REAL ESTATE FINANCE
THE QUARTERLY REVIEW OF COMMERCIAL FINANCE TECHNIQUES

VOLUME 18, NUMBER 3 FALL 2001

New News from the Census

Huge demographic surveys are never perfect; however, most are informative and the 2000 U.S. Census was particularly informative. It is true that millions of people were "imputed." It is also true that the most important details in the survey won't be available to the public until 2002. Still, there is much news and even new news in the 2000 Census.

Since *Real Estate Finance* always seeks to provide its readers with the new news, we polled the leading real estate demographers. We asked each of them to list the five most important things that they had learned so far from the 2000 Census.

In alpha order, these real estate demographic experts are: Sara Johnson and Jim Difny from the newly merged DRI/WEFA. Susan Hudson-Wilson from Property and Portfolio Research. Lloyd Lynsford from the REIS reports. Ray Torto of Torto Wheaton. And, everybody's favorite, Mark Zandi from Economy.com.

Here, in Letterman-like order, is the composite of their recent learning. We begin with point ten as the most obvious and move on toward point one which is possibly less obvious, but probably even more relevant. In the interest of full disclosure, the editor did adjust a few comments to fit the list.

10. Soooo many more bodies—maybe. The 2000 Census has already told us that a nation the size of Israel was living unknown inside the U.S. borders. Clearly immigration and particularly illegal immigration had been far faster than the INS had previously reported. In fairness, the INS has been suggesting that the 250,000 per year number was low, but nobody thought it was as high as 500,000 per year.

The cautionary maybe is necessary because there is the possibility that some of the excess people were there in 1990, but we missed counting them. The Census is currently studying this issue, but the consensus among the demographers is that while there is a little of both, it is primarily a case of a lot more bodies.

Several of our real estate demographers cited the work of William Frey of the Milken Institute and the University of Michigan. His early work on the 2000 Census has shown that the immigrant explosion has moved beyond the traditional six immigrant states—New York, New Jersey, Florida, Texas, Illinois, and California. In these six states, immigration has always been critical. In the 1990s, California lost 7% of its population to domestic migration while picking up an equivalent 7% from international migration. Likewise, New York lost 10% to domestic migration, picking up 6% from international migration. The new news lay in the new migrant magnet metro. Atlanta had half a million new bodies while Phoenix and Las Vegas had 400,000 new bodies each.

9. Immigrants everywhere—Frey versus Garreau. We all remember Garreau's classic *Nine Nations of North America* where he argued that it was not one melting pot, but nine distinct regions, which constituted the United States. Frey's work takes this one step further. While he clearly shows three racial groupings in the country—black in the South, Hispanic in the Southwest and West, and white across the northern border—he also shows that the immigrant impact has created quite diverse metro markets within the broad three-region categorization.

After September 11, it is even more important not to straight-line past trends. Thinking about the traditional immigrant magnet states, international immigration has been critical in maintaining their population levels. Likewise, the new immigrant magnets have shown especially rapid population growth in large part because of legal and illegal immigration. Will new security concerns dramatically reduce the inflow of immigrants to this country? If it does, growth patterns are sure to change and with them real estate values.

8. 90% of school-age kids have access to a computer—self-education over formal education? This is the obligatory positive comment in the "new news list." We have all been concerned about the declining quality of our educational infrastructure in this country. It is true, as the Census points out, that self-education has gotten a big boost from the computer and that access to a computer is very widespread. While this is clearly a positive, it probably isn't a big enough positive to suggest that we need to stop focusing on educational improvement.

7. Yet more single parents—possibly higher female participation rate, certainly higher stress rate. Following quickly on the heels of the previous positive comment is a very disconcerting negative. Just as there are so many more bodies, there are so many more single parent households. With Americans facing longer commutes and more time commitments to raising children, this has got to create a tremendous amount of stress.

6. The number of old men is growing faster than the number of old women—will they work? While interesting in and of itself by providing the grist for all sorts of demographic changes in the social character of nursing homes, this point allows consideration of the labor force participation rate. The number of people between 16 and 64 not in the military and not in school constitutes the traditional work force. Of this group, 67% are active participants in the labor force. This is up slightly less than 1% over the last 10 years.

At the same time, the share of self-employed in the work force has actually declined from just under 8% to just over 6%. So, we have a slight increase in participation with a significant decrease in the share of people working on their own.

With more, healthier old men, are we about to see a change as the boomers age? Will both participation rates and the number of self-employed, possibly at less than 40 hours a week, expand dramatically over the next two decades? This is tremendously important in light of a potential decline in the number of immigrants that would definitely reduce the labor pool. Possibly cabs will cease to exist with the reduced number of immigrants and be replaced by retiree-driven limos.

5. The increase in home ownership continued, but at a slower rate—note the relationship to annual multi-family starts. This point allows us to remember the ever-important contrast between stocks and flows. Home ownership increased dramatically after World War II and continued that increase in the 1990s. However, the last decade increase to 67% was much slower since home ownership had already grown to 65% in 1990.

Annual multi-family starts have run between 300,000 and 400,000 over the last decade. If a sustained recession caused the home ownership percentage to actually dip, a small change in the ownership percentage can appear very large in relation to multi-family starts and hence to rental vacancies going forward. A 1% drop in home ownership from today's record rate would produce 1.2 million more renters. Certainly a drop of 1% wouldn't be expected in any one year, but if it happened over a few years, the impact on multi-family vacancies would be very, very substantial.

4. The payroll survey does not equal the household survey—It includes dual jobs, but not the self-employed. Bottom line: employment growth over the last decade ran at closer to a 1.3% annual rate than the 1.8% per year most commonly reported. The payroll survey consists of a monthly inventory of leading employers referred to as the 790 supplemented well after the fact by employment tax records off the 202 form. This "survey at the office" is quite different than the household survey. Clearly, a dual job counts as two people employed in the payroll survey. Further, self-employed people don't appear in the payroll survey. Since the number of dual jobs was growing and the number of self-employed was declining, the payroll survey showed an unusually high difference from the household survey over the 1990s.

If you're mathematically inclined, you have probably been wondering how job growth could be close to 2% for 10 years when population growth was barely 1%. Clearly, the unemployed could go to work, but dropping from 7½% unemployment to 5% unemployment adds only 3 million bodies. If the participation rate is only up less than 1%, then the total number of additional bodies available to work is 4 million plus population growth. Over 10 years, jobs couldn't have been growing at 2% with population growing at only 1%.

This may be the first of the "don't forget this" facts in our top 10 list. Look back at the statistics supporting your developments/investments and be sure that you aren't incorporating the larger number in your demand forecasts.

3. It really isn't getting more egalitarian: the spread between mean and median income narrowed in the last five years, but it was largely an "xer fake." It has been popular to say that 5% employment lifts all boats. It is true that the Census shows a narrowing between the mean and median income numbers. This would normally mean a more egalitarian society. Recall that the median is the middle person, like you, while the mean is dramatically impacted by Bill Gates and Warren Buffett, who have a tremendous amount of income and wealth.

Unfortunately, several things contributed to this accurate number that does not support the egalitarian conclusion. First off, the baby bust came into the work force over the last 10 years. This was the xer fake. A larger number of entry-level workers at the lower average wages which are typical for entry-level workers meant that the mean income would be slightly higher. More importantly, the Government's income statistics do not include capital gains, but do include the taxes on capital gains. Over the last 10 years, a significant number of people were attempting to shift their intake from ordinary income to capital gains income both to take advantage of the rapid stock market run-up and for tax reasons. In addition to the attempt to keep salaries down and replace the incentive with capital gains, there were very substantial capital gains. Again, these were not included in calculating the mean income. The truth is in point two.

2. Mean household wealth growth was growing faster than median household wealth, even before the decline in quality of public goods. The latest issue of the *Milken Institutes Review* focuses on class warfare. Here is the real story. Over the decade of the 1990s, median household wealth increased just under 4%, while mean wealth increased over 11%. Without a doubt, the top 5% did very, very well. On the other hand, the middle household barely kept pace with inflation.

This is a phenomenon that we all have been aware of and have built to. The number of new high-end resorts, high-end residential communities, and high-end golf courses has been phenomenal over the last decade. Many people sought to build the apartment for the renter by choice, particularly the higher income "infill" apartment. This list goes on and on.

1. The 21st century has less air at the top—$5 trillion to $8 trillion to $12 trillion gone. This is the most important switch since the Census. In the 1990s, the top 1%-5% of our society did very, very well. We are all aware that the stock market is down since the turn of the millennium, but it is possible to forget just how far down. American net worth at the end of the decade was close to $40 trillion. Already, $5 trillion is gone as evidenced by the drop in the Wilshire Index (the broadest measure of the value of all publicly traded equity issues). In other words, publicly traded equities have caused a reduction in our collective net worth by 12%. This has already happened and it's clearly recorded. It is highly likely that privately owned businesses have declined a similar percentage over the last two years. If this is the case, then the drop in net worth is $8 trillion rather than $5 trillion. Again, this has probably already happened, though in this case it's not as clearly recorded as with publicly traded equities. Finally, if commercial real estate and individual homes take a downtick following the general reduction in wealth, we could see as much as $12 trillion gone, or nearly a 1/3 of our end of century wealth.

These numbers are staggering. At the very least, they show a dramatic reversal of point two above. This has very obvious implications for a lot of the real estate that we have just built. Certainly, many of those developments will find fewer than expected customers with a reduction in "air at the top." On the positive side, after September 11, we will probably all be a little more focused on taking care of the other 95%.

Mike Miles
Editor