

The Economic Outlook: 2009



**Succeeding Despite
Challenging
Circumstances**

Dr. Mark G. Dotzour
Chief Economist
Real Estate Center
Texas A&M University
dotzour@tamu.edu

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

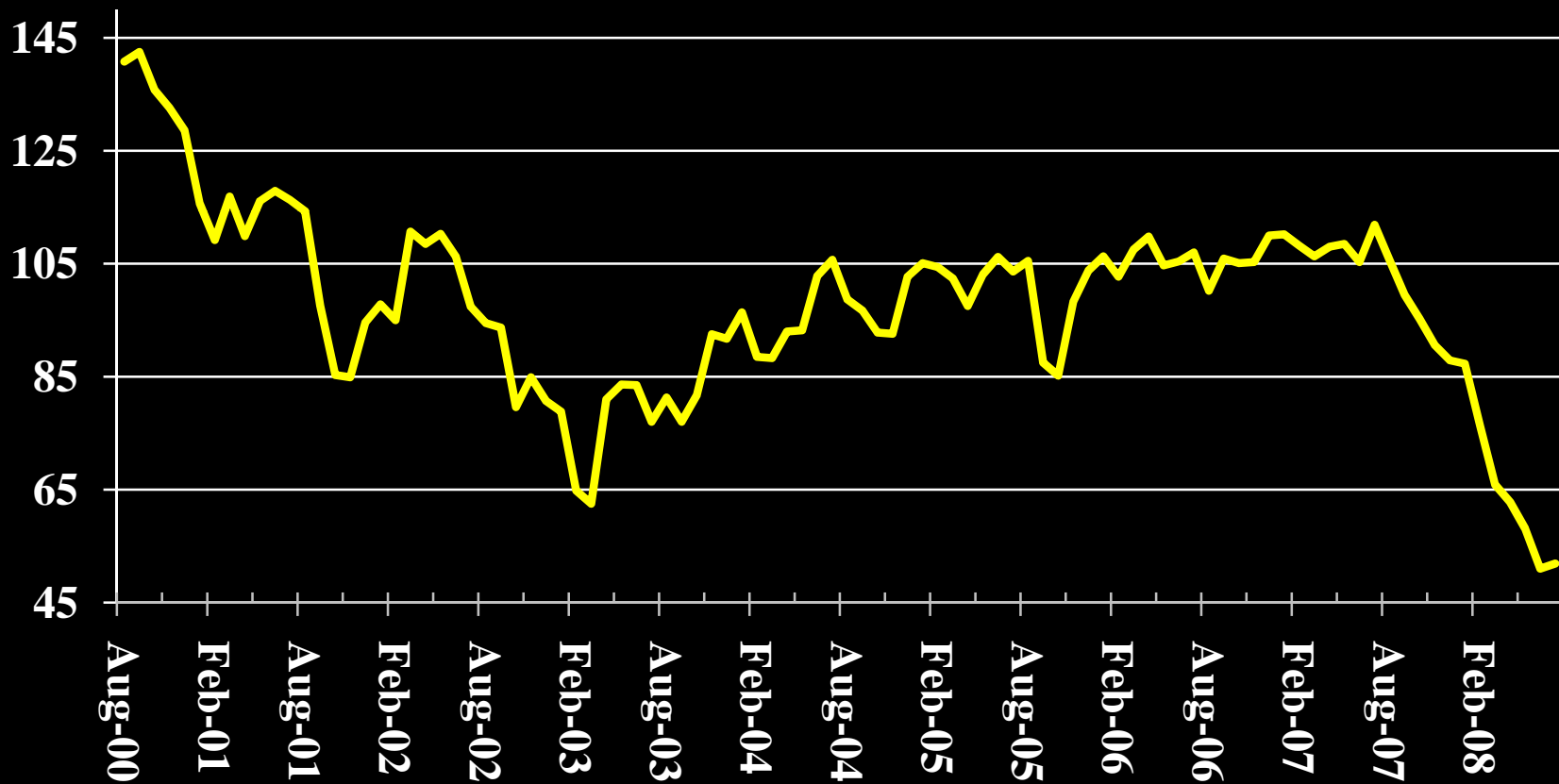
Issues on the Radar Screen

Composition of the US Economy

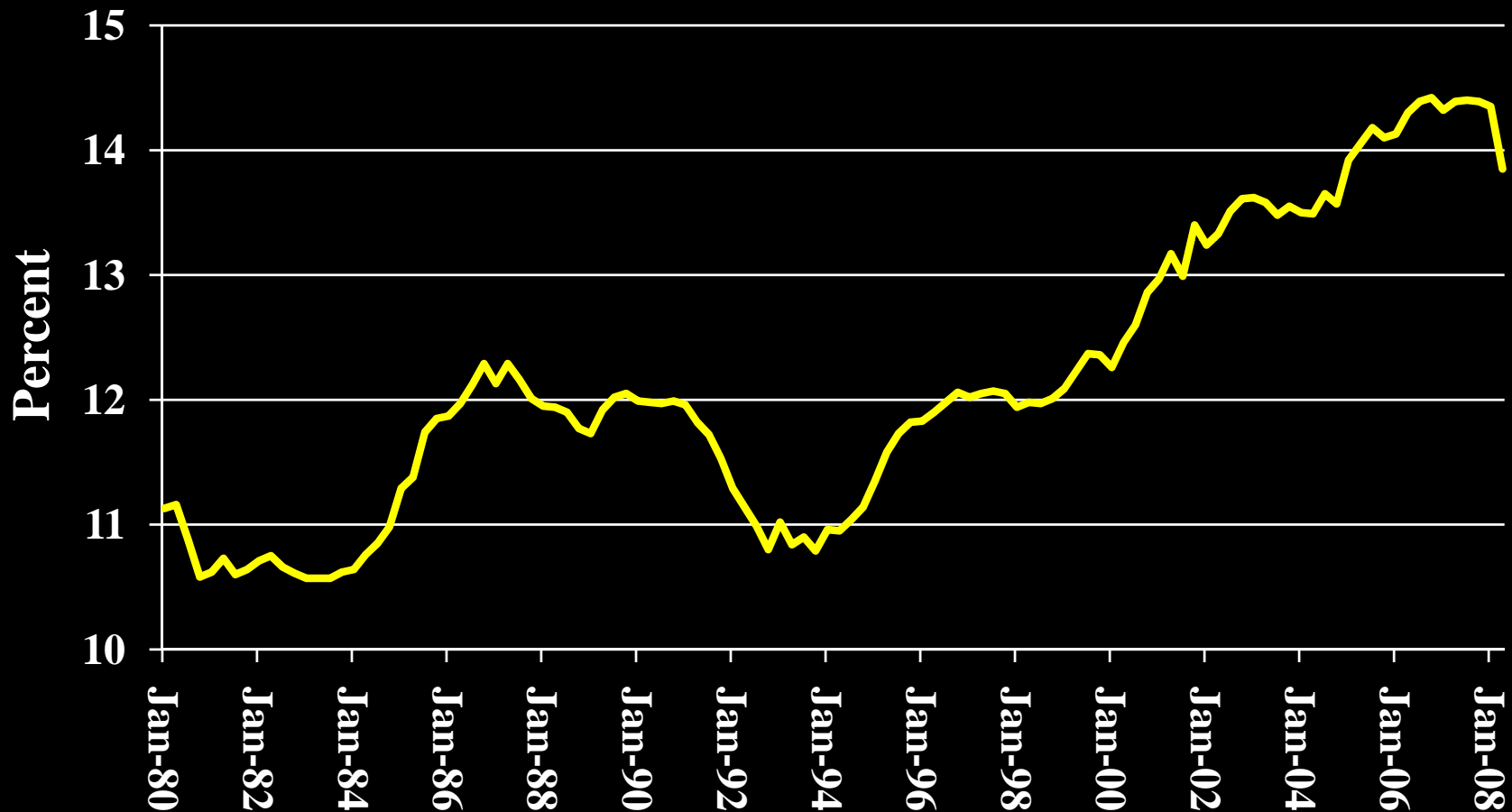
71.2%	Consumer Spending
13.9%	Business Investment
20.1%	Government Spending
- 5.2%	Net Exports



Consumer Confidence Index

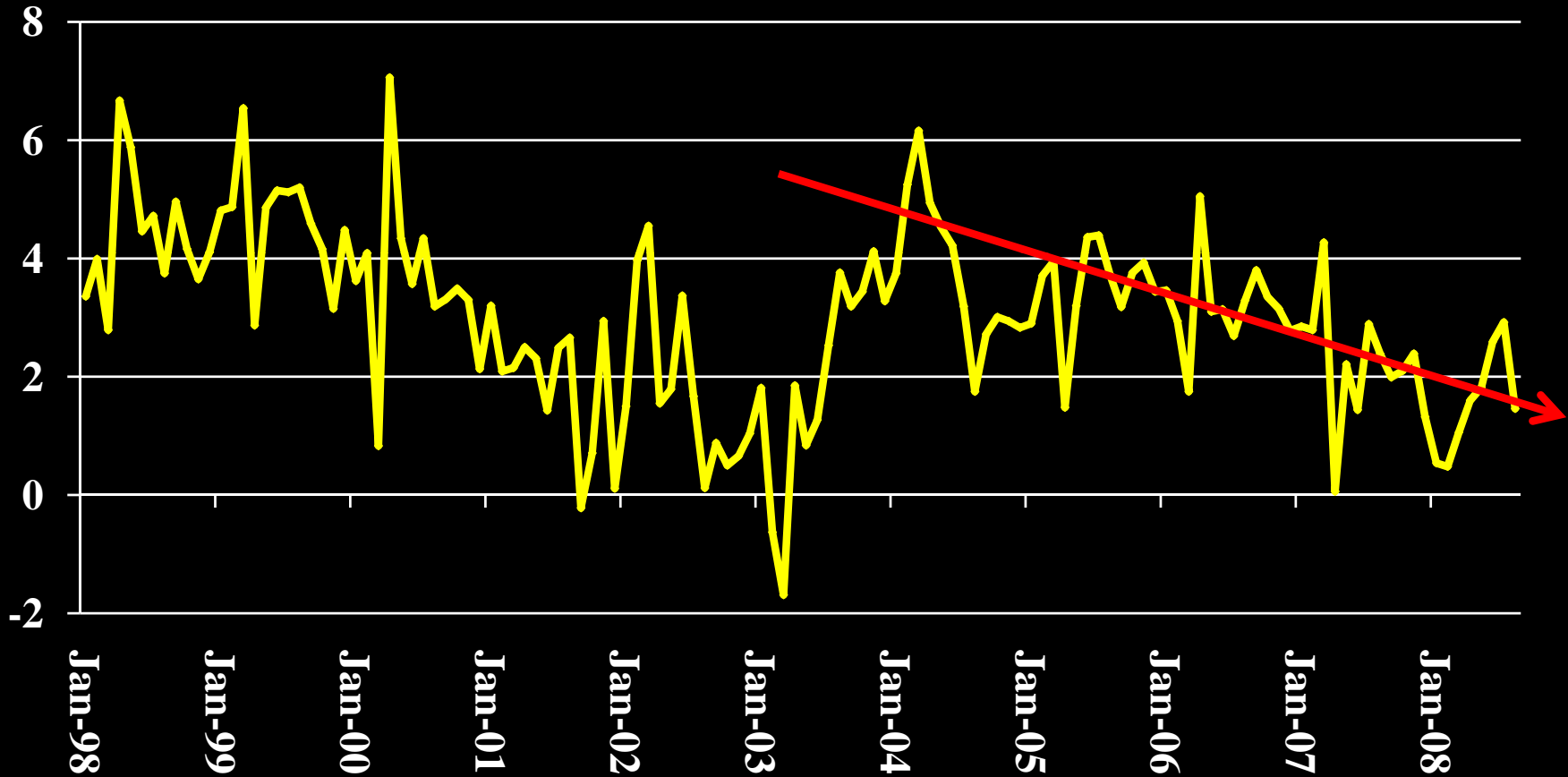


Debt Service Payments as a Percent of Disposable Personal Income



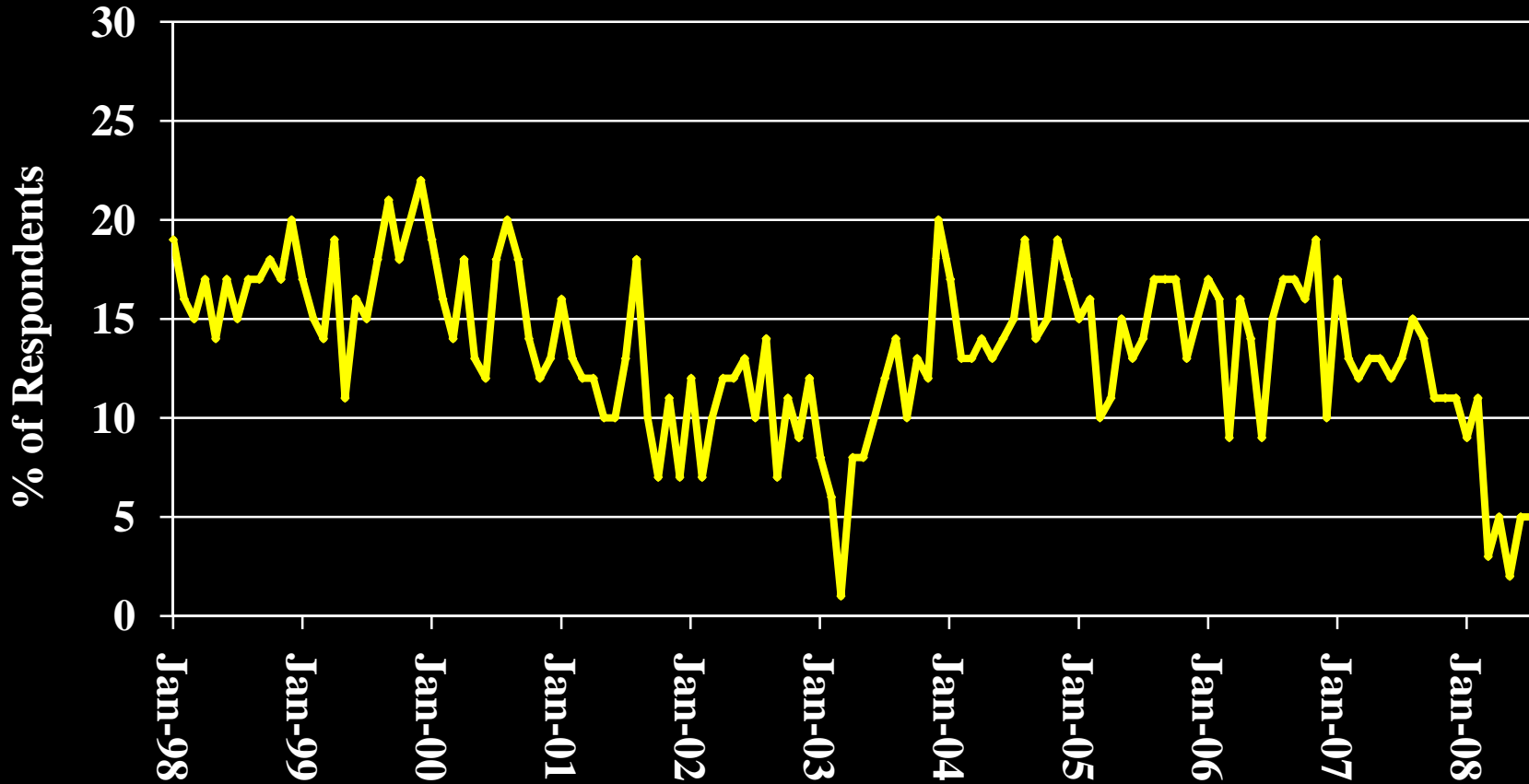
General Merchandise Retail Sales

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

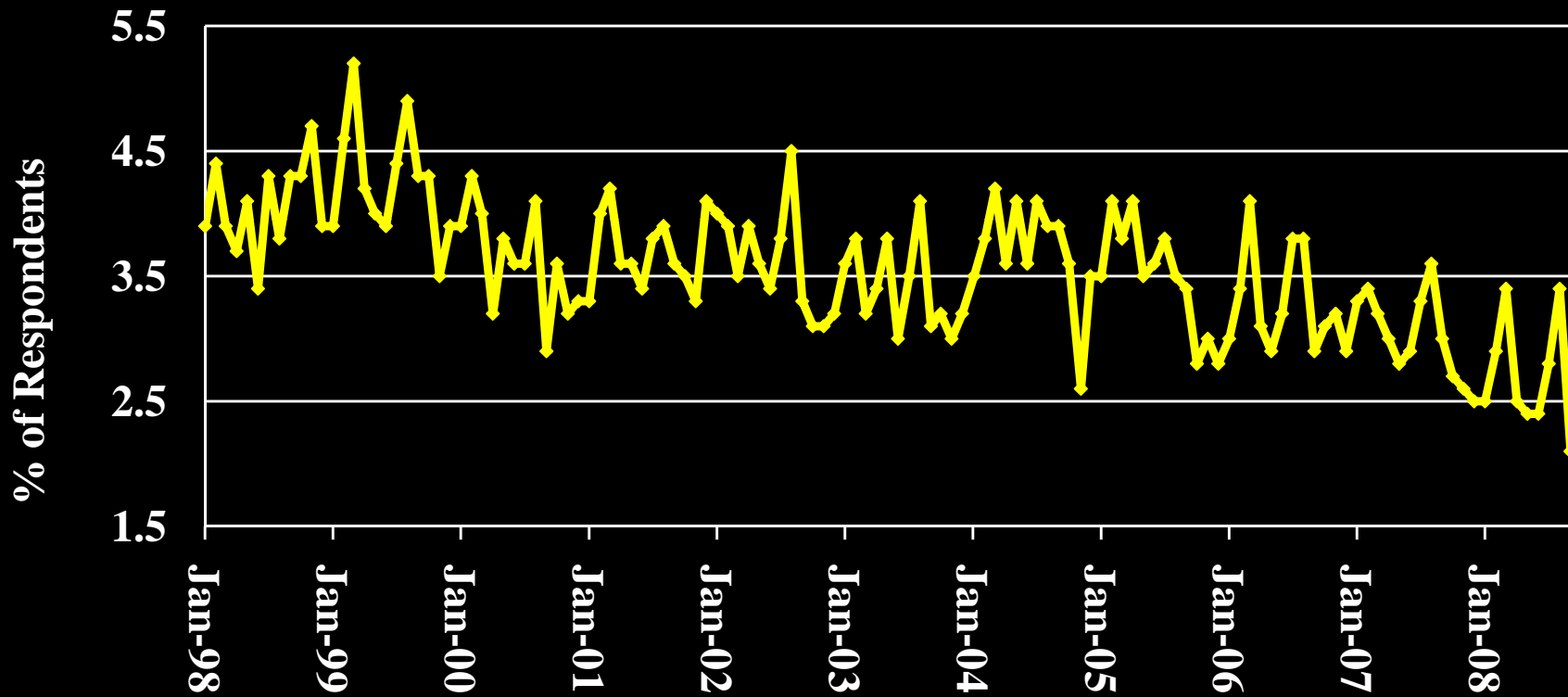
	Q3-08	Q2-08	Q1-08	Q4-07
More Jobs	29%	28%	30%	33%
Less Jobs	32%	31%	22%	22%

Corporate Profits

(With Inventory Valuation Adjustment & Capital Consumption Adjustment)

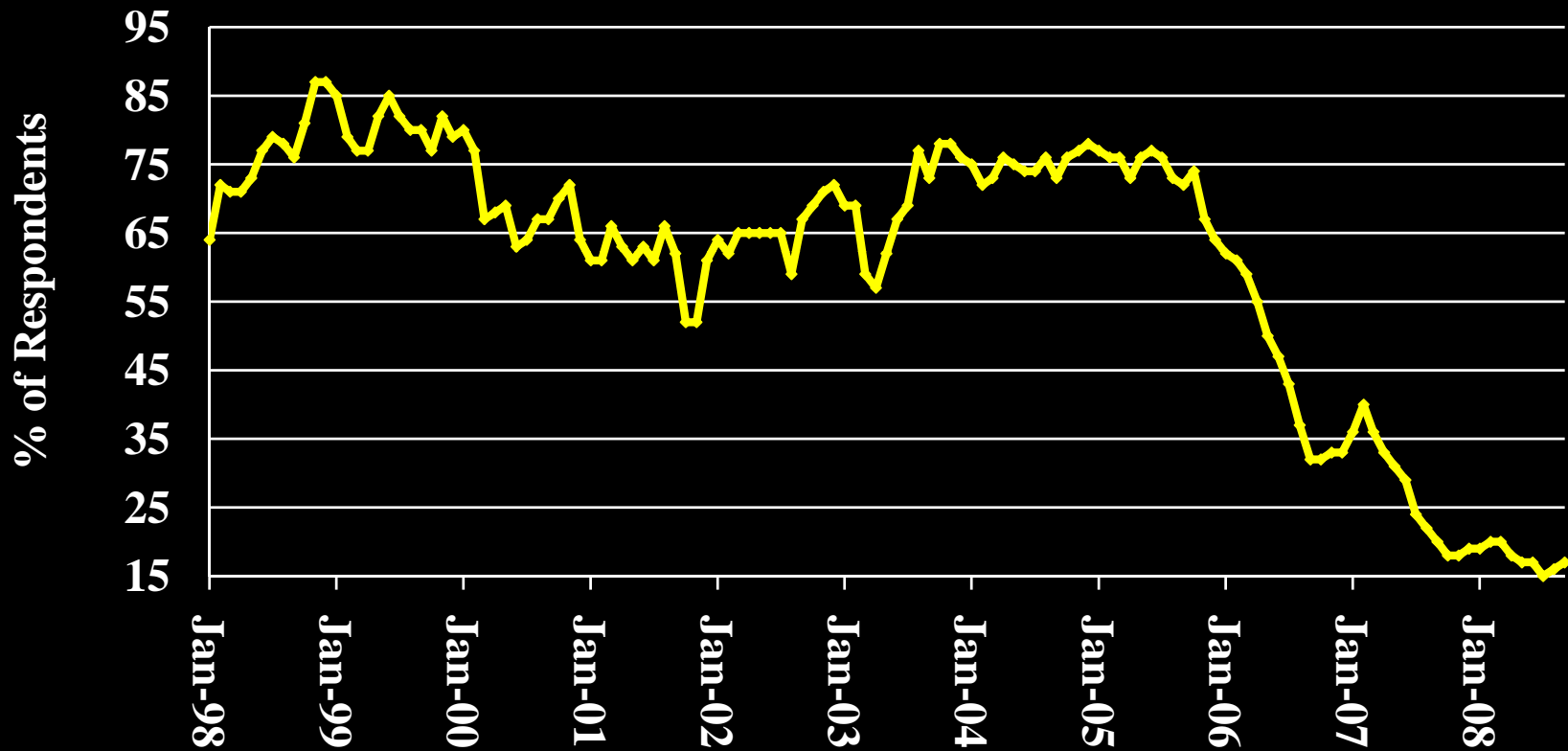


People Who Plan to Buy a Home in the Next Six Months

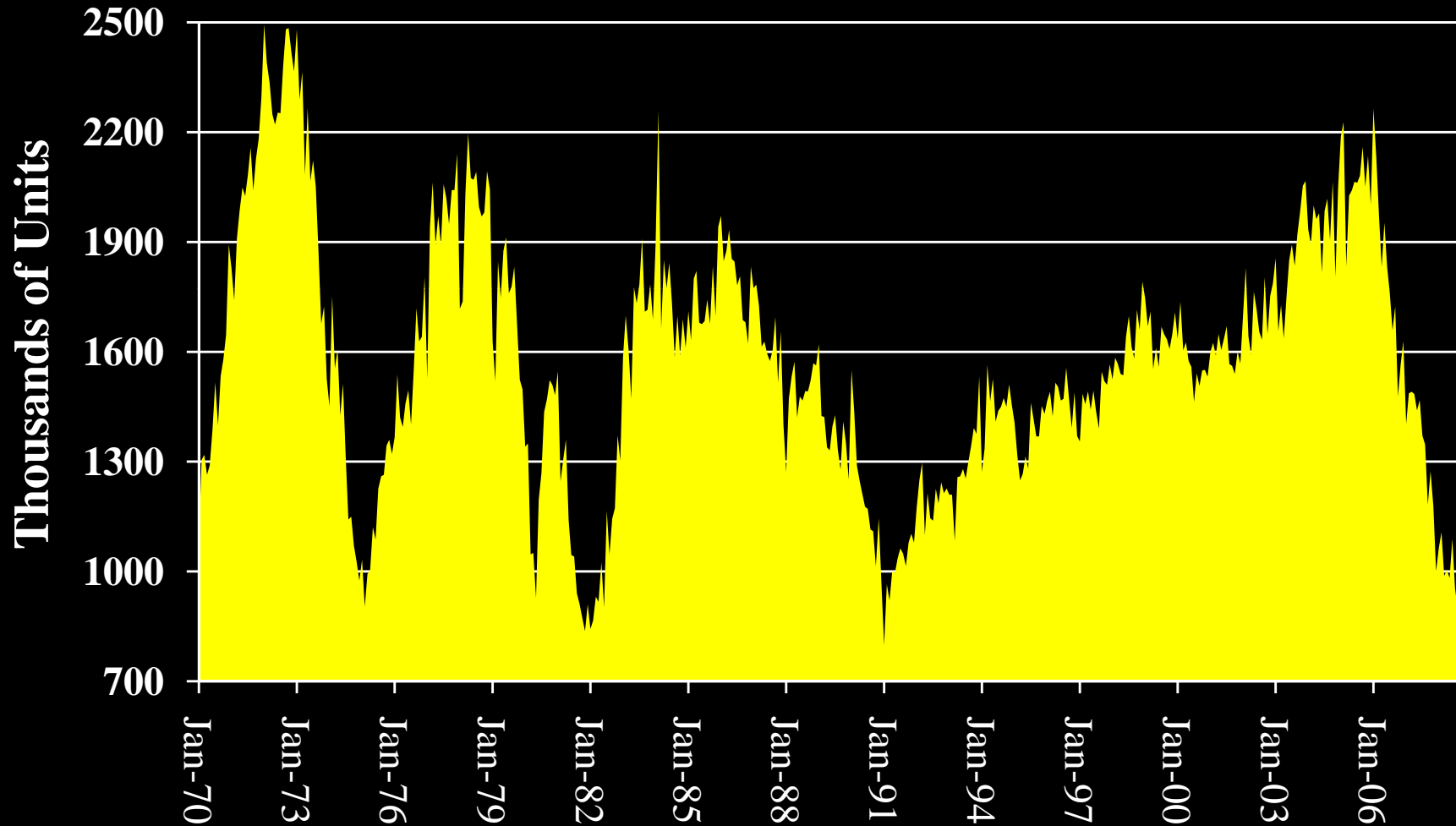


Builders Sentiment

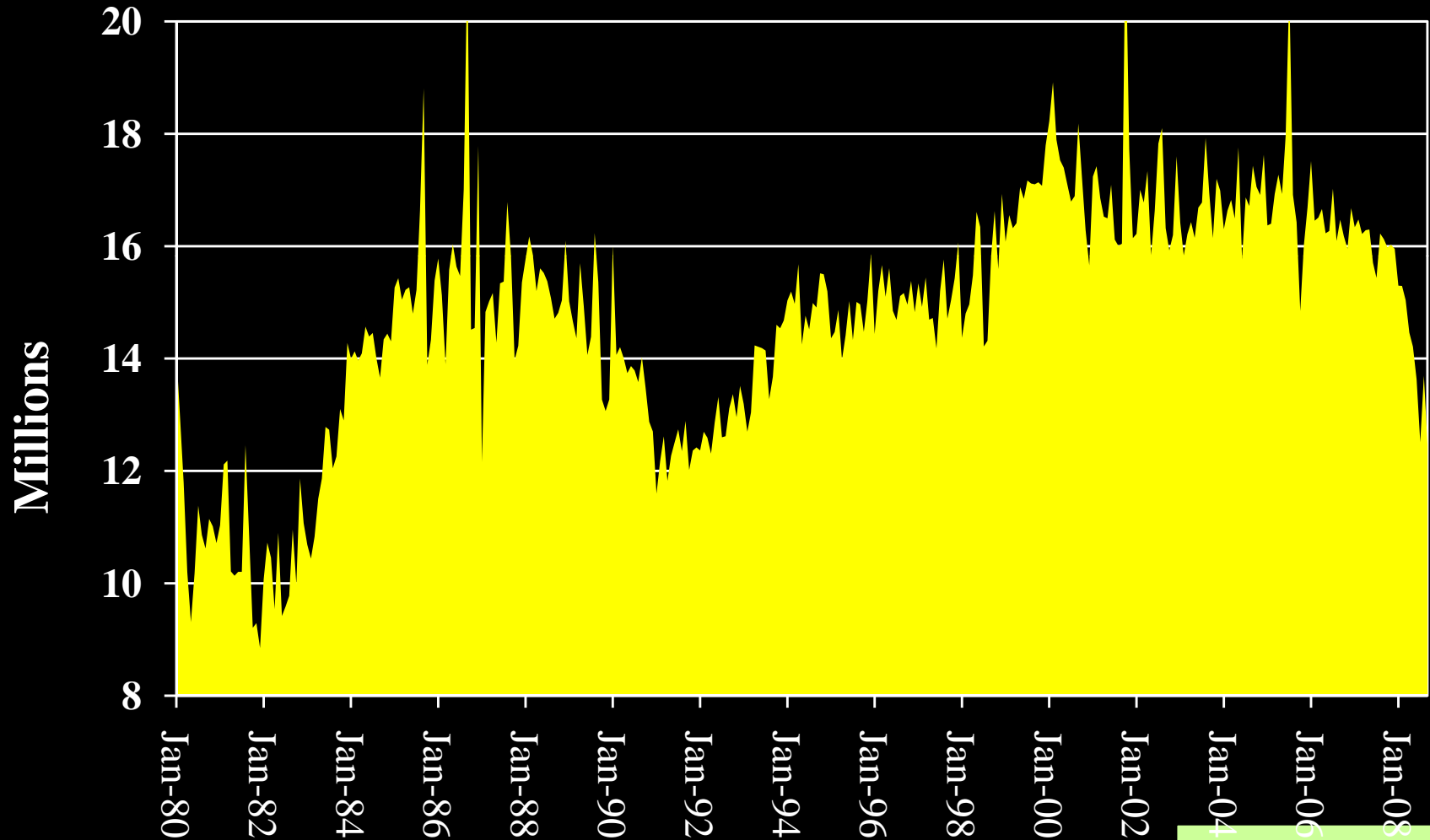
“Current Sales Are Good”



Housing Starts in the US



Car and Light Truck Sales



Updated 10/6/08

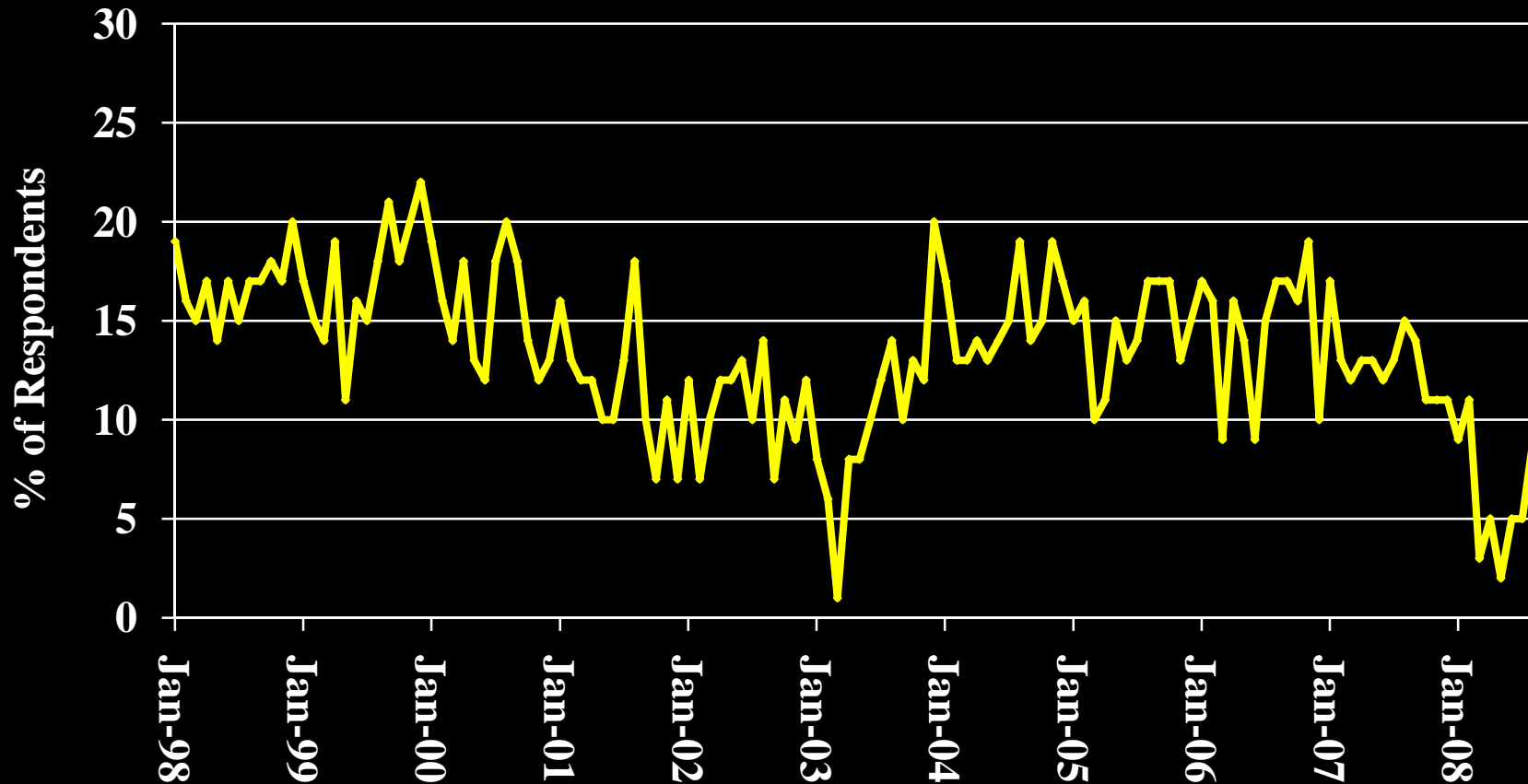
StLFed Bus/Fiscal



Source: Bureau of Economic Analysis

Small Business Outlook

“Planning To Hire People In The Next Six Months”



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

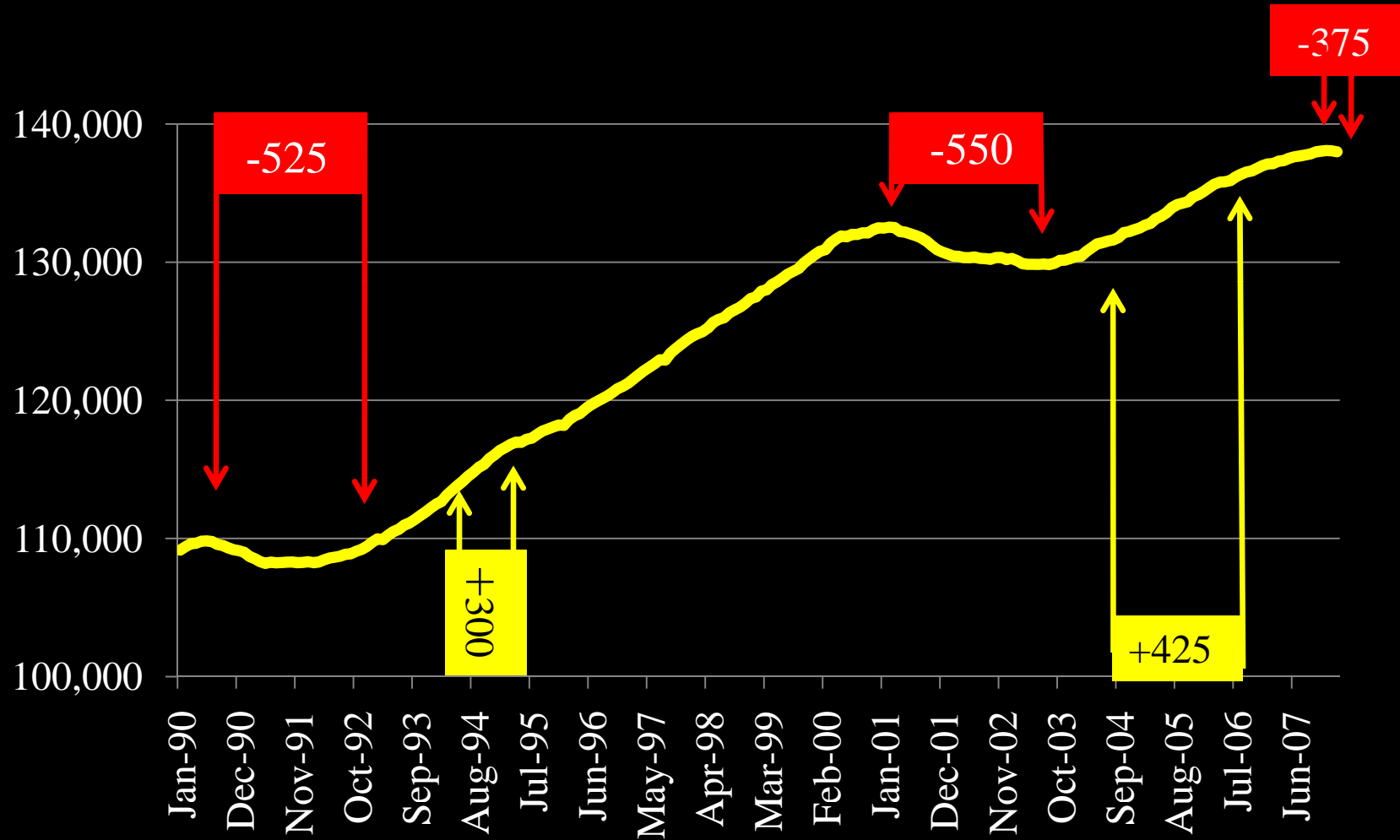
Recessions and Unemployment

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) –

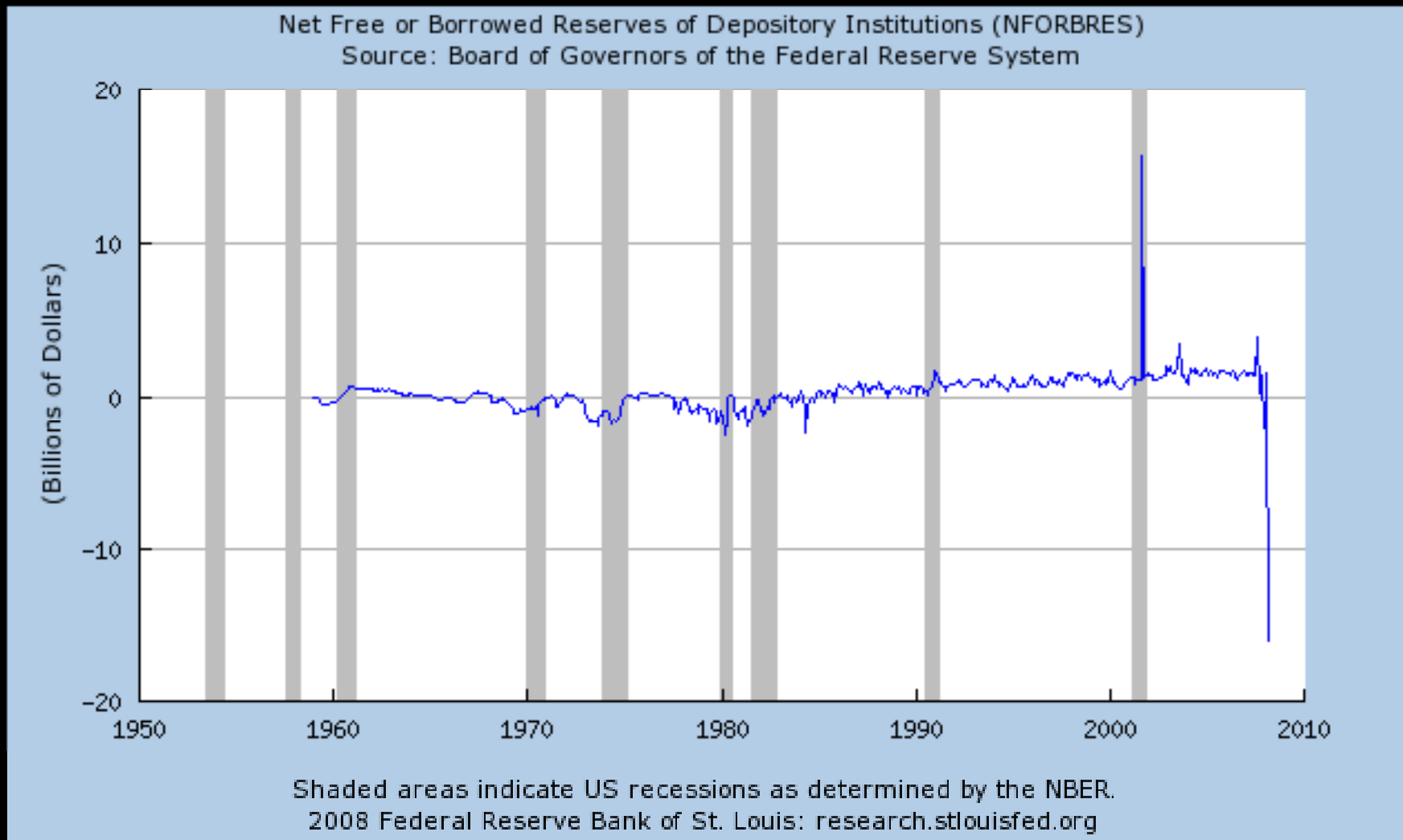
The Merrill deal included the sale of \$30.6 billion of repackaged debt known as collateralized debt obligations, or CDOs, to buyout firm Lone Star Funds, for just \$6.7 billion, or about 22 cents on the dollar.

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



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.

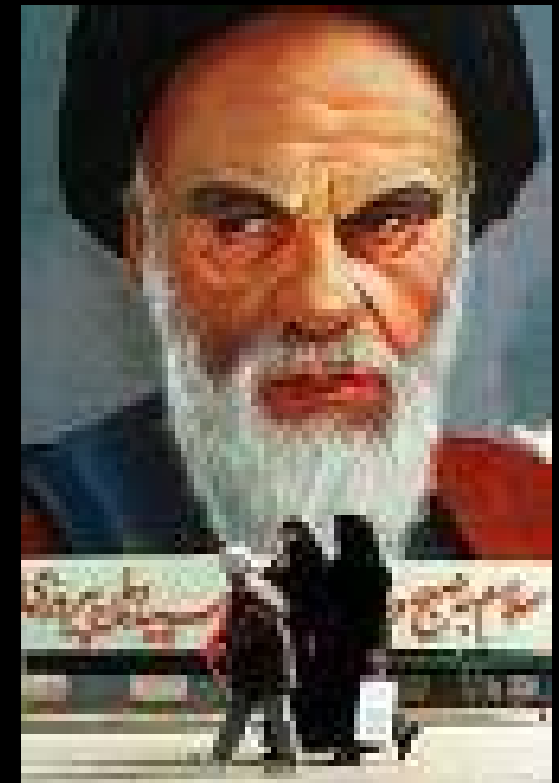
By January, 1975,
unemployment rose to 8.1%,
up from 4.9% in January, 1973.

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.