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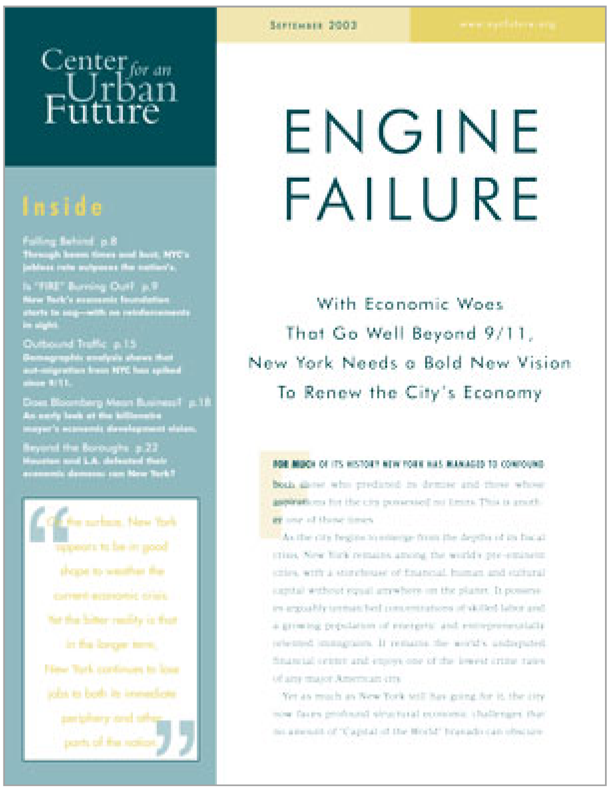
# Engine Failure




Report - September 2003

## Engine Failure

With economic woes that go well beyond 9/11, New York needs a bold new vision to renew the city's economy. In this acclaimed report, the Center for an Urban Future lays out a plan for growth that transcends skyscrapers and stock tickers.

by Jonathan Bowles and Joel Kotkin

*This is an excerpt. Click here to read the full report (PDF).*

**Update:** In August 2007, a state-commissioned study called for wholesale changes to New York's economic development programs and advocated for a new strategy that involves growing the "innovation economy" and capitalizing on its educational and research institutions. The Center has long advocated for a more forward-looking economic development strategy that focuses on tapping unique assets—such as our scientific research institutions—and supporting sectors that have significant potential for growth instead of providing tax breaks for individual corporations.

For much of its history New York has managed to confound both those who predicted its demise and those whoseaspirations for the city possessed no limits. This is another one of those times.

As the city begins to emerge from the depths of its fiscal crisis, New York remains among the world's pre-eminent cities, with a storehouse of financial, human and cultural capital without equal anywhere on the planet. It possesses arguably unmatched concentrations of skilled labor and a growing population of energetic and entrepreneurially oriented immigrants. It remains the world's undisputed financial center and enjoys one of the lowest crime rates of any major American city.

Yet as much as New York still has going for it, the city now faces profound structural economic challenges that no amount of "Capital of the World" bravado can obscure. The hyper stock market boom of the late 1990s—and the employment gains it produced on Wall Street, in Silicon Alley and in a host of service sectors—temporarily deflected attention away from the city's economic vulnerability. But the long-term trends are inescapable:

Many of the city's normally reliable industries, like finance, are expected to produce little, if any, employment growth over the next few decades.

New York continues to lose jobs and market share in a variety of high-wage industries-—including the important professional and business services sector-—to the rest of the region and to other major metropolitan centers across the country.

Despite its storied past as an entrepreneurial center, New York lags seriously behind other cities as an incubator of growth companies and a recipient of venture capital. Too many of the city's fastest-growing entrepreneurial endeavors-—from immigrant-owned manufacturers of specialty food products to innovative software and biotech firms—-choose to expand elsewhere.

Many other cities, including heavily urbanized places like Chicago and Los Angeles, have done much better than New Yorkin retaining jobs in traditional industries like wholesale trade and manufacturing.
Making matters worse, many of these troubling trends have been amplified and accelerated by both the after-effects of the September 11 attacks and advances in telecommunications technology. It has been clear for some time that 9/11 prompted several large corporations, from insurance giants and investment banks to law firms, to decentralize their operations throughout the region. But a new demographic analysis done for this report by William H. Frey of the Brookings Institution reveals that 9/11 also appears to be having a significant impact on the city's ability to attract and retain two of the demographic groups that were so critical to New York's success in the 1990s: young, educated people who moved to New York from other parts of the country and foreign-born immigrants.

Underlying these trends is the economic bottom line of recent decades: during both boom and bust, the city vastly underperforms the rest of the region and the United States as a whole. For instance, between 1969 and 2000—-the two peak years for employment in the city—-the five boroughs lost 75,000 jobs (a 2 percent decline) while the state gained 1.45 million jobs (a 20 percent increase) and the nation added 61.3 million (an 87 percent gain). Meanwhile, over the past two years, the city accounted for 97 percent of all job losses in the state.

This report, funded by the Rockefeller Foundation and based on an eight-month study by the Center for an Urban Future, looks to provide a sober and comprehensive examination of the economic challenges facing New York City in the post-9/11 world. We believe this represents the first comprehensive attempt to assess the many long-term economic, demographic and political threats now facing the city. Most importantly, the report does not stop at diagnostics; it also suggests a new paradigm for growing the city's economy and creating both jobs and prosperity for residents of all five boroughs.

This work was built upon extensive data analysis, a comparison of how the city is faring on a variety of economic measures with its suburbs and with several other major American cities, focus groups with business leaders and roughly 100 interviews with business owners from an array of industries, the directors of business associations, real estate developers, ethnographers, local development officials and government officials from across the five boroughs. It also rests upon an historical analysis of economic trends affecting the city and an in-depth analysis of recent demographic trends affecting New York.

It's easy, and not entirely inaccurate, to blame some of the problems highlighted in this report on the terrorist attacks on the

World Trade Center and continuing fears that New York remains a potential target for future assaults. But the inescapable truth remains that there are also long-term trends at work that the events of 9/11 only reinforced. Most of these have been developing for at least a decade—-sometimes, even longer. And they will continue to impact job growth in the city's high-wage sectors for years to come.

These trends are part of a fundamental secular shift now confronting major cities across the nation and the world: the decentralization of industry. This process applies not only to industries blithely written off by the city establishment, such as wholesale trade and manufacturing, but to favored sectors like the securities industry and professional and business services, which includes everything from lawyers to advertising agencies.

Financial and business services, arguably the core industry of modern New York, serves as a chilling case in point. Even though the city has managed to retain a considerable share of the headquarters operations in these sectors, the bulk of new job creation is taking place elsewhere. For example, the number of new securities jobs created in New York State since the 1987 stock market crash is just three percent of the number created in the other 49 states. The city's share of jobs in the nation's security industry has fallen from 36 percent to 23 percent during this period.

On top of this, technological improvements are allowing many companies to increase revenues without increasing their workforce. "Forecasts for the next decade have the [New York] region as a whole experiencing little growth in the FIRE [Finance, Insurance and Real Estate] sector as technology continues to find substitutes for workers," says William Wheaton, of MIT-based Torto Wheaton Research, one of the nation's top office real estate market analysts.

With technology increasingly freeing firms to create or reallocate new positions in locations of their choosing, there has been a notable increase in the number of companies outsourcing high-end service operations, like software programming, elsewhere in the nation and overseas. At the same time, the expansion of broadband and wireless telecommunications technologies allows more people to work from home, miles away from their clients in Manhattan.

"Globalization and technology have changed economic realities of cities like New York," says Kathryn S. Wylde, president and CEO of the Partnership for New York City, the city's leading advocacy organization for businesses. "Only a handful of industries are now locked into location. There's real estate, there's utilities, but the driver industries are no longer locked into location. 9/11, I think, significantly exacerbated and accelerated this process."

This new economic reality has major implications for New York. "All of these circumstances mean that what we've taken for granted in the past we can't take for granted in the future," Wylde adds. "I don't think the city's economy—-or the economies of any city-—will automatically renew themselves. We've got to be more strategic than in the past."

Fortunately, New York has the tools to overcome these challenges. As this report demonstrates, many of the city's rich natural assets-—from its entrepreneurial immigrant population and its dense concentration of academic research institutions to its diverse neighborhoods and its waterfront—-have gone largely untapped by local economic development officials. These underused resources have significant potential for growth in the decade ahead.

It's also heartening that other large cities like Los Angeles and Houston have overcome similar economic obstacles—-including the 1992 riots in Los Angeles and the meltdown of Houston's energy industry in the 1980s—-to become two of the most resilient urban economies in the nation today. New York has more in common with these cities than it might choose to acknowledge and could certainly learn from what city officials there did to remake their economies.

New York can recharge its economy. But it will require city officials to abandon failed policies of the past and embrace a new vision that stresses economic growth.

Above all else, New York needs to rethink the way it approaches economic development. Among other things, this means a shift away from the city's long-time overemphasis on a few favored sectors and approaches, such as financial and producer services, large-scale commercial development projects and near-exclusive focus on Manhattan's central business districts. Instead, the city should adopt a broader economic strategy to facilitate the creation of a better climate for growing small businesses, tap the potential of the boroughs outside of Manhattan and put New York's human assets to greater use.

This approach can provide New York with a break from the destructive impacts of the current economic monoculture and the tyranny of Wall Street's boom-bust cycle. It will also provide more opportunities for wealth creation throughout the city's diverse neighborhoods.

The blueprint we lay out for restoring New York's economic vitality is intended to address the future by returning to what has fueled the city's past greatness. A renewed focus on smaller firms, diverse industries, entrepreneurs and immigrants makes sense given the realities of the digital era. It also gives New York a chance to recover its rightful place as a premier incubator of entrepreneurship, opportunity and innovation.

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