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# A message to appraisers: Should we be mad about the state of the economy? Part 1

September 11, 2008 - Appraisal & Consulting

With events proceeding out of the shambles that constitutes the housing market, the words of the out of control newscaster, Howard Beele, in "Network" come to mind. As you may recall, he yelled "I'm mad as hell and I'm not going to take it anymore" and convinced others to do so. The c.1977 film with a cast including Faye Dunaway, William Holden, Peter Finch, and Ned Beatty, won 4 Oscars. In its way, it summed up the great dissatisfaction felt with government during those economic times of stagflation, high energy costs, and low economic growth. It can be argued that, in many ways, that time resembles today's conditions.

Consider our current mess and how we got there. Here is the very short, simplistic scenario.
The economy was in dire straits in the early part of the decade. The stock market bubble had burst and many fortunes are lost, consumer demand and travel are down, economic activity has slowed.

During this time, inflation is not a major issue. To stimulate the economy, interest rates are lowered and lowered again to historically low levels. All the cleverness and sophistication that was brought to bear in the then recently concluded tech bust is now brought into play with real estate. In a low interest rate environment, residential real estate, the last frontier, the secure long term investment, the foundation of wealth for individuals, comes into the rangefinders of Wall Street. Existing securitization methods, an essential part of providing liquidity to housing markets, began to reach new levels of volume and sophistication.
With rates low, activity kicked up both in terms of home financing and related activity, i.e., the "multiplier" effect that housing activity engenders such as the purchase of non-durable goods and services. The gods smiled and found this to be good, "stimulative", if you will.
Propped up by the free flow of credit, buyers bought freely, homeowners refinanced, developers developed, and builders built. Housing prices and volume exploded.  In the states, in many parts of the world, all was well, economic growth took place. The stock market improved, bank stock prices swelled.
In an effort to keep pace with the promise of the "ownership society," lenders found ever more clever ways to lend money to those who needed it most and could least afford the debt. The whole notion of clever credit solutions, i.e., ways to disguise lack of ability to repay, lack of equity or downpayments, swept the markets, from borrower, originator, lender, and investors. The financial community was enthralled with "sub prime" lending and its yield prospects. If there were concerns about  borrower creditworthiness, the strength of the underlying (and appreciating) collateral (real estate) would more than offset any credit glitches.
Packages of this debt got sold off in various permutations to buyers worldwide. In a low interest rate

environment, investors eagerly bought up high yielding debt instruments vetted by the ratings agencies - those objective, impartial, and independent bastions of the financial world, and by venerable investment banks and brokerage houses.

Risk seemed a secondary issue, an old school concept. Housing prices were rising everywhere. Demand was insatiable. Any problems in these packages of debt would be counterbalanced by further asset appreciation and the competency of market makers.

The perception existed that the whole system was self-correcting. Having gone through the real estate depression of the 1990s and the stock market bubble early in the first decade of the millennium, a couple different lines of thinking prevailed. A common line of thought was that, "while things are a bit out of control here, this is a short term problem, we've been there before and, after all, there are controls in place to prevent a recurrence of the last real estate problem. That can't happen again, we've learned too much." The other line of thinking was, "let's go for it, here's the time to make some serious money. Either we'll be on to the next Big Thing or we'll clean this up once the party is over." (The notion of "irrational exuberance" had already been floated during the late 1990s but somehow didn't appear to apply).

As events unfolded, the first line of thinking was that of fools in paradise. The second was nothing more than that of greed and avarice, expected and common behavior given the times.

The resulting snow blindness from both positions created the mess we are in. It appears that the cleanup (and the consequences from it) will exceed the length of time of the actual party.

Part two will appear in the October 10th edition of the New England Real Estate Journal in the Appraisal and Consulting section.

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