THE CITY OF NEW YORK
INDEPENDENT BUDGET OFFICE
110 WILLIAM STREET, 14TH FLOOR
NEW YORK, NEW YORK 10038
(212) 442-0632 • FAX (212) 442-0350 •EMAIL: iboenews@ibo.nyc.ny.us
http://www.ibo.nyc.ny.us

Testimony of Ronnie Lowenstein
Director, New York City Independent Budget Office
To the New York City Council Finance Committee
On the Mayor's Preliminary Budget for Fiscal Year 2014 and Financial Plan through 2017

March 4, 2013

Good afternoon Chairman Recchia and members of the committee. I am Ronnie Lowenstein, the Director of New York City's Independent Budget Office. I appreciate the opportunity to be here today and discuss some of the details from our latest economic forecast and tax revenue and spending projections, which are based on the budget plan presented by the Mayor in January. Attached to this testimony are tables that present our projections. Our report providing a fuller analysis of the Mayor's budget and details of our forecast will be available by March 29.

I'll begin by going straight to the bottom line—our estimates of budget gaps or surpluses for 2013 and beyond—and then cover some of the key points underlying our projections. The testimony concludes by presenting some cautionary notes to our forecast, most notably the absence of funding for labor settlements with the city's major unions, which are all currently working without contracts.

Based on our economic forecast and tax revenue and spending projections, we anticipate the city will end the current fiscal year with a $1.2 billion surplus, about $160 million more than the Mayor estimates. We project that under the Bloomberg Administration's budget plan, the city would end 2014 with a $427 million surplus. While we expect budget shortfalls in the out-years, the amounts are unusually modest. But New Yorkers should be cautious in their interpretation of what these estimates mean: These gap and surplus numbers for fiscal years 2013 through 2017 do not reflect all the pressures on the city's budget, and the fiscal outlook is not as benign as it appears.

Given continued difficulties on Wall Street, the local economy is surprisingly strong. Since the 1970s, the city's recovery from recessions has been led by the financial sector, and in particular the securities industry. The industry has long had an outsized place in the local economy because of its extraordinarily high pay—comprising 5 percent of the city's private-sector workforce but generating about 23 percent of private-sector wages and salaries. But even as Wall Street has been contracting, New York City has been gaining jobs. We estimate that when the final numbers are in for 2012, the city will have gained about 75,000 jobs, the second consecutive year of strong growth. We anticipate somewhat slower but still solid employment growth in the coming years, including increases of 56,800 in 2013 and 65,000 in 2014.

Yet with job growth coming from sectors other than Wall Street, we have not been experiencing the increase in total wages and salaries that typically accompanies such rising levels of employment. In fact, we estimate that in 2012 aggregate wages and salaries actually *fell* by 1 percent. Dating back to the 1950s, we see no other year with a similar combination of strong employment growth but shrinking aggregate compensation. While we do not expect compensation to contract again this year, we do expect a similar pattern: a considerable rise in local employment but only a modest increase in total wages and salaries. The earnings picture does brighten in 2014, when we expect compensation growth will rebound and employment to again increase strongly.

Two of the industry sectors that we expect will continue to have strong employment growth over the next few years have in the past had their fortunes tied to the rise and fall of the financial sector. For business and professional services that seems to be changing as recent growth in the industry appears driven by other sectors such as information. We expect employment in business and professional services to produce the largest share of the job growth in the city over the coming years, providing 30 percent (95,600 jobs) of the new jobs from this year through 2017. But with its mix of relatively low-paying administrative services, including temp jobs, along with higher-paying professional services such a legal and accounting, the sector's share of aggregate wage growth will be moderated—24 percent of earnings growth over the 2013-2017 period.

Leisure and hospitality is another sector that tended to follow the ups and downs of Wall Street but has been getting an increasing boost from the city's record number of tourists. But the relatively low level of pay in the sector is reflected in the fact that although we expect leisure and hospitality to generate 15 percent of the new jobs in 2013-2017 (46,800 jobs), it will make up only about 5 percent of the rise in aggregate wages and salaries over that period.

The other fastest growing industry is education and health care. We expect that 22 percent of the new jobs in the city over 2013-2017 will come from this sector (71,900 jobs). Yet because many of the sector's jobs are relatively low-paying such as those in the home health care field, it will generate just 12 percent of the increase in total wages and salaries. Conversely, the securities industry is expected to produce only 1 percent of the new jobs in the city over 2013-2017 (3,100 jobs), yet it will account for 19 percent of the aggregate compensation growth over those five-years.

The city's softer growth in earnings when compared with robust employment increases is reflected in our estimates for tax revenue collections in fiscal years 2013 through 2017. Overall, we project tax collections will grow an average of 5.1 percent annually over the five years, increasing from $43.4 billion this fiscal year to just over $53.0 billion in 2017. We anticipate that the city's major tax sources will grow steadily through the period, with the exception of a small dip in personal income tax collections in 2014. This dip is the result of some New Yorkers shifting income into calendar year 2012 to avoid the expected increase in federal tax rates for 2013 and beyond.

Although our tax revenue forecast projects steady, if unspectacular, growth rates, we do anticipate more revenues than estimated by the Bloomberg Administration—about $415 million more in fiscal year 2014, and $1.3 billion more in 2015. Our forecast is also higher than that of the City Council's Finance Division, which projects $163 million more than the Mayor's budget office in 2014 and $343 million more in 2015.

On the expense side of the budget, the Council is well aware of the cuts contained in the Mayor's budget plan, both the new cuts in the 2014 plan and the spending reductions for fire companies, child care, libraries, and other services that were only restored in negotiations last June for the current fiscal year. So I will focus briefly on a few examples of spending that we think will be higher than the Mayor projects. The largest area of additional spending is expected to be in education. The Mayor's budget plan does not yet recognize the scheduled opening of 37 new charter schools this September as well as the expansion of existing charter schools that are expected to increase the number of grades they serve. We estimate the planned expansion will cost an additional $123 million in fiscal year 2014, $170 million in 2015, and grow to $306 million in 2017.

Although the Mayor's budget plan increases the funding for shelter for homeless families, we expect that this increase will not be sufficient given the rising numbers of homeless families over the past year. We project shelter spending will be about $70 million higher than currently budgeted for 2014 and 2015 and total just over $500 million in each of those years. (About $25 million of the funds would come from city-generated revenue, with the remainder drawn from state and federal sources.) And based on past experience, we also expect that at least one of the upcoming primary elections will result in a runoff and will cost an additional $20 million in city funds that has not yet been budgeted.

Despite these and other estimates of spending above the level in the Mayor's plan, our higher tax revenue projections lead to a comparatively small surplus in 2014 and modest budget shortfalls in the subsequent years of the budget plan. Yet as stated earlier, these projections should be viewed with caution.

The single largest reason for caution is that contracts for all of the city's major municipal unions have expired and there is virtually no money set aside to cover contract settlements through 2013. If the unions for teachers and principals were to receive the 4 percent increases that other unions won in the 2008-2010 round of bargaining and all unions with contracts that have expired since 2010 were to receive 2 percent raises for the next two contract years, it would cost the city $3.8 billion through this June.

Another significant reason for caution is the continued expectation of $1.5 billion in revenue from the proposed sale of new taxi medallions. The budget plan now includes $600 million from the medallion sale in 2014 with the balance expected in 2015 and 2016. With the sale tied up in court and the next hearing date scheduled for late April, these revenue projections are far from certain. Uncertainty also follows from the still unfolding effects of federal budget cutbacks, the so-called sequestration, along with after-effects of Sandy and the still developing plans for how the city will rebuild and protect itself from future storms.

Thank you again for the opportunity to be here today and I am pleased to take any questions.