crain's new york business.com

Weighing New York City Exceptionalism

By Greg David
April 8, 2012 5:59 a.m.

In his new book, Modern New York: The Life and Economics of a City*, being published this week,* Crain's *columnist Greg David explores the major events and controversies of the past half-century that affect New York City even today.*

In the following excerpt, Mr. David offers an assessment of the current state of the city that may surprise even seasoned observers.

Barring another meltdown or terrorist attack, the New York that Mayor Michael Bloomberg will turn over to his successor on Jan. 1, 2014, will be prosperous, safe, sound and a magnet for the rest of the nation, if not the world. The recession had only nicked New York, and its employment is nearing the 1969 peak even with a too-high unemployment rate. His police commissioner, Ray Kelly, has continued to drive down crime for almost 12 years, employing technology to offset a decline in the number of police.

But it will also be a city that is not growing as quickly as the mayor proclaimed. He had expected the 2010 Census to show New York at a record 8.4 million people, on its way to 9 million in the year 2030. When the Census found only 8.175 million people, he yelled foul and claimed that it had missed at least 50,000 New Yorkers. Even if he was right, the number is well below his projection.

The most likely explanation for the missing 200,000 people was that immigration has slowed. Immigrants were attracted to New York because there was so much opportunity and because there were many rundown neighborhoods where housing was cheap. Four periods of prosperity in the postwar period have led to gentrification in every borough and almost every neighborhood. For example, the once downtrodden and dangerous Bed-Stuy area of Brooklyn drew thousands of upscale whites who integrated this once almost exclusively African-American neighborhood. Newcomers to the United States simply headed to cheaper places.

More important, New York will be a city that can grow thanks to the legacy of Deputy Mayor Dan Doctoroff. The city had approached the 1969 employment peak of 3,797,700 three times, and it faltered even before Wall Street collapsed because there was nowhere to put the professional and white-collar jobs being created. Instead, gleaming office towers went up across the Hudson, in other suburbs and in other cities to house those people.

Doctoroff's ambitious agenda to rezone and remake New York broke through the chains of the myth that manufacturing had to be preserved, and now the city has many places, most of them along the waterfront, to build the commercial and residential space to keep the jobs here and allow the population to grow. Whether they will be built, however, may depend on the fate of Wall Street.

The true genius of Wall Street in modern New York was figuring out how to make itself rich. Whatever Wall Street created between the late 1980s and the last boom could not justify Goldman's Lloyd Blankfein being paid nine times more than Salomon's John Gutfreund. Nor could it justify the billions of dollars Steve Schwarzman took from creating Blackstone or Paul Tudor Jones II's wealth amassed from his hedge fund. The irony, of course, is that it was this innovation that made New York so rich.

Wall Street's ability to pay so much for office space and investment bankers' ability to spend unlimited sums on apartments made real estate developers and landlords wealthy. Its bonuses supported luxury retail. Its philanthropy made New York the home of so many nonprofits. The taxes it paid allowed city government to grow so large and to pay its own workers so well.

Wall Street's ability to continue to support the city remains in doubt. Its rescue from the financial crisis may have been only a temporary reprieve. The Dodd-Frank law passed by Congress to ensure that there is never another financial crisis ordered a sweeping change in the structure of Wall Street. For example, firms like Goldman Sachs and JPMorgan must sell off or shut down their proprietary trading units on which they came to rely for a large percentage of their profits. Regulators are insisting that financial institutions build up their capital in the belief that the bigger cushion will make them better able to survive financial shocks.

But it is the opposite approach—borrowing more instead of amassing capital—that made the firms so profitable. Even if the political pressures to reduce compensation ebb—and they have had only a modest impact—lower profits will mean that the firms themselves will cut their pay and bonuses.

Economists and politicians believe that the solution is to diversify the economy so New York is not so dependent on Wall Street. The last recession shows that goal has already been achieved. But it won't save New York. If Wall Street is permanently restructured, New York will be much less wealthy. No industry will pay its people so well that they will be able to generate two other jobs in the city. No industry will pay so many billions of dollars in taxes.

The effects will be wrenching. If financial firms can no longer pay $80 a square foot for office space, building values will decline. No new construction will take place until land prices drop. Both will mean big losses for real estate people. The same will be true for workers. Construction unions will have to accept a sharp decline in their wages and benefits to make new building possible.

The financial squeeze will radiate throughout the city. Without young investment bankers to support the market, apartment prices will decline. The ranks of luxury retailers will thin. Nonprofits will find fundraising much more difficult, and many will close their doors. The public sector will feel the most pain. Wall Street still accounts for 9% of all city tax revenue and 15% of state revenue, which allows Albany to send so much money to the city.

Bloomberg himself has contributed to the illusion that New York can afford whatever it wants, especially when, like Mayor Ed Koch, he made deals to win approval for his big development schemes. When the City Council approved the rezoning of Greenpoint-Williamsburg, the mayor agreed that about 20% of the housing would be set aside for low- and moderate--income people. He also agreed that any high-rises must use union doormen and other workers. Raising the prices on other units finances affordable housing. The higher wages for union doormen mean that renters and condo owners pay higher rents or maintenance charges.

When Willets Point was approved several years later, Bloomberg agreed that 35% of the units would be for lower- and moderate-income people, and that prevailing wages—which means union wages—would be paid to construction workers, building service workers and even the people who staff retail stores.

He also saddled the city with an enormous increase in its debt burden, nearly doubling the amount the city owes, to $105 billion, from $55 billion when he took office. In a less wealthy New York, the city won't be able to afford its pension or debt burden or all the commitments to affordable housing and other amenities in its development projects.

The inability of the mayor to pare the public sector shows the difficulty. For most of 2011, Bloomberg insisted that the city would have to lay off several thousand teachers for the first time in more than a decade. It was a reasonable step to close the big deficits that New York faces in future years. The teachers mounted a vigorous campaign against the job cuts, and the City Council sided with them. In the end, Bloomberg agreed that there would be no layoffs. Some jobs were eliminated through attrition, and the union made concessions that provided some savings. The bulk of the money came from simply increasing his estimate for tax collections. Carol Kellermann, president of the Citizens Budget Commission, said the result just postponed the day of reckoning. She felt as frustrated as had her predecessors in the decade leading up to the fiscal crisis of the 1970s as they railed against reckless financial maneuvers.

The likely candidates in the 2013 mayoral election not only do not accept the mayor's view that some cutbacks in city government are necessary, they pose a formidable challenge to the fundamental Koch-Giuliani-Bloomberg philosophy of putting the economy and the businesses that make it work at the center of policy.

By the beginning of Bloomberg's third term his opponents began coalescing around a series of economic issues. The stark inequality in the city, the high unemployment rate that

stemmed from the recession and the enormous growth in mostly low-paying retail jobs led to the formation of a coalition determined to use city government to improve the lives of those left out of the city's great prosperity. The efforts were sparked by labor unions and the organizations they financed, like the Fiscal Policy Institute, the Working Families Party and other traditionally liberal groups.

The first issue to gain traction concerned paid sick leave. A bill introduced in the City Council originally required any employer with more than 10 workers to provide at least five paid days off for illness. Proponents argued that it was a simple matter of health and fairness. Small businesses regarded the bill as a threat to their very existence. With small margins and a need for great flexibility, they believed that the bill would be enormously costly.

The second measure would require most employers to pay a living wage, usually defined as $10 an hour with benefits and $12 without. Both supporters and opponents believed that the living wage would eventually apply to virtually all companies in the city. This idea was as much anathema to small firms as paid sick leave, and it attracted the ire of larger businesses as well. Developers in particular worried that it would hurt their ability to attract national retailers, which would not be willing to pay higher wages at a store in New York City compared with their operations in nearby suburbs.

Unions and their allies also pushed a third initiative, higher taxes on the wealthy, by making the city's income tax even more progressive.

All three issues are based on the idea of New York as a special place for special people—different from the rest of the country, and even from the suburbs that surround it.

The debates over sick leave, living wage and higher taxes came as the clout of the city's business community declined precipitously. Two decades had elapsed since an organization called the New York Chamber of Commerce had faded into oblivion. The Partnership for New York City, founded by David Rockefeller as a broad business union group to influence policy in the aftermath of the fiscal crisis, was the most visible advocate of business interests. It had evolved into the representative of the city's most important corporations in finance, business services and real estate.

The Real Estate Board of New York, whose membership overlapped some with the Partnership, appeared powerful, too, and looked out for the interests of landlords and developers. They were allies on most issues, but not all. In fact, their clout primarily came because of their alliance with the mayor. Small businesses were virtually powerless. A decade earlier, real estate and finance executives had made sure that their views were considered through large campaign donations to key City Council members. Since the most ambitious council people aspired to citywide office, they courted business leaders because they knew they would have to ask them for money for expensive campaigns. Over time, the city enacted ever-smaller limits on the amount any individual could give. It introduced a taxpayer-financed system that provided city money that matched only small contributions.

Finally, Mayor Bloomberg agreed to a sweeping restriction on contributions from executives whose companies did business with the city.

By essentially eliminating business contributions, the city had empowered labor unions because they could still give money and they could mobilize workers for campaigns. The election of City Council members depended almost exclusively on whom the unions supported, either directly or through the Working Families Party, a union-created political party. Of the 51 members, only one was a businessperson. The council moved sharply to the left, especially when compared with the Dinkins era, when the council fought higher taxes and reflected the values of the city's middle class.

The leading Democratic candidates for the 2013 mayoral race all embraced the challenge to the Koch-Giuliani-Bloomberg philosophy. All three—Comptroller John Liu, the first Asian-American elected to the council, Public Advocate Bill de Blasio and council Speaker Christine Quinn—were elected with strong Working Families Party support. Quinn positioned herself as the most moderate and blocked the sick leave bill, although she did so not because it was bad policy but because the economy was too weak to impose it on small businesses.

It is unclear whether a Republican or independent candidate will emerge to capitalize on that sentiment as Rudy Giuliani did in 1993 and Bloomberg did in 2001. The lack of such a candidate in 2009 contributed to Bloomberg's decision to run again. If the city faces another economic or fiscal crisis, business executives will try desperately to find a candidate. If the economy continues to recover, they may decide to make the best of whoever wins the Democratic primary, as they did when David Dinkins beat Koch and when they kept their distance from Giuliani in his first campaign.

Wall Street may save the city again, as it has done so often in modern New York. The investment bankers, traders, hedge fund executives and private equity specialists may concoct another financial innovation that propels the markets and sends their own pay and bonuses soaring. If Wall Street does that, New York will be rich again, tax revenues will be plentiful and the political disputes over handing out the spoils affordable. If not, the next mayor will face the daunting task of leading New York into a future much less prosperous than its present. Or the next mayor could ignore those forces and push New York into a new era of expansive government, as John Lindsay did. The result could well be another economic and fiscal cataclysm.

From Modern New York: The Life and Economics of a City *by Greg David. Copyright © 2012 by the author and reprinted by permission of Palgrave Macmillan, a division of Macmillan Publishers Ltd.*

Read more:
http://www.crainsnewyork.com/article/20120408/ECONOMY/304089992#ixzz1toxnhxEN