SURVIVE AND THRIVE: MARKET STRATEGIES

2008 in Review and Forecast

After a year of turmoil, there are still options for builders who plan ahead

By Patrick S. Duffy

When 2008 began, the common wisdom of the day was that 2008 would prove to be a difficult year, and that builders should prepare for a market rebound sometime in 2009. However, with the world falling into recession and federal government bailouts becoming a staple of daily news, it now looks like any sustained market rebound could very well be postponed until 2010. There are however, still specific opportunities for builders who are willing to conduct detailed demand studies and plan for worst-case scenarios.

The current recession, like any others, began with a large shock to the economy – in this case, correcting a large imbalance in real estate markets nationwide. But what's making this shock even worse is that the combination of falling prices and tighter credit is preventing people from either refinancing their way out of trouble and staying put or simply selling their homes and perhaps changing both locales and careers.

If that wasn't enough with which to contend, this same lack of credit is beginning to force a correction in a related area – consumer spending and savings. Over the last 12 or 13 years, American households have been saving little and spending more. Add to that the additional monies from rising home values and fatter stock market valuations, and it's not hard to see why contributions to 401k accounts and savings accounts declined as household debt rose and incomes remained mostly stagnant.

Consequently we're in what the folks at Beacon Economics have dubbed 'the mother of all hangovers,' which in the short-run leads to something called the 'paradox of thrift:' as the savings rate goes up (which is good for household budgets) the overall economy shrinks due to less overall demand. Yet in the long run, these types of economic shifts are critical for an eventual recovery and to better leverage a productive workforce, great technology and solid investments in infrastructure.

So what's ahead for the overall U.S. economy in 2009? At this point in time, the forecast calls for mostly more hangovers with occasional sunny days in particular markets. As forecast recently by Beacon, GDP is expected to continue declining through the third quarter of 2009 as excessive demand based on debt is wrung out of the economy.

> **"One thing on which most economists agree is the important role played by new home affordability."**

Fortunately, the fear of inflation will be kept in check and rise only slightly to approach 1.29% per quarter by the end of 2010, although the entire amount of various federal bail-outs of the automobile, housing and other industries will also undoubtedly impact long-term inflation rates if the Federal Reserve continues to print money.

What that likely means for the new home market in 2009 is continued turmoil, although retiring NAHB chief economist David Seiders is hopeful for a mid-year rebound. Looking at the most recent figures, although the pace of annual new home sales rose slightly in September over August levels to 464,000 units, that level is still down by one-third from a year ago and marks the lowest September numbers since 1981. Even as builders continue to clamp down on production in an attempt to bring down inventory levels, at current sales rates, the number of unsold single-family homes – 394,000 – would take just over 10 months to sell. Still, at a recent semi-annual construction forecast, Seiders was hopeful that 2009 would be a rebound year and finish up with a seasonally adjusted rate of 600,000 single-family sales.

One thing on which most economists agree is the important role played by new home affordability. With a median selling price of just over $218,000 in September, the sharpest spikes in regional sales have been in markets suffering the steepest price drops, and the consensus is for prices not to fall more than another 10 percent in 2009. It's also in those same areas that builders, who have already cut prices just about as far as they can to remain in business, continue to compete with foreclosures. Yet as one economist presenting at the NAHB forecast concluded, builders don't have to convince everyone to buy a new home – just some people. B&D

Patrick Duffy *is a Principal with MetroIntelligence Real Estate Advisors (www.metrointel.com), a division of Beacon Economics (www.beaconecon.com) and authors The Housing Chronicles Blog (www.housingchronicles.com). He can be reached at pduffy@metrointel.com or at 888-82-DEVELOP.*

Fast Facts

- 2009 will be the 'mother of all hangovers' for the overall economy.
- Unemployment will rise as inflation remains in check.
- Less production will continue to help inventory levels.
- Rising affordability will spike sales in larger & healthier markets.