REAL ESTATE: Ups and downs ahead

FROM PAGE 1

The relationship between real estate and jobs is a complicated one. On the one hand, a lack of affordable housing can hurt growth, as economist Mark Schniepp wrote in the UCLA Anderson Forecast's 2007 Orange County Outlook.

"Housing poses the largest constraint to significant job creation and net migration in Orange County," Schniepp concluded. "To the extent that affordable and available housing is present, economic growth in the form of job creation would expand."

But as Anil Puri and Mira Farka of Cal State Fullerton said in their 2007 economic forecast for Orange County, housing prices take time to show up in the job picture.

"Higher housing payments require that more jobs with higher salaries and value be created," they wrote. "The supporting jobs, mostly in the population-serving categories such as restaurants and recreational activities, building maintenance and related areas, will also increase but these tend to be towards the lower end of skill level and consequently lower-paying."

COMMERCIAL

Commercial construction is booming in Orange County at just the right time.

The boom is injecting money and jobs into the economy just as other work opportunities are being drained by a drop in homebuilding and other residential real estate industries.

Forecasters at Chapman University's A. Gary Anderson Center for Economic Research, for example, expect nonresidential construction in the county to outpace residential next year – reversing the norm of the housing boom.

Nonresidential construction should rise 4 percent in value next year to $2.4 billion. Th [illegible] percent drop i [illegible] $2.1 billion.

Even so, Cha [illegible] 2,000 jobs, or [illegible] County's cons [illegible] tivities sectors [illegible] the slowdown [illegible] Without the [illegible] boom, the job [illegible] Chapman econ [illegible]

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In an illustra [illegible] ed the local eco [illegible] other sector, [illegible] services, is par [illegible] fice constructi [illegible] cludes lawyers [illegible] rary-help comp [illegible] Orange County [illegible] November.

Developers are building 5 million square feet of larger office properties – the equivalent of 135 floors – according to **Voit Commercial Brokerage**. That's enough to increase supply by 5 percent.

It's also the largest total under construction since developers worked on 5.6 million square feet in late 2000, before a downturn among technology companies led to big office vacancies.

The county's low vacancy rate of 7.5 percent for office buildings is enticing developers, said Jerry Holdner, vice president of market research with Voit.

"When the vacancy rate goes below 10 percent, that's when the cranes come out," Holdner said.

Yet the building boom is coming just as mortgage companies are shrinking and moving out of some of their big offices. **ACC Capital Holdings**, the Orange-based parent of **Ameriquest**, is leading the trend by putting up 600,000 square feet for sublease after announcing 3,800 layoffs in May.

Holdner said growth in office rent [illegible]

Even Mac Mackenzie, a real estate agent for Coldwell Banker who was the county's top salesman in 2005, worries there will be more homes than buyers in the market next year. Mackenzie is worried about bad debt and poor financial management by homeowners.
"I really think that the potential of a downturn is very, very high, and that a lot of people have overborrowed to the point of insanity," he said.

[illegible] cording to DataQuick Information Systems. That's down 27 percent from the same period in 2005 and the lowest since 1995.

But even as homes began to languish on the market for want of buyers, the median price of local homes continued climbing through the first half of the year, hitting a record $646,000 in June.

Since then, the standoff between buyers and sellers eroded and the median price dropped $40,000, retreating to November 2005 levels.

PAUL SAKUMA, THE ASSOCIATED PRESS

HOUSING MARKET: The California Association of Realtors expects prices for resale houses to fall by 2 percent in 2007. Chapman University analysts forecast that the drop in Orange County will be even greater: 6.4 percent.

Some analysts say prices should bottom out in the next three to six months and stay level through next year, if not longer.

"The question is: Between now and then, are things going to come down by 2 percent or 5 percent?" DataQuick analyst John Karevoll said.

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[illegible] es? Builders, who [illegible] d in 2006 by can- [illegible] percent or more, [illegible] o manageable lev- [illegible] of 2007, said Jay [illegible] manager for **KB** [illegible]

[illegible] buyers will remain [illegible] said. He predict- [illegible] rket will be "dor- [illegible] for homeowners [illegible] and buy a new [illegible]

[illegible] may see a little re- [illegible] but not much, ac- [illegible] ent-research ser- [illegible]

[illegible] vering around 96 [illegible] as will rent in- [illegible]

[illegible] rch and analysis [illegible] F YieldStar, fore- [illegible] nts will go up be- [illegible] percent next year. [illegible] cts believes it will be around 6 percent.

"It won't be quite as aggressive on the rent increases as we've seen recently," Willett said, citing a slowdown in job growth next year. But while Los Angeles and the Inland Empire have seen new apartment communities built, Orange County has not.

"So Orange County is going to continue to be a very tight market," Willett said.

BUY OR WAIT?

So what does all this mean for the Palas family of San Clemente? Should they buy now, or should they wait?

If you believe the economists, there might not be any harm in waiting.

Robert Kleinhenz, deputy chief economist for the California Association of Realtors, said it's too soon to say that the market has hit bottom. But he said sales have been steady for the past three months.

"It looks like we're moving toward a more stable set of market conditions," Kleinhenz said. "These things tell me we're not seeing a market that's in free fall."

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"I really think that the potential of a downturn is very, very high, and that a lot of people have overborrowed to the point of insanity," he said.

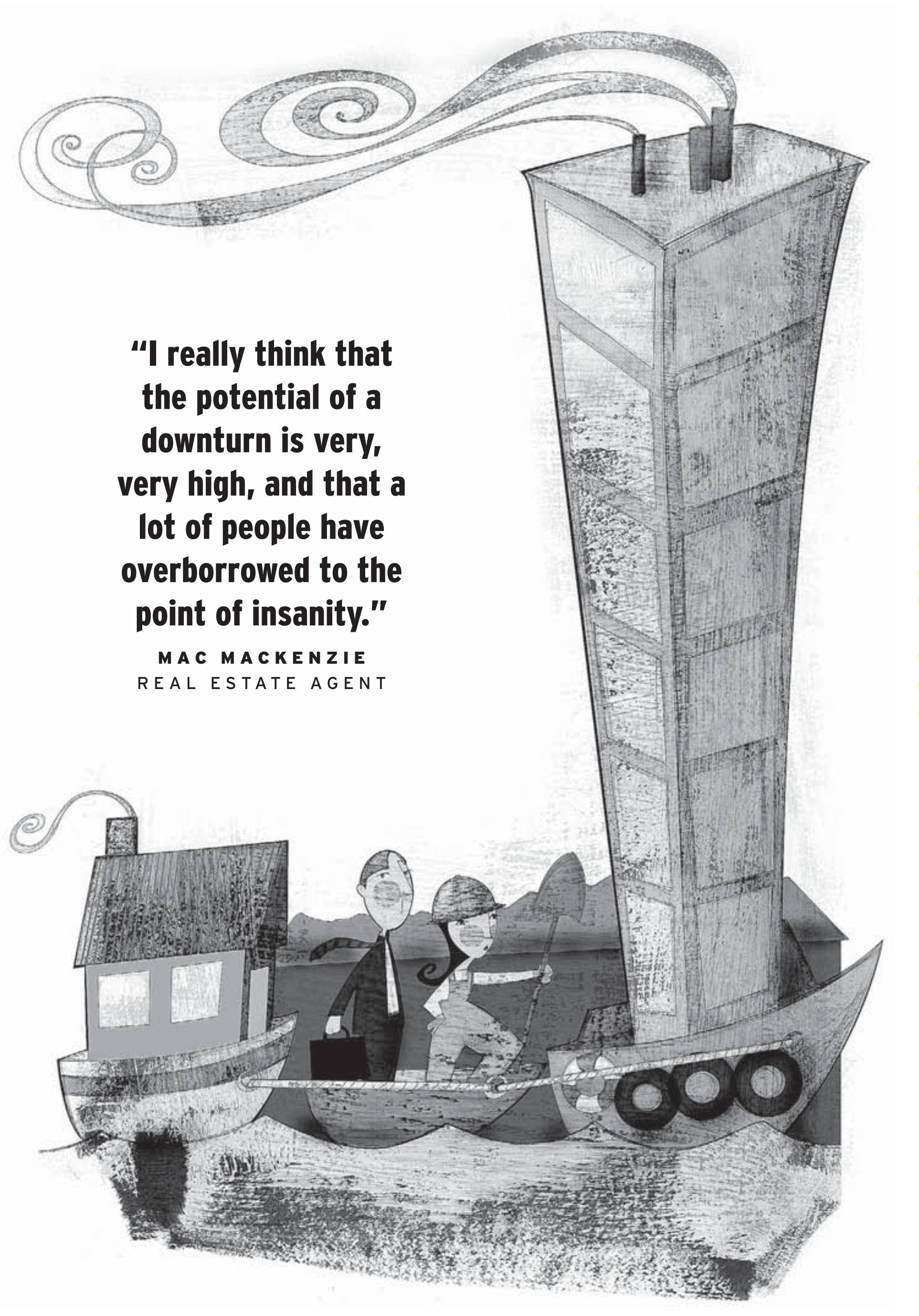
But other real estate agents say they're bullish.

Interest rates are relatively low, prices are down, sellers are conciliatory and there are lots of homes to choose from.

Bob Chapman of **Prudential California Real Estate**, a former president of the Newport Beach Association of Realtors, said activity has picked up as buyers sense that big price drops aren't happening. Next year will be more active, he said.

"I don't see any declines in values," Chapman said. "It will continue along like this for awhile. I don't think we'll see a big decline."

Thinking a moment, he added, "Maybe now is a good time to buy."



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MAC MACKENZIE
REAL ESTATE AGENT

CONTACT THE WRITER:
714-796-7734 or jcollins@ocregister.com

LANSNER: Upside surprise could be a real long shot

FROM PAGE 1

Quite often, when the consensus opinion is tightly wrapped around one possible outcome, that outcome is proved to be wrong. And the error can be to either the upside or downside.

As UCLA economist Ed Leamer said half-jokingly about what might stun us all a year from now: "The surprise will be that our forecasts are correct. That is something to talk about."

The contrarian in me looks to this relative widespread agreement on a modest dip in home prices and wonders if common wisdom is way off, then what?

Could '07 be a major disaster?

Or an unexpected, pleasant surprise?

AN UGLY CALL

Clearly, housing's risks are high as 2007 starts.

Momentum and shopper psyche are weak. Some owners are in trouble, too, placing added pressure on the market. It feels like it would not take much to turn 2006's skittish housing market into a full-fledged 2007 fire sale.

The overall economy, the engine really driving housing, feels mushy. Local bosses are hiring, but at a reserved pace. Consumer spending appears tepid.

So if the business scene really weakens, real estate would lose a key underpinning. And the housing market needs all the support it can get. A significant economic reversal would doom local housing to probably double-digit percentage point losses.

Don't forget outside risks, like a national economic tumble – or war.

As veteran O.C. real estate watcher Walter Hahn put it, when asked what could dramatically alter his '07 outlook: "Israel bombs the Iranian nuclear facilities, and oil goes to $150-a-barrel-plus, causing serious national and local economic and housing-market recession."

For the rosy outlook to bloom, the local economy has to get hot. It's added jobs in 12 of the past 13 years, though recent payroll growth has been meek. Technically that weakness isn't fact yet; it's just a guess. We'll find out what really happened in 2006 when state job counters revise their stats in March.

The recent housing rally was fueled in part by new financing tricks that have – or will – pound local checkbooks. Short-lived, discounted house payments got certain buyers into homes they otherwise could not afford. As those initial loan discounts end, numerous homeowners face higher monthly costs on an asset – their home – that may be depreciating in value. That's not a happy formula.

Cheaper interest rates from a suddenly helpful Federal Reserve, in this kind of meltdown circumstance, won't help much.

The grand question overhanging the market is: Did bankers and borrowers know what they were doing?

If the bankers or borrowers guess wrong, this gloomy outlook for 2007 – and future years, too – could prove true. And it won't only be the effect of foreclosed homes dumped on the market. Lenders and the investors who buy mortgages will back off, further dousing a chilled housing market.

Saumil Parikh at Pimco bond traders in Newport Beach thinks wariness will appear in certain loan niches, at a minimum: "We believe the subprime mortgage market (for the diciest borrowers) will reprice credit risk during 2007, thereby making it more expensive and onerous for first-time homebuyers to enter the market."

Housing's doomsday scenario is a blend of overlapping and interwoven headaches: the confluence of dark events combining to scare off market participants from shopper to builder to lender.

A perfect storm bursts the bubble.

OR GOLDEN DAYS?

If you buy into my thesis that a tight consensus is likely wrong, and the apocalyptic scenario seems off, there's another intriguing possibility.

Imagine O.C. real estate enjoying a very hearty 2007.

That's right. A "What bubble?" kind of year.

It's the kind of shocker that Anil Puri, Cal State Fullerton business school dean, suggested when I asked him what surprise we might be discussing a year from now.

"Median price goes up 10 percent or more," he said.

Not as truly far-fetched as you think.

What a quick housing turnabout requires is a lot of help from outside the industry. Plus a bit of luck.

Essentially, economic perfection to get nervous shoppers off the fence in a meaningful degree.

Bill Plattos at FirstTeam Real Estate suggests that in '07, "There will be many buyers who will see a buyer's market as a time to buy, instead of waiting for a seller's market."

For the rosy outlook to bloom, the local economy has to get hot. It's added jobs in 12 of the past 13 years, though recent payroll growth has been meek. Technically that weakness isn't fact yet; it's just a guess. We'll find out what really happened in 2006 when state job counters revise their stats in March.

The local economic challenge will be replacing the employment and spending oomph that real estate kindly added during the nine-year boom.

Finding the next hot thing will be a struggle, but not out of the question. Have you noticed a hot stock market lately? That paper wealth could boost consumers, for example.

Next, assuming the local business climate turns torrid, the better-than-expected housing '07 scenario demands that nothing else go wrong outside Orange County.

Nothing.

I'm talking a national economy back in high gear. Peace on Earth and good will to all men, and I mean around the globe. No terror attacks, natural disasters or other hiccups. Maybe even a happy Iraqi solution.

Basically, geopolitical and commercial nirvana.

Plus, to see O.C. housing succeed in '07, one must pray that the Federal Reserve doesn't do anything stupid.

These policy-makers seem obsessed to worry that some workers might get a decent raise and that a few merchants might be able to raise prices at will.

Any whiff of economic energy may spook the Fed into thinking problematic inflation is back. Thus, the Fed may slam on the business brakes by raising the influential interest rates it controls. That could dampen the national economic revival and derail hopes that O.C. housing could have a stellar year.

So, an upside surprise for '07 is a long shot.

But so is a total property meltdown – though it has better odds than a remake of double-digit property gains in this town.

That leaves one to assume that the consensus view – small losses in '07 – is the best bet.

But how often is the consensus view correct?

CONTACT THE WRITER:
949-459-3569 or
jlansner@ocregister.com