

The Great Recession & the Real Estate Market

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I. Importance of Construction & Real Estate

2008 % GDP	Construction	Δ (2008 – 2007)	Residential	Δ (2008 – 2007)
Spain	16.6	-1.3	8.0	-1.3
Euro Area	12.2	-0.1	6.1	-0.2
Greece	10.7	-2.0	5.4	-2.4
UK	9.8	-0.8	3.5	-0.5
USA	9.6	-0.7	3.4	-1.2

Source: European Commission, Federal Reserve

1. GDP ↑ without an increase in inflation

- ⇒ **disposable income** ↑
- ⇒ **demand for RE** ↑
- ⇒ **RE prices** ↑

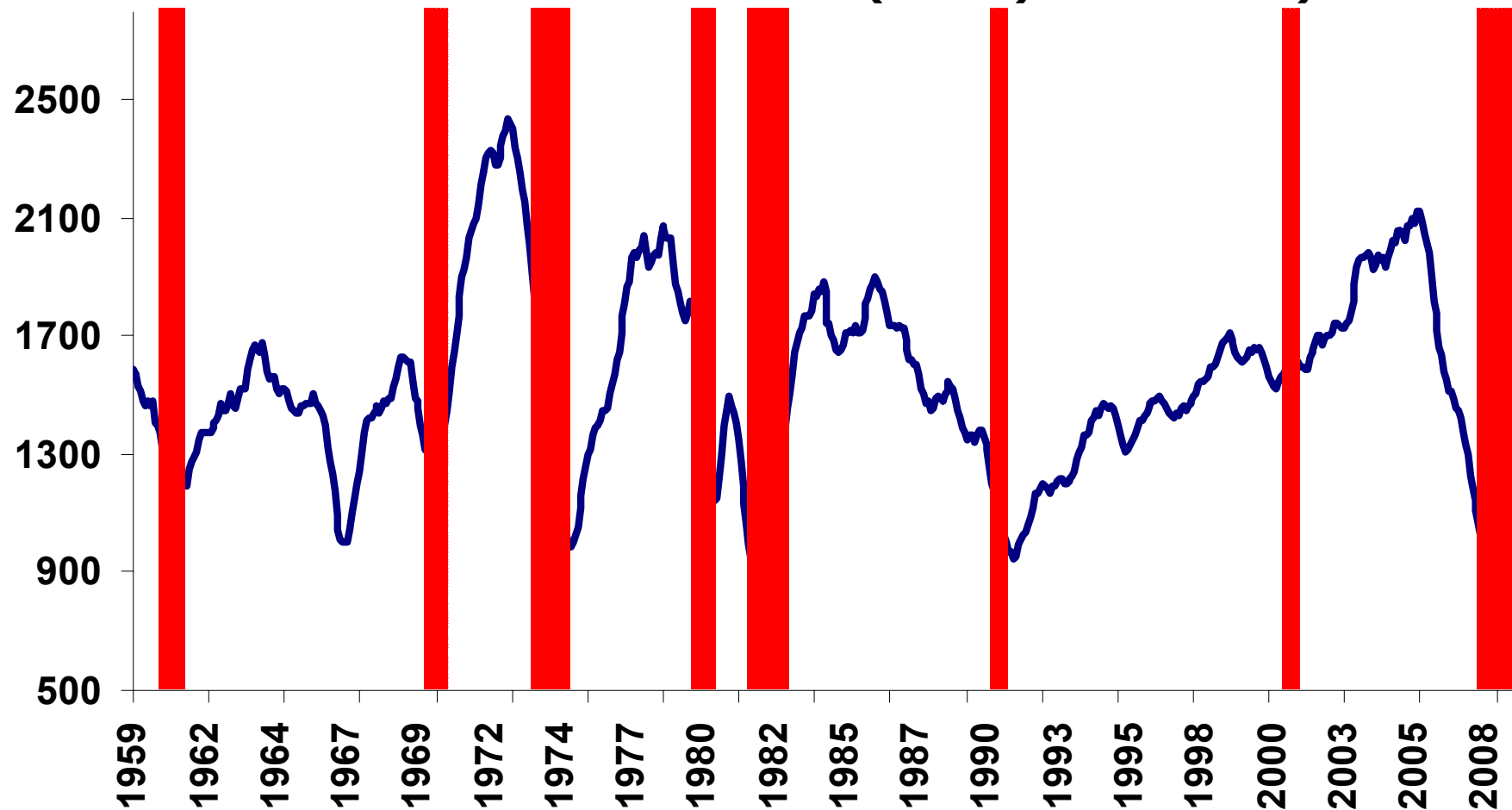
2. RE prices ↑, expectations ↑

- ⇒ (i) **Investments ↑ Employment ↑**
 - ⇒ (ii) **Wealth ↑ ⇒ Consumption ↑**
 - ⇒ (iii) **Loosening of credit standards ⇒ acceleration of investment & consumption**
- (i)-(ii)- (iii) ⇒ GDP ↑**

I. Investment in Residential Construction as a leading indicator of the economic cycle in the USA

Housing Starts

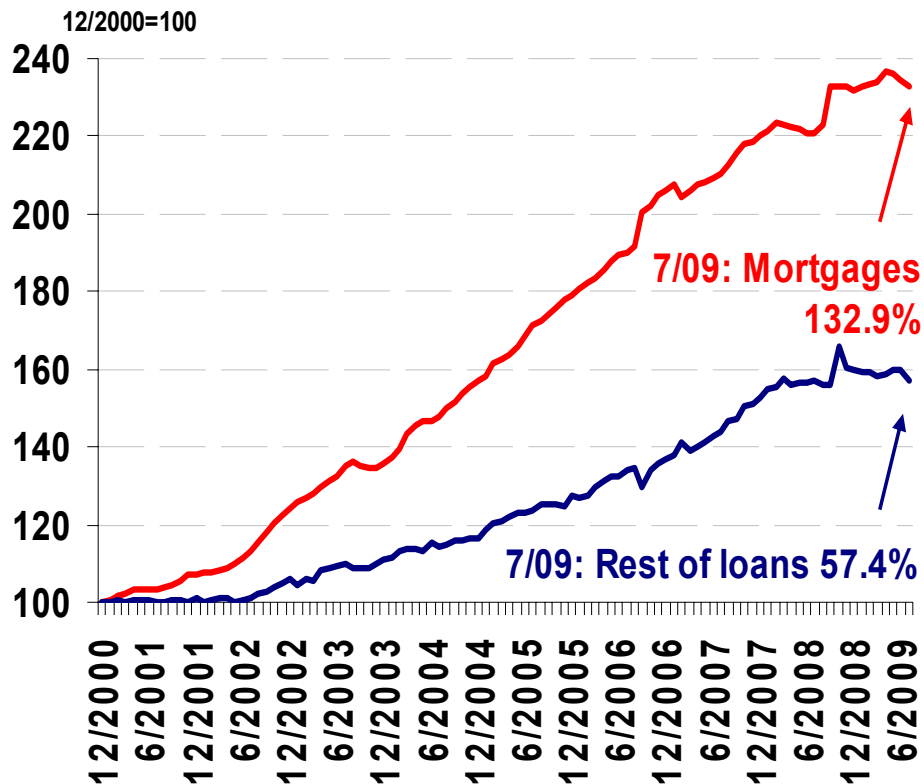
(thousands of houses, 6 month moving average, shaded areas indicate US (NBER) recessions)



Source: Federal Reserve

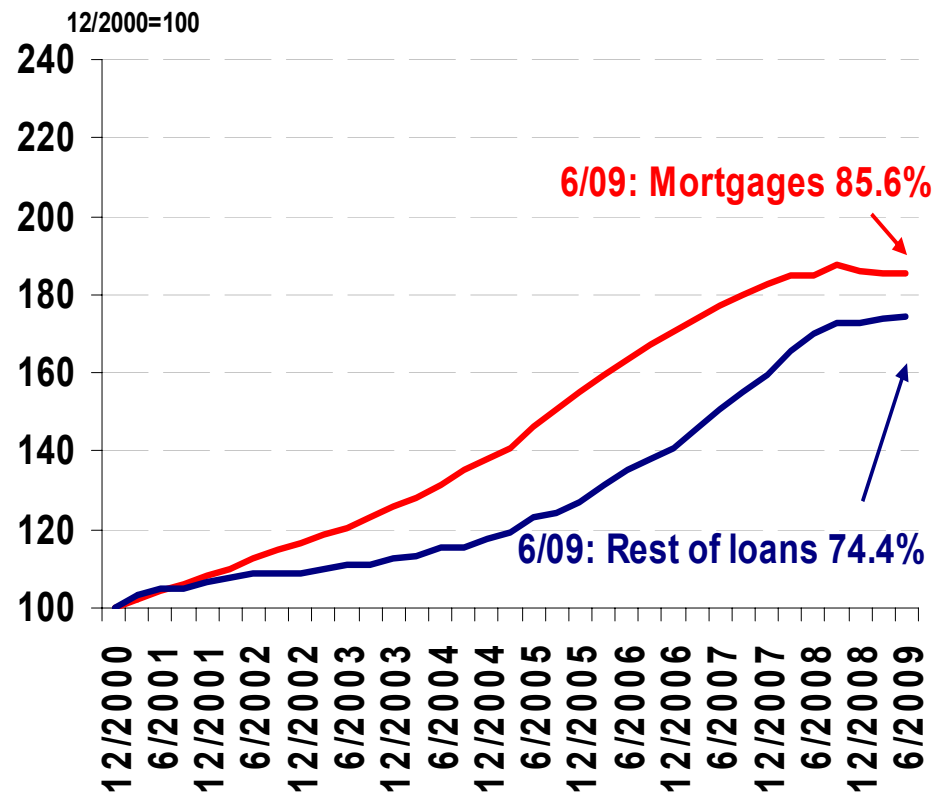
I. A rapid rise in mortgage credit expansion prior to the Great Recession

USA



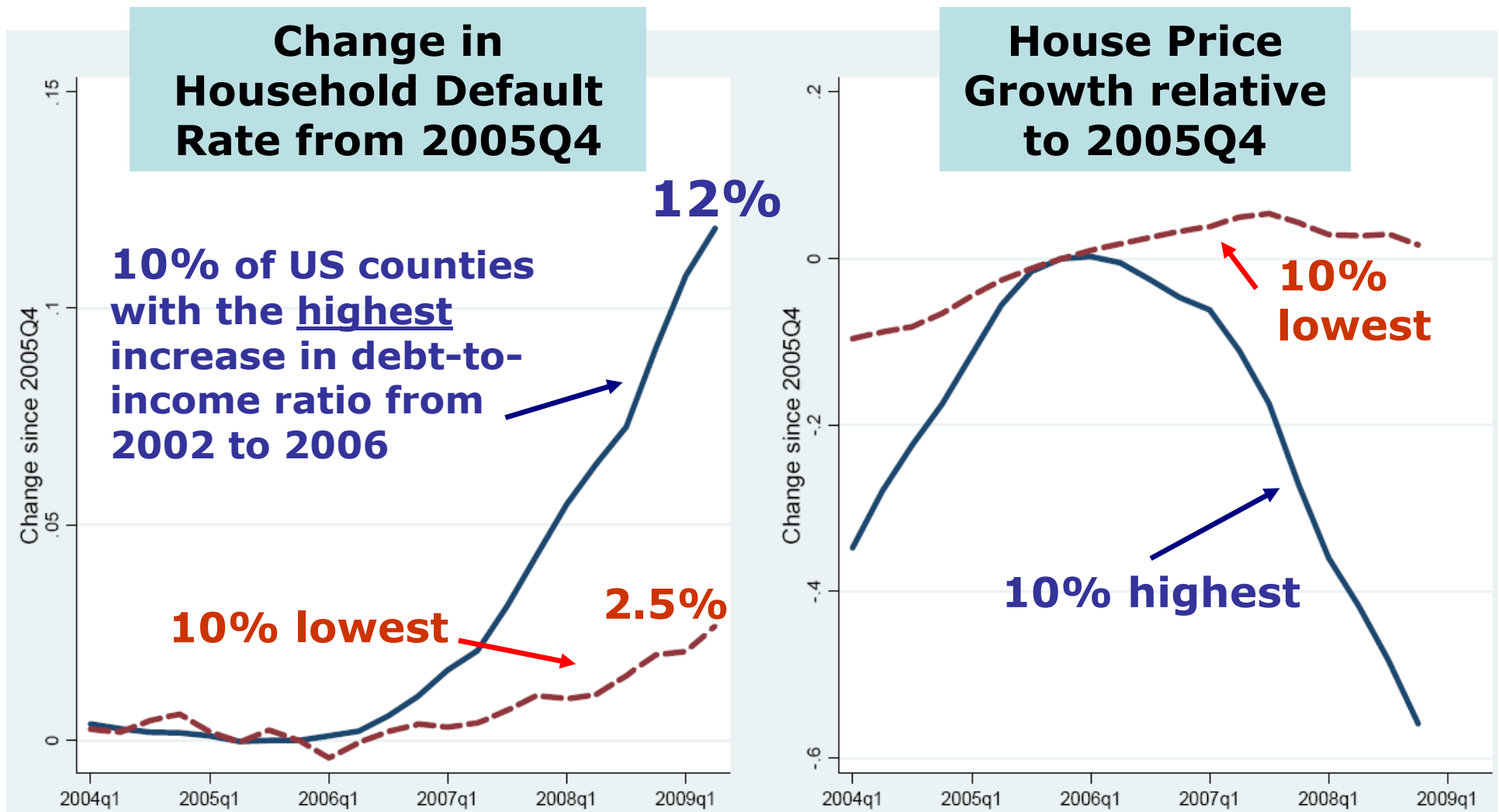
Source: Federal Reserve

EURO AREA



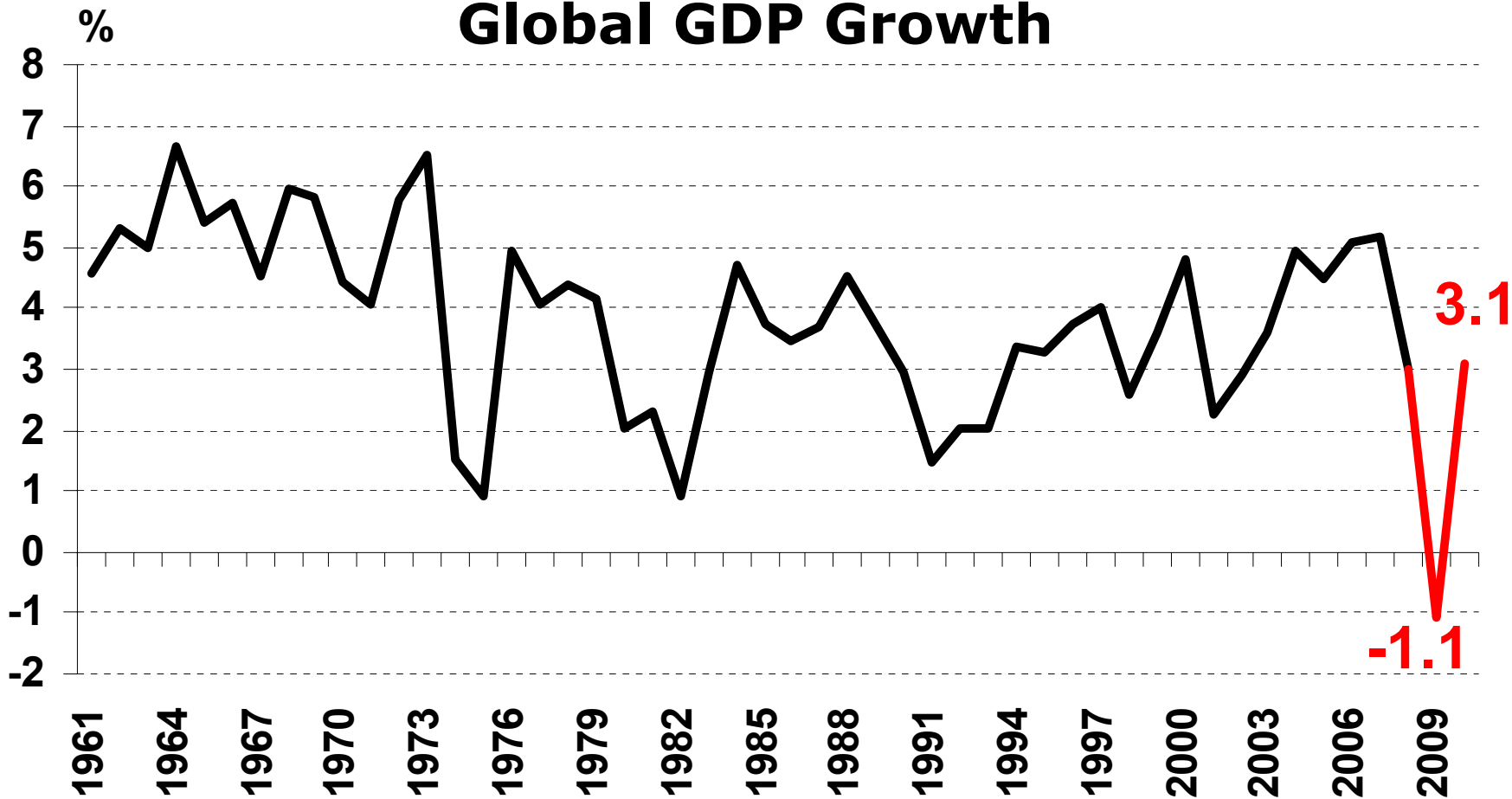
Source: ECB

I. The causal role of household leverage flushed out by a US cross-county analysis



Source: *Mian & Soufi*, *Un. of Chicago*, August 2009

I. The Great Global Recession

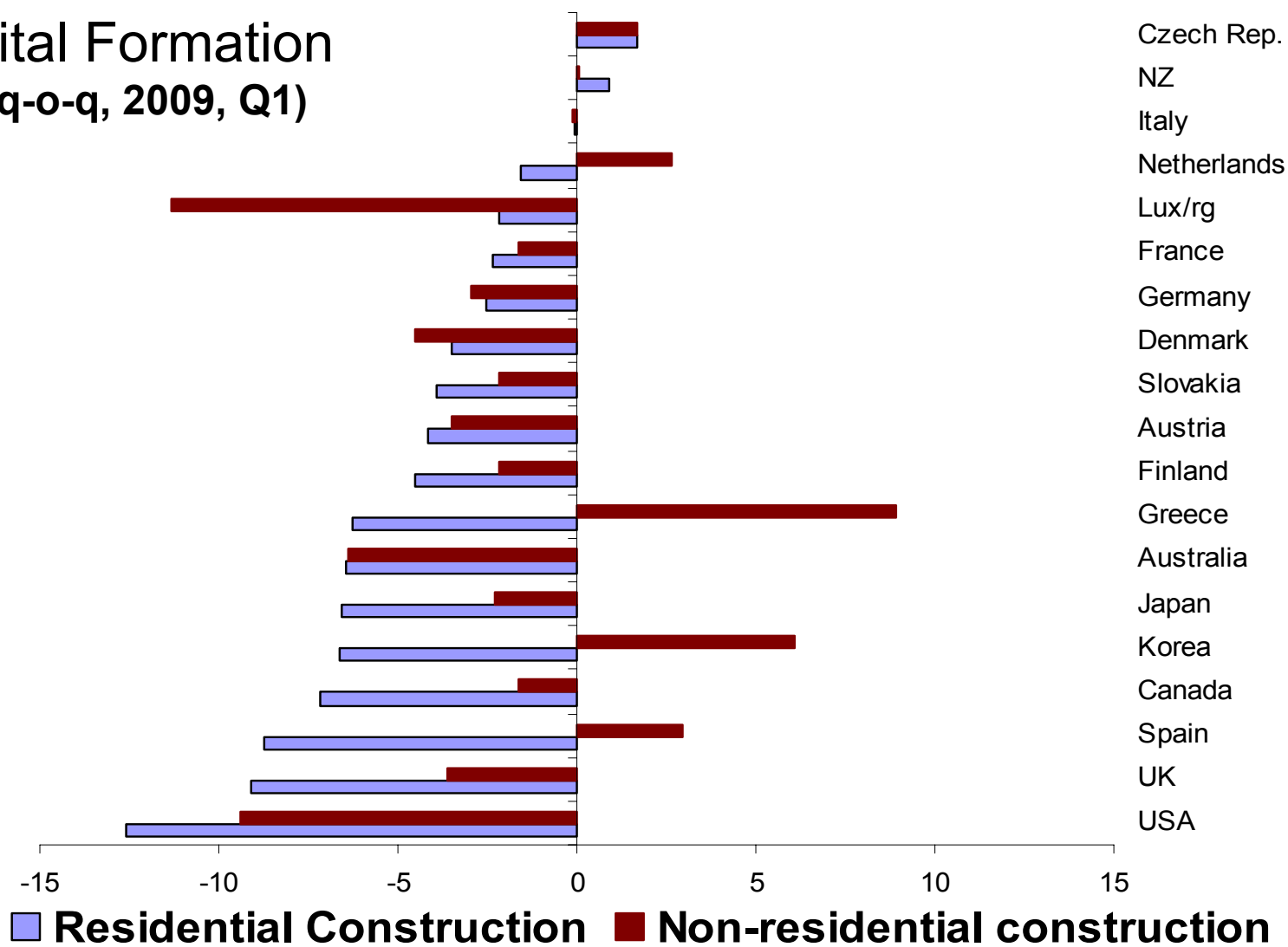


Growth in global market GDP in real terms

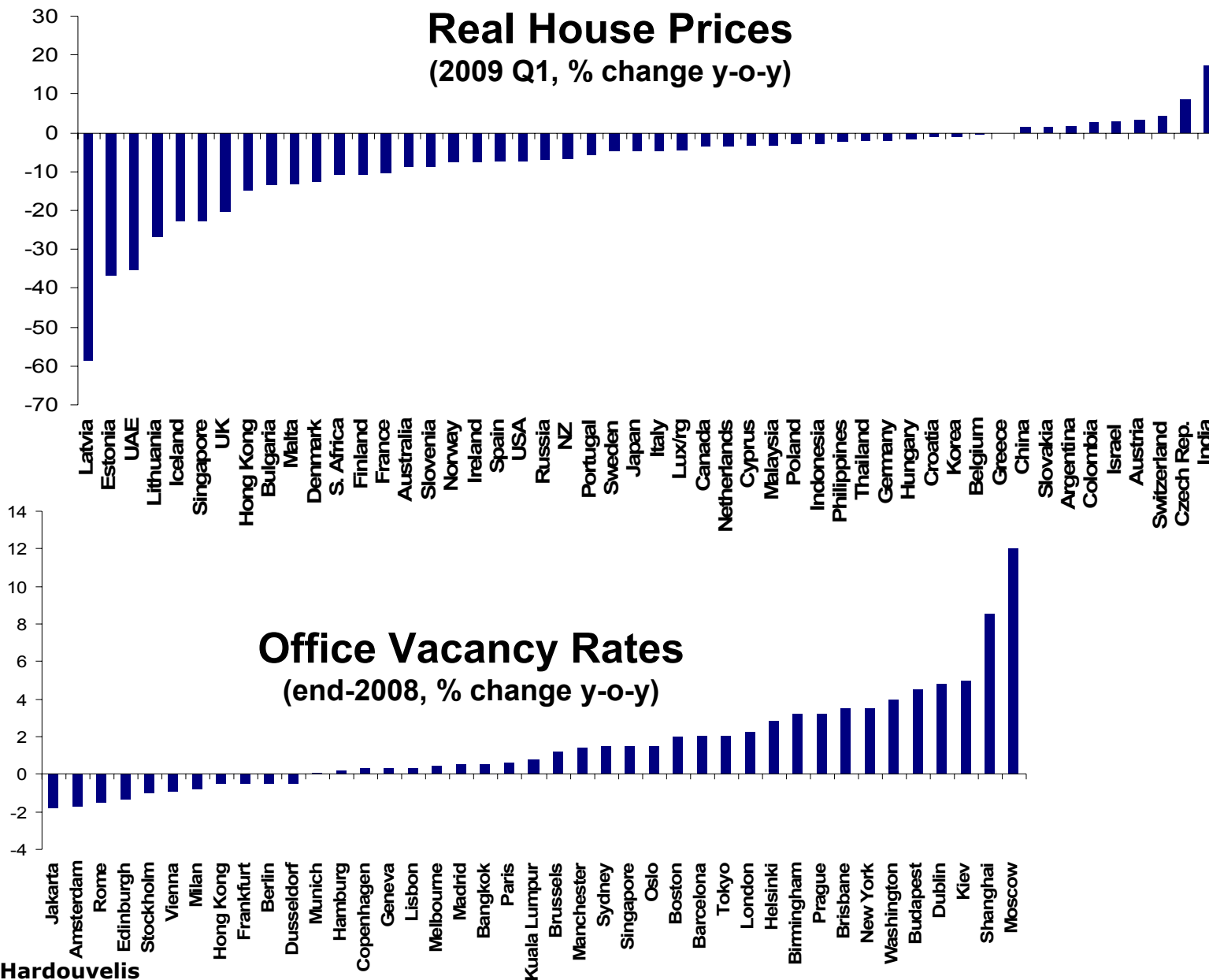
Source: IMF, World Bank

I. Construction investment down

Gross Fixed
Capital Formation
(%, q-o-q, 2009, Q1)



I. The fall in real housing prices and in commercial real estate is worldwide



Source: IMF

II.

IS THE FINANCIAL CRISIS OVER?

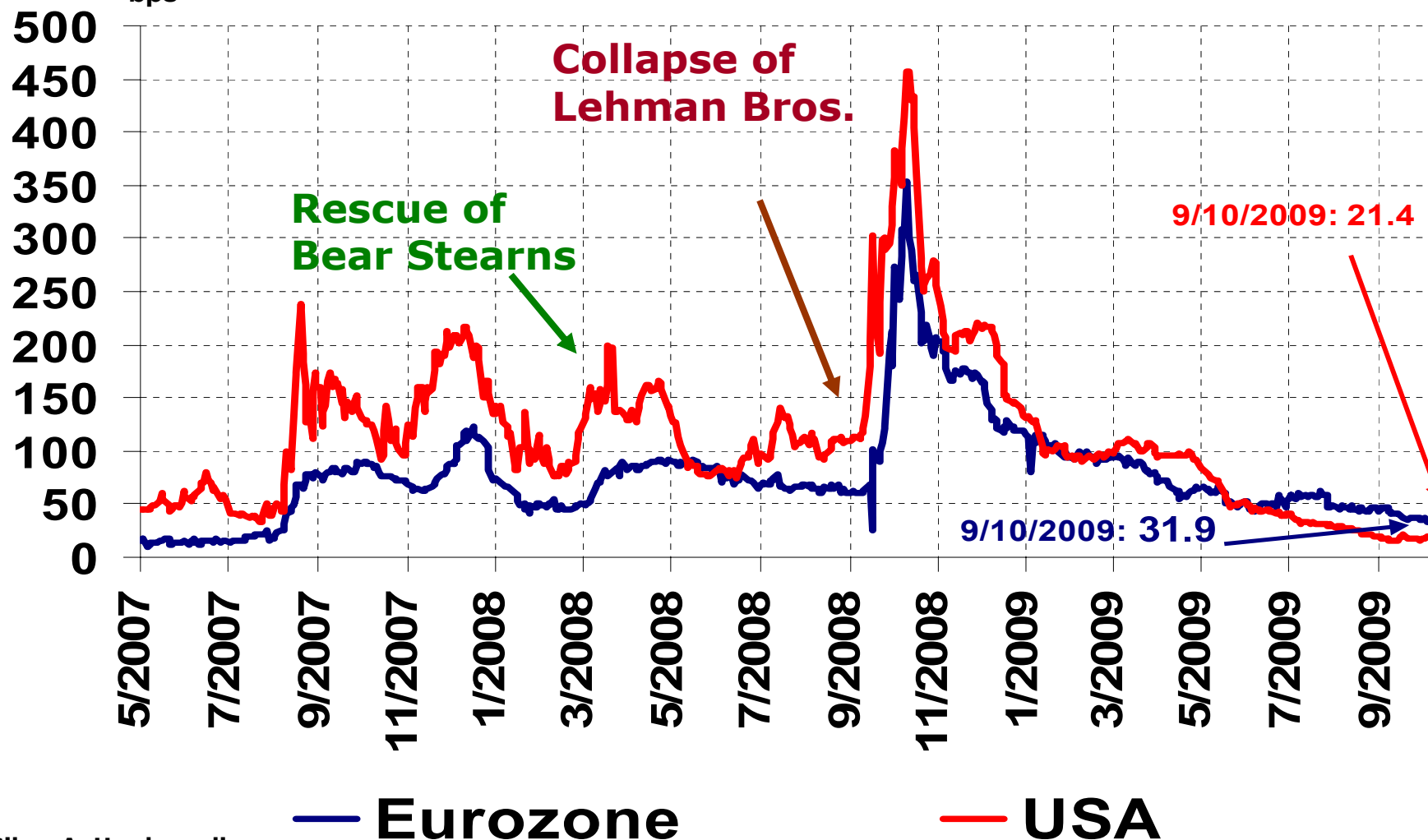
*“From the future of capitalism
to the future of capital requirements”*

What a difference 6 months have made in our discussions!

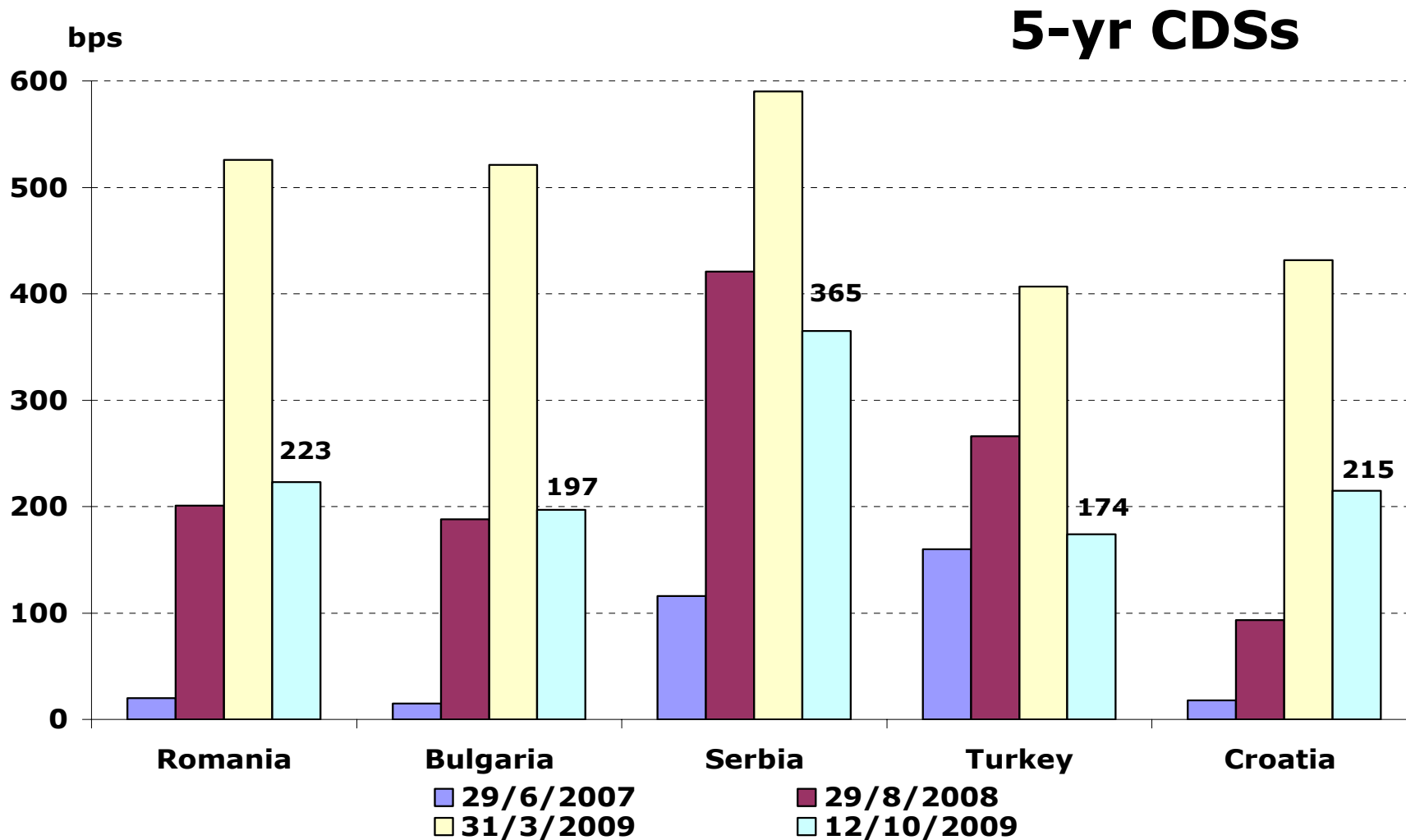
The Economist, October 3-10, 2009

II. The fear of financial collapse is now a distant memory

- ✓ US TED spread, 3m Eurodollar - 3m Tbill, points to an increase in **default premia** and a **flight to quality**
- ✓_{bps} Same is true in the Euro Area (3m Euribor – 3m Euro Area Tbills)

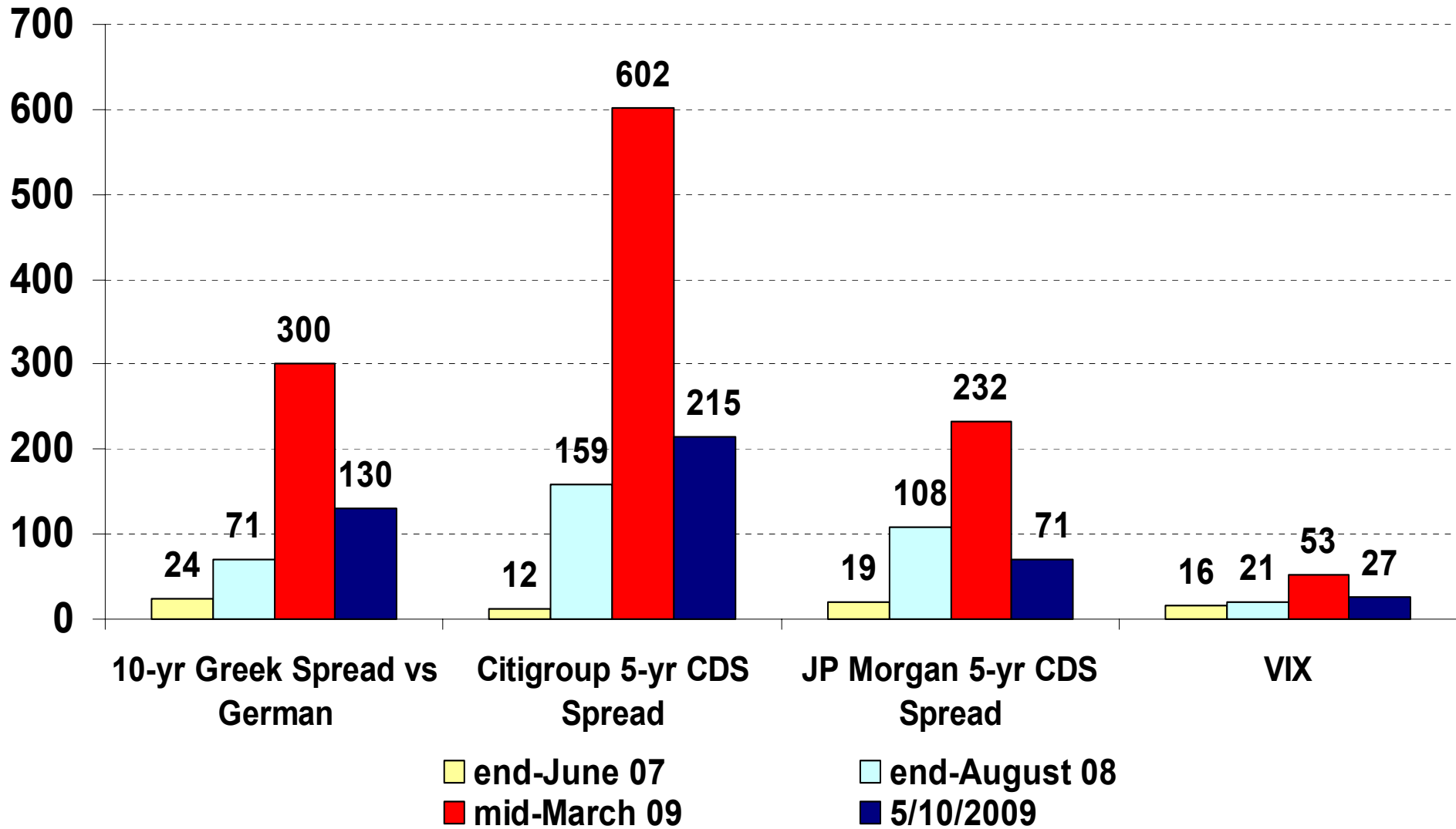


II. Risk premia down but not at pre-crisis levels



Source: Bloomberg

II. Risk aversion down but not at pre-crisis levels



Source: Bloomberg

II. Recession is ending

- ✓ **Different views on the robustness of recovery, yet ...**
- ✓ **Worries of a W-shape recession seem to subside**

OECD Real GDP Quarterly Projections (2009)

	Q1 09	Q2 09	Q3 09f	Q4 09f
US	-6.4	-0.7	1.6	2.4
Eurozone	-10.0	-0.4	0.3	2.0
Germany	-14.0	1.2	4.2	1.8
France	-5.6	1.2	1.6	1.9
Japan	-13.2	2.4	1.1	-0.9
UK	-9.6	-2.8	-1.0	0.0
Canada	-6.1	-3.2	-2.0	0.4

Source: OECD quarter-on-quarter annualized GDP forecasts

II. October 2009 forecasts

	2009f		2010f			
	INF	GDP	INF	GDP	ΔINF	ΔGDP
US	-0.5	-2.6	1.9	2.4	2.4	5.0
Euro Area	0.4	-3.9	1.2	1.0	0.8	4.9
Japan	-1.1	-6.0	-0.6	0.8	0.5	6.8
China	-0.6	8.3	2.7	9.4	3.3	1.1
Brazil	4.3	0.0	4.4	3.8	0.1	3.8
Russia	11.8	-7.9	9.8	2.5	-2.0	10.4
India	7.5	5.5	5.5	6.3	-2.0	0.8
Greece	1.0	-1.0	1.7	-0.3	0.7	0.7
Ukraine	16.5	-12.0	13.5	1.0	-3.0	13.0
Poland	3.2	0.9	2.5	1.8	-0.7	0.9
Bulgaria	4.5	-6.3	2.8	-2.0	-1.7	4.3
Romania	5.5	-7.5	3.8	-1.0	-1.7	6.5
Serbia	8.0	-4.5	7.0	0.5	-1.0	5.0
Turkey	6.0	-6.0	6.5	2.0	0.5	8.0

III.

**HAS THE REAL
ESTATE MARKET
BOTTOMED OUT?**

III. Previous crises in RE markets: Duration and cost*

Comparison of Current Housing Cycle to Past Cycles

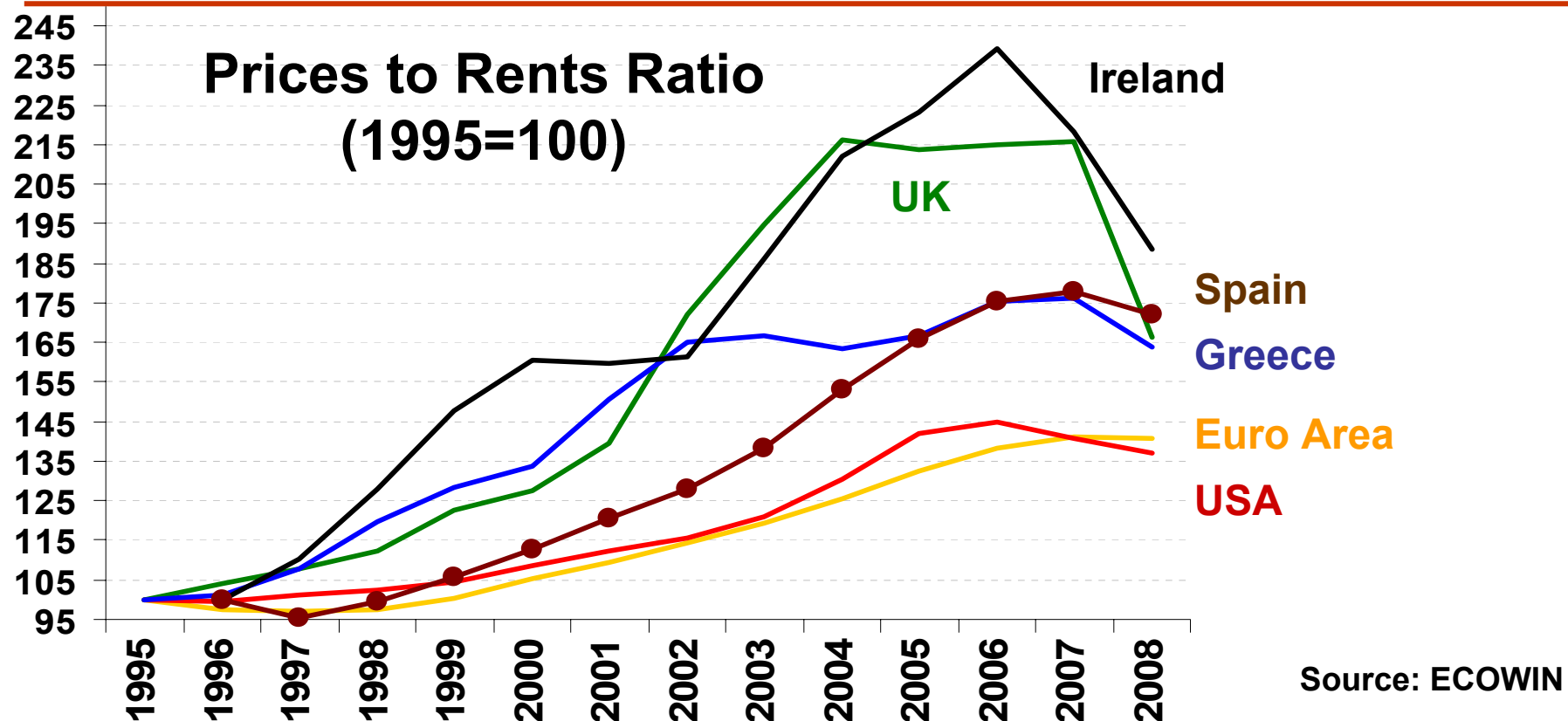
	Upturn		Downturn	
	Duration	Amplitude	Duration	Amplitude
Past cycles	23	48	19	-24
Current cycle	46	124	8	-20

Source: Collyns, Igan, and Loungani (2009).

Note: Average values across 18 advanced economies. Duration is in quarters; amplitude is in percent.

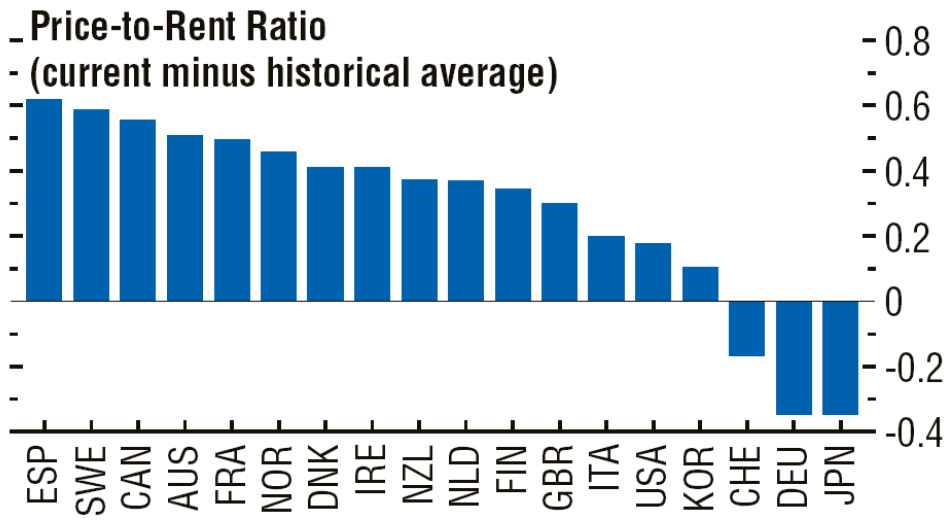
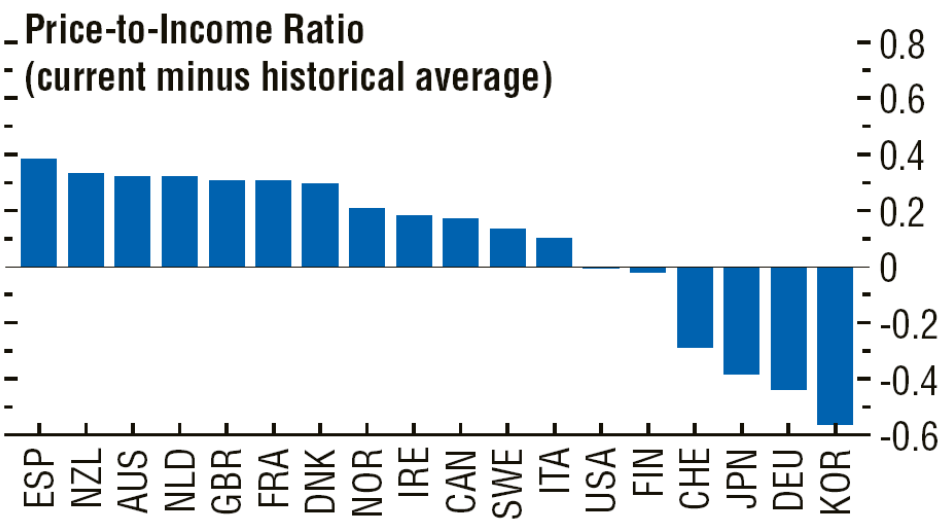
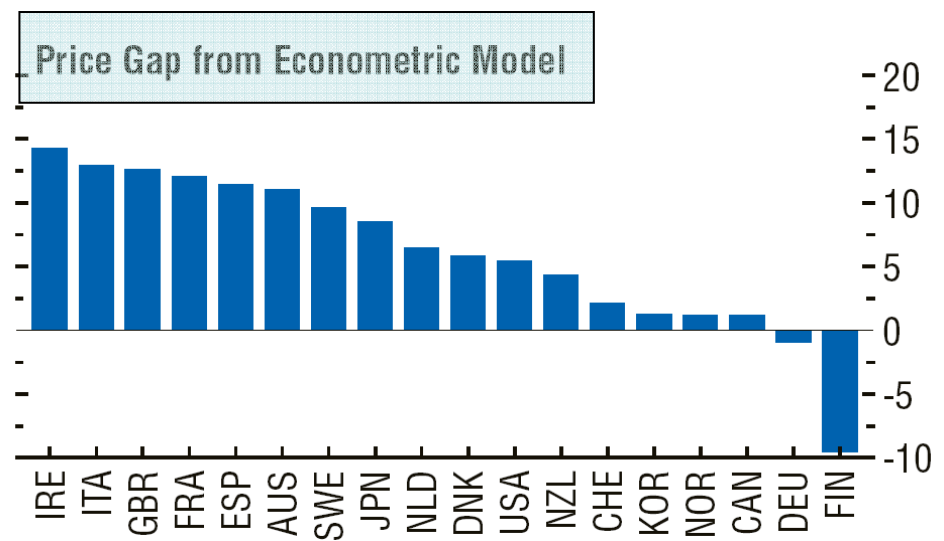
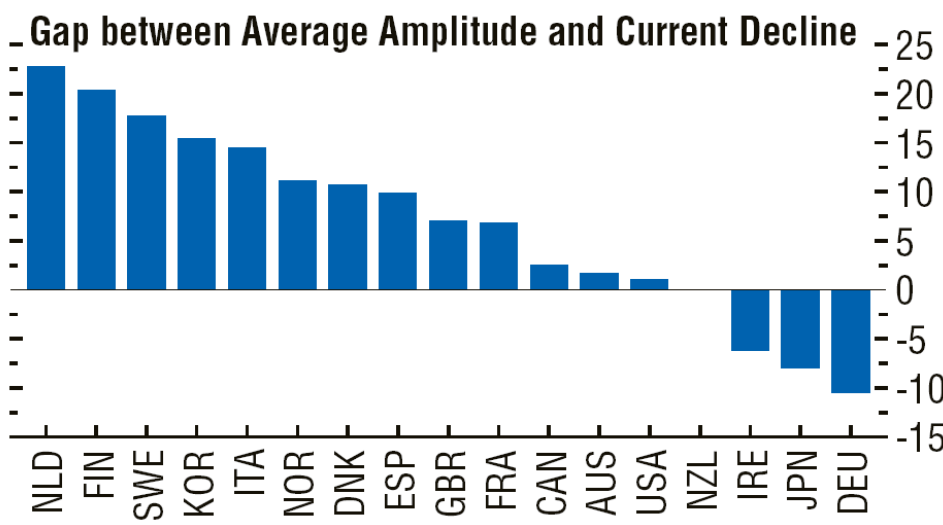
*% change in real house prices

III. Rapid increase and decline in ratio of prices to rents ratios in many countries

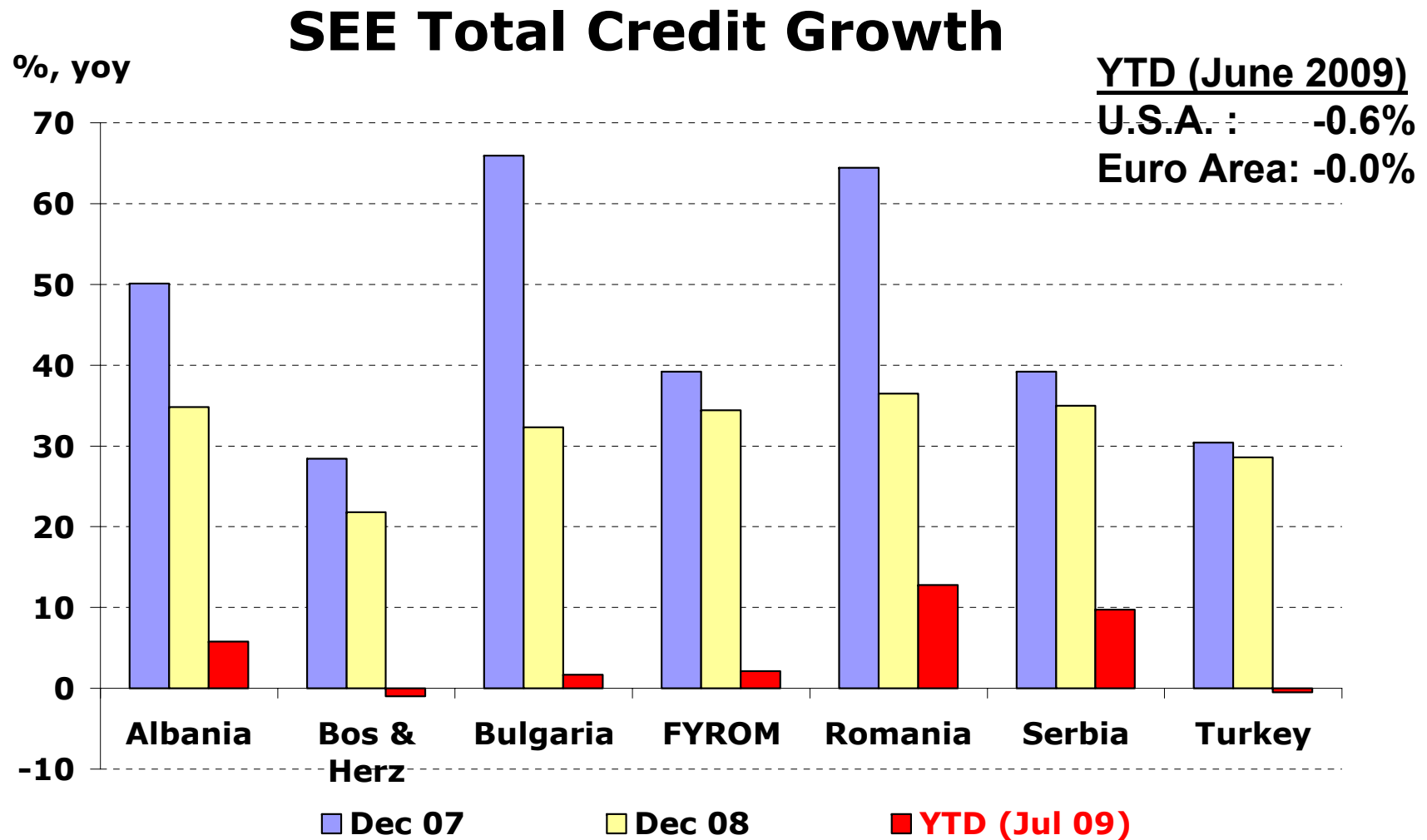


- ✓ The increase of the ratio in Greece up to 2002 can be attributed to the entry in the EMU and the significant decrease of real interest rates.
- ✓ The fall in RE prices in many countries can be attributed to: (α) the rise in required returns due to increased risk premia or/and (β) the bursting of a bubble

III. Have RE prices bottomed out?



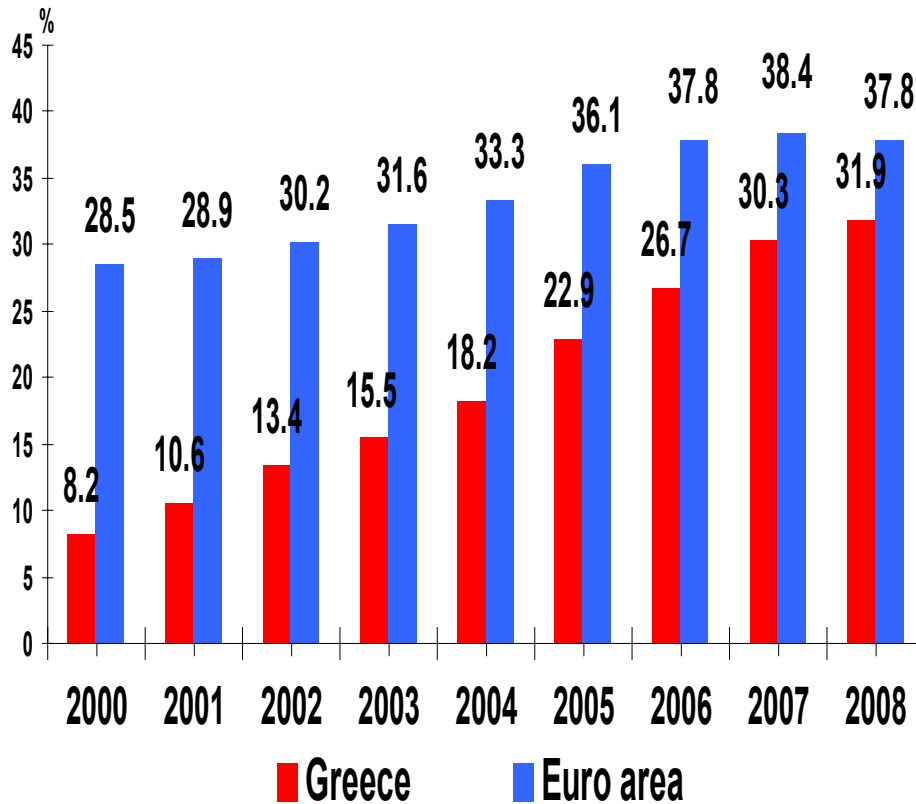
III. Current flattening in SEE credit expansion prolongs recession in RE



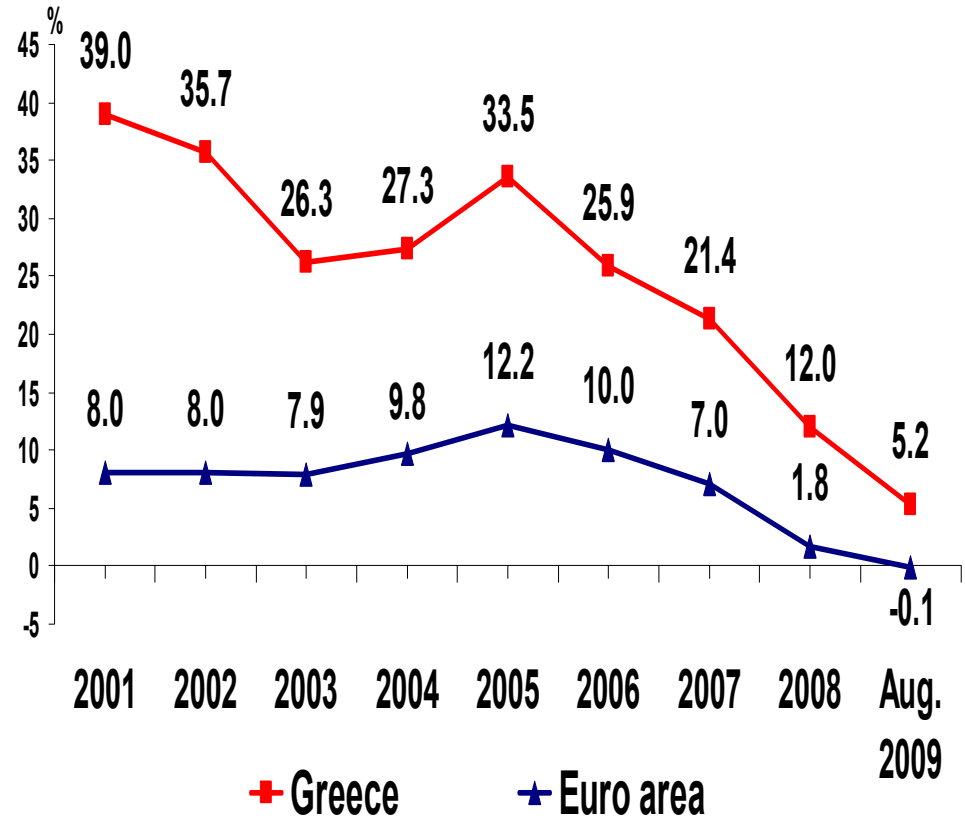
Source: Central Banks, Eurobank Research

III. Greek credit availability down but better than in Euro Area

**Mortgages
(% GDP)**

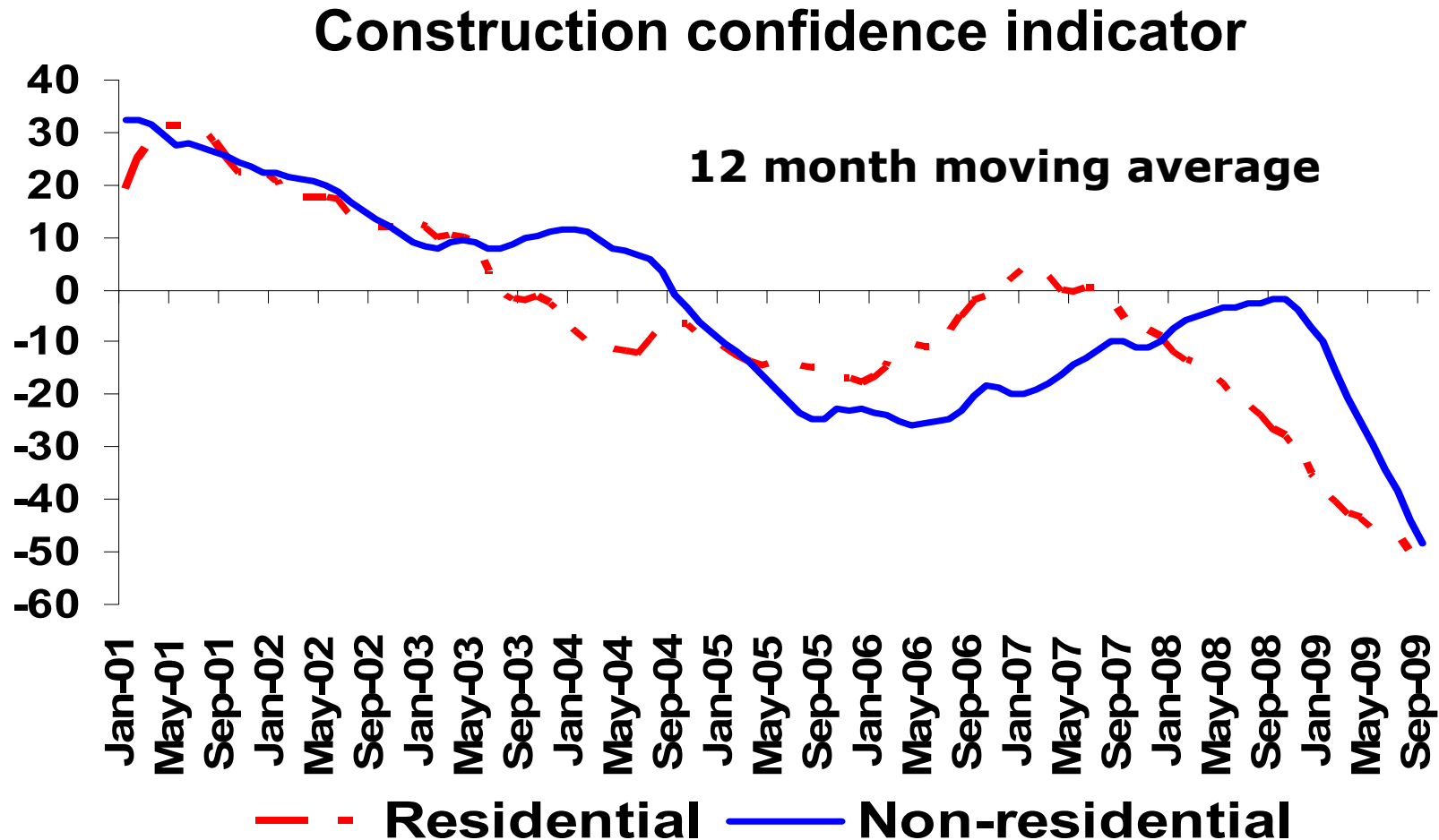


**Mortgages
(% rate of growth)**



Greece, August 2009: € 78,8 bn. outstanding amount

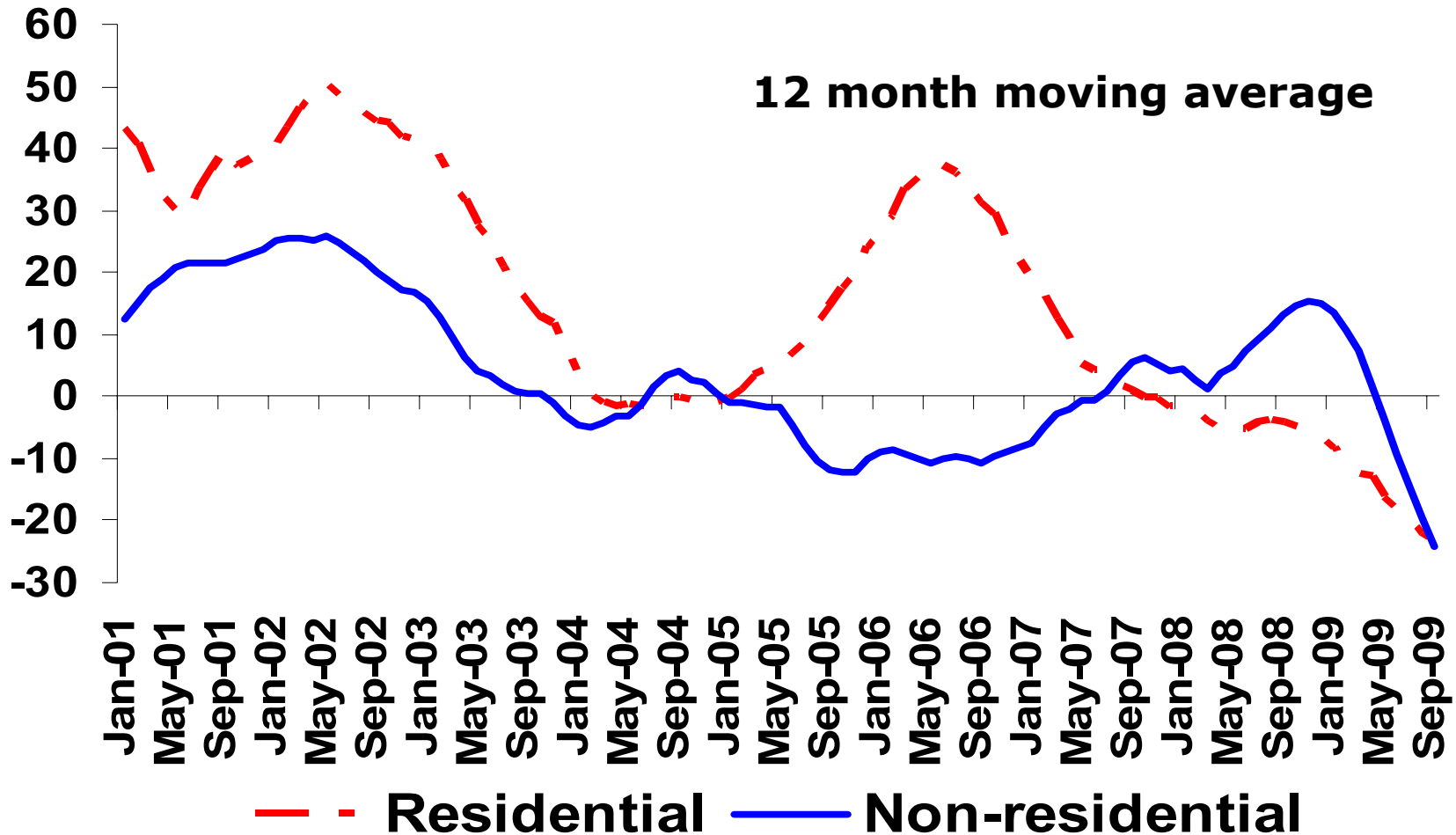
III. Greek business confidence in the RE market keeps declining



The construction confidence indicator is the arithmetic average of the balances (in percentage points) of the answers to the questions on order book and employment expectations. Balances are seasonally adjusted.

Source: European Commission, Eurobank EFG Research

III. Greek constructors expect a further fall in prices



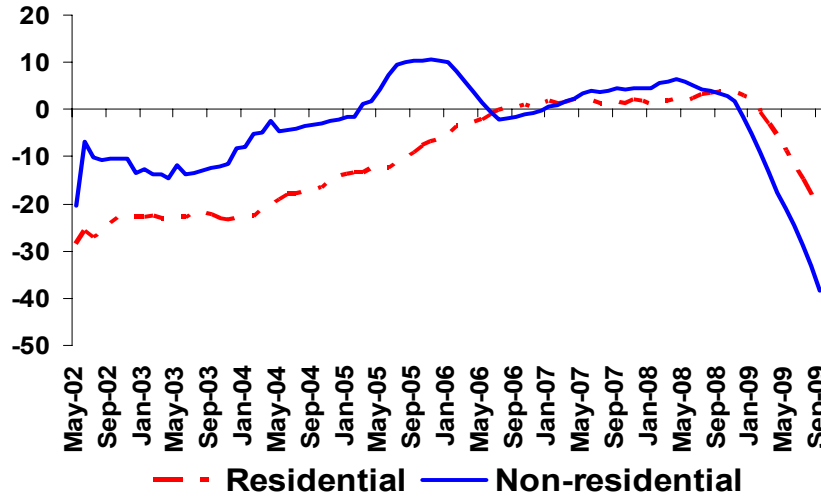
The balance of answers to the question:

“How do you expect the prices you charge to change over the next 3 months?”

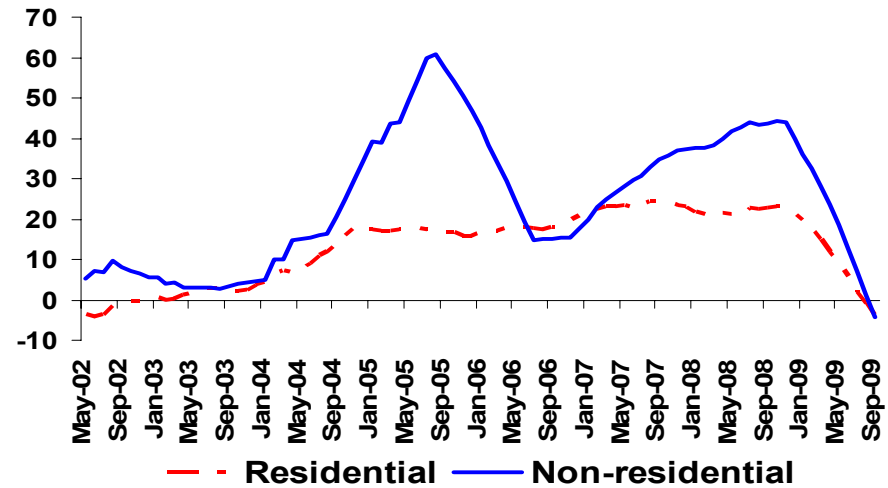
III. Bulgaria & Romania: RE Business expectations

BULGARIA

Construction Confidence Indicator

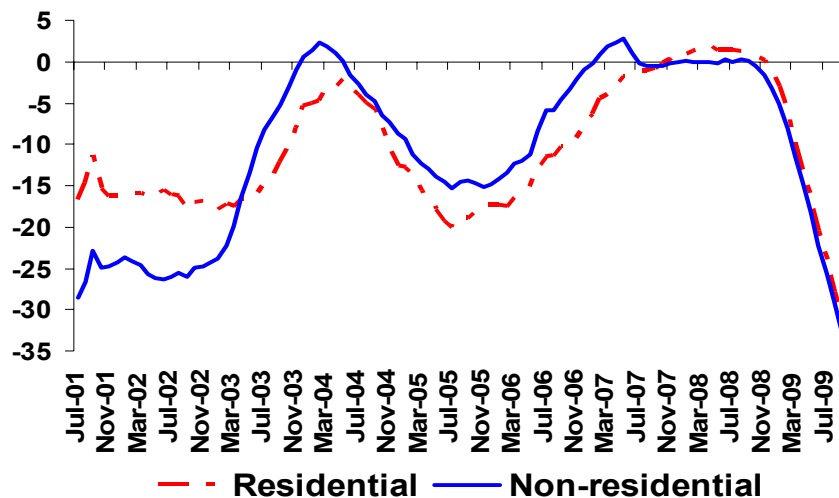


RE Price Expectations

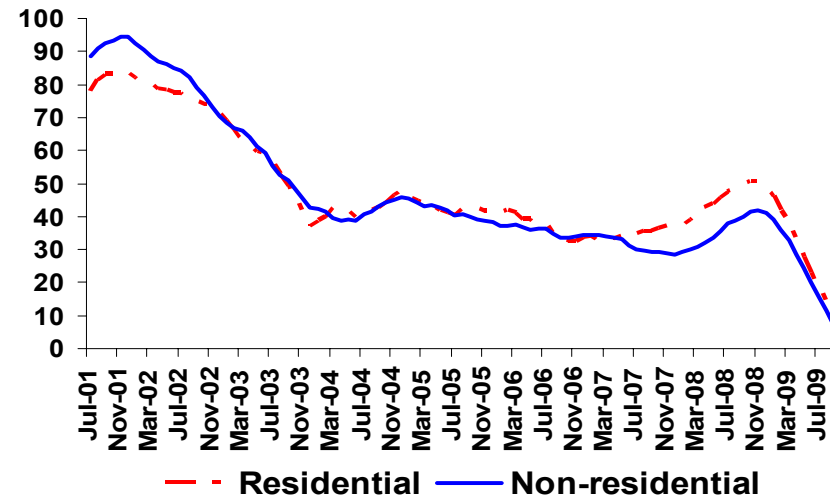


ROMANIA

Construction Confidence Indicator

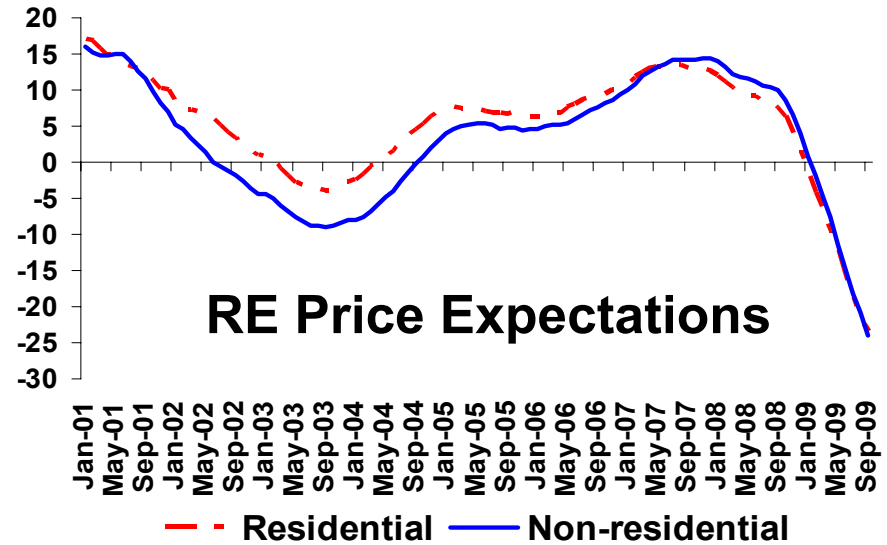
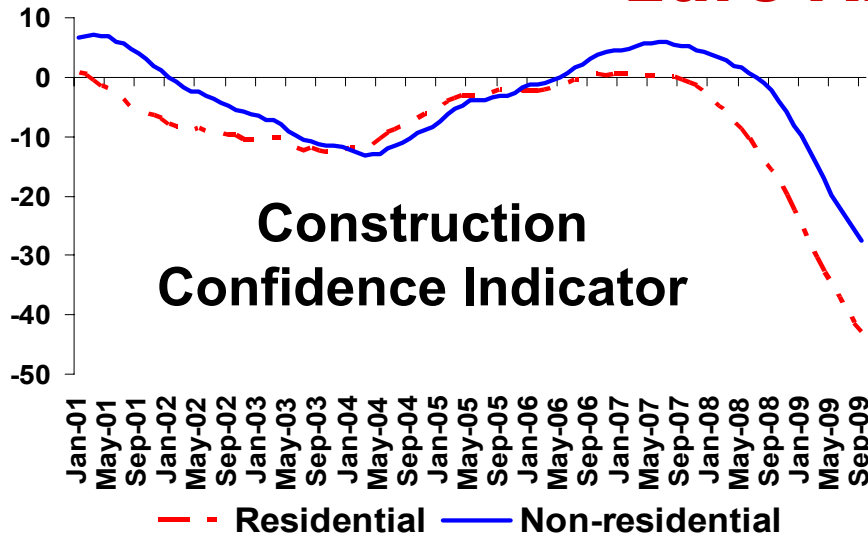


RE Price Expectations

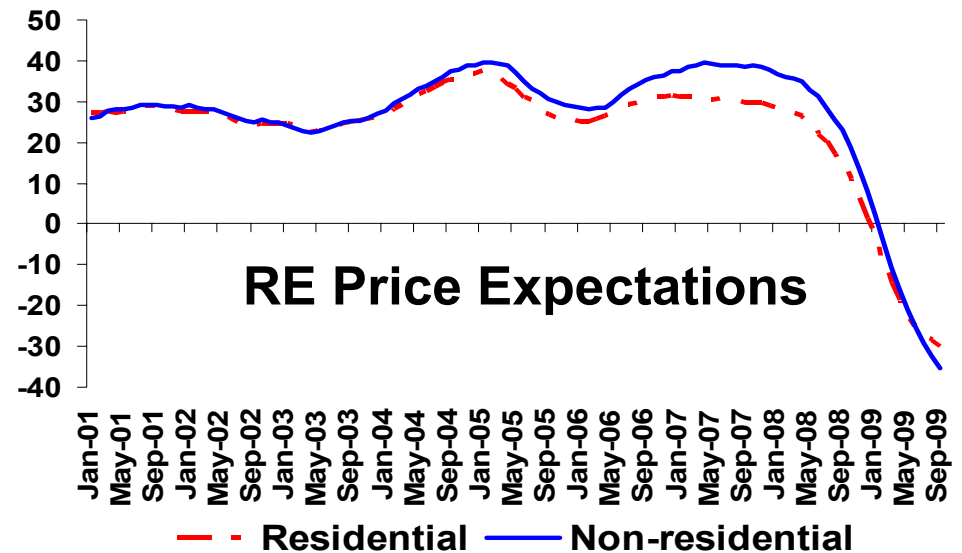
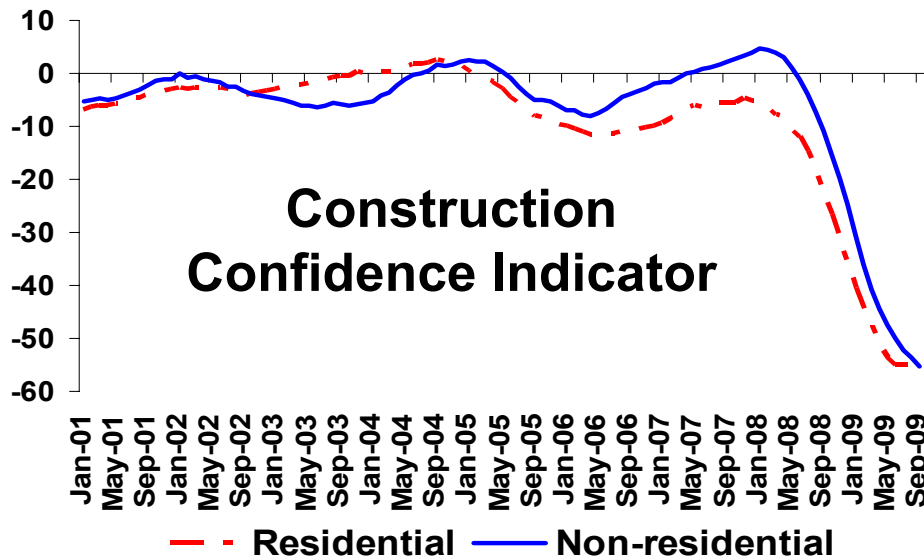


III. Euro Area & UK: RE business expectations

Euro Area



United Kingdom



IV.

FUTURE TRENDS

IV. Looking ahead: Slower future world growth

This was not the Great Depression or Capitalism's 1989, yet Great Recession is likely to leave permanent marks

Despite the renewed optimism for 2010, the long-term view is for lower growth than the period leading up to the crisis

- ✓ Assuming the financial sector stabilizes gradually, global demand will grow slower than in the period before the crisis as
 - The US consumer is forced to reduce leverage and increase savings – same is true in other countries with high household indebtedness
 - The Chinese consumer is not ready yet
 - India is still a closed economy
 - Europe depends on exports
- ✓ Risk premia to stay high
- ✓ Higher demand for new bank equity capital
- ✓ Fiscal debt higher than before [non-financial private (175% of GDP) and public (61% of GDP) sectors in the US]
- ✓ Central bank intervention interest rates expected to go back up
- ✓ Hence, a scenario of a 7-yr-long sluggish global growth is not unlikely

IV. A different world ahead

- ✓ Economics: Slower global growth
 - New Europe has a natural anchor
 - Many risks in Greece
- ✓ Politics: Economic & political power → Asia and G-20
- ✓ Global Regulation:
 - The Financial Stability Board gains power
 - A stronger IMF, better able to fight crises
 - Stricter regulation, easier implementation in Europe than in the US
- ✓ **G-20 decisions will affect banks**
- ❖ Yet Wall Street continues to hold considerable **political power against future regulatory restrictions**

V. Conclusions

- ✓ The real estate market has its share of the blame for the current Great Recession
- ✓ Sluggish growth in 2010 and lower global growth in the next 10 years relative to the 10 years leading up to the crisis
- ✓ Greece faces major challenges ahead due to its fiscal and current account imbalances
- ✓ The SEE region is expected to recover with a lag in 2011 but then grow strongly after that
- ✓ Average overvaluation in the Real Estate market continues
- ✓ Recovery in the RE market will lag the recovery of the underlying economies

THANK YOU FOR YOUR ATTENTION!!

My thanks to the Research Department of Eurobank EFG for able research assistance and support

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