USA Economic Recovery Via Real Estate Markets?

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Recently the USA economy does not seem to be doing too well, and there are debates on whether there will be a "double-dip recession" (which the famous Paul Krugman of Princeton thinks is not entirely without reasons). Your humble author will leave these to the proper authorities and economists to further explore, though as a pure amateur on economics tend to side with the double dippers. The confidence required for continuing with spending / consumption thus leading to / sustaining an economic recovery, some say, will need to come from the real estate sector (with steady home prices etc), now that the stock market pillar becomes marginalized. Your author tends to think not, at least not from an angle of spending your (potential) recession away, here are some of the observations and reasons:

a) **"Last Real Estate Bust"** = As a very rough statement, real estate in North America boomed following the 1987 stock crash. It lasted for a few years and then it busted, cumulating into a savings and loans crisis. Real estate values in some sectors lost 30% to 40% of their peaks though markets stabilized after an initial crunch. Nonetheless, prices only got to recover several years later. Any similarity here this time around?

b) **The last boom and bust being more comprehensive** = The boom and bust in the late 80s and early 90s was more across the board, and not just residential real estate gained, but the office, retail and industrial sectors were doing well too. Today, the office sector is suffering and the only shining star seems to be the residential sector. Is this enough to support an economic recovery if any and at all?

c) **The median home price is not overly high** = based on published statistics, it hovers around US$170,000. Given that the home is the greatest asset for most families, and even if some bank savings (reportedly families saved 7% of their income 10 years ago, now they save practically nothing) and / or direct or indirect stock holdings (much reduced in value now) are assumed, families may need to be more frugal than they used to be. And this has not taken into consideration the family debts such as mortgages etc.

d) **The changing household profile** = In1948, 80% of the US families involve couples with kids, and less than 20% of the households consist of singles etc. Today, the former category occupies 53% and the rest are single-parent families or singles etc, in part reflecting the higher divorce rate etc (note: divorces adds to residential demand from 1 unit to 2 units). The advantage is that for real estate developers and home builders, there has been a constant changing need for new styles and designs of homes. The disadvantage is that certain home (old) styles, say for instance single family detached homes in some cities or areas, may have a hard time trying to find a buyer when and if the original owners (couples) retire or wish to move. Generally, these changes take place slowly or go largely unnoticed until one day when a certain critical mass is achieved. Then the issue may become quite obvious.

e) **The graying population** = when people age, they tend to become less aggressive in their investment behavior (whether they actually invest safely and conservatively is another thing). Reportedly, in the next 10 years or so, there will be 4M to 5M people reaching their 50s and 60s each year. Attention for the better off ones may be given to leisure, family, and fun (though these consumptions will benefit the economy and thus indirectly the asset prices), and less toward direct investment opportunities, real estate included. Hence, it is not that real estate may not boom, it is just that the pattern of growth may be different from what were seen in the past.

f) **Average family income per year is around US$55,000** = based on figures from year 2000, 88% of the households earn less than US$100,000 per year. These are not small numbers to smear at, yet given the taxation system and tax rates, probably most households will have little left to invest or spend other than those afforded by law such as 401K etc. IF the economy is to be given some push by real estate, in particular the residential sector, then it may imply having each home-owning household taking additional mortgage to finance their spending. Will they?

g) **Real estate in the long run does NOT lead the economy, it reflects it only** = real estate is a derivative industry, and while it is true that a new home implies new furniture, new decorations and the like, thus contributing to GDP, which in turn thus give a false impression of ' leading' the economy, very technically it does not. Here' s an analogy: Say a person becomes successful and has accumulated much wealth / money [Event A]. With greater wealth, the person wishes to buy a home [Event B]. Thus, Event A (successful business, more money, or high earning power of the person) leads to Event B (home buying). Generally, when people buy homes, they will include in their budget sums for furniture, legal fees, decorations and the like. These things do not pop out all of a sudden nor are they optional in the process. Hence these items are just part of Event B and are not separately events on their own. From another angle, IF real estate can really LEAD an economy, all one has to do to solve any economic problem will be to build more properties. But does it really work like that?

Again, the author is not an expert on economics and does not know exactly where the US economy will go. Yet the expectation of a recovery stimulated by (residential) real estate activities seems wishful thinking.

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