WE ARE IN A MINI DEPRESSION

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The economic downturn seems to be getting worse and the question becomes "is this a recession or a mini depression?" Let's examine the economic variables to see if we are in a mini depression.

<u>Job Losses</u>

I have always felt that job losses are the most important variable as laid off workers and those worried about keeping their job refrain from buying cars, plasma TV's, homes, renting more expensive apartments, etc.

UNITED STATES

- 8.9% unemployment April 2009
- 17 consecutive months of job loss as of April 2009
- Projected over 610,000 job losses in April in the private sector unemployment to reach 11%

13.7 million people are unemployed. Almost 6 million jobs have been lost since December 2007. To stay in equilibrium the U.S. Economy needs to add between 100,000 to 125,000 jobs per month to keep pace with the population growth. Federal Reserve Chairman, Ben Bernanke testified to Congress that the Fed expects the jobless rate to remain high well after cresting above 9% in early 2010. Other economists expect the unemployment rate to exceed 10% before it begins to decline.

CALIFORNIA

- 11.2% unemployment April 2009
- 62,000 job losses over 2 million unemployed
- 11 consecutive months of job loss as of April 2009

ORANGE COUNTY

- 8.5% unemployment
- 30,900 jobs lost in 2008
- 20,000 projected job losses in 2009 (Cal State Fullerton)

<u>Government Deficit</u>

Our current National Debt is 11.2 Trillion with 412 Billion tacked on as interest payment on 2008 budget. The U.S. budget deficit projected for 2010 is <$2.3> Trillion. The forecast is $20.5 Trillion by 2020. Stimulus package of $825 Billion will probably grow to 3 Trillion. The Government is increasing the money supply to combat deflation and increase economic growth. The question is how it will ever be paid back without large tax increases to pay this enormous debt.

<u>Housing Price Drop</u>

The median price of homes in California has fallen over 40% and is still declining. The California Association of REALTORS® projects another steep decline in median price in 2009 to $248,000.

<u>Sub-Prime Meltdown</u>

We are still bleeding from the easy money, no down payment, no documentation loans. Fannie and Freddie each lost over $50 Billion in 2008. Fannie lost $23.2 Billion in the 1st Quarter of 2009 and needs another $19 Billion in cash infusion from the Feds. In other words, we are still not finished with the sub-prime meltdown.

Stock Market Decline

The stock market is down 49% average over 52 weeks with no light at the end of the tunnel. Dividends are being cut or eliminated to conserve cash so there is no return for investors.

Inflation

Inflation has been held in check for over 20 years in the short term this trend should with our last year negative CPI the past year. The skeleton in the closet is the Federal Debt to GDP ratio will increase from 40% in 2008 to 80% in 2016. The Feds will still try by intervention to keep the inflation rate low in the coming years, however, may not succeed due to international pressures.

Financing for Commercial

Commercial buyers need more equity as down payment, often 40-50% vs. the old 20-30% in years past. The Debt Cover Ratio (DCR) which is the safety margin between Net Operating Income (NOI) and cash flow is now between 1.25-1.30 on actual and not proforma figures. Lenders are looking at stabilized numbers of 6 months to a year. With stronger underwriting guidelines loans are taking longer and harder to obtain. In commercial markets rates have increased due to risk and difficulty of reselling of loans by the banks to institutional investors.

Capitalized Rates in Real Estate

The CAP Rates have increased which equates to (value decline) in all market segments. The perceived risk of holding real estate is higher risk. Lending now is based on cash flow and not assets or replacement value of real estate. In other words, buyers and lenders alike are asking what my cash flow is each month. There is still a disconnect between seller expectations and what the buyer can finance and pay. Unlike in years past, there are no white knight buyers today as the real estate market is still declining.

COMPARISON CHART

	Depression 1929-1933	Mini Depression 2008-2009
Housing Price Decline (25%) or more	YES	YES
Mortgage Delinquency Rate High	YES	YES
Unemployment (1933-22%)	1930 - 8.7%	April 2009 - 8.9%
Decline in GDP	26.50%	12.40%
Stock Market Decline	85%	49%

We can see from the chart above we are in a mini depression, however it doesn't compare to the Great Depression of 1929-1933. How long will the characteristics of a depression last? The characteristics include a decline in business activity, failing prices, raising unemployment, declining housing prices and stock market losses. The last three quarters of the U.S. GDP were negative and unemployment is predicted to increase both nationally and in California. The Federal Government is spending billions of dollars to end the mini depression but little of this money is going into creating good paying jobs, which I feel is the key to any turnaround. Many economists disagree and are predicting a turnaround before the end of 2009. Then again, how many rich economist do we know, so be prepared for several years in a mini depression.

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