NAIOP 2001 Economic Forecast

Panelists:

Ken Mayland  
*President, ClearView Economics LLC*  
*Cleveland, Ohio*

Tucker Hart-Adams  
*Chief Economist*  
*US Bank*

Moderator:

Paul Luber  
*Ernst & Young*  
*Real Estate Advisory Services*
What Should You Expect From a Soft Landing?

Dr. Ken Mayland,
President

ClearView Economics, LLC
Welcome to the **REAL**
New Millennium!

Speaking of hangovers…

- Industrial production is in retreat
- Talk of the R-word
- Debate over whether the Fed went “too far”
- NASDAQ stocks have given back one-half of their TOTAL gains!
How Did We Get Here?

- A *Fed-engineered* slowdown

### Interest Rate Trends:
10 Year T-Bonds and Fed Funds

### Money Growth: MZM

Year-Over-Year % Change
How Did We Get Here (cont’d)?

- Normal cyclical forces

Business Inventories Vs. Business Sales Growth

12 Mo. % Ch.

- Inventories
- Bus. Sales
• Normal cyclical forces, inventories

A Recent History of Inventory Adjustments

<table>
<thead>
<tr>
<th>Starting:</th>
<th># of Quarters</th>
<th>GDP Subtraction ('96$)</th>
</tr>
</thead>
<tbody>
<tr>
<td>84:Q1</td>
<td>11</td>
<td>-$96 Bil.</td>
</tr>
<tr>
<td>89:Q1</td>
<td>9</td>
<td>-$71 Bil.</td>
</tr>
<tr>
<td>94:Q2</td>
<td>7</td>
<td>-$80 Bil.</td>
</tr>
<tr>
<td>98:Q1</td>
<td>5</td>
<td>-$104 Bil.</td>
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How Did We Get Here (cont’d)?
Key Issues: What to Expect Now (2001)?

- Duration
- Key aspects of economic behavior
  - Growth, sector differences
  - Inflation
  - Interest rates
  - Asset prices
- Signs of the coming reacceleration
Duration

- Avg. duration of post-WWII recessions: 11 months
- Avg. duration of soft landings: one to two years (e.g., 1995, mid-1984-86)
- Fed policy works with a year lag; will run its course in 2001
- Tax cuts coming???
Key Behaviors

- **Growth slowdown...**

GDP Growth Vs. the Prime Rate

- Don’t forget: we are already 2 quarters into the soft landing!
Key Behaviors, cont’d

**The consumer: turning conservative**

**Spending Vs. Income Growth**

What Is the “Right” Period of Change To Judge “Wealth Effect” Impacts?

<table>
<thead>
<tr>
<th>Equation R²</th>
<th>Period of Change, in Quarters</th>
<th>t-statistic on Wealth Variable</th>
</tr>
</thead>
<tbody>
<tr>
<td>.24</td>
<td>None</td>
<td>NA</td>
</tr>
<tr>
<td>.24</td>
<td>1</td>
<td>0</td>
</tr>
<tr>
<td>.29</td>
<td>2</td>
<td>2.7</td>
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<td>.32</td>
<td>3</td>
<td>3.5</td>
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<td>.31</td>
<td>4</td>
<td>3.5</td>
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<tr>
<td>.29</td>
<td>6</td>
<td>2.8</td>
</tr>
<tr>
<td>.28</td>
<td>8</td>
<td>2.3</td>
</tr>
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</table>
Key Behaviors, cont’d

- **Sector impacts**: for a 1.0% change of GDP growth (since 1989) ...
  - Manufacturing, 1.26%
  - Autos+ mfg., 1.45%
  - All durables mfg., 2.10%
- **Media bias**: disproportionate reporting on sectors that are disproportionately bearing the burden of the growth slowdown; *can be misleading!*
Key Behaviors, cont’d

- **Sector impacts**: construction, industrial bldgs.

Real Construction Spending: Industrial Buildings

Yr./Yr. % Ch.  |  Percent
--- | ---
75 | 70
80 | 75
85 | 80
90 | 85
95 | 90
00 | 95

- Indus. Bldg. (L)
- Cap. Utilization (R)
Key Behaviors, cont’d

- **Sector impacts:** construction, office bldgs.

Real Construction Spending:
Office Buildings

- Yr./Yr. % Ch.
- 75 80 85 90 95 00
- Office Bldg. (L)
- Jobs (HH Sur., R)
Key Behaviors, cont’d

- **Unemployment**: higher (by design!)
- **Inflation**: unwinding

Core Wholesale Inflation: Down at ALL Levels
Key Behaviors, Cont’d

• **Interest rates**: long rates, already down; short rates, coming down (stepping back from a restrictive monetary policy)
Key Behaviors, Cont’d

• Asset prices
  – Stock prices in general; profits vs. interest rates
  – When is the BEST time to buy stocks?

GDP Growth Vs. Stock Prices

% Ch. at Ann. Rate
Index

83:1 83:3 84:1 84:3 85:1 85:3

GDP (L)
S&P500 (EoP,R)
Key Behaviors, Cont’d

• **Asset prices**, cont’d
  – P/E expansion

![Graph showing Market Valuation (S&P500 P/E) Vs. Core Intermed. PPI Ratio (trailing 12 mo.) Y/Y % Ch.](image)
What About the **New President?**

- **Tax cuts!**
  - Marriage penalty
  - Estate taxes
  - Marginal tax rates
- Step-up of *defense* spending
- Less onerous business regulations
- **CONCLUSION:** these are “market and economy friendly” measures!
When Will the **Soft Landing** Be Done?

- Remember how Fed policy affects the economy!
- The inventory cycle will turn **positive**

![Business Inventories Vs. Business Sales Growth](chart.png)
When Will the **Soft Landing** Be Done?

- **Bottoming** of the Pur. Managers’ Survey
- **Bottoming** of factory job growth

GDP Growth vs. Mfg. Job Growth

- **Keep in touch with** *ClearView Economics*!

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*ClearView Economics*
Key Behaviors, Cont’d

• **Asset prices**, cont’d
  – Valuation

**Market Valuation (S&P500 P/E)**  
Vs. Inverted Bond Yield (1/T10)

Ratio (trailing 12 mo.)

Dec. based on 5.18% yield on 12/15/00
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