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Special Coronavirus Market Update

SAN DIEGO ECONOMY

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IS IT 1929 – THE GREAT DEPRESSION? I THINK NOT. IS IT VERY SERIOUS? ABSOLUTELY.

First, and foremost, we have to look at the National economy.

From the time of The Great Recession, we have gradually moved from a production economy to a service economy. In 1929, 39% of all non-farm jobs were in manufacturing. In 2019, it was 9%.

Thus, in 2020, as manufacturing jobs fall due to reduced demand and the lack of new materials from other parts of the world (especially China), it is hurting the economy. But, it will not destroy it as it did in 1929.

Manufacturing is something that can only function inside a factory environment.

Employment by Industry (000) (1)
United States
1929 & 2019

Category	1929		2019	
	No.	%	No.	%
Manufacturing	**10,659**	**39%**	**12,827**	**9%**
Government	2,676	10%	22,528	15%
Other	13,743	51%	114,927	76%
Total	27,078	100%	150,282	555%

(1) Excludes farm employment
Source: BLS

Today, the majority of our professional jobs can be conducted at home on computers and by phone. Our offices may be empty, but business continues as usual telephonically and electronically.

Will there be a recession? Yes, but not severe. Nothing like 2008-2009. Recession by Federal definition is two quarters with no increase in gross domestic product (GDP). By that standard, we will have a recession. But there is a difference between a recession and a disaster.

Economic Factors: The Last Recession and Today in the United States

There is an enormous difference between 2008 and today.

First, the industrialized countries of the world are in far better shape than in 2008 and have reacted incredibly fast to this malaise. The U.S. economy is also in much better shape than it was in 2008, as shown in this exhibit.

Economic Factors
The Last Recession and Today
United States

Category	Dec 2008	March 2020
Employment		
Unemployment Rate	**6.8%**	**3.6%**
Initial Claims - Monthly Unemployment Claims	587,000	277,000
Job Openings (1)	3,059,000	7,000,000
Interest Rates		
10-Year T-Bill	**4.7%**	**1.0%**
Fed Fund Rate	**2.0%**	**0.0%**
Mortgage Rate - 30 Year	**6.14%**	**3.60%**
Mortgage Rate - 15 Year	**5.73%**	**2.77%**
Real Estate		
Foreclosure Filings (Annual)	2,330,483	624,753
ExistingHome Sales (monthly)	343,333	445,000

(1) Job openings are anticiipated to declline in the near future

In September 2008, when Lehmann Brothers went under, the Feds, including the White House, were completely unprepared to act. They did little until it was too late. In 2008, the financial world was in complete disarray worldwide. The proliferation of "liar loans" created a totally unstable market which totally collapsed and rightly so. Now our banks are structurally sound, though their branches may shorten their hours. Since the Depression, banks may not close more than three days in a row.

And mortgage loans and lines of credit are readily available. Lenders have to get their money out in order to generate profits. And they are deluged with cash because Americans have been saving at a much higher rate than at the time of the last recession.

This time, reaction has been swift, nationally and internationally. The Feds did not hesitate to drop the Fed Funds rate to effectively zero. And they have put in place a number of programs to assist small business and low income households who may lose their jobs. For instance:

- The Department of Housing and Urban Development is suspending all foreclosures and evictions until the end of April for HUD properties.
- The Federal Housing Finance Agency announced that it is directing Fannie Mae and Freddie Mac to suspend foreclosures and evictions for at least 60 days for enterprise-backed mortgages.
- The Secretary of the Treasury announced a 90 day extension for any federal taxes due - from April 15 to July 15.

The San Diego Economy

We are blessed. We have an enormous military and governmental presence in San Diego County. And manufacturing is 7% of our jobs. Many of those jobs are manufacturing equipment for the military.

Military and non-military government employment account for another 22% of our economy; 12% health care and 9% for professional, scientific and technical jobs. That means that half of our jobs are very stable and most probably affected little at all by the virus except for the logistics establishing remote work setups and covering for people who get sick. Thus, half of our jobs are stable.

Civilian Employment by Industry (000) (1)
San Diego County
2019

Category	2019 No.	2019 %
Manufacturing	**116,400**	**7%**
Government	249,600	**15%**
Military in Uniform	110,000	**7%**
Health Care	189,100	**12%**
Professional, Scientific & Technical	148,800	**9%**
Support Jobs	797,100	**49%**
Total	1,611,000	**100%**

(1) Excludes farm employment & military in uniform
Source: BLS

Which Sectors of Support Jobs Will be Hurt Least?

In 2009 the unemployment rate for those with college degrees was 9%. Now it's 2%.

There are several: health care, education, the military, government employment, software firms, information systems, utilities, transportation and some financial activities, including lenders, stockbrokers and financial advisors. Most professionals like attorneys, accountants and engineers should weather the storm fairly well unless this plague goes on much longer than I think it will.

The big difference between the last recession and this one is connectivity. In 2008, we were just beginning our romance with on-line connectivity. Now, most professionals can work at home and have conferences with Skype and Facetime and can really live without going into the office. They may not be as productive as they have to look after their kids, but it's manageable.

Which Sectors of Our Local Economy Will Be Hurt?

Some sectors of the economy will be hurt, particularly tourism and the big three R's: retailing, restaurants and real estate. Still others will get some benefit particularly anything that can be delivered to your home.

Tourism & Travel

Tourism and travel will take the biggest hit by far. San Diego is the destination for 35 million visitors each year. They stay in our 55,000 hotel rooms, dine in our restaurants, take cruises from our port and inevitably visit the now closed Zoo, SeaWorld and Legoland. The thousands of service people employed in this sector will be hit hard.

The San Diego Economy

Retail Business

Part of the GIG economy (Door Dash) and firms like Amazon will prosper because of their amazing delivery ability. The goods may not land on your doorstep within 24 hours, but they will get there. The GIG economy workers that rely on people transport (Uber, Lyft) may not fare as well if lockdowns go into effect and people cut non-essential travel.

Regional shopping centers, big box centers, movie theaters and other retail venues that rely on foot traffic will suffer the most.

Pointedly, people still want "things." Maybe not quite as many but they will shop on-line and wait for the doorbell to ring. There will probably be a surge in home cooking-related items.

Don't expect your usual selection of grocery goods since so many of them are imported from Mexico and South America and may be quarantined.

The jury is out on the automobile business. It is still unknown whether new and used car sales will suffer. Buyers may determine that it is a great time to strike a bargain and take advantage of near zero interest rates. On the other hand, many brands may not be able to deliver product because the parts come from countries that are shut down. It is probable that automobile dealers will turn to the Japanese model wherein the sales force brings a vehicle to your home for you to try out and buy. No showrooms.

Restaurants and Food Service

Restaurants that depend exclusively on dining-in will suffer (particularly those at the high end), but those that have delivery capacity and pick-up service will muddle through. The wait staff will suffer because many waiters, bartenders and others depend heavily on income from dining service tips.

Restaurants that are in regional-type centers will hurt the most because of the absence of foot traffic. Grocery stores, drug stores and other retailers of necessities will do just fine, maybe better than just fine, if they can fill their shelves.

Obviously, the supply chain is affected. The wholesalers that supply the restaurants and bars and tourism venues will feel the pain.

San Diegans are resilient. The hourly workers may change employers and industries, but they get employed. There continue to be a substantial number of job openings in this County for folks without a college degree.

The Unemployment Rate

During this sad time in our economy, I am projecting that the unemployment rate for college-educated persons will be 4-6%; however, for the non-degreed sector, unemployment will be in the 15-20% range.

And here is my take on Real Estate:

Construction

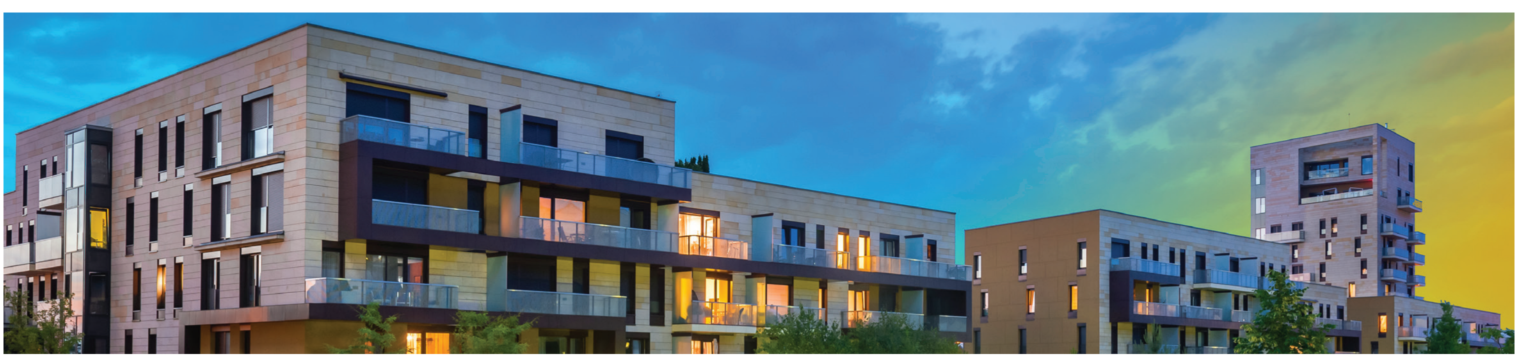
Construction, especially housing construction, is listed in the Federal critical infrastructure sectors so they are exempt from California's State Shelter Order.

Projects that are underway, especially high-rises (residential and commercial) and garden apartment projects will just keep on building as long as the materials are available. Apartment projects may be delayed because many of the kitchen and bathroom fixtures come from China. And some builders just may delay construction of new projects.

The new home and condominium sector has produced so little product that there is rarely any standing inventory. It's not as if there are hundreds of completed homes awaiting buyers. That is rare in this town. So sales may slow down, but they won't stop.

Several major homebuilders are considering closing their sales office and will show by appointment only. So the jury is out on whether new homebuyers will stay home, even though they are drooling over 3.0% loans and with homebuilders most willing to do buy-downs or pick up closing costs or toss in some landscaping.

We are uncertain about how this virus will effect pricing. Construction products made in the U.S. appear to be remaining stable, but those products made abroad may become more expensive due to supply shortage.The remodeling business should remain healthy and in this County, about 40% of all construction dollars are in remodeling rather than new construction. With home equity loans readily available, home remodeling is very tempting.



The Apartment Market

The apartment market has been in a remarkably positive market for the past 6-7 years, at least as far as owners go. Occupancy rates have been 95%+ and rents have been rising.

I suspect that will change very soon, but more so in the lower rent segments as vulnerable employees get laid off and can no longer afford their apartments. They may double up or move back in with their parents, but, in either event, vacancy rates will rise. And there is scant chance that rents will rise during the virus months.

There probably won't be a lot of foreclosures of apartment projects because the leverage in this County is fairly low and a substantial part of the inventory has no debt (often folks who have owned their units for decades). "B" and "A" quality projects will muddle through though they will be forced to offer give-aways.

Like the new home market, there has been little overbuilding in the apartment sector, except in downtown San Diego. The only glitch is that the local governments may invoke "no eviction" actions which I interpret as meaning that if someone doesn't pay their rent, you can't kick them out. That could be devastating for landlords. Lenders may be lenient.

The Existing Home Resale Market

This remains a puzzle. From a pure economic perspective, demand for resale homes remains strong. We have a population that wants to own homes or trade up their existing homes or trade down their existing homes and can afford to do so. The millennials are seething to buy a home. They are tired of renting apartments for amounts that are equivalent to mortgage payments. They want a tax write-off. They want a place to raise a family. That desire is not going away. Last year, SDAR members sold 33,000 homes. The median single family home price was $650,000 and the attached home price $428,000. Not cheap, but affordable by many.

The real problem is inventory. There isn't much out there to sell. The question arises: will homeowners who were going to sell their homes take them off the market? We don't know that yet. We don't know the thought process at this point in time. Do owners think that prices will accelerate after the virus subsides. Or do they think there are no buyers out there now? Or they don't want to have open houses? Or they can't find something else to buy? Or all of the above.

Are there soft spots: yes, the upper end of the market will be sluggish, but not moribund.

And lenders may be a little more fussy on requiring reserves.

The Solution:

It sounds to me like there needs to be a major campaign that lets potential sellers know that there are willing and able buyers out there and they are not being put off by the virus.

Right now there is a disconnect between sellers and buyers and it is imperative for our industry to re-connect them. It's time for virtual caravans and virtual open houses. It's time for creative marketing.

This is what I suspect:

- The major REALTOR® brands will come up with major media programs for their agents.
- There will be virtual prospecting, actively engaging on various social media platforms.
- Full-time agents will do OK and the agents that sell one or two homes a year will drop out of the market, leaving more sales for the full-time agents.
- Full-time agents will work harder and maintain their usual incomes.
- Buyers with wisdom will recognize that this is a very good time to buy. They remember the generous returns they or their friends earned when they bought in 2008-2009.
- Buyers with wisdom recognize that San Diego remains one of the strongest economies in the Nation and that when it bounced back, it does so with vigor.

Final Thought

Not to be too cynical, but the President can use this tragedy to show that he can be a leader, and therefore be worthy of a second term. This President doesn't like to lose.

This virus is not going away anytime soon; therefore, it is imperative that you develop new, different and inventive strategies to sell your product. The demand is there; you just need to access it effectively.

Connectivity will help us weather the storm.

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