

# Del Mar Times

## *Will a slowdown in housing hit the economy?*



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“If you build it, they will come” worked for Field of Dreams, but it may be losing its legs in the housing market.

The housing market has been very strong for several years due to low interest rates and the rising popularity of real estate investing. The National Association of Realtors projects that total housing starts this year will reach 2.06 million units, the highest since 1972. However, four weeks ago one of the country’s largest high-end homebuilders surprised Wall Street by announcing it was cutting the number of homes it expects to build in 2006 to between 9,500 and 10,200.

That is down from a previous forecast of between 10,200 and 10,600 homes. The company cited softening demand, an increasing regulatory environment and community-opening delays.

Perhaps Wall Street analysts should not have been too surprised at this announcement. The Dow Jones U.S. Home Construction Index has been telegraphing a slow-down in the housing market for the past few months. That index hit an all-time high of 1,115 in July but closed on Nov. 11 at 878, according to data from MarketWatch, Inc. This 21-percent decline suggests that some people expected a decline was on the horizon, and they sold out. However, even if the housing industry has run its course for this cycle, our economy is so resilient that there may be another sector waiting in the wings to take its place. We might have a little more trouble locally.

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Just like the post office, neither rain, nor snow, nor heat, nor hurricanes, nor gloom of night seems to be able to slow down our economy.

The U.S. economy grew at a respectable 3.8 percent annual rate in the third quarter, according to gross domestic product data released on Oct. 28 by the Commerce Department. Remarkably, this was the eighth quarter in a row that the economy grew between 3 percent and 4.5 percent, a level of consistency not seen since World War II, according to the Wall Street Journal.

How did the stock market react during those eight quarters? Quite well. The S&P 500 Index rose 23.3 percent for the two years ending Sept. 30, 2005, according to data from Yahoo! Finance.

With two years of steady gross domestic product growth under our belt, are we in a new era of economic stability?

Economists have suggested the steady growth was due to an effective Federal Reserve monetary policy directed by Alan Greenspan, highly sophisticated financial markets that have done a better job of spreading risks, just-in-time inventory management techniques that have reduced gluts, and better business forecasting techniques.

Do those factors mean this time is different and we can expect steady gross domestic product growth to continue indefinitely? Well, usually when people make the "this time is different" statement, they end up with egg on their face and holes in their pocketbook. So for now, we will take the steady growth as a two-year gift and stay focused on trying to discern how much longer it may last.

Inflation has been grabbing the headlines lately; should we be worried? If it gets out of hand, then yes. The last time inflation wreaked havoc in the economy was back in the late 1970s and early 1980s.

As you may recall, those were difficult economic times. Here are a few examples of the problems we experienced back then due to inflation:

Today, rates average just over 6 percent. To put that in perspective, the monthly payment on a 30-year, \$300,000 mortgage at 18.5 percent would be \$4,643 versus \$1,808 at 6.1 percent.

Interest rates rose dramatically back then, as the Federal Reserve purposefully drove up short-term rates in an effort to break the grip of inflation. The Fed succeeded, and by 1983 inflation dropped to 3.2 percent. However, the high interest rates had a nasty side effect.

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