Desperately Seeking Traction

By James W. Hughes and Joseph J. Seneca

As the final quarter of 2002 unfolded, New Jersey’s economy still had not yet been able to gain full traction. Total payroll employment unexpectedly fell by 3,300 jobs in September 2002, and dipped below 4 million jobs for the first time since May 2000, a full 28 months earlier. Thus, the state’s economy is still struggling, and cumulative employment losses are starting to mount. It increasingly looks like New Jersey is entering a prolonged period of slow economic growth, commencing with a modest economic recovery in 2003. To provide a basic perspective on this less-than-ebullient outlook, a look in the rear-view mirror is warranted because history can reveal something about the future.

New Millennium in Review

So far during the new millennium, New Jersey has gone from a “go-go” economy in 2000, then to a “slow-go” economy in 2001, and finally to a “no-go” economy in 2002. The “go-go” economy was the final phase of the “Great Transmillennial Expansion,” which spanned from May 1992 to June 2001 (Table A). Initially, the expansion started slowly, commencing with a period of jobless economic growth. It actually took until 1997—a full five years later—for New Jersey to recover all of the job losses suffered in the 1989–1992 recession! Obviously, the state was emerging from a deep economic hole. But a key lesson for today is that recovery periods can be quite long. (continued, p. 2)

Opportunity Knocks on the Route 287 Corridor

By Gregg J. Nowell and John Shibles

New Jersey serves as a “home base” to many Fortune 500 companies and is also a leading “host state” for commuters traveling into Manhattan. The Route 287 corridor is located right in the center of New Jersey’s commercial markets and offers a diversified labor pool with reasonable access to a variety of housing defined as both affordable and affluent. With current office vacancies at their highest levels in recent memory, companies are exploring the Route 287 corridor as a means to reduce operating costs and tap into a skilled and affordable labor market.

Route 287 may be a north/south highway, but current demand for commercial office market space along the corridor is almost exclusively southbound. In recent years, the Bridgewater Market to the north and the Woodbridge/Edison market to the south have both enjoyed strong leasing activity. The 287 Corridor market centering on Piscataway has historically lagged behind these markets and continues to do so in 2002. There are currently at least a dozen blocks of space of over 100,000 square feet in size along Route 287 from Edison to Franklin Township. Furthermore, an additional dozen blocks of available space 100,000 square feet or more can be found within a short distance of the corridor as one drives from Franklin Township north towards the Bridgewater Market. Overall, nearly one-third of 100,000-plus square foot units available in the eleven county region can be found along the (continued, p. 8)
After finally returning to 1989 job levels in 1997, the capstone of the Transmillennial Expansion was reached—the extraordinary economic growth that then took place between 1997 and 2000. This leads to the second lesson of the “go-go” years: the 1997 to 2000 period encompassed a once-in-a-generation growth surge stemming in part from an unprecedented business capital investment bubble as well as over-exuberant corporate expansion. In other words, the period constituted a wild economic party. It is this growth experience that has retained a lingering sense of being “normal,” setting our basic growth expectation. However, this is obviously not the case; 1997 through 2000 are not the appropriate years to use as a projection baseline, and not the appropriate years to use as a set of expectations for the future. It is unlikely that New Jersey will ever see growth of that scale during this decade. Moreover, wild economic parties often lead to prolonged hangovers. The return to full economic sobriety could take a long time, as the early 1990s’ recovery period attested.

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In any case, a new economic reality gradually unfolded in 2001. The state moved first to “slow-go” and then to “no-go.” New Jersey’s boom finally expired in June 2001 after adding 586,700 jobs (Table A). A job-creating economy was then fully transformed into a job-devouring economy. Between June 2001 and September 2002, New Jersey lost 34,600 jobs. To date, this is not that severe an employment loss. For example, it is dwarfed by the 258,600 jobs lost in the 1989-1992 recession (Table A). Thus, by traditional statistical measures, it is still a recessionette in New Jersey. Nonetheless, our recessionette has obviously created more than enough real economic pain to date.

What are the lessons from the “no-go” economy, and what do the characteristics of the recession reveal about the “soon to be” recovery? First, the national slowdown initially began as a traditional manufacturing recession in the summer of 2000. Since New Jersey is no longer a manufacturing state, New Jersey was somewhat insulated from this part of the downturn. The downside is that the state will probably get a below-average boost when manufacturing finally recovers.

Second, New Jersey was finally enveloped by the national slowdown in 2001 by the aftereffects of the bursting of America’s extraordinary business capital investment bubble centered on information technology and telecommunications. Lucent stands as the New Jersey poster child of the current problem. The ramifications is that a really strong recovery will depend on the return of business capital
Desperately, continued

investment. However, the economic hangover from the wild investment binge will still take time to fully pass.

Third, the new economy retreat also reflected a new type of slowdown. Since 1946, every slowdown in this country has been driven by rising interest rates, consumer spending declines, and a slump in housing activity. The recent recession, however, was quite different. It was led by a collapse in business capital investment, while consumer spending and housing, supported by record low interest rates, kept the economy afloat. This is a unique situation in the current era. The downside is that it limits future growth potential. Because housing and consumer spending remained robust during the recession, there is limited upside here.

Fourth, and finally, is the productivity paradox. Productivity nationally remained strong throughout the recession. This pleasant surprise may prove to be a mixed blessing. An old adage is that one person's productivity gain is another's continued unemployment. Since productivity allows for the production of more with fewer workers, the need for fewer workers will result. So the advent of strong job growth will be pushed further into the future.

The economic bottom line is that the four unique characteristics of the “no-go” years point to a less than vigorous expansion during 2003. Thus, there will not be a sustained return to the level of growth that characterized the second half of the 1990s. The state’s post-recession world will be one of much more modest long-term growth. In fact, jobless economic growth appears to be New Jersey’s immediate destiny—a pattern similar to that of a decade ago as the economy emerged from the 1989-1992 recession.

The Recession’s Scorecard

New Jersey’s employment reached a historic high in June 2001 at 4,034,300 jobs, the peak month of the Great Transmillennial Expansion. (continued, p. 4)

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The resilience of construction employment represents a unique feature of New Jersey’s 2001–2002 recession.

4 Desperately, continued

It lasted for 109 months, falling one month short of tying the longest New Jersey expansion on record. The subsequent recession has now reached fifteen months in length in September 2002. It is now a mature downturn, two months longer than the average postwar recession (13 months) in New Jersey.

During this fifteen-month economic retreat, the state’s economy contracted by 34,600 jobs, falling to a total of 3,999,700 jobs (Table B). About 90 percent of the total losses were accounted for by manufacturing (-30,600 jobs). Thus, despite this being the first new economy recession, it is the old economy (manufacturing) that has again been impacted most severely. The transportation and public utilities sector was the second biggest loser (-12,000 jobs), due to the impacts of utility deregulation, the telecommunications bust, and the post-September 11 difficulties of the airline business. In addition, retail trade lost 4,200 jobs. Conversely, the finance (+6,400 jobs) and services (+3,200 jobs) sectors actually registered growth during the downturn, as did government (+2,400 jobs).

Construction Resiliency

The resilience of construction employment represents a unique feature of New Jersey’s 2001–2002 recession. The history of the expansion and contraction of construction employment as New Jersey traversed business cycles proves illustrative. During the great boom of the 1980s (1982–1989), construction employment in the state increased from 107,000 jobs to 164,700 jobs, a gain of approximately 54 percent. This was due to the great office construction boom and the resulting real estate bubble. However, the boom ultimately imploded, and the 1989–1992 recession ensued. By the end of this downturn (1992), construction employment fell to 107,600 jobs, the same level as a decade earlier. The spectacular gains of the 1980s were fully erased.

The 1990s have been praised as a period of disciplined real estate lending and construction, following the reforms instituted in the early 1990s. Nonetheless, construction employment again soared during the 1992–2001 expansion, increasing by 50 percent to the 161,000 level by June 2001, the start of the most current recession (Table B). On the upside, construction again proved to be highly cyclical, showing the fastest rate of job growth among the eight major industrial sectors during the Great Transmillennial Expansion. However, during the ensuing downside (June 2001 through September 2002), construction employment failed to retreat, the expected recessionary pattern. In fact, by September 2002, construction employment reached 162,000 jobs, 1,000 higher than at the beginning of the downturn.

Thus, during the most recent recession, construction has proved to be an economic locomotive rather than a caboose, keeping the state—as well as the nation—from tipping into a much more severe recession. The downside of this remarkable performance is that it limits our future growth potential. Traditional recessions generate significant pent-up consumer demand and significant pent-up housing demand. Satisfying this demand is what usually jump-starts economic recoveries. But because housing, construction, and consumer spending remained robust during the recession, there is limited upside here. Thus, the New Jersey economy awaits a strengthening in national economic activity. The aggressive use of expansionary monetary policy by the Federal Reserve and the fast return to federal deficit spending have kept the recession mild. But an acceleration in economic activity depends on a return to business investment spending, which requires improved sales and profit expectations.
A Year Later, Sublease is Still the Story
By Matthew J. Dolly

The tragedy of September 11 had an enormous impact on the office market in the New York Metropolitan area. The destruction of the World Trade Center ("WTC") caused an increased demand for office space in the New Jersey market. At the time the office market was headed for its sixth consecutive quarter of increased sublease space, but the demand for space was projected to increase as many WTC tenants began scrambling for office space, searching particularly in the New Jersey market. Through the remainder of September and continuing on into the fourth quarter of 2001, several New Jersey office tenants put much of their oversupply of space on the market for sublease in hopes that it would be taken by a displaced WTC tenant. Unfortunately, less space than expected was leased by displaced WTC tenants, and the amount of sublease space available on the market has increased ever since.

In the eleven-county region of northern and central New Jersey there are nearly 14 million square feet of office sublease space available. This indicates an increase of 1.5 million square feet of sublease space from the second quarter of 2002 and an increase of nearly five million square feet from the third quarter one year ago. Somerset and Hudson counties experienced the largest increases in sublease space availability. Somerset’s increase was largely due to Lucent Technologies moving out of the Warren Corporate Center. Lucent vacated so much space during the third quarter that Somerset moved ahead of Morris and Middlesex as the county with the largest amount of sublease space available, reporting nearly 2.9 million square feet. Similarly, Hudson County suffers from an overabundance of sublease space. There are large blocks of space offered on the waterfront in newly constructed buildings that were preleased but never occupied (continued, p. 6).
some larger tenants, such as Charles Schwab at Harborside Plaza 10 in Jersey City.

In addition to what became available in Somerset and Hudson counties, there were some additional large blocks of space added to the market in other counties through the third quarter. In Morris County, American Express and Global Crossing put a combined total of 520,000 square feet on the market. Pharmacopeia has vacated 86,000 square feet in Monmouth Junction, Middlesex County. In Mercer County, a total of 112,000 square feet has come back on the market at 7 Roszel Road in West Windsor. Overall, there are 30 blocks of sublease space greater than 100,000 square feet available in the region, compared to 49 blocks of new and relet space.

However, while large blocks of space continue to saturate the market, sublease availabilities and overall vacancy rates have stabilized in most areas of the region, providing some encouragement that leasing activity has improved.

Absorption statistics improved during the quarter, largely due to occupancy taken by tenants who had preleased buildings under construction. That is very evident on the Hudson Waterfront, where several large tenants have taken occupancy during the quarter in Jersey City and Hoboken, including Forest Laboratories, Fidelity National Financial, Tradeweb, Sun America, Andover Brokerage, and John Wiley & Sons. In addition, Mizuho and Instinet took occupancy at Harborside Plaza 10 in space subleased from Charles Schwab. Net absorption was positive in Union County as several tenants took occupancy at Connell Corporate Center in Berkeley Heights. Leading the way was Agere Systems, a Lucent technologies spin-off, which leased 110,000 square feet in the new building at Connell Corporate Center IV.

In Morris County, large leases have steadied the vacancy rate and amount of sublease space available. In Parsippany, both Cendant and Gemini subleased large blocks of space. Cendant took 145,000 square feet previously occupied by Nabisco and Gemini Technical Services moved into 205,000 square feet at Gatehall II. Wells REIT later purchased Gatehall II.

### Northern and Central New Jersey Class “A” Office Market
#### Third Quarter 2002

<table>
<thead>
<tr>
<th>County</th>
<th>Buildings</th>
<th>Total Inventory</th>
<th>Available Space</th>
<th>Vacancy Rate</th>
<th>Sublet Available</th>
<th>Average Asking Rent</th>
<th>3rd. Qtr. Net Absorption</th>
<th>2002 YTD Net Absorption</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bergen</td>
<td>131</td>
<td>17,922,487</td>
<td>1,689,088</td>
<td>9.4%</td>
<td>1,375,958</td>
<td>$26.60</td>
<td>187,513</td>
<td>8,418</td>
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<tr>
<td>Essex</td>
<td>70</td>
<td>14,029,348</td>
<td>1,371,674</td>
<td>9.8%</td>
<td>560,508</td>
<td>$26.21</td>
<td>107,912</td>
<td>186,338</td>
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<tr>
<td>Hudson</td>
<td>51</td>
<td>18,028,408</td>
<td>1,173,472</td>
<td>6.5%</td>
<td>1,793,638</td>
<td>$25.88</td>
<td>195,052</td>
<td>1,986,658</td>
</tr>
<tr>
<td>Hunterdon</td>
<td>7</td>
<td>406,791</td>
<td>30,914</td>
<td>7.6%</td>
<td>—</td>
<td>$25.00</td>
<td>—</td>
<td>1,488</td>
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<tr>
<td>Mercer</td>
<td>69</td>
<td>6,817,336</td>
<td>622,656</td>
<td>9.1%</td>
<td>763,239</td>
<td>$26.58</td>
<td>99,509</td>
<td>(120,601)</td>
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<tr>
<td>Middlesex</td>
<td>101</td>
<td>14,170,099</td>
<td>1,964,300</td>
<td>13.9%</td>
<td>1,634,684</td>
<td>$24.81</td>
<td>(99,302)</td>
<td>(398,590)</td>
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<tr>
<td>Monmouth</td>
<td>44</td>
<td>5,594,985</td>
<td>264,227</td>
<td>4.7%</td>
<td>537,993</td>
<td>$24.45</td>
<td>(9,854)</td>
<td>(41,270)</td>
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<tr>
<td>Morris</td>
<td>145</td>
<td>18,216,468</td>
<td>2,607,120</td>
<td>14.3%</td>
<td>2,345,489</td>
<td>$26.40</td>
<td>(135,566)</td>
<td>(231,363)</td>
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<tr>
<td>Passaic</td>
<td>22</td>
<td>2,336,754</td>
<td>124,407</td>
<td>5.3%</td>
<td>53,204</td>
<td>$22.58</td>
<td>(4,977)</td>
<td>(38,173)</td>
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<tr>
<td>Somerset</td>
<td>101</td>
<td>13,013,830</td>
<td>2,355,217</td>
<td>18.1%</td>
<td>2,734,103</td>
<td>$28.32</td>
<td>20,626</td>
<td>625,796</td>
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<tr>
<td>Union</td>
<td>26</td>
<td>3,460,870</td>
<td>347,900</td>
<td>10.1%</td>
<td>292,727</td>
<td>$27.08</td>
<td>203,976</td>
<td>96,053</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>767</strong></td>
<td><strong>113,997,376</strong></td>
<td><strong>12,550,975</strong></td>
<td><strong>11.0%</strong></td>
<td><strong>12,091,543</strong></td>
<td><strong>$26.12</strong></td>
<td><strong>564,889</strong></td>
<td><strong>2,074,754</strong></td>
</tr>
</tbody>
</table>

| Central NJ | 341 | 43,057,120 | 5,554,300 | 12.9% | 5,962,746 | $25.75 | 214,955 | 161,388 |
| Northern NJ | 426 | 70,940,256 | 6,996,675 | 9.9%  | 6,128,797 | $26.20 | 349,934 | 1,913,366 |

*Includes all office buildings, 10,000 square feet and greater. Does not include owner-occupied facilities.
for $101 million, or $251 per square foot. Also helping the overall vacancy rate was T-Mobile USA’s (Voicestream) lease of 105,000 square feet at 4 Sylvan Way in Parsippany. Other large leases commencing in the region included 100,000 square feet by Chubb & Son, which leased the entire new building at 3 Mountainview Road in Warren, and CNBC, which moved into the new, 300,000 square foot building constructed for them on Sylvan Avenue in Englewood Cliffs.

In addition, asking rents reportedly increased in six of the eleven counties studied in the region, resulting in an overall average of $24.62 per square foot gross, up a penny from $24.61 per square foot. Monmouth County has experienced the highest increase in average asking rents. The increase of $3.52 per square foot in Monmouth County during the third quarter is a result of a reported asking rent of $24.50 per square foot gross for 482,000 square feet at River Centre in Middletown, weighing heavily on the average for the county. Recently, that building reported rents on a net basis, therefore not being factored into the average. Conversely, in Hudson County, asking rents have reportedly dropped to $25.56 per square foot gross, the lowest level for that area since year-end 2000.

Although not nearly as healthy as it once was, the lease activity mentioned above provides some positive indication that the office market in New Jersey may be ready for a recovery in the not-so-distant future. Construction levels are lower than in the past as developers are careful not to flood the market with new product only to compete with the quality sublease space available to prospective tenants. A year has passed since the 9/11 tragedy, which may help companies move forward and feel confident that there will be an economic rebound. Discounted rents and landlord incentives help ease tenant fears of a continued recession. However, as terrorist activity continues to loom and the threat of war heightens, many will continue playing it safe, at least for the short term.
Route 287 corridor between Edison and Bridgewater. Telcordia will put another 500,000 square feet on the market in the near future. Landlords and commercial brokers seeking to lease these blocks of space face the challenges of traffic congestion during peak travel hours on Route 287 and an abundance of quality office space elsewhere throughout the state. Potential tenants are being offered aggressive incentives, and often without positive results.

It is no secret that the major employers of this region—pharmaceutical, telecommunication, and financial service companies—are in holding patterns for hiring or in some situations are laying off employees. Consolidating functions and departments will lead to more efficient use of existing facilities and buildings and will further reduce the need for additional space.

Yet companies are beginning to explore the Route 287 corridor as an alternative to downsizing and outsourcing because it offers affordable office space with a diversified labor force in the New York metropolitan area. There is sufficient variety in the size of available space blocks to accommodate the needs of most companies. Viable tenants in the marketplace have their choice of facilities and will reap the rewards of reduced rents and concessions. Tenants can benefit from close proximity to essential support systems such as hotels, restaurants, shopping, universities, and cultural activities. In addition, the corridor is one hour from Manhattan via car or mass transit. This offers reasonable access for meetings and conferences as well as a convenient location for "back office" space.

The Route 287 corridor also offers easy access to the New Brunswick/Piscataway campus of Rutgers University. Many "back office" users seek to operate on a flex schedule, which may also include part-timers in the evening and weekends. The labor pool to fill this niche is within close proximity of the university. Other companies may need the skills and research that a university may provide to implement their product or service.

In August 2002, Olivetti Office USA leased 25,000 square feet in Somerset. Twenty-two competing office spaces were considered within a four-mile geographic area before this lease was signed, which is indicative of the vast amount of space available on the market in a relatively concentrated area. It is difficult to predict when the economy and the commercial office market will return to good health. Until then, corporate tenants hold all the cards and can look forward to spectacular discounts as they negotiate lease transactions on or around the Route 287 corridor.

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