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The Federal Reserve board steps up by reducing rates

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With a little help from the Fed, try a 125- basis-point cut in 8 days, the recession, if and when it occurs, is expected to be a short one. Marginal job growth continues and relatively full employment persists. Nevertheless, economists have raised the probability of recession from 30% to 40% to 50% during 2008 in response to credit crunch, poor housing market and weakening job gains. Bi-partisan support for a stimulus package in the range of at least $150 billion is being expedited in Washington, and the Senate and the House and the White House are all fully engaged. The preparedness is definitely hopeful, and the resulting cautious optimism might be just enough to sustain fundamentals in the property markets.

The credit crunch has impacted commercial property markets. More restrictive and selective underwriting is combined with lower leverage and tougher terms, constricting the flow of refinancing and transactional capital. Most expect only marginal improvement in 2008 with increasing capital flows and declining rates following Fed activity. Respondents to The Federal Reserve's Beige Book for the First District of Boston dated January 16th expect activity levels to flatten or decline - less sales volume, less appreciation, lower rental increases, lower absorption, possible declining occupancy, declining prices/increasing cap rates. Participants are watching job growth and credit supply.

The already poor housing market is expected to get worse. National Association of Realtors (NAR) forecasts 2008 starts at 1.15 million, down from a 1.5 million pace in early 2007 and 1.2 million pace in late 2007. NAR forecasts gross domestic product (GDP) at 2.6% in first quarter with marginal increases each succeeding quarter in 2008, 2.6% in the second, 3.0% in the third, and 3.1% in the fourth. NAR expects home mortgage rates to hover around 6%, historically low. Foreclosures and subprime mortgage write-offs will continue. NAR speculates that some of the recent foreclosure volume is attributable to investors walking away and that volume may subside. Further, NAR speculates that it is possible that the actual subprime portfolio losses may be measurably lower than reserve levels taken when liquidity returns to that market. NAR concludes that it is a slowdown we can handle.

The Wall Street Journal released its January survey of economists on January 11th. The survey reported a 42% chance of recession in 2008, up from 38% in December and 23% six months ago. The survey forecast GDP growth for the first and second quarter 2008 below 2% and rising above 2% for the third and fourth quarters. Alan Greenspan estimated 50% probability of recession during 2008 in an interview abroad on January 30th. The economic data and resulting forecasts send mixed signals. Although the weakness is apparent, so is the marginal strength in both the regional and national economy. There appears to be enough economic activity and enough efforts to bolster what does exist to be cautiously optimistic. Most are cautiously optimistic about moderate growth or short and mild recession or visa versa.

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