one percent in 2007 and 2008, a reflection of the slowdown in residential construction activity.

New York State employment growth will be helped by employment growth in the New York City area. Upstate growth, however, continues to lag both the nation and the rest of the State. Overall, New York State employment growth is usually ranked around 40th when compared to other states and the District of Columbia. Upstate (if ranked as a state) frequently ranks near last.

Wage growth in New York State will decelerate slightly in 2007 and 2008 compared to 2006 (see Figure 8). This is indicative of a slowdown in growth of both variable compensation and base wages. Variable compensation remains a major contribution to State wage growth due to the economy's concentration in the securities industry. The majority of variable wages are paid by firms in the securities industry, and the volatility of such payments represents considerable risk to the forecast. Variable wages are forecast to grow 15.0 percent in 2007, followed by 10.0 percent in 2008.



Note: Data for 2006 is estimated; 2007 and 2008 are forecasts.
Sources: NYS Department of Labor, QCEW; Bureau of Economic Analysis; NYS Assembly Ways and Means Committee staff.

Figure 8

Gross Domestic Product

The national economy, as measured by real Gross Domestic Product (GDP), is estimated to have accelerated slightly to 3.3 percent year-over-year in 2006, after growing 3.2 percent in 2005 (see Figure 9). Accounting for the estimated acceleration in 2006 was stronger growth in both net foreign demand and government spending (see Figure 10).

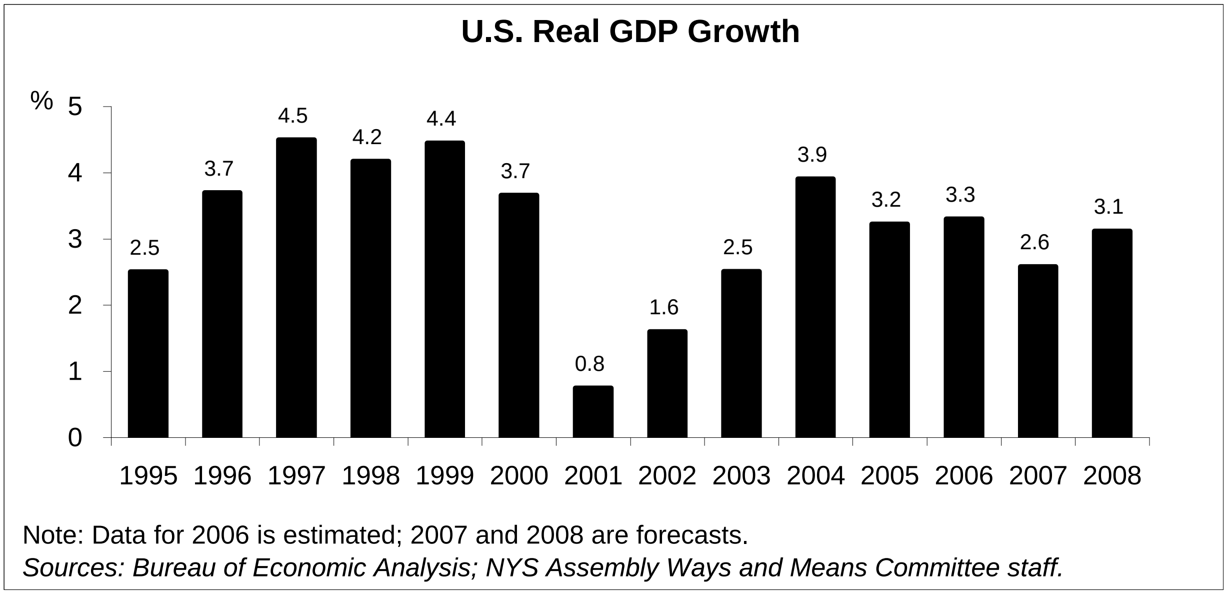


Figure 9

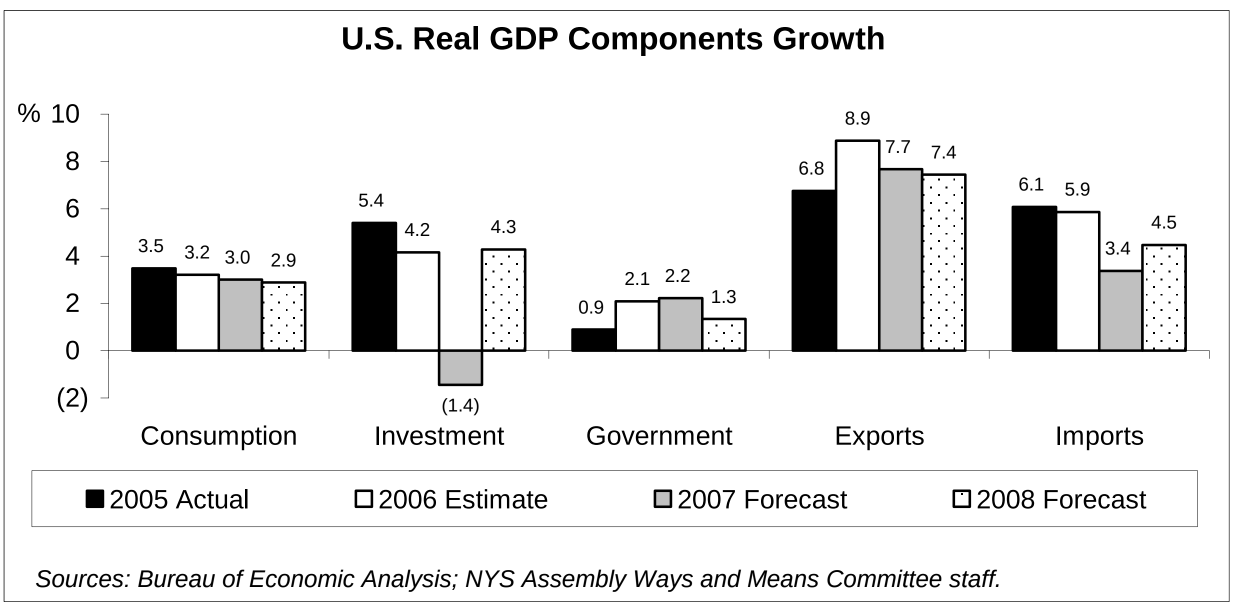
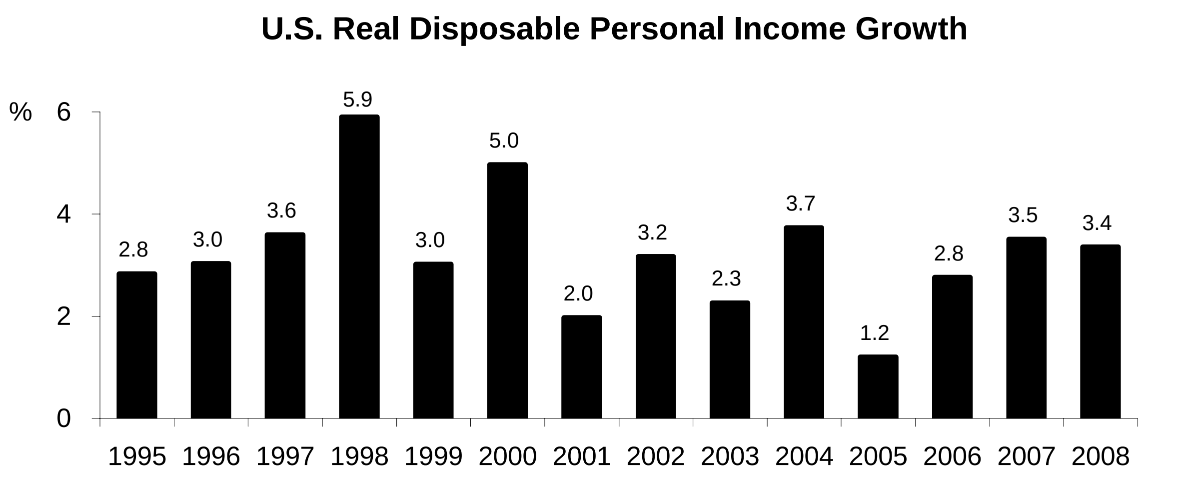


Figure 10

Due primarily to a slowdown in personal consumption spending growth and a decline in residential construction activity, real GDP growth is forecast to decelerate to a below-trend 2.6 percent during 2007. As the housing market rebounds and energy prices are expected to continue to stabilize into 2008, downward pressures on real disposable personal income will be lifted and the national economy will rebound to 3.1 percent in 2008, a rate close to the long-term trend.

Consumption

Despite increases in crude oil prices that cut into the consumer's purchasing power, personal consumption spending adjusted for overall consumer price inflation grew a healthy 3.5 percent year-over-year during 2005.[18] It further expanded 4.8 percent (annualized) in the first quarter of 2006 before it slowed to 2.6 percent in the second quarter, 2.8 percent in the third quarter, and 4.4 percent in the fourth quarter. The strong growth in real personal consumption spending in 2005 was supported by a sluggish but steady recovery in payroll employment and a continued gain in real disposable personal income (see Figure 11). Steady appreciation in home prices as well as corporate equities held by households also contributed to the robust growth in real personal consumption spending in 2005.



Note: Data for 2006 is estimated; 2007 and 2008 are forecasts.
Sources: Bureau of Economic Analysis; NYS Assembly Ways and Means Committee staff.

Figure 11

[18] The share of U.S. personal spending on energy in total personal consumption spending was 4.0 percent in the third quarter of 2006. Although significantly higher than the post-World War II record low of 2.1 percent seen in the second quarter of 1999, it was well below the post-WWII record high of 6.0 percent seen in the second quarter of 1980 (see Figure 15). Personal consumption spending declined 0.3 percent during 1980, while it grew 5.1 percent in 1999, the fastest since 1985.

Personal consumption spending is expected to continue to be helped by a steady increase in personal income. Employment gain, though still sluggish compared to previous recoveries, and a healthier gain in hourly compensations are expected to continue to support the growth in personal income throughout 2008. Energy prices are expected to stabilize in the coming months, helping to sustain the consumer's purchasing power.

Household net worth continued to grow during 2005, thanks to steady growth in real estate values and continued increases in corporate equity values (see Figure 12). Corporate equity markets suffered in the second quarter of 2006 in the midst of worries among investors about economic slowdown and further interest rate hikes, but they have since rebounded. Equity markets will likely improve further in the coming months as economic expansion is expected to continue.

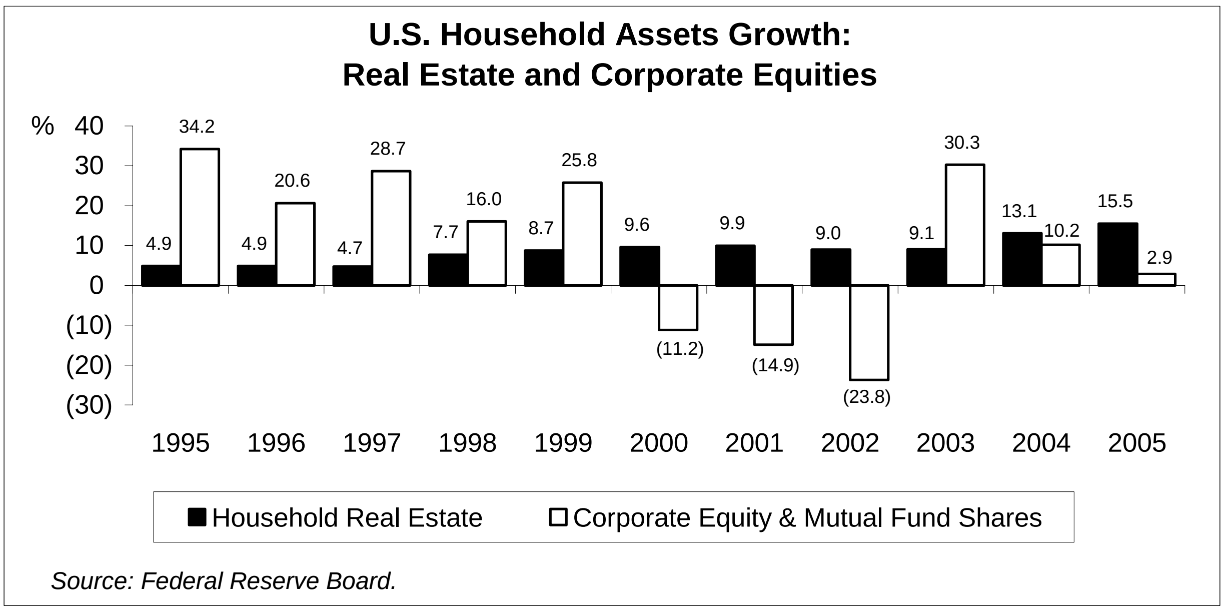


Figure 12

New orders for consumer goods plunged in September 2006, due mainly to a large 4.6 percent decline in nondurable goods orders. This was the largest decline in a decade (see Figure 13). The primary driver was a 14 percent decline in petroleum and coal products resulting from the recent decline in energy prices. As energy prices are expected to stabilize in the coming months, new orders for consumer goods will likely resume the upward trend, consistent with the consumer spending growth forecast.

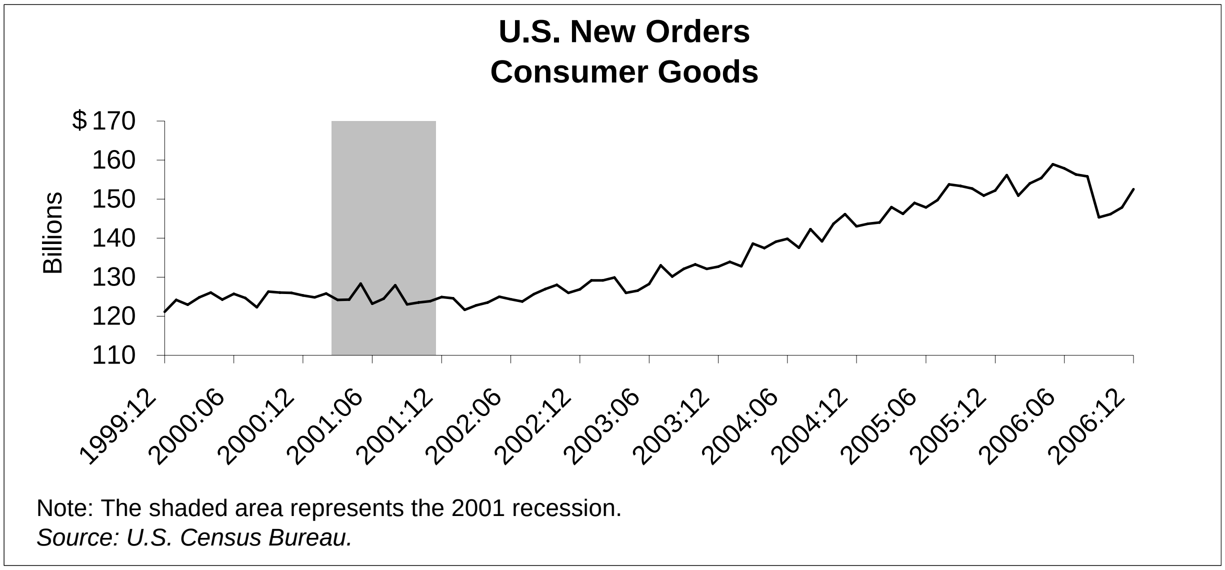


Figure 13

However, consumer spending may be negatively affected by several factors. With housing market activity expected to continue to decline, cash flow from refinancing will drop significantly, restraining overall consumer spending (see Figure 14). In particular, outlays on consumer goods and services by lower income households will likely soften significantly. Lower income homeowners have relied more heavily on home equity financing for their consumption spending in recent years than higher income earners and wealthier consumers.[19]

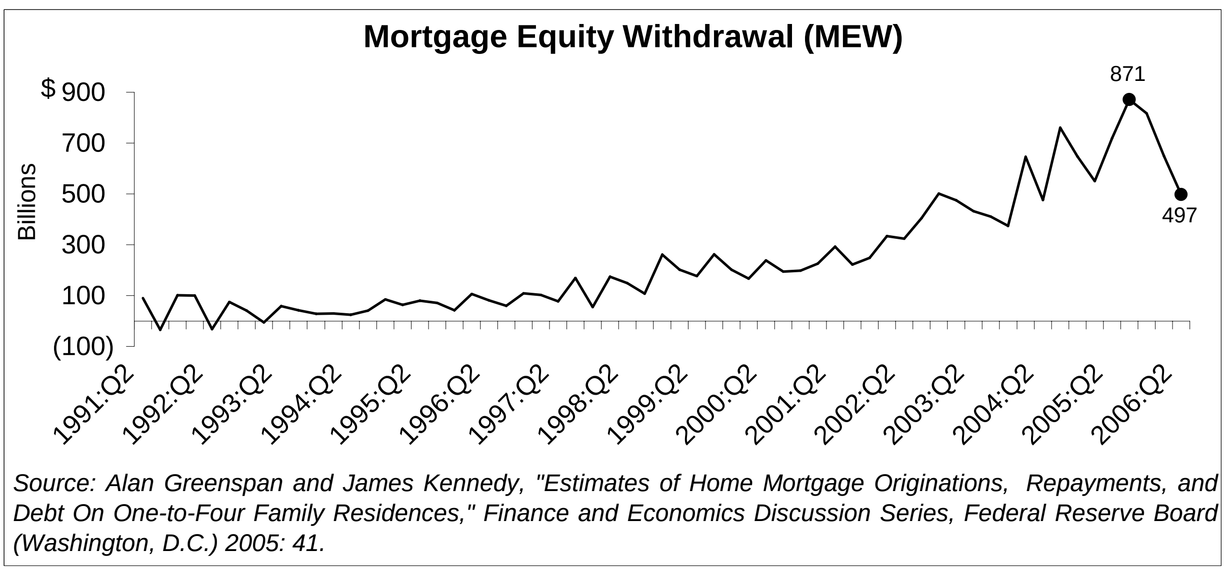


Figure 14

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[19] Mark M. Zandi and Zoltan Pozsar, Moody's Economy.com, "MEW Matters," *Regional Financial Review,* vol. 16, no. 12, April 2006.

The Assembly Ways and Means Committee staff estimates that consumer spending, adjusted for price inflation, increased 3.2 percent during 2006 after growing 3.5 percent during 2005. Consumer spending is forecast to slow to 3.0 percent in 2007 as growth in real disposable personal income is restrained somewhat by relatively high energy prices and cash-out refinancing is limited by declining home prices. With the worst in the housing market expected to be over by the end of 2007 and energy prices expected to stabilize, consumer spending will continue to grow by 2.9 percent in 2008 (see Figure 10 on page 11 and Table 1).

Table 1

U.S. Economic Outlook
(Percent Change)

	Actual 2005	Estimate 2006	Forecast 2007	Forecast 2008
Real GDP	3.2	3.3	2.6	3.1
Real Consumption	3.5	3.2	3.0	2.9
Real Investment	5.4	4.2	(1.4)	4.3
Real Exports	6.8	8.9	7.7	7.4
Real Imports	6.1	5.9	3.4	4.5
Real Government	0.9	2.1	2.2	1.3
Federal	1.5	2.0	1.7	0.7
State and Local	0.5	2.2	2.5	1.7
Personal Income	5.2	6.4	5.4	5.5
Wages & Salaries	5.1	6.6	5.0	5.3
Corporate Profits (Economic Basis)	12.5	21.0	5.1	5.6
Productivity	2.3	2.1	1.9	2.3
Employment	1.7	1.9	1.3	1.5
CPI-Urban	3.4	3.2	1.9	2.4
S&P 500 Stock Price	6.8	8.6	9.2	6.0
Treasury Bill Rate (3-month)*	3.1	4.7	4.9	5.0
Treasury Note Rate (10-year)*	4.3	4.8	4.8	5.1

* Annual average rate.
Sources: Bureau of Economic Analysis; Bureau of Labor Statistics; Federal Reserve Board of Governors; Standard & Poor's; NYS Assembly Ways and Means Committee staff.

Services consumption, the least volatile as well as the largest component of consumption (about 57 percent of the total), grew 2.6 percent during 2005 following a 3.5 percent growth during 2004.[20] Growth is estimated to have slowed slightly to 2.5 percent during 2006 as higher energy prices continued to dampen real disposable personal income growth. Growth in consumer spending on services is forecast to rebound to 2.8 percent during both 2007 and 2008 due to robust growth in consumer spending on medical care and "other" services including personal business services.

[20] The 57 percent share is an average based on the last five years of data.

Energy consumption, which accounted for 13.4 percent of total nondurable goods consumption in the third quarter of 2006, has surged in nominal terms and will likely remain high due to higher energy prices (see Figure 15). In real terms, however, energy consumption spending actually declined for four quarters in a row from the second quarter of 2005 to the first quarter of 2006. Inflation-adjusted consumer spending on other nondurable goods, which include food and clothing, also sharply decelerated to a mere 1.4 percent in the second quarter and 1.5 percent in the third quarter of 2006 after previously increasing 4 to 7 percent each quarter for several quarters. Total nondurable goods consumption spending, adjusted for inflation, is estimated to have slowed to 3.8 percent year-over-year during 2006 after growing 4.5 percent in 2005. Due to a slowdown in overall economic growth, among other factors, nondurable consumption spending growth will further slow to 3.0 percent in 2007 and 2.6 percent in 2008.

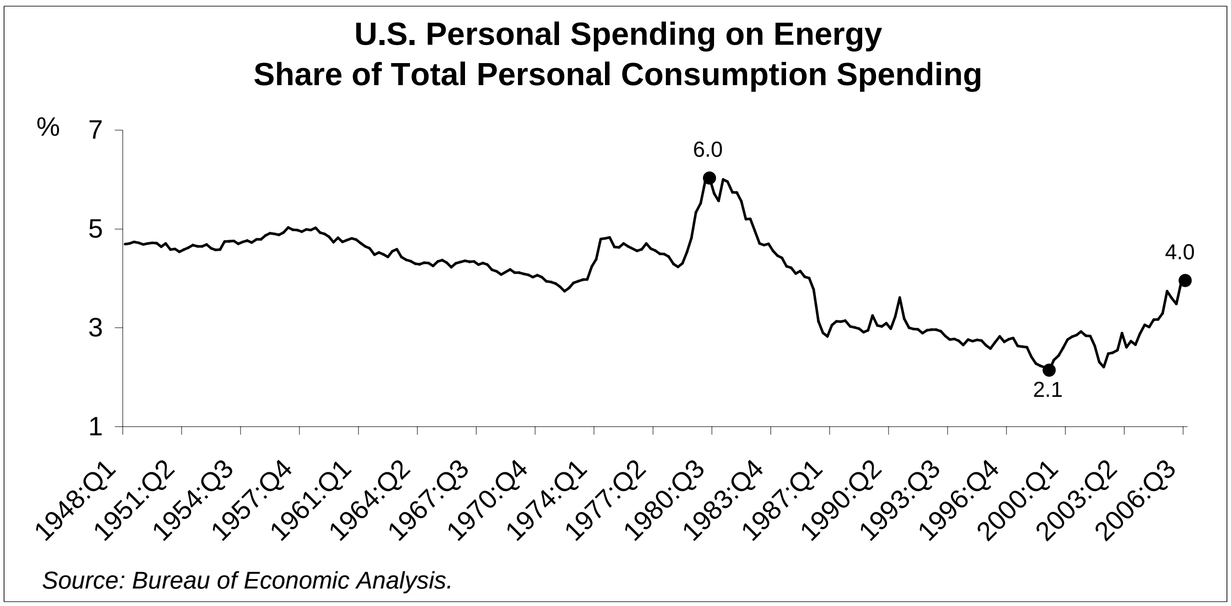

Figure 15

Durable goods consumption, the most volatile and the smallest component of total consumption (about 14 percent), grew 5.5 percent year-over-year during 2005, after growing 6.4 percent in 2004 (see Figure 16). A good part of the steady growth in durable goods consumption for the past few years can be ascribed to the unusually strong auto sales due to various sales incentives. As auto sales and housing activity (which indirectly affects durable goods purchases) declined in 2006, consumer expenditures on durable goods slowed to an estimated 5.1 percent in 2006. With housing activity expected to continue to cool in 2007 and overall economic growth to slow through 2008 (compared to 2006), growth in consumer spending on durable goods will likely decelerate in 2007 and 2008.

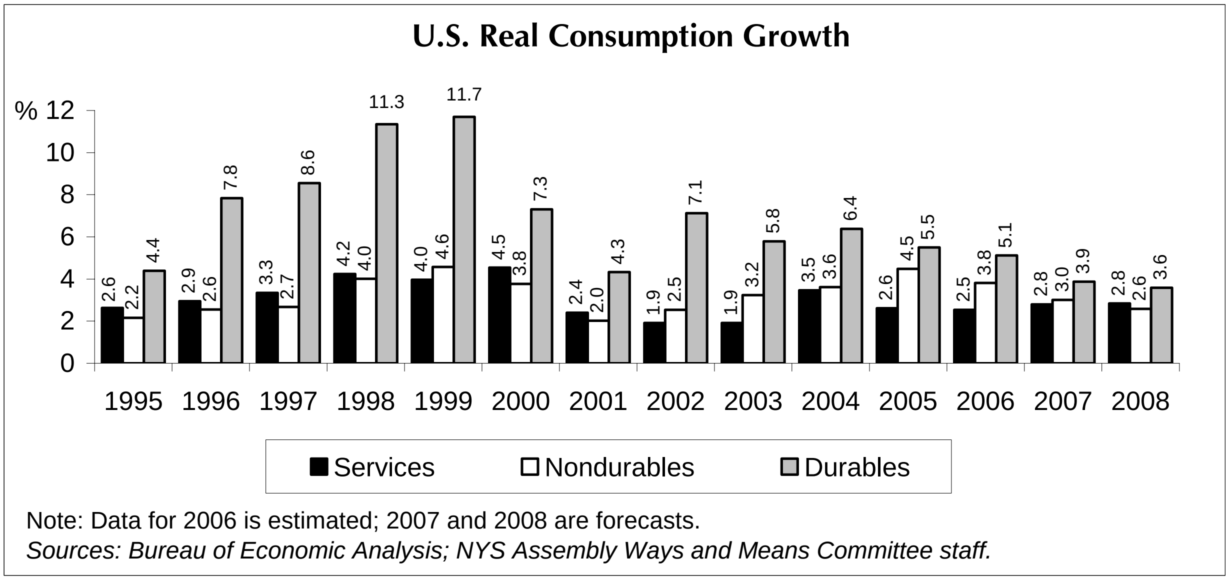

Figure 16

Investment

Private investment spending continued to expand during 2005, growing 5.4 percent year-over-year after increasing 9.8 percent in 2004. As residential construction activity has been declining amidst various signs of a deteriorating housing market, overall private investment spending slowed to an estimated 4.2 percent in 2006. With the economy expected to slow to a below-trend growth rate in 2007, however, private investment spending will continue to slow in 2007, due mainly to continued weakness in residential construction activity.[21]

The share of nonresidential fixed investment spending in GDP has been steadily rising since it fell to a seven-year low of 10.3 percent in the first quarter of 2003 (see Figure 17).[22] On the other hand, the share of residential fixed investment (or residential construction) spending in GDP has recently started to fall after reaching a twenty-five-year high of 5.6 percent in the third quarter of 2005. It is worth noting that the residential construction spending share increased through the 2001 recession unlike during previous recessions; the U.S. economy did not slide into a recession every time the residential construction share was on a downward trend. In fact, the U.S. economy managed to stay on an expansion path whenever the decrease in the share of residential investment spending was compensated for by the coincident increase in the share of nonresidential investment spending. It is thus reasonable to argue that although residential investment

[21] See the Housing Market section on page 20 for more details.

[22] Nonresidential fixed investment spending includes business equipment, software spending, and commercial construction spending.

spending share has been declining for four consecutive quarters, the projected increase in the share of nonresidential investment spending during the forecast period may be significant enough to continue to keep the economy on its current expansion path.

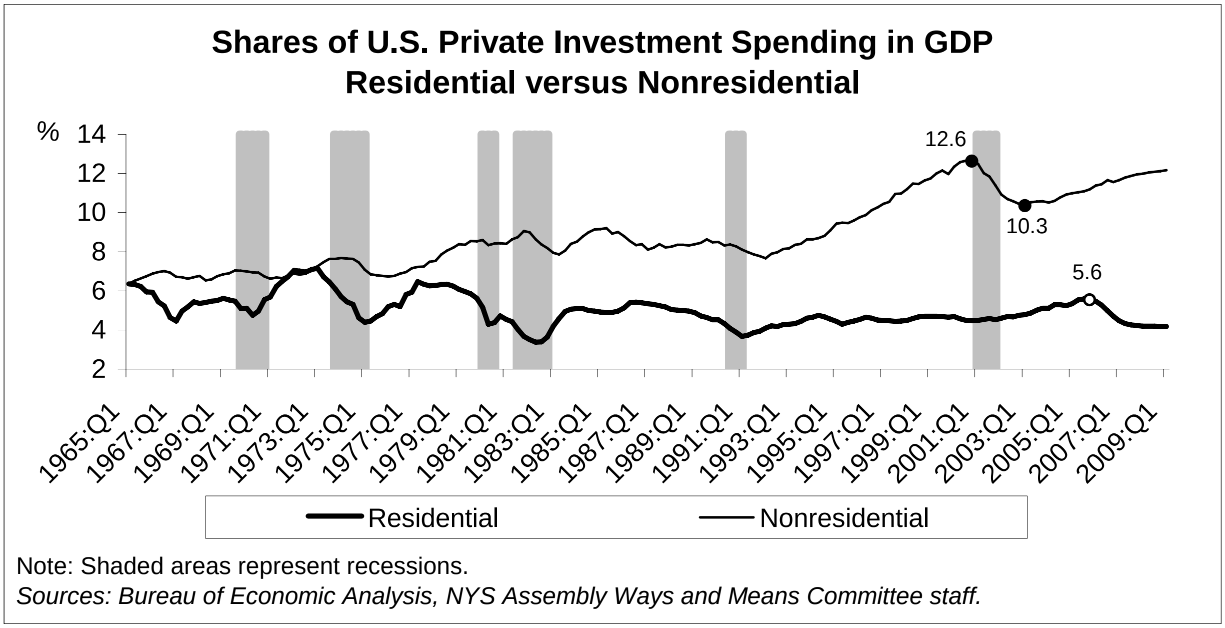

Figure 17

Despite month-to-month volatility, nonmilitary capital goods orders are overall on an upward trend (see Figure 18). As businesses expect overall economic expansion to continue beyond the expected slowdown in 2007, business capital orders and spending should continue to increase in 2007 and 2008.

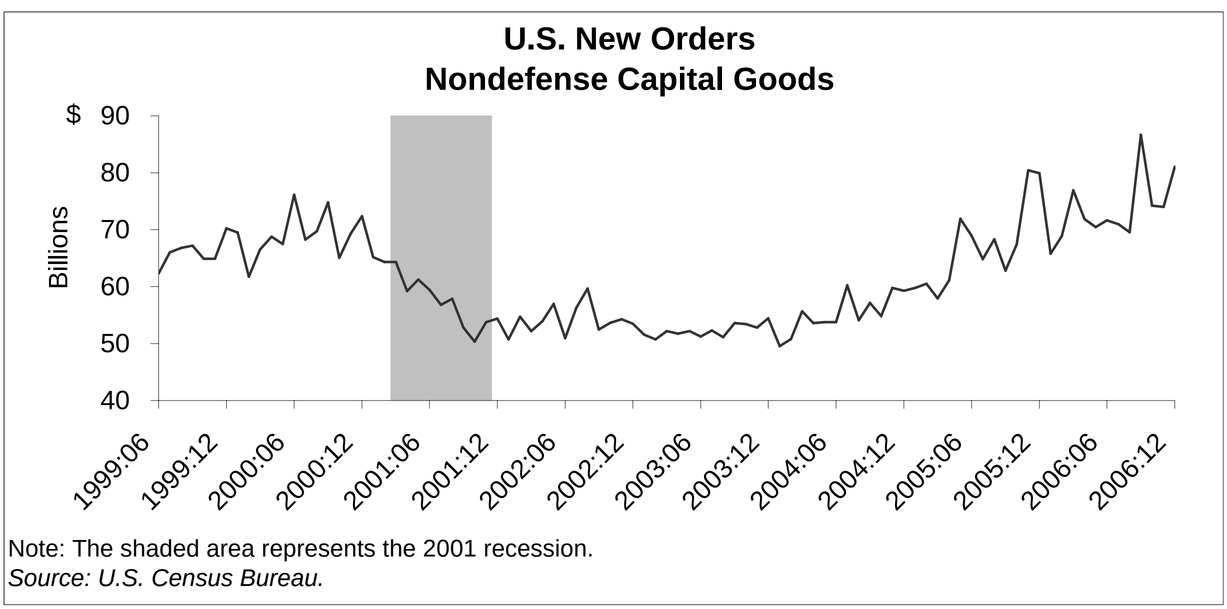

Figure 18

In constant dollar terms, business spending on information processing equipment and software accelerated to an estimated 9.0 percent during 2006, after growing 8.5 percent in 2005. Along with overall economic activity, business spending on information processing equipment and software is forecast to slow in both 2007 and 2008 to 5.9 percent and 6.3 percent, respectively (see Figure 19).

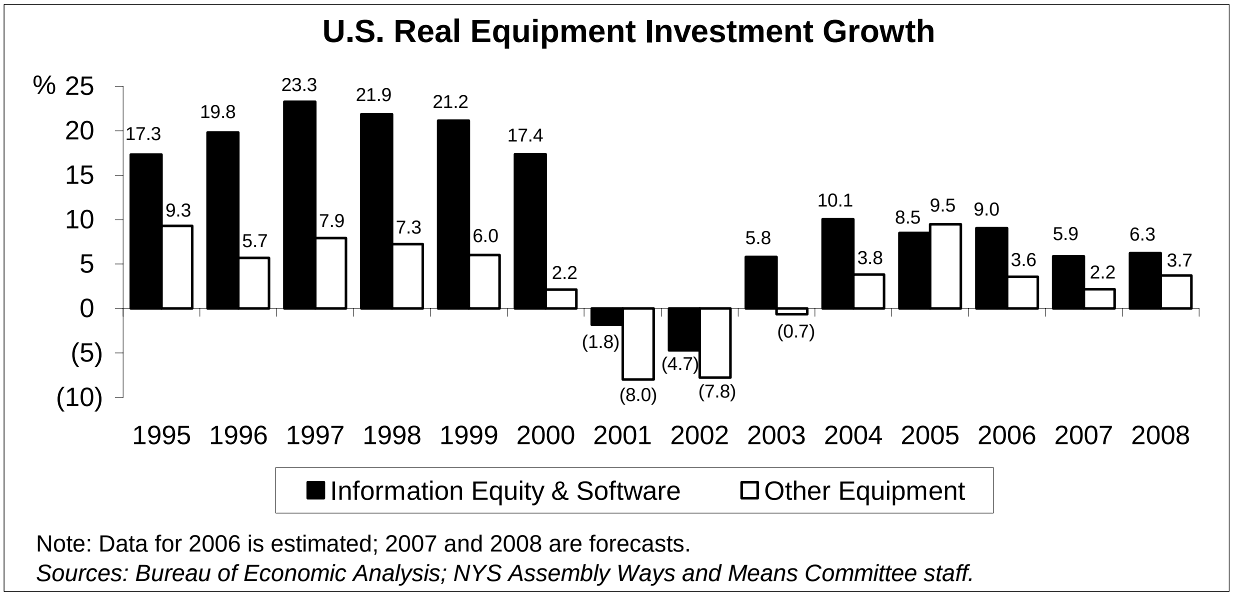

Figure 19

After declining for eleven quarters since the second quarter of 2000, business spending on non-information processing equipment (i.e., industrial, transportation, and other equipment) started turning around beginning in 2004. It grew 3.8 percent year-over-year during 2004, followed by a healthy 9.5 percent surge during 2005. Non-information equipment spending decelerated to an estimated 3.6 percent year-over-year during 2006. The expected slowdown in overall economic growth in 2007 will likely lead to a continued slowdown in non-information equipment spending growth. It is forecast to grow 2.2 percent in 2007 and 3.7 percent in 2008.

Residential construction spending, which accounts for about a third of total private fixed investment spending, declined 18.6 percent (annualized) in the third quarter of 2006, the largest quarterly decline since the first quarter of 1991 and also the fourth consecutive quarterly decline since the third quarter of 2005. Residential construction activity had increased year-over-year for ten years in a row through 2005. As housing starts are likely to decline further in response to increasing inventories of unsold new homes and a general slowdown in economic growth, residential construction activity will likely continue to decline throughout 2007 (see Figure 1 on page 1 and Figure 20). Residential construction spending declined an estimated 4.2 percent during 2006 after growing 8.6 percent in 2005 and is forecast to further decline 13.1 percent in 2007 before stabilizing in 2008.

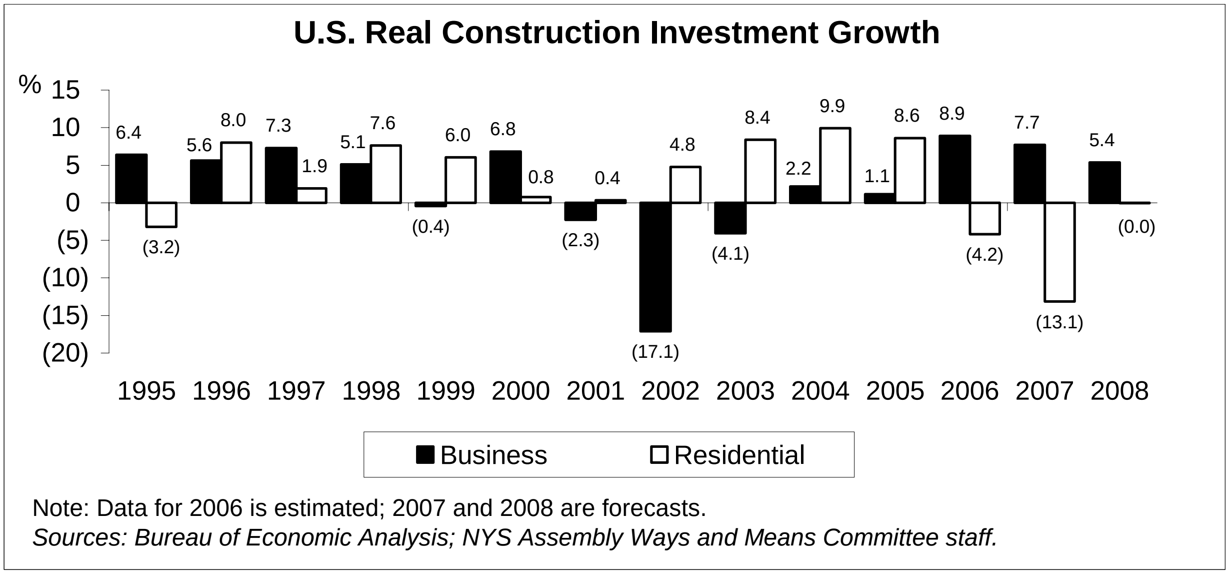

Figure 20

Nonresidential construction spending, on the other hand, increased 15.7 percent (annualized) in the third quarter of 2006, following 20.3 percent growth in the second quarter. It was the fourth consecutive quarterly increase putting the estimated year-over-year growth for 2006 close to 9 percent, the fastest yearly expansion in commercial construction spending in twenty-two years. As more intensified utilization of the existing production capacity puts upward pressure on demand for new capacity, nonresidential construction activity will likely further increase during 2007 and 2008, growing 7.7 percent and 5.4 percent, respectively.

Housing Market

The housing market has given both the State and national economies a big boost over the past several years. Historically low interest rates during the past few years contributed to rapid home price appreciation; in some areas beyond a level that can be supported by the economic and demographic fundamentals.

Currently, housing-related employment accounts for about 10 percent of all jobs. In addition, more than a third of all new jobs since the housing boom earlier in the decade have been housing related.[23] It is estimated that a weak housing market could cut as much as a percentage point off economic growth over the next year or so.[24]

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[23] Alex Markels, "Housing Slump Threatens Jobs," *U.S. News and World Report*, August 20, 2006, http://www.usnews.com/usnews/biztech/articles/060820/28jobs.htm.

[24] James R. Hagerty and Michael Corkery, "After the Boom: Housing Slump Proves Painful For Some Owners and Builders," *Wall Street Journal*, August 23, 2006, A1.

As home prices appreciate, many households are using nontraditional mortgages, such as an adjustable rate mortgage or an interest-only mortgage, which allow a buyer to purchase a house that would not have otherwise been affordable with a traditional mortgage. With rising interest rates and a weakening housing market, many households may face difficulty when these rates move up. Some buyers may need to sell their house or default on their loan, which could have an adverse impact on the mortgage industry. Foreclosure filing rose 42 percent from 2005 to 1.3 million in 2006.[25]

In the third quarter of 2006, home prices increased at an annualized rate of 3.45 percent, the lowest appreciation rate seen since the third quarter of 1998.[26] Historically, sharp drops in home prices often occur when there are other economic distresses. While employment and wages remain strong nationally, sharp declines in home prices is unlikely. Another positive factor that may help relieve the impact of a cooling housing market is the increase of commercial construction activities. So far, commercial construction activities have been picking up where residential construction left off.

Though at a slower pace, median selling prices of existing homes in both the State and the nation continued to rise in the first three quarters of 2006. The median price of new homes, however, declined during the same period (see Table 2). It is likely that homes price appreciation will continue to slow or decline in some areas through 2007.

Table 2

Home Price Appreciation Comparison
2004:Q3 to 2005:Q3 and 2005:Q3 to 2006:Q3
(Percent Change)

	OFHEO Home Price Index		Median Price of New Homes Sold	
	2004:Q3-05:Q3	2005:Q3-06:Q3	2004:Q3-05:Q3	2005:Q3-06:Q3
New York-White Plains	14.4	9.4	27.4	7.5
Nassau-Suffolk	13.1	6.8	6.8	2.3
Albany-Schenectady-Troy	15.4	7.9	N/A	N/A
Syracuse	7.9	7.1	N/A	N/A
Buffalo-Niagara Falls	6.8	3.7	(10.5)	3.5
Rochester	5.8	0.8	N/A	N/A
NYS	**12.7**	**6.5**	**N/A**	**N/A**
U.S.	**12.7**	**7.7**	**12.4**	**(2.0)**

Sources: Office of Federal Housing Enterprise Oversight (OFHEO); National Association of Home Builders.

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[25] Linda Rawls, "PBC Foreclosures Soar 29 percent in 2006," *Palm Beach Post*, January 19, 2007, http://www.palmbeachpost.com/business/content/business/epaper/2007/01/19/a1d_foreclose_0119.html.

[26] Office of Federal Housing Enterprise Oversight, "House Price Appreciation Slows Further," (table on p. 4 titled "OFHEO House Price Index for USA,") released November 30, 2006, http://www.ofheo.gov/media/pdf/2q06hpi.pdf.

Rapid home price appreciation over the last several years has reduced housing affordability in New York State. A wide disparity exists in housing affordability across New York. Over the past few years, some metropolitan areas in the State have become more affordable, while in other metropolitan areas, the opposite has occurred.

In 2005, less than 35 percent of all New York homeowners paid more than 30 percent of their income on housing expenditure, while almost half of all renters paid more than 30 percent of their income on rent payment.[27] At the regional level, about half of the renters in Long Island and New York City paid more than 30 percent of their income on housing expenditure. On the contrary, in Ithaca only 21 percent of homeowners paid more than 30 percent of their income on housing expenditure. Similarly, less than 40 percent of renters in Glens Falls paid more than 30 percent of their household income on rent payment (see Table 3).

Table 3

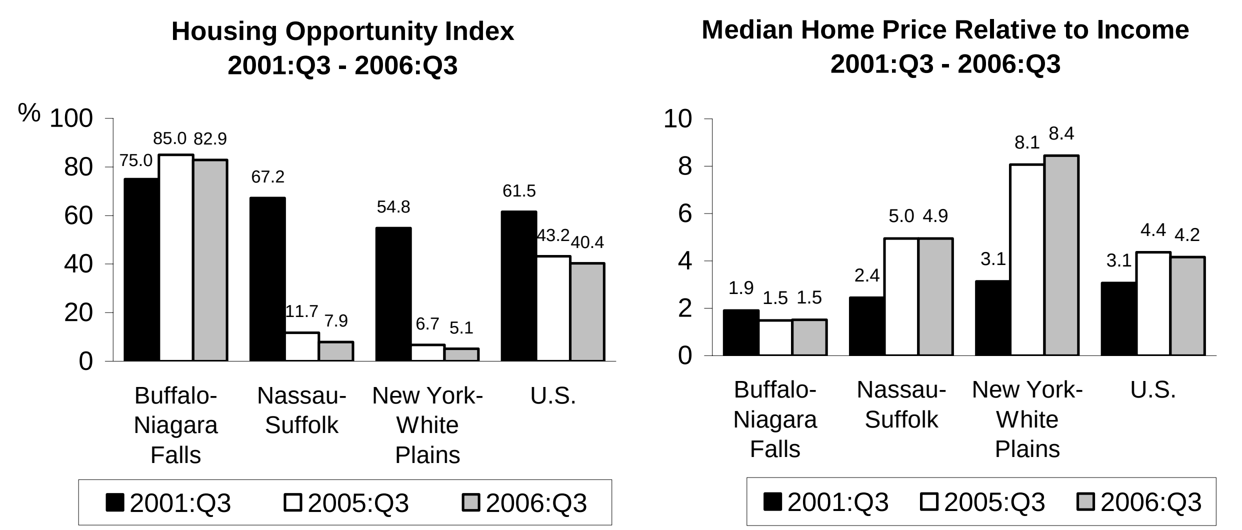
New York State Housing Expenditure as a percentage of Household Income

	Owner		Renter	
	Total Units	Percent of Units with Housing Costs Over 30% of Household Income	Total Units	Percent of Units with Housing Costs Over 30% of Household Income
Metropolitan Statistical Area				
Long Island	766,166	42.3	155,055	52.0
New York City	1,002,272	39.0	2,023,924	49.4
Poughkeepsie-Newburgh-Middletown	156,946	33.3	68,772	45.2
Kingston	45,281	30.5	23,120	52.1
Rochester	279,249	26.1	123,411	52.0
Glens Falls	36,848	25.5	13,299	39.5
Albany-Schenectady-Troy	225,352	25.0	112,310	40.0
Elmira	23,797	25.0	11,322	52.1
Buffalo-Niagara Falls	315,695	24.6	155,137	46.0
Utica-Rome	81,458	24.0	36,185	41.8
Binghamton	69,439	23.5	32,080	48.3
Syracuse	173,529	22.3	82,892	43.3
Ithaca	19,236	21.4	17,278	55.0
New York State	**3,936,378**	**32.9**	**3,178,053**	**48.3**
United States	**74,318,982**	**28.3**	**36,771,635**	**45.7**

Note: Housing costs for home owners includes mortgage payment; real estate taxes; fire hazard and flood insurance; utilities; and fuels. Housing costs for renters is gross rent.
Source: U.S. Census Bureau, 2005 American Community Survey.

[27] Housing is considered affordable when it costs no more than 30 percent of household income.

Since last year housing affordability remains relatively unchanged. The ratio of the median price of a new home divided by median household income in New York/White Plains rose from 3.1 to 8.1 from the third quarter of 2001 to the third quarter of 2005 before rising slightly to 8.4 in the third quarter of 2006. During the same period, the Housing Opportunity Index, which is defined as the share of homes sold in the area that would have been affordable to a family earning the median income (i.e., the total monthly payment is less than 28 percent of the monthly median household income), in the Buffalo-Niagara Falls area rose from 75.0 percent in the third quarter of 2001 to 85.0 percent in the third quarter of 2005, before dropping slightly to 82.9 percent in the third quarter of 2006 (see Figure 21).[28]



Source: National Association of Home Builders.

Figure 21

The negative impact of a cooling housing market has been widely debated. The slowdown of home prices may have a positive impact on local labor markets and the competitiveness of the region. Elevated home prices in the Long Island region is one of the possible causes of out-migration of young college-educated workers.[29] An increase in housing affordability may help persuade young people to stay in the area and stimulate more job growth in the region.

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[28] For more detail see the National Association of Home Builders, "What is the NAHB-Wells Fargo Housing Opportunity Index (HOI)?" September 1, 2005.

[29] Long Island Index, "Long Island Index 2006," 15, http://www.longislandindex.org/fileadmin/reports/INDEX2006a.pdf.

Government Spending

In constant dollars, federal government spending is expected to grow 1.7 percent in 2007 and 0.7 percent in 2008, after growing an estimated 2.0 percent in 2006 (see Figure 22).

Despite a decline in federal government employment growth throughout the forecast period, compensation expenditures are expected to continue to grow due to the growing cost of pay and benefits for military and civilian personnel. Defense spending, which has grown very rapidly in the past several years, is expected to increase further due to an expected increase of the U.S. military presence in Iraq.

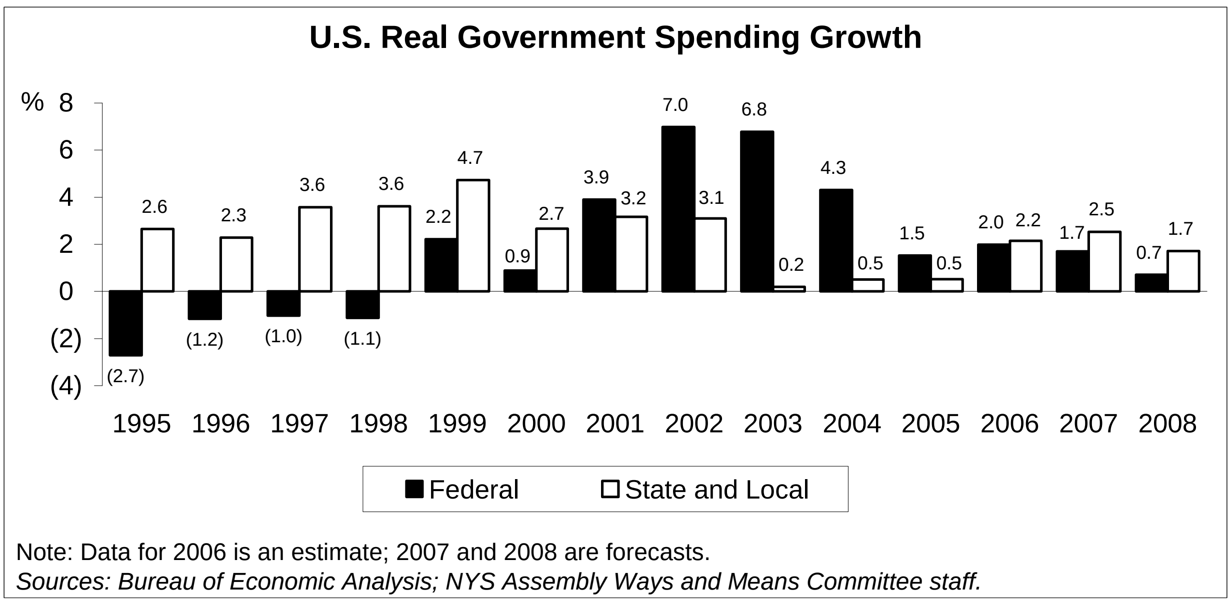


Figure 22

One of the major categories recently affecting nondefense spending is hurricane relief appropriations. Part of the slowdown from 2006 to 2007 is attributed to a reduction in the amount of hurricane-related spending due to a less extreme hurricane season in 2006. In 2006, appropriations related to hurricane relief for hurricane Katrina and other storms were still in the billions of dollars.

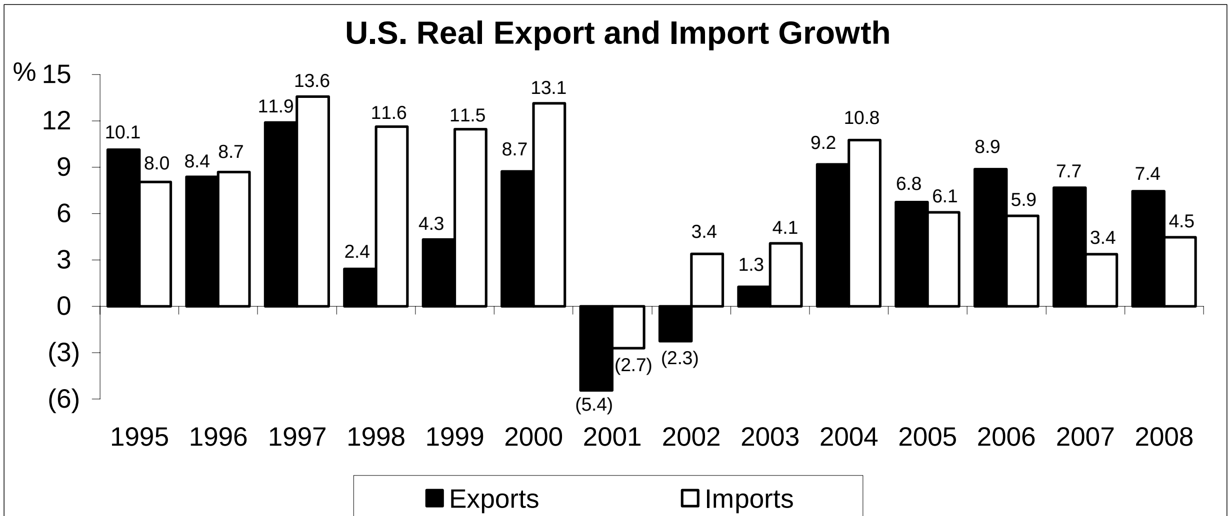
The fiscal year 2005-06 federal budget deficit was $247.7 billion, $71 billion less than prior fiscal year's deficit of $318.7 billion, and is the smallest deficit since fiscal year 2001-02. This improvement is largely attributed to very strong revenue growth, mostly from personal and corporate income taxes. The deficit, however, is unlikely to improve further in the next few years.

State and local government spending is expected to grow 2.5 percent in 2007 and 1.7 percent in 2008 in constant dollars. Investment spending in structures and information technology were the main drivers of the spending growth in 2006 and are expected to continue to be the main contributors in 2007.

Exports and Imports

The Assembly Ways and Means Committee staff forecasts that, in constant dollars, exports will grow 7.7 percent in 2007 and 7.4 percent in 2008, after rising 8.9 percent in 2006. Imports are forecasted to grow 3.4 percent year-over-year in 2007 and 4.5 percent in 2008, following 5.9 percent growth in 2006 (see Figure 23). The trade deficit rose from $58.1 billion in November to $61.2 billion in December 2006.[30] Approximately 30 percent of the goods deficit is with China. In part, this is due to the undervalued yuan. Since China abandoned its fixed exchange rate more than a year ago, the yuan has only appreciated 6.0 percent.

Net exports, defined as exports minus imports, have declined (becoming more negative) every year from 1995 through 2006, adversely affecting the exchange rate, external debt, and GDP. Net exports are likely to improve in 2007 and 2008. This improvement in net exports is a result of the strong demand from a steady economic growth around the world as well as the declining dollar.

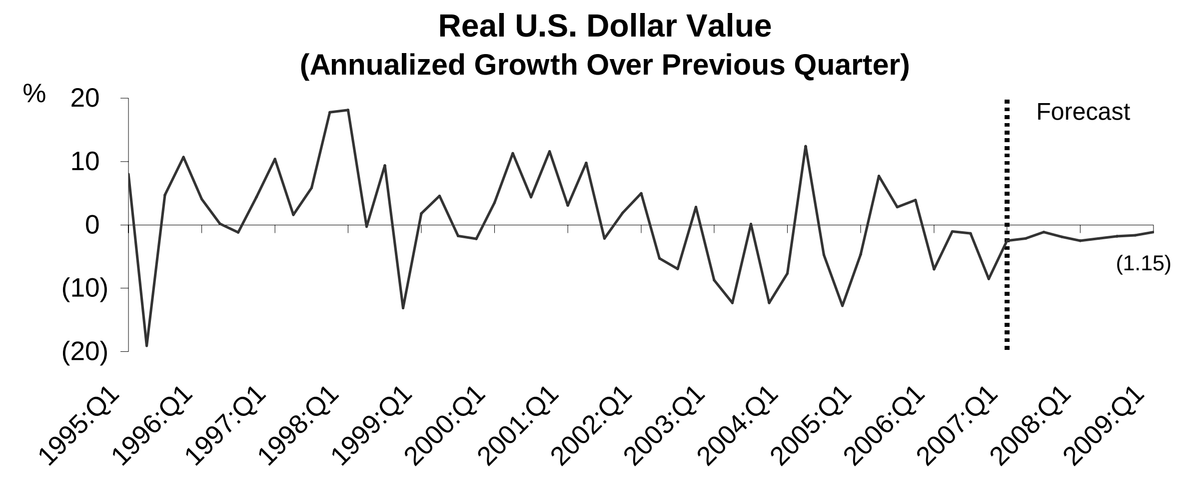


Note: Data for 2006 is estimated; 2007 and 2008 are forecasts.
Sources: Bureau of Economic Analysis; NYS Assembly Ways and Means Committee staff.

Figure 23

[30] U.S. Bureau of Economic Analysis, *U.S. International Trade in Goods and Services*, February 13, 2007.

The dollar is expected to decline further in 2007 and 2008 (see Figure 24). The decline of the dollar has helped to boost exports and reduce imports. However, concerns arise about the potential impact of the continual drop of the dollar's value on the world economy, especially on oil prices and the world financial market.[31] The dollar's decline can hurt the prices of United States assets. In addition, a declining dollar can cause increased inflation. This is partly because imported goods become more expensive. In addition, the increased prices of competing imports in dollars reduce the pressure on domestic manufacturers to keep prices down.



Note: The first forecast period is 2007:Q1.
Sources: NYS Assembly Ways and Means Committee staff; Federal Reserve Board of Governors.

Figure 24

The decline of the dollar is driven mainly by the budget deficit and the growing current account deficit, which reached a record high of $902.2 billion in the third quarter of 2006 (see Figure 25). Although the budget deficit improved in fiscal year 2006, it is likely to worsen in the next few years as the cyclical boost to revenues comes to an end.[32] Both the budget deficit and the weakening U.S. economy is expected to cause the dollar to continue to decline in 2007 and 2008.

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[31] Mark Drajem and Shamim Adam, "IMF Signals Risk of `Disorderly' Drop in U.S. Dollar," *Bloomberg.com*, September 12, 2006.

[32] Moody's Economy.com, *Précis Macro*, vol. 12, no. 7, October 2007.

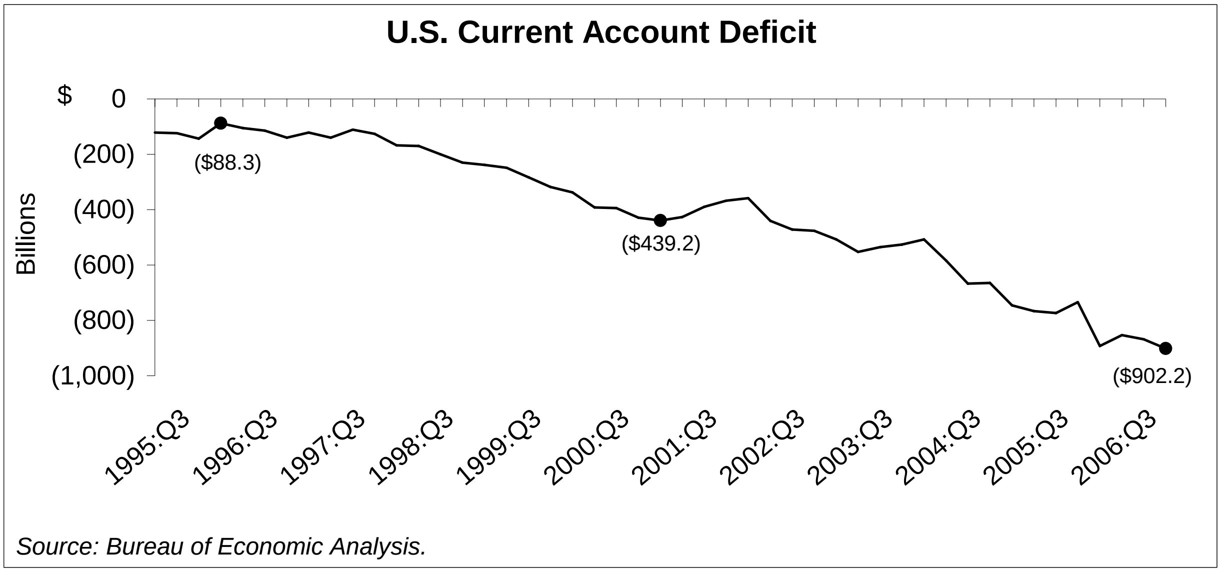

Figure 25

The world economy is expected to continue on a healthy growth path. World GDP growth is estimated to remain above 3.0 percent in both 2007 and 2008. According to a poll of forecasters taken by the *Economist*, developed countries are all expected to see positive growth in 2007.[33] However, according to the poll, most developed countries will experience slower growth in 2007 than in 2006. Europe is expected to grow 2.0 percent in 2007, while Canada, the largest trade partner for the United States, is expected to grow 2.3 percent. Japan is expected to continue its positive growth after years of stagnant economic performance with 2.1 percent in 2006 and 1.9 percent in 2007.

Much of the developing world is continuing to experience rapid growth. China has been the focus of considerable attention, with growth in the fourth quarter of 2006 at 10.4 percent. The Chinese government has been acting to slow growth to a more controlled pace. Some other Asian countries are also growing rapidly. Similarly, South American countries are also expanding rapidly, with 10.2 percent GDP growth in the third quarter of 2006 for Venezuela.

With economic activity worldwide expanding for nearly all of our significant trading partners, the global economy will be a positive stimulus for the United States economy.

Employment

The United States employment profile shows a relatively slower employment growth in 2007 and 2008 (see Figure 26). After growing an estimated 1.9 percent in 2006,

[33] "Economic and Financial Indicators," *Economist*, February 15, 2007.

employment is expected to grow 1.3 percent in 2007 due to the slowdown in overall economic growth. Employment will likely grow 1.5 percent in 2008 as economic growth is expected to return to near-trend growth. It is expected that there will be 1.7 million more jobs in 2007 compared to 2006.

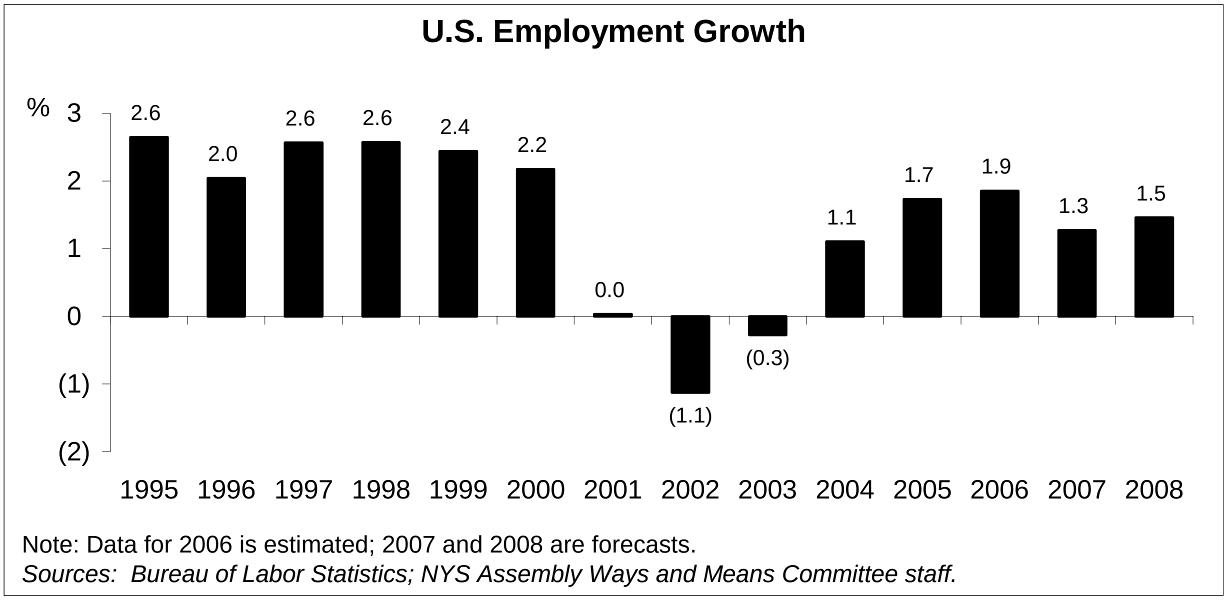

Figure 26

By sector, the highest percentage growth in employment in 2007 is expected to be in the professional services sector, the leisure and hospitality sector, and the education and health sector. All sectors except manufacturing are expected to experience an increase in employment in 2007 and 2008 (see Table 4). Service-producing employment is anticipated to show stronger gains than goods-producing employment, a trend that has been present throughout the current expansion period.

Employment in the manufacturing sector is expected to decline slightly in 2007 and 2008. Flat and declining manufacturing employment continues to be a concern in many areas of the country. The loss of factory jobs on a large scale has been especially prominent in the auto industry lately. For example, Ford has announced plans to cut 45,000 jobs and close several U.S. factories over the next four years. It had a record loss of $12.7 billion in 2006.[34] Currently the number two producer in the United States after General Motors, Ford may soon be surpassed in market share by Japanese rival, Toyota.[35]

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[34] "Ford Says 8,000 Workers Left in January," *CNNMoney.com*, February 7, 2007.

[35] General Motors' U.S. market share was 24.3 percent in 2006. Ford's market share was 16.4 percent compared to Toyota's 15.4 percent. See also AP: Detroit, "GM, Ford Report December U.S. Sales Slide," *MSNBC*, January 4, 2007, http://www.msnbc.msn.com/id/16454619.

Construction employment growth is expected to decline from 4.8 percent growth in 2006 to a mere 0.7 percent in 2007. This slowdown may be explained by the anticipation of further weakness in the residential construction sector. This weakness will be partially outweighed by continued strength in the non-residential construction sector.

Table 4

U.S. Employment by Sector
(Percent Change)

	Actual 2005	Estimate 2006	Forecast 2007	Forecast 2008
Total	**1.7**	**1.9**	**1.3**	**1.5**
Professional Services	4.1	4.5	3.4	3.5
Leisure & Hospitality	2.6	2.5	2.5	2.2
Education and Health	2.5	2.7	2.4	2.5
Mgmt. of Companies	2.0	2.8	2.1	2.3
Transp. & Utilities[4]	2.2	2.0	2.0	1.9
FIRE[3]	1.5	2.6	1.5	1.7
Other Services[2]	1.7	2.0	1.3	1.8
Wholesale Trade	1.8	2.3	1.3	1.6
Information	(1.8)	(0.2)	0.9	0.9
Government	0.9	0.8	0.8	0.7
Construction	5.2	4.8	0.7	1.6
Retail Trade	1.5	0.3	0.2	0.6
Manufacturing[1]	(0.3)	0.2	(0.6)	(0.2)

[1] Including Mining and Logging.
[2] Including Administrative, Support, and Waste Management Services.
[3] Financial activities including Finance, Insurance, Real Estate, Rental, and Leasing.
[4] Transportation, Warehousing, and Utilities.
Sources: Bureau of Labor Statistics, CES; NYS Assembly Ways and Means Committee staff.

Slower employment growth in the current forecast period may be explained by the slowdown in overall economic activity, but longer-term there have been structural changes to the economy that may lead to insights on slowing employment. Underlying gains in total factor productivity can account for the ability of firms to produce more with less increase in employment. Although there can be variation in productivity measures, a good part of the variation in labor productivity is cyclical: labor productivity typically falls during the initial stages of a recession, since output falls faster than employment in an economic slowdown; labor productivity also increases sharply after a recession since output recovers faster.

Personal Income

Personal income slowed to 5.2 percent in 2005 after an increase of 6.2 percent in 2004. Most of the major components of U.S personal income remained strong or grew faster in 2006 than in the previous years, resulting in a healthy 6.4 percent year-over-year growth in 2006. This involves strong growth in wages and salaries, dividends, and interest income.

Due to a slowdown in employment growth and overall economic activity, personal income growth will likely slow in 2007 and 2008, growing at 5.4 percent and 5.5 percent, respectively (see Figure 27).

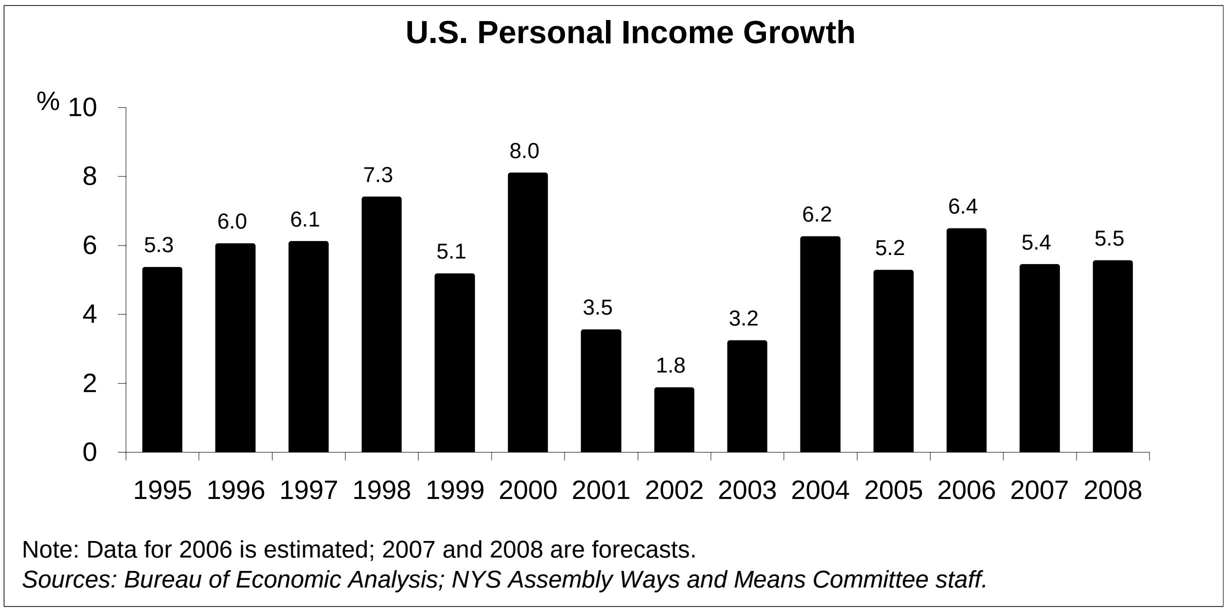

Figure 27

Wages and salaries income is the largest component of total personal income, accounting for around 55 percent. Due largely to a big surge in variable compensation (including cash bonuses and stock options exercised), this component grew 13.3 percent in the first quarter of 2006. It increased an estimated 6.6 percent year-over-year during 2006 after growing 5.1 percent during 2005. Wages and salaries income growth is expected to slow to 5.0 percent in 2007 as growth in both employment and wage rates are expected to slow from 2006. Wages and salaries income is forecast to grow 5.3 percent in 2008.

With a big jump in corporate profits, dividend income grew an estimated 11.3 percent in 2006, following 7.0 percent growth in 2005. As corporate profit growth is expected to slow in 2007 and 2008, however, dividend income also will slow to 10.4 percent in 2007 and 7.5 percent in 2008.

Personal interest income grew an estimated 7.7 percent in 2006 after two years of Federal Reserve interest rate hikes. With interest rates expected to remain relatively stable during 2007 and 2008, interest income growth is forecast to slow to 4.6 percent year-over-year in 2007 and further down to 4.3 percent in 2008.

With a relatively calm hurricane season and a resulting lack of any major aid money expected out of the federal government, transfer income growth slowed to an estimated 4.9 percent in 2006 compared to 7.0 percent in 2005. However, with economic growth expected to slow down and employment gain also likely to remain weaker, unemployment will likely rise throughout the forecast period. This will lead to an increase in personal unemployment insurance receipts. Medicare benefits will also continue to increase because of the new prescription drug plan. Together, these factors will account for faster growth in personal transfer income during 2007 and 2008 compared to 2006.

Prices

Increases in consumer and producer prices in 2004 were driven by volatile energy prices, and this continued into 2005 and 2006. A sustained increase in nominal oil prices led to high gasoline prices in 2005 and 2006.[36]

The core Consumer Price Index (CPI), which excludes more volatile items such as energy and food from the overall consumer price index, increased 2.1 percent in 2005 (see Figure 28). It further increased 2.4 percent in 2006. The gain in the core CPI was caused by underlying fundamentals that put upward pressure on the general price level. Productivity growth decelerated to 2.1 percent in 2006 and 2.3 percent in 2005 after growing 3.0 percent in 2004 and 3.7 percent in 2003. Unit labor costs for the U.S. nonfarm business sector also posted a significant increase in recent months. They accelerated to 3.2 percent in 2006 after rising 2.0 percent in 2005, a substantial jump from the 0.6 percent increase in 2004 and a 0.3 percent increase in 2003. As high energy prices have persisted longer than expected since 2003, companies have been increasingly stressed to pass part of the higher costs on to consumers. These fundamental forces have caused an increase in core CPI. Increasing import prices as a result of a declining U.S. dollar also have contributed to core CPI inflation.

[36] In 2005 dollars, the highest monthly price of the refiner acquisition cost of oil between January 1980 and October 2006 was in January 1981. On a monthly basis, real gasoline prices (2005 dollars) were highest in March 1981. See Energy Information Administration, *Short-Term Energy Outlook*, (November 2006), http://www.eia.doe.gov/emeu/steo/pub/fsheets/PetroleumPrices_files/frame.htm.

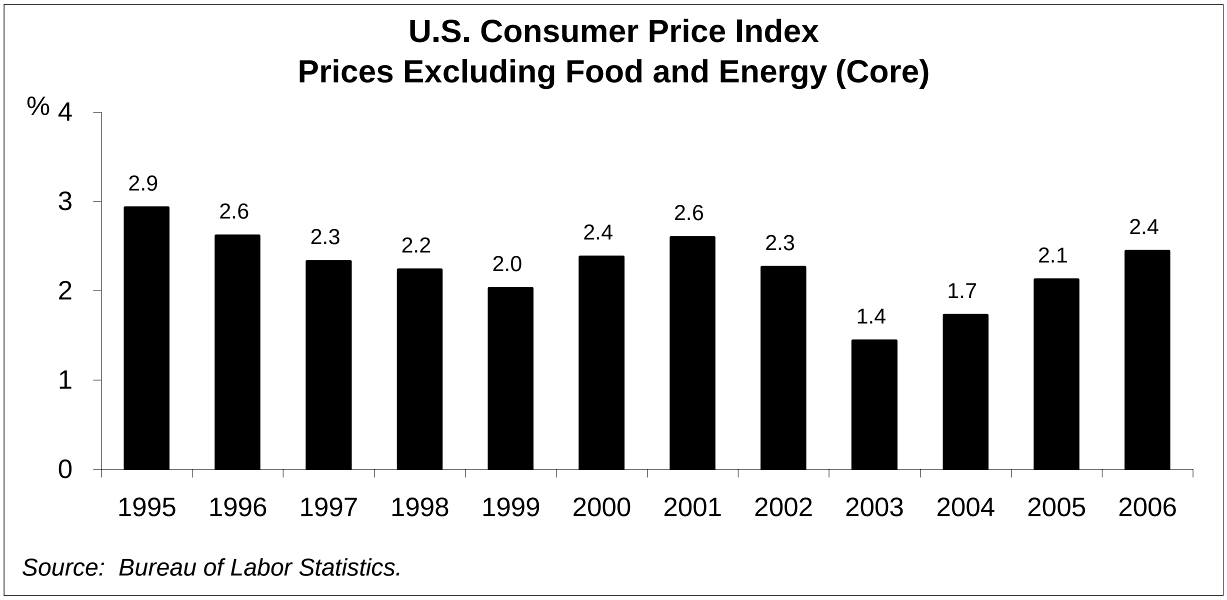

Figure 28

The general price level, as measured by the CPI, increased 3.2 percent year-over-year in 2006 after accelerating to 3.4 percent during 2005 from the 2.7 percent in 2004 (see Figure 29). However, as energy markets are expected to stabilize and economic growth is likely to soften to a below-trend rate in the course of the current forecast period, overall consumer price inflation will likely slow to 1.9 percent during 2007 and 2.4 percent in 2008.

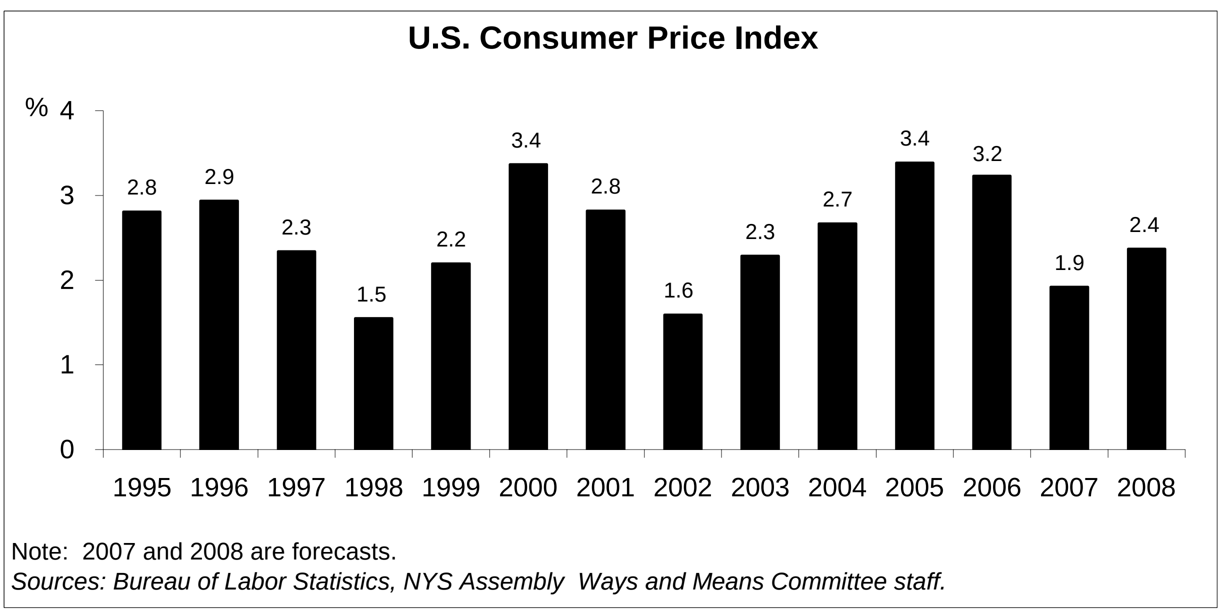

Figure 29

Energy Prices

Energy prices represent a critical issue for the United States economy, and remain one of the most volatile risk factors for the health of the economy. Current political and geographical considerations, as well as weather conditions (such as the possibility of hurricanes or a cold winter) add uncertainty to future energy prices, including prices of oil, gasoline, and natural gas.

Oil prices have fallen noticeably since the midsummer of 2006 as a result of concerns about the slowing economy, growing stockpiles, and the absence of a strong hurricane season.[37] The U.S. refiner acquisition cost of imported oil was $55.21 per barrel in December 2006, compared to $58.79 in September of 2005. The drop in the West Texas Intermediate (WTI) spot price for this time period was even more dramatic. However, this decline in prices may only be temporary as the Organization of the Petroleum Exporting Countries (OPEC) moves to stabilize prices and the market reacts to current events. Prices of crude oil and other energy commodities can move significantly on a daily basis, usually in response to current events. Some of the events that may have caused an impact on energy prices in the past several months include:

- OPEC has implemented supply cuts in order to stop prices from declining. The latest planned cut was 500,000 barrels as of February 1, 2007. This is in addition to the production cut of 1.2 million barrels per day as of November 1, 2006.[38] The Saudi Arabian oil minister has indicated that if current fundamentals hold, there will be no reason for the cartel to cut production further when they meet in March. However, the situation could change by mid-March, prompting further action by OPEC.[39]

- Weather-related events can have a significant impact on energy prices. In 2006, the hurricane season was mild and of little effect on energy prices. A heat wave in July 2006 however created higher electricity demand. Winter 2007 has so far been mild, helping to ease pressure and keep prices down. U.S. household heating expenditures this winter are predicted to average $862 compared to $948 last winter.[40]

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[37] London (Reuters): "Oil Falls Below $58," *CNNMoney.com*, November 2, 2006.

[38] Grant Smith, "Oil Declines to Six-Week Low in New York on Mild U.S. Weather," Bloomberg.com, January 4, 2007, http://www.bloomberg.com/apps/news?pid=20601101&sid=aGIvmsbMCmM4&refer=japan.

[39] Karen Elliott House, "Saudi Oil Minister Says Market is Balanced, Requires No Changes," *Wall Street Journal*, February 12, 2007, A13.

[40] "Energy Information Administration, *Short-Term Energy Outlook*, February 6, 2007.

- Nigerian oil output has been affected by unrest in the country. During 2006, militants forced the reduction of Nigerian oil output by about a quarter of their normal 2.5 million barrels per day.[41]

- On September 5, 2006, Chevron Corporation announced that it had successfully drilled for oil at record depths in the Gulf of Mexico. The oil field could hold as much as 15 billion barrels of oil and gas. This would boost United States reserves by 50 percent. However, the discovery may do little in the near future to impact prices, as production could take years to begin and the exact amount of oil there is unknown.[42]

- On August 6, 2006, BP announced the shutdown of part of the production from the Prudhoe Bay oil field in Alaska, which in total produces about 8 percent of the United States domestic oil.[43] The shutdown portion was reopened in late September 2006.

Rising energy prices present a concern for the overall economy because energy is required for all production. Households face both a direct impact (such as rising gasoline and home heating oil prices) and the possibility of an indirect impact (i.e., producers passing their higher energy costs to consumers in the form of higher prices on final products). Estimates for the impact of rising energy products on the economy as a whole are varied. Also, as energy efficiency continues to increase, impacts of swings in energy prices on the overall economy may be reduced. The Congressional Budget Office offered an analysis in July 2006 indicating that rising energy prices have reduced GDP by less than one-half of a percentage point per year between 2004 and 2006.[44] Falling energy prices would also impact GDP. A January 2007 study by Global Insight indicates that a drop of $10 in the WTI price would lead to a boost of 0.2 percentage point in GDP.

The price of oil (as measured by the U.S. refinery's average acquisition price of imported oil) has increased in the past several years due to many factors. These include supply constraints, dramatic growth in demand, weather-induced disasters, the War in Iraq, political unrest in oil producing countries, uncertainty in the market, and speculation on the part of investors. However, if the price of oil is adjusted for inflation, oil prices are not as high as in the early 1980s (see Figure 30).

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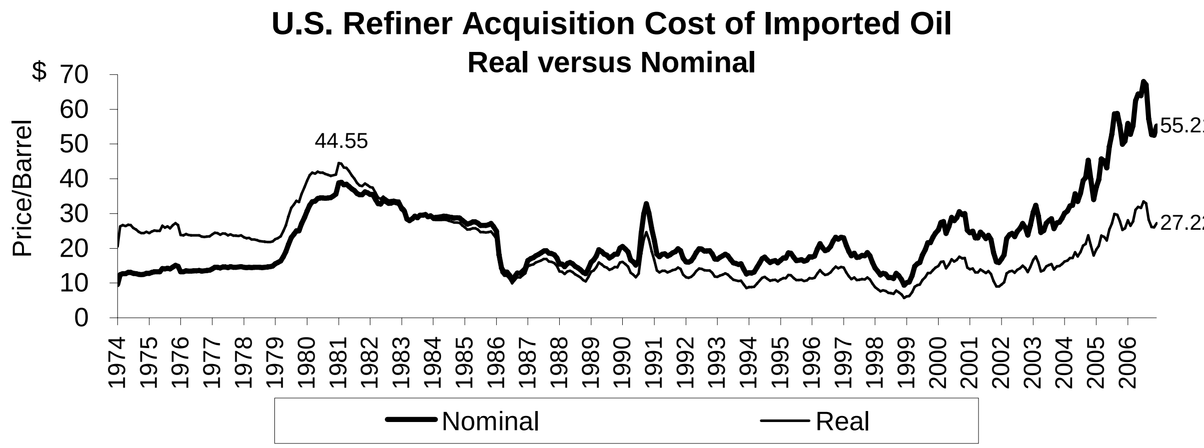
[41] AP: "Oil Prices Rise on Nigeria Worries," *Yahoo!News*, November 3, 2006.

[42] Paul Davidson, "Oil Field Find Could Raise U.S. Reserves by 50%," *USA Today*, September 6, 2006, http://www.usatoday.com/money/industries/energy/2006-09-05-oil-jack_x.htm?csp=N009.

[43] Energy Information Administration, *Short-Term Energy Outlook*, August 8, 2006, http://www.eia.doe.gov/pub/forecasting/steo/oldsteos/aug06.pdf.

[44] U.S. Congressional Budget Office, *Economic Effects of Recent Increases in Energy Prices*, July 2006.



Note: Real values are inflation-adjusted using CPI: All Urban Consumers 1982-84 = 100. Data is monthly through December 2006. The refiner acquisition cost of oil is a volume weighted average price of imported oils. It is generally about $2 less than the West Texas Intermediate price, which is commonly reported in the media.
Sources: Bureau of Labor Statistics; Energy Information Administration.

Figure 30

Along with crude oil, other energy prices in the United States have also been volatile. For example, in 2005 natural gas spot prices rose 49.3 percent and then fell in 2006 by 21.2 percent as a result of unusually mild winter temperatures. However, the level has doubled since 2000. Heating oil prices have also followed a general upward trend in the past few years with double-digit growth each year since 2002 (see Table 5). Electricity prices are estimated to remain at higher levels and possibly increase, depending on the impact of fuel prices and state energy policies.

Table 5

U.S. Energy Prices Annual Average						
		2002	**2003**	**2004**	**2005**	**2006**
Crude Oil - RAC	***Percent Change***	**7.8**	**17.0**	**29.8**	**36.0**	**20.4**
	Level	23.71	27.73	35.99	48.96	58.93
Crude Oil - WTI	***Percent Change***	**0.7**	**19.1**	**33.2**	**36.3**	**16.9**
	Level	26.12	31.12	41.44	56.49	66.02
Natural Gas	***Percent Change***	**(15.4)**	**64.2**	**7.3**	**49.3**	**(21.2)**
	Level	3.35	5.50	5.90	8.81	6.94
Heating Oil	***Percent Change***	**(9.6)**	**20.4**	**14.0**	**32.3**	**15.1**
	Level	1.13	1.36	1.55	2.05	2.36
Gasoline	***Percent Change***	**(6.3)**	**16.4**	**18.6**	**22.7**	**13.2**
	Level	1.34	1.56	1.85	2.27	2.57

Note: All levels are nominal. Oil prices are per barrel. The refiner acquisition cost (RAC) of oil is a volume weighted average price of imported oils. The RAC daily spot price is generally about $2 less than the West Texas Intermediate (WTI) spot price, which is commonly reported in the media. Natural gas figures are average of monthly Henry Hub Spot Price, dollars per thousand cubic feet; heating oil figures are for No. 2 heating oil, retail, dollars per gallon; gasoline prices are for retail, regular grade, dollars per gallon.

Source: Energy Information Administration.

Corporate Profits

Corporate profits on an economic basis have been steadily improving at a double-digit rate—for five years in a row—after plummeting 6.2 percent in 2001. Robust growth in productivity, among other factors, is believed to account for much of the recent continued improvement in corporate profits. Profits are estimated to record another solid gain in 2006, thanks to a 60.8 percent (annualized) surge in the first quarter. The gain was helped largely by strong economic growth in that quarter. As output growth is expected to slow, corporate profit growth will likely slow during the current forecast period from an estimated 21.0 percent in 2006 to 5.1 percent in 2007 and 5.6 percent in 2008 (see Figure 31).

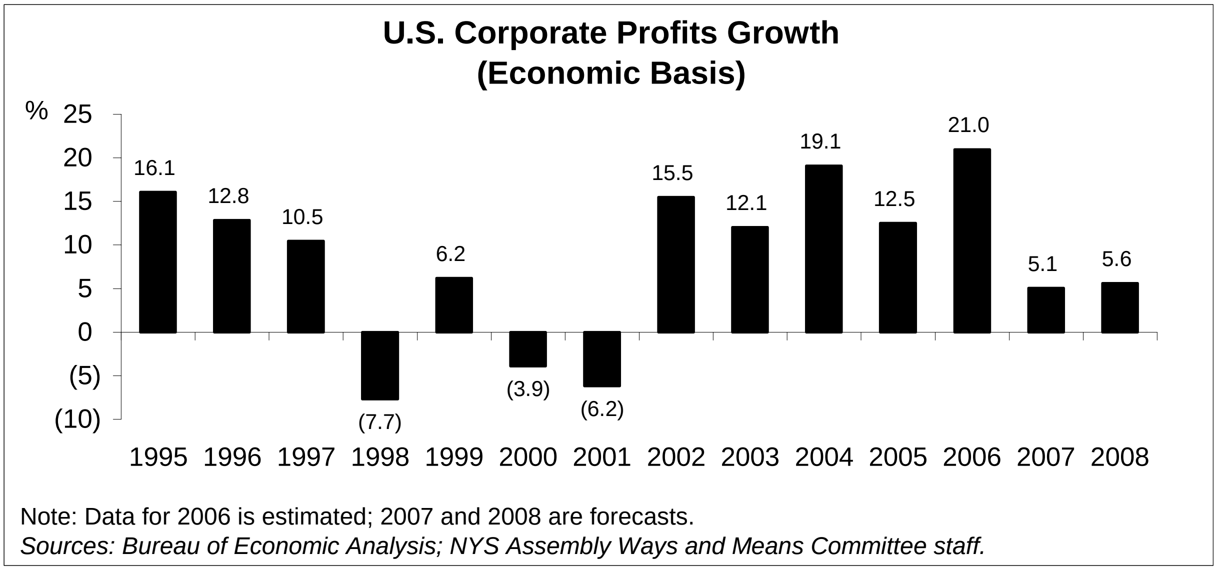


Figure 31

The share of corporate profits in national income rose to 14.1 percent in the third quarter of 2006 from the nine-year low of 8.0 percent seen in the third quarter of 2001, while the share of labor income (the sum of wages and salaries and employee benefits) fell to 63.9 percent from the 66.8 percent seen in the same quarter in 2001 (see Figure 32). Labor income share will likely gain in the near future as corporate profit growth is expected to slow, but the current importance of corporate profits in national income will likely remain mostly intact during the forecast period.

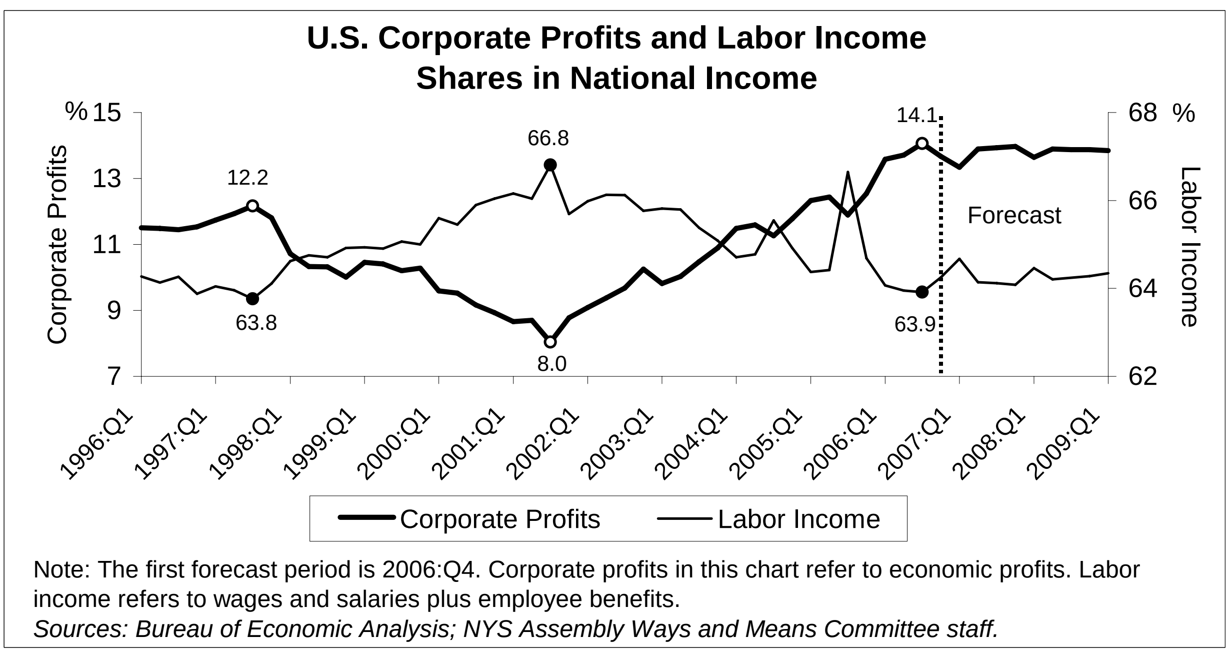
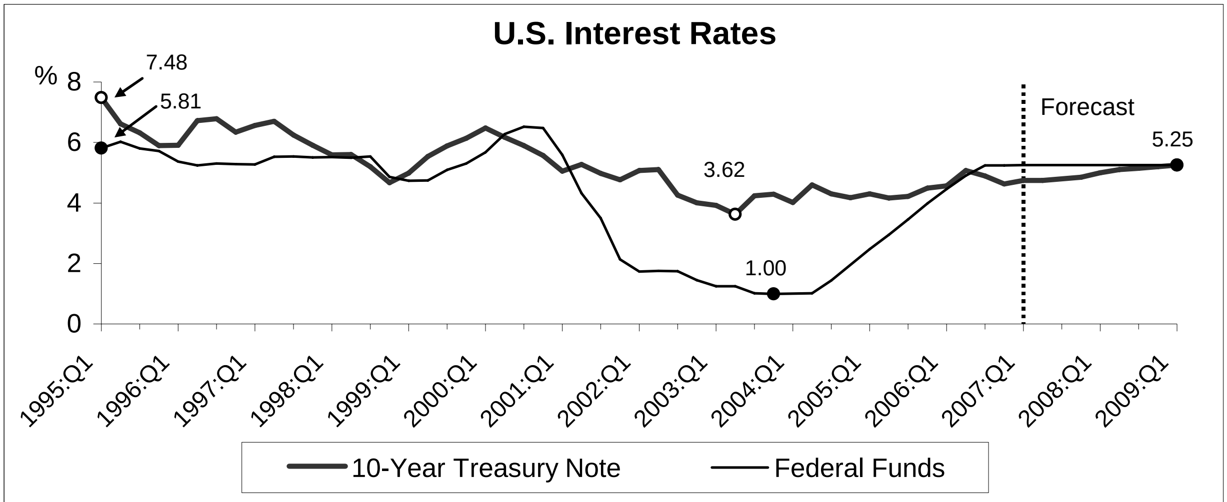


Figure 32

Interest Rates

With economic growth expected to slow and inflation to moderate, the Fed will likely refrain from raising rates any further. The current forecast assumes that the Fed will keep the short-term rate at the current level of 5.25 percent throughout the forecast period. The federal funds rate averaged 5.0 percent in 2006 and is expected to average 5.25 percent in 2007 and 2008. The three-month Treasury bill rate averaged 4.7 percent in 2006, and is expected to average 4.9 percent in 2007 and 5.0 percent in 2008. As the economy is expected to slow down, the bond market will become more attractive for domestic investors who seek a safer investment. Foreign investors have also become a large holder of U.S. Treasury bonds, looking for the safety and liquidity provided by those bonds. The 10-year Treasury note rate averaged 4.8 percent in 2006 and is expected to average 4.8 percent again in 2007 and 5.1 percent in 2008. By the fourth quarter of 2008, the federal funds rate will be 4.25 percentage points higher than its recent low of 1.0 percent in the fourth quarter of 2003, while the 10-year Treasury note rate will be 1.6 percentage points higher than its most recent low of 3.6 percent in the second quarter of 2003 (see Figure 33).

In the period between June 2004 and June 2006, the federal funds rate more than quadrupled, rising from 1.0 percent to 5.25 percent. This was the result of seventeen quarter-point increases implemented by the Federal Reserve. Before the first increase in June 2004, the federal funds rate had remained at an unusually low rate of 1.0 percent for a year. The federal funds rate had not been this low since 1961 using weekly data.



Note: The first forecast period is 2007:Q1.
Sources: Moody's Economy.com; NYS Assembly Ways and Means Committee staff.

Figure 33

The leadership of the Federal Reserve changed in February 2006. Initially, incoming Chairman Bernanke appeared to be taking a strong anti-inflationary stance, possibly at the risk of sustained solid economic growth. However, in August 2006 the Fed decided to stop raising the federal funds rate for the first time since 2004. In deciding whether to increase the federal funds rate in the future, the Federal Reserve must weigh the inflationary pressure (which is reduced by increasing rates) against the risk of a recession or stagnant growth (this risk is reduced by lowering rates).

The net effects of rising energy prices on inflation and the housing boom appear to have been factors in inducing the Fed to raise interest rates in the past. In recent months, economic growth has slowed, partly reflecting the cooling of the housing market. Inflationary pressures remain a concern. Moderating energy prices and a slow consumption spending growth, however, will likely ease this pressure over time. These two factors will likely keep the Fed from raising interest rates any further.

The yield curve has inverted during the last seven months. Historically, an inverted yield curve often precedes a recession. Hence, it is considered a leading indicator for a recession. The recent inverted yield curve may be a signal that short-term interest rates may have increased sufficiently and a recession has become likely. However, this should not be of overly concern since the greater contribution points to foreign factors rather than domestic. The recent inverted yield curve is due to the decline in the long-term interest rate, which is caused in part by high foreign demand for U.S. debt that leads to high bond prices and low yields.

Stock Market

Using yearly average values, the S&P 500 Index increased 17.3 percent year-over-year in 2004 and 6.8 percent in 2005 following annual declines for three years straight in 2001, 2002, and 2003.[45] Healthy corporate profits and dividend income have supported further improvement in the corporate equity market in 2006, especially with the expectations that the Fed may have stopped raising interest rates for now. The S&P 500 increased 8.6 percent in 2006. Although corporate profit growth is likely to slow in 2007 and 2008 compared to 2006, stable inflation and interest rate outlook will help to sustain the stock market. The S&P 500 is expected to grow 9.2 percent in 2007 and 6.0 percent in 2008.

After rising rapidly throughout most of the 1990s and into 2000, stock prices, as measured by the S&P 500 Index, declined sharply from late 2000 until early 2003. The

[45] This method of comparison is used to be consistent with other growth rates cited in this report. However, yearly growth rates for the stock market are often cited using year-end values rather than yearly averages.

decline took away about half of the stock price gains experienced since 1990. Since the first quarter of 2003, stock prices have generally been rising, and the S&P 500 is expected to return to its former peak of 1,476 reached in the third quarter of 2000 during the second quarter of 2008 (see Figure 34).

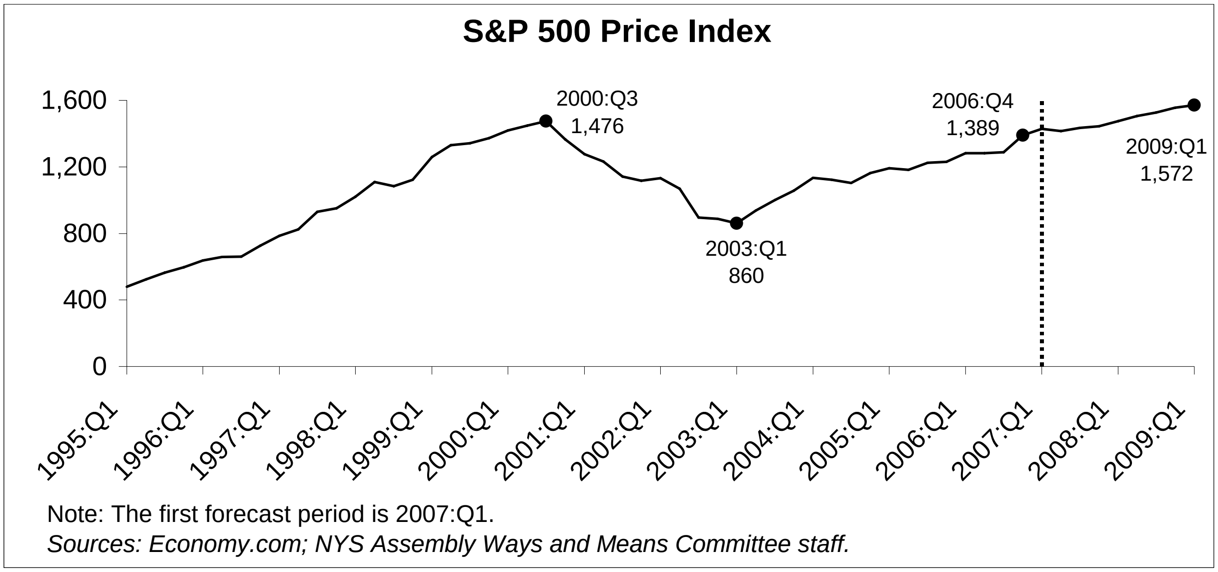
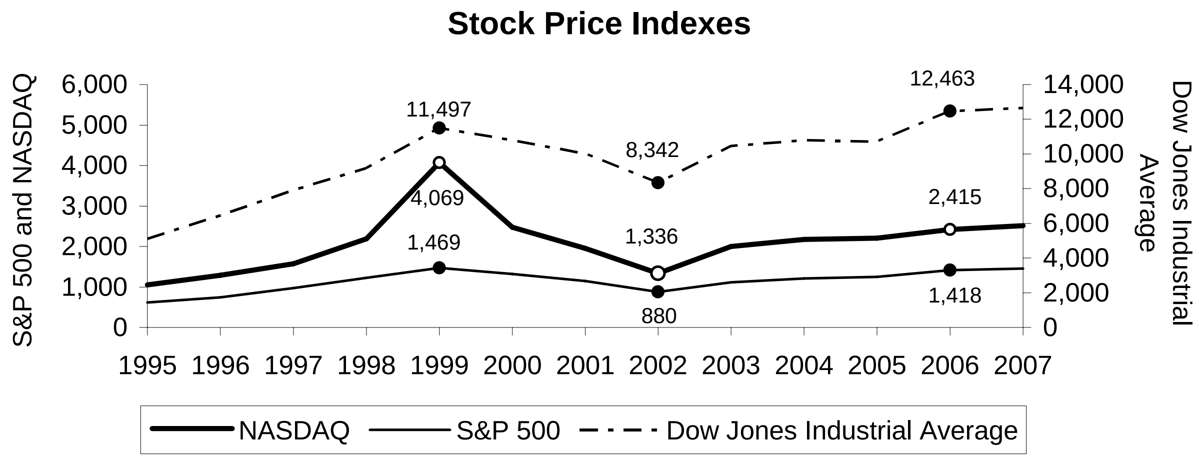


Figure 34

The NASDAQ and Dow Jones Industrial Average (DJIA) have shown trends similar to the S&P 500. Based on year-end price, all three markets peaked in 1999 and bottomed out in 2002.[46] Though the pattern was similar, NASDAQ had a much more pronounced peak and trough, consistent with the higher volatility of this market which is heavily weighted towards growth and technology stocks. The S&P 500 is well on its way towards its prior peak, DJIA has already surpassed its previous peak, while NASDAQ remains at only about 60 percent of its peak value (see Figure 35).

[46] The 2000 peak in the S&P 500 discussed previously was based on quarterly data. However, since stock prices started declining in the first half of 2000, the annual average price was higher in 1999 than in 2000.



Note: Data for 2007 is February 23 day-end index value.

Sources: Securities Industry and Financial Markets Association; Wall Street Journal (February 23 day-end index values).

Figure 35

United States Forecast Comparison

The Assembly Ways and Means Committee staff forecast for overall national economic growth in 2007 is 2.6 percent. It is 0.2 percentage point lower than the forecast of Macroeconomic Advisers and 0.2 percentage point higher than the Division of the Budget. The forecast is 0.1 percentage point lower than Blue Chip, Moody's Economy.com, and Global Insight.

Table 6

U.S. Real GDP Forecast Comparison
(Percent Change)

	Actual 2005	Estimate 2006	Forecast 2007	Forecast 2008
Ways and Means	3.2	3.3	2.6	3.1
Blue Chip Consensus	3.2	3.4	2.7	3.0
Division of the Budget	3.2	3.3	2.4	3.0
Moody's Economy.com	3.2	3.4	2.7	3.2
Macroeconomic Advisers	3.2	3.4	2.8	3.2
Global Insight	3.2	3.4	2.7	3.0

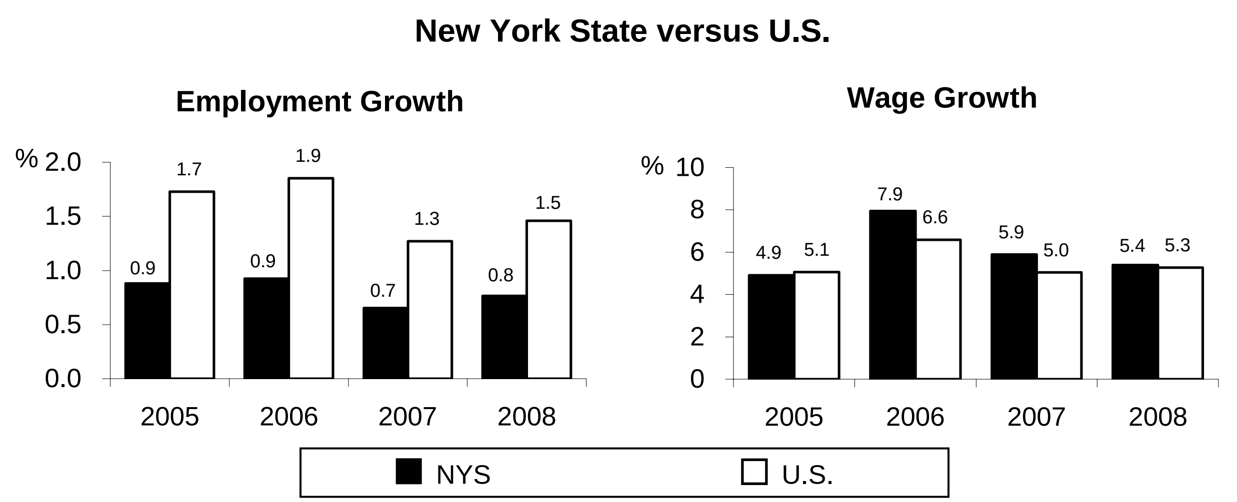
Sources: NYS Assembly Ways and Means Committee staff; Blue Chip, February 2007; New York State Financial Plan Projections, 2007-08 Executive Budget Supplemented for 21-Day Amendments, 2006-07 through 2010-11, February 21, 2007; Moody's Economy.com, February 2007; Global Insight, February 2007; Macroeconomic Advisers, February 2007.

The Assembly Ways and Means Committee staff forecast for overall national economic growth in 2008 is 3.1 percent. This is 0.1 percentage point higher than Blue Chip, the Division of the Budget, and Global Insight. It is 0.1 percentage point lower than both Moody's Economy.com and Macroeconomic Advisers.

NEW YORK STATE FORECAST

The New York State economy will continue to benefit as the national economy expands. In 2006, State employment grew an estimated 0.9 percent, slower than most years in the 1990s. On the other hand, State wages grew an estimated 7.9 percent in 2006, the second fastest annual growth since 1988. As Wall Street economic activity is expected to remain robust in 2007 and 2008, wages will likely continue to grow solidly, although at a slower rate than in 2006 (see Figure 36).

New York State employment will grow slower than national employment in 2007 and 2008. Gains in State employment will be concentrated in service sectors; however, in many sectors the State will grow slower or decline more than the corresponding sector in the nation. For example, in 2007 New York State manufacturing employment is forecast to decline 2.8 percent compared to a decline of 0.6 percent in the nation. This is not a new phenomenon as New York State growth rates in manufacturing have historically been lower than in the nation. This pattern is also present in other industries, most notably leisure and hospitality, wholesale trade, and other services.



Note: Data for 2006 is estimated; 2007 and 2008 are forecasts.
Sources: NYS Department of Labor, QCEW; Bureau of Economic Analysis; NYS Assembly Ways and Means Committee staff.

Figure 36

New York will also gain from a positive securities industry outlook. Although industry employment is only expected to return to its 2001 peak in the second half of 2008, growth in the industry will continue to contribute to the economic growth of the State.

Employment

In 2006, New York State accounted for approximately 6.3 percent of total United States employment. The State ranks third in the size of employment, behind California and Texas. However, New York lags these other large employment states in terms of employment growth. New York's employment growth in 2006 was ranked 40th (see Table 7). Employment growth in upstate New York was slower than that of the rest of the State.

Table 7

2006 Employment Growth and Share of National Employment by State

Geography	Employment Growth		Share of Total U.S. Employment	
	Growth	Rank	Share	Rank
United States	**1.8**	**-**	**100.0**	**-**
Top Ten				
Nevada	5.3	1	0.9	32
Arizona	4.9	2	1.9	20
Idaho	4.6	3	0.5	41
Utah	4.6	4	0.9	33
Wyoming	4.2	5	0.2	51
Florida	3.2	6	5.9	4
Oregon	3.2	7	1.3	27
Washington	3.1	8	2.1	16
Montana	3.0	9	0.3	46
New Mexico	2.7	10	0.6	37
Bottom Twelve				
New York	**0.9**	**40**	**6.3**	**3**
New Jersey	0.9	41	3.0	10
Vermont	0.8	42	0.2	50
Massachusetts	0.7	43	2.4	13
Indiana	0.7	44	2.2	14
Connecticut	0.6	45	1.2	28
Kansas	0.5	46	1.0	31
Ohio	0.4	47	4.0	7
Rhode Island	0.4	48	0.4	44
Maine	0.3	49	0.5	43
Michigan	(0.4)	50	3.2	8
Louisiana	(5.0)	51	1.3	26

Note: This data may differ from QCEW data usually used by the NYS Assembly Ways and Means Committee, as it is more timely and may be revised, possibly significantly. Rankings are based on two decimal places.
Source: Bureau of Labor Statistics, CES.

New York State employment grew at an average rate of 0.8 percent per year during 1995-2005, slower than the national average growth rate of 1.3 percent per year. The regions with the fastest growth in employment during this period were the Mid Hudson and Long Island regions, which grew at 1.3 and 1.2 percent per year respectively. Employment growth in New York City and in all upstate regions, except for the Capital region, was slower than the State employment growth (see Figure 37).

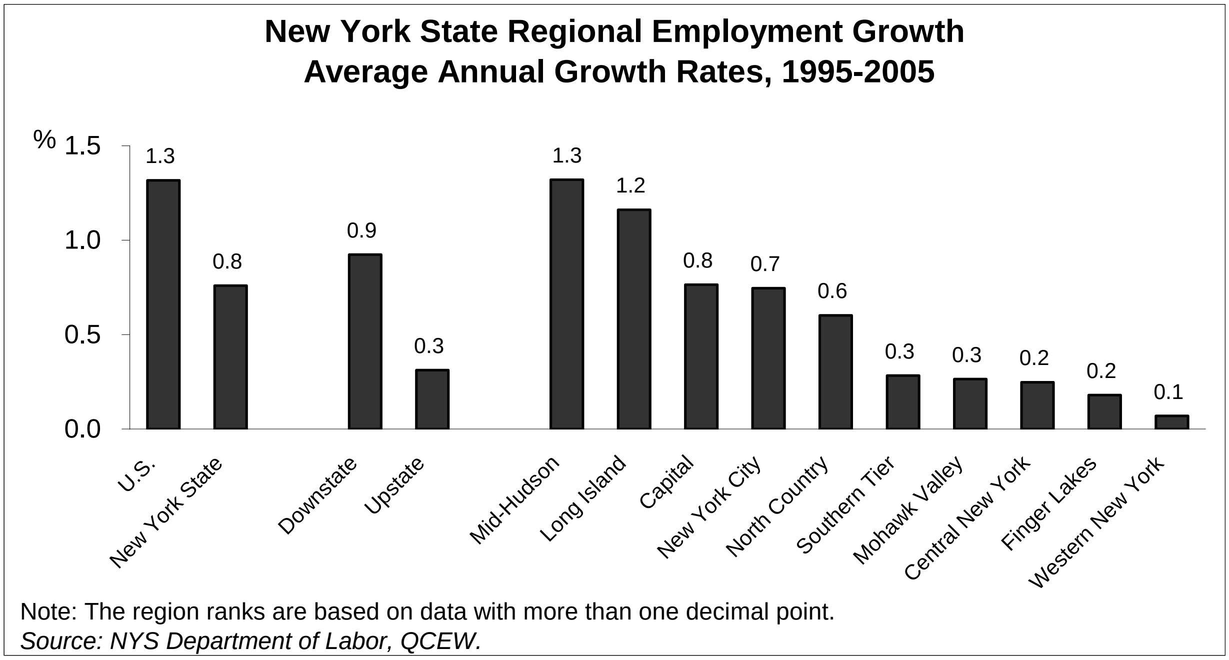


Figure 37

In 2007, New York State employment is expected to grow 0.7 percent, compared to 0.9 percent in 2006. As in the nation, the rate of growth of employment in New York has stabilized. However, the rate of State employment growth is expected to be lower than that of the nation, reflecting a lower long-run rate of growth. Manufacturing job losses are expected to continue in 2007 and 2008 at a similar rate as in 2006. The slow rate of growth of government and construction employment (due to the slowdown in residential construction) will also affect employment growth in 2007 (see Table 8). The largest employment gains are expected to be in education and health: this sector is expected to generate almost half of the 55,000 State employment gain in 2007.

The sectoral composition of job gains in 2007 is expected to be similar to that of 2006. The largest employment gains (in levels) will be in education and health, professional services, and securities. The stable rate of employment growth reflects both business expansion and growing consumer spending. Though manufacturing and construction employment is expected to decline in 2007, employment in the information sector is expected to grow.

Table 8

New York State Employment by Sector (Percent Change)				
	Actual 2005	Estimate 2006	Forecast 2007	Forecast 2008
Total Employment	**0.9**	**0.9**	**0.7**	**0.8**
Mgmt. of Companies	2.2	4.2	3.1	3.3
Professional Services	2.9	4.2	3.0	3.0
Transp. & Utilities[2]	1.1	2.0	1.7	1.6
Education & Health	1.5	1.5	1.5	1.6
FIRE[1]	1.7	1.7	1.4	1.5
Leisure & Hospitality	1.0	0.7	0.7	0.8
Other Services[3]	1.5	0.2	0.4	0.6
Construction	1.0	2.8	0.4	0.8
Information	(0.1)	0.4	0.3	0.3
Retail Trade	1.3	0.0	0.3	0.8
Government	0.2	(0.0)	0.2	0.2
Wholesale Trade	(0.2)	(0.1)	(0.3)	0.3
Manufacturing[4]	(2.4)	(2.4)	(2.8)	(2.3)

[1] Financial Activities including Finance, Insurance, Real Estate, Rental, and Leasing.
[2] Transportation, Warehousing, and Utilities.
[3] Including Administrative, Support, and Waste Management Services.
[4] Including Mining.

Sources: NYS Department of Labor, QCEW; NYS Assembly Ways and Means Committee staff.

Table 9 shows the sectoral rates of employment growth in the past year in each region. Employment increased in both upstate and downstate regions, though the rates of expansion of the sectors show regional variations. For example, employment in the construction sector grew 4.3 percent in the New York City from the second quarter of 2005 to the second quarter of 2006, whereas the upstate rate of growth in the same sector was 2.6 percent. Similarly, professional services employment grew 5.8 percent in New York City from the second quarter of 2005 to the second quarter of 2006, while the rate of growth of employment in the same sector in the New York City suburbs and upstate New York was 2.2 percent. Employment was lost in the manufacturing sector in the same period in all regions, however, manufacturing represents a larger share of total upstate employment than total downstate employment.[47]

[47] In 2005, manufacturing employment made up 4.7 percent of downstate employment and 12.2 percent of upstate employment. Manufacturing employment is 7.8 percent of total New York City employment.

Table 9

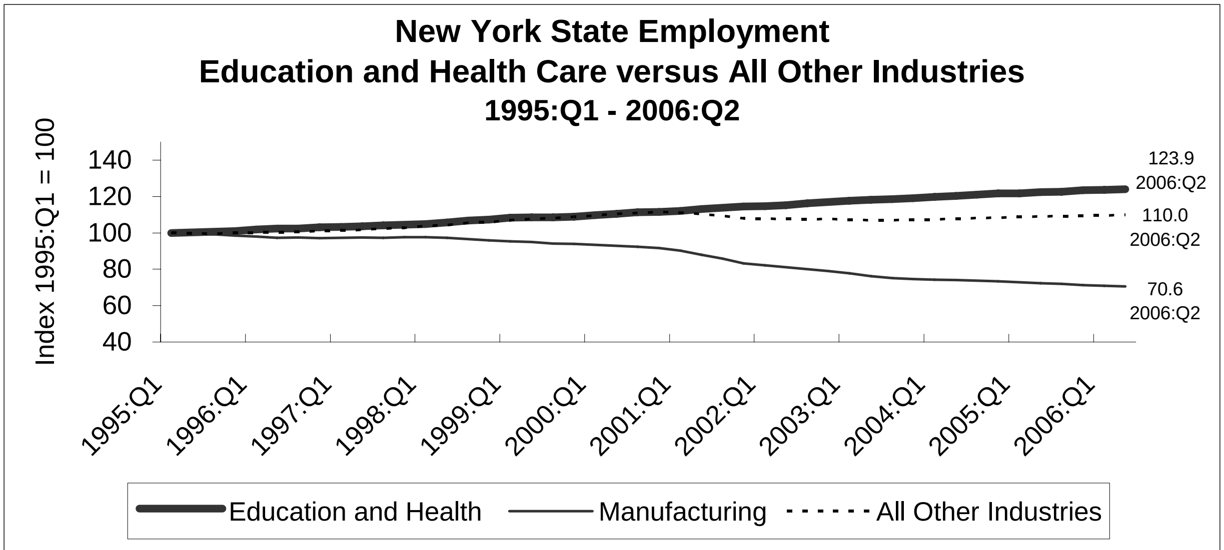
New York State Employment Change 2005:Q2 to 2006:Q2 (Percent Change)				
	New York State	Downstate		Upstate New York
		New York City	NYC Suburbs	
Total	**1.0**	**1.9**	**0.5**	**0.1**
Professional Services	4.2	**5.8**	2.2	2.2
Mgmt. of Companies	4.1	2.6	3.0	**7.6**
Construction	3.8	**4.3**	3.9	2.6
Transportation and Utilities[3]	2.1	**4.2**	(0.8)	1.7
FIRE[2]	1.9	**2.5**	(1.1)	1.5
Education and Health	1.5	**2.5**	0.8	0.3
Leisure and Hospitality	0.7	**2.2**	(0.6)	(0.1)
Wholesale Trade	0.2	0.8	**1.0**	(1.6)
Information	0.2	**2.0**	(1.7)	(3.7)
Retail Trade	(0.0)	**1.8**	(0.8)	(0.8)
Other Services[1]	(0.1)	(0.1)	**1.3**	(0.0)
Government	(0.1)	(0.3)	**0.3**	(0.3)
Manufacturing[4]	(2.1)	(6.6)	(1.4)	**(0.8)**

Note: Bolded sector numbers are largest in each sector.
[1] Including Administrative, Support, and Waste Management Services.
[2] FIRE includes Finance, Insurance, Real Estate, Rental, and Leasing.
[3] Transportation, Warehousing, and Utilities.
[4] Including Mining.
Source: NYS Department of Labor, QCEW.

The largest regional job gain was in New York City but there were also notable job gains in the New York City suburbs, while employment in the upstate region stayed flat. In all regions, the largest employment level increase was in the education and health sector. While most sectors lost jobs during the economic downturn, the rate of job growth in this sector was not affected much by the economic downturn. Employment in the education and health sector has been steadily increasing since the 1980s. Health employment rose an average of 2.5 percent annually between 1980 and 2000 and continued to increase in the recent years, while at the same time total employment in the rest of the economy remained relatively stable (see Figure 38).[48] This persistent employment gain was caused by both the cyclical and the structural change in the economy from industrial to service sectors. In contrast to the manufacturing sector, which has been declining since the 1980s, the health

[48] Ronnie Lowenstein, "The Health Sector's Role in New York's Regional Economy," *Current Issues in Economics and Finance*, vol. 1, no. 5, Federal Reserve Bank of New York, August 1995.

industry is the only sector that showed a significant structural gain during the 2001 economic downturn.[49]



Source: NYS Department of Labor, QCEW.

Figure 38

The opposite has occurred in the manufacturing sector. Manufacturing employment in both New York and the nation has experienced substantial job losses over the past decade. However, manufacturing employment in the State declined much faster than in the nation. In New York State, manufacturing employment declined by almost 50 percent between 1990 and 2005. From 1995 to 2005, manufacturing employment in the State fell by 227,200, an average annual loss of more than 3.0 percent compared to less than a 2.0 percent decline nationally.

Much of the long-term decline in the manufacturing sector has been influenced by both a structural shift in the economy as well as some economic factors. These factors include an increase in productivity through the use of laborsaving technologies in production, competition from foreign producers, increases in employee benefit costs, changes from permanent employment to temporary employment, and a shift in demand from manufacturing to services goods.[50] Part of the decline in demand for these goods may also have contributed to the excessive build-up in business assets in these goods in the 1990s. One sector that was particularly hard hit from this decline is the auto industry,

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[49] Erica L. Groshen, Simon Potter, and Rebecca J. Sela, "Economic Restructuring in New York State," *Current Issues in Economics and Finance*, vol. 10, no. 7, Federal Reserve Bank of New York, June 2004.

[50] U.S. Congressional Budget Office, *Economic and Budget Issue Brief*, "What Accounts for the Decline in Manufacturing Employment?," February 18, 2004, 3, http://www.cbo.gov/ftpdocs/50xx/doc5078/02-18-ManufacturingEmployment.pdf.

where several automakers plan to either cut back on production and employment over the next few years or have already done so.

In 2006, the estimated rate of manufacturing job loss in New York State was somewhat lower than in 2005. In the forecast period, national manufacturing employment is expected to decline slightly, while job losses in the State are expected to continue at more than 2 percent each year. Though some of the structural and cyclical job losses were similar for both the State and the nation, in New York the structural job losses will be much larger than the cyclical gains over the next few years due to a continuing decline in the manufacturing industries prevalent in New York State relative to that of the nation.

Securities industry employment in New York is estimated to have grown 4.9 percent in 2006. It is forecast to grow 3.7 percent in 2007 and 4.0 percent in 2008. This follows a sharp decline during 2002 and 2003 (see Figure 39). Growth for the industry turned positive in the first quarter of 2004 and is expected to remain strong for the entire forecast period. However, 2007 employment will still be slightly lower than its 2001 peak. Securities industry employment will grow slightly slower in the nation than in New York State, averaging 3.8 percent in 2006, 3.5 percent in 2007, and 3.6 percent in 2008.

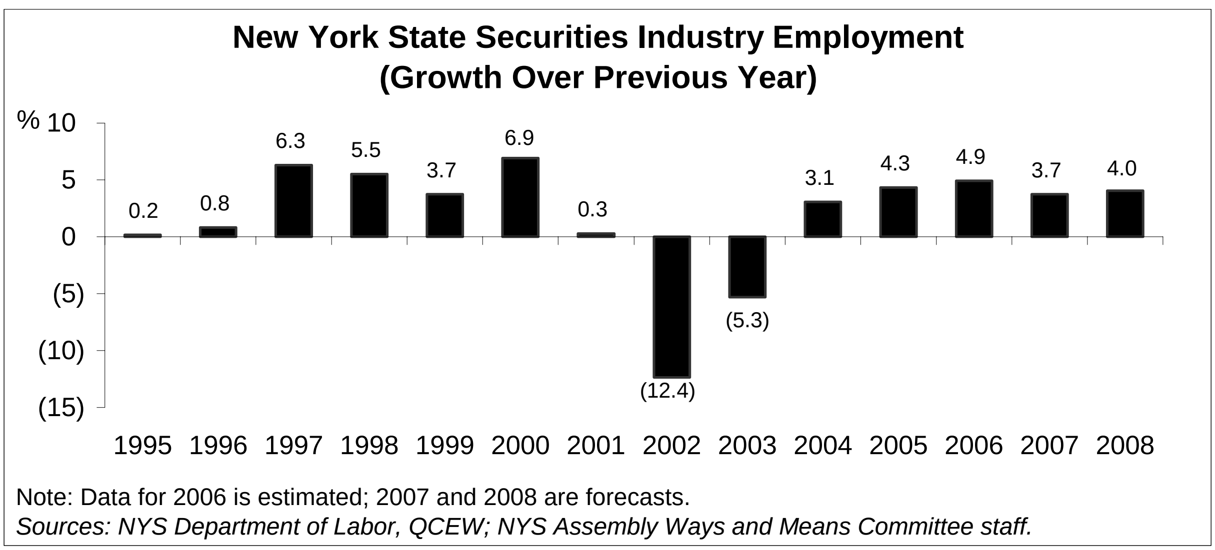
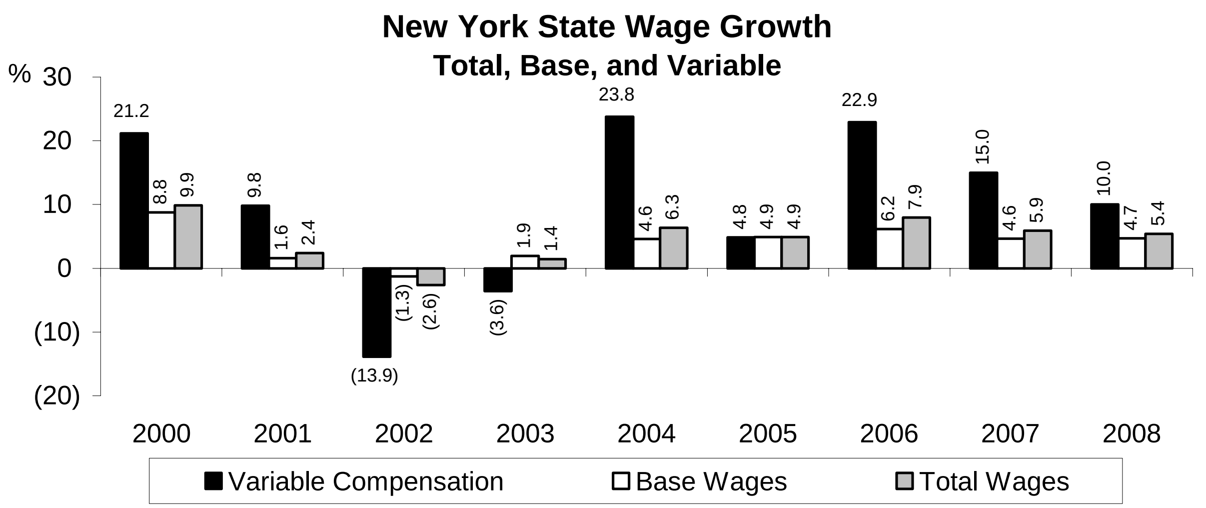


Figure 39

Wages

Wage growth in New York State is expected to be 5.9 percent in 2007, following an estimated 7.9 percent in 2006 (see Figure 40). Variable compensation is expected to continue to show stronger growth than base wages throughout the forecast period. In 2007, base wages are forecast to grow 4.6 percent, compared to 15.0 percent growth in variable compensation. In 2008, total wages are expected to grow 5.4 percent. This lower growth than in 2007 is as a result of slower variable wage growth in 2008 compared to 2007. Base wage growth will also slow from 2006 due to moderating inflation and slower growth in employment (see Table 10).



Note: Data for 2006 and earlier are estimates; 2007 and 2008 are forecasts. Base wages and variable compensation sum to total wages, which are derived from NYS Department of Labor QCEW data.
Sources: NYS Department of Labor, QCEW; NYS Assembly Ways and Means Committee staff estimates.

Figure 40

Table 10

Personal Income, Wages, and CPI					
New York State					
		Actual 2005	**Estimate 2006**	**Forecast 2007**	**Forecast 2008**
Personal Income	***Percent Change***	**4.1**	**6.9**	**5.8**	**5.4**
	Level Change	29.8	52.2	46.9	45.6
Total Wages	***Percent Change***	**4.9**	**7.9**	**5.9**	**5.4**
	Level Change	20.2	34.4	27.5	26.7
Base Wages	***Percent Change***	**4.9**	**6.2**	**4.6**	**4.7**
	Level Change	18.1	23.9	19.1	20.2
Variable Compensation	***Percent Change***	**4.8**	**22.9**	**15.0**	**10.0**
	Level Change	2.1	10.5	8.4	6.5
CPI	***Percent Change***	**3.9**	**3.8**	**2.4**	**2.7**

Note: Level changes in income and wages are in billions of dollars.
Sources: Bureau of Economic Analysis; NYS Department of Labor, QCEW; Bureau of Labor Statistics; NYS Assembly Ways and Means Committee staff.

Stronger wage growth may occur even in the absence of stronger employment growth, due to the composition of the New York State economy. The State economy's strong concentration in the securities industry, which has high wages and large bonuses at times, helps to bolster wage growth. This concentration helps contribute to the volatility in total wages because the sector has a large amount of variable compensation. Generally, base wages in the State exhibit a more stable pattern. In recent years, base wage growth has been helped by growth in both employment and average base wages (see Figure 41). Productivity gains have also played a role in strengthening wages.

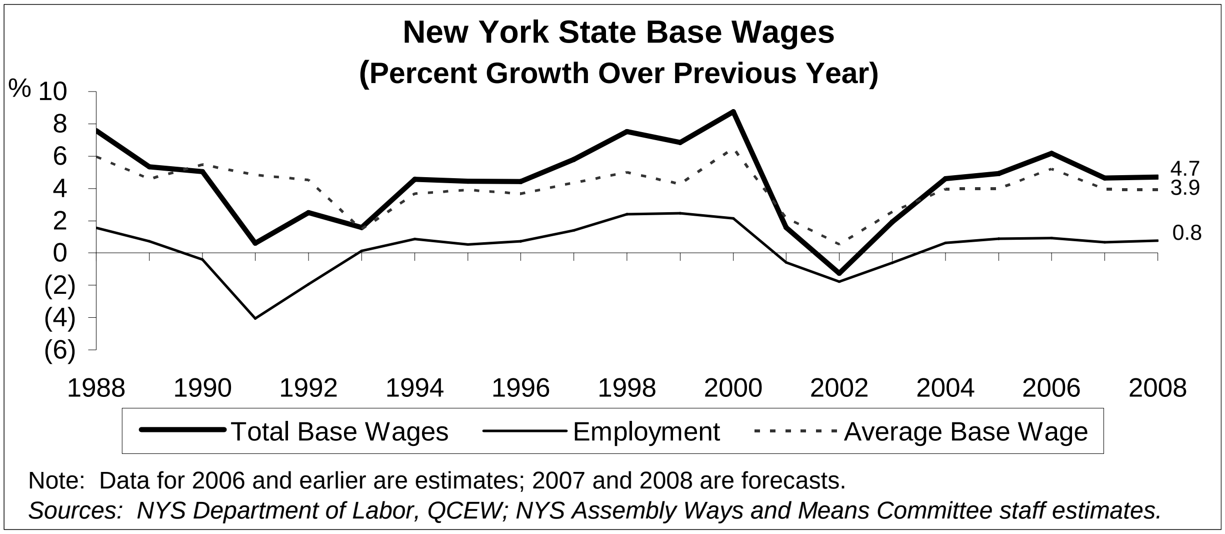


Figure 41

In 2006, estimated wage growth in New York State was 1.3 percentage point higher than in the nation as a whole (see Figure 42). New York State wages are predicted to grow slightly faster than national wages throughout the forecast period. On a long-term basis, the average annual growth rates of wages in the State and in the nation are quite similar. Between 1980 and 2005, the average annual growth rate of wages in the nation was 6.0 percent. In the State the wage growth rate was 5.8 percent.

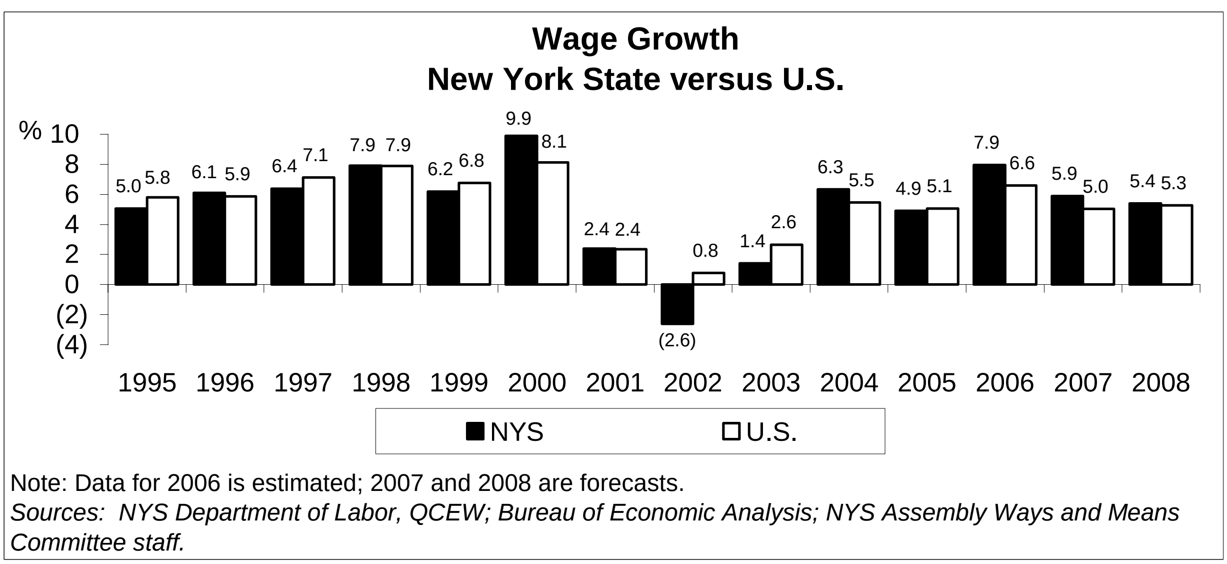
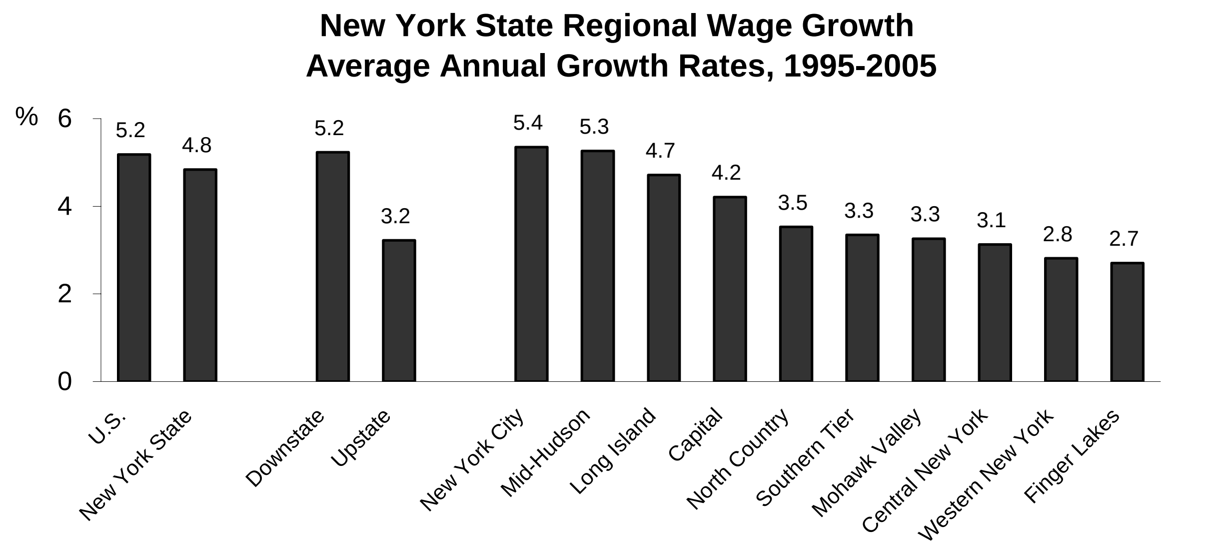


Figure 42

In 1995-2005, New York State wages grew at an average rate of 4.8 percent per year, slower than the national rate of 5.2 percent per year. Wages grew fastest in the downstate regions. Downstate wages grew at an average of 5.2 percent per year, much faster than the upstate wage growth of 3.2 percent per year. The highest wage growth in the State was in the New York City region, where wages grew 5.4 percent per year in the 1995-2005 period, compared to just 2.7 percent for the Finger Lakes region, the region with the slowest wage growth. The fastest wage growth among upstate regions was in the Capital region. In all other regions of upstate, the rate of wage growth was much lower than the rate of wage growth in the State (see Figure 43).



Note: The region ranks are based on data with more than one decimal point.
Sources: NYS Department of Labor, QCEW.

Figure 43

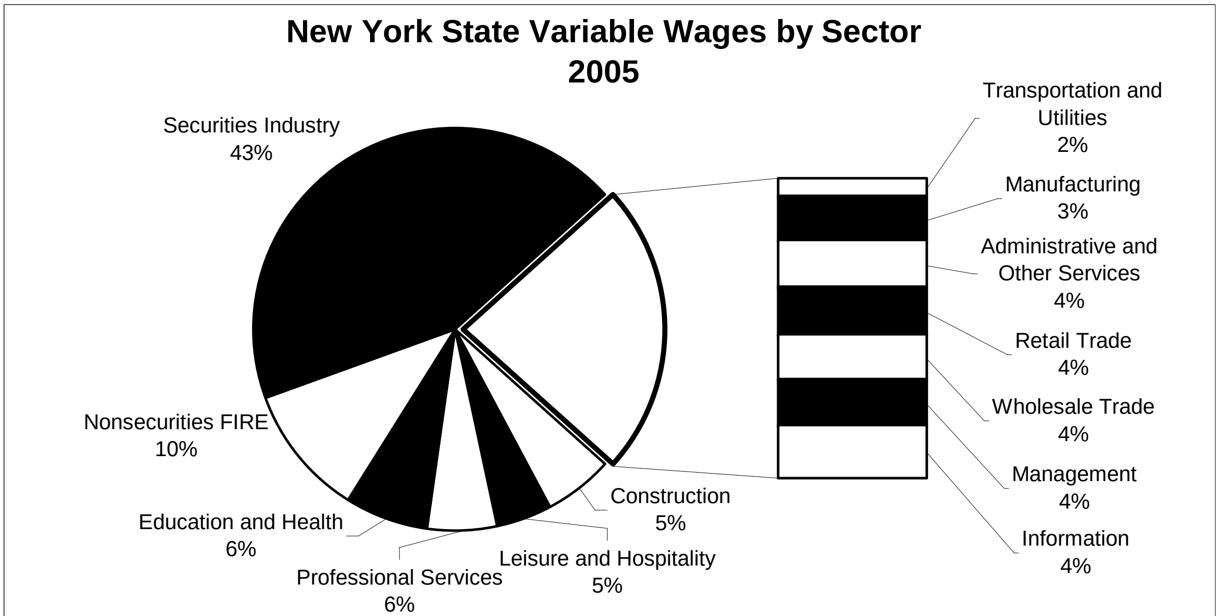
Variable Compensation

Variable compensation is the most volatile component of New York wages and plays an important role in forecasting State wages.[51] Variable compensation accounted for 10.1 percent of total compensation over the last five years. Even though the share of

[51] There is no known series of data for state or national variable compensation. The NYS Assembly Ways and Means Committee staff estimates variable compensation based on seasonal variations in wage patterns. These seasonal patterns are broken down by sector (at the NAICS three-digit level) to improve the precision of the estimate. The growth in this variation over time is also accounted for in the estimate. Since this estimate is based on seasonal variation, it may underestimate bonuses and commissions that come at frequent intervals throughout the year. It also may underestimate stock options to the extent that they are exercised throughout the year. On the other hand, in some cases non-variable pay may be included in variable compensation if there are regular seasonal patterns (such as if overtime regularly occurs in a certain quarter). Therefore, variable compensation contains high uncertainty—even in terms of the data history.

variable compensation is small compared to base wages, its impact on changes in total compensation cannot be ignored. Variable compensation is particularly prominent in the securities industry. Securities industry variable compensation has made up 41.9 percent of total variable compensation in the State over the last five years.

Following the securities industry, the second largest source of variable compensation is non-securities FIRE, followed by professional services, education and health, leisure and hospitality, and construction (see Figure 44). Combined, these sectors account for three-quarters of variable compensation.



Sources: NYS Department of Labor, QCEW; NYS Assembly Ways and Means Committee staff estimates.

Figure 44

The Assembly Ways and Means Committee staff estimates that New York State total variable compensation, which was $45.7 billion in 2005, increased by 22.9 percent to $56.2 billion for 2006. This will be followed by growth of 15.0 percent year-over-year during 2007 and 10.0 percent in 2008.

Securities Industry

Securities industry variable compensation is linked with both securities industry revenue and profits. Security industry profits in 2006 were below the peak profitability level of 2000. However, profits in 2006 rose significantly from 2005, jumping to an estimated $16.5 billion from $9.4 billion (see Figure 45). The surge in profits has led to record level bonuses paid out by investment firms.[52] Total revenue for NYSE member firms was up an estimated 36.2 percent in 2006.[53]

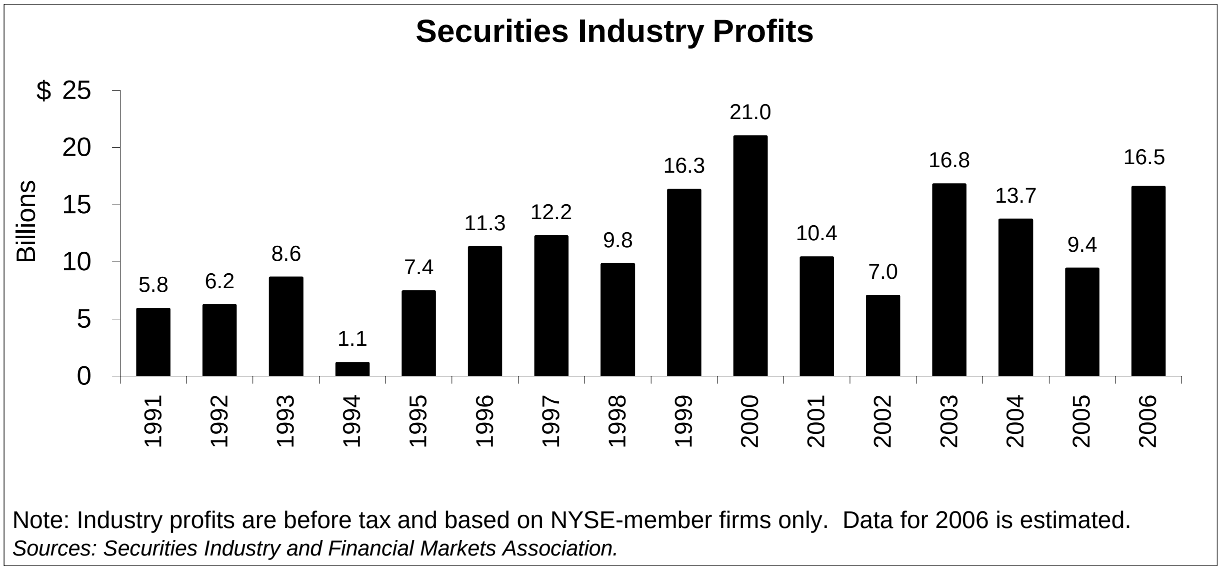


Figure 45

Announced United States mergers and acquisitions were strong in 2006, although not quite at the record levels seen in 2000 (see Figure 46). Worldwide-announced mergers and acquisitions, which exceeded $1 trillion in activity in 2005, surged 38 percent in 2006 to a record $3.8 trillion.[54] Pending and completed mergers and acquisitions also were strong in 2006. Low interest rates, along with increasing corporate earnings, have created favorable conditions for mergers and acquisitions.[55] In addition, both initial public offering (IPO) activity and announcements of companies going private also were strong. According to Thomson Financial, the number of deals of announced companies going private as well as the value of deals has significantly increased. The outlook for IPOs, private equity, and mergers and acquisitions is positive.[56] The sectors that may have a lot of merger and

[52] Paul Tharp, "Billion Chillin', Wall Street Bonuses Hit New All-Time High," *New York Post*, December 20, 2006, http://www.nypost.com/seven/12202006/business/billion_chillin_business_paul_tharp.htm; and Vinnee Tong, AP: "Goldman CEO's $53.4M Bonus Breaks Record," *Business Week*, December 20, 2006, http://www.businessweek.com/ap/financialnews/D8M4OAC80.htm?chan=search.

[53] Securities Industry and Financial Markets Association, January 2007.

[54] Judy Radler Cohen, "The M&A Year Soars to a Close and a Record," Thomson Media, New York: January 8, 2007.

[55] Dennis K. Berman, "Stock Market Quarterly Review: Merger Activity Sets Stage for Record Year," *Wall Street Journal*, October 2, 2006, C11.

[56] Global merger and acquisition volume was up 36 percent in the first seven weeks of 2007. For more details, see AP: Joe Bel Bruno, "Analysts Predict Record Merger Year," *Beacon Journal*, February 18, 2007.

acquisition activity in the coming year are telecommunications, energy and utilities, and financial services.[57]

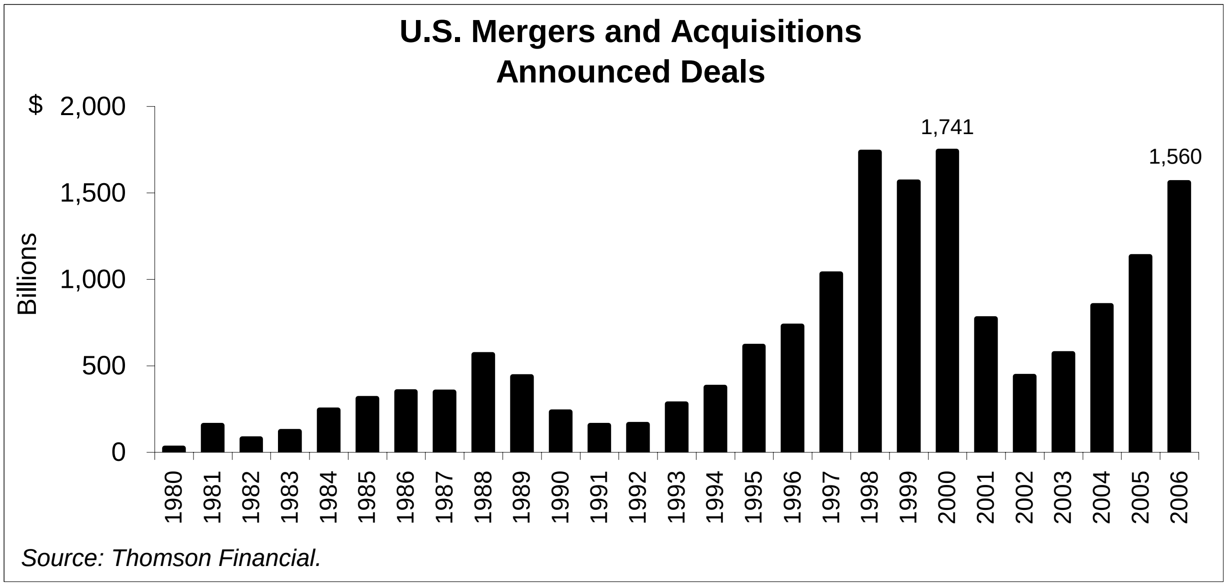


Figure 46

Changes in interest rates can have an effect on the industry through trading gains or losses. The securities industry is increasingly taking its own positions in the market through proprietary trading. Large changes in interest rates can cause significant variability in the value of the financial assets held by securities firms. Whether the industry gains additional income from these financial assets or suffers a loss depends on how the market moves relative to expectations. Recently, long-term interest rates have been increasing less than expected by most market analysts (see the Interest Rates section on page 38). This could either have a positive or negative impact on securities industry firms depending on the positions taken by the market.

Currently, 19 percent of industry revenue comes from commissions and trading gains, as well as activities related mostly to the trading of stocks and bonds (see Figure 47). Underwriting, including initial public offerings, asset management fee, and margin interest each contribute 6 percent of revenue. Over half of revenue comes from other revenue sources. The three largest sources of revenue in this category are mergers and acquisitions (M&A), prime brokerage revenue from growth in hedge fund activities, and interest revenue (aside from margin interest). Unfortunately, the current system of categorizing financial data used by the securities industry does not allow revenue from these three categories to be measured precisely.

[57] Knowledge @ Wharton, "Big Deal(s): What's Driving the M&A Frenzy?" *Knowledge @ Wharton*, January 24, 2007, http://www.wharton.upenn.edu.

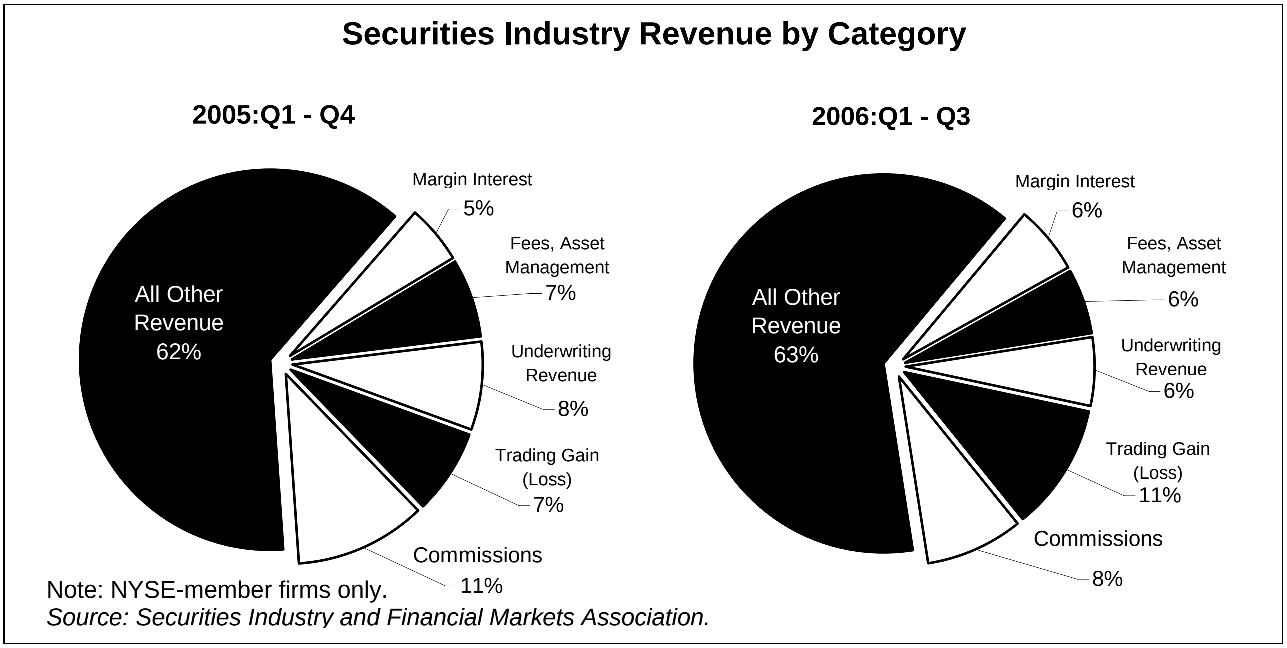


Figure 47

The two greatest expenses for the industry are interest expense and compensation (see Figure 48). Despite a very high presence in expensive high-end Manhattan real estate, less than three percent of the industry's expenses are related to the cost of property (i.e. occupancy expense). Given the structure of these expenses, it is likely that the securities industry will continue to maintain a heavy presence in Manhattan as long as it allows the industry's highly paid workers to conduct business more efficiently or is simply a more attractive place to work for high-productivity employees.

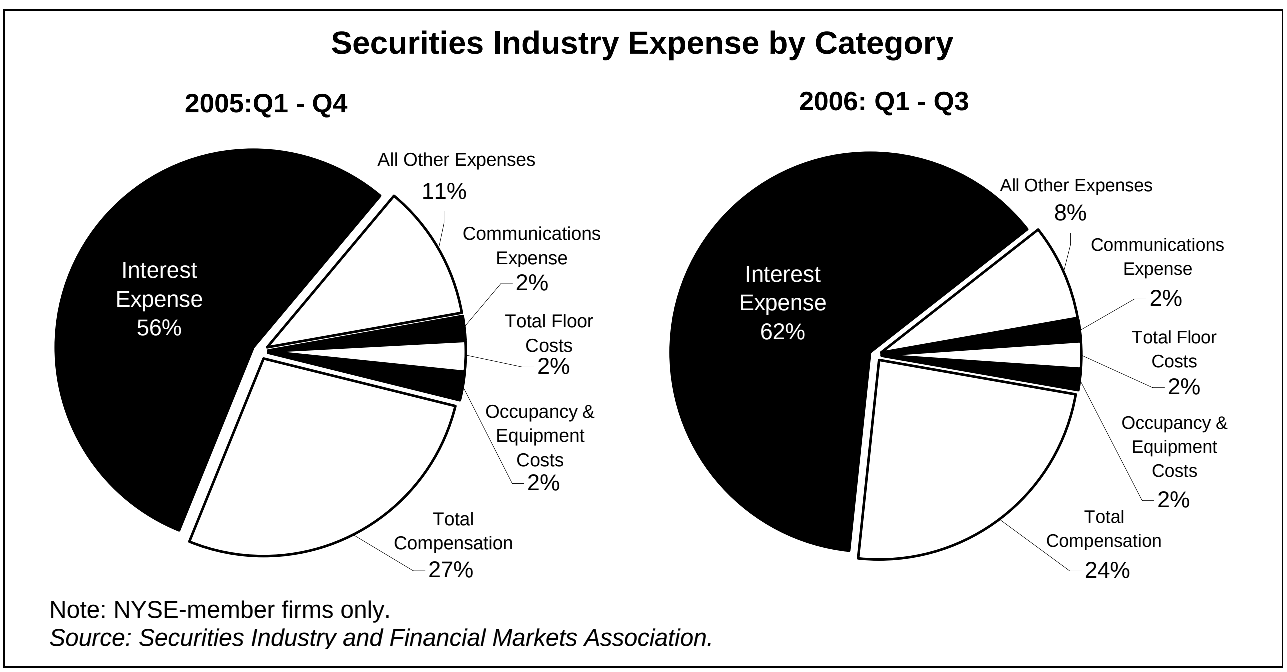
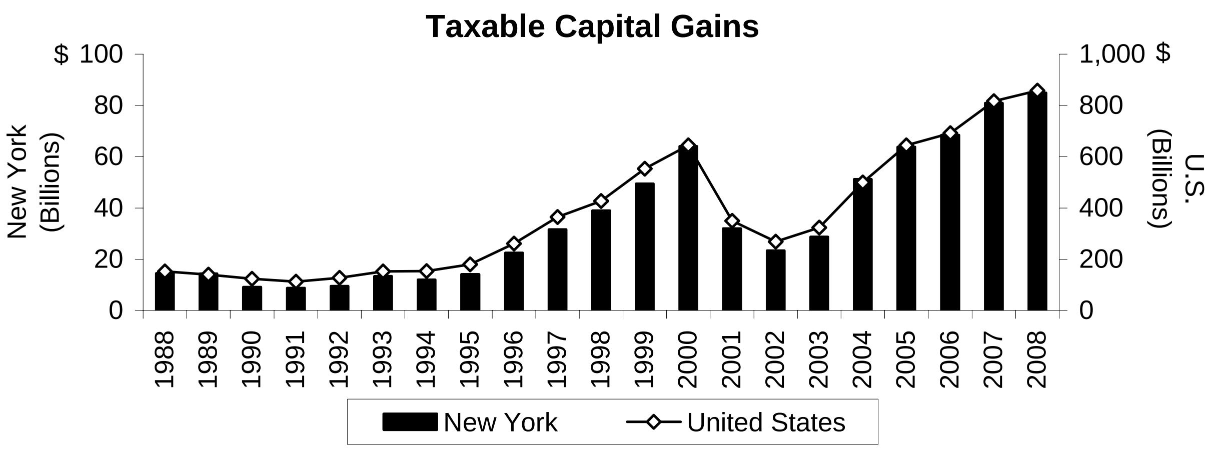


Figure 48

Capital Gains

After rising rapidly during the booming stock market of the late 1990s, capital gains realizations plummeted in 2001 and declined further in 2002. They increased in 2003 and 2004 for both New York State and the nation (see Figure 49). In 2005, capital gains for the nation are estimated to have grown 29.0 percent to $644 billion, while State capital gains are estimated to have grown 24.6 percent to $63.8 billion.



Note: The first forecast period is 2005.
Sources: U.S. Department of the Treasury; NYS Department of Taxation and Finance; NYS Assembly Ways and Means Committee staff.

Figure 49

This will be followed by capital gains growth of 7.3 percent to $691 billion in 2006 for the nation and growth of 7.3 percent to $68.4 billion for New York State. In 2007, capital gains for the nation and the State are expected to grow 18.2 percent. In 2008, the growth rate is expected to be 5.0 percent for both the nation and the State.

Traditionally, the single most important factor driving capital gains for the nation and New York State is the performance of financial markets, particularly the equity markets. However, model results indicate that it is long-term change in equity markets rather than the year-over-year price growth that has the greatest influence on capital gains. Property prices have also increasingly influenced capital gains, particularly in the recent environment of rapid price growth, increasing purchases of homes for investment purposes and the high numbers of home sales. However, as home prices are set to decline amidst sharply declining housing market activity, capital gains will be negatively affected to some extent. Tax rates also affect how and when people choose to cash out their market gains.

New York State Forecast Comparison

The Assembly Ways and Means Committee staff's employment growth forecast for 2007 is 0.7 percent (see Table 11). This forecast is the same as the Division of the Budget, 0.2 percentage point higher than Global Insight, and 0.1 percentage point lower than Moody's Economy.com.

The Assembly Ways and Means Committee staff anticipates that employment will increase by 0.8 percent in 2008. This is close to other major forecasting groups. The forecast is 0.1 percentage point higher than the Division of Budget and Moody's Economy.com forecasts, and the same as Global Insight.

Table 11

NYS Forecast Comparison
(Percent Change)

	Actual 2005	Estimate 2006	Forecast 2007	Forecast 2008
Employment				
Ways and Means	0.9	0.9	0.7	0.8
Division of the Budget	0.9	0.9	0.7	0.7
Global Insight	0.9	0.8	0.5	0.8
Moody's Economy.com	0.9	0.8	0.8	0.7
Wages				
Ways and Means	4.9	7.9	5.9	5.4
Division of the Budget	5.1	7.6	5.5	5.2
Global Insight	4.8	6.3	3.6	4.7
Moody's Economy.com	4.8	6.3	5.6	3.7

Sources: NYS Assembly Ways and Means Committee staff; New York State Financial Plan Projections, 2007-08 Executive Budget Supplemented for 21-Day Amendments, 2006-07 through 2010-11, February 21, 2007; Global Insight, Winter 2007 Short-term Forecast, January 2007; Moody's Economy.com, February 2007.

The Assembly Ways and Means Committee staff's wage growth forecast for 2007 is 5.9 percent. This forecast is 0.4 percentage point higher than the Division of Budget forecast, 0.3 percentage point higher than Moody's Economy.com, and 2.3 percentage points higher than Global Insight's forecast.

The Assembly Ways and Means Committee staff's wage growth forecast for 2008 is 5.4 percent. This is 0.2 percentage point higher than the Division of Budget forecast, 1.7 percentage points higher than Moody's Economy.com and 0.7 percentage point higher than Global Insight's forecast.

RISKS TO THE FORECAST

Uncertainty in many economic indicators and global activities always represents a risk to both the national and the New York State forecasts. Uncertainty surrounds many of the factors taken into account in forecasting, and may be real or perceived. Current events that may add to economic uncertainty include the War in Iraq, other tensions in the Middle East, the potential of another terrorist attack, volatility in the energy markets, and the housing market. Uncertainty can lead to lower consumer confidence, and possibly lower consumer spending.

Energy prices continue to represent a significant risk to the forecast, although recent movements in the market make it difficult to assess if energy prices are an upside or downside risk. Unexpected events constrain supply, while demand continues to grow. This ambiguity, combined with speculation in the market, makes it extremely difficult to predict crude oil prices for the near or far future. Therefore, oil prices add a large amount of uncertainty to the forecast. On the upside, declining energy prices, as seen in January 2007, could provide a boost to the economy through lower inflation and positive effects on consumption.

Continued decline of the dollar also represents a risk to the forecast. A weakening dollar does have the potential of reducing the trade deficit somewhat, as American goods become cheaper (exports go up) and foreign goods become more expensive (imports go down).[58] However, a depreciating U.S. dollar may produce inflationary pressures in our economy.

Interest rates present a risk to the forecast, including the uncertainty surrounding the Federal Reserve's actions regarding rates. Relatively high interest rates present a risk in the housing market. If the housing market decelerates at a faster pace than expected and does not stabilize, it could pose a risk for factors like household consumption and taxable capital gains. The popularity of adjustable rate mortgages when interest rates were extremely low poses a risk for the economy now. As rates rise some consumers are no longer able to meet their required payments, while others adjust their consumption patterns to meet mortgage payments.

The risks of interest rates and energy prices are also tied into the risk of rising inflation, both overall and core (excluding food and energy prices). Continued rising prices can erode consumption and consumer confidence, as well as disrupt investment.

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[58] Mark Whitehouse, "Why U.S. Should Root for Dollar to Weaken More," *Wall Street Journal*, January 8, 2007, A2.

The securities industry outlook represents a significant risk to the New York State economy, as the industry is volatile. As the industry is a major driver of State wages, unexpected movements in the industry can have an effect on the State wage forecast.

APPENDIX A

The North American Industry Classification System (NAICS)	
Code	**NAICS Title**
11	**Agriculture, Forestry, Fishing and Hunting**
111	Crop Production
112	Animal Production
113	Forestry and Logging
114	Fishing, Hunting and Trapping
115	Support Activities for Agriculture and Forestry
21	**Mining**
211	Oil and Gas Extraction
212	Mining (except Oil and Gas)
213	Support Activities for Mining
22	**Utilities**
221	Utilities
23	**Construction**
236	Construction of Buildings
237	Heavy and Civil Engineering Construction
238	Specialty Trade Contractors
31-33	**Manufacturing**
311	Food Manufacturing
312	Beverage and Tobacco Product Manufacturing
313	Textile Mills
314	Textile Product Mills
315	Apparel Manufacturing
316	Leather and Allied Product Manufacturing
321	Wood Product Manufacturing
322	Paper Manufacturing
323	Printing and Related Support Activities
324	Petroleum and Coal Products Manufacturing
325	Chemical Manufacturing
326	Plastics and Rubber Products Manufacturing
327	Nonmetallic Mineral Product Manufacturing
331	Primary Metal Manufacturing
332	Fabricated Metal Product Manufacturing
333	Machinery Manufacturing
334	Computer and Electronic Product Manufacturing
335	Electrical Equipment, Appliance, and Component Manufacturing
336	Transportation Equipment Manufacturing
337	Furniture and Related Product Manufacturing
339	Miscellaneous Manufacturing
42	**Wholesale Trade**
423	Merchant Wholesalers, Durable Goods
424	Merchant Wholesalers, Nondurable Goods
425	Wholesale Electronic Markets and Agents and Brokers

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The North American Industry Classification System (NAICS) -- *(continued)*

Code	NAICS Title
44-45	**Retail Trade**
441	Motor Vehicle and Parts Dealers
442	Furniture and Home Furnishings Stores
443	Electronics and Appliance Stores
444	Building Material and Garden Equipment and Supplies Dealers
445	Food and Beverage Stores
446	Health and Personal Care Stores
447	Gasoline Stations
448	Clothing and Clothing Accessories Stores
451	Sporting Goods, Hobby, Book, and Music Stores
452	General Merchandise Stores
453	Miscellaneous Store Retailers
454	Nonstore Retailers
48-49	**Transportation and Warehousing**
481	Air Transportation
482	Rail Transportation
483	Water Transportation
484	Truck Transportation
485	Transit and Ground Passenger Transportation
486	Pipeline Transportation
487	Scenic and Sightseeing Transportation
488	Support Activities for Transportation
491	Postal Service
492	Couriers and Messengers
493	Warehousing and Storage
51	**Information**
511	Publishing Industries (except Internet)
512	Motion Picture and Sound Recording Industries
515	Broadcasting (except Internet)
516	Internet Publishing and Broadcasting
517	Telecommunications
518	Internet Service Providers, Web Search Portals, and Data Processing Services
519	Other Information Services
52	**Finance and Insurance**
521	Monetary Authorities - Central Bank
522	Credit Intermediation and Related Activities
523	Securities, Commodity Contracts, and Other Financial Investments and Related Activities
524	Insurance Carriers and Related Activities
525	Funds, Trusts, and Other Financial Vehicles
53	**Real Estate and Rental and Leasing**
531	Real Estate
532	Rental and Leasing Services
533	Lessors of Nonfinancial Intangible Assets (except Copyrighted Works)
54	**Professional, Scientific, and Technical Services**
541	Professional, Scientific, and Technical Services

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The North American Industry Classification System (NAICS) -- *(continued)*

Code	NAICS Title
55	**Management of Companies and Enterprises**
551	Management of Companies and Enterprises
56	**Administrative and Support and Waste Management and Remediation Services**
561	Administrative and Support Services
562	Waste Management and Remediation Services
61	**Educational Services**
611	Educational Services
62	**Health Care and Social Assistance**
621	Ambulatory Health Care Services
622	Hospitals
623	Nursing and Residential Care Facilities
624	Social Assistance
71	**Arts, Entertainment, and Recreation**
711	Performing Arts, Spectator Sports, and Related Industries
712	Museums, Historical Sites, and Similar Institutions
713	Amusement, Gambling, and Recreation Industries
72	**Accommodation and Food Services**
721	Accommodation
722	Food Services and Drinking Places
81	**Other Services - except Public Administration**
811	Repair and Maintenance
812	Personal and Laundry Services
813	Religious, Grantmaking, Civic, Professional, and Similar Organizations
814	Private Households
92	**Public Administration**
921	Executive, Legislative, and Other General Government Support
922	Justice, Public Order, and Safety Activities
923	Administration of Human Resource Programs
924	Administration of Environmental Quality Programs
925	Administration of Housing Programs, Urban Planning, and Community Development
926	Administration of Economic Programs
927	Space Research and Technology
928	National Security and International Affairs

Source: Executive Office of the President, Office of Management and Budget, North American Industry Classification System, United States, 2002.

APPENDIX B

NYS Employment and Wages in NAICS Sectors

	Employment (Thousands)			Wages ($ in Billions)		
	Estimate 2006	Forecast 2007	Forecast 2008	Estimate 2006	Forecast 2007	Forecast 2008
Total	**8,402.5**	**8,457.5**	**8,522.1**	**467.5**	**495.0**	**521.7**
Education & Health	1,458.3	1,479.9	1,503.6	59.2	62.1	65.2
Government	1,420.9	1,423.4	1,426.2	69.6	71.8	73.9
Retail Trade	875.3	877.7	884.5	24.2	25.1	26.1
Other Services	742.5	745.5	750.2	25.6	26.8	28.0
FIRE	721.5	731.5	742.8	105.7	119.1	130.3
Leisure & Hospitality	671.7	676.2	681.6	16.5	17.1	17.7
Manufacturing	570.0	554.0	541.4	30.3	30.4	30.9
Professional Services	551.8	568.1	584.9	44.4	47.1	50.0
Wholesale Trade	351.6	350.4	351.6	23.0	23.8	24.7
Construction	332.5	333.9	336.6	17.0	17.4	18.1
Information	269.0	269.9	270.8	21.8	22.6	23.4
Transport & Utilities	264.8	269.3	273.5	12.5	13.0	13.6
Management of Companies	127.1	131.1	135.3	16.0	17.0	18.1

Note: Some NAICS sectors are grouped with others. For sector definitions, see Appendix A.

Sources: NYS Department of Labor, QCEW; NYS Assembly Ways and Means Committee staff.

NYS Employment and Wages Growth in NAICS Sectors
(Percent Change)

	Employment			Wages		
	Estimate 2006	Forecast 2007	Forecast 2008	Estimate 2006	Forecast 2007	Forecast 2008
Total	**0.9**	**0.7**	**0.8**	**7.9**	**5.9**	**5.4**
Management of Companies	4.2	3.1	3.3	8.8	6.4	6.7
Professional Services	4.2	3.0	3.0	8.7	6.1	6.1
Construction	2.8	0.4	0.8	4.5	2.2	4.2
Transport & Utilities	2.0	1.7	1.6	5.7	4.1	4.1
FIRE	1.7	1.4	1.5	18.4	12.7	9.3
Education & Health	1.5	1.5	1.6	6.2	5.0	5.0
Leisure & Hospitality	0.7	0.7	0.8	6.6	3.8	3.7
Information	0.4	0.3	0.3	6.4	3.8	3.6
Other Services	0.2	0.4	0.6	5.4	4.6	4.7
Retail Trade	0.0	0.3	0.8	1.6	3.6	4.0
Government	(0.0)	0.2	0.2	4.5	3.0	3.0
Wholesale Trade	(0.1)	(0.3)	0.3	4.7	3.5	3.7
Manufacturing	(2.4)	(2.8)	(2.3)	0.0	0.4	1.6

Note: Some NAICS sectors are grouped with others. For sector definitions, see Appendix A.

Sources: NYS Department of Labor, QCEW; NYS Assembly Ways and Means Committee staff.

APPENDIX D

U.S. Economic Outlook

	Actual 2005	Estimate 2006	Forecast 2007	Forecast 2008
Real GDP*	11,048.6	11,413.5	11,708.1	12,073.5
Real Consumption*	7,841.2	8,092.3	8,335.1	8,575.6
Real Investment*	1,866.3	1,943.9	1,915.8	1,997.7
Real Exports*	1,196.1	1,302.3	1,402.3	1,506.7
Real Imports*	1,815.3	1,921.6	1,986.3	2,075.1
Real Government*	1,958.0	1,998.9	2,043.2	2,070.7
*Federal**	727.6	742.0	754.5	759.9
*State and Local**	1,230.4	1,256.8	1,288.6	1,310.7
Personal Income**	10,239.2	10,897.4	11,484.3	12,115.7
*Wages & Salaries***	5,664.8	6,037.7	6,342.2	6,676.4
Corporate Profits (Economic Basis)**	1,330.7	1,609.5	1,691.0	1,786.1
Productivity (1992=100)	134.8	137.7	140.3	143.5
Employment***	133.7	136.2	137.9	139.9
CPI-Urban (1982-84=100)	195.3	201.6	205.4	210.3
S&P 500 Stock Price (1941-43=10)	1,207.1	1,310.7	1,430.7	1,515.8
Treasury Bill Rate (3-month)****	3.1	4.7	4.9	5.0
Treasury Bond Rate (10-year)****	4.3	4.8	4.8	5.1

* In billions of chained 2000 dollars.
** In billions of dollars.
*** In millions.
**** Annual average rate.

Sources: Bureau of Economic Analysis; Bureau of Labor Statistics; Federal Reserve Board of Governors; Standard and Poor's; NYS Assembly Ways and Means Committee staff.

APPENDIX E

U.S. Economic Outlook
(Percent Change)

	Actual 2005	Estimate 2006	Forecast 2007	Forecast 2008
Real GDP	3.2	3.3	2.6	3.1
Real Consumption	3.5	3.2	3.0	2.9
Real Investment	5.4	4.2	(1.4)	4.3
Real Exports	6.8	8.9	7.7	7.4
Real Imports	6.1	5.9	3.4	4.5
Real Government	0.9	2.1	2.2	1.3
Federal	1.5	2.0	1.7	0.7
State and Local	0.5	2.2	2.5	1.7
Personal Income	5.2	6.4	5.4	5.5
Wages & Salaries	5.1	6.6	5.0	5.3
Corporate Profits (Economic Basis)	12.5	21.0	5.1	5.6
Productivity	2.3	2.1	1.9	2.3
Employment	1.7	1.9	1.3	1.5
CPI-Urban	3.4	3.2	1.9	2.4
S&P 500 Stock Price	6.8	8.6	9.2	6.0
Treasury Bill Rate (3-month)*	3.1	4.7	4.9	5.0
Treasury Note Rate (10-year)*	4.3	4.8	4.8	5.1

* Annual average rate.
Sources: Bureau of Economic Analysis; Bureau of Labor Statistics; Federal Reserve Board of Governors; Standard & Poor's; NYS Assembly Ways and Means Committee staff.