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## **Burgeoning national debt: Does it matter to real estate? - by Daniel Calano**

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The total US national debt has just risen to almost \$27 trillion, up from \$23 million trillion just six months ago, and \$11 trillion a few years ago. The annual budget deficit is projected to reach \$3.3 trillion in 2020, largely brought on by government spending on the pandemic. Budget deficits are “simply” added to national debt each year. I use the word “simply,” because it sounds so easy, and that is the unfortunate fact.

This 2020 budget deficit is projected to reach 16% of GDP, the largest it has been since 1945. Assuming the pandemic impact will diminish in 2021, the deficit is projected to be down to 8.6% of GDP, and this level has only been exceeded twice since 1946. Scary, right? Time to panic? Bad impacts on real estate? Some say yes; some say no. It’s complicated but let’s try a deeper dive.

First, a review of the major factors impacting budget deficits. This year, the major culprits have been COVID, mandatory entitlement programs like Social Security, Medicare/Medicaid, military, and tax cuts. Tax cuts are different in that they mean less revenue, and thus greater deficits.

Some economists say that tax cuts boost the economy, and economic growth which produces greater revenues, thus balancing the tax revenue loss. However, the National Bureau of Economic Research found that, historically, less than 20% of lost revenue from tax cuts has been regained through economic growth. Other economists opine that how the debt is incurred/spent is the problem. They distinguish between productive and non-productive spending. They agree there can be a positive government spending multiplier, increasing growth, but only if the spending is “productive”. Productive spending can range from things like infrastructure construction to subsidizing housing. Actions like these produce jobs, facilitate travel and work, or just put money into consumer’s pockets.

How does it all relate to real estate? How hurtful is our constantly increasing debt? The Counselors of Real Estate have determined that public and private debt is #4 on the 2020-21 top ten issues

affecting the real estate world. Articles by Counselors cite the potential increase in interest rates as being a major concern. Although the Federal Reserve has committed to low rates for the next few years, that comes at a cost. In order to pay for these current benefits, they have to “print money” through various actions, increasing supply, and thus devaluing the dollar, potentially creating inflation in the process. Real estate can cost more to finance, and tenants pay higher rents with devalued dollars. Credit ratings can slip both in government as well as consumers, thus reducing borrowing capacity.

Most writers concur that budget deficit and national debt are not immediate crisis. Productive spending can certainly have positive ripple effects through the economy. It can potentially increase economic growth and help put money in the pockets of businesses and families who can then further grow the economy. All that said, most also agree that there is a tipping point where too much debt becomes onerous, and thus hurtful to economic growth. Should inflation occur, higher costs in real estate may well limit demand. Some of us remember well, when residential mortgages were 15%, it was not easy to buy a house.

These thoughts are only scratching the surface of a very complicated issue. My take-away is that I wouldn't change directions because of anticipated problems of growing debt. On the other hand, it seems clear there will be a future point when we will have to pay for our heretofore “free lunch.”

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