

# The Economic Outlook: 2009



**Succeeding Despite  
Challenging  
Circumstances**

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# Today's Topics

The Outlook for the US Economy

The Outlook for Job Growth

The Outlook for Inflation Interest Rates

The Outlook for Commercial Property

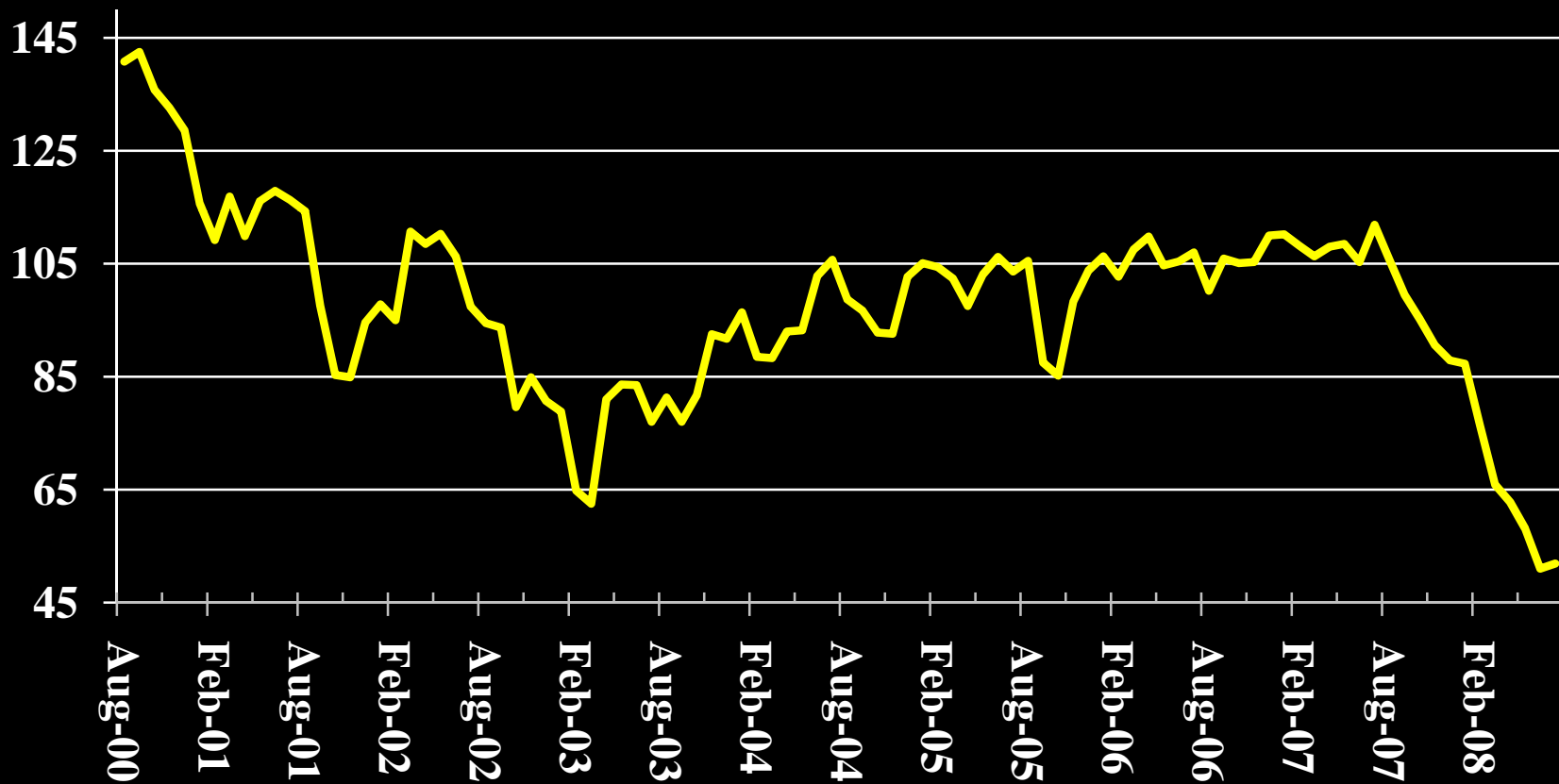
Issues on the Radar Screen

# Composition of the US Economy

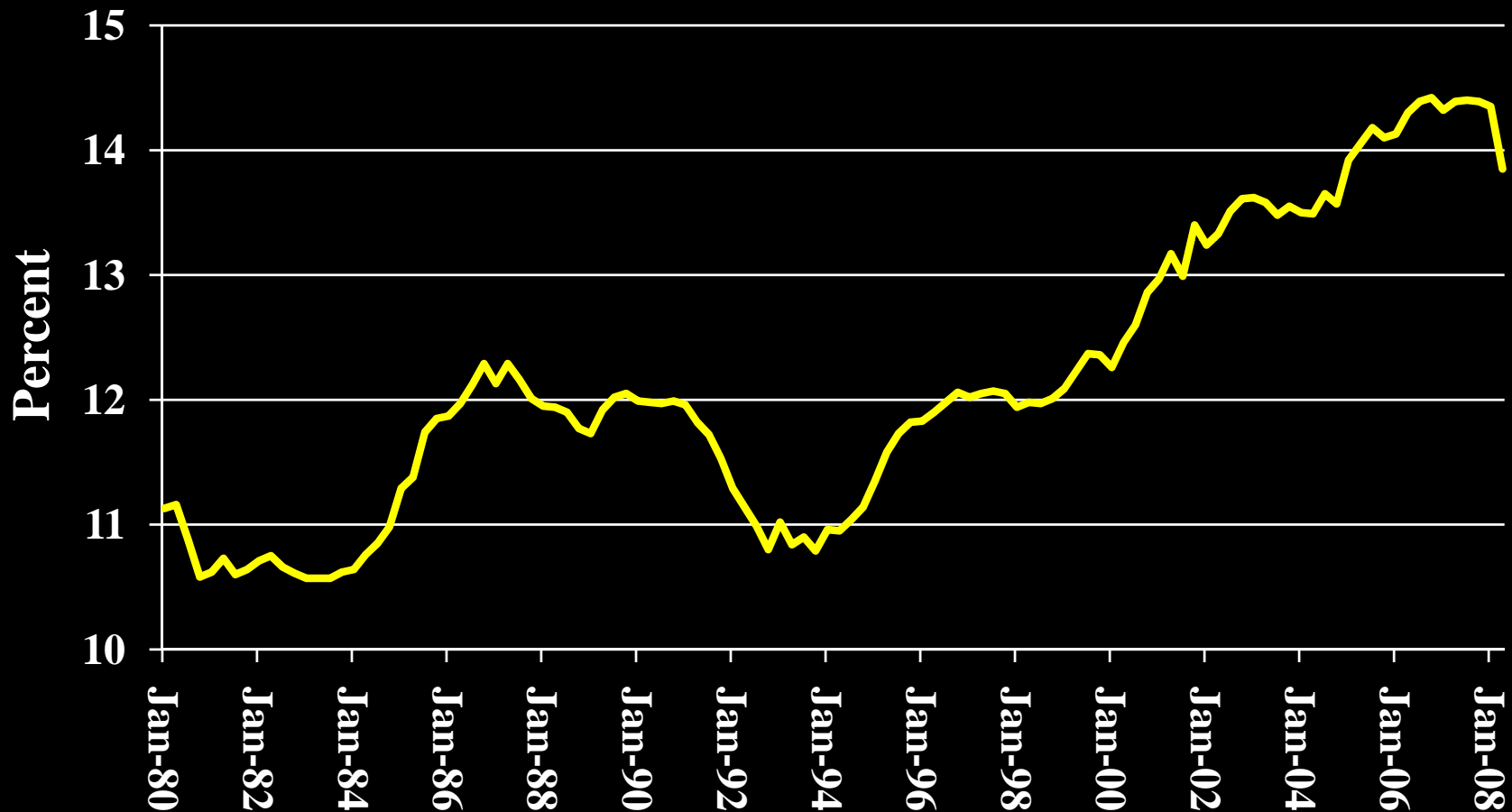
71.2%	Consumer Spending
13.9%	Business Investment
20.1%	Government Spending
- 5.2%	Net Exports



# Consumer Confidence Index

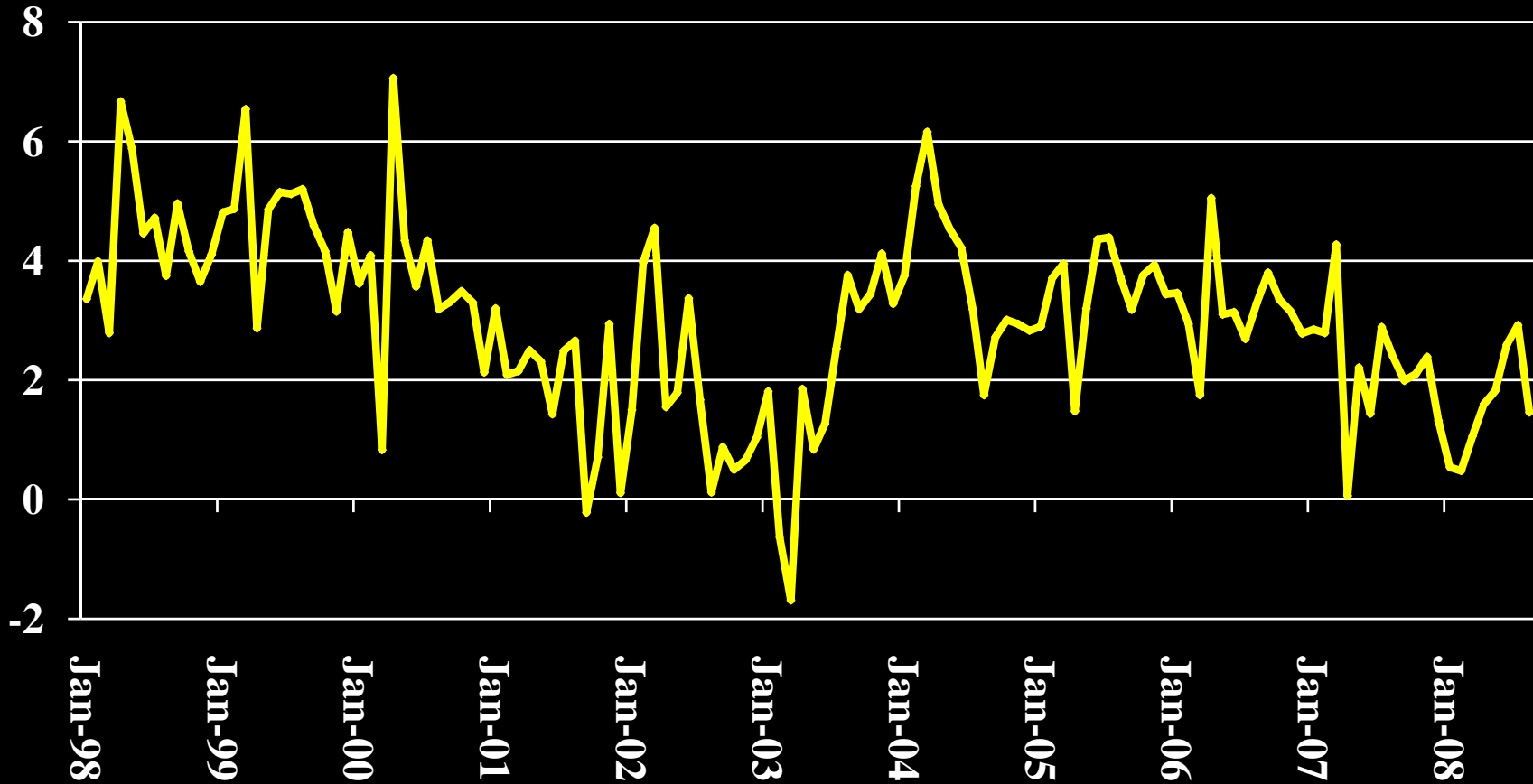


# Debt Service Payments as a Percent of Disposable Personal Income



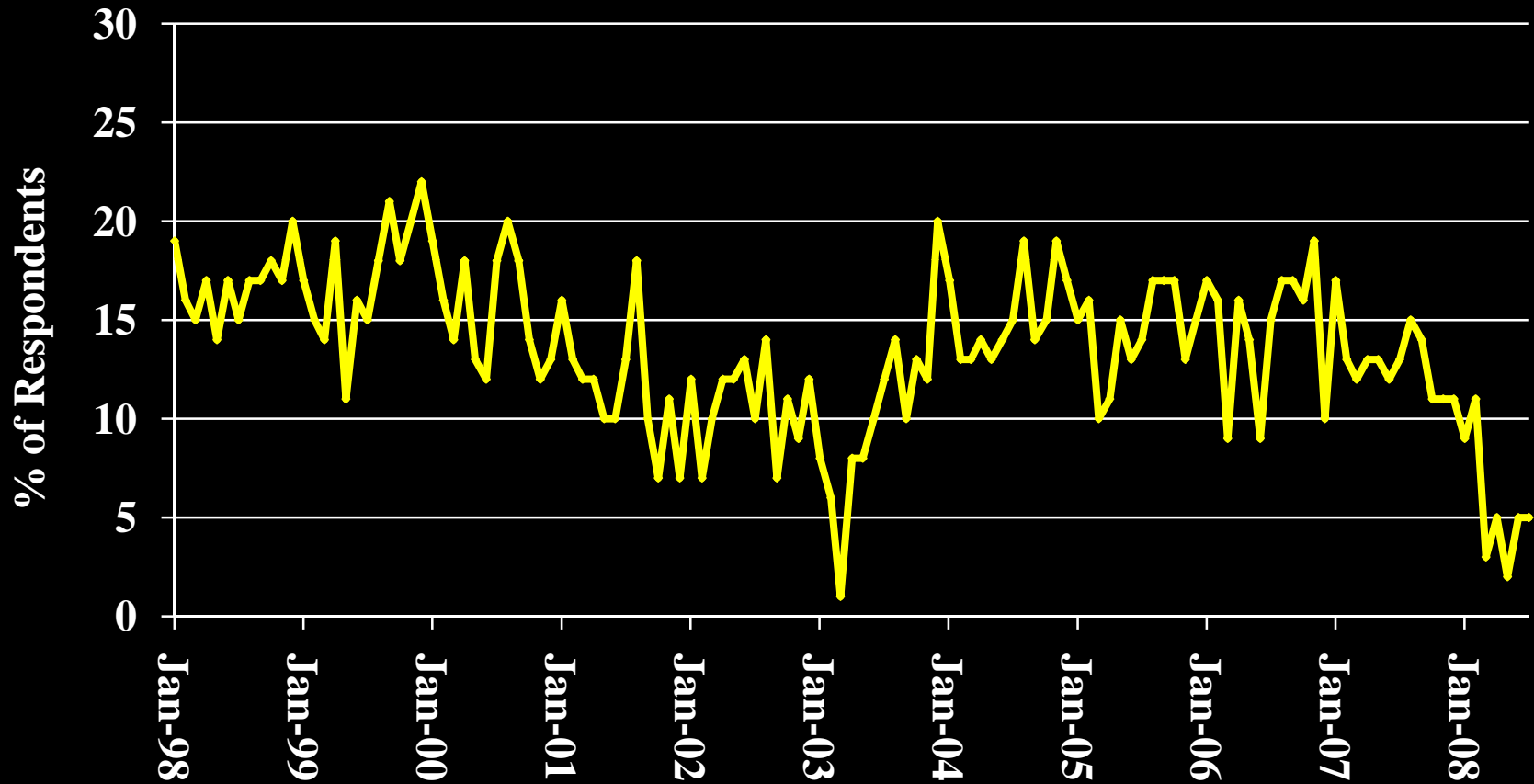
# General Merchandise Retail Sales

Same Store Sales % Change from Year Earlier



# Small Business Outlook

“Planning To Hire People In The Next Six Months”



# Corporate Hiring Plans: Next 6 Months

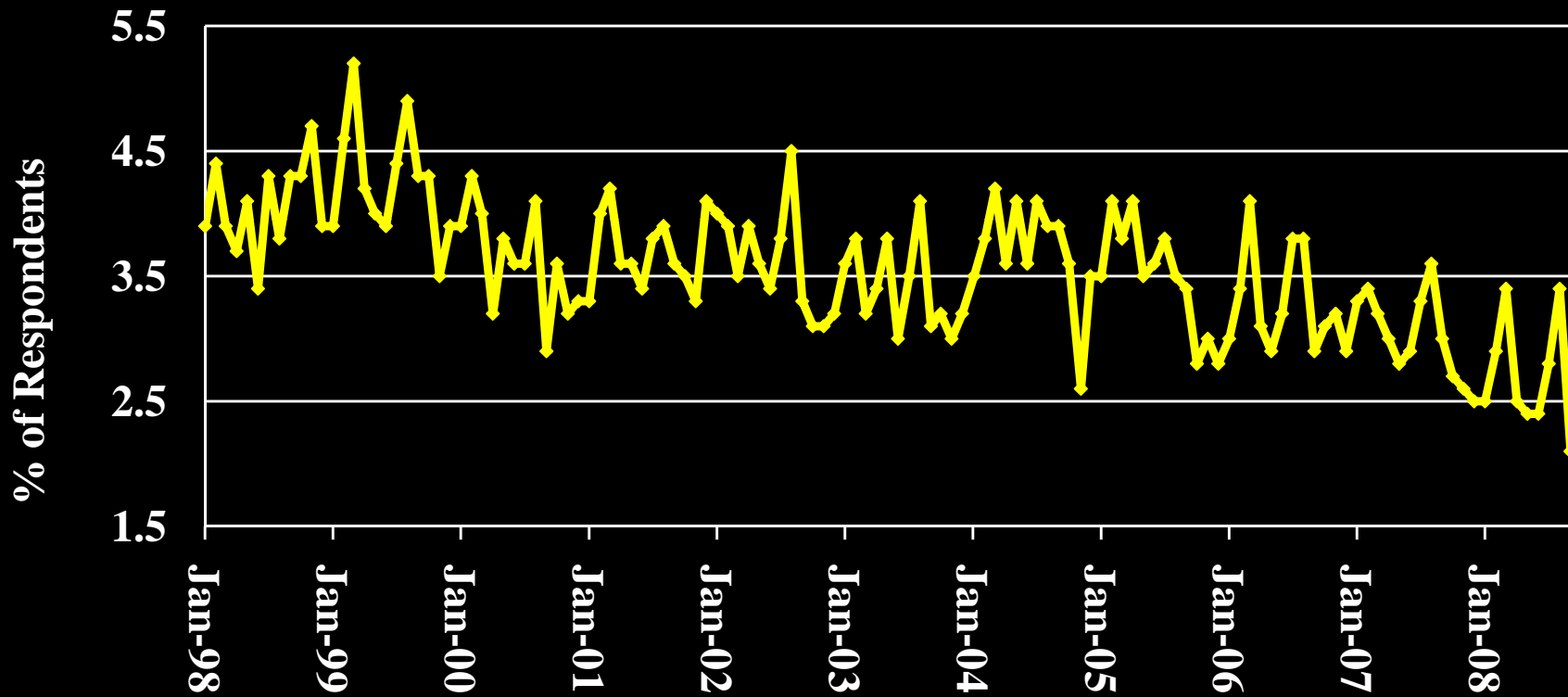
	Q3-08	Q2-08	Q1-08	Q4-07
More Jobs	29%	28%	30%	33%
Less Jobs	32%	31%	22%	22%

# Corporate Profits

(With Inventory Valuation Adjustment & Capital Consumption Adjustment)

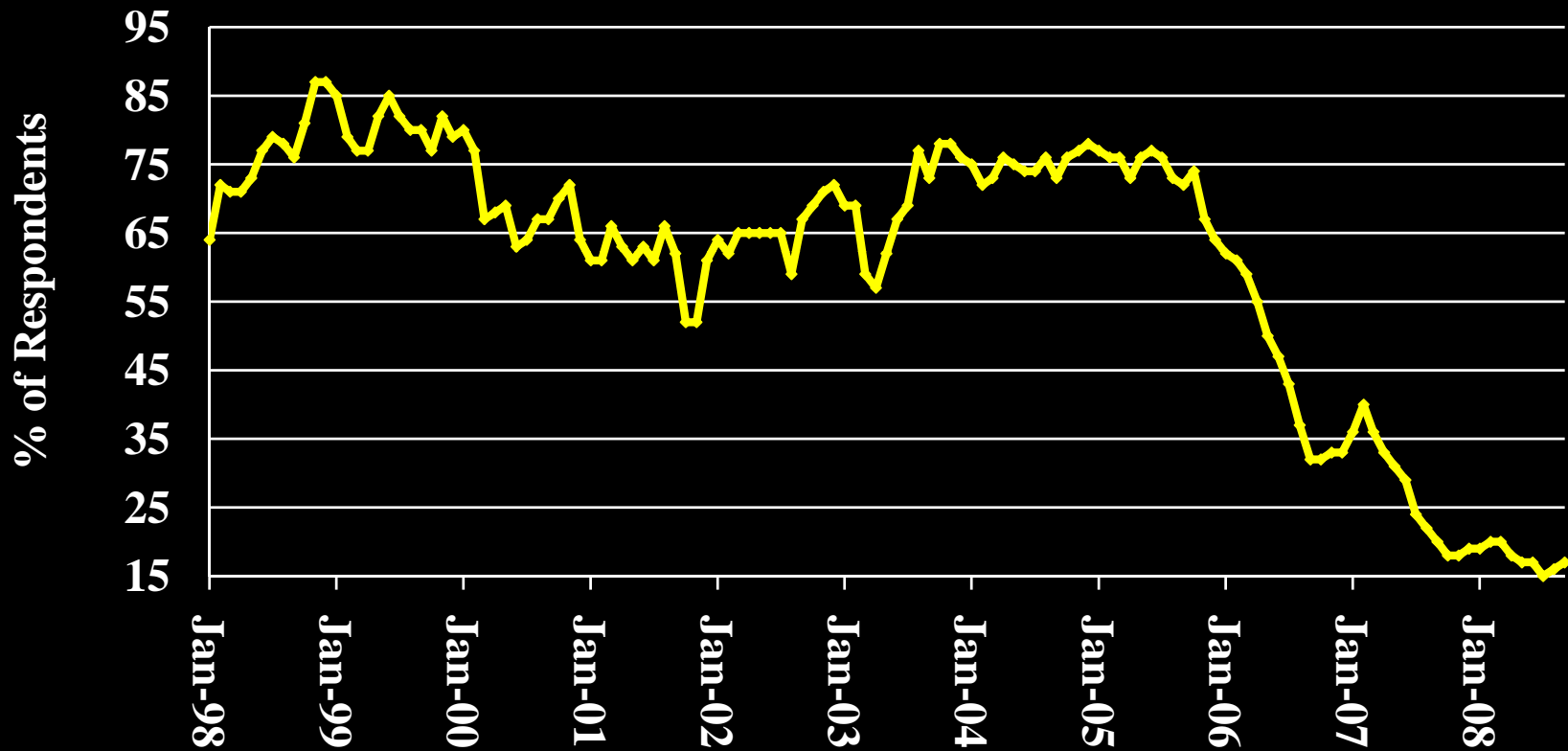


# People Who Plan to Buy a Home in the Next Six Months

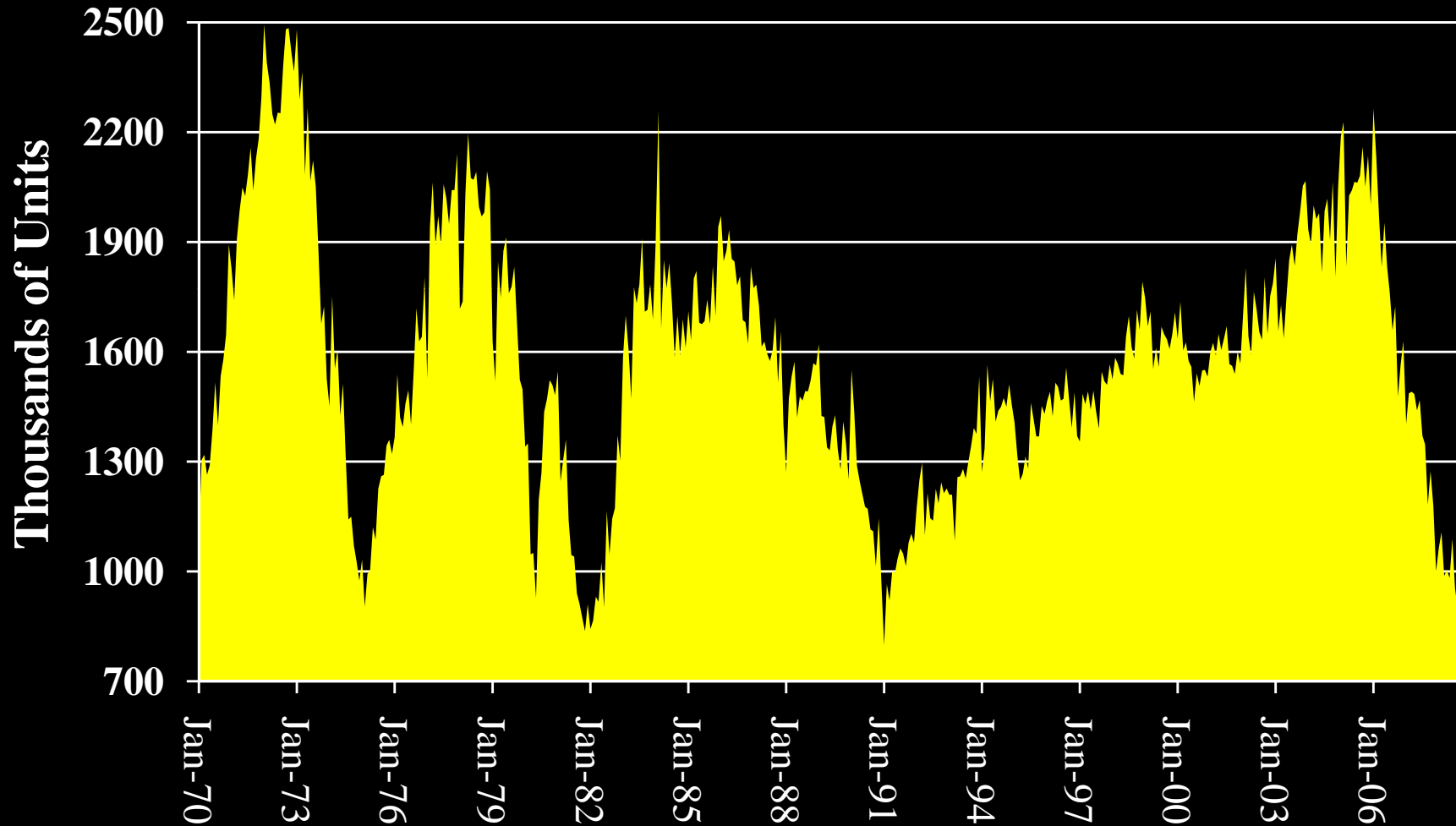


# Builders Sentiment

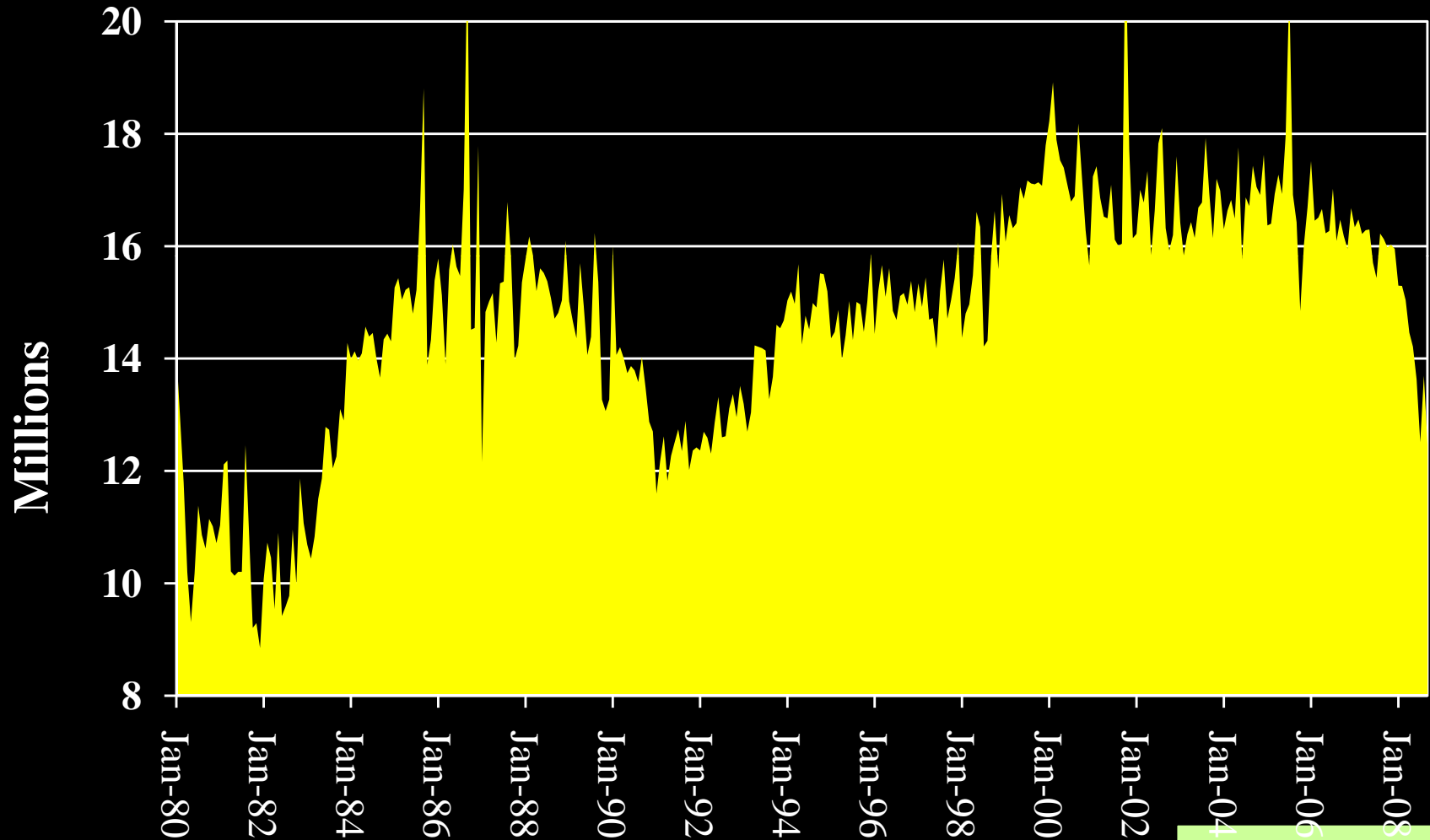
“Current Sales Are Good”



# Housing Starts in the US



# Car and Light Truck Sales



Updated 10/6/08

StLFed Bus/Fiscal



Source: Bureau of Economic Analysis

# Recessions and Employment

## In 2001 recession,

employment fell by 2.0% over 30 months.

## In 1991 recession,

employment fell by 1.5% over 11 months.

## In 1981 recession,

employment fell by 3.1% over 17 months.

## In 1974 recession,

employment fell by 2.7% over 11 months.

# Recessions and Employment

In the past four recessions (on average)  
the employment level decreased for 17 months from peak to trough.

The employment level in the US hit a peak of 138,078,000 in  
December, 2007.

So the decline in employment should come  
to an end between January and May, 2009.

# Recessions and Unemployment

In 2001 recession, unemployment rose from 3.8% in April 2000 to 6.3% in June, 2003. 38 months

In 1991 recession, unemployment rose from 5.0% in March, 1989 to 7.8% in Jun 1992. 39 months

In 1981 recession, unemployment rose from 5.7% in June, 1979 to 10.8% in November, 1982. 41 months

In 1974 recession, unemployment rose from 4.8% in July, 1973 to 9.0% in May, 1975. 22 months

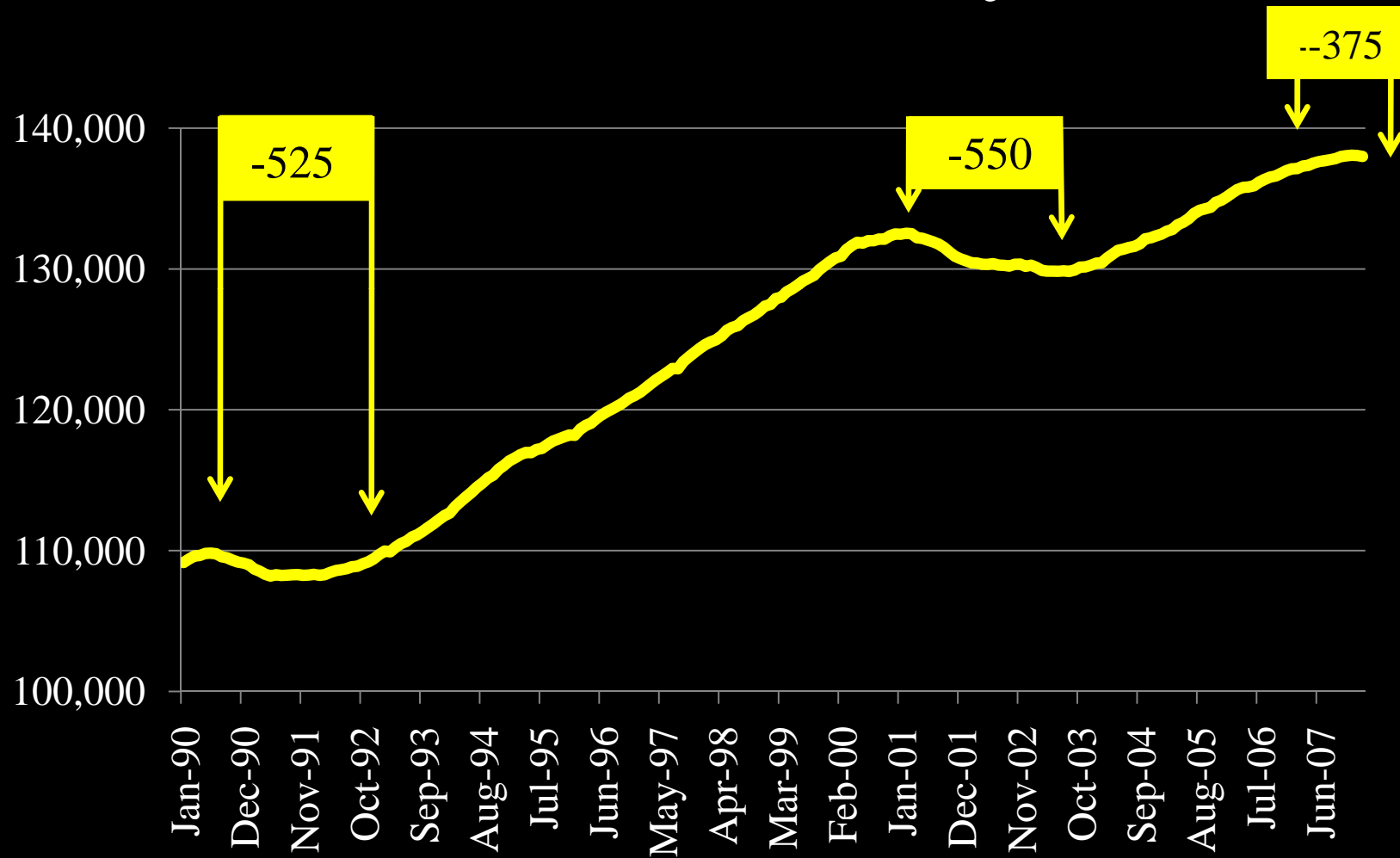
# Recessions and Unemployment

In the past four recessions (on average)  
the unemployment rate increased for 35 months from trough to peak.

The unemployment rate in the US hit a trough at 4.4% in  
December, 2006.

So the unemployment rate should peak  
around November, 2009

# Fed Rate Moves and Total Non-Farm Payrolls



# Issues on the Radar Screen

- The Mortgage Market
- The Banking System
- Political Uncertainty
- Capital Gains Tax Rate



# The Frozen Credit Markets Are Beginning to Thaw



Still Have Significant Challenges

# Merrill Lynch Offloads CDOs

NEW YORK, July 29 (Reuters) –

The Merrill deal included the sale of \$30.6 billion of repackaged debt known as collateralized debt obligations, or CDOs, to buyout firm Lone Star Funds, for just \$6.7 billion, or about 22 cents on the dollar.

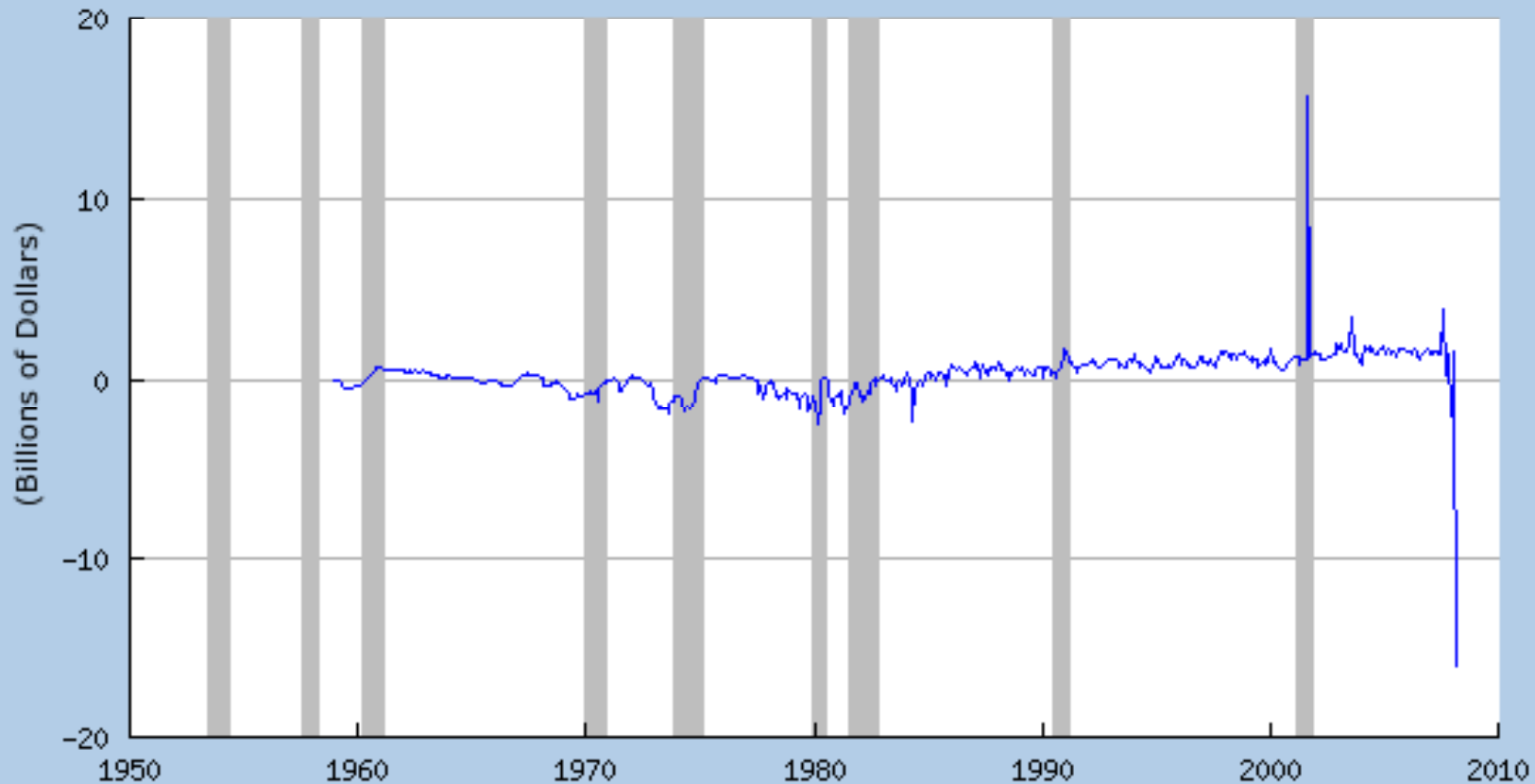
Funds specializing in distressed assets swelled to \$129 billion, their highest ever, from \$118 billion at the end of 2007, according to industry tracker Hedge Fund Research.

CIT Group Inc said on Tuesday that it had agreed to sell a \$9.3 billion subprime mortgage portfolio to them for \$1.5 billion in cash, with Lone Star assuming \$4.4 billion of outstanding debt and other liabilities.

# Banks Short on Capital

## Net Free or Borrowed Reserves

Net Free or Borrowed Reserves of Depository Institutions (NFORBRES)  
Source: Board of Governors of the Federal Reserve System



Shaded areas indicate US recessions as determined by the NBER.  
2008 Federal Reserve Bank of St. Louis: [research.stlouisfed.org](http://research.stlouisfed.org)

# Regional Bank Stress

## ADC Loans

27% of survey responded that lenders are tightening the terms or conditions on outstanding loans prior to maturity

Among those 27%,

51% reported lenders demanding additional collateral

45% reported lenders requiring partial paydown based on reappraisal

37% report lenders are refusing to allow additional draws

20% report lenders are calling the loans

# Regional Bank Stress

## ADC Loans

19% said they are having problems repaying land acquisition loans

24% said they are having problems repaying land development loans

23% said they are having problems repaying single-family construction loans

# Regional Bank Stress

## ADC Loans

76% reported that loan availability was “worse” in 2Q08

Of these 76% who reported “worse”,

78% reported lenders lowering loan-to-cost ratios

77% reported lenders are reducing amount willing to lend

63% reported lenders are not making new loans

\*\*\*So that means that 42% of the builders surveyed across the nation report that lenders are not making new loans.

# Oil Price Shock of 1973

Oil tripled from \$4 to \$13 in one year



“Arab Oil Embargo”



# Oil Price Shock of 1973

Oil tripled from \$4 to \$13 in one year

By July, 1974,  
the Fed Funds rate was 12.9%,  
up from 5.9% in January, 1973.

By October, 1974  
the DOW bottomed at 601,  
down 40% from January, 1973.

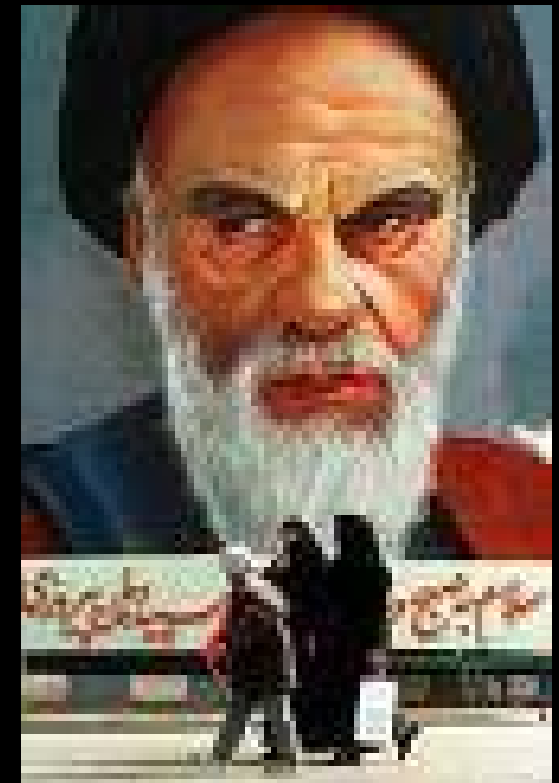
By January, 1975,  
unemployment rose to 8.1%,  
up from 4.9% in January, 1973.

# Oil Price Shock of 1978-81

Oil went from \$15 to \$37



The Overthrow of the  
Shah of Iran



# Oil Price Shock of 1978-81

Oil went from \$15 to \$37

By January, 1981,  
the Fed Funds rate was 19%,  
up from 10% in January, 1979.

By October, 1982,  
unemployment rose to 10.4%,  
up from 5.9% in January, 1979.

By January, 1982, the DOW was 882,  
up from 811 in January, 1979.

# Investors “Waiting to See”

Increase in capital gains and dividend taxes from 15% to 24% decreases the value of stocks and real estate by 11% overnight.



# Shoes to Fall on the Banking System

- Sub-prime loans
- Alt-A loans
- Payment option ARMs
- Home equity loans
- Commercial real estate loans (circa 2006-07)

# Shoes to Fall on the Banking System

- Credit card loans
- Auto loans
- Credit default swaps

# Investors will return, when:

- You can believe bond ratings agencies again
- You can believe corporate accounting again
- You think the recession is nearing an end
- You think that house prices are stabilizing
- You regain confidence in value of a contract

# Investors will return, when:

- You get clarity of the new tax regimes
- You have time to sort out all of the massive government intervention and determine the unintended consequences of their actions
- The return on cash gets so low that dividends look attractive again.

# Outlook for Commercial Real Estate

2009

- Virtually no construction and development for commercial real estate for the next 2 years
- Construction materials prices will continue to fall
- Job cuts in all sectors of the economy until corporate profits start to increase
- Heavy pressure on marginal retailers
- Office demand will fall due to massive consolidation in the financial services industry

# Outlook for Commercial Real Estate

2009

- Tepid retail demand as consumers repair their balance sheet
- Commercial real estate prices likely to fall from 2006-2007 levels as cost of capital increases
- Prices will have support from private equity firms that have amassed billions for distressed real estate
- Transaction volume will rebound in second half of 2008 as political uncertainty resolves

# Outlook for Commercial Real Estate

## Longer Term

- Intense Wall Street focus on global investment will rebound back to the US as the concept of “de-coupling” is debunked.
- Low interest rates create speculative asset bubbles; and the next will be the US stock market.
- The next wave up in commercial real estate prices will occur after the next boom in US stocks.