

Thriving in Wartime Conditions

Dr. Mark G. Dotzour

Real Estate Economist

College Station, TX

mdotzour@gmail.com

www.markdotzour.com

The American Economy Continues to Expand Despite Fighting Wars on Five Fronts

- Hot war in Iraq, Syria and Afghanistan
- Cyber war with Russia, North Korea
- Currency war with China, Japan and Europe
- Carbon war with OPEC
- Mortgage war with Dodd-Frank regulators

Since 1945, there have been **11** economic cycles

- The average recession has been 11.1 months
- The average expansion has been 58.4 months

Since 1945, there have been 11 economic cycles

- The average recession has been 11.1 months
- The average expansion has been 58.4 months.
- As of October, the current expansion is 76 months.

Since 1945

Longest U.S. Economic Expansions

- Mar 1991 to Mar 2001 120 months
- Feb 1961 to Dec 1969 106 months
- Nov 1982 to Jul 1990 92 months
- Jun 1938 to Feb 1945 80 months
- Nov 2001 to Dec 2007 73 months

Mythical Chimera

- Something that exists only in the imagination and is not possible in reality.



Mark Dotzour's Chimera: Winning the Masters with an 18 Handicap



Japan's Chimera: Quantitative Easing in a “New Dimension”

On Apr 4, 2013 BOJ will buy 50 trillion in JGB and 10 trillion in Nikkei ETFs

Plan to double the monetary base from 135 trillion yen to 270 in two years.

Government Pension Investment Fund will cut holdings of government bonds from 60% to 35% to increase demand for stocks.

“This is taking monetary easing into an entirely new dimension.”

H. Kuroda, Governor BOJ



Chinese Chimera: The Shanghai Stock Exchange

Shanghai Composite Streaming Chart



Plunged 30% in three weeks in June.

- You can buy, but you can't sell.
- Please borrow money to buy stocks.
- Half of all shares are suspended from trading.
- Declared war on "foreign puppet masters" and vicious short sellers.



Shanghai Stock Exchange

European Chimera:



I can help countries that are heavily in debt by loaning them even more money.

And I can print money to buy their bonds even when nobody else wants to buy them.

The Investment World Today: Globally

- Europe, Japan and China barely hanging on, even with massive printing of money.
- Commodity prices in a four-year free fall is hammering countries all over the world
 - Canada, Mexico, Brazil
 - Russia, Iran, Saudi Arabia
 - Australia
 - African oil exporting countries
- Hence, bonds from these countries are considered more risky.

The Investment World Today: United States of America

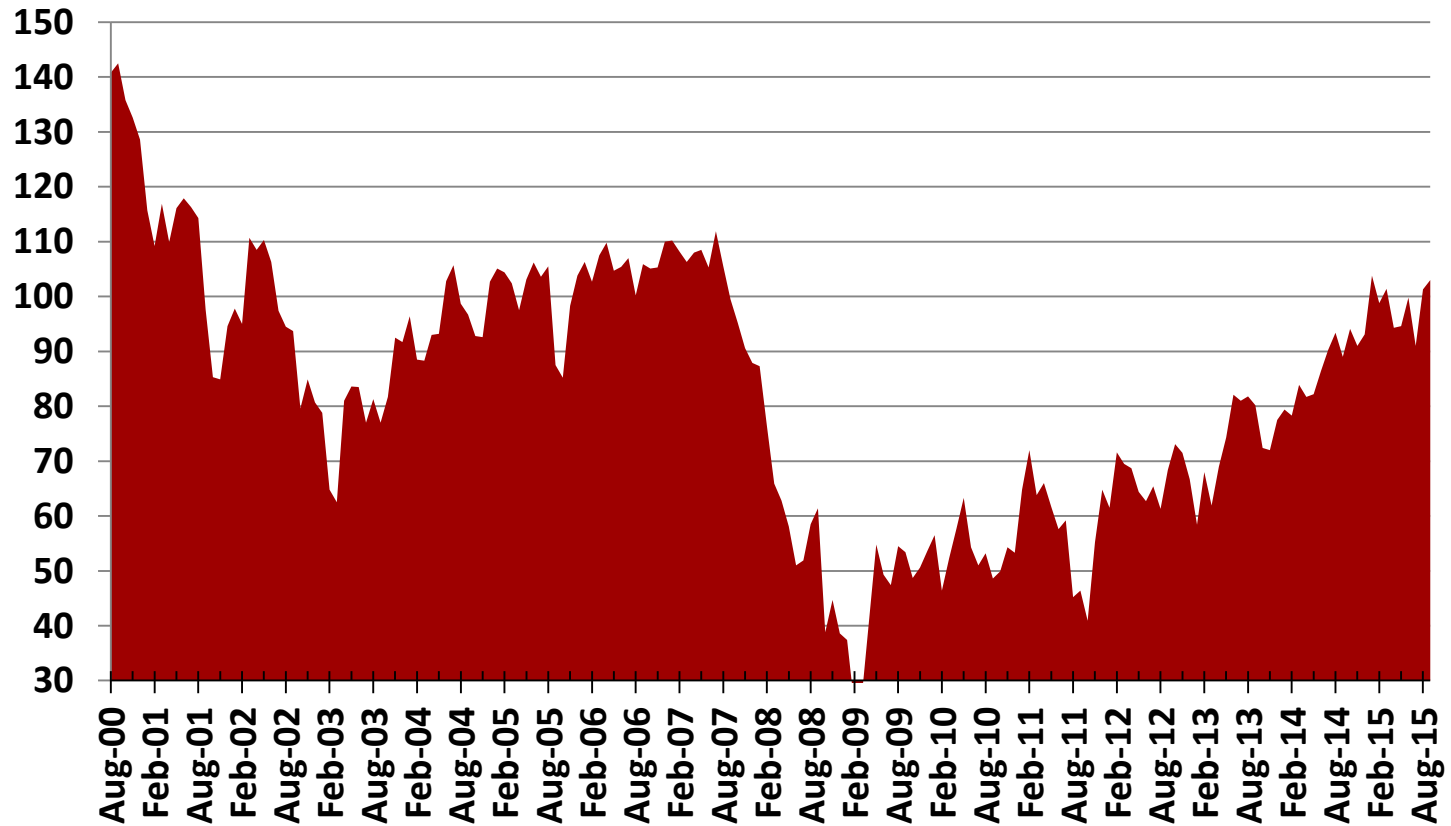
- The US economy could be in the 7th or 8th inning of this economic expansion.
- Spreads on junk bonds have widened substantially.
- Municipal default in Puerto Rico and the possibility of Chicago and Illinois have caused muni spreads to widen as well.
- Risk premiums on bonds have increased a lot in recent months.

The Challenge for the FED

- They need to normalize rates before we have the next recession.
- Declining 10-year treasury rate is signaling global economic weakness ahead.
- Higher rates mean a stronger dollar.
 - Less manufacturing
 - Less foreign investment in the US
 - More US investment in foreign countries

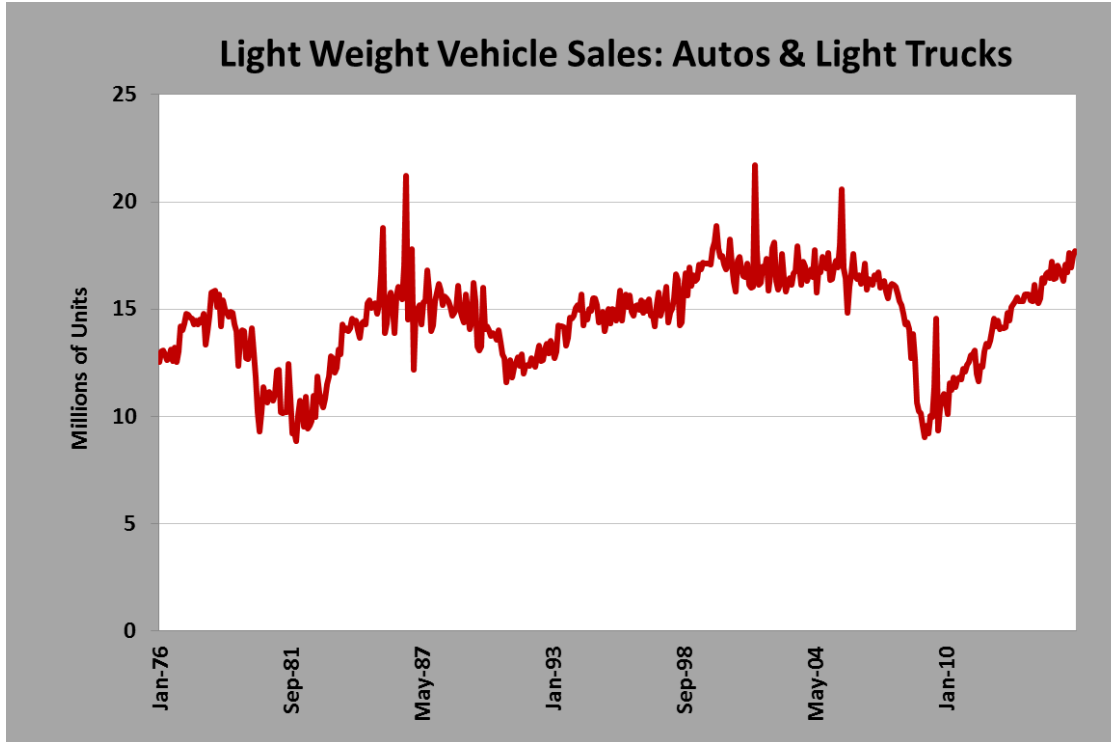
Nationally the Bullish Outlook Continues

Consumer Confidence Index



Source: The Conference Board

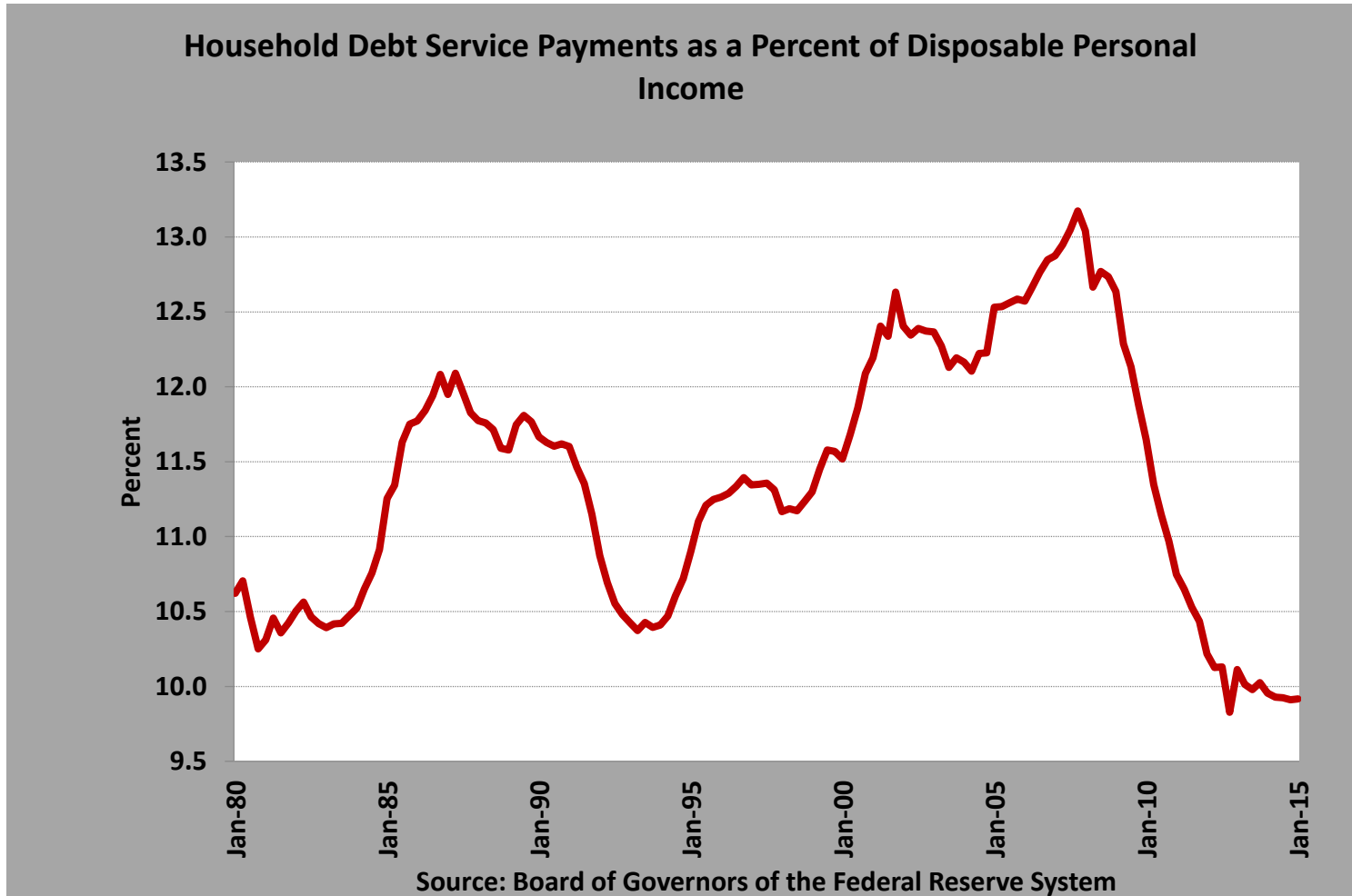
Light Weight Vehicle Sales: Autos & Light Trucks



Almost 40 percent of all auto and credit card loans in 2014 went to sub-prime customers.

In 2014, 2.1 million new cars and trucks were built in the US and shipped to other countries. This is a 74% increase from 2004.

Household Debt Service Payments as a Percent of Disposable Personal Income



Household Debt Service Payments as a Percent of Disposable Personal Income

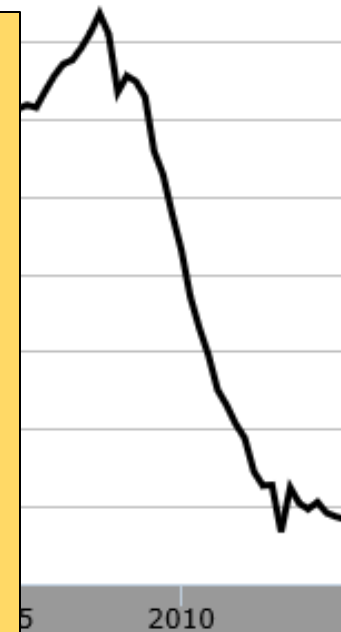
FRED 

— Household Debt Service Payments as a Percent of Disposable Personal Income

13.5

Consumers allocating disposable income to:

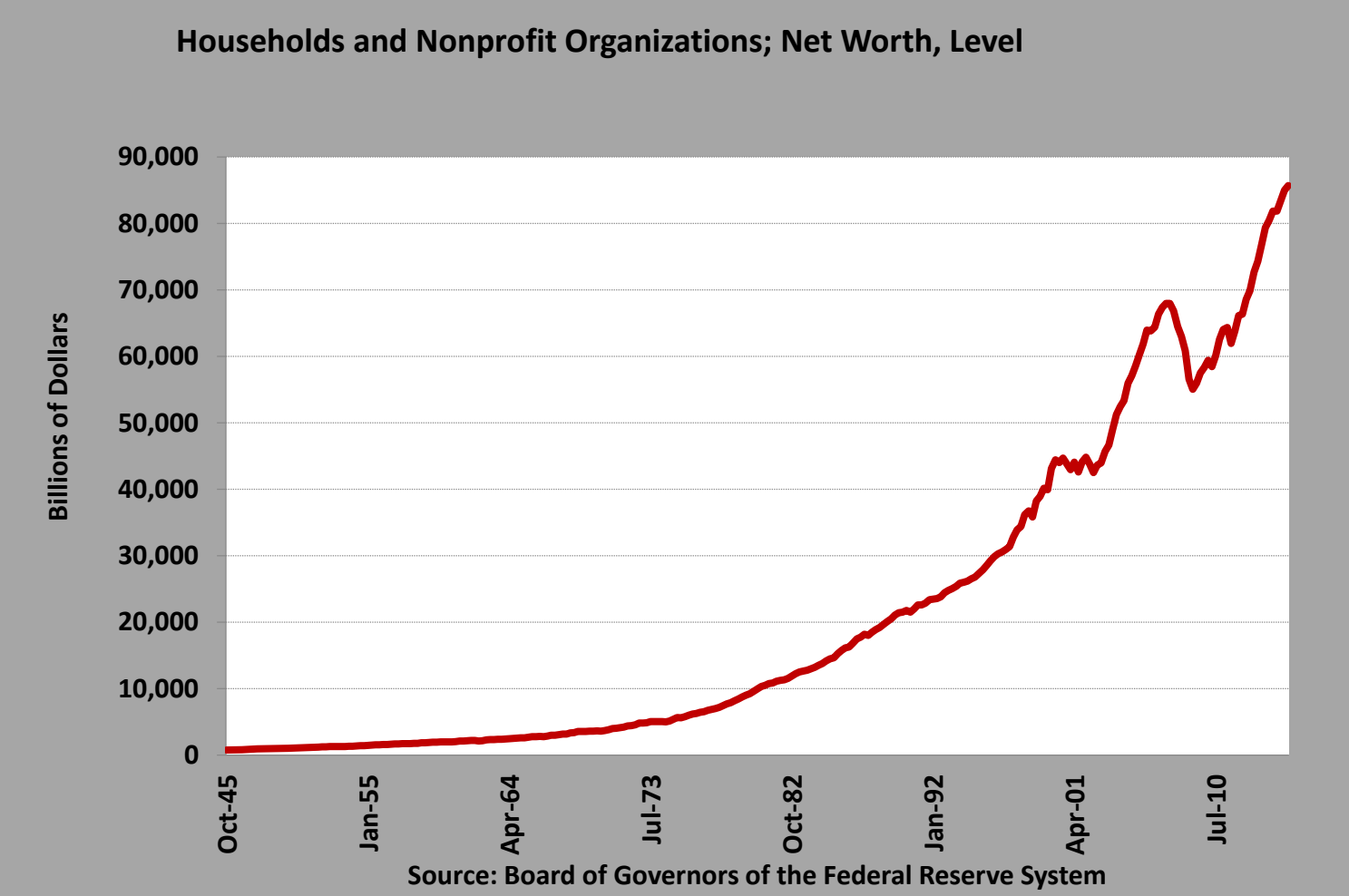
- Cell phones
- Internet connections
- Cable television
- Rent



Source: Board of Governors of the Federal Reserve System

2014 research.stlouisfed.org

Household Net Worth Recovering After Stock Market Rally

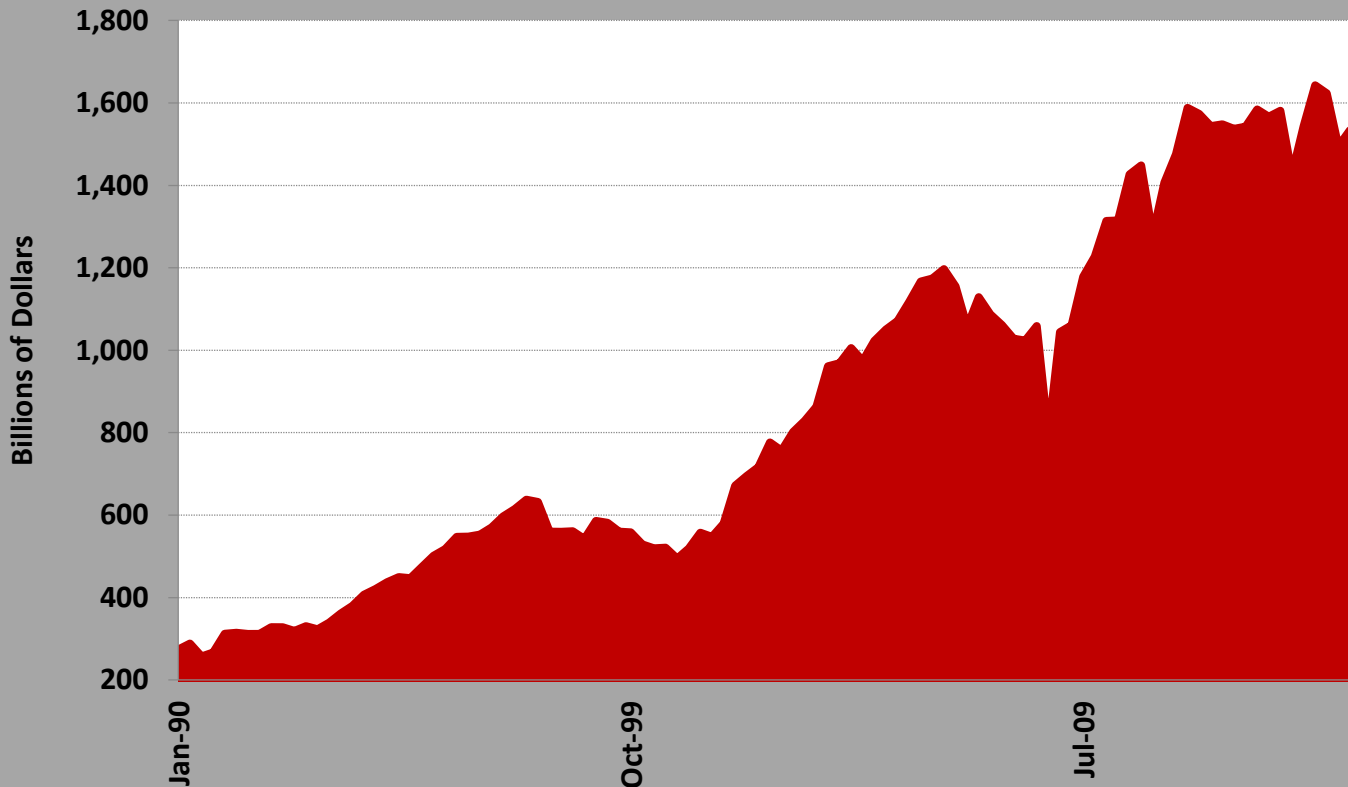


The Business Sector

Corporate Profits

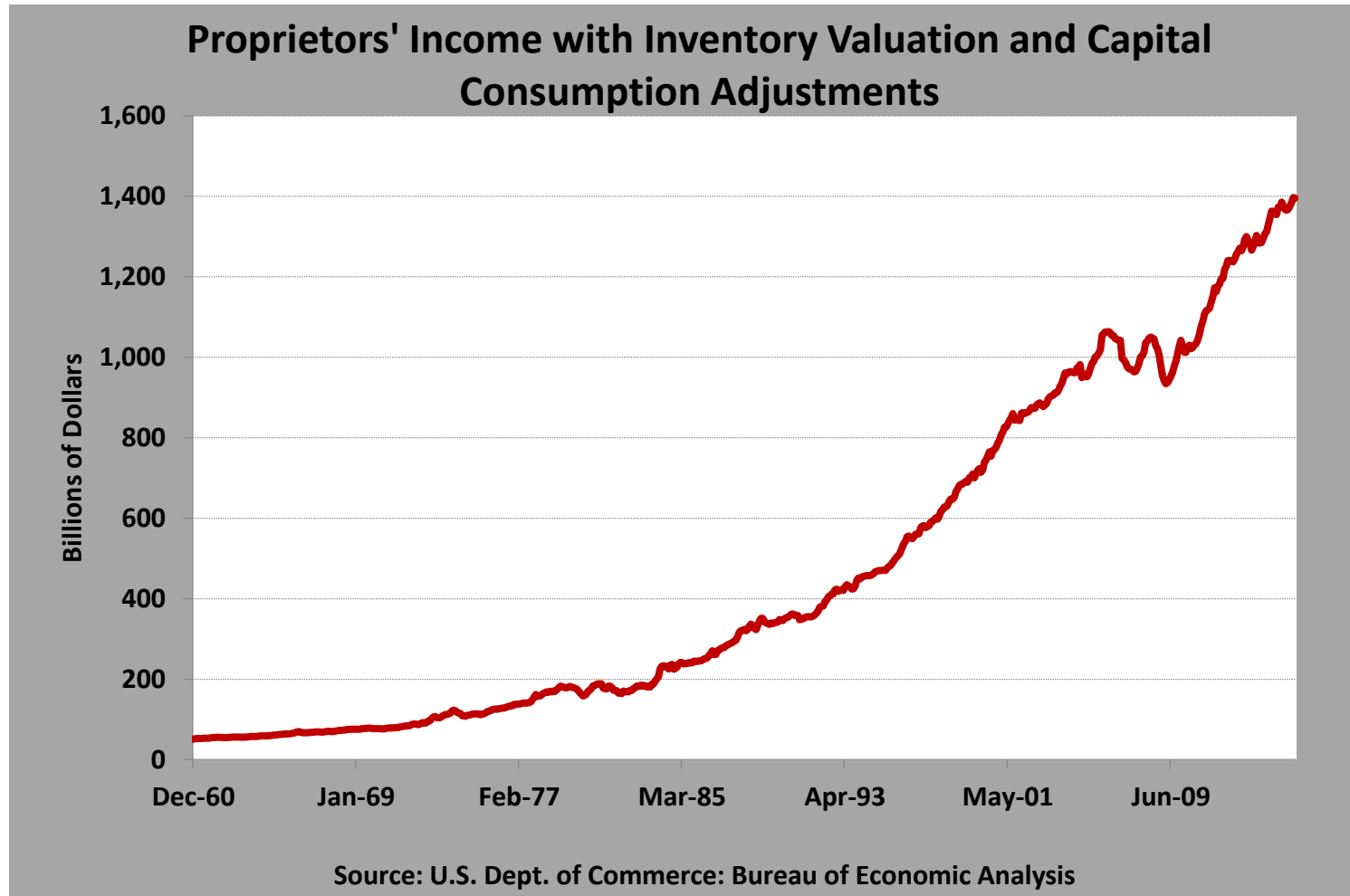
(With Inventory Valuation Adjustment & Capital Consumption Adjustment)

Corporate Profits After Tax with Inventory Valuation Adjustment (IVA) and Capital Consumption Adjustment



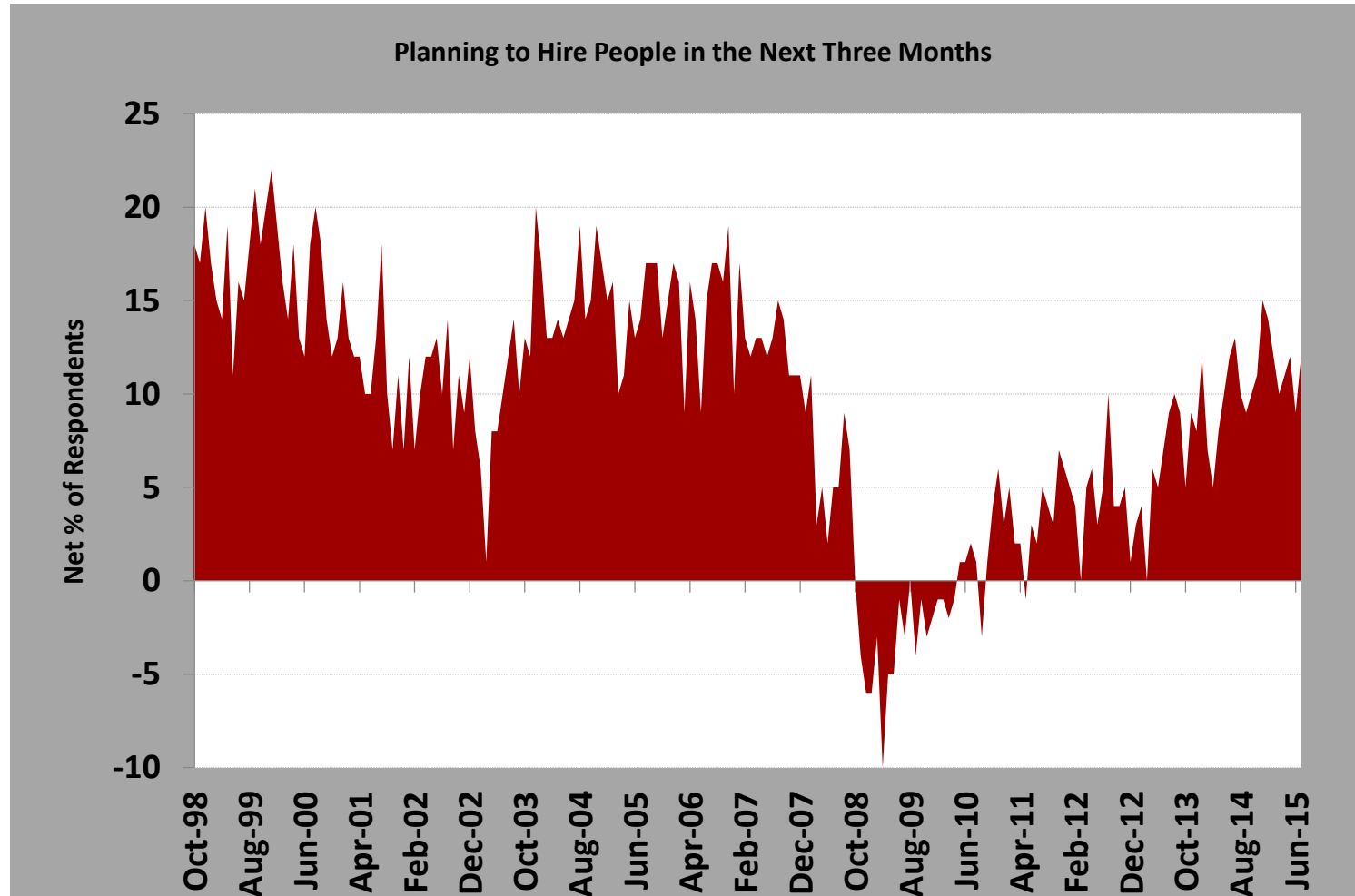
Source: U.S. Dept. of Commerce: Bureau of Economic Analysis

The Economy: Proprietor's Income



Small Business Outlook

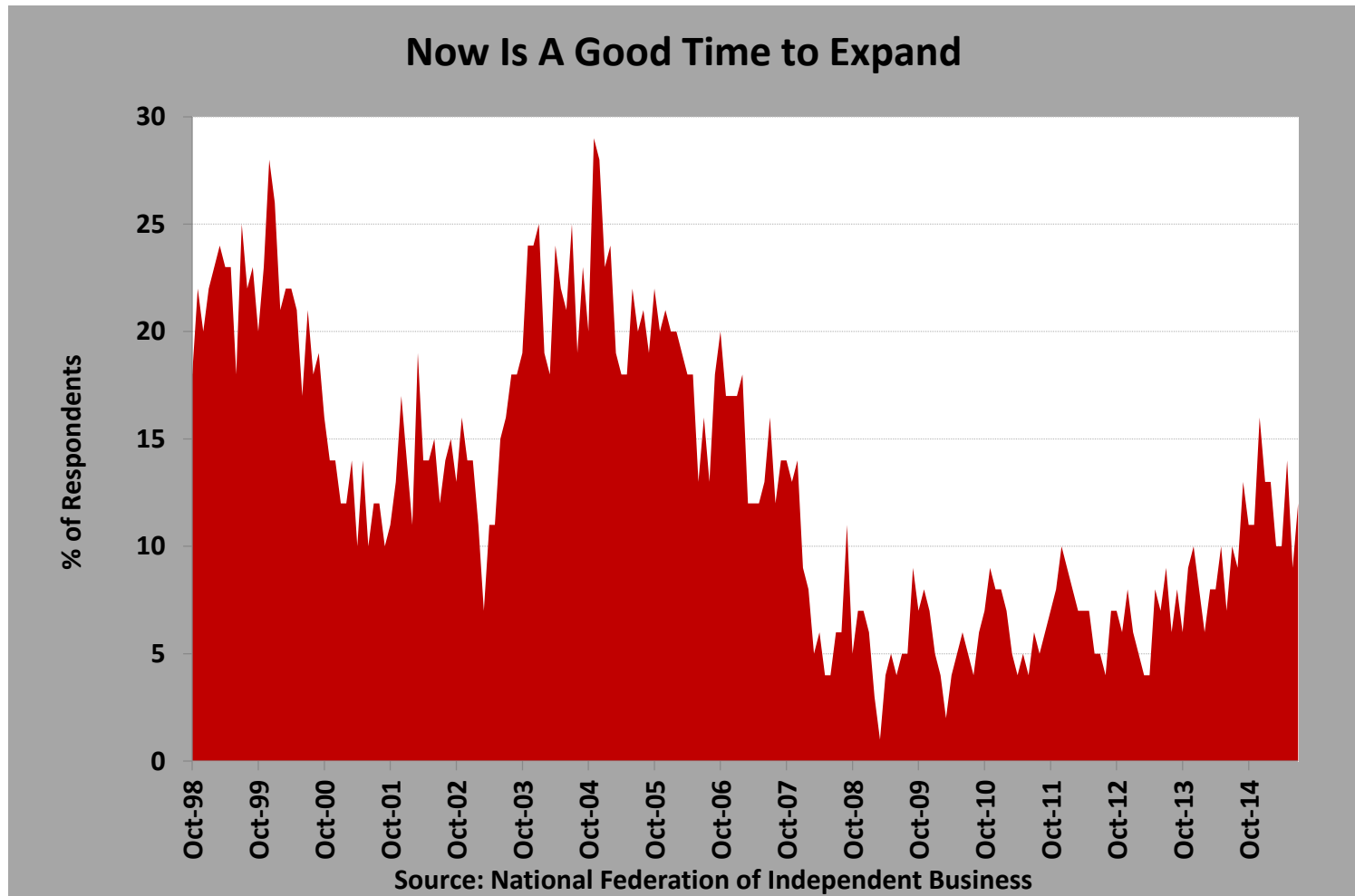
“Planning To Hire People In The Next Three Months”



Source: National Federation of Independent Business

Small Business Outlook

“Now Is A Good Time To Expand”



Corporate Hiring Plans: Next 6 Months

	<u>Q2-15</u>	<u>Q1-15</u>	<u>Q4-14</u>	<u>Q3-14</u>
More Jobs	34%	40%	40%	34%
Less Jobs	26%	23%	23%	20%

Source: Business Roundtable

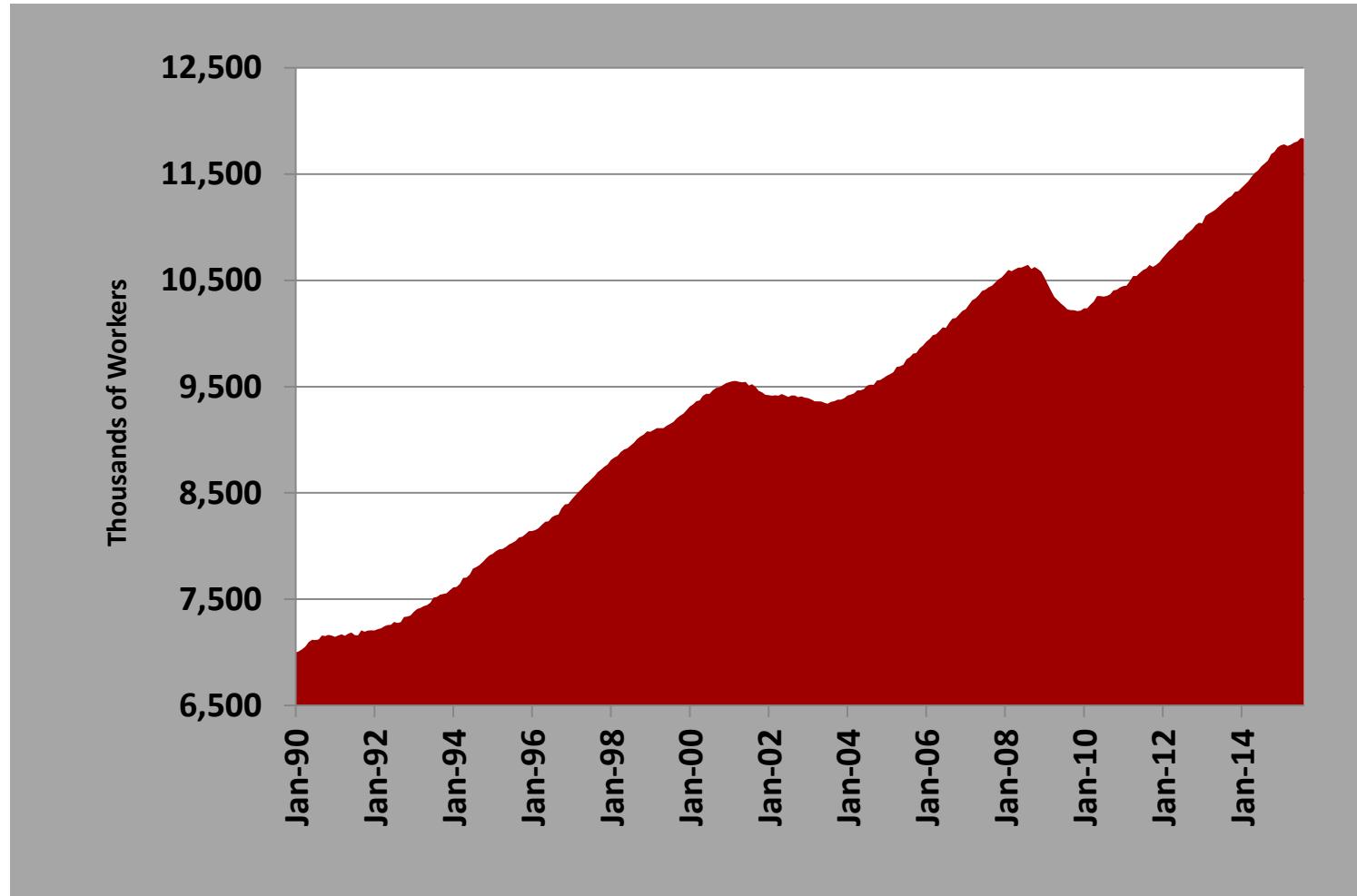
Job Openings in America

Looking for Workers

Total Job Openings	5,753,000
Construction	137,000
Manufacturing	342,000
Trade, Transportation, Utilities	1,018,000
Professional & Business Services	1,331,000
Education & Health Care	1,030,000
Leisure & Hospitality	770,000
Government	486,000

Source: Bureau of Labor Statistics
BLS release on September 9, 2015

Total Texas Non-Farm Employment



Source: Federal Reserve Bank of Dallas

The Texas Index of Leading Indicators

Texas Leading Index

Index, 1987 = 100*



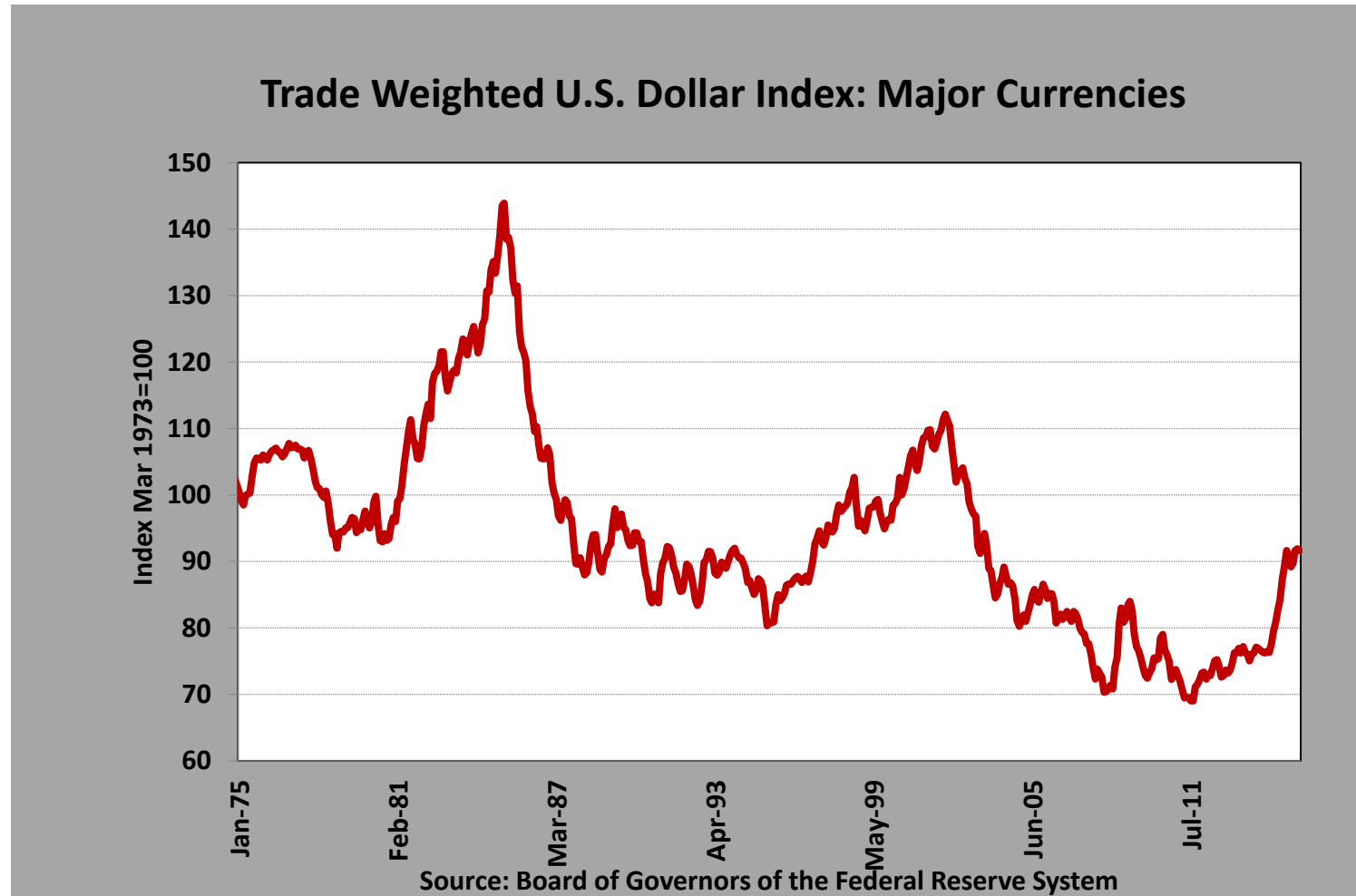
*Monthly, seasonally adjusted.

Last data entry July 2015.

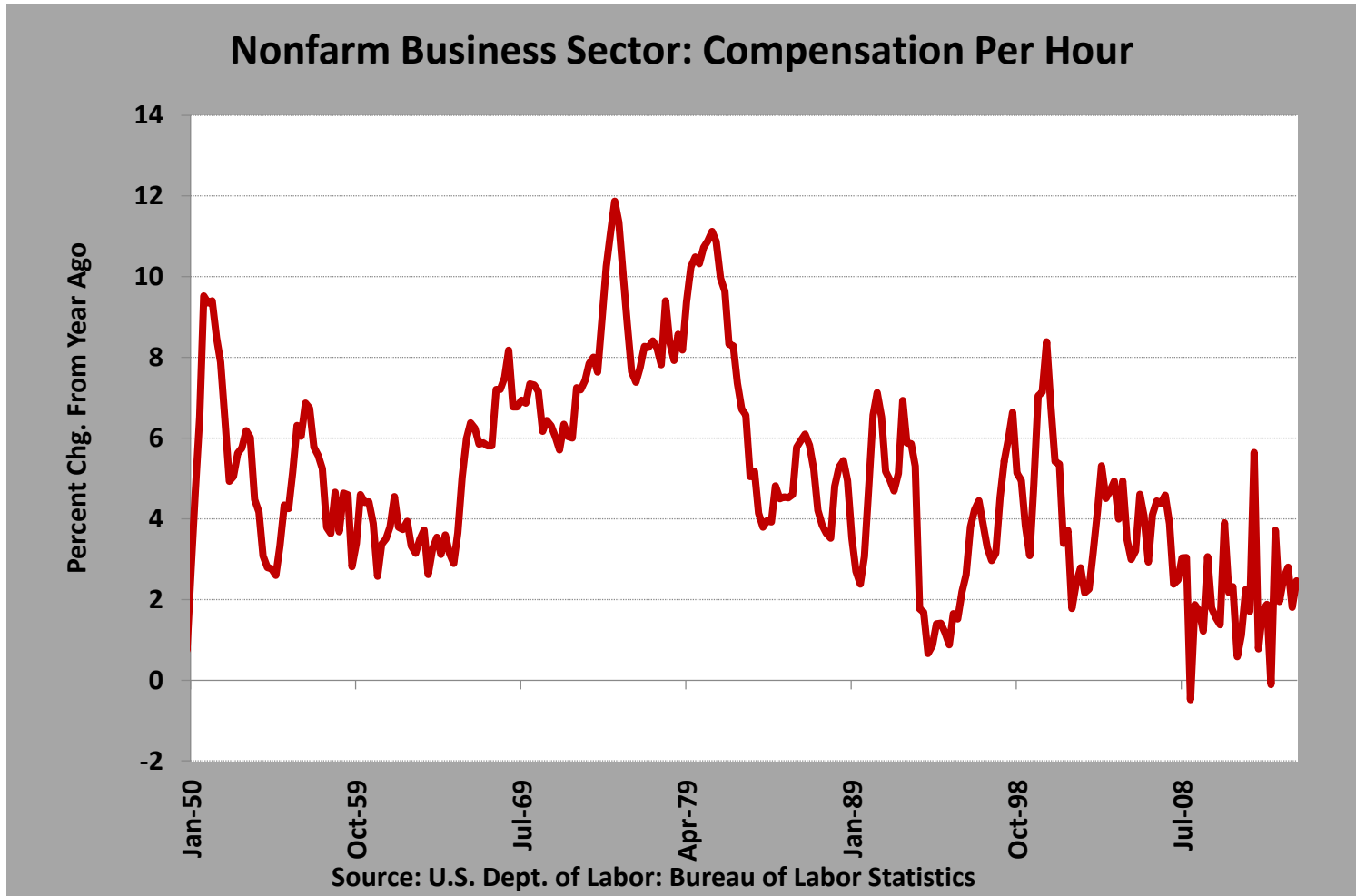
SOURCE: Federal Reserve Bank of Dallas.

Inflation Outlook and Interest Rates

Trade Weighted Exchange Index: Major Currencies

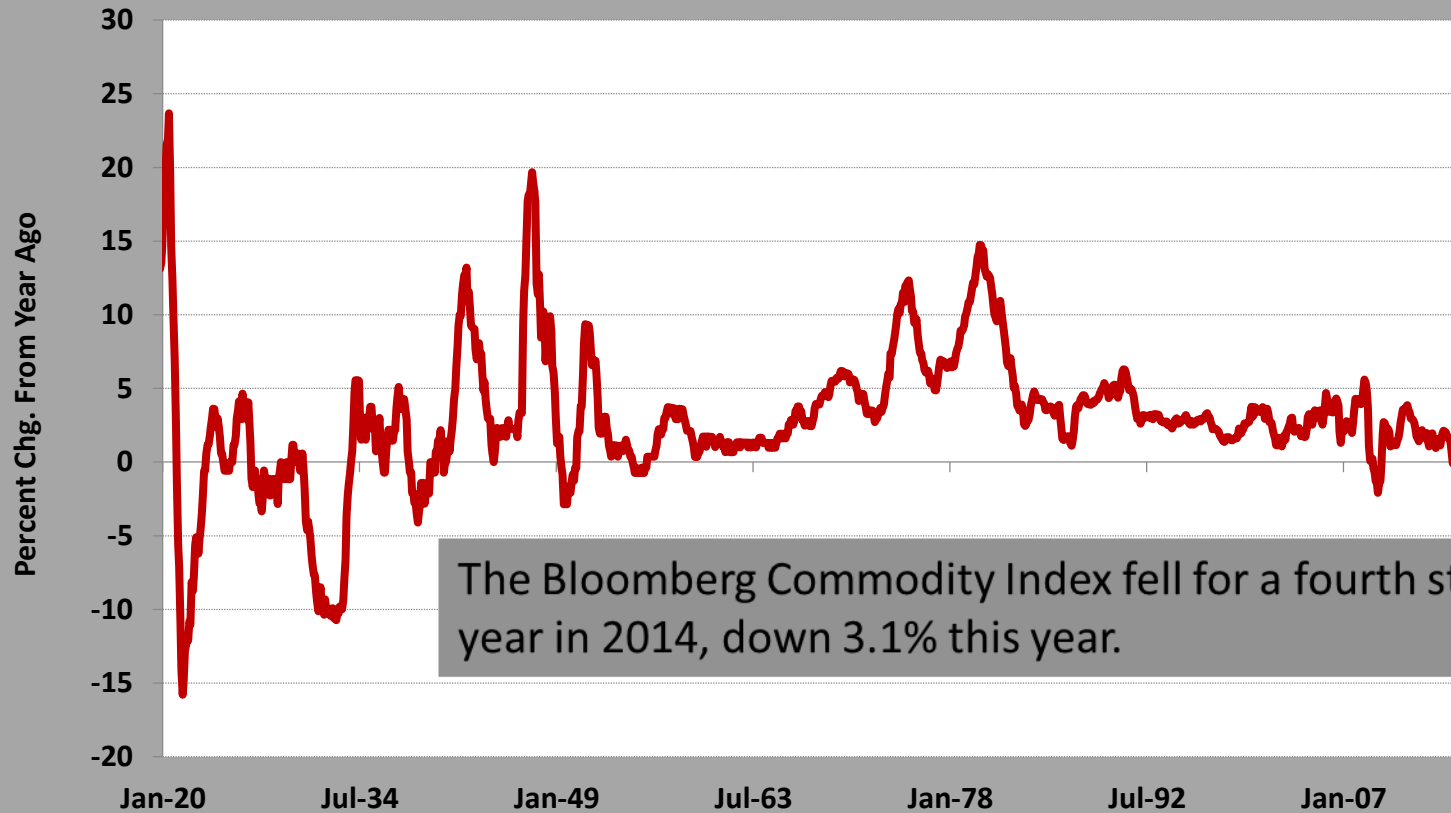


The Economy: Wage Rates Increase Slowly



Inflation Rate: CPI Remains Low

Consumer Price Index for All Urban Consumers: All Items



Source: U.S. Dept. of Labor: Bureau of Labor Statistics

The 10-Year Treasury Rate: Other Countries Even Lower

- U.S. 10-year 2.03
- Italian 10-year 1.73
- Spanish 10-year 1.89
- Swedish 10-year .71
- French 10-year 1.00
- German 10-year .59
- Japanese 10-year .32
- Swiss 10-year **-.17**

Rates on October 1, 2015

The Investment Environment

Our federal government continues to have no ability to encourage business expansion through fiscal policy.

Monetary policy continues to do its job:

MAKE RICH PEOPLE RICHER
BY INFLATING THE PRICE OF STOCKS, BONDS AND REAL ESTATE

The Investment Environment

Bond prices at record highs

Stock markets at record highs

Margin debt in the stock market at record highs

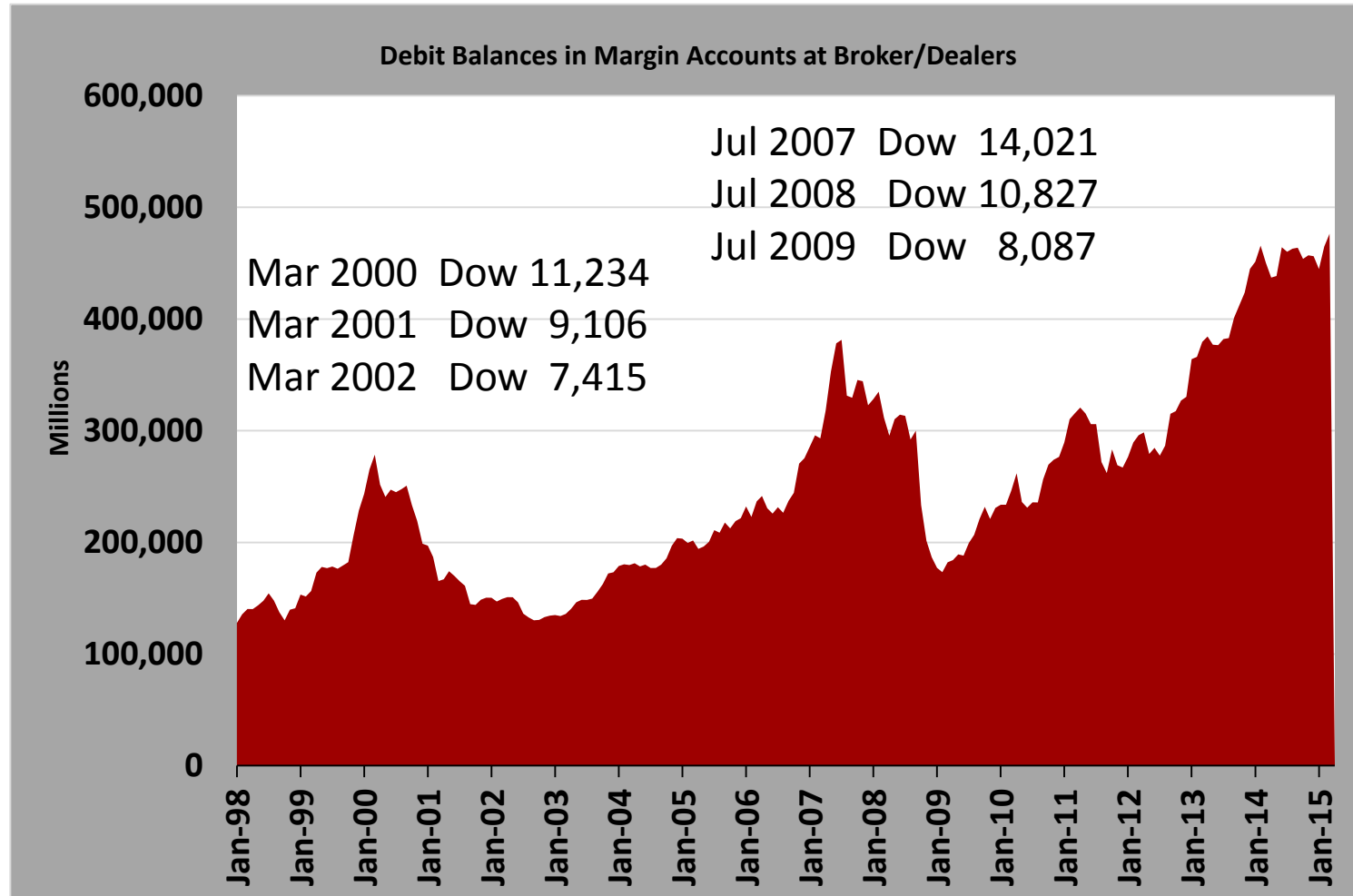
Commercial real estate values at record highs

Even more money is ready to pour into CRE

CMBS underwriting standards getting “more aggressive”

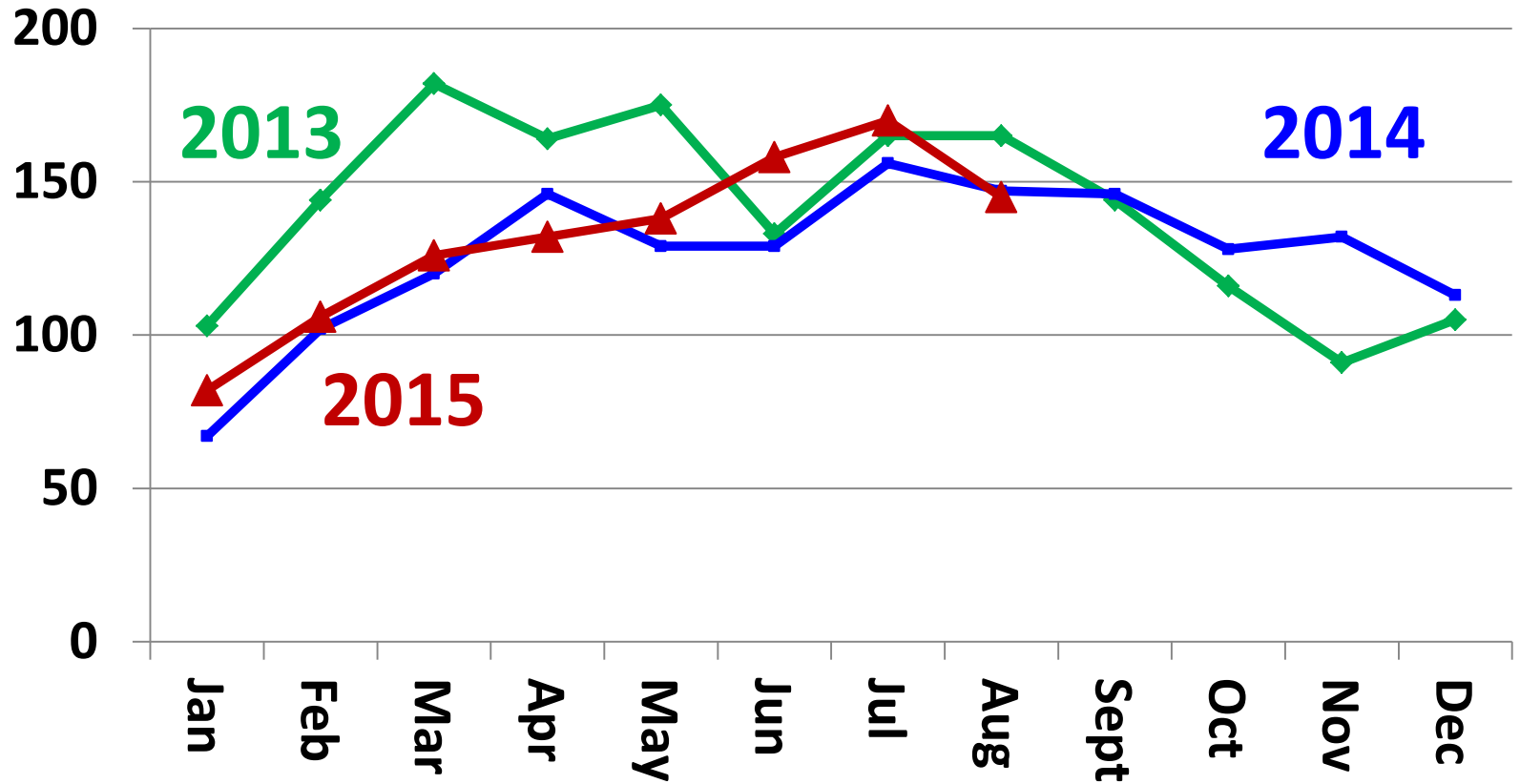
Margin Debt

Debit Balances at Broker/Dealers



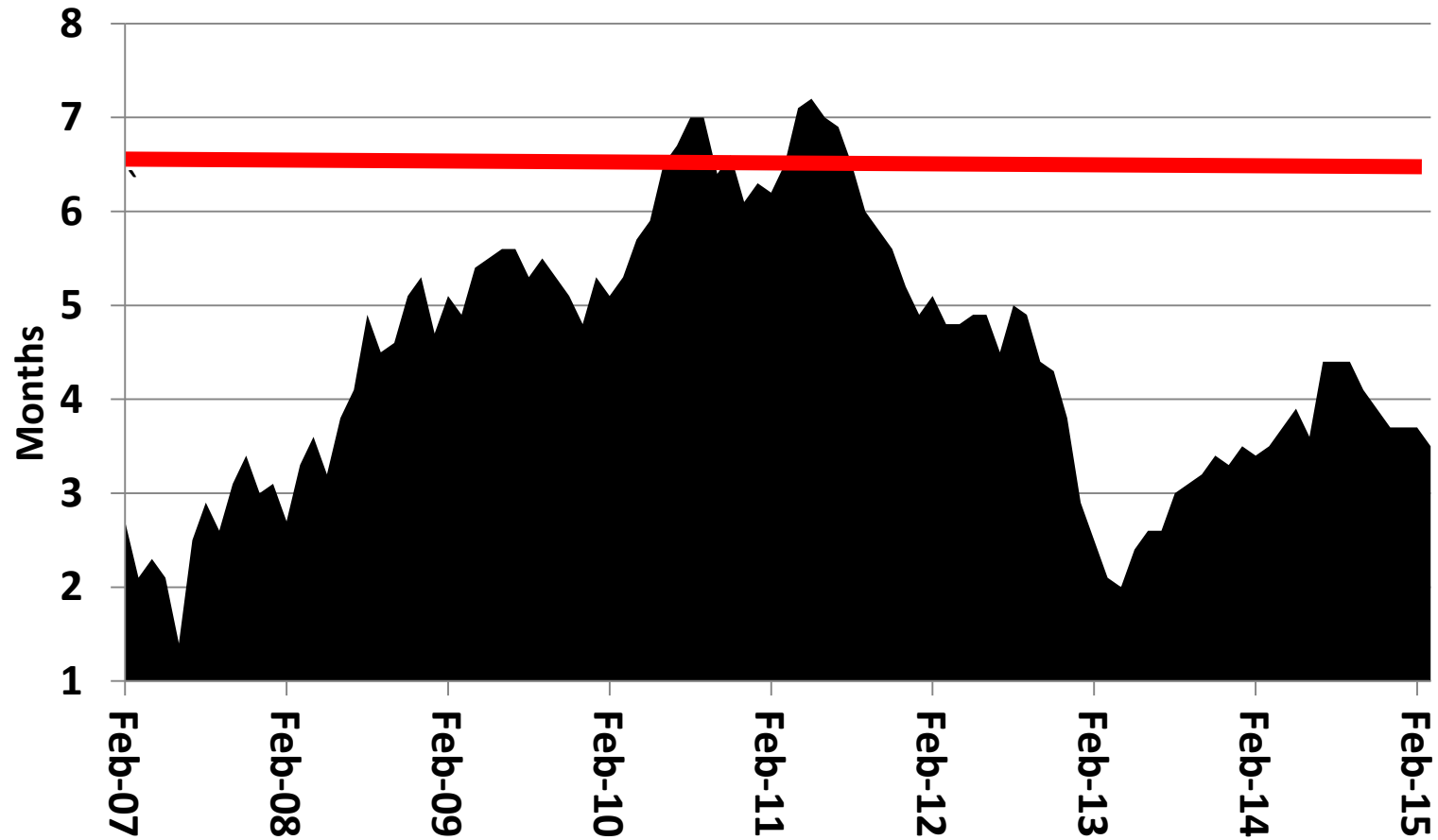
Source: Standard and Poor's/Haver Analytics

Existing Home Sales San Angelo



Source: Real Estate Center

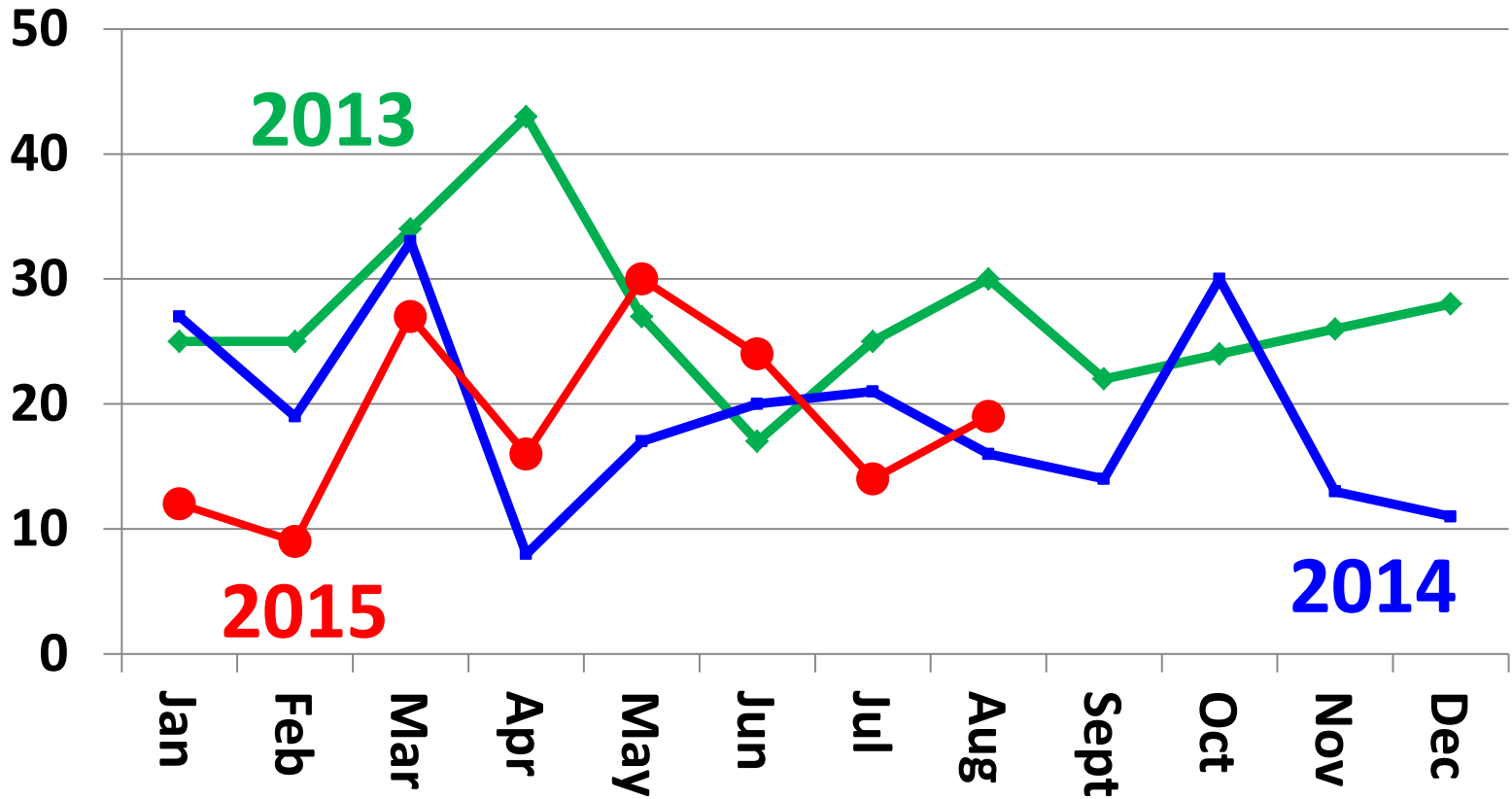
Inventory of Unsold Homes San Angelo



Jan. 2007 to present

Source: Real Estate Center

Single-Family Building Permits San Angelo



Source: Real Estate Center

Median House Price in San Angelo

August, 2011	\$116,900
August, 2012	\$131,800
August, 2013	\$146,700
August, 2014	\$162,400
August, 2015	\$160,000