

# Sitar–Rutgers

## Regional Report

James W. Hughes and Joseph J. Seneca, editors

## National Economic Downturn Confronts New Jersey in 2008

By James W. Hughes and Joseph J. Seneca

**N**ew Jersey's employment growth during the past four years of national economic expansion did not come close to the historical annual averages of job gains during the state expansions of the 1980s and 1990s. Even though New Jersey added almost 100,000 private-sector jobs from 2004 to 2007, the total number of private-sector jobs in the state in December 2007 was only 22,500 jobs greater, or 0.7 percent, than in December 2000, the cyclical peak of the last expansion (3,452,500 jobs versus 3,430,000 jobs). Consequently, it is not surprising that the state's office vacancy rates have remained stubbornly

high, despite (until recently) a national economy that was growing quite vigorously. Now, those national economic tailwinds of the last four years have shifted dramatically and have, instead, become formidable headwinds confronting the New Jersey economy as it faces the new year.

### A National Economy at Risk

Early this year, it became apparent that the current national expansion had achieved senior citizen status and was becoming increasingly vulnerable. As of December 2007, the expansion reached 73 months in length, or a *(continued, page 4)*

## New Jersey Office Market Proving Stable

By Sachiyo Asakawa; Gregg Nowell, Senior Vice President;  
and Christopher Santoro, Assistant Vice President

**D**espite economic instability caused by a serious mortgage crisis and an uncertain financial climate, the Northern and Central New Jersey Office market was stable throughout the year in 2007. The year began and ended with a total vacancy rate of 15.3 percent, while the asking rate increased by \$0.58, from \$25.23 to \$25.81. Year-to-date (2007, 1Q–4Q) net absorption for the overall Northern and Central New Jersey office

market was a positive 815,000 square feet, making 2007 the third consecutive positive year. Leasing activity totaled 13.35 million square foot, almost identical to the 13.38 million square feet seen at the end of 2006.

The situation was quite similar for the Class A market. The vacancy rate for Class A office space was also stable, with only a 0.1 percent change, from 18.1 percent at the beginning of *(continued, page 2)*

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## 2 Office Market Stable, continued

*The Hudson Waterfront submarket continued to be the magnet for global financial giants.*

Northern and Central New Jersey Total Office Market Fourth Quarter 2007									
County	Buildings	Total Inventory	DIRECT		TOTAL (Direct and Sublet)		Average Asking Rent	QTD Net Absorption	2007 YTD Net Absorption
			Space Available	Vacancy Rate	Space Available	Vacancy Rate			
Bergen	570	29,523,378	3,789,743	12.8%	4,405,156	14.9%	\$27.44	(5,677)	329,111
Essex	400	28,490,457	2,855,815	10.0%	2,959,554	10.4%	\$25.72	44,523	(49,562)
Hudson	171	23,912,884	2,221,273	9.3%	2,720,357	11.4%	\$28.36	451,121	249,574
Hunterdon	63	2,028,586	664,258	32.7%	668,822	33.0%	\$23.57	(100,704)	(193,810)
Mercer	352	16,935,067	2,604,917	15.4%	2,749,051	16.2%	\$27.63	18,985	46,642
Middlesex	477	29,018,426	4,002,804	13.8%	4,815,844	16.6%	\$24.36	401,592	690,921
Monmouth	438	15,606,518	1,935,111	12.4%	2,031,858	13.0%	\$22.43	123,880	(329,458)
Morris	430	29,906,744	5,152,138	17.2%	6,140,526	20.5%	\$27.03	(79,851)	(3,255)
Passaic	159	6,599,332	921,090	14.0%	968,060	14.7%	\$21.94	28,929	43,781
Somerset	279	21,057,749	3,058,071	14.5%	4,334,243	20.6%	\$24.16	(186,594)	247,009
Union	315	11,801,003	921,179	7.8%	1,098,661	9.3%	\$25.62	6,905	(215,953)
<b>Total</b>	<b>3,654</b>	<b>214,880,144</b>	<b>28,126,399</b>	<b>13.1%</b>	<b>32,892,132</b>	<b>15.3%</b>	<b>\$25.81</b>	<b>703,109</b>	<b>815,000</b>
Central NJ	1,861	94,418,763	12,522,082	13.3%	15,029,657	15.9%	\$24.73	364,768	439,161
Northern NJ	1,793	120,461,381	15,604,317	13.0%	17,862,475	14.8%	\$26.71	338,341	375,839

*Notes:* Includes all office buildings, 10,000 square feet and greater. Does not include owner-occupied facilities. Total Inventory, Space Available, and Net Absorption figures are in square feet.

the year to 18.2 percent at the end of the year. The average asking rent climbed by \$0.85, from \$27.16 to \$28.01. Leasing activity was a little slower at 9.6 million square feet, compared with 12.3 million square feet at the end of 2006.

Throughout the year, the Hudson Waterfront submarket continued to be the magnet for global financial giants. The total vacancy rate dropped to 9.8 percent, and the average rent hit \$32.36 per square foot. Deutsche Bank, Lehman Brothers, Merrill Lynch, and BNP Paribas all have offices in the market through either relocation or expansion of current space. Although the super-

modern high-rise office clusters in the Hudson Waterfront submarket appear to be flourishing more than ever, industry professionals are hesitant to say that this unique submarket depicts the real condition of the New Jersey office market because the Hudson Waterfront submarket is mainly spilled over from the Manhattan market.

After several quiet years, the Parsippany submarket experienced significant leasing activity in 2007. The direct vacancy rate for Class A space dropped to 12.4 percent in the fourth quarter, which was the lowest since the

Northern and Central New Jersey "Class A" Office Market  
Fourth Quarter 2007

County	Buildings	Total Inventory	DIRECT		TOTAL (Direct and Sublet)		Average Asking Rent	QTD Net Absorption	2007 YTD Net Absorption
			Space Available	Vacancy Rate	Space Available	Vacancy Rate			
Bergen	81	13,113,896	2,081,547	15.9%	2,609,675	19.9%	\$29.52	(90,195)	102,233
Essex	62	15,007,566	1,525,695	10.2%	1,615,499	10.8%	\$27.94	86,695	92,416
Hudson	49	19,189,530	1,695,775	8.8%	2,164,659	11.3%	\$30.63	486,825	312,670
Hunterdon	8	811,320	400,685	49.4%	400,685	49.4%	\$25.34	(99,692)	(118,302)
Mercer	75	7,612,268	1,604,365	21.1%	1,687,500	22.2%	\$30.96	24,348	(23,010)
Middlesex	121	17,735,512	2,392,191	13.5%	3,065,556	17.3%	\$26.16	129,354	323,513
Monmouth	56	5,371,981	750,757	14.0%	776,749	14.5%	\$26.36	16,619	(299,665)
Morris	121	18,386,277	3,770,218	20.5%	4,549,042	24.7%	\$29.64	(111,561)	231,997
Passaic	16	2,042,045	492,062	24.1%	510,031	25.0%	\$23.65	14,872	(8,695)
Somerset	101	15,092,093	2,306,845	15.3%	3,567,624	23.6%	\$24.64	(140,288)	252,995
Union	31	3,922,689	404,379	10.3%	579,865	14.8%	\$28.48	11,027	(172,103)
<b>Total</b>	<b>721</b>	<b>118,285,177</b>	<b>17,424,519</b>	<b>14.7%</b>	<b>21,512,326</b>	<b>18.2%</b>	<b>\$28.01</b>	<b>328,004</b>	<b>694,049</b>
Central NJ	384	49,734,543	7,458,537	15.0%	9,677,294	19.5%	\$26.59	41,060	81,730
Northern NJ	337	68,550,634	9,965,982	14.5%	11,849,591	17.3%	\$29.16	286,944	612,319

Notes: Includes all office buildings, 10,000 square feet and greater. Does not include owner-occupied facilities. Total Inventory, Space Available, and Net Absorption figures are in square feet.

*The top two largest office leases of the year in the entire Northern and Central New Jersey office market took place in the Parsippany submarket.*

end of 2002. The top two largest office leases of the year in the entire Northern and Central New Jersey office market took place in the Parsippany submarket. The Parsippany submarket was on the rise throughout the year, driven by pharmaceutical companies. The Medicines Company took a nearly 173,000-square-foot vacant building at 8 Sylvan Way in the third quarter, and IMS Health leased a 120,000-square-foot building in the Waterview Corporate Park, another long-vacant building.

Whereas the active Hudson Waterfront submarket enjoys mostly the spillover effect from the Manhattan office market, the Parsippany submarket

offers companies with the traditional New Jersey office market advantages such as excellent highway accessibility and an abundance of skilled labor. Thus, while this year's boom of the Parsippany submarket gave industry professionals some optimism for the New Jersey office market, it is too early to tell if this was only a temporary resurgence of the Parsippany submarket or a sign of recovery of the larger New Jersey office market.

Several Central New Jersey submarkets saw some light during the year with regard to Class A office space. Middlesex County, with approximately 30 million square feet, experienced a *(continued, page 7)*

## 4 Economic Downturn, continued

*Between June 2004 and June 2006, the federal funds rate was raised 17 times in quarter-point increments.*

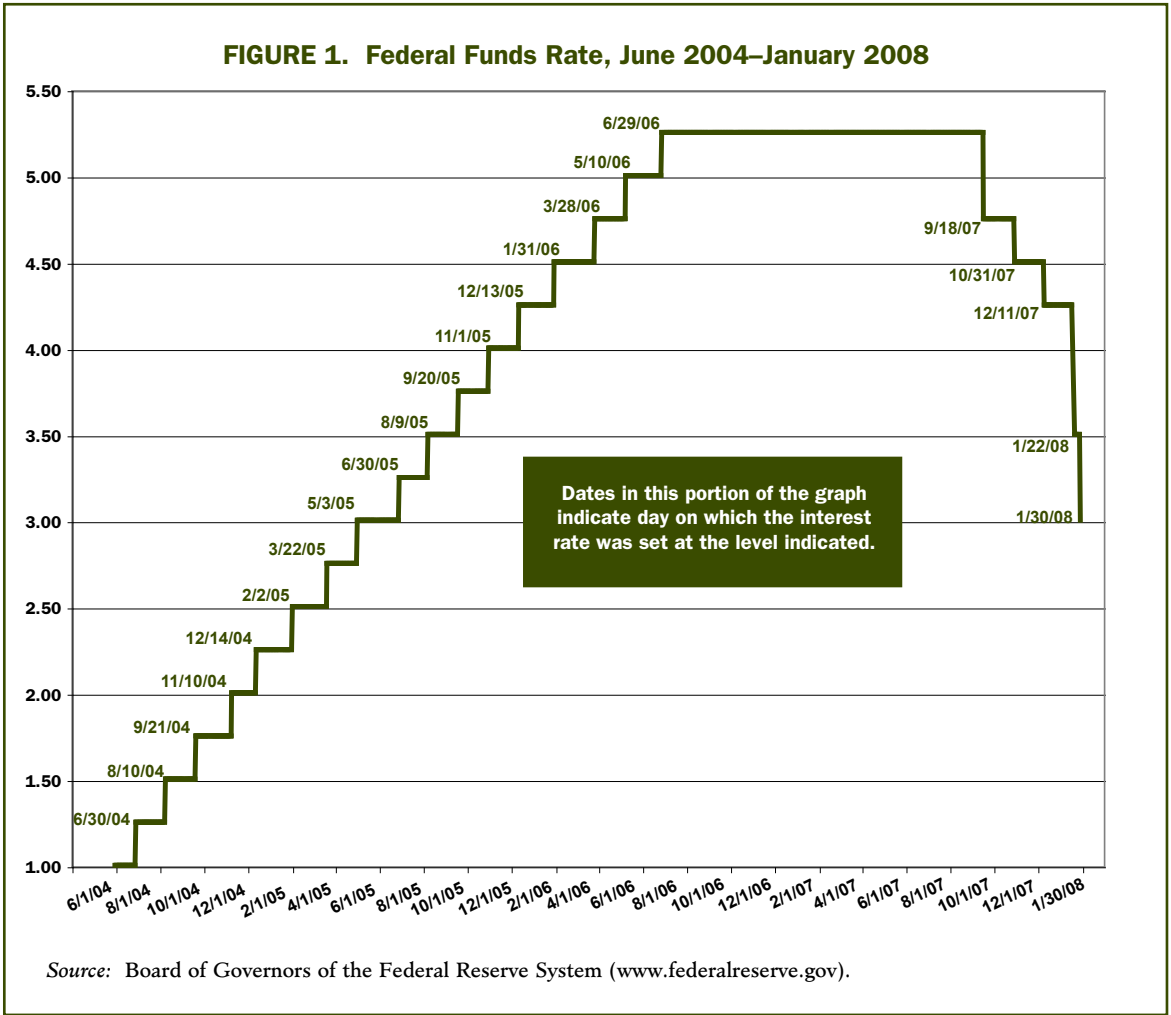
year and a half beyond the 57-month average length of the 10 post–World War II expansions. Thus, it was becoming “chronologically gifted”! But, despite historical averages, all economic expansions are different. In fact, it is the Federal Reserve (Fed) that usually does them in! That may be happening right now, or it may have already happened. In 2004, the Fed sensed that robust economic growth (caused, in part, by the Fed’s own prolonged low-interest-rate policy) was starting to stoke inflation. As a result, the Fed reversed course and started to increase interest rates. Between June 2004 and June 2006, the federal funds rate was raised 17 times in quarter-point increments, increasing the rate from 1.0 percent to 5.25 percent. As former Fed chairman William McChesney Martin quoted in a 1955 speech before the New York chapter of the Investment Bankers Association of America, “The Federal Reserve . . . is in the position of the chaperone who has ordered the punch bowl removed just when the party was really warming up.” In other words, raise interest rates when a booming economy threatens to accelerate inflation.

Apparently, the Fed’s moves were more than successful. In 2005 and 2006, national employment growth averaged a robust 2.3 million jobs per year. But as a delayed result of Fed interest rate increases, job growth decelerated sharply in 2007. Overall, the national employment gain in 2007 fell to 1.1 million jobs, a decline of 52 percent from the pace of the previous two years. And, during the last six months of the year (June 2007–December 2007), employment growth slowed to an annual rate of just under 1 million jobs, which was far less than half of the pace of 2005 and 2006. Given this employment slowdown along with continued turmoil in the nation’s housing markets, the increasing severity and dispersion of the negative effects of the subprime lending debacle, and broader turbulence in financial markets, the Fed finally shifted gear and lowered the federal funds rate from 5.25 percent to 4.75 percent on September 18, 2007 (figure 1). The Fed lowered it again to 4.5 percent on October 31, and

yet again to 4.25 percent on December 11. Still, some observers thought that this monetary medicine was too little and too late. The sharp 0.3 percentage-points spike in the national unemployment rate in December was evidence in support of such a view since an increase of that scale usually foreshadows a recession.

The Fed became increasingly alarmed in the first weeks of January by worsening economic conditions in the United States. Goldman Sachs switched its forecast to an “outright recession call” during the second week of the month and predicted that the Fed would reduce the federal funds rate to 2.5 percent from 4.25 percent. They were quite prescient. Following the meltdown in international financial markets on the Martin Luther King holiday in the United States, the Fed lowered the federal funds rate by 75 basis points to 3.5 percent at a hastily called policy meeting on January 22. According to *Business Week*, this was the largest reduction by the Fed since it started setting a target for that benchmark rate in 1990. Then, at its regularly scheduled meeting on January 30, the Fed cut the federal funds rate again, this time by an additional 0.5 percent, or 50 basis points, to 3.0 percent—a level very close to the Goldman Sachs call made earlier in the month.

In addition, the President and Congress, also becoming concerned with the unraveling of the equity markets, weakening employment, and persisting deep problems in housing, put partisanship aside (well, maybe) and—in what was warp speed for Washington—came close to agreement on a fiscal stimulus package. As this issue goes to press, the final components and size of the stimulus are still to be determined, but a key feature will be temporary tax rebates. The goal is to provide a boost of fiscal adrenaline to the consumer and thereby ensure that consumer spending, which comprises more than 70 percent of gross domestic product, keeps growing. While some of the tax rebates will leak into spending on imports, and some may even be saved or used to pay down consumer debt, the aggregate size of the rebates (well over \$100 billion) will mean that the weakened battery of the consumer spending engine of the economy will get a jump



*The time lag between changes in interest rates and the subsequent positive effects on the economy is estimated to be six months to more than a year.*

start. In addition, some tax incentives for business investment will also be part of the fiscal package.

The possible rapid agreement by the President and Congress on a fiscal stimulus indicates the fear of both parties that they would risk voter retaliation later in this presidential election year for any failure to respond now to the obvious signs of an economy in trouble. Even if an agreement is quickly reached, rebate checks for taxpayers will arrive only in May or later. Any positive spending effects of the business investment incentives will occur with even a longer lag. Moreover, the time lag between changes in interest rates and the subsequent positive effects on the economy is estimated to be six months to more than a year.

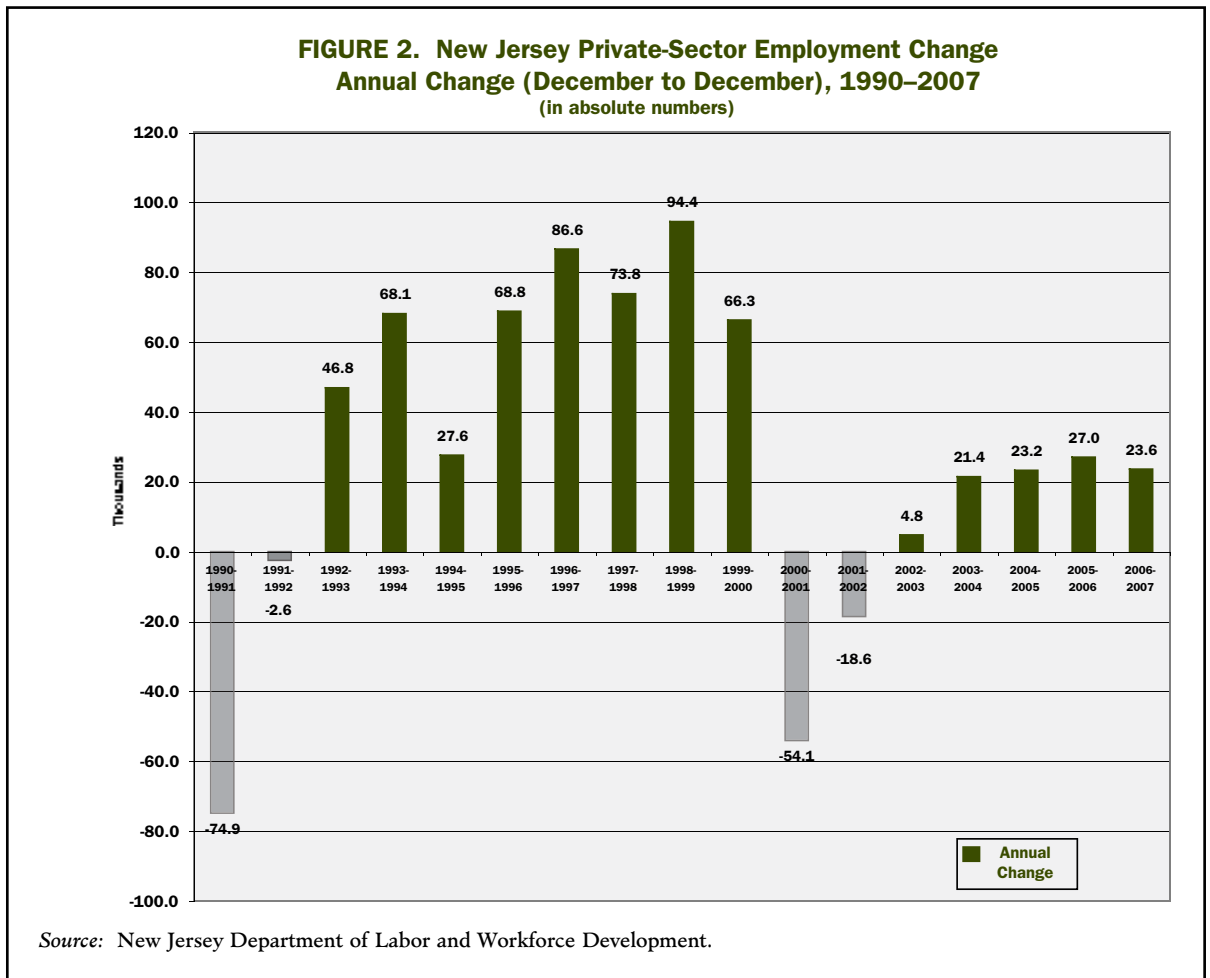
Thus, even with the aggressively expansionary monetary policy of the Fed and an accompanying large federal fiscal stimulus, the U.S. economy during the first half of 2008 remains at risk of recession. A probable scenario is that the combination of both monetary and fiscal policies will help to mitigate the duration and depth of an economic slowdown, but not avoid it. This is particularly worrisome given the already slow-growth trajectory of the New Jersey economy.

### New Jersey

The December payroll employment report provided preliminary job figures for (*continued, page 6*)

## 6 Economic Downturn, continued

The state has to confront a troubled national economy in 2008 with only modest economic momentum.



the year 2007. Measured from December 2006 to December 2007, New Jersey added 23,600 private-sector jobs, down nearly 13 percent from the 27,000 private-sector jobs gained in 2006. During the last four expansion years (2004–2007), the state added an average of about 24,000 private-sector jobs per year. As noted in the November 2007 of the *Sitar-Rutgers Regional Report*, during the last two economic expansions (1982–1989 and 1992–2000) New Jersey gained an average of 74,000 private-sector jobs per year, or more than triple the current pace (see figure 2). In fact, the slowest year of private-sector employment growth during the expansion of the 1990s occurred in 1994–1995, when 27,600 new jobs were added. It is

noteworthy that only one year (2005–2006) thus far in the current decade comes close to what was the *weakest* year in the previous expansion. So the state has to confront a troubled national economy in 2008 with only modest economic momentum.

It should also be noted that the employment data for 2003 through 2007 will be subject to the annual Bureau of Labor Statistics benchmark revisions that will be released on February 27, 2008; thus, the numbers cited above may be adjusted up or down, altering these conclusions. Nonetheless, given the shaky national economic forecast, particularly for the first half of the year, it will be difficult for New Jersey to maintain its 2004–2007 pace of private-sector employment growth in 2008. ■

**Northern and Central New Jersey  
Top 10 Office Leases, 2007**  
(by square footage)

	<b>Building</b>	<b>Submarket</b>	<b>Tenant</b>	<b>Space (sq. ft.)</b>	<b>2007 Quarter</b>
1	Chubb Institute	Parsippany	The Medicines Company	172,998	3Q
2	100 Kimball Drive	Parsippany	Deloitte & Touche LLP	160,047	2Q
3	Gateway Center 4 <sup>†</sup>	Newark	McCarter & English LLP	155,000	2Q
4	South Plainfield Corporate Center <sup>†</sup>	Route 287	Motorola	145,000	3Q
5	225 Summit Avenue	Upper Parkway	Barr Pharmaceuticals	144,000	2Q
6	429 Ridge Road	Princeton North	[not available]	142,385	3Q
7	Atrium 3 <sup>†</sup>	Meadowlands	Buck Consultants	124,060	4Q
8	Turner	Parsippany	IMS Health Incorporated	120,000	2Q
9	2 Hilton Court	Parsippany	Daiichi Sankyo	116,452	2Q
10	Somerset Corporate Center Bldg. 5	Route 22 West	Qualcomm Incorporated	115,013	2Q

Note: † Indicates renewal.

Source: CoStar Group, Inc.

*Approximately 1.8 million square feet of space was delivered in 2007, compared with 950,000 square feet at the end of 2006.*

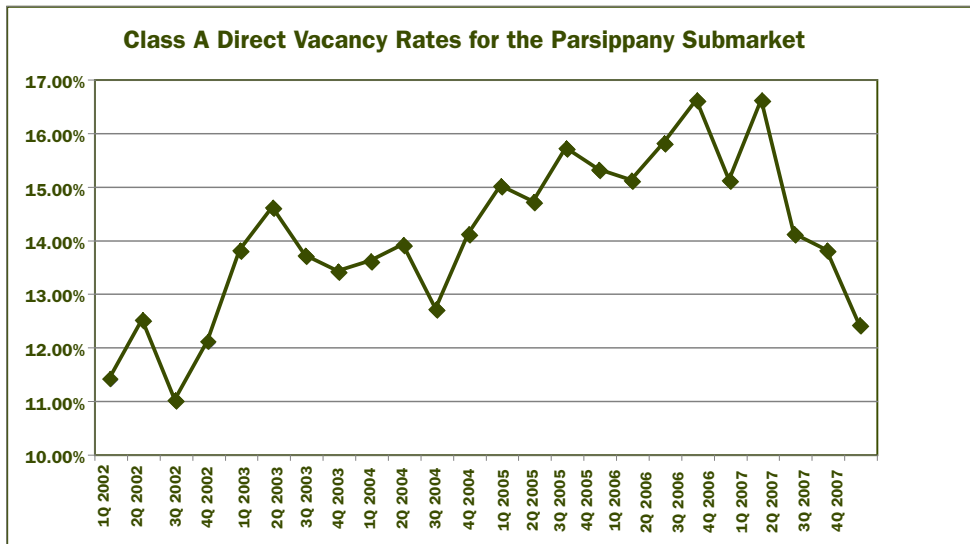
significant drop in the total direct vacancy rate, from 18.1 percent at the end of 2006 to 16.6 percent at the end of 2007. The I-287 corridor office submarket, which has experienced a more than 30 percent vacancy rate for the last few years, fell to 25 percent. A couple of large communications-related companies signed significant leases in this submarket earlier in the year. Cablevision took 64,125 square feet at 30 Knightsbridge Road, a former AT&T building, in Piscataway. This “comeback” of the communications industry to an area that once flourished as a communications center was good news to the market.

The Princeton submarket experienced a sluggish first half-year, with vacancy rates as high as 17 percent due to the delivery of several large, new spaces since the last quarter of 2006. Contrary to

some concerns, the submarket regained its strength, and the vacancy rate dropped to 16.7 percent at the end of the year. Novo Nordisk Pharmaceutical, one of the leading companies in diabetes care headquartered in Denmark, took a 166,282-square-foot building at 1100 Campus Road in November. Comcast signed a 60,000-square-foot lease at 1100 Cornwall Road. A total of 1.43 million square feet was leased in 2007, with 917,000 square feet of new delivery to the market.

Approximately 1.8 million square feet of space was delivered in 2007, compared with 950,000 square feet at the end of 2006. Nearly half of the new delivery occurred in the Princeton submarket and in the Monmouth County market. The largest building delivered was 1 University Square in Princeton, a Class A, 316,000-square-foot, (*continued, page 8*)

## Office Market Stable, continued



Source: CoStar Group, Inc.

five-story building currently marketed at \$36.50 per square foot. Monmouth County delivered 352,388 square feet of new space. Encouraged by the trend toward low vacancy rates in this market in the last couple of quarters, developers appear optimistic about the future of the market. There are currently nine buildings, totaling 455,744 square feet, under construction in Monmouth County.

The Northern and Central New Jersey office market proved its strength and consistency in 2007 despite a discouraging financial climate. The comeback of historically strong industries like pharmaceuticals and communications to some office markets was welcomed by industry professionals. However, 2007 was more a steady year than an active year. Sitar Company's industry professionals continued to observe companies' caution about the amount of space being leased and future growth projections. It appears that more companies are consistently seeking smaller Class A facilities—in the 2,000 to 10,000 square-foot range—in Middlesex and Monmouth counties. The landlord who is willing to divide larger spaces and

provide limited capital tenant improvement is most likely to lease existing available space. We expect this trend to continue throughout 2008 as well. While larger corporate users are wise to exercise some caution in these uncertain times, there is certainly evidence of significant interest in the Northern and Central New Jersey office market from Fortune 500 companies. ■

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