December 2015 Housing Commentary

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Return TOC

Table of Contents

This report is a free monthly service of Virginia Tech. Past issues can be found at: http://woodproducts.sbio.vt.edu/housing-report/

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December 2015
Housing Scorecard

	M/M	Y/Y
Housing Starts	▽ 2.5%	△ 6.4%
Single-Family Starts	▽ 3.3%	△ 6.1%
Housing Permits	▽ 3.9%	△ 14.4%
Housing Completions	△ 5.6%	△ 7.9%
New Single-Family House Sales	△ 10.8%	△ 9.9%
Existing House Sales (NAR®)	△ 14.7%	▽ 7.7%
Private Residential Construction Spending	△ 0.9%	△ 8.1%
Single-Family Construction Spending	△ 1.0%	△ 8.7%

M/M = month-over-month; Y/Y = year-over-year

Source: U.S. Department of Commerce-Construction ; National Association of Realtors® (NAR®)

Return TOC

Housing Data

	December	November	Dec. 2014
Total permits*	1,232,000	1,282,000	1,077,000
Single-family permits	740,000	727,000	685,000
Multi-family 2-4 unit permits	37,000	29,000	24,000
Multi-family ≥ 5 unit permits	455,000	526,000	368,000
Total starts	1,149,000	1,179,000	1,080,000
Single-family starts	768,000	794,000	724,000
Multi-family 2-4 unit starts**	16,000	7,000	20,000
Multi-family ≥ 5 unit starts	365,000	378,000	336,000
Total completions	1,013,000	959,000	939,000
Single-family completions	696,000	640,000	665,000
Multi-family 2-4 unit completions**	10,000	13,000	6,000
Multi-family ≥ 5 unit completions	307,000	306,000	268,000

* All data are presented at a seasonally adjusted annual rate (SAAR).

** US DOC does not report 2-4 multi-family starts and completions directly, this is an estimation.

Source: U.S. Department of Commerce-Construction: www.census.gov/construction/nrc/pdf/newresconst.pdf; 01/20/16

Return TOC

Housing Data

	December	November	Dec. 2014
New single-family sales	544,000	491,000	495,000
Median price	$288,900	$297,000	$302,800
Existing sales [a]	5,460,000	4,760,000	5,069,638
Median price	$224,100	$220,300	$208,200
Private Residential Construction	$429.6 billion	$425.8 billion	$397.4 billion
SF construction	$231.3 billion	$229.0 billion	$212.8 billion
MF construction	$52.8 billion	$51.4 billion	$47.2 billion
Improvement construction [b]	$145.5 billion	$145.4 billion	$137.4 billion

[a] NAR®

[b] The US DOC does not report improvements directly, this is an estimation. All data is SAAR and is reported in nominal US$.

Sources:

NAR® www.realtor.org/topics/existing-home-sales; 01/22/16
U.S. Department of Commerce-Construction: www.census.gov/construction/nrs/pdf/newressales.pdf; 01/27/16
U.S. Department of Commerce-C30 Construction: www.census.gov/construction/c30/pdf/privsa.pdf; 02/01/16

Return TOC

Conclusions

December's housing data is a mixed bag – total starts down by 2.5% (m/m), single family homes down by 3.3%, and permits down by 3.9%. However, completions were up by 5.6% (m/m) and existing home sales were up by 14.7% from November's data. First time buyers still at 32%, well below the more typical 40% and household formation remains below trend as well. Multi family housing still strong with 34% of total and rents still increasing, thereby further strengthening the importance of multi family construction.

With the real unemployment rate in the U.S. at 10.3% (16 million individuals unemployed, stopped locking, or work part-time) and household income growth nonexistent or negative, it's hard to envision a scenario where the U.S. housing market returns to "normal" anytime soon. A strengthening Dollar and slowing economies in China, Europe, and many other countries around the globe, numerous negative macro-factors endangering a robust housing recovery exist:

1) A constrained quantity of well-paying jobs being created;
2) a tepid economy;
3) declining real median annual household incomes;
4) strict home loan lending standards – though loosening with new programs; and
5) slowing world economy; and
6) global uncertainty

Return TOC

November 2015
EU Housing Scorecard

		M/M	Y/Y
Production in Construction[A]	EU 28	△ 0.7%[s]	△ 2.1%[s]
	EU 18	△ 0.8%[s]	△ 1.9%[s]
	Germany	△ 1.8%	△ 2.2%
	France	△ 0.2%	▽ 0.9%
	UK	0.0%[p]	△ 0.1%[p]
	Spain	▽ 1.3%[ps]	▽ 1.2%[p]
Building permits (m^2 floor)[A]	EU 28	-.-	-.-
	EU 18	▽ 4.3%[(10)]	△ 14.5[s(10)]
	Germany	▽ 2.8%[s]	△ 8.6%
	France	▽ 1.2%[s]	△ 23.8%[e]
	UK	-.-	-.-
	Spain	▽ 11.6[s(10)]	△ 73.3[e(10)]

M/M = month-over-month; Y/Y = year-over-year

Source: Eurostat (http://ec.europa.eu/eurostat/web/short-term-business-statistics/data/main-tables; 02/03/16)
[A] see http://ec.europa.eu/eurostat/web/short-term-business-statistics/overview/sts-in-brief
[e] estimate [s] Eurostat estimate [p] provisional -.- no data available [(10)] October data

Return TOC

Housing comments – December 2015 data

- *December totals were down 2.5% (to 1.149 million, annual rate) - SF at 768,000, down 3.3% (SAAR) – MF still 34% of total*
- Multi family still the driver – rental prices still increasing – single family sales remain relatively low and this has big impact on wood product prices.
- Economic issues - slowing world economy (China GDP slowest in past 8 years). China slowdown plus currency devaluation will drive commodity prices lower, and rekindle deflation concerns around the world.
- *Increasing geopolitical risk and continued domestic/Washington gridlock* - causes uncertainty which leads to less investment which leads to slower productivity growth, and ultimately to slower GDP growth and lower standard of living!
- Job market is improving, albeit slowly, and wage gains remain weak. The real unemployment rate remains high at 10.3%. This equates to about 16 million people who are either unemployed, stopped looking, or are working part time because they can't find full time jobs. This "slack" in the job market will keep wage gains modest for some time.
- *Income growth in U.S. remains pathetic – latest Census report shows real incomes fell again in 2014. This suggests to me that housing will remain sub par for some time – many 1st time buyers just can't enter the market.*
- World GDP growth outlook is shaky at best – main problem today is the slowdown in China which has been the major economic engine over the past 8 years. European growth is expected to be relatively weak while back here in USA, growth will probably remain below par (~ 2%) for some time.

Return TOC

The Fed raised interest rates – finally - in December. And, they said further increases will probably be gradual in 2016 and beyond. However, with current problems with falling oil prices and world stock markets, I expect the FED will delay any further rate hikes for several months at least. Plus, there is no sign of inflation, anywhere, except equity markets.

Here are some thoughts:
The dollar will continue to strengthen, and commodity prices will fall further as most are priced in US$. World demand is relatively weak with problems in China expected to worsen. Europe remains weak, and the commodity currency countries (e.g., Canada, Australia, ..) will face even more economic headwinds. As far as housing goes, modestly higher rates should not hurt housing too much. As we have discussed many times before, income and job growth is the key to any substantial housing recovery. On that score, income growth is non existent (real $) for past 25 years, and the job market still has problems. 30% of jobs created in past 8 years have been part time with few if any benefits. Furthermore, credit remains tough for many potential 1st time buyers. Big problem today is lack of confidence by our business leaders – e.g., spending on stock buybacks has increased 200% since 2009 - i.e., <u>they are not investing for the future!</u>

Return TOC

The global economy is losing steam (WSJ Jan 20, J. Hilsenrath) – monetary policy in USA, Europe, … has "reached its limits." Debt is out of control here in USA and elsewhere. We've had credit driven growth (via central banks) for the past 6 - 7 years with questionable success. Now, we have huge debts that will eventually have to be paid off.

Long term issues like aging populations and slower productivity growth mean weak GDP growth and lower standard of living in many parts of the world. Solutions include tax reform, infrastructure investment, R&D, ..
We desperately need innovation and more risk taking to create products and services desired by the marketplace.

This won't happen without strong leadership –
which is lacking in the USA, Europe, and elsewhere.

It is going to be tough for housing to improve much in today's economic environment! That means wood product prices will remain subdued.

Return TOC

A few comments re: recent terrorism

The current administration has misjudged ISIS/ISIL/whatever, from the beginning. If this is the "JV team", I would hate to see the "Varsity team"! Latest attacks in Paris, Africa, California, Pakistan, …… clearly demonstrate that the world's response is not working. They are not being "contained" as the current administration suggests. Whether we like it or not, the world needs a "world policeman" and the only country capable of filling that role is USA.

I'm tired of war as are most Americans, but now is not the time to become an isolationist. If we continue down that path, terrorism will only increase.

We need leadership today more than ever. A strong leader gives people confidence in the future – we don't have that today in America (and other parts of the world for that matter). Confidence is a must if we are going to invest in our future – without confidence, we drift as a country and as a people.

What has this got to do with housing you ask? If we continue the current course, world economic growth will continue to weaken, U.S. growth will barely reach 2%, and U.S. housing will remain below trend. And, wood prices will continue to languish.

Return TOC

Main problem with U.S. economy (and world) is weak demand and low interest rates are not the answer – see next slide for more analysis

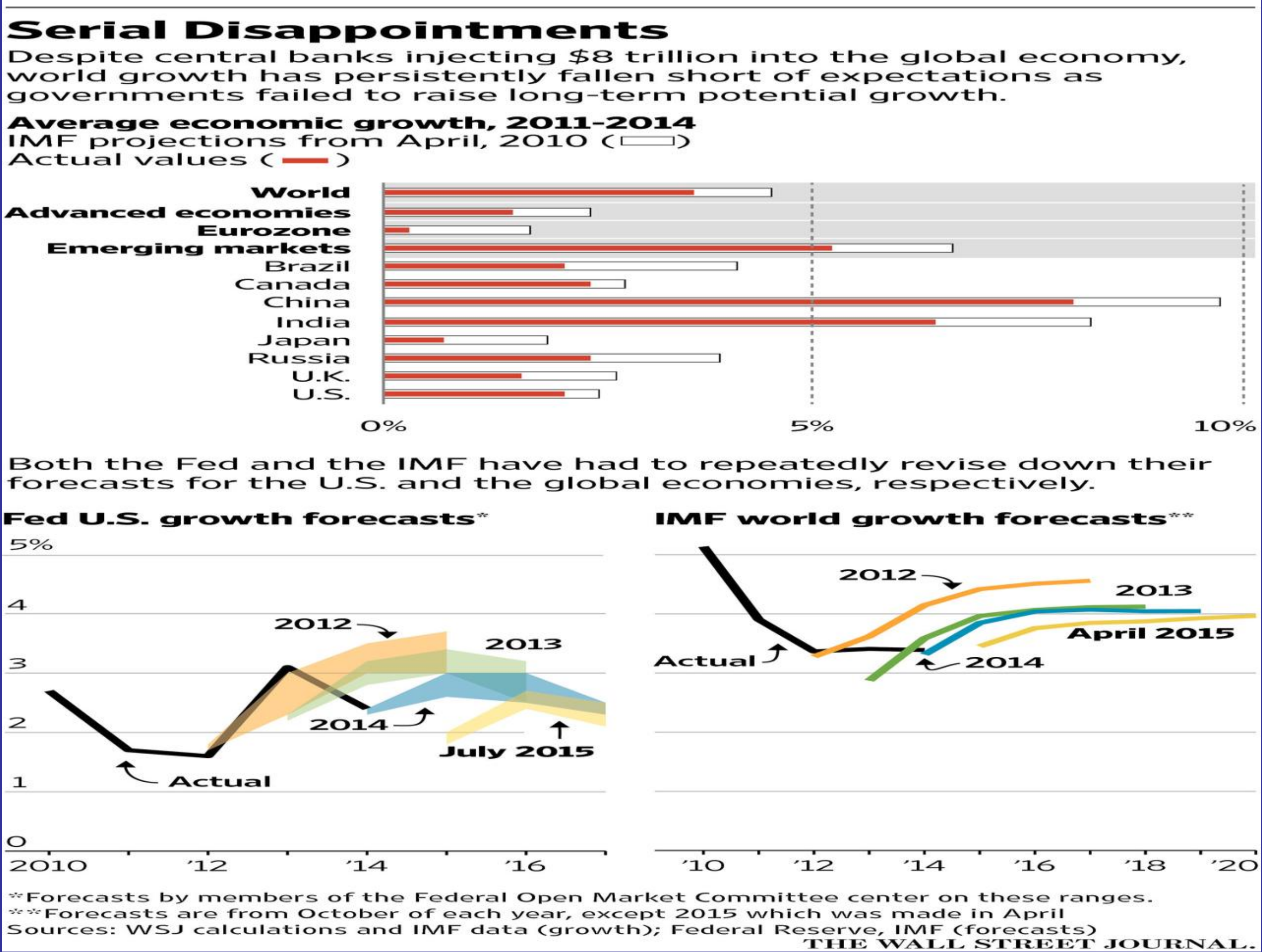
Fed doesn't know what to do – and the current crop of politicians is disappointing – hopefully, someone will emerge from the political debates with credible ideas and the ability to communicate a strategy for addressing the serious problems facing our country. Otherwise, we're in for extended period of weak economic growth, and that means weak housing, job creation, lower standard of living, and sad sack wood prices.

Productivity is a problem for U.S. economy – and jobs miss match is one reason for low productivity - there are jobs out there, but many people lack the necessary skill set. Solution - - education and infrastructure investment. Difficult to solve these problems due to student debt issues and government debt approaching 18 trillion $. Many analysts expect U.S. economy to remain weak with GDP averaging about 2% over next several years.

Return TOC

“Cheap money alone can’t fix the world’s economy” – India’s Central Bank Governor – “economies need to be more innovative, productive, and competitive.”

My opinion – gutsy leadership missing here in USA, Europe, Canada, and rest of Developed world! Current polls in US and elsewhere indicate many voters are disgusted with current crop of politicians, and for good reason.



Source: WSJ (http://www.wsj.com/articles/central-banks-lesson-easy-money-alone-isnt-a-growth-salve-1442505860?cb=logged0.39475020127295923)

Future world GDP growth – studies in wsj and elsewhere suggest that demographic shifts will slow growth – main reason is slower population growth rates in many parts of the world – USA; Europe; Russia; China; ….

Bottom line – slower world demand growth and this can't be fixed very easily unless we get more creative with immigration reform. That will be difficult with increasing Terrorism concerns.

And, we need to get more creative with "supply side" issues. E.g., innovation and investment to create new products – this requires tax reform, less regulation, less government, …….

See Greg Ip, WSJ "demographic destiny" WSJ 2050 (http://www.wsj.com/articles/how-demographics-rule-the-global-economy-1448203724?mod=ST1)

Return TOC

Rental demand versus single family housing ---

Rental demand may continue to increase for some time – a recent study by the Urban Institute suggests it may continue for another decade or two

(http://www.wsj.com/articles/new-housing-crisis-looms-as-fewer-renters-can-afford-to-own-1433698639)

Why - - demographics; growing minority population; student debt; weak income growth; …. E.g., minorities (nonwhite) will make up 75% of net household growth over the next 10 years, and 85% during 2020- 2030 (see next slide). They are less likely to own homes (lower incomes is main reason), so home ownership continues to fall toward 60% by 2030. During this time, rental demand will increase dramatically. Although this is just one study, it provides food for thought. One potential question with the study, however, is that other studies show that although immigrants, for example, rent initially, but, over time they purchase homes at a rate equal to or higher than native born Americans. Why? People come to the U.S. to improve quality of life, and for most, this means homeownership. This suggests that the U.S. has to find solutions to immigration issues like "Illegal immigrants" while encouraging legal immigration. This country was founded by immigrants seeking a better life, and they are key to our future. And, incomes for all Minorities has to improve if home ownership is to return to "good old days"

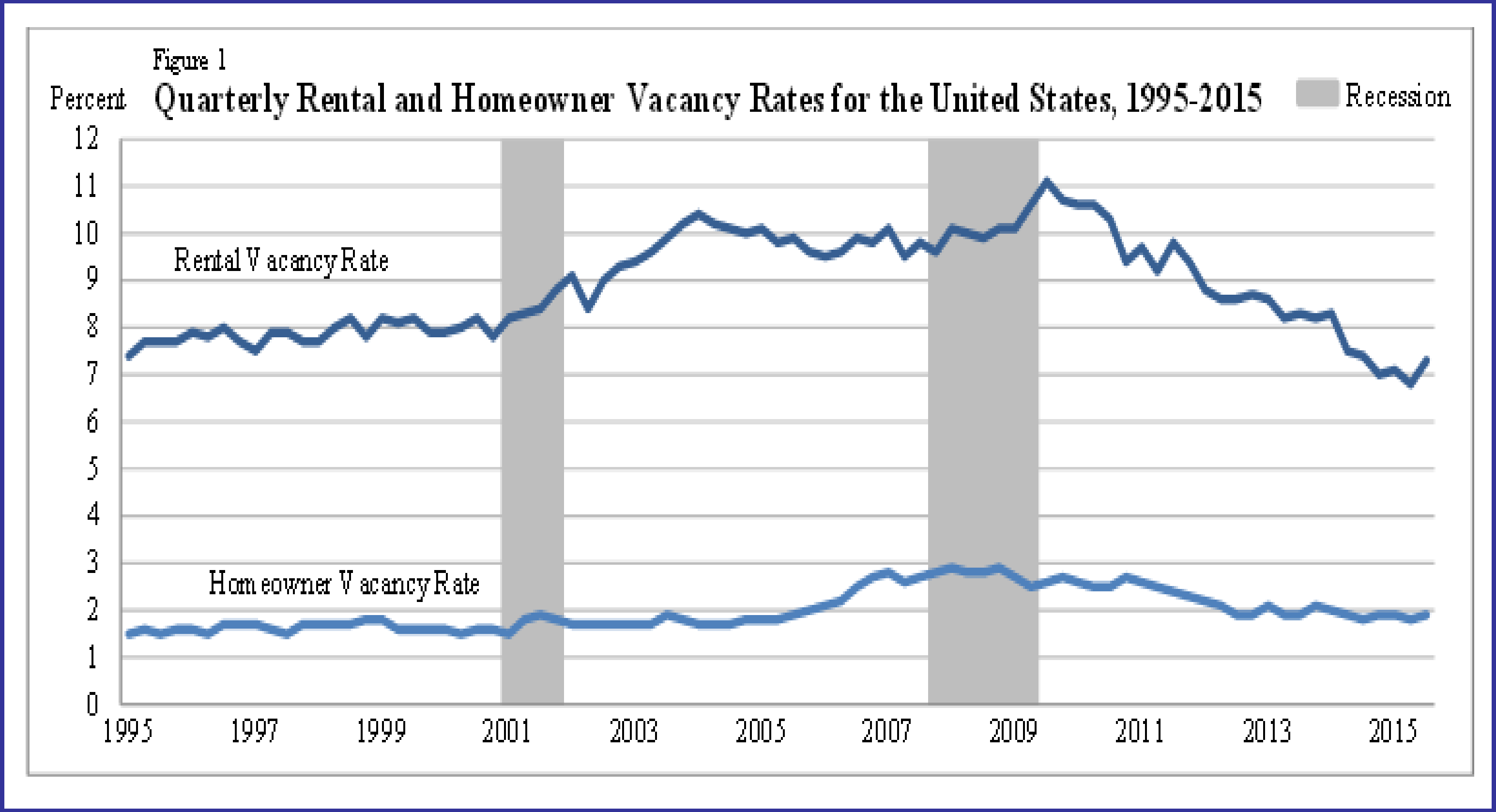
(http://www.engineeredwood.org/Data/sites/3/documents/EngWoodJournal/EWJ_Spring2010.pdf)

Anyway, this has potential implications for home ownership; single family construction; and demand for wood products – lots of variables and scenarios.

Return TOC

Rental vacancy rates lowest in 20 years

Falling rental vacancy rates will drive rental prices higher
and this will drive multi family construction – Economics 101

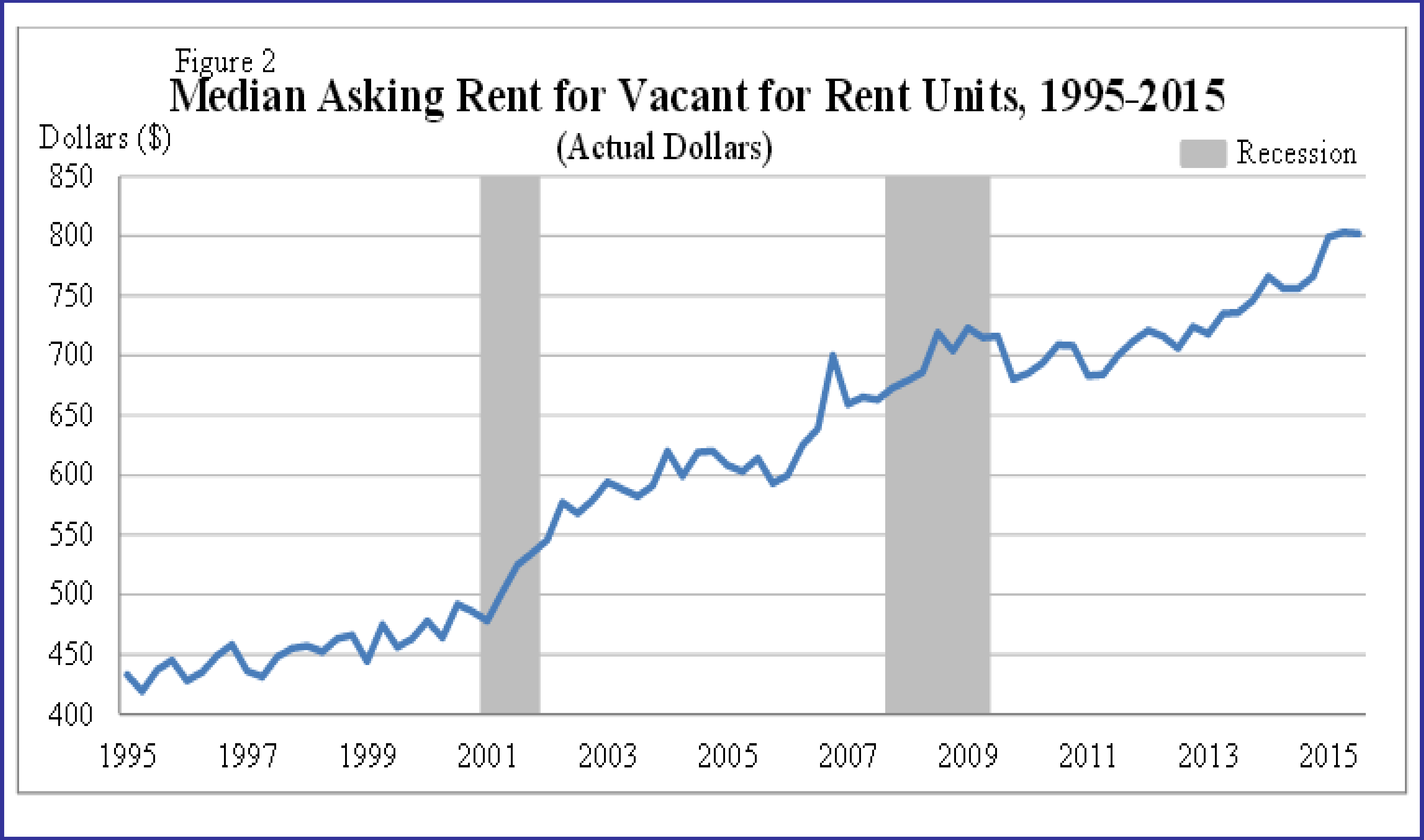


Source; Census (http://www.census.gov/housing/hvs/files/qtr215/currenthvspress.pdf)

Return TOC

Increasing rents will slow housing starts - -

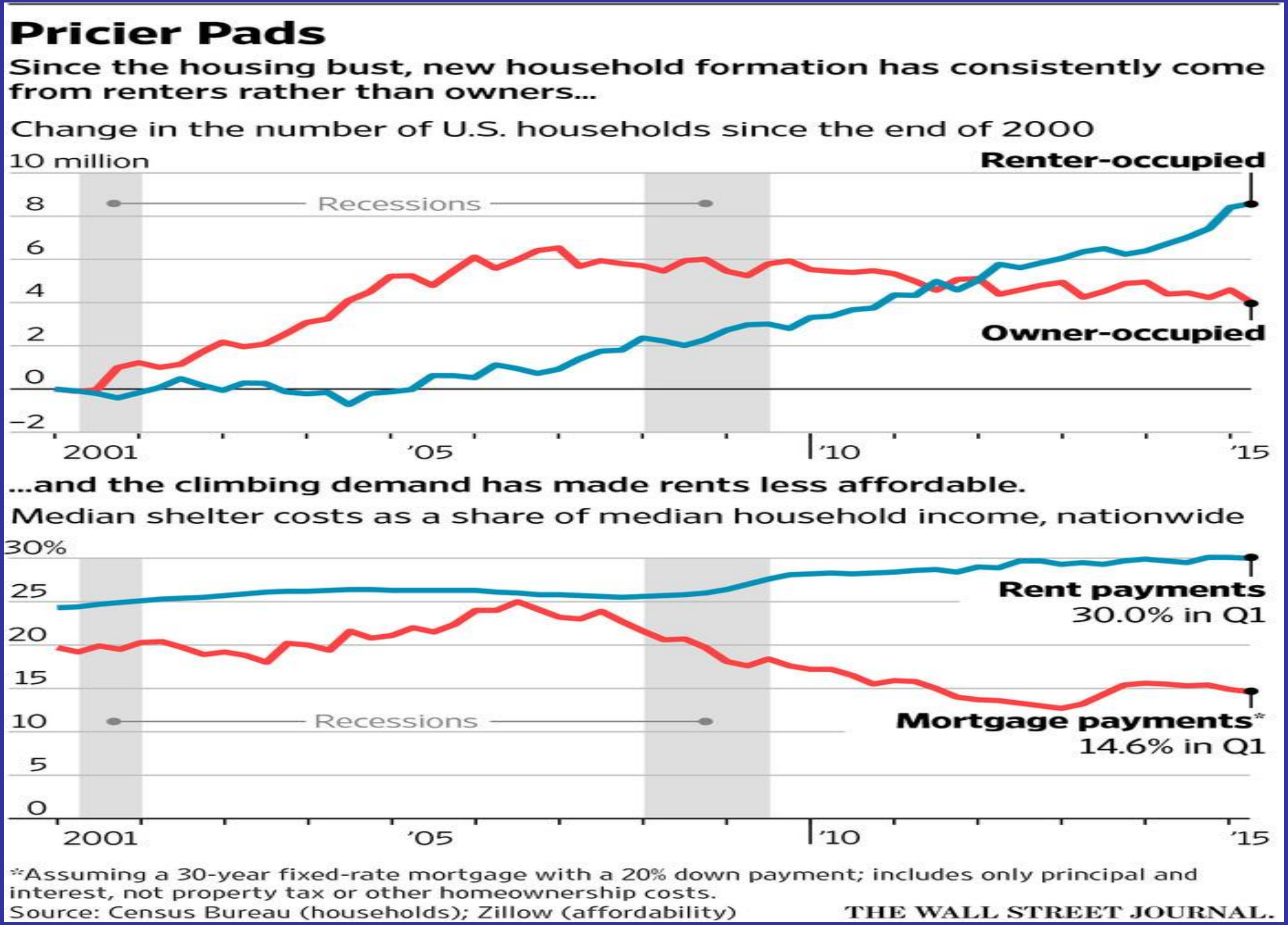
makes it more difficult for renters to save for down payment for house purchase



Source: Census : (http://www.census.gov/housing/hvs/files/qtr115/currenthvspress.pdf)

Return TOC

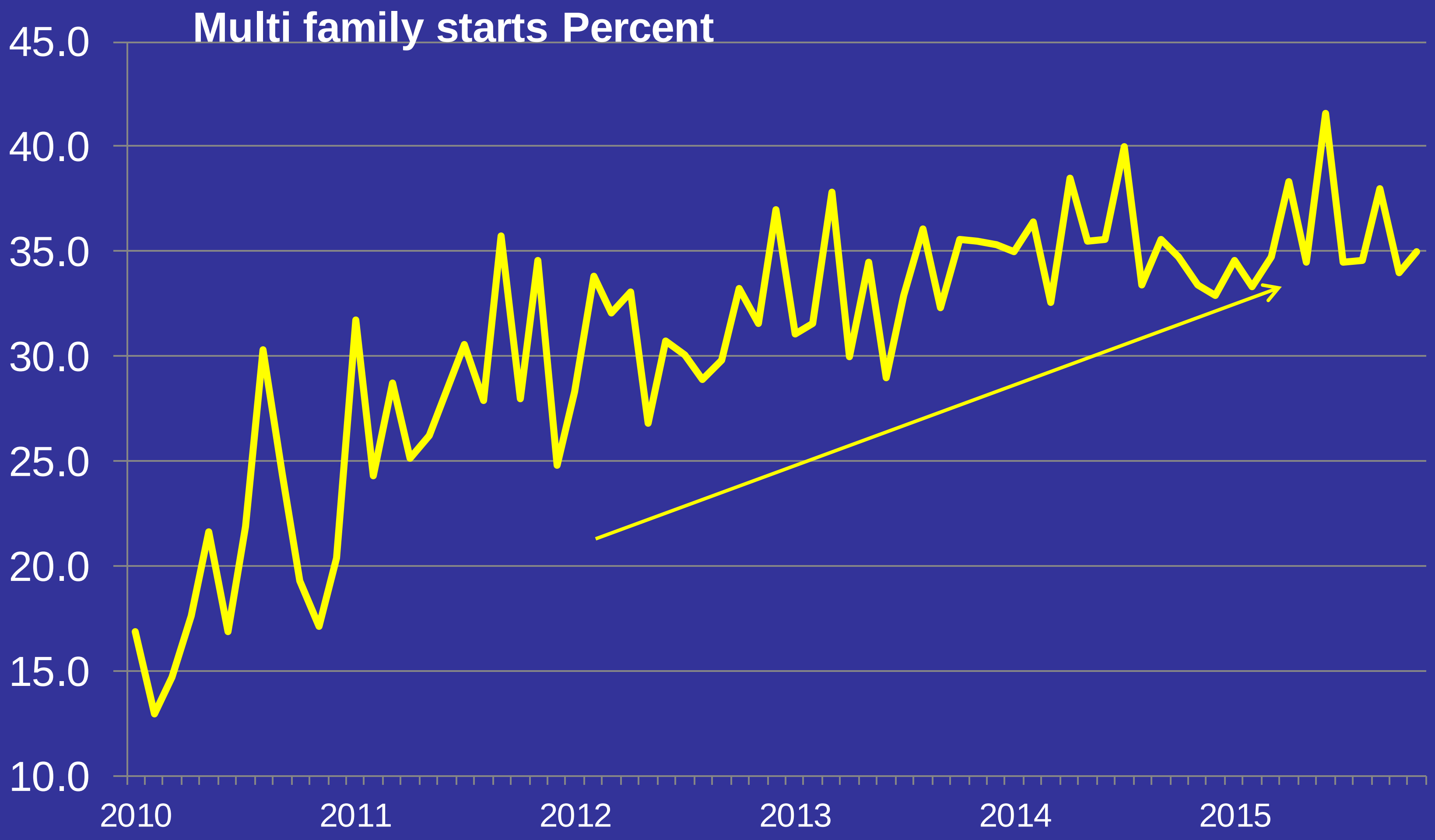
Household formations are up, but most are renting, and, in the past decade, rent payments exceeded mortgage payments – but, most can't get a mortgage due to poor credit or can't save enough for a down payment – vicious circle



Source: WSJ (http://www.wsj.com/articles/rising-rents-outpace-wages-in-wide-swaths-of-the-u-s-1438117026?cb=logged0.40234478570971755)

Return TOC

Multi family share of housing starts – upward trend expected to continue for some time. Also, since the housing crash in 2008, single family rentals have now reached 13% of overall housing stock, up from 9% in 2005 (http://blogs.wsj.com/economics/2015/07/20/signs-of-overheating-in-the-single-family-rental-market/)



Source: Census

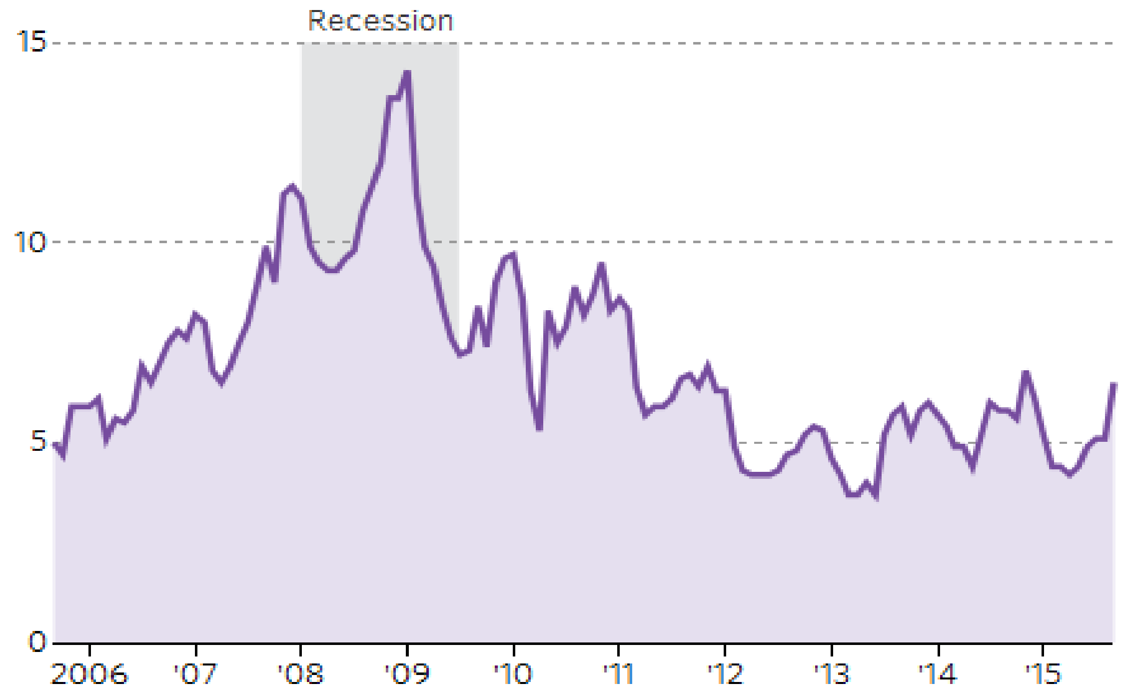
Return TOC

Low new home inventory drives prices higher and out of reach to most 1st time buyers

Months' supply

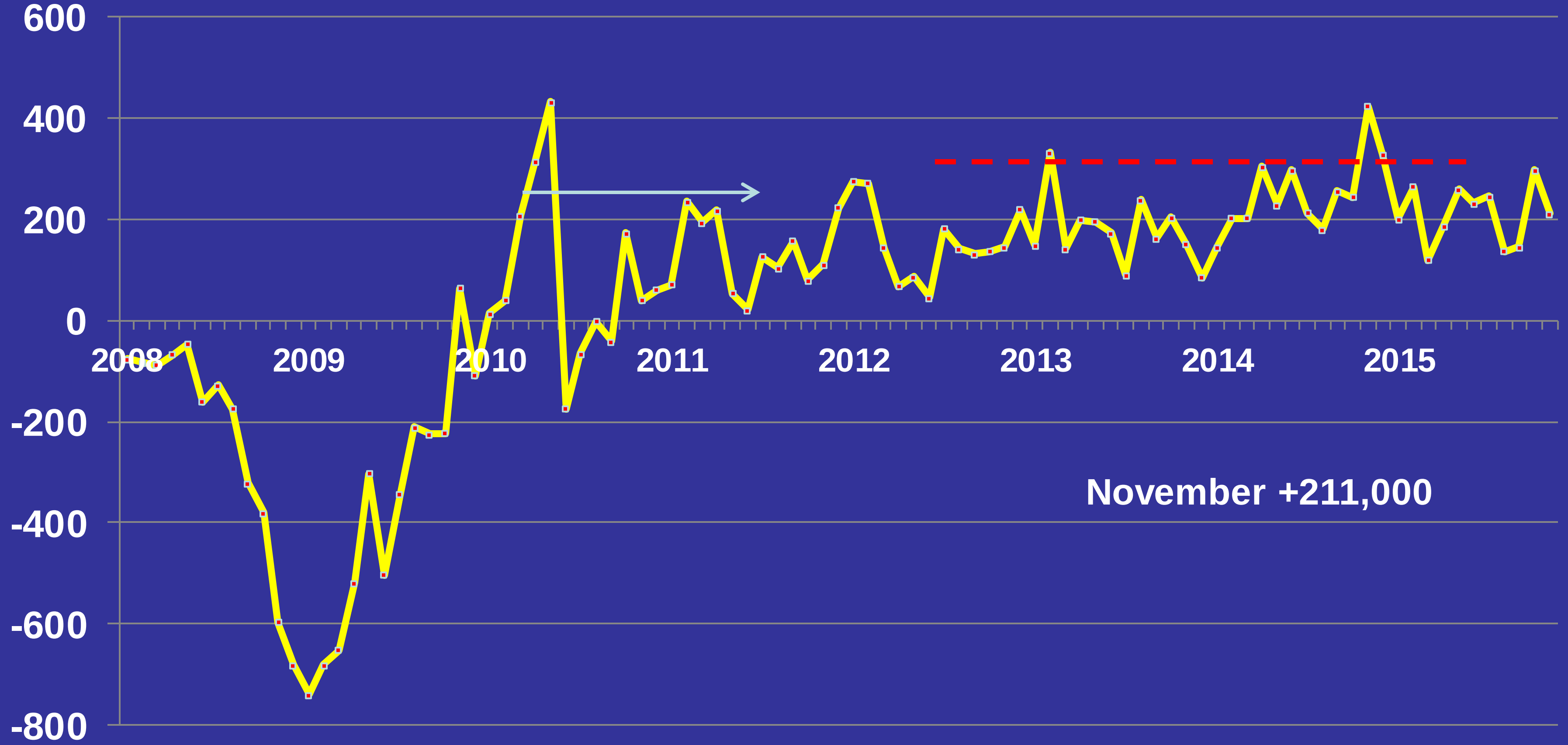
The amount of time it would take, in months, to sell the stock of newly-built homes available for sale at the current sales pace. The National Association of Realtors considers a six-month supply to be a balanced market.

Months' supply of newly-built homes for the past 10 years



Employment situation - our biggest problem – stuck near 200,000, and many of these jobs are part time with little or no benefits – not conducive to driving housing demand higher

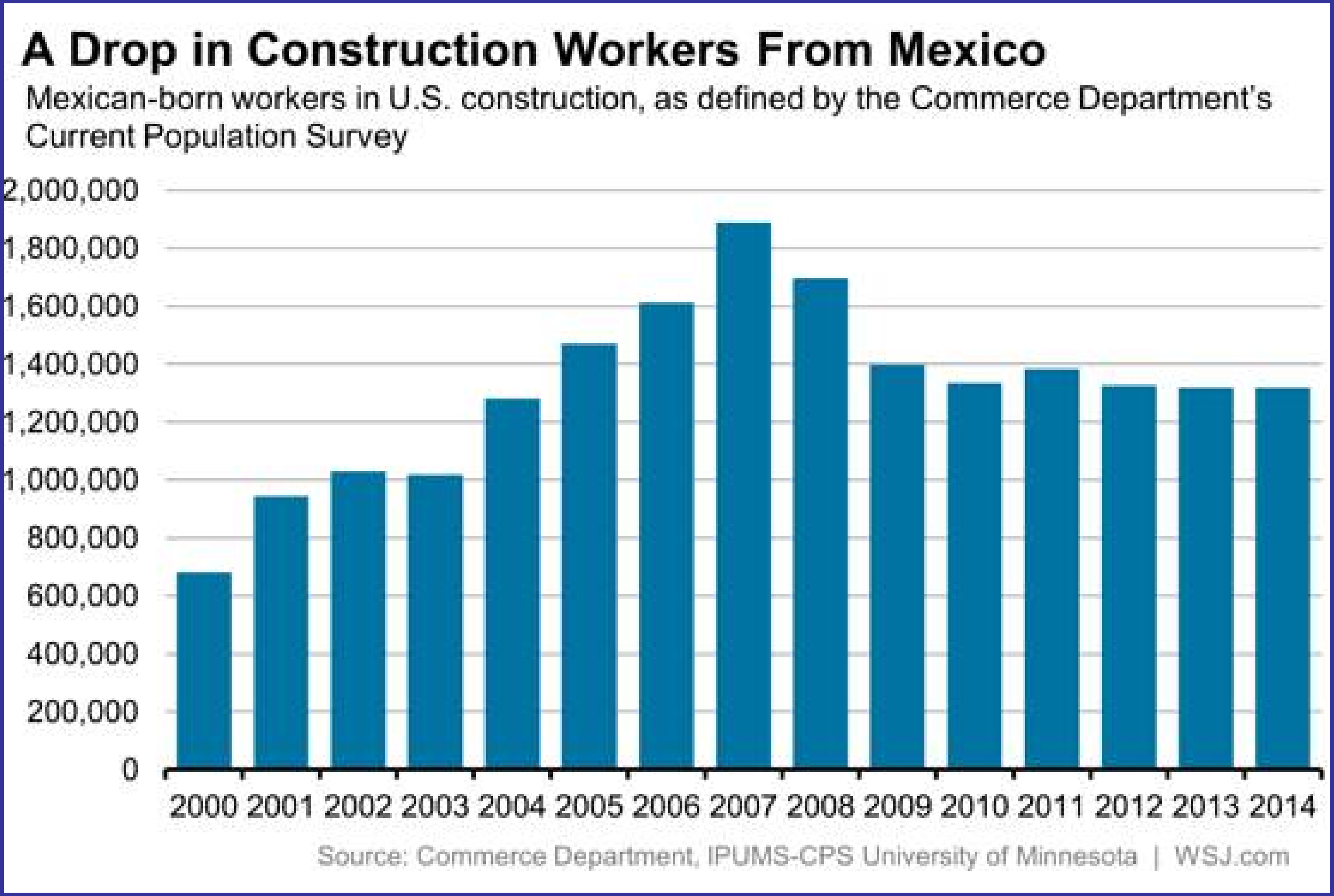
Net change in non farm payrolls – monthly, thousands



Source: U.S. BLS (www.bls.gov)

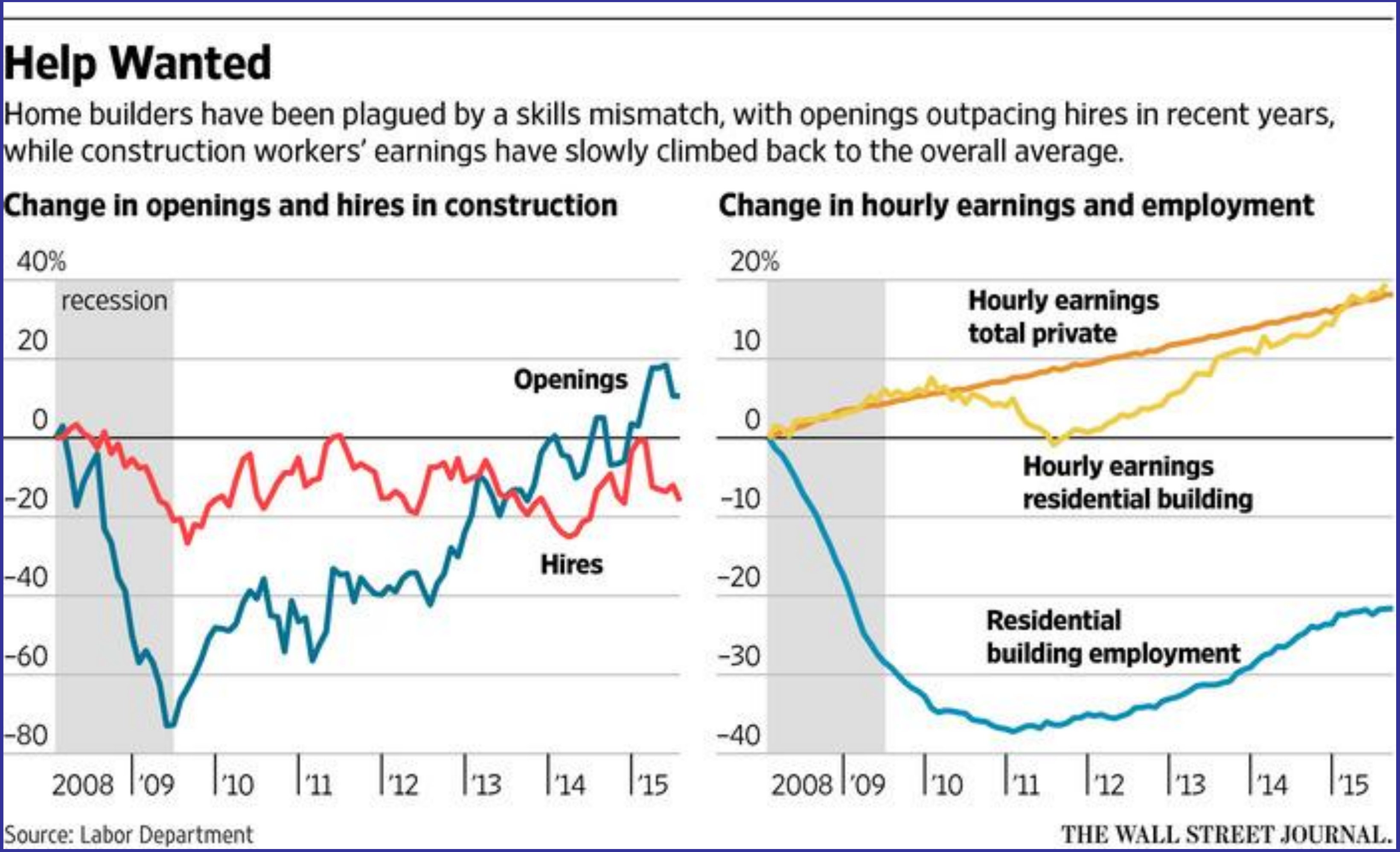
Return TOC

Another problem (like we need more) for housing is labor shortages - - -
Fewer immigrants from Mexico, plus aging demographics with native born Americans suggest that construction costs will increase driving prices higher And slowing home construction



Source: WSJ (http://blogs.wsj.com/economics/2015/09/21/how-immigration-has-contributed-to-the-construction-worker-shortage/)

Nearly 700,000 fewer construction workers today compared with 2007 – will mean construction delays and higher costs

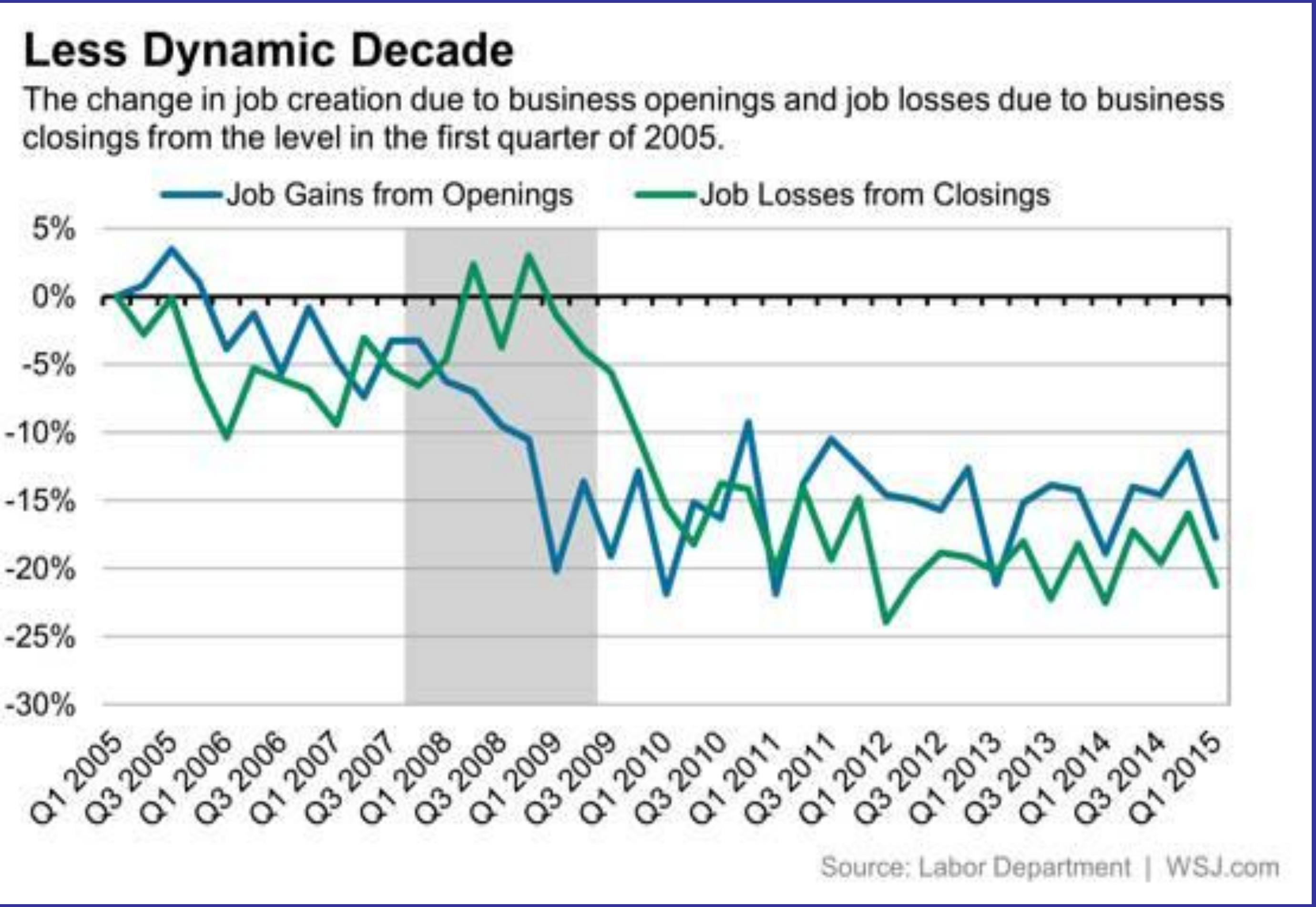


Source: (http://www.wsj.com/articles/labor-shortage-pinches-home-builders-1444688976?cb=logged0.39370374416477216)

Return TOC

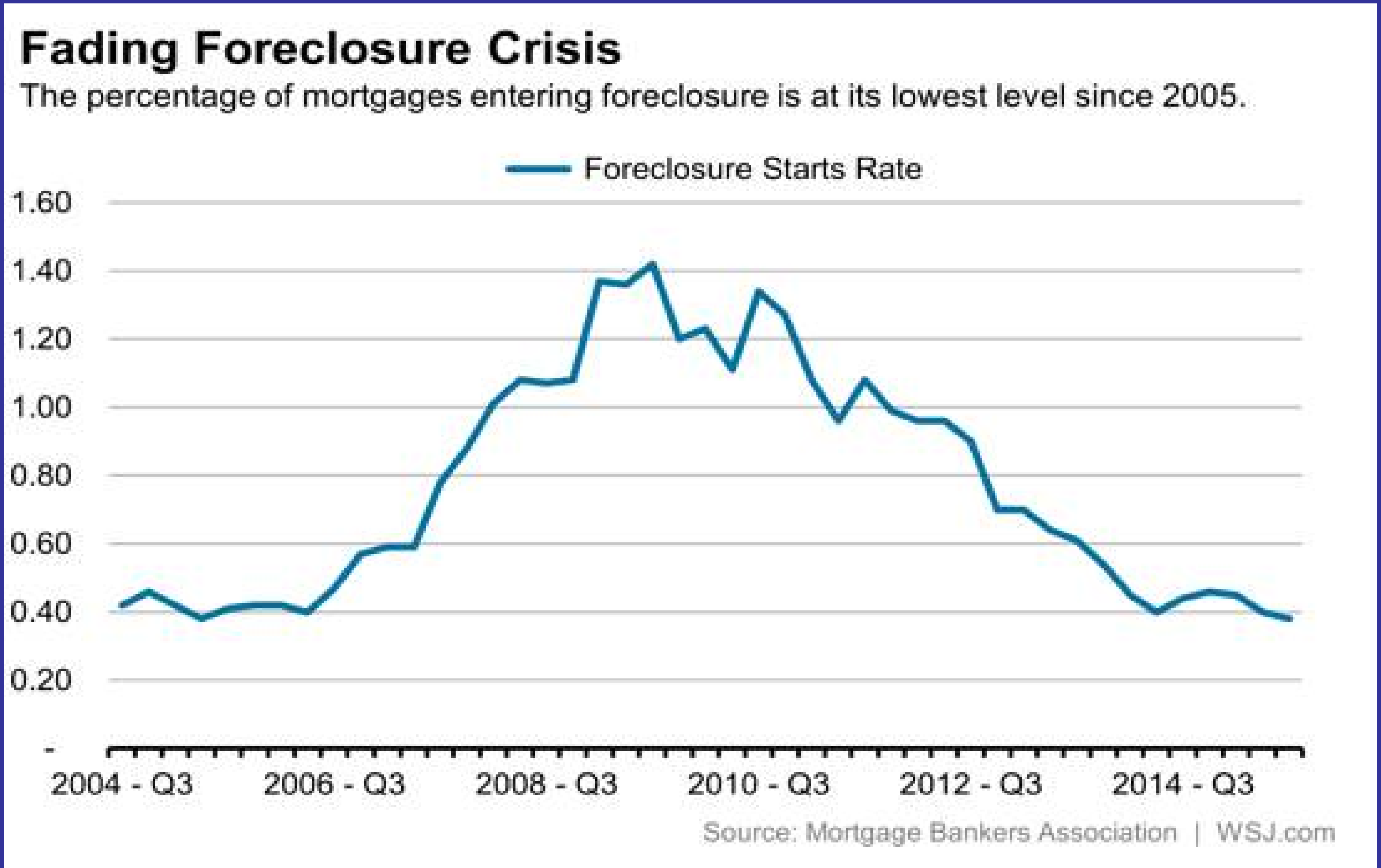
Another reason why job picture not so good – job creation by businesses is down significantly in past 7 – 8 years. Less innovation and risk taking is part of problem. My opinion – this is due to uncertainty and lack of confidence in the future direction of the country/economy.

Again – lack of leadership from White House and Congress



Return TOC

Some good news re: housing – lower foreclosures will support healthier pricing as more distressed homes are kept off the market - also helps existing mortgage holders refinance into better rates, and underwater mortgages are down (13.4% today vs 16.9% a year ago)
(http://www.wsj.com/article_email/more-homeowners-rise-from-underwater-1449196595-lMyQjAxMTI1NDA1NDQwMzQ1Wj)



Return TOC

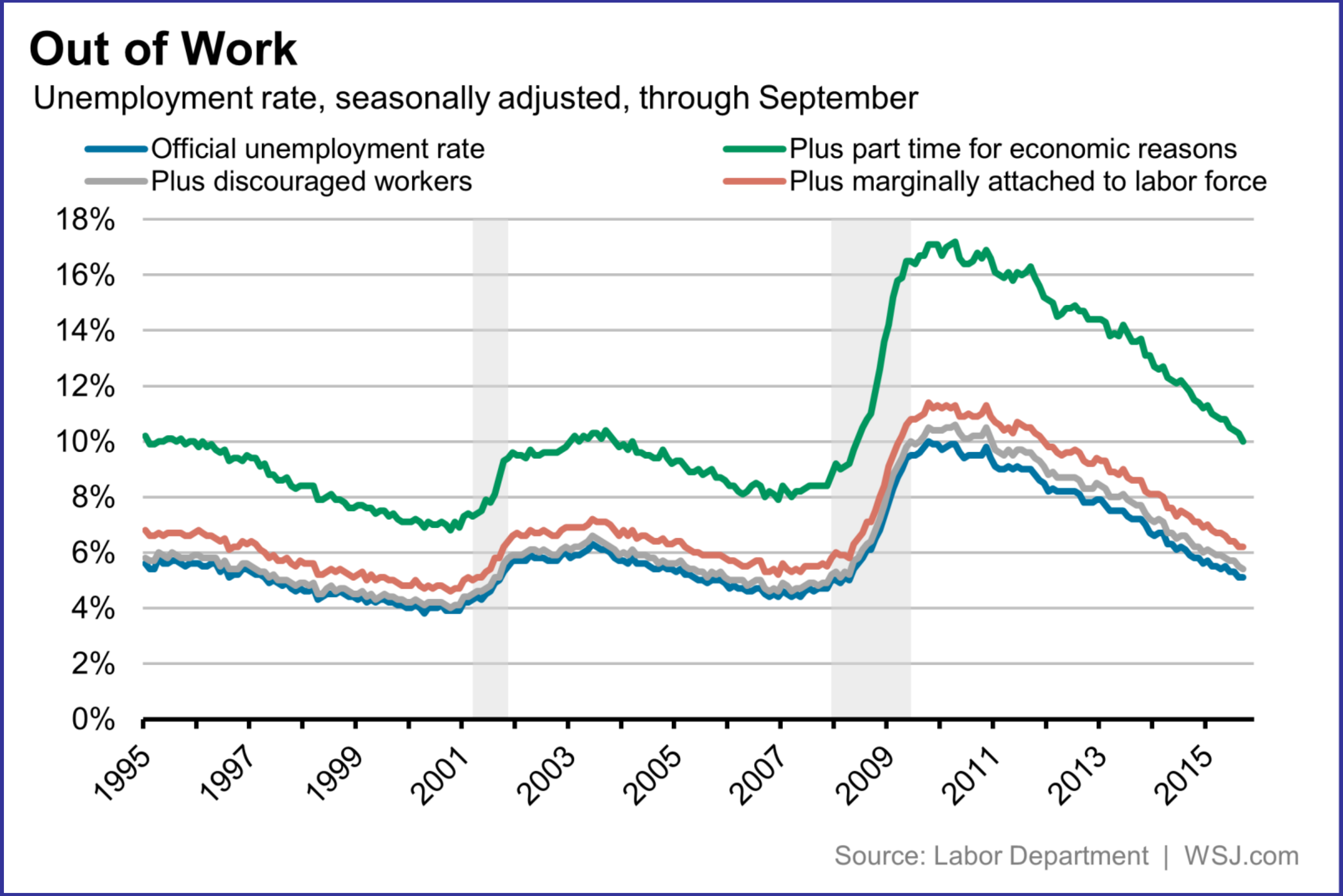
Unemployment rate keeps coming down – but, nearly 7 million remain "underemployed" – working part time, but want full time jobs

There are about 16 million people either unemployed , underemployed, or stopped Looking – **Key reason why wage increases are stagnant!

Source - - BLS: http://www.bls.gov/news.release/pdf/empsit.pdf; http://data.bls.gov/cgi-bin/surveymost?ln

Return TOC

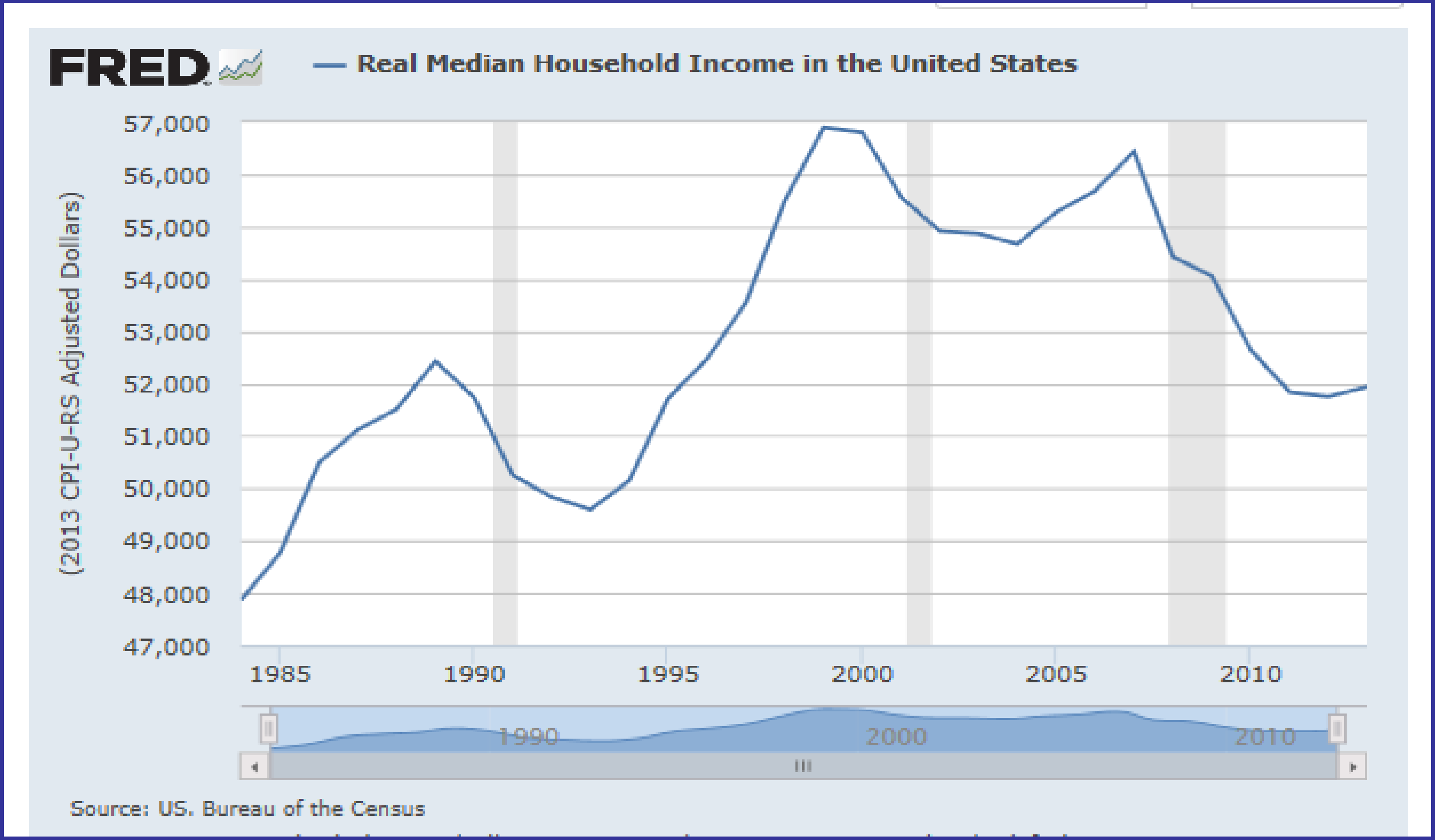
Closer look at "real unemployment rate" – things are improving, but we really need stronger *earnings* growth



Source: WSJ (http://blogs.wsj.com/economics/2015/07/02/the-june-jobs-report-in-10-charts/)

A look at real incomes over the past twenty years ---

real incomes have been shrinking for the past 20 years
and the reason is probably tied to productivity – here is good article
on the subject (http://www.wsj.com/articles/politicians-pay-heed-to-productivity-problem-1437582206?cb=logged0.19101819254186214)

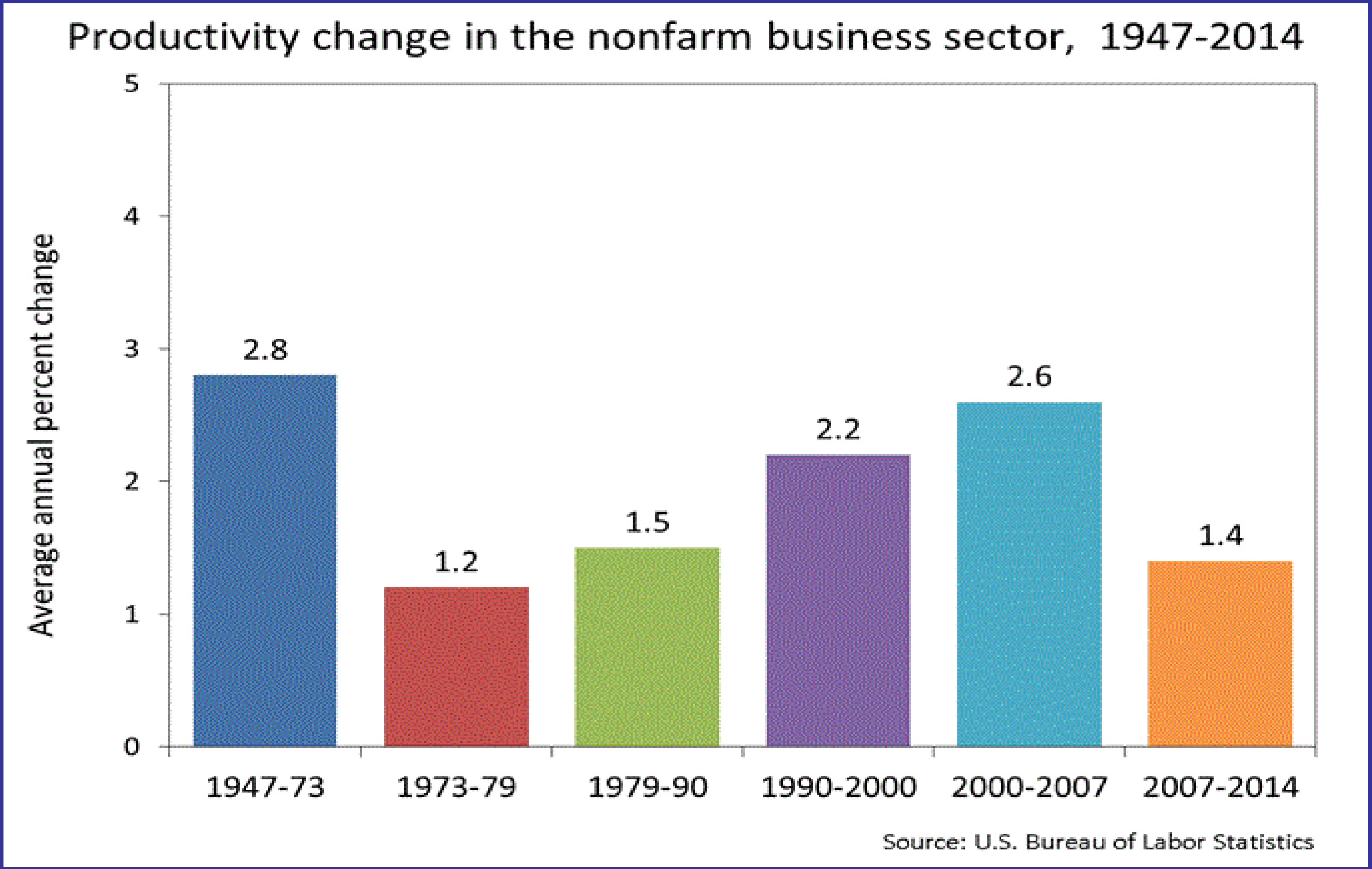


Return TOC

We need to invest more to become more competitive, create better paying jobs, this best way to grow GDP

GDP derives from number of workers plus productivity (real GDP/worker) – (http://marketrealist.com/2015/01/2-factors-drive-real-gdp-growth/) -- with lower productivity, higher employment won't generate as much growth in GDP – this is why improving employment doesn't give us strong GDP growth.

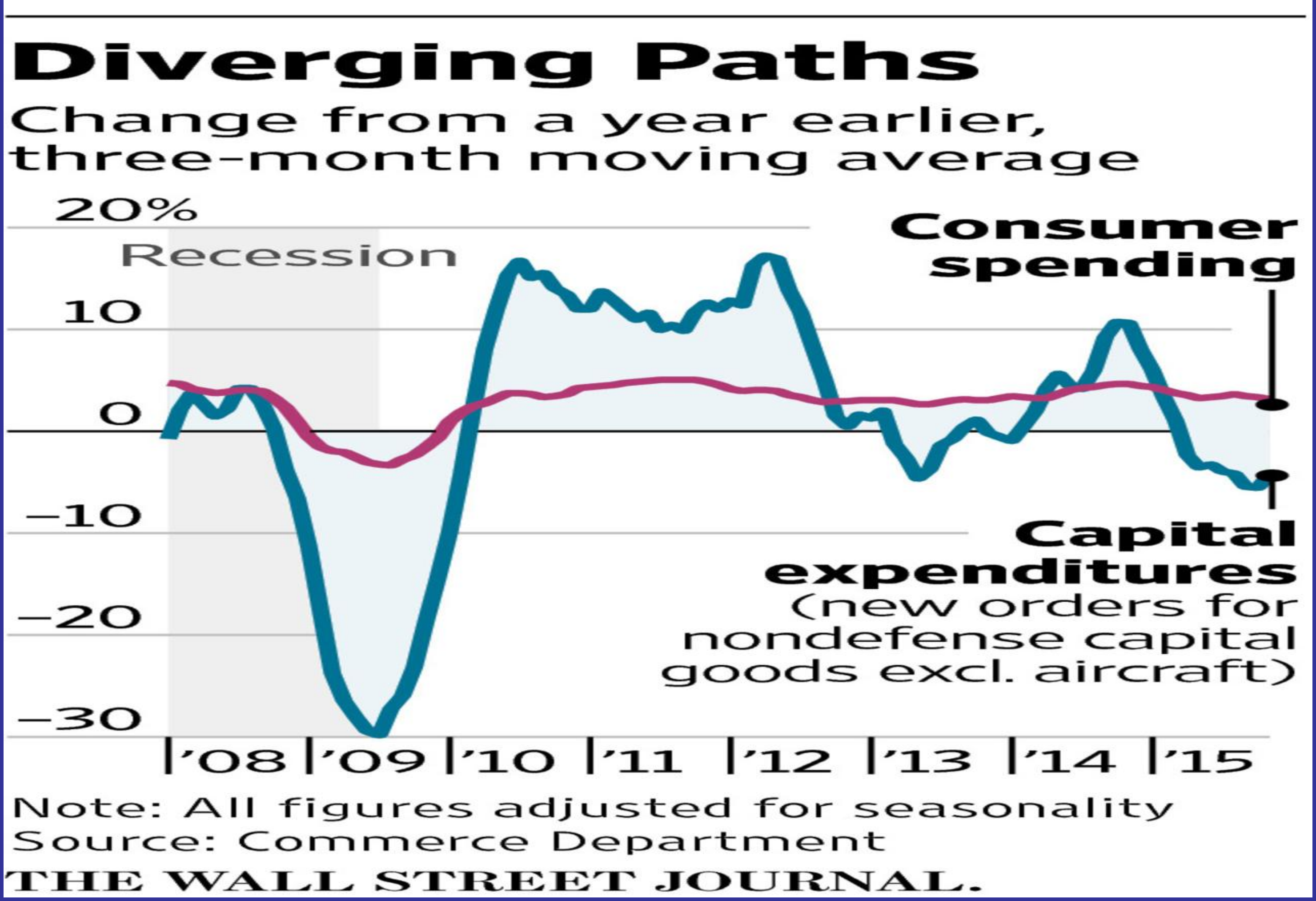
Innovation and entrepreneurship is key to increasing productivity



Source: BLS (http://www.bls.gov/lpc/prodybar.htm)

Return TOC

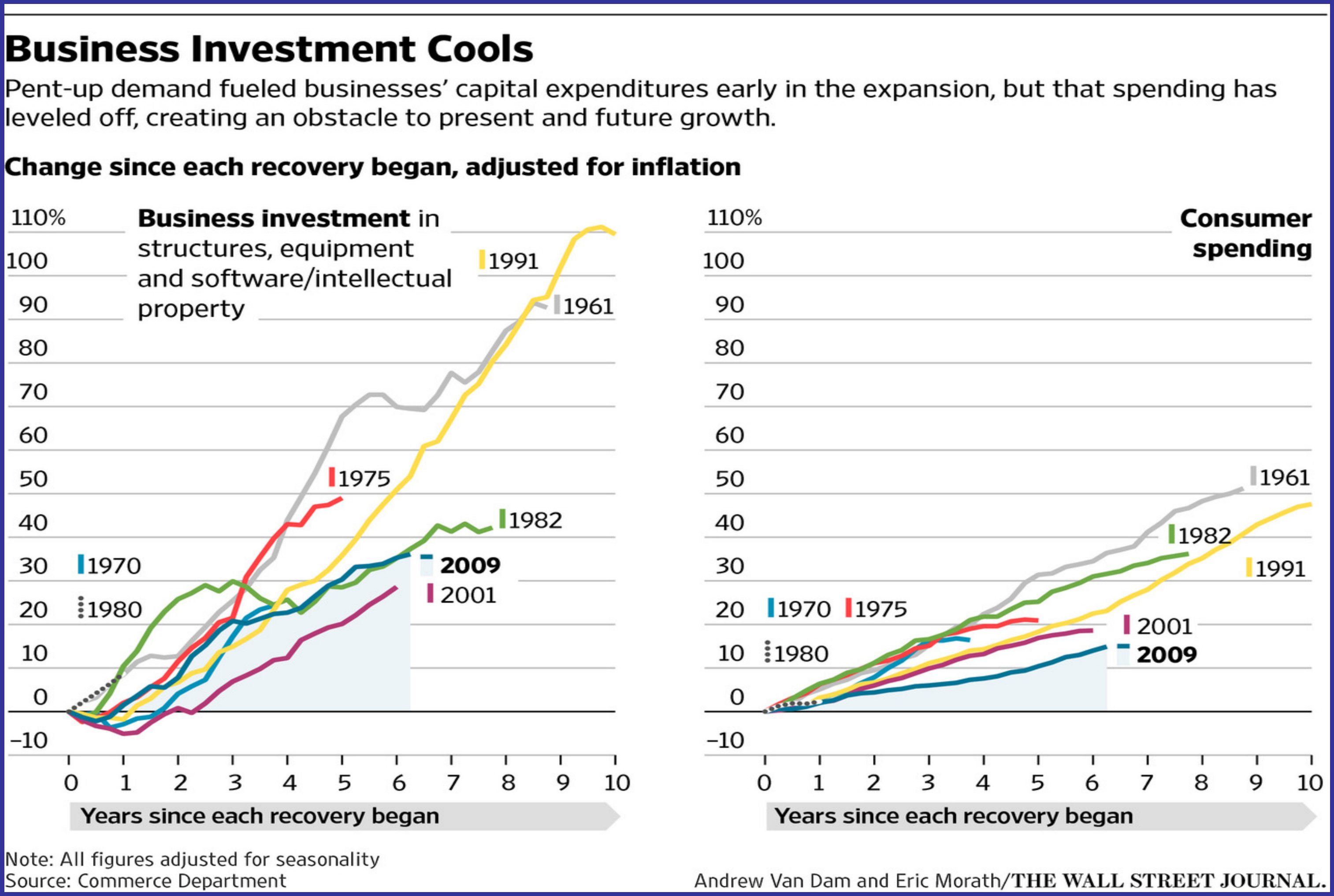
GDP growth comes from more workers and increasing productivity. Workforce participation (and population growth rate) is falling in USA. Now, capital expenditures are falling. Less investment leads to less productivity. Bottom line – slower growth over next 5 – 10 years? And less demand for housing!



(http://www.wsj.com/articles/companies-shy-away-from-spending-1448931106?cb=logged0.1367790653727522)

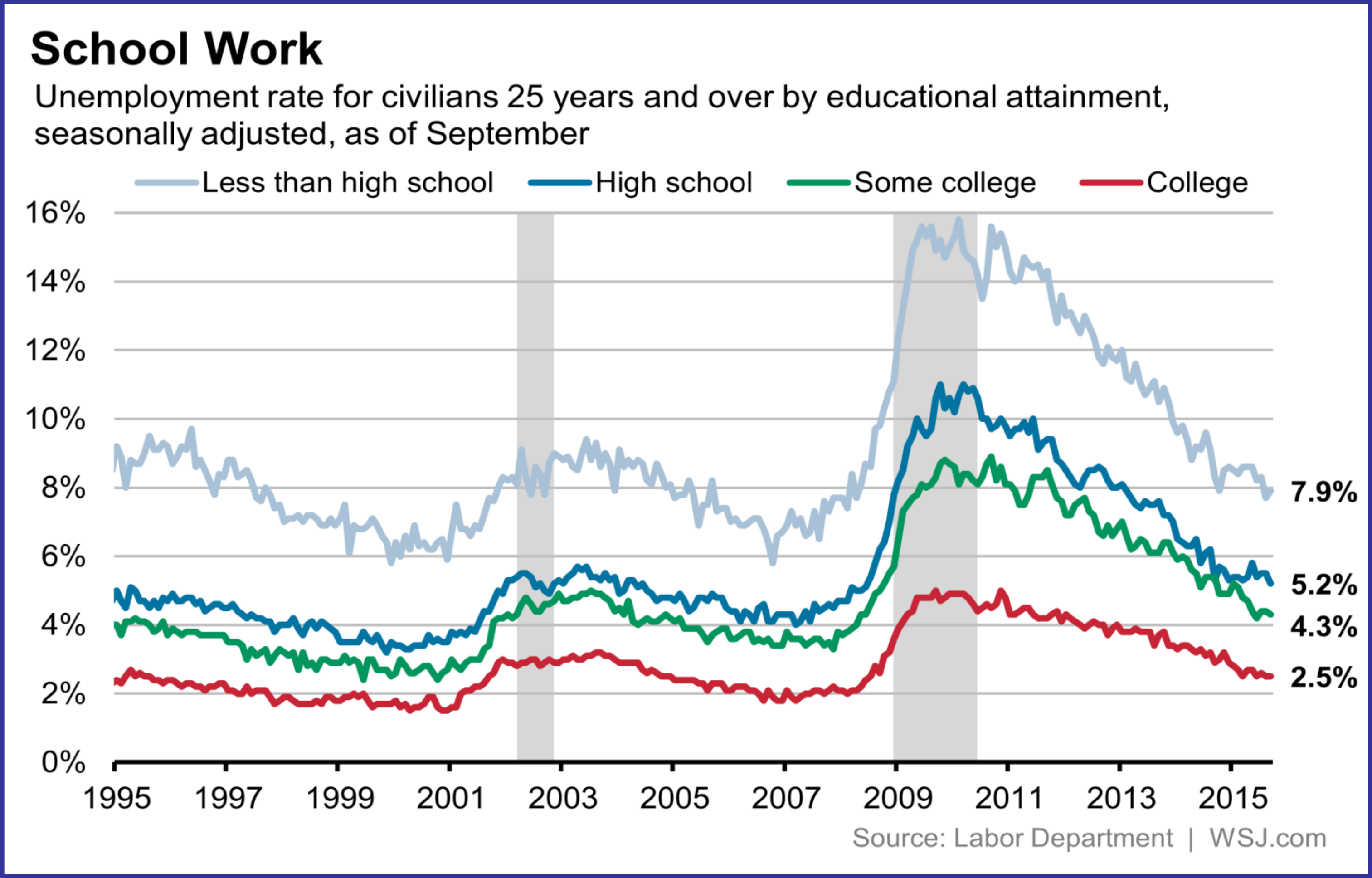
Return TOC

Investment is down because demand just isn't there – maybe we're not creating enough new products people want to buy.



Return TOC

One way to improve productivity and incomes ---
education improves your chances of staying out of the unemployment line

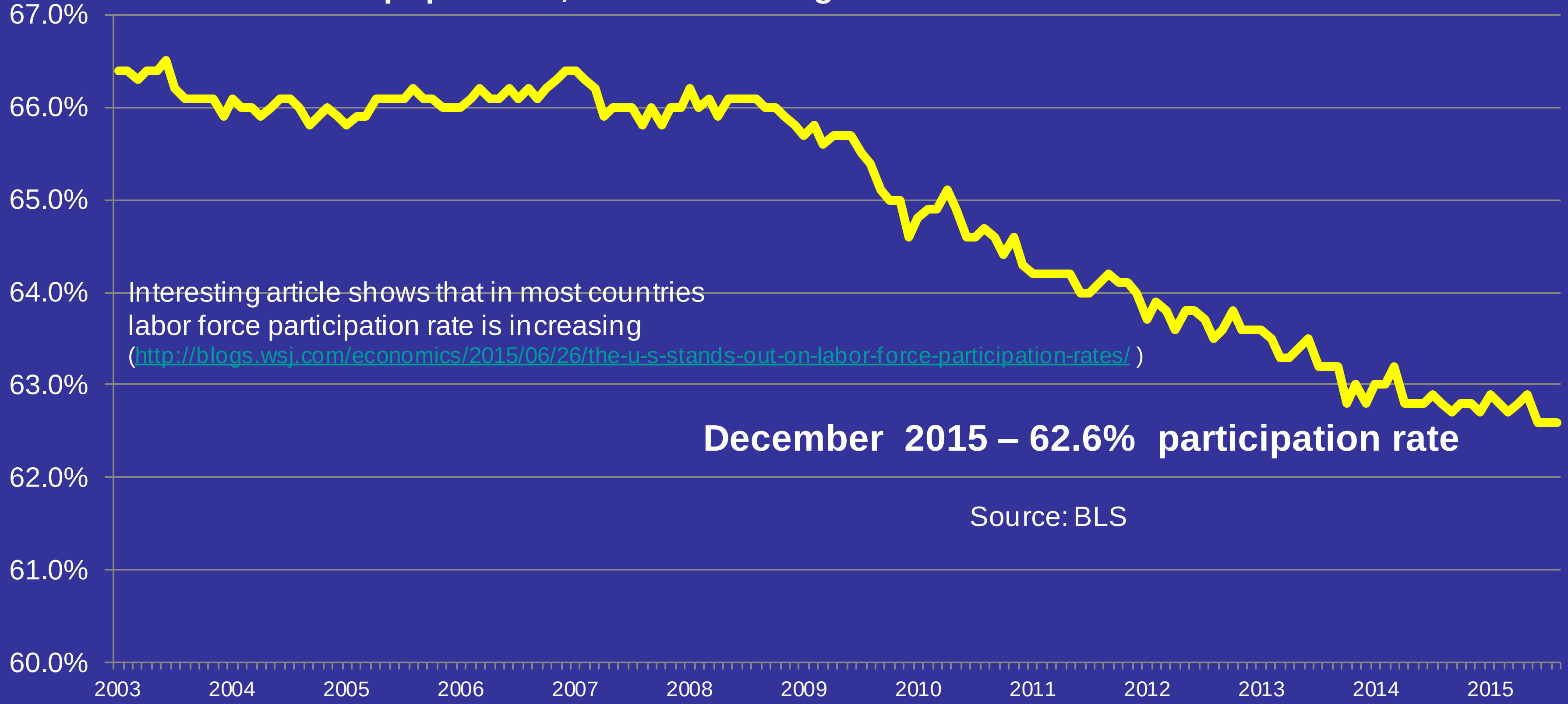


Source: WSJ (http://blogs.wsj.com/economics/2015/07/02/the-june-jobs-report-in-10-charts//)

Return TOC

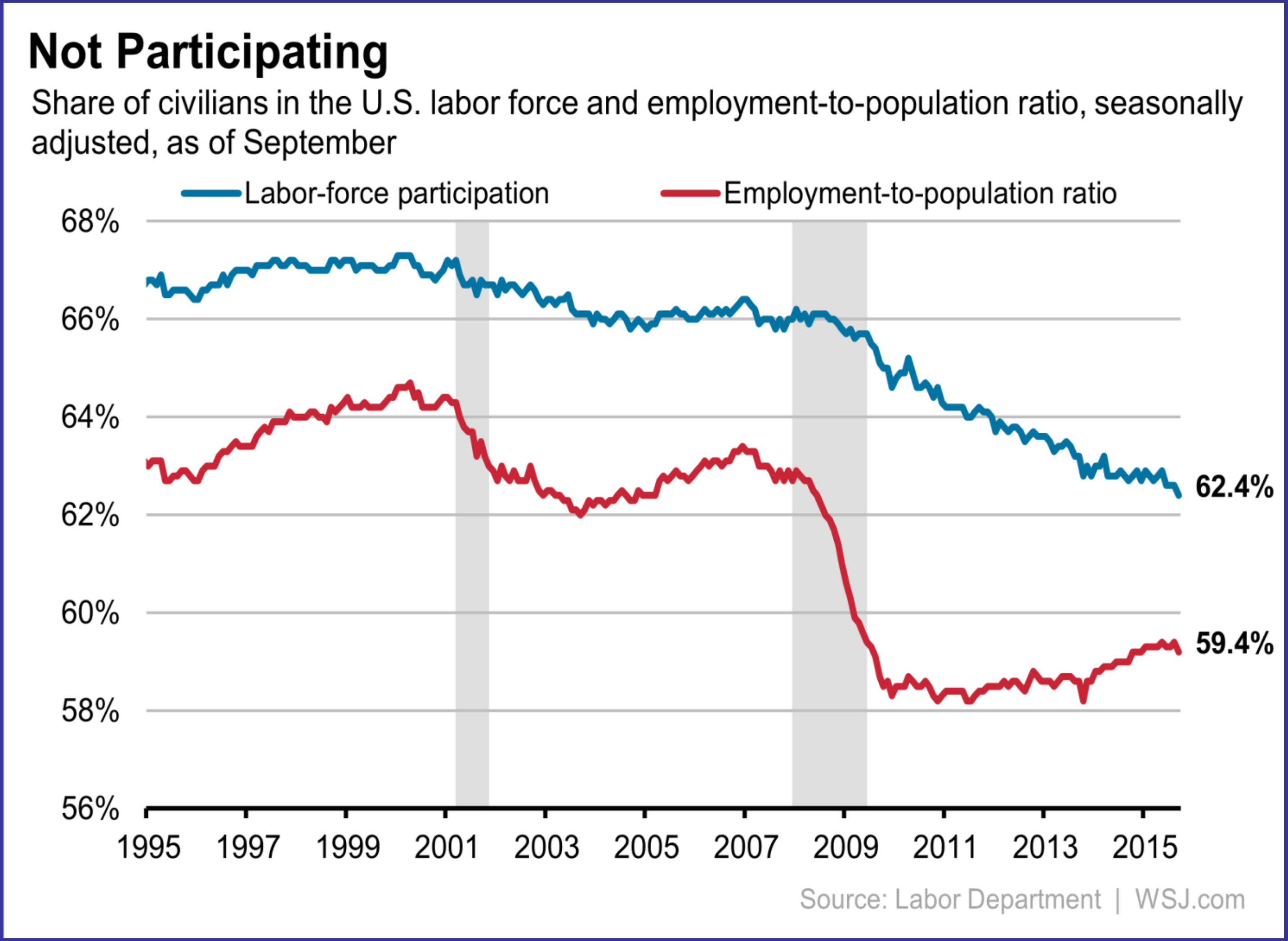
Labor force participation rate is shrinking – demographics is probably the main reason – we'll see skilled labor shortages increase over the next decade - we're already seeing construction related shortages with brick layers, masons, electricians, plumbers, etc. One solution – Revamp our education system (a 4 year degree isn't for everyone – 2 year Community colleges, vocational schools, are better fit for many, and they are much cheaper). Excellent article at:
http://finance.yahoo.com/news/should-i-go-to-a-trade-school-162413337.html#

% of civilian adult population, that are working



Return TOC

Aging population is part of the problem, but weak economy and mismatch between skills of job seekers and available jobs isn't helping



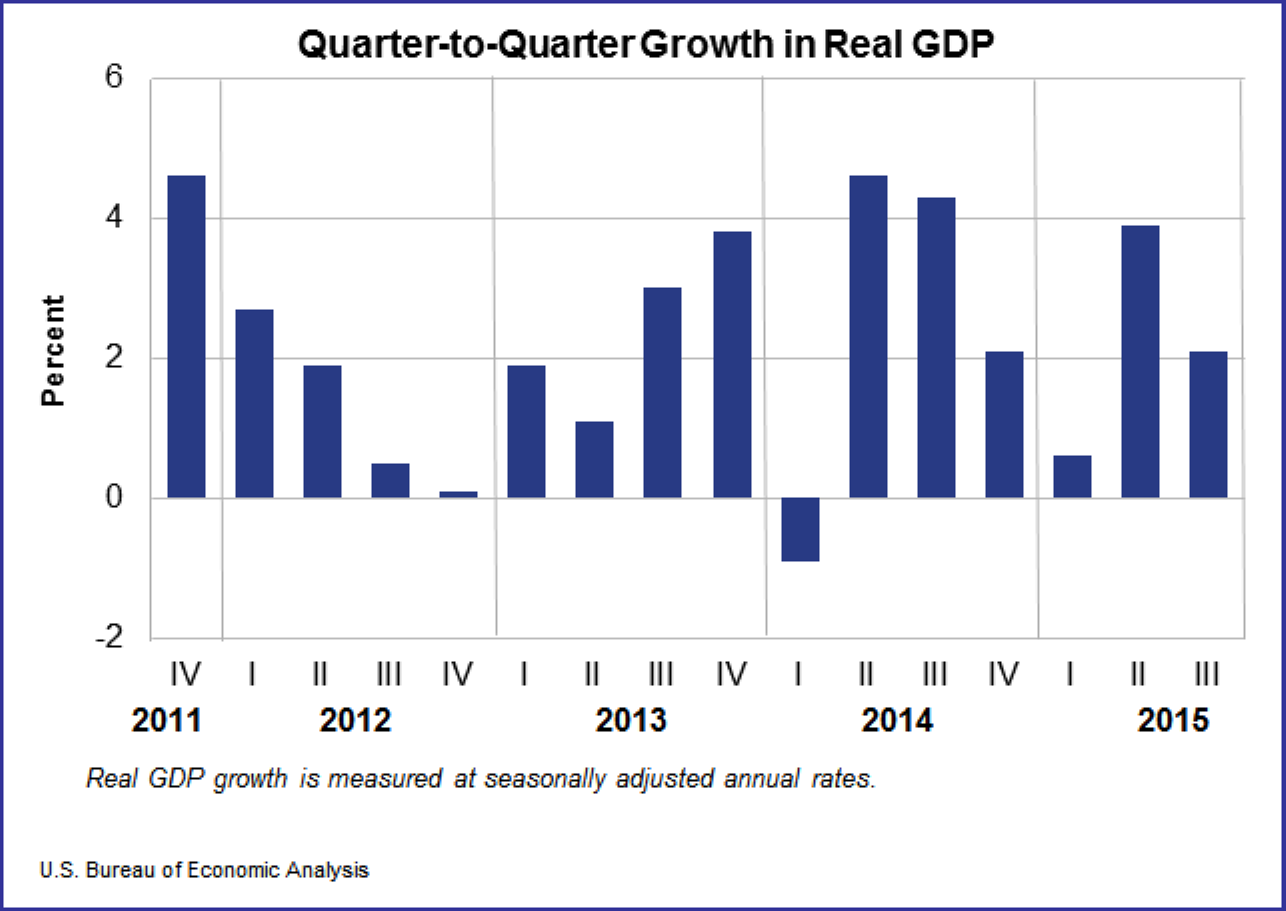
3rd Qtr Economic growth of 2.1% , down from revised 3.9% in Qtr 2 - - 2015/2016 GDP expected to remain about 2% - not enough to drive housing

(1) Slowing world economy (weaker China and European growth)

(2) Stronger dollar will reduce exports and increase imports – negative impact on manufacturing jobs which is key to income growth in USA

(3) Political stalemate/weak leadership, terrorism, currency wars, growing national debt, ...

(4) Weak income growth and continuing high "real unemployment"

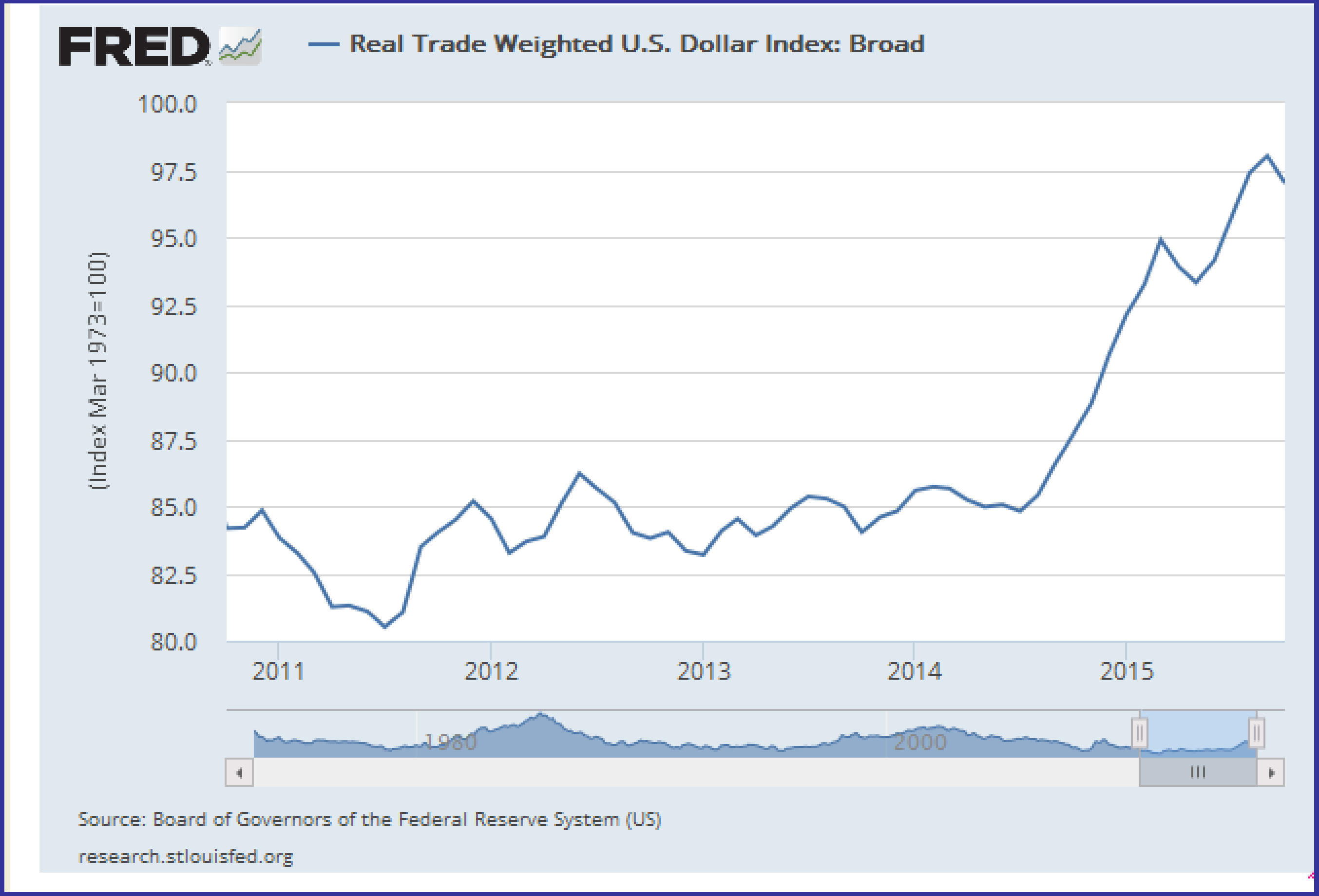


Source: BEA (http://www.bea.gov/newsreleases/national/gdp/gdp_glance.htm)

Return TOC

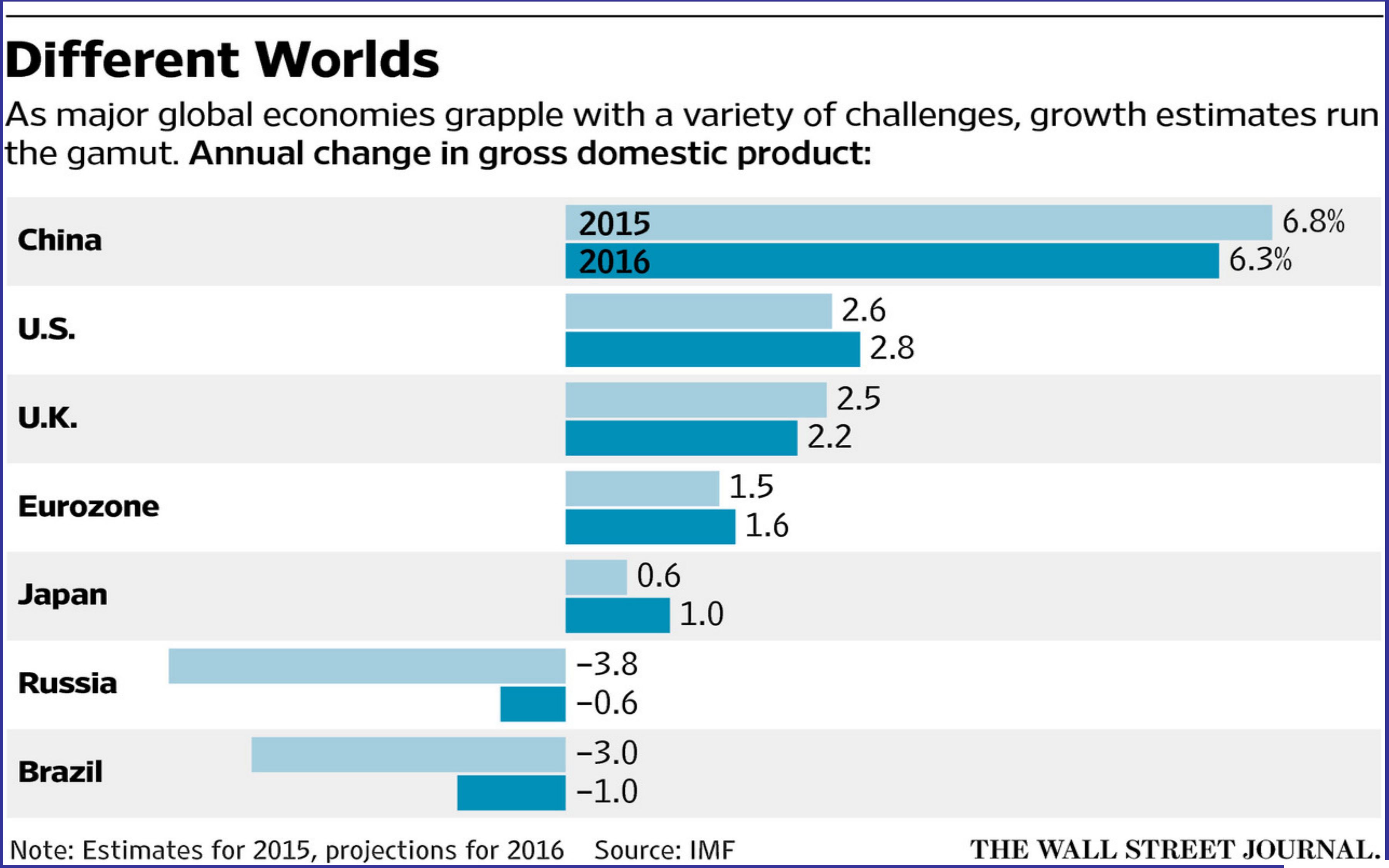
Strengthening dollar another headwind for U.S. economy.

Keeps inflation down, but hurts exports from key manufacturing sector.
Most countries are deflating their currencies to prop up weak economies further strengthening US dollar.



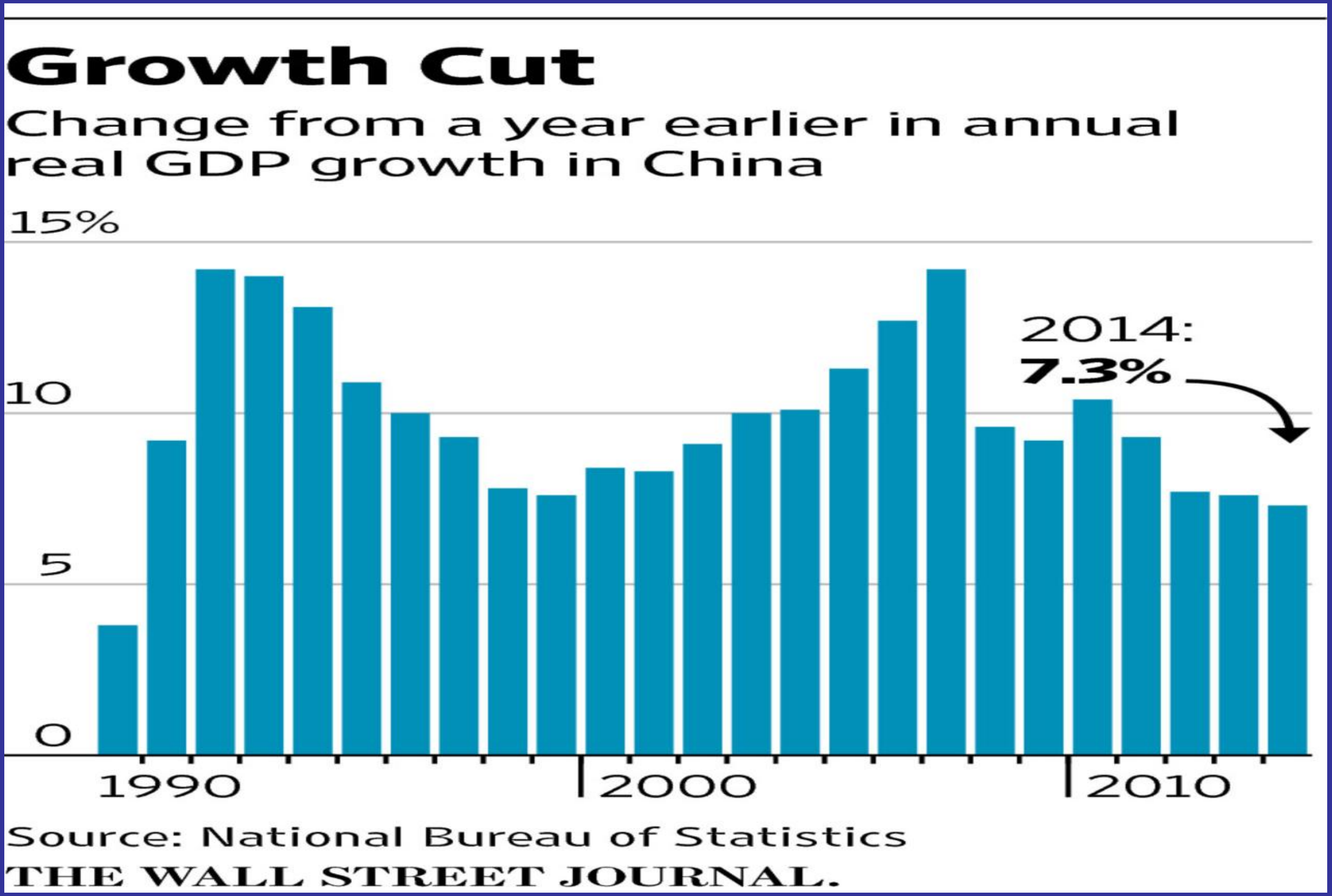
Return TOC

Slowing world economy – even these forecasts are a bit optimistic (my opinion) – e.g., USA GDP will be 2% at best and China's GDP will probably be about 6% or less.



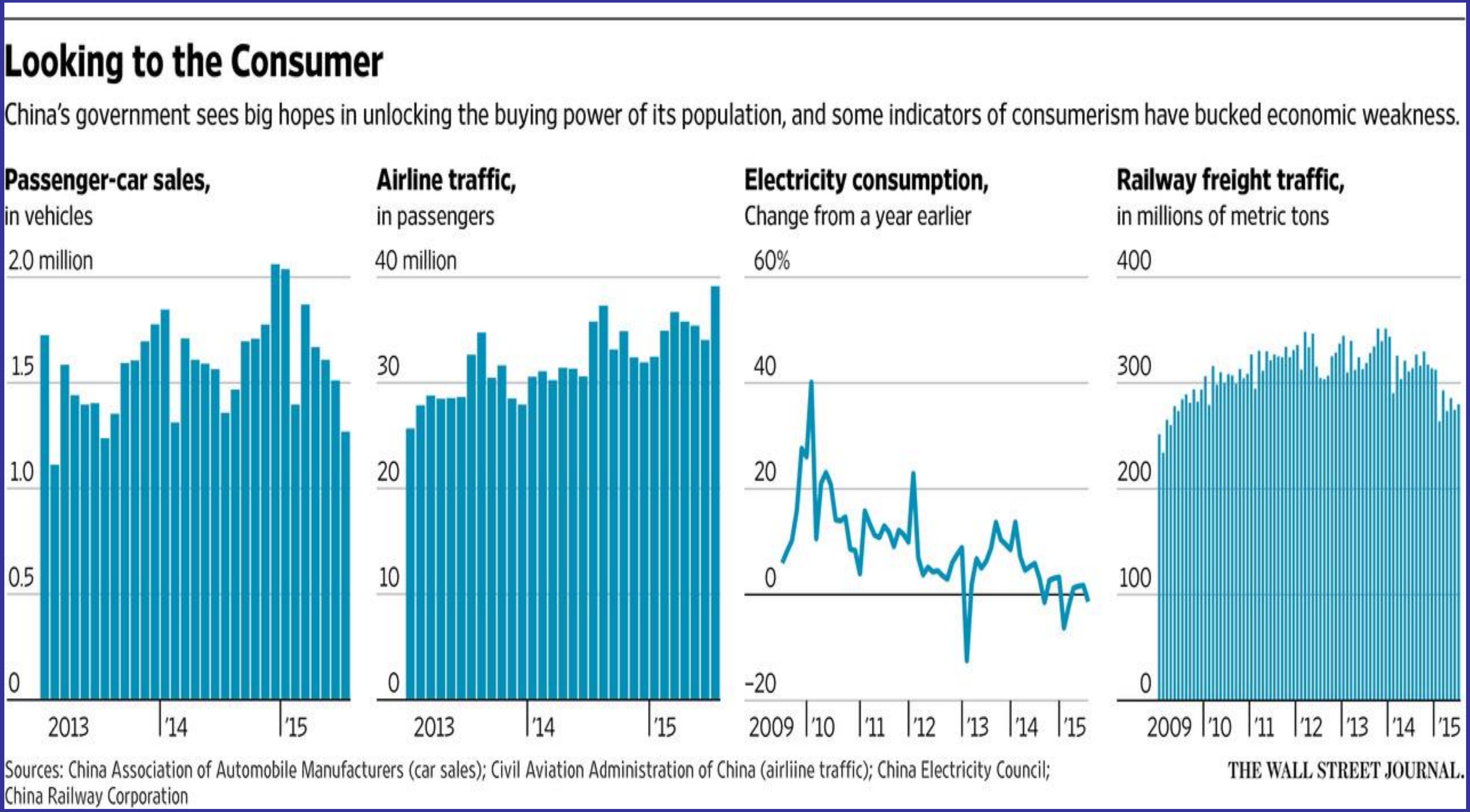
Return TOC

China's growth is slowing, – this is key to world economy (China is the world's 2nd largest economy) and even more important for commodity prices The recent Yuan devaluation is an indication that the Chinese government is concerned. *For past 5 – 6 years, China accounted forthe bulk of world GDP growth, so any slowdown will have major ripple effects*



Source: WSJ (http://www.wsj.com/articles/china-cuts-2014-economic-growth-to-7-3-from-7-4-1441593730)

China's economy shifting from infrastructure investments and exports (smokestack industries) to domestic demand driven economy (services and consumers) – this will take time – in the transition, GDP growth will probably slow significantly thus impacting world GDP growth



(http://www.wsj.com/articles/the-world-struggles-to-adjust-to-chinas-new-normal-1440552939?cb=logged0.14596216171606102)

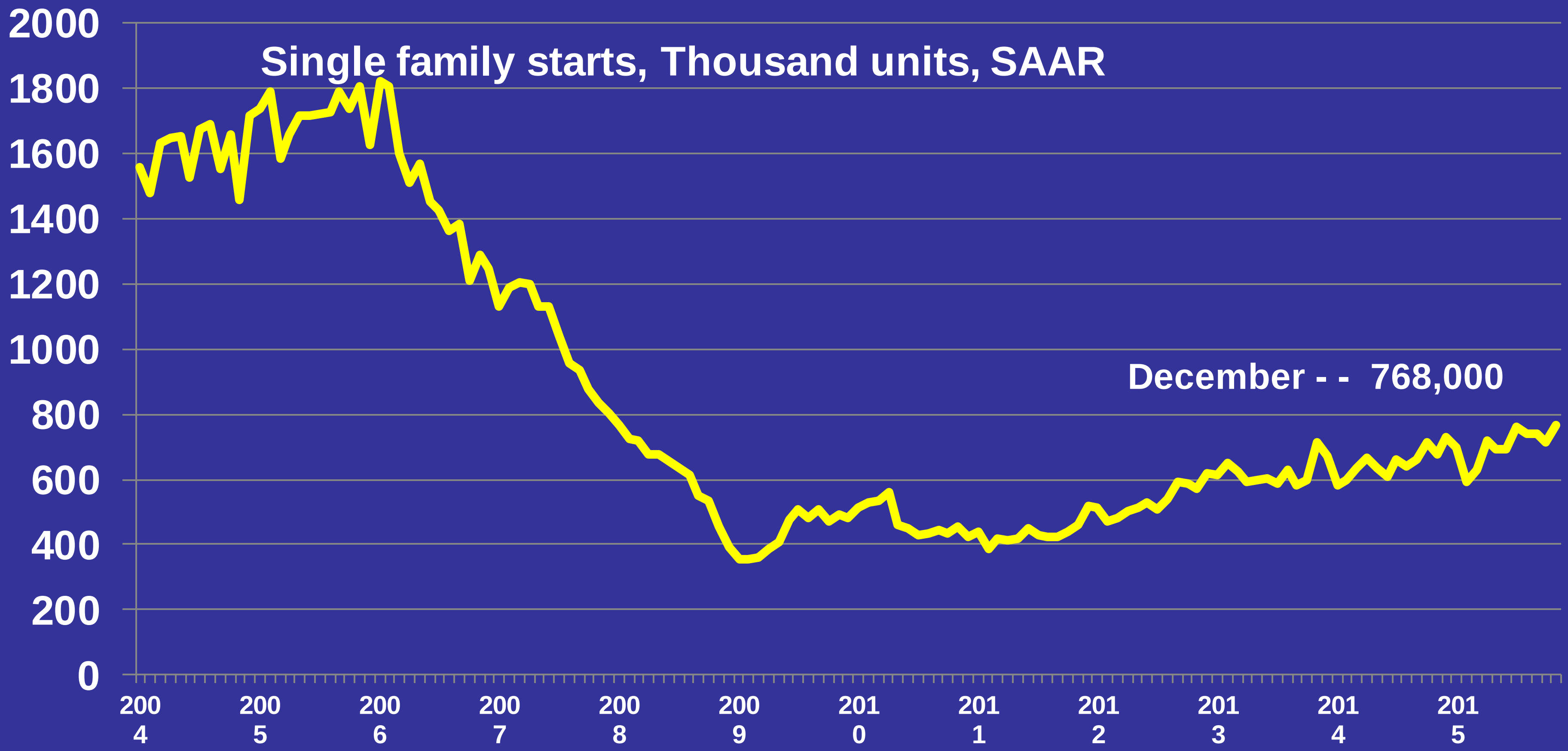
Return TOC

Recent Housing statistics

Return TOC

Starts are inching forward – I'm concerned that the Feds will 'grease the wheels" again – e.g., Fannie and Freddie, FHA --- lowering down payment requirements and premiums on mortgage insurance, …. I guess they forgot what happened in 2008? The FED has kept interest rates near zero for *8 years, but housing remains lethargic.*

Low interest rates won't fix housing!

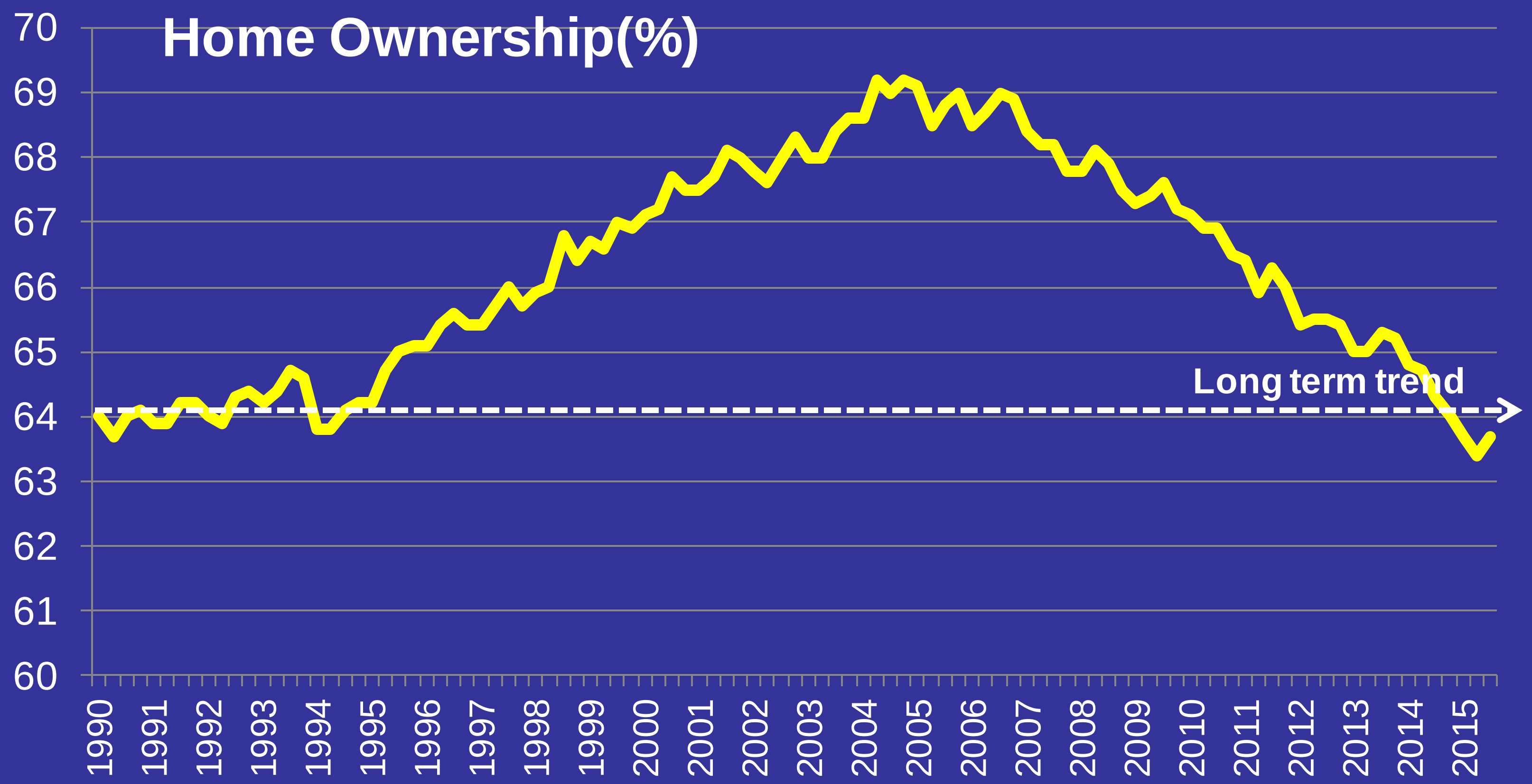


Source: Census (http://www.census.gov/const/www/newresconstindex.html)

Return TOC

Impact of weak household formations and shift to renting - -
homeownership rates have been falling for the past ten years – when the economy gets back to normal, will people return to to single family or will renting remain in favor with many? There will be impacts on wood products demand

Good article with some reasons why ownership is falling and why it will continue to fall for some time
(http://finance.yahoo.com/news/why-americans-waiting-longer-ever-070132848.html)



Source: Census (https://www.census.gov/housing/hvs/data/q413ind.html)

Return TOC

New Single Family Home sales are the key statistic to watch – Sales drive housing starts – this drives demand for wood products!!!

Getting better – up 4.7% versus October 2014 but, still disappointing considering we're 8 years "recovering" from the 2008 collapse

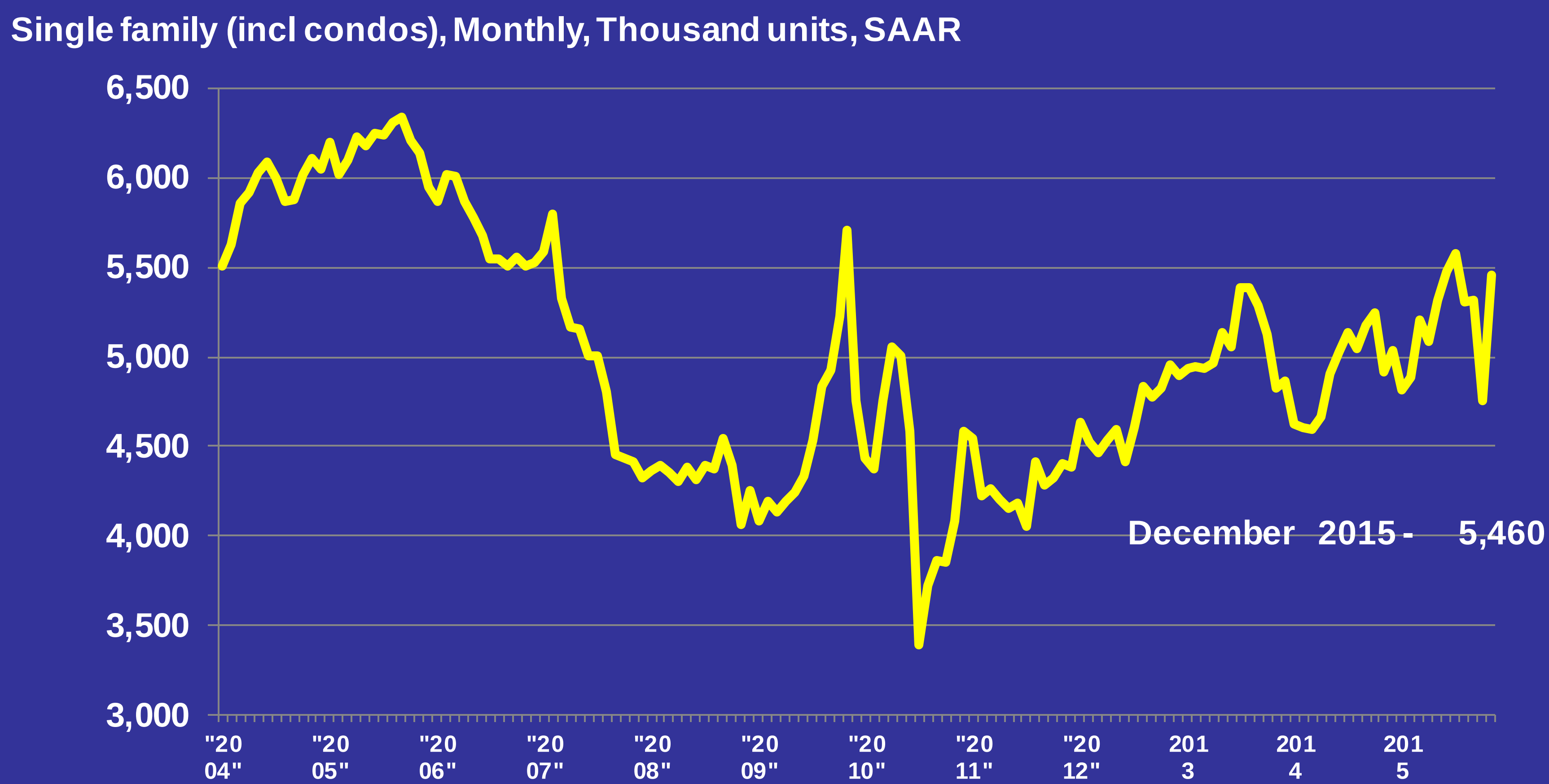
Note: Sales represent only houses built for sale or "spec homes" – does not include contractor built or homes built by the owner. Historically, "spec homes" represent about 70% of the market (https://www.census.gov/construction/nrc/salesvsstarts.html)

November 490,000

Source: Census (http://www.census.gov/const/www/newressalesindex.html)

Return TOC

Resale market continues to improve, but still heavy to cash sales (20%) with 1st time buyers still below trend, but improving (traditionally they represent about 40 – 45% of market, but today they are at 33%). Another problem today is tight supply (which drives prices), currently at 5.4 months. Healthy market is about 6 months supply.



Source: NAR (http://www.realtor.org/news-releases/2015/06/existing-home-sales-bounce-back-strongly-in-may-as-first-time-buyers-return)

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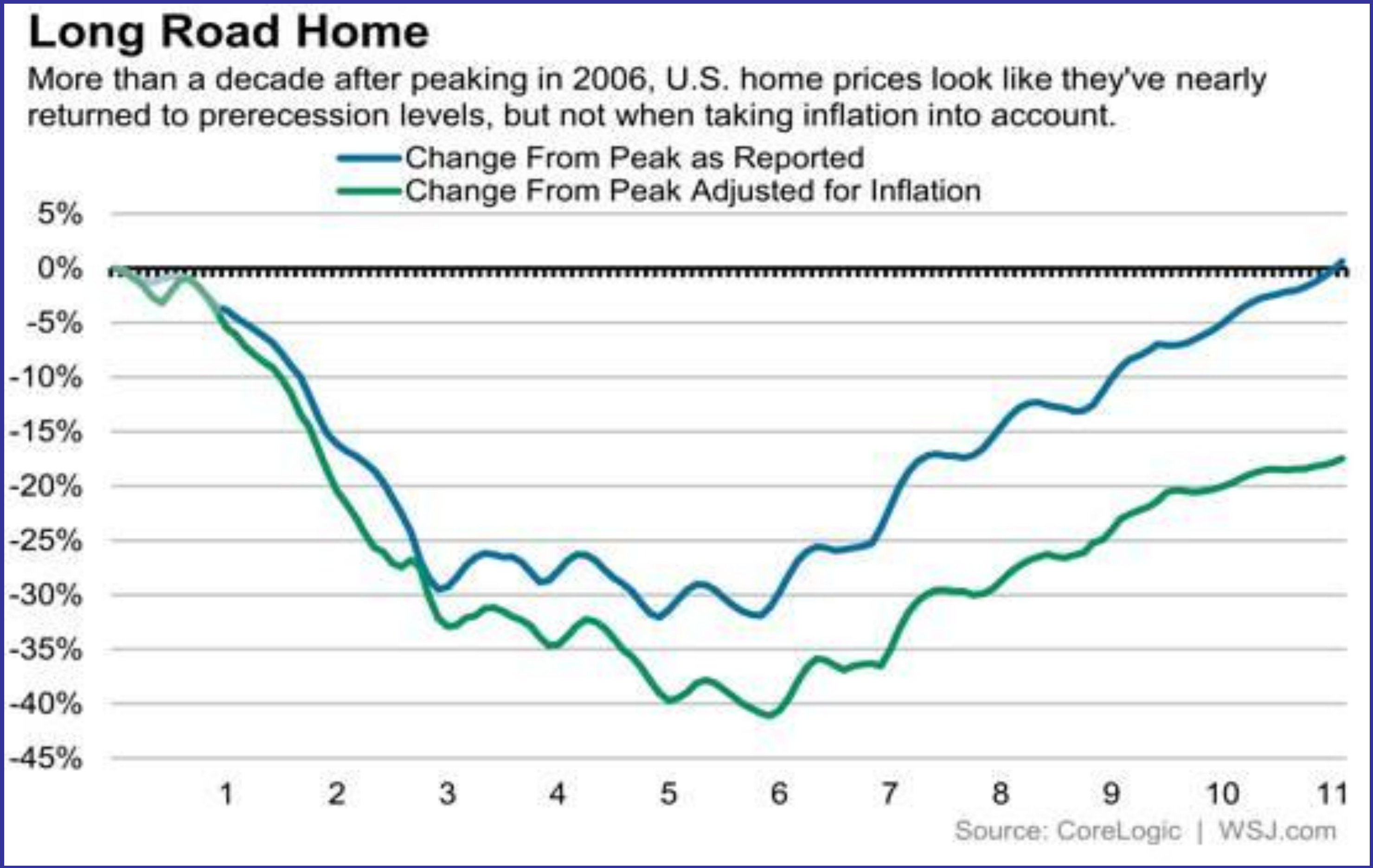
Home prices , adjusted for inflation, still down 20% from 2006 peak



(http://blogs.wsj.com/economics/2015/11/24/real-home-prices-could-take-17-years-to-return-to-peak/http://blogs.wsj.com/economics/2015/11/24/real-home-prices-could-take-17-years-to-return-to-peak

Some conclusions – housing continues to improve albeit slowly

(1) Economy will continue to improve slowly -- 2015 growth expected to be about 2.0% - however, slowdown in China will have serious ripple effects on world economy

(2) Still not a healthy housing market - 1st time buyers (32% today) are below trend (45%) and household formations are off 50% from trend.

(4) Political discourse will continue to slow a truly strong economic and housing recovery – too much uncertainty re: Affordable Care Act/Obama care; immigration reform; direction of economy.

(5) Productivity is a problem for U.S. economy – real GDP driven by population (number of workers) and real GDP/worker or productivity. During past 7 years, productivity has grown 1.7% annually whereas the average over previous 17 years it was 2.4%. The recent drop is probably due to in large part to lack of investment by private sector. That won't change much until they get more confident about the future of the country. Political discord is a real drag on the economy whether you want to believe it or not – it creates uncertainty, and clouds decision making. Plus, these are difficult times geopolitically. Uncertainty means less investment and slower GDP growth

(6) World economy is slowing – China, particularly, but Europe also face problems as well as the commodity focused economies like Australia and Canada. Demographics are a major reason as world fertility rates continue to fall in most of the developed world. Immigration reform needed, but this will be difficult with terrorism concerns.

(7) The fed raised interest rates this month – but most analysts expect any increases to be gradual. Minor impact on housing, but, then, housing doesn't need more headwinds.

Return TOC

Longer term:

*(1) **Makeup of U.S. economy is changing and this is impacting spending patterns and housing choices. The job market is undergoing long term – structural – changes. Automation is reducing job prospects for the middle class while creating jobs for the highly skilled and less skilled sectors . End result is stagnating family incomes that could translate to lower total housing demand with more emphasis on multi family/rental demand. Doesn't bode well for wood product demand and prices.***

*(2) **Education is more important today than ever before – don't forget two year programs; community Colleges; apprenticeships;… 4 year/University degree not always best option***

(4) Currency devaluations are the preferred solution to "low inflation" concerns. Central banks in Europe and Japan are following the U.S. with quantitative easing/printing money, in order to spur demand by weakening their currencies. Good article in WSJ suggesting that the "low inflation world" is really a symptom of too much capacity relative to demand, and the solution isn't currency devaluation. Better solution may be developing technology to produce products that fulfill market place demands not being met by existing products http://www.wsj.com/articles/global-glut-challenges-policy-makers-1429867807?mod=rss_markets_main

(5) Eventually, Central banks will have to raise rates and nobody knows how the various economies will respond. We've never had so much liquidity in the system – it causes various types of bubbles (assets like houses, stocks, etc.), and a misallocation of resources. Interesting times ahead.

(6) Rental housing demand is expected to remain relatively strong for some time into the future – demographics; economy; debt/credit issues; … will constrain single family demand

Return TOC

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