I am delighted to be here this evening to address such a distinguished gathering of business and community leaders. We are particularly enriched at the New York Federal Reserve Bank by the participation of your Rochester colleagues on our Buffalo branch board of directors and from our association with others of you in various programs in western New York State.

This evening, I would like to begin my remarks with some comments about the performance of the national economy and then turn to the regional economy and that of Rochester. I also would like my time with you this evening to be a conversation. I encourage your observations and comments, as well as any questions.

Turning first to the national economy, I must say that I am very pleased with the cyclical performance of the U.S. economy. We currently are in our sixth year of expansion. The underlying fundamentals of the economy—such as consumer, business, and financial balance sheets—remain vastly improved from where they were in the late 1980s. The unemployment rate is around 5 1/2 percent, which most economists would agree is close to full employment. In fact, it has been below 6 percent for over two years.

The inflation story also has been good. Over the first half of 1996, core consumer price inflation actually decelerated from around 3 percent to around 2 3/4 percent, a positive picture for the sixth year of this economic expansion.

Growth of wages has begun to increase somewhat recently, but in this era of global competition there remains some question as to whether that will lead to a faster pace of price inflation. Indeed, recent experience suggests that it is difficult to predict the so-called "natural rate" of unemployment associated with intensified inflationary pressures. There is no easily-seen red line that the economy should stay away from. I disagree, though, with those who feel that the current good behavior of prices means we can ignore signs of intensified use of labor and capital resources. The Fed must remain vigilant with regard to incipient signs of inflation; it is clear that the failure to contain price inflation at its earliest stages only makes it more difficult and costlier to bring it under control later.

Despite all the good news of our six year expansion, there is growing frustration with the fact that the economy is not providing a large number of our citizens with a rising standard of living. We are at a point in our history where the economy's long-run potential growth rate is substantially lower than it was in the 1960s, or even the 1970s. In part, this is the result of the fact that our labor force is growing rather slowly due to demographic trends. But more important, the growth of labor productivity continues to be disappointing. Over this business cycle, productivity growth has been in the range of only about 1 percent; we have not observed in the economic data, at least not yet, any productivity miracle from significant investments in computers.

Higher rates of overall economic growth are neither necessary nor sufficient to increase the well-being of the mass of the population—rather, that depends on how the economic pie is sliced. While President Kennedy may have overstated the benefits of faster growth in his well-known statement that "a rising tide lifts all boats" there is no question that more rapid productivity growth will ease the task of dealing with crucial problems that face our nation, such as providing for the retirement incomes of the baby boomer generation and raising the living standards of the poorest part of our population.

I don't think that we should just wait for some high technology miracle to generate higher growth. It may come some day, but we cannot count on it. We must do more to raise the overall level of savings in our economy so that we can finance more investment in physical and human capital as well as public infrastructure, all of the things that history has proven will raise overall living standards.

In this region, economic growth has come more grudgingly than it has to the nation as a whole. The 1990-1991 U.S. recession hit New York State harder and lasted longer than was the case in most of the rest of the country. Large scale restructuring in the financial services sector, continued downsizing in manufacturing and defense-related industries, and the bursting of the bubble in real estate values all contributed to the region's plodding advance.

But despite the stresses in many parts of the region, the economy of New York is experiencing a gradual comeback. New York's large and diverse trade and services sectors have flourished, fostered by renewed prosperity in the financial services sector. In addition, new jobs in the large health-related and social services fields continue to come on stream and the job counts at many of the region's smaller industries, such as private education and consulting, have also advanced. The construction industry has begun to show more signs of life; new home sales are up and home prices have risen. The region has also been helped by slightly slower cost of living increases than the national average.

Job growth in New York State is likely to continue its gradual recovery. Despite the likelihood of some moderation in national economic growth in 1997, economists at the New York Fed believe that the State's job growth rate will accelerate modestly to 1.0 percent from 0.8 percent in 1996. Stated differently, roughly 80,000 new jobs will be added next year in New York. The acceleration in job growth is largely the result of continued strength in the region's key private sector industries and a slackening of the recent rapid pace of decline in the government sector which, for the past several years, has been a significant drag on overall growth.

Business and consumer services are expected to be the key driving forces for private sector job growth in the State. Health and social services will also contribute to overall job growth, though consolidation and cost-cutting trends in hospitals will moderate the rapid pace of gains seen in previous years, particularly here in New York. And, healthy gains in income and retail sales should hold up retail trade employment.

Manufacturing job declines will likely continue to act as a brake on private sector job growth, although the large job losses of recent years are moderating. Moreover, consolidation trends in the banking sector will continue to slow growth in the region. And the recently enacted welfare reform legislation could increase projected state budget deficits as local governments strive to provide workforce and other assistance to those welfare recipients and legal immigrants who lose federal benefits.

It is true that there are many challenges ahead for New York State and its cities and counties: the shifting of budget responsibilities from the federal government to states and the rapid pace of technological change in manufacturing are just two. Yet, many times, strength comes from difficulty and the resiliency of our citizens cannot be underestimated.

The economy of Rochester is a prime example of that resiliency. All too often, people focus on problems rather than successes. Let me just tick off a few examples of the strengths in the Rochester economy.

First, although it has lost 12,000 manufacturing jobs since 1990, Rochester has the lowest unemployment rate of all the metropolitan statistical...
areas in the state, at 4.3 percent. The resilience of the Rochester economy is even more extraordinary in light of its concentration in manufacturing. Together, Buffalo and Rochester account for about 14 percent of state employment—but collectively they account for 23 percent of manufacturing jobs in the state. And, manufacturing in Rochester constitutes about 24 percent of employment, compared with 12 percent for the state and 15 percent nationwide.

Second, Rochester remains a national leader in some key industrial sectors. Powered by firms such as Kodak, Bausch & Lomb and Xerox, and many smaller, dynamic firms, Rochester is a world leader in optics technology. It is also one of the largest tool and die centers in the United States. Both of these industries have a strong export component that has bolstered growth. Although data are rather soft in this area, Rochester has one of the highest dollar export volumes per capita in the United States.

Third, the Rochester community is creating new jobs. The fastest growing area of the Rochester economy, as in the rest of the nation, is in services. Business services have accounted for somewhat more than half of the 3,100 net new jobs created in the twelve months ended in July. And, these have not been temporary jobs that are mentioned frequently in the national media. Many of the new positions in business services are in the promising fields of computer services, programming and data-processing.

I believe this evidence of rather remarkable vitality in segments of the Rochester economy bodes well for its future and that of the region, even if we continue to see rapid change in manufacturing industries.

Finally, Rochester is indeed fortunate to have several local universities that have come together with the private and public sector in collaborative arrangements. At a conference the New York Fed cosponsored with the New York Academy of Sciences last year on technology and economic development in the region, speaker after speaker underscored the special roles that universities and other centers of higher learning play in our society: creating knowledge through research, training the next generation of scientists and workers; and engaging in partnerships to link research innovation to product development.

I believe the schools in upstate New York have been doing especially well in these areas. But more remains to be done to cement the symbiotic relationship between institutions of learning and exploration, and the businesses that adapt their research, employ their graduates, and provide the basis for long-term economic well-being.

I believe that the business community and civic leaders in particular can most directly promote economic well-being by taking active, participatory roles in the education and training of our region's youths and workers. The same forces that continue to reshape the region's economy—industrial restructuring, global competition and rapid, persistent technological change—are the ones that have put enormous strains on much of our work force and educational establishments. Without greater direct linkages—in both capital and human resources—from businesses in their communities, students and the schools they attend will lack some of the tools needed to achieve their potential.

Every one of our organizations can and must do more to bolster the readiness for work of all who are entering, and others who have been, in the region's labor force. At the New York Fed, we have committed substantial effort to the development and implementation of a wide range of participatory programs geared mainly toward easing student's transition from school to career and toward developing a better understanding of business, economics and finance.

Some of our efforts, which are throughout the New York Fed's district, have been in the Rochester area where we have been involved in a number of programs. For example, we worked both this year and last with the Rochester Council on Economic Education and the Rochester Institute of Technology on distance learning programs aimed at both teachers and students at area high schools. In addition to discussing the Fed's role in formulating and implementing monetary policy, our staff presented a workshop demonstrating new techniques for teaching about money and banking, and a lecture was televised to high schools classes via the educational network. Some of our economists have spoken at the University of Rochester and we have a commitment to come back next year.

Our two-year old program, "The Fed Challenge," is a competition among high school students that has earned national recognition. Teams of students from participating schools present an analysis of current economic conditions, a forecast, and a monetary policy prescription before a panel of judges consisting of senior-level New York Fed staff. This year, several high schools from Buffalo participated along with about 40 schools from downstate New York and almost 100 schools nationwide. Next year, Carl Turnipseed will be expanding the program at the Buffalo branch to include, with your help, some schools from Rochester and other parts of western New York.

For most of the public, the reputation of the Federal Reserve will continue to be measured mainly by our success in promoting economic growth with price stability, rather than by our interactions with educators and students. But we must also respond to the social needs of our community. In that context, the bank will continue to work both independently and with community leaders to help make the Second Federal Reserve District a better place to live and work. I encourage you to join with me and many others in committing our organizations and ourselves more fully to the task of meeting these challenges head on.

Thank you very much.