ECONOMY

The National Economy

According to the Executive, the national economy will continue to expand, but it will grow at a decreasing rate in the next few years. The Executive believes that growth in 2006 and 2007 will be dampened by a weakening housing sector, high energy prices, and rising interest rates.

Real Gross Domestic Product (GDP) is expected by the Executive to grow 3.3 percent in 2006, after growing an estimated 3.6 percent in 2005 (Table 18). The Executive's 2006 GDP forecast is 0.1 percentage point below the Blue Chip Consensus, with the Consensus forecast averaging 3.4 percent compared to the Executive's 3.3 percent forecast. In 2007, the Executive expects GDP growth to slow to 2.7 percent. This is unusually slow growth for the middle of an economic expansion and it is 0.4 percentage points lower than the Blue Chip Consensus.

The Executive expects declining cash available from refinancing of housing assets and declining purchases of home furnishings and appliances to lead to a deceleration of consumption growth, with growth in 2006 of 2.9 percent following estimated growth of 3.5 percent in 2005. Nonresidential fixed investment is expected to slow slightly to 8.4 percent growth in 2006 from the 9.0 percent growth estimated for 2005. Residential investment is expected to decelerate sharply and decline 0.2 percent in 2006, compared to the 7.1 percent growth estimated for 2005. In 2007, residential investment is expected to decline further by 3.1 percent.

Employment is expected to grow 1.6 percent in 2006 following growth of 1.6 percent in 2005 (Table 18). The unemployment rate will decline to 4.9 percent in 2006 and 2007 before rising again in 2008. As the Executive's figures indicate, much of the decrease in the unemployment rate in recent years can be attributed to a decline in the labor force participation rate rather than rapidly rising employment.

The Executive forecasts that oil prices will decline moderately. Oil prices will decrease from current highs of $55 per barrel to about $50 per barrel by the end of 2006.

The Federal Reserve is expected by the Executive to raise short term rates beyond the range that most experts consider to be "neutral". The Executive expects the Federal Funds rate to reach 5.1 percent by the end of 2006.

The stock market, as measured by the S&P 500, is expected by the Executive to grow 10.0 percent in 2006 (Table 18). As of January 15, 2005, the S&P 500 opened at 1285.8, an increase of 6.9 percent over the average level in 2005. Therefore, for the Executive's stock market forecast to be accurate, price levels on average in 2006 must rise 2.9 percent from their current level.

Table 18

Executive Compared to Major Forecasters (Percent Change)	Estimate 2005	Forecast 2006	Forecast 2007
U.S. Real GDP			
Division of the Budget	3.6	3.3	2.7
Blue Chip Consensus	3.6	3.4	3.1
Economy.com	3.6	3.7	2.9
Global Insight	3.6	3.4	2.7
U.S. Nonfarm Employment			
Division of the Budget	1.6	1.6	1.6
Economy.com	1.6	1.8	1.2
Global Insight	1.6	1.5	1.4
S&P 500			
Division of the Budget	6.8	10.0	9.1
Economy.com	6.9	6.2	4.9
Global Insight	6.7	5.5	1.8
New York State Employment			
Division of the Budget	0.9	0.8	0.7
Economy.com	0.8	1.0	0.6
New York State Wages			
Division of the Budget	5.1	6.1	5.1
Economy.com	4.6	3.4	4.4

Sources: Division of the Budget, Executive Budget 2006-07, January 2006; Blue Chip Economic Indicators, January 2006; Economy.com, Precis U.S. Macro, January 2006, NYS Forecast as of January 17, 2006, <http://www.economy.com>; Global Insight, U.S. Executive Summary, January 2006, <http://www.globalinsight.com>.

The New York State Economy

According to the Executive, New York State economy is in its third year of recovery from a recession that lasted 2.5 years, much longer than the length of the national recession. Total employment for the State is estimated to have increased 0.9 percent in 2005, or about half of the rate of growth of the nation. Employment growth is expected to decelerate slightly in 2006 and 2007 despite a stable rate of employment growth for the nation (Table 18). New York wages are expected to grow 6.1 percent in 2006 following estimated growth of 5.1 percent in 2005. The growth will be due to rising variable compensation, particularly in the financial industry. In 2005, both estimated employment and wage growth were slower than the nation (Figure 20).

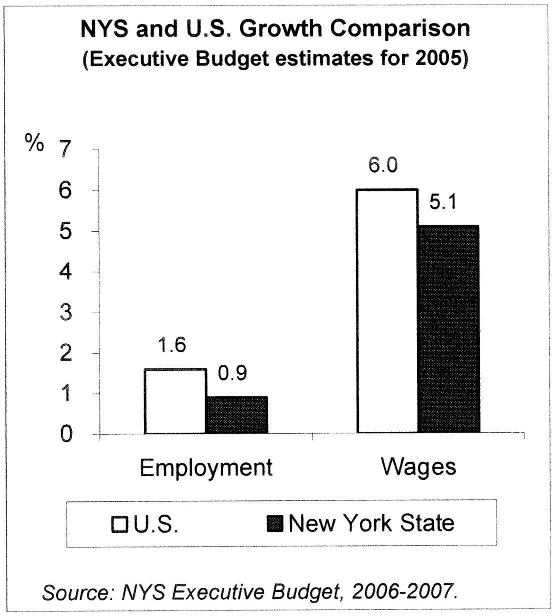


Figure 20

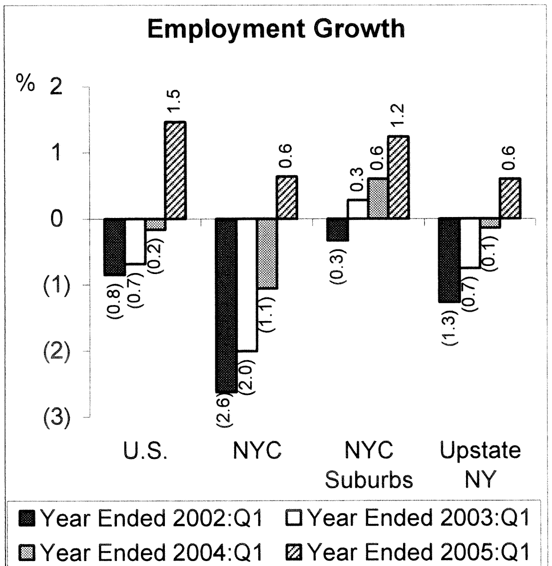
Unemployment in 2006 is expected to average 5.0 percent for the State, 0.1 percentage points above the national average for the same period. In 2007, unemployment for the State is expected to average 5.1 percent, 0.2 percentage points above the national rate. New York State's unemployment rate is expected by the Executive to slightly underperform relative to the nation at least until 2009.

The Executive expects State wages and salaries to grow faster than the forecast from Economy.com in both 2006 and 2007 (see Table 18). In 2006, wages and salaries are expected to grow 6.1 percent, 2.7 percentage points higher than the forecast from Economy.com. In 2007, wages and salaries are expected to grow 5.1 percent, 0.7 percentage point higher than the forecast from Economy.com.

For the second year in a row, the Executive has dramatically increased estimated and forecast capital gains for New York State. In the current 2006-07 Executive Budget, 2004 capital gains are estimated to be $52.0 billion. This is up 29.7 percent from the estimated capital gains of $40.1 billion for the same period presented a year ago in the 2005-06 Executive Budget. For 2005, capital gains in the current 2006-07 Executive Budget are estimated to be $72.5 billion. This is up 63.7 percent from the forecast of $44.3 billion presented a year ago for the same period in the 2005-06 Executive Budget. In 2006 the Executive now expects capital gains to decline by 3.1 percent, followed by growth of 6.7 percent in 2007.

The State has a very high concentration of economic activity in the finance and insurance sector, particularly in the securities industry. The Executive expects finance and insurance sector variable wages (i.e. bonuses) to grow 21.2 percent during the 2005-06 fiscal year. To justify this sizable increase in the sector's variable wages, the Executive cites the relatively high profitability of securities industry activity centered in New York City. The Executive also points out that securities industry revenue increased 36.2 percent in the first three quarters of 2005, suggesting that this increase was primarily driven by mergers and acquisitions, proprietary trading activity, and strong demand for bond underwriting. However, a good portion of the increase in revenues was likely due to increases in interest as a result of rising interest rates. This likely did little to improve profitability.

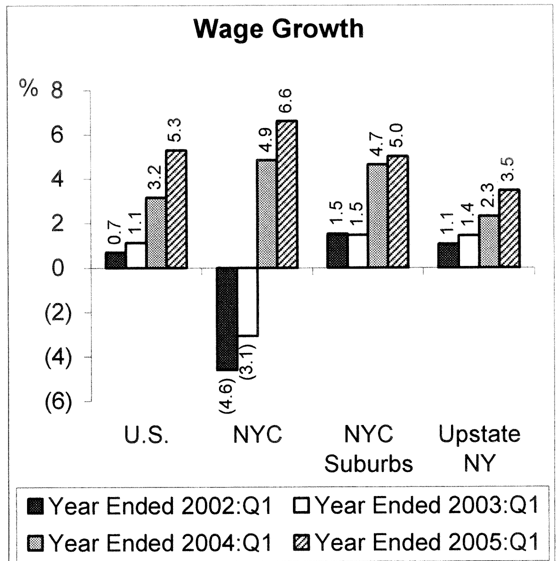
All regions of New York State grew more slowly than the nation in the first quarter of 2005, with the New York City Suburbs growing faster than New York City or upstate New York. In the prior three years, the New York City suburbs outperformed the nation, growing in two of the three years despite declining employment nationally, while New York City employment declined more than the nation (Figure 21).



Sources: U.S. Bureau of Labor Statistics, QCEW; NYS Department of Labor, QCEW.

Figure 21

The situation with wages is somewhat different than that for employment. New York City has performed better than the nation in the last two years, while in the two prior yearly periods New York City was hit particularly hard (Figure 22). The New York City suburbs performed slightly worse than the nation in the most recent annual period. Upstate New York performed worse than the nation or any other part of New York in the most recent annual period.



Sources: U.S. Bureau of Labor Statistics, QCEW; NYS Department of Labor, QCEW.

Figure 22