



The Economic Outlook for Real Estate Investors

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Beginning our Initial Approach for this Flight



Now

Still at high altitude at rapid speed,
starting a gradual descent

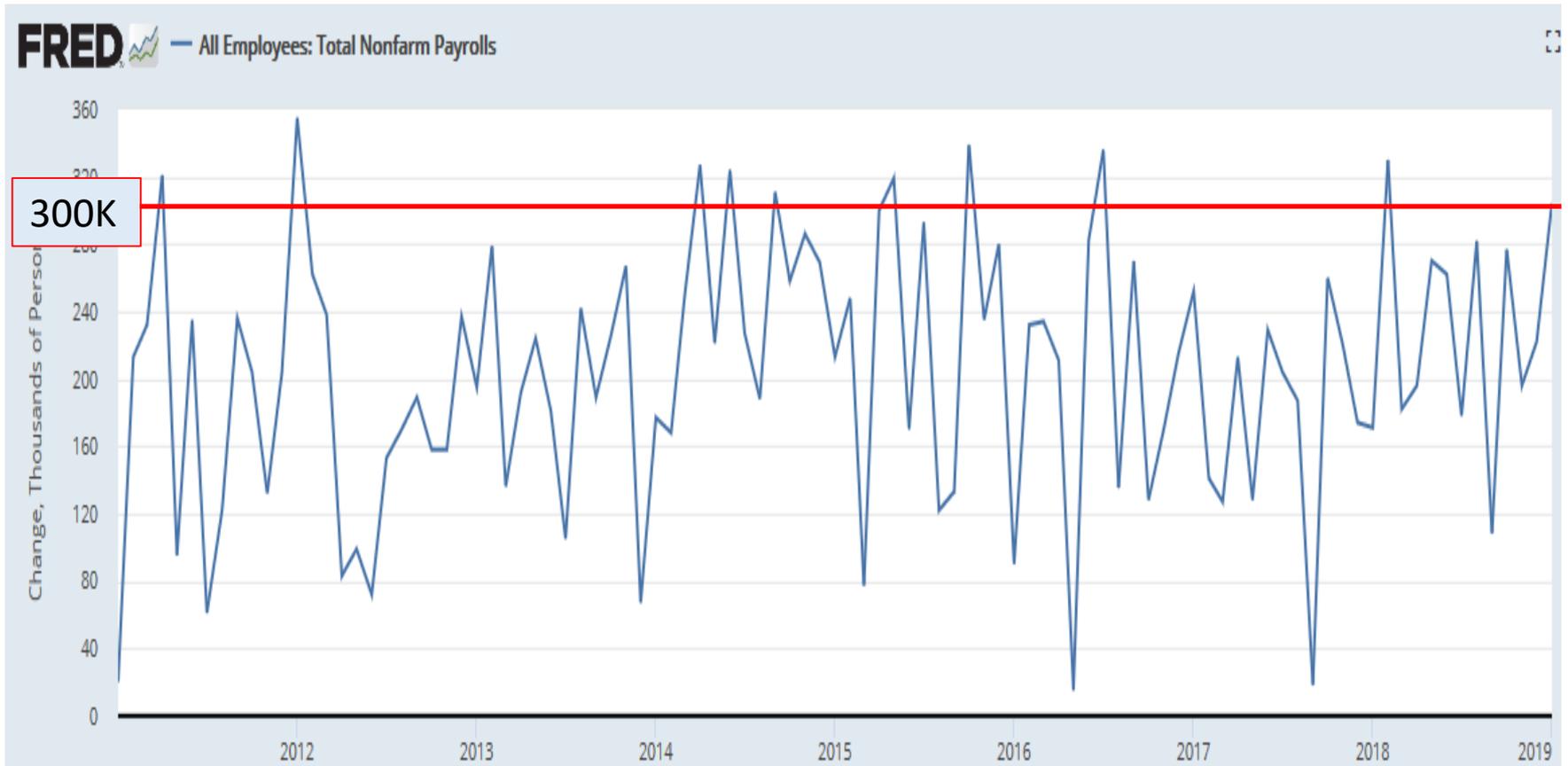


Not touching down

Not a crash



Monthly Increase in Jobs 2011 to present

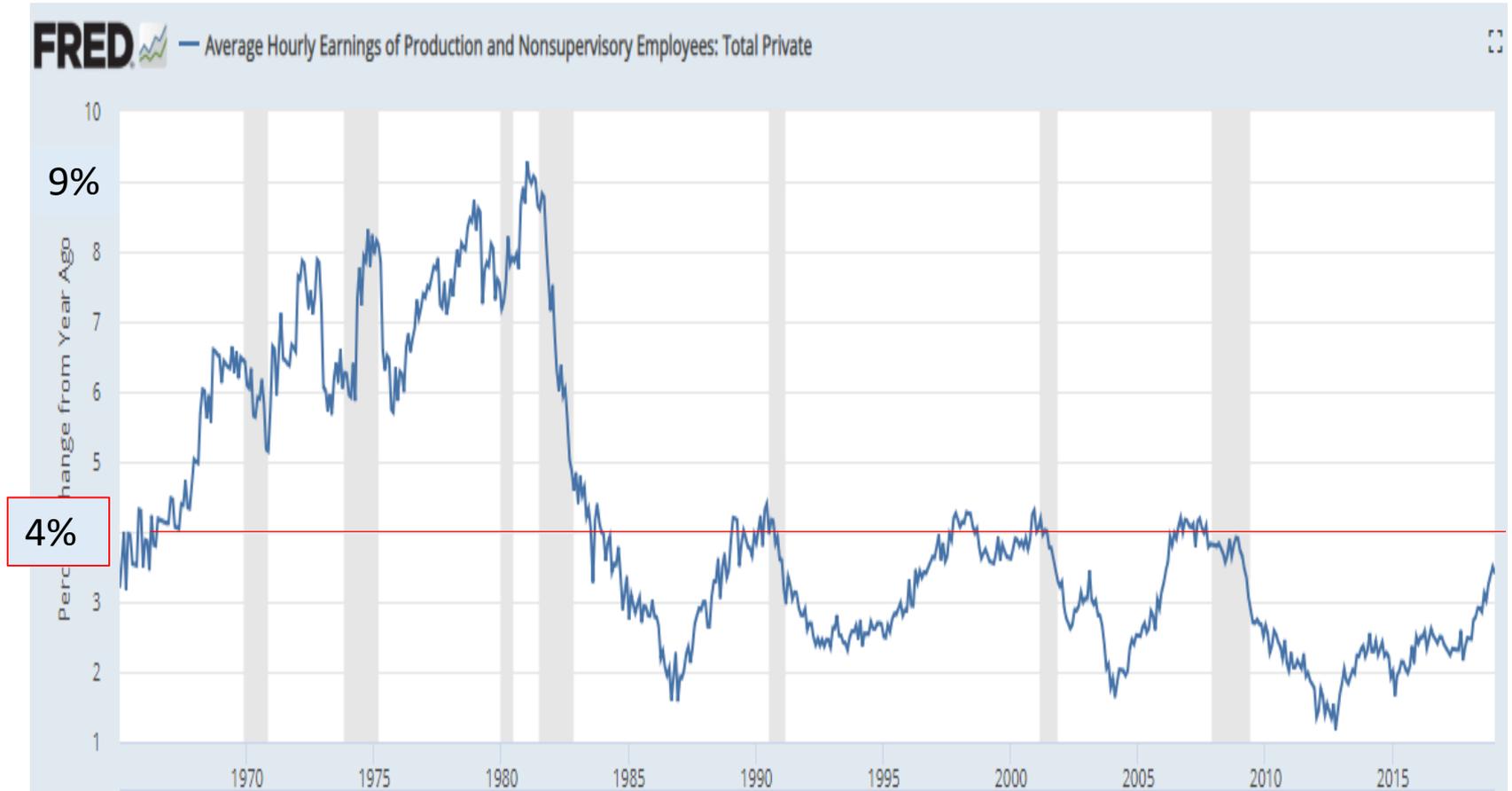


304,000 new jobs in January

Source: Bureau of Labor Statistics; Federal Reserve Bank of St. Louis

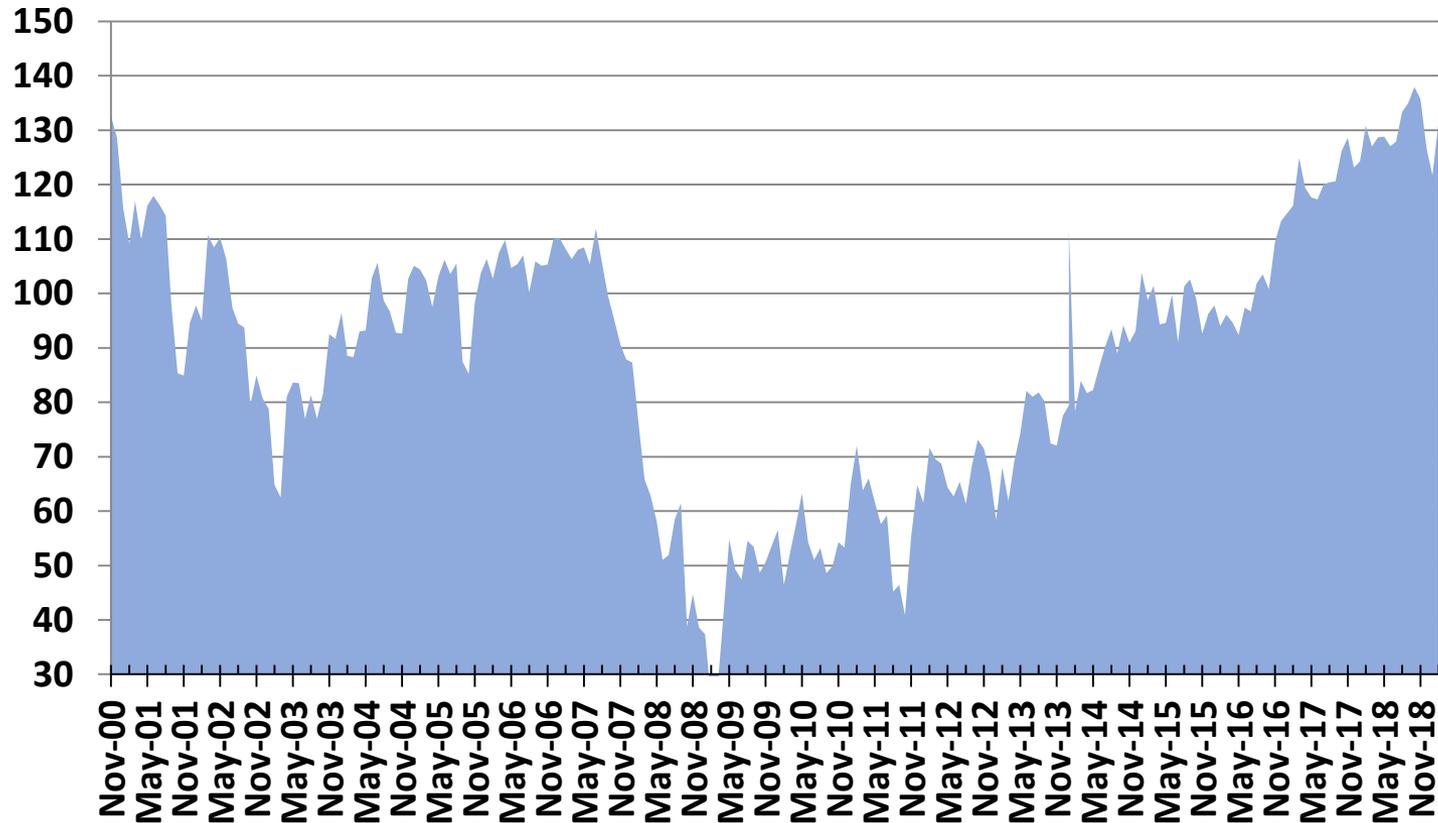
Rate of Wage Growth

1960 to present



Source: Federal Reserve Bank of St. Louis

Consumer Confidence Index



18-year high in October '18

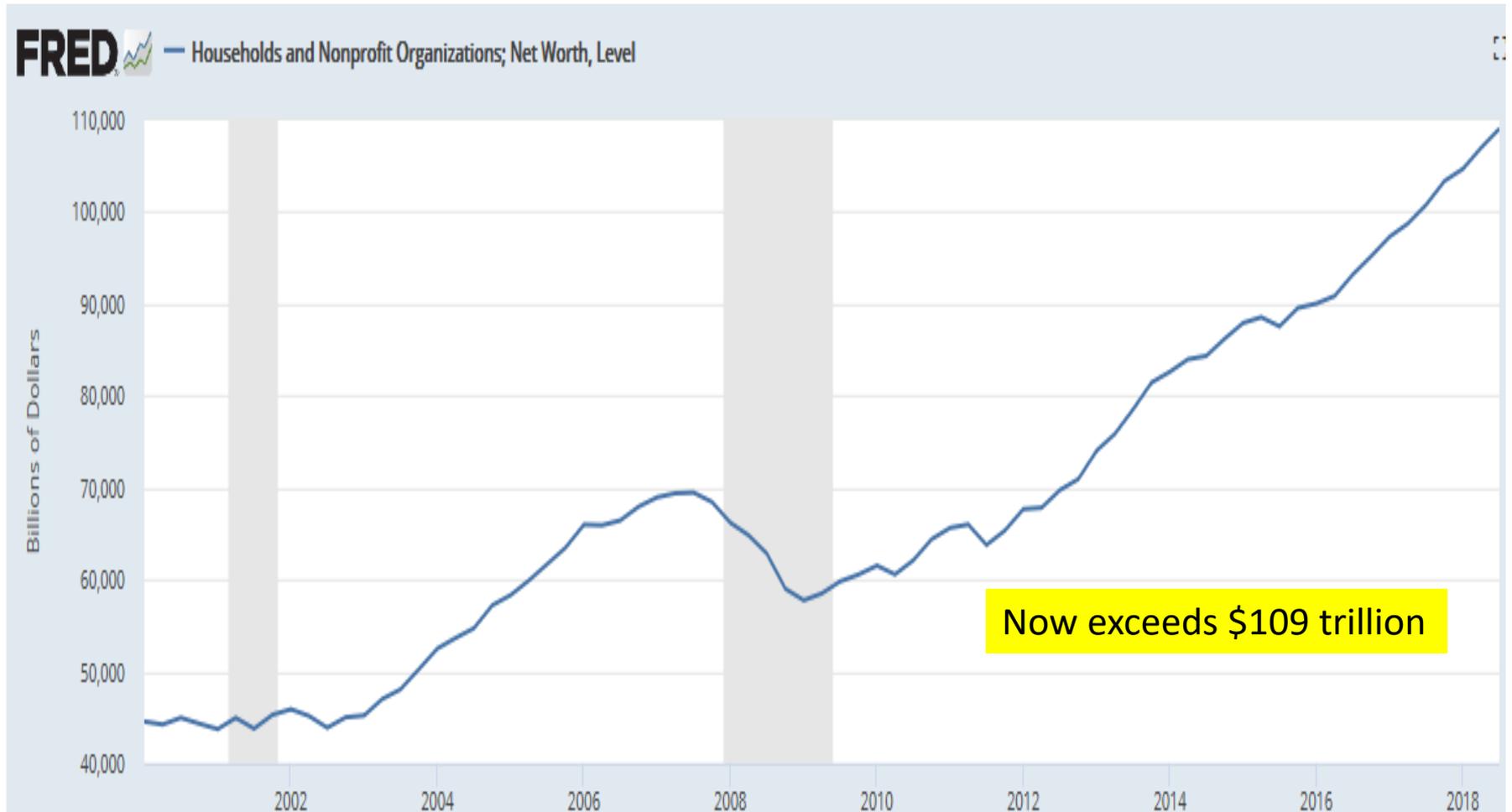
Job Openings in America

Looking for Workers



Source: Bureau of Labor Statistics

Household Net Worth since 2000



Source: Federal Reserve Bank of St. Louis

Why 2019 Will Be Slower

- Housing industry appears to have peaked
- Auto industry appears to have peaked
- Smart phone sales declined in 2017 for first time
- Low oil prices will pressure oil and gas
- Heavy duty trade negotiations with China
- Businesses not using tax benefits to expand
- Congress won't be interested in growth
- Downturn in stocks due to lower earnings growth

Why 2019 Will Be Slower

- Corporate earnings growth may have peaked
 - Defense spending may have peaked
 - Federal budget deficits can't get too much higher
 - Companies “buying ahead” inventory in front of tariffs
-
- **2.6% Interest on the 10-Year Treasury**

Longest U.S. Economic Expansions

Current expansion began in June, 2009

- Mar 1991 to Mar 2001 120 months
- Feb 1961 to Dec 1969 106 months
- Nov 1982 to Jul 1990 92 months
- Jun 1938 to Feb 1945 80 months
- Nov 2001 to Dec 2007 73 months

Current expansion as of April 2019 is 118 months

HOW LONG CAN IT LAST?

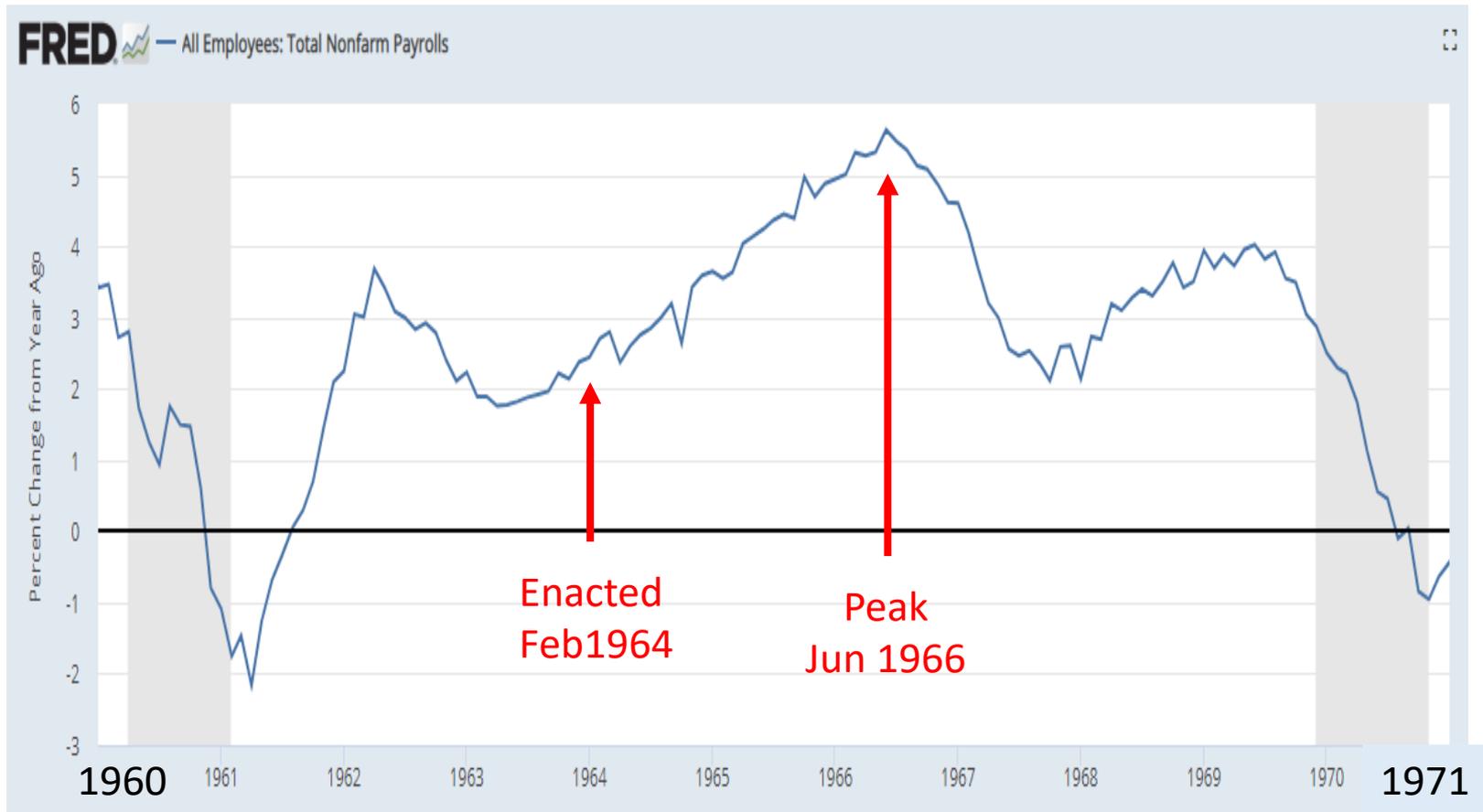


Revenue Act of 1964

Enacted February 26, 1964

- Recovery from recession of 1958 was slow.
- JFK campaigned in 1960 with the slogan of "getting America moving again."
- Proposed cutting individual tax rates from 20-91% to 14-65%
- Proposed cutting the corporate tax rate from 52% to 47%.

Percentage Change in Employment After the Kennedy Tax Cuts



Source: Federal Reserve Bank of St. Louis

Tax Reform Act of 1986

Enacted October 22, 1986

Top rate for individuals cut from 50% to 38.5%.

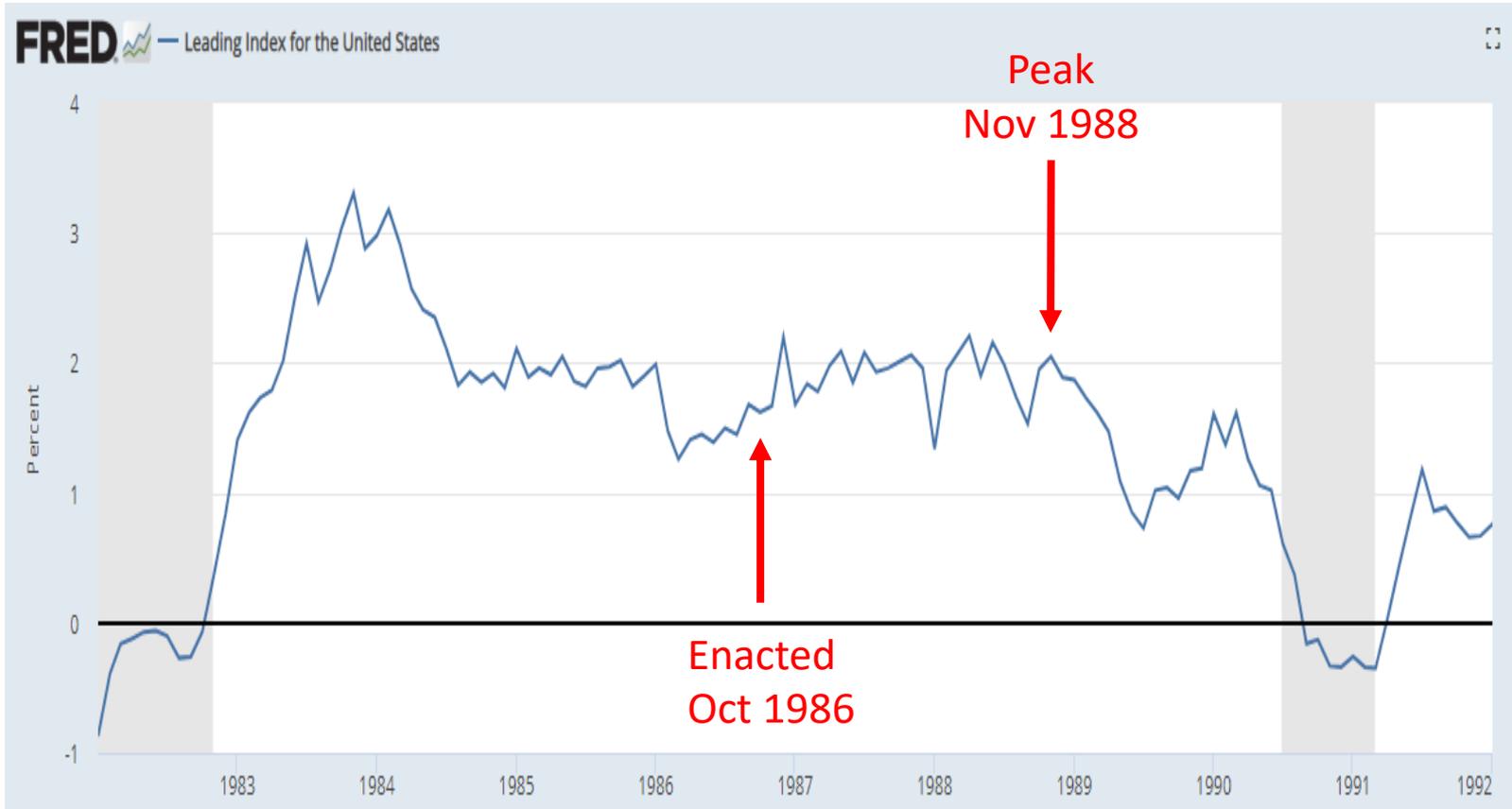
Major reduction of depreciation for real estate

Raised tax rates on capital gains.

Corporate tax rate lowered from 50% to 35%.



Index of Leading Economic Indicators After Reagan Tax Cuts



Source: Federal Reserve Bank of St. Louis

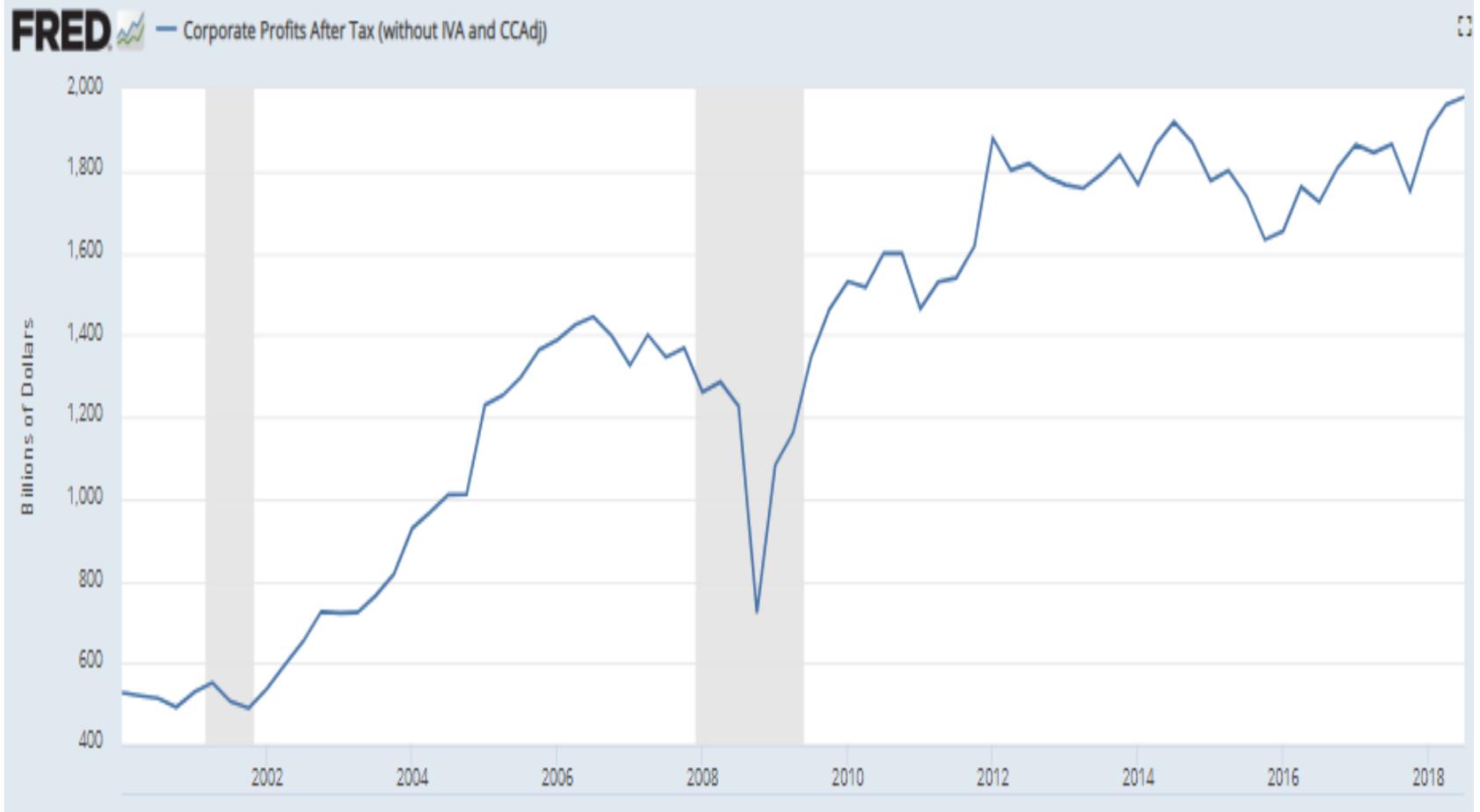


Early Warning Detection System





Corporate Profits



Source: Federal Reserve Bank of St. Louis



Corporate Bond Spread

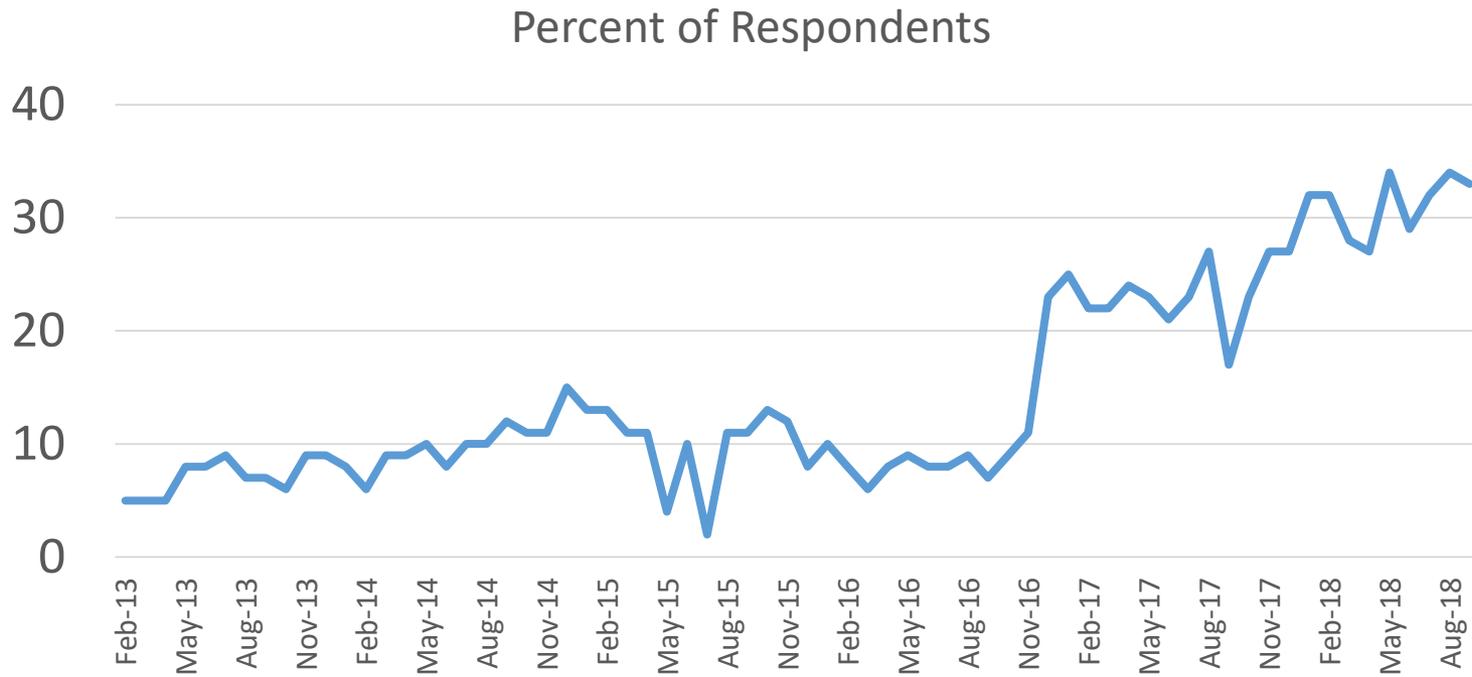
BB Corporate – 10 Year Treasury



Source: Federal Reserve Bank of St. Louis



Small Business Confidence: “Now is a Good Time to Expand”

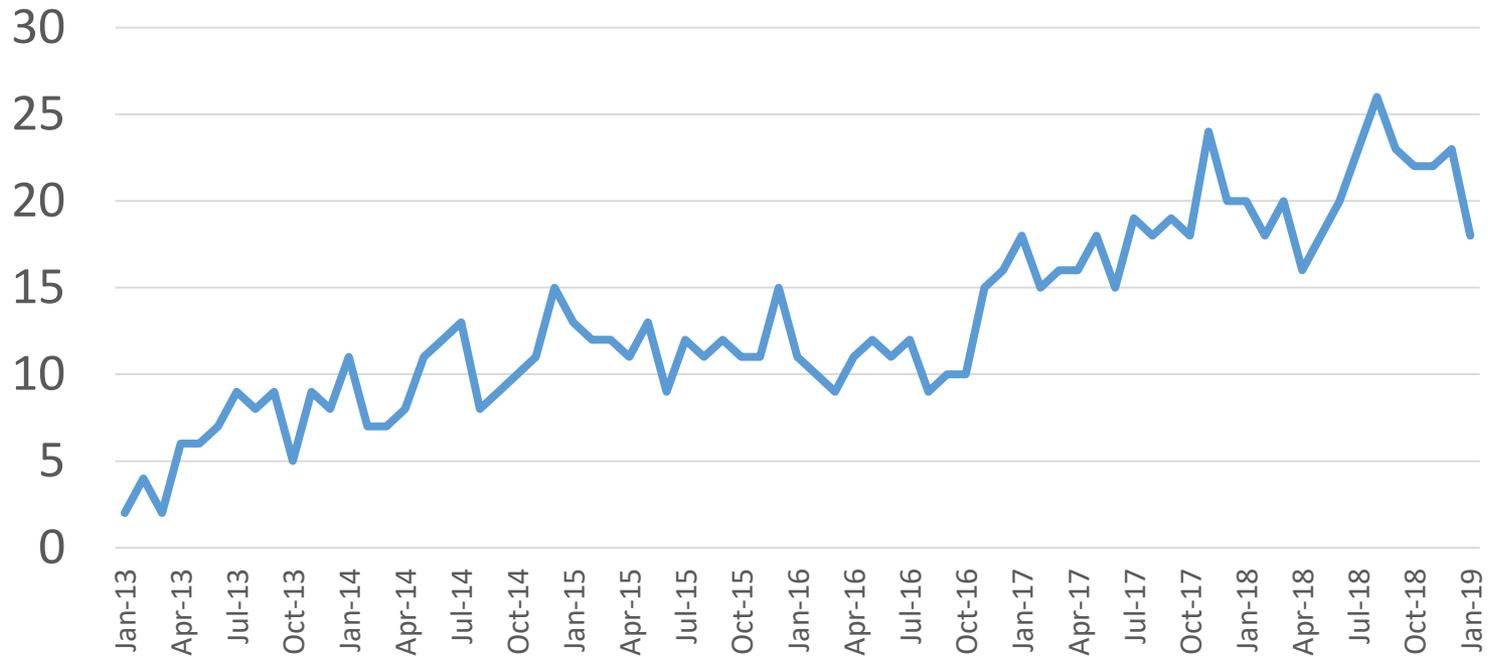


Source: National Federation of Independent Business



Small Business Confidence: “Hiring Plans in the Next Three Months”

Net Percent of Respondents



Source: National Federation of Independent Business



Large Corporate Hiring Plans: Next 6 Months

Q4-18 **Q3-18** **Q2-18** **Q1-18**

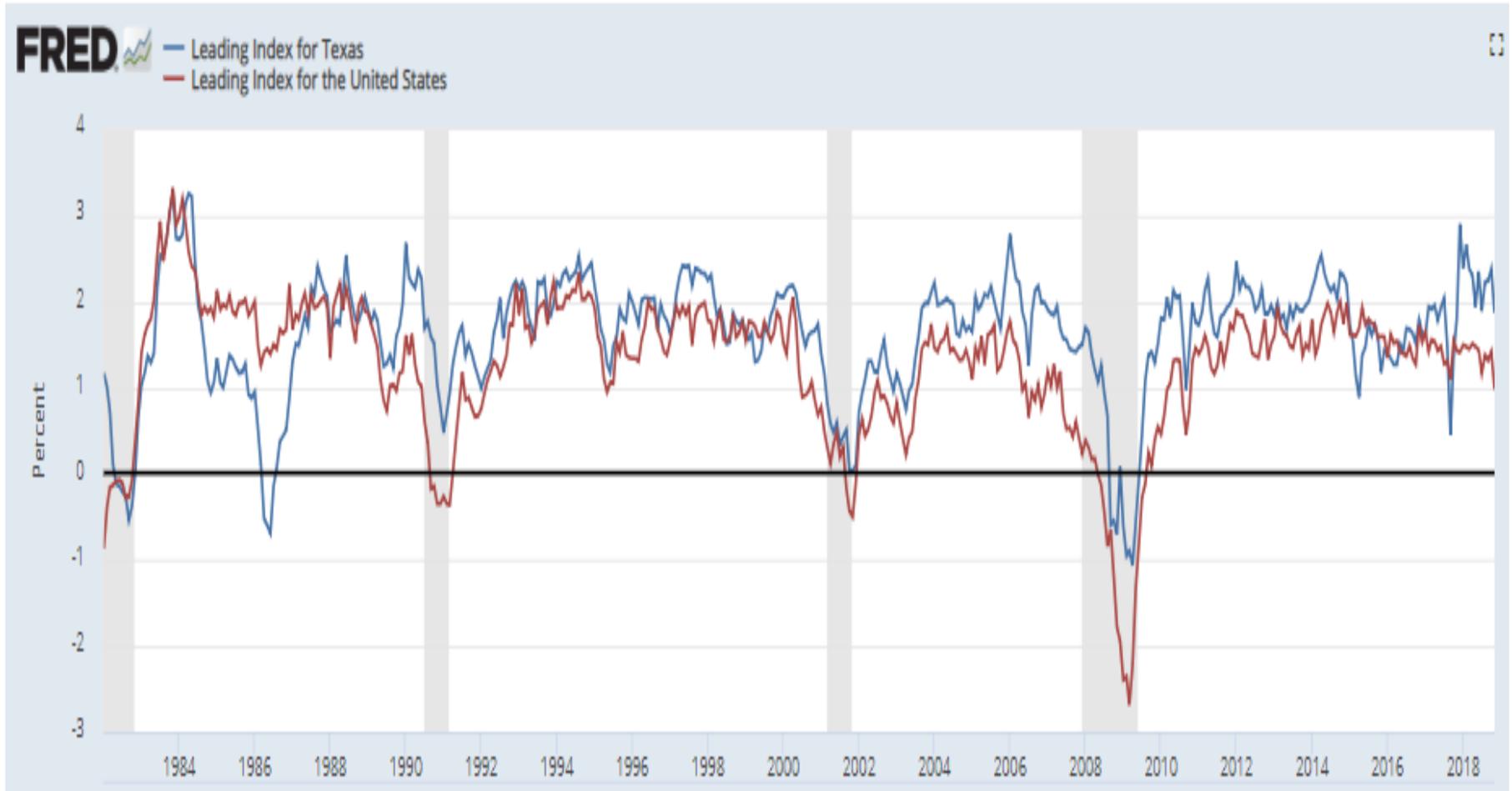
More Jobs 56% 56% 58% 61%

Less Jobs 14% 13% 13% 18%



Leading Index of Economic Indicators

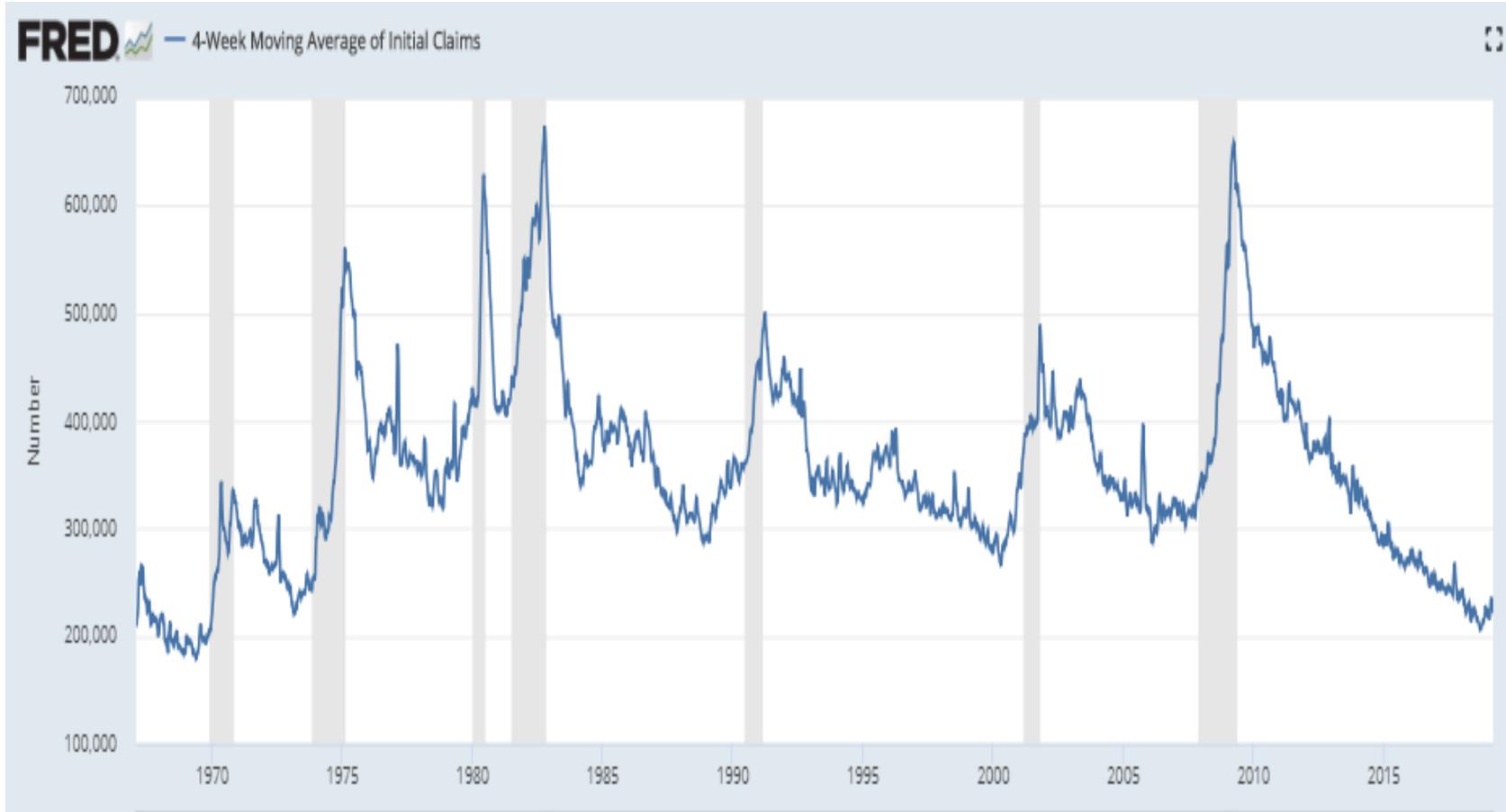
1982 to present



Source: Federal Reserve Bank of St. Louis

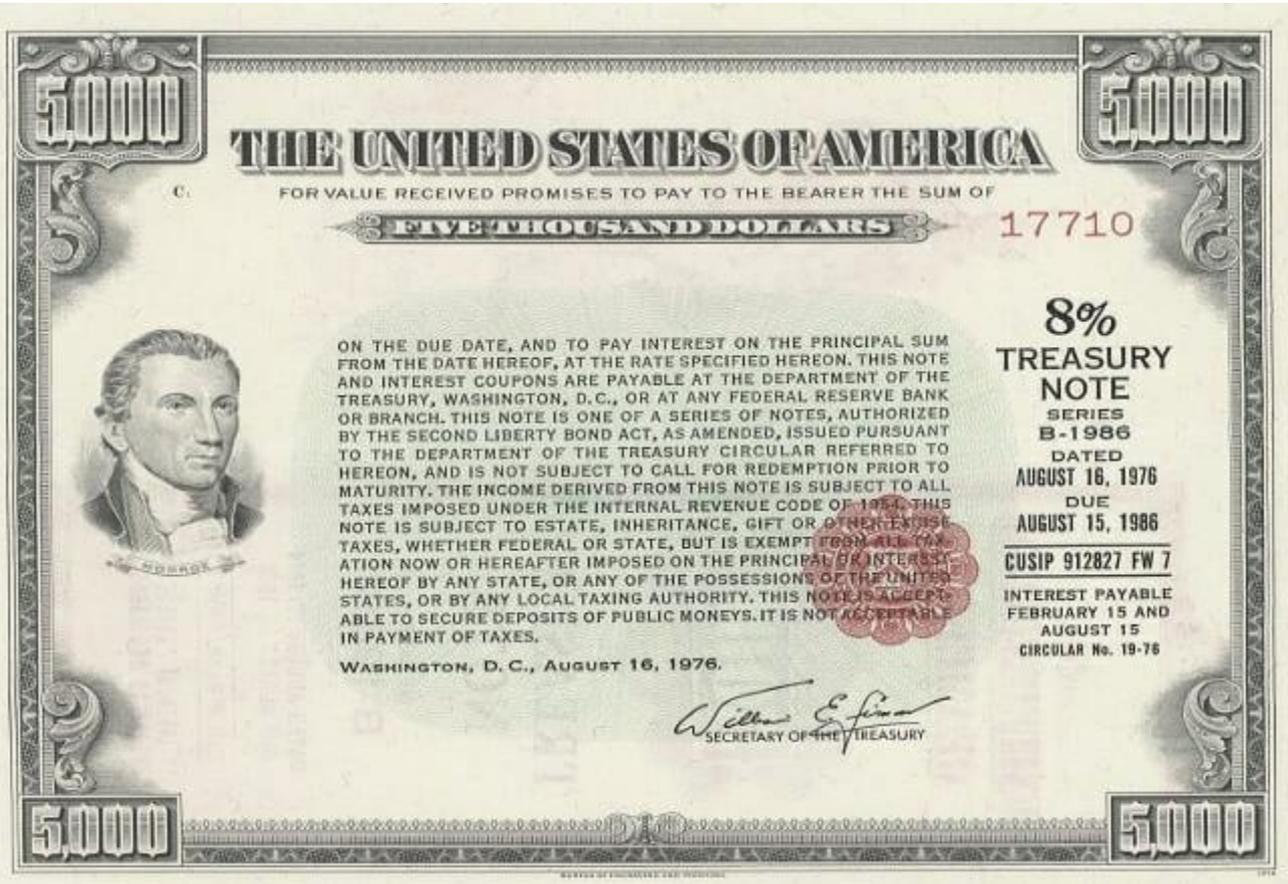


Initial Claims for Unemployment



Source: Federal Reserve Bank of St. Louis

Where Do Interest Rates Go From Here?



Rate Impact on the Housing Market



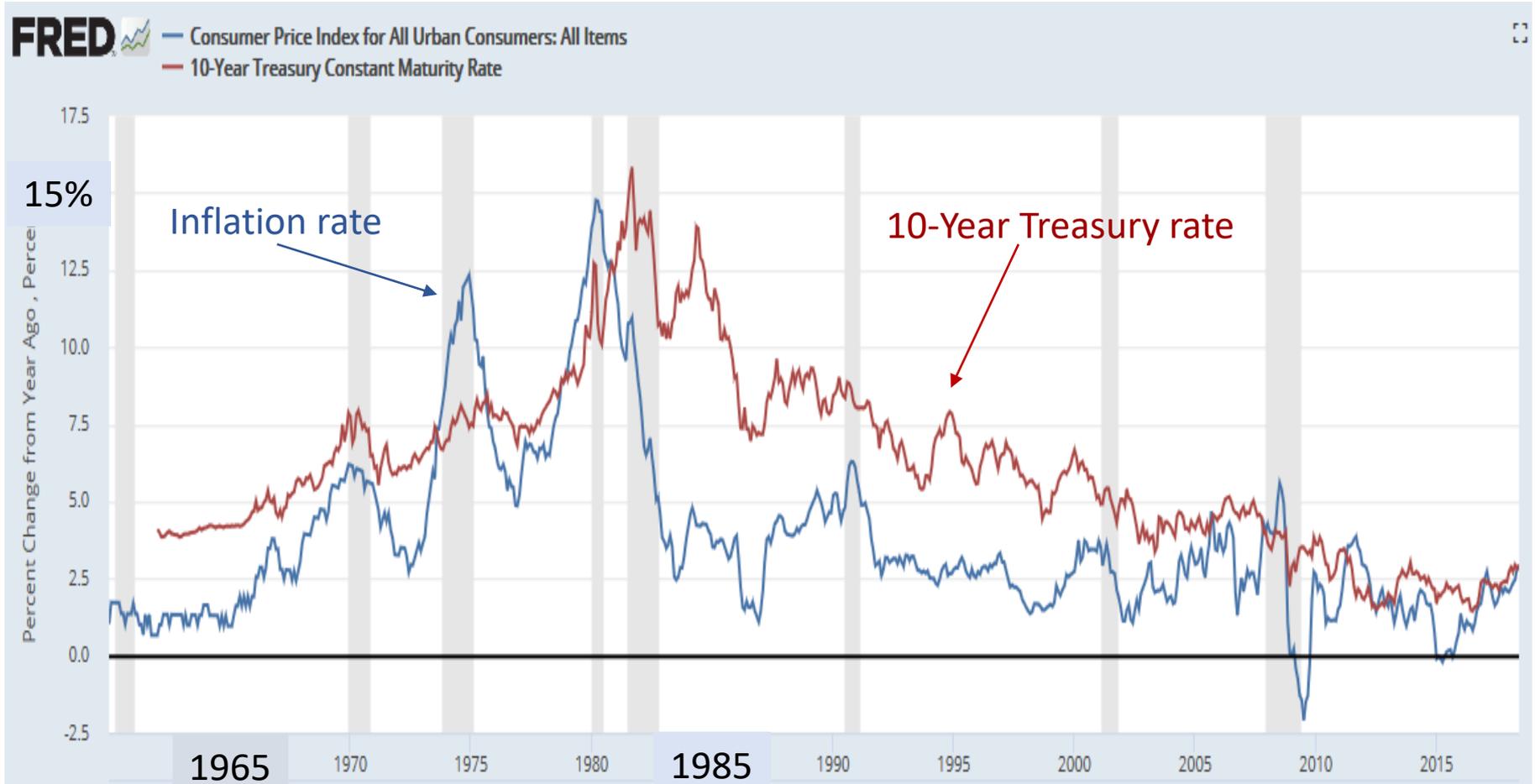
- Thirty-year mortgage rates are highly correlated with the 10-year U.S. Treasury bond rate
- The 10-year bond rate is not controlled by the Fed
- The 10-year bond rate moves up and down with the expected rate of inflation
- Conclusion: mortgage rates increase only when inflation expectations increase

Rate Impact on the CRE Market



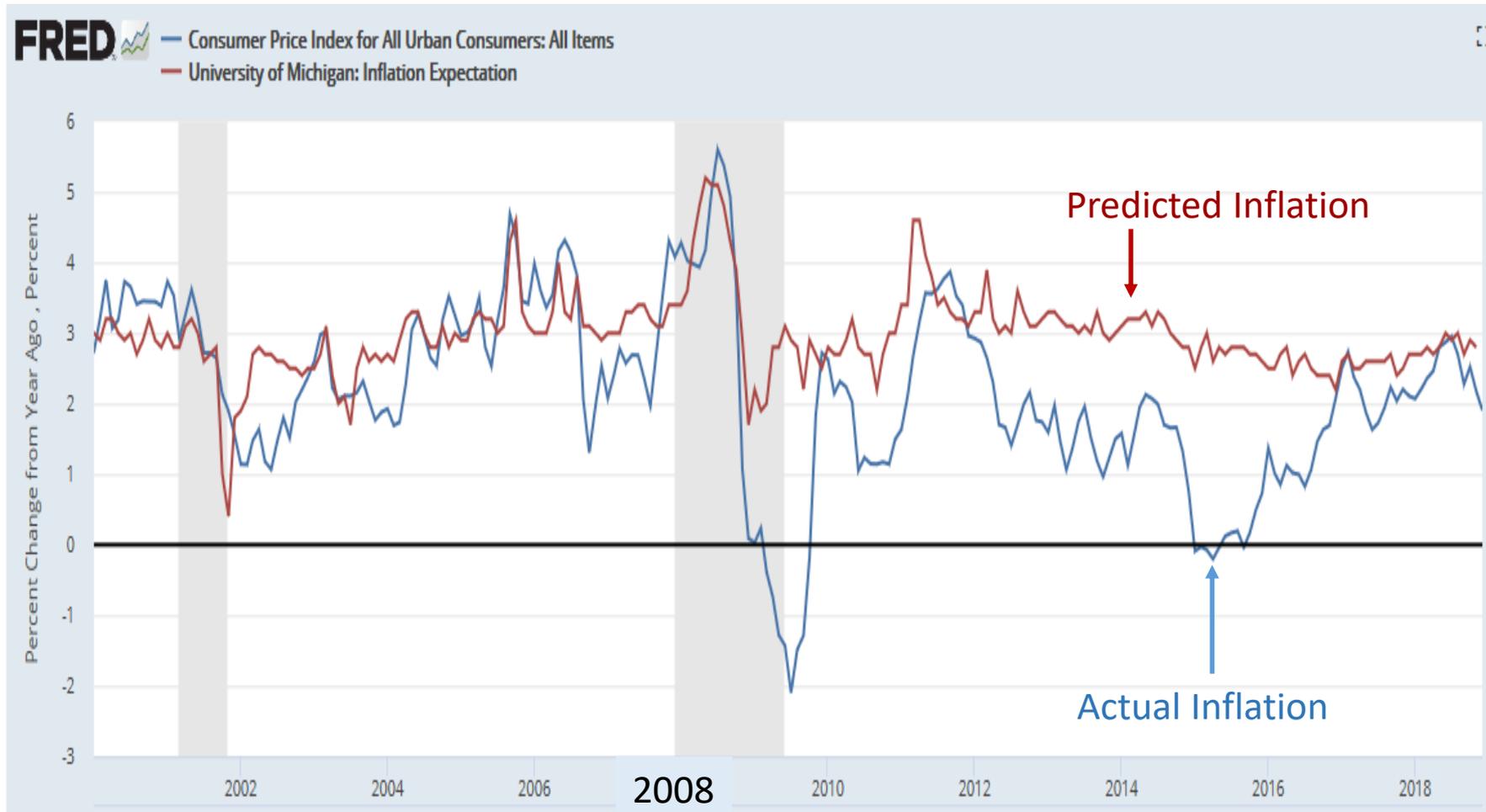
- Cap rates are moderately correlated with the 10-year U.S. Treasury bond rate
- The 10-year bond rate is not controlled by the Fed
- The 10-year bond rate moves up and down with the expected rate of inflation
- Conclusion: Cap rates might increase when inflation expectations increase

Inflation moves the 10-Yr Treasury Rate



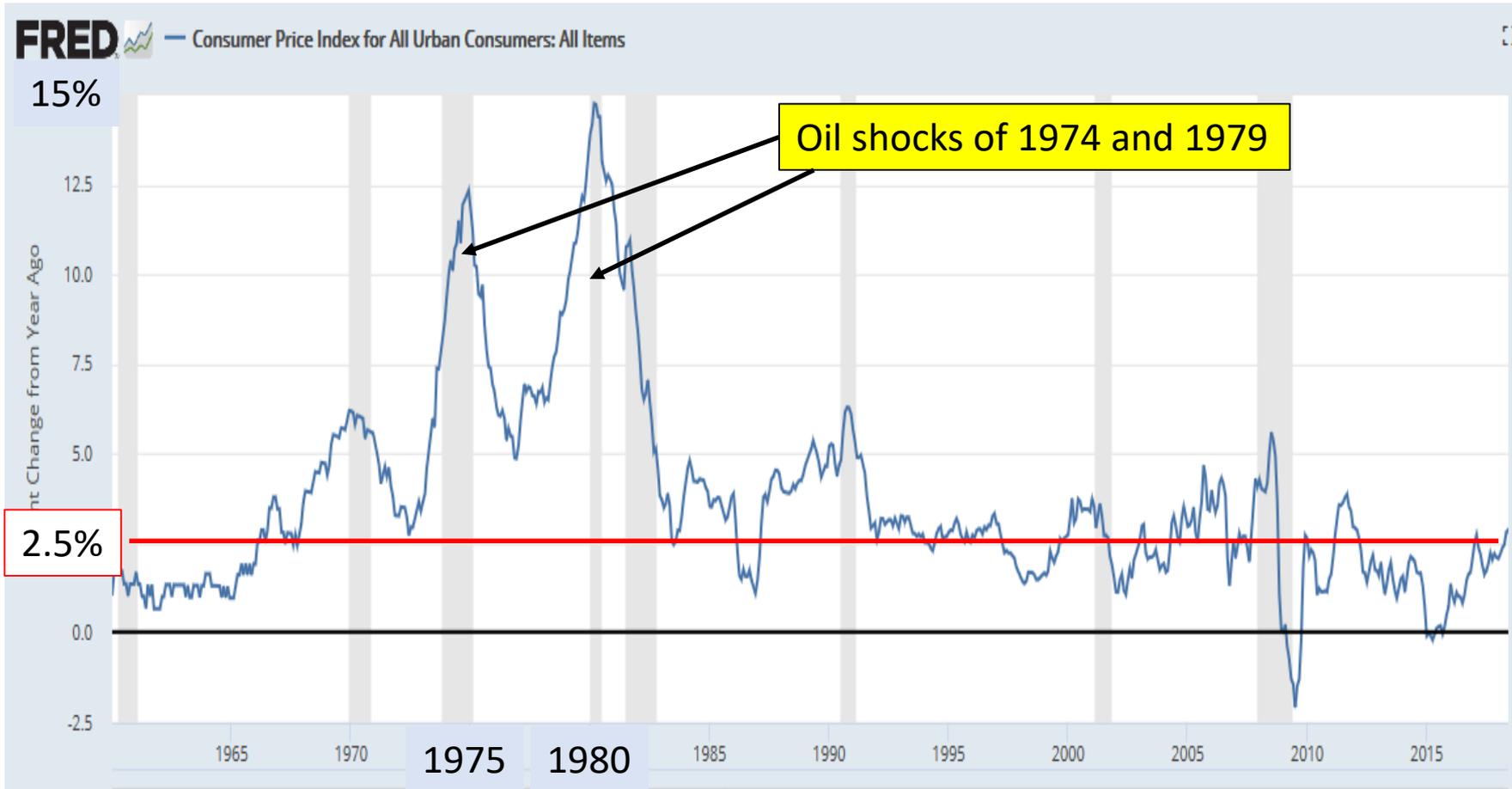
Source: Federal Reserve Bank of St. Louis

Economists Have Overestimated Inflation Consistently Since 2007



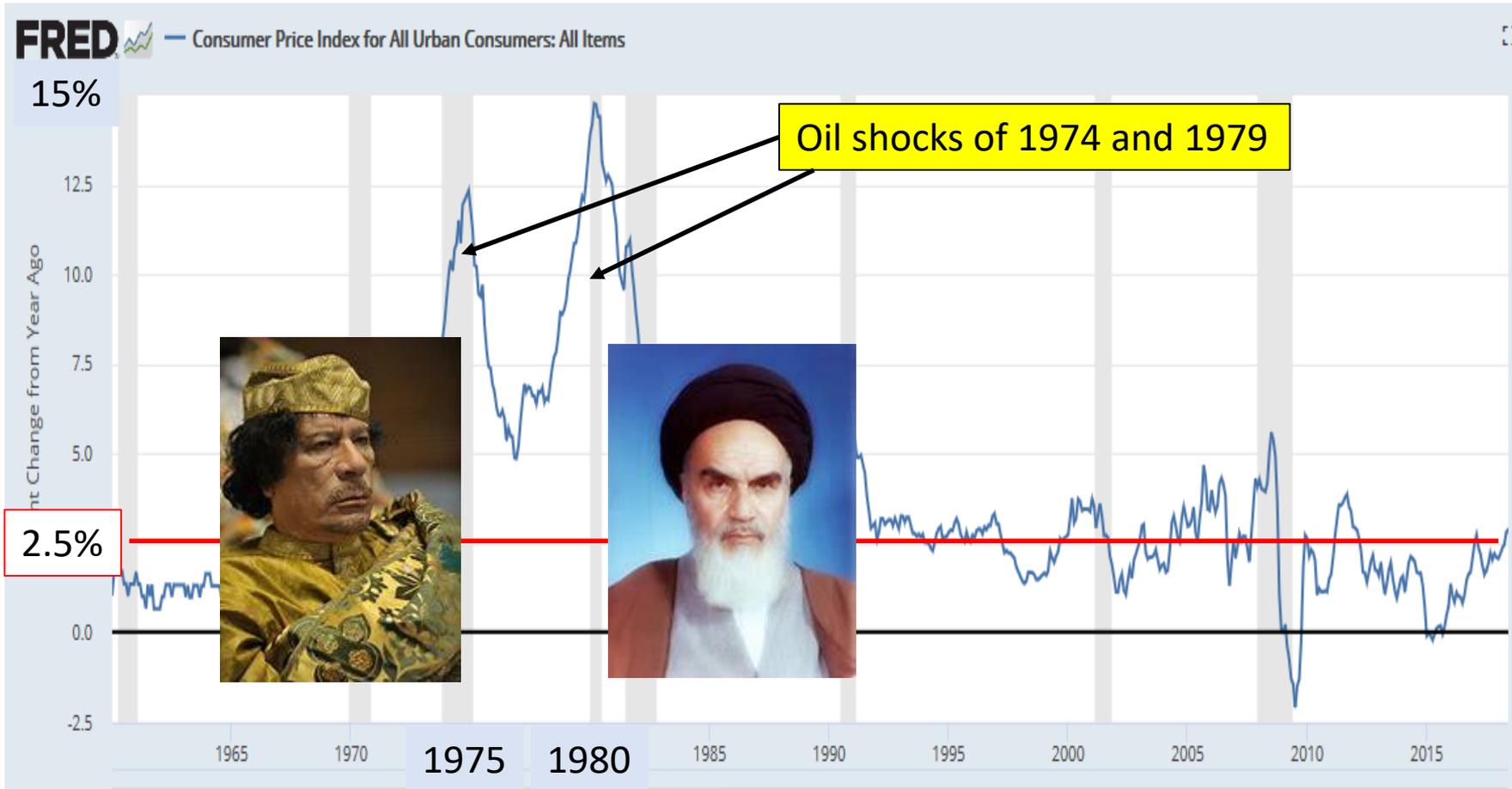
Source: University of Michigan and Federal Reserve Bank of St. Louis

Inflation Rate since 1960



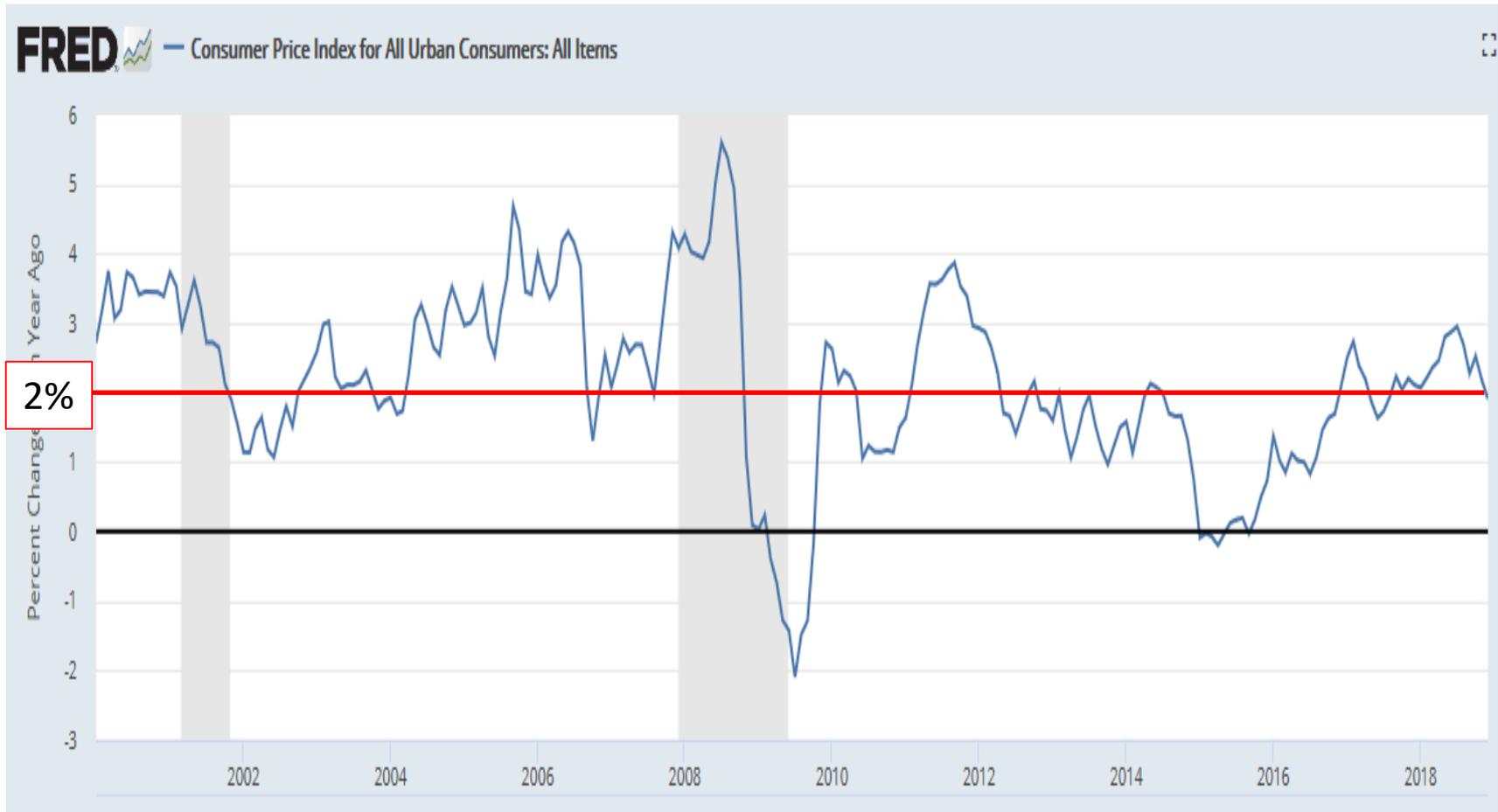
Source: Federal Reserve Bank of St. Louis

Inflation Rate since 1960



Source: Federal Reserve Bank of St. Louis

Inflation Rate since 2000



Source: Federal Reserve Bank of St. Louis

The Neutral Rate of Interest



“It is very difficult to know where that so-called neutral rate is. But we probably will know it when we are there because we will observe a certain degree of balance, which we had not perceived before, which would suggest that we are somewhere very close to where that is.”

Alan Greenspan, Financial Advisor News, June 9, 2005

Conclusions

- Positive job growth through presidential election.
- Interest rates unlikely to increase further.
- Tight supply and limited new single-family construction will continue to fuel demand for apartments.
- Industrial demand from e-commerce continues.
- Intense appetite for commercial real estate continues.
- Stock market vulnerable to slowing growth of earnings.
- Credit markets look strong.