March 24, 1989

The Editor, Business Week
1221 Avenue of the Americas
NY NY 10020

Dear Sir:

We were pleased to see the reference to Henry George in your issue of March 27 in the article "The House Party is Winding Down." However, George was not simply offering advice on how to get rich by buying land; he was also warning that this was a problem to society. Buying land and holding it for a higher price may be all right for those playing the real life "Monopoly" game, but not so good for the rest of us. This is what keeps the dream of owning a home out of reach of most young seekers. The author of the article, Christopher Farrell notes this in his last sentence: "The worry now is making sure the American Dream doesn't become just a dream to the young and less-than-wealthy home-seekers in strong local economies."

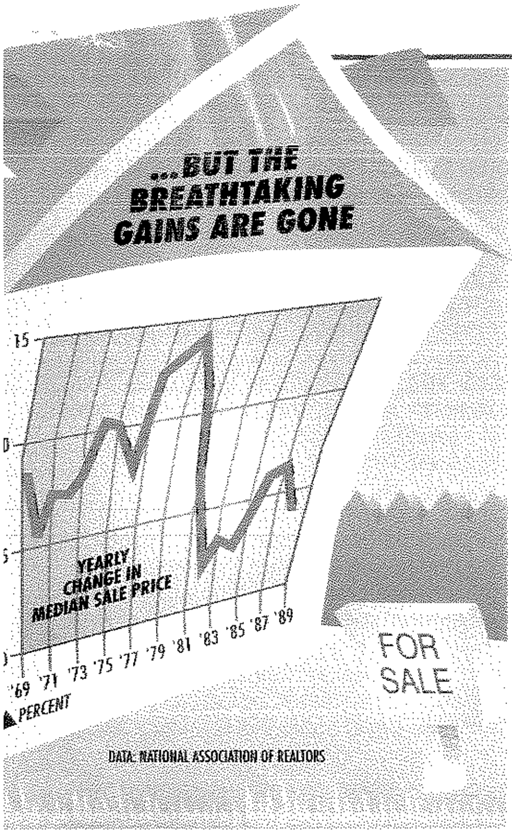
It should be noted too that the current decline in real estate prices is not likely to last forever. Land prices tend to be cyclical, but with each upswing the prices get higher.

Henry George had a proposal to deal with the situation - land value taxation. The idea is that the taxation of land values would put a damper on that part of the value which should be dampened - the speculative price of land. And along with this, there should be a concomitant lowering of the tax on the building.

Sincerely,

Robert Clancy
President

(H.G. [illegible])



biography of his father, famed boxer Joe Louis. On Jan. 25, he put his remodeled carriage house in Denver on the market for $289,000. A scant month later he sold it for $280,000.

In the Northeast, however, the boom is over. Boston home prices went from year-to-year gains of 35% in the mid-1980s to an anemic 2.4% last year. Prices will stay flat to slightly lower in New England, says Gary L. Ciminero, chief economist at Fleet/Norstar Financial Group Inc. In the New York City area, hit with a loss of roughly 20,000 jobs in the financial-services sector after the 1987 market crash, prices squeezed out a 2.9% gain for the year, but fell by 3.6% from the fourth quarter of 1987 to the same period in 1988. The Northeast's lackluster market even helped cool off Florida. "When it's soft up there, a drop in demand is sure to be felt here," says real estate economist Lewis M. Goodkin.

Indeed, some worry that the Northeast's worsening market is a harbinger of a nationwide real estate crash. For instance, Comstock Partners Inc., a New York-based money management firm, believes that real estate could fast become a depreciating asset. After all, says Comstock partner Michael Aronstein, "you can't say it's just a regional problem" since the Northeast accounts for some one-quarter of the nation's housing market.

Yet home-price weakness in the Northeast isn't about to snowball into an avalanche of collapsing prices that could bury the nation's economy. Instead, the workings of supply and demand suggest a stagnant market for several years.

First of all, real estate prices typically don't plunge absent a calamity, such as the Great Depression. More recently, plummeting oil prices sent the Southwest into an economic tailspin just as a home-building boom was going full tilt. By contrast, the Northeast "is a strong diversified economy that's not about to fall apart," says Wellesley College professor Karl E. Case. And many home sellers will take their "product" off the market if they don't like the price.

Helping to hold up prices are a panoply of local rules and regulations limiting the supply of new housing. Many folks in New York and Boston, for example, resist multifamily housing projects in their suburban communities as fiercely as they would a penitentiary.

BIG DISPARITY. Keeping a tight rein on price increases is the glaring disparity between prices and incomes. The time-honored rule is that a household can afford to pay about 2.5 times its annual income to buy a house. According to a Salomon Brothers Inc. report by Anthony Downs, senior fellow at the Brookings Institution, the median price in the New York area in the third quarter of 1988 was an astounding 7.1 times median income. It was 4.5 times income in Boston, 4.4 times in Providence, and 4 times in Hartford. "High housing prices are affecting the growth rate of certain economic areas," says Downs.

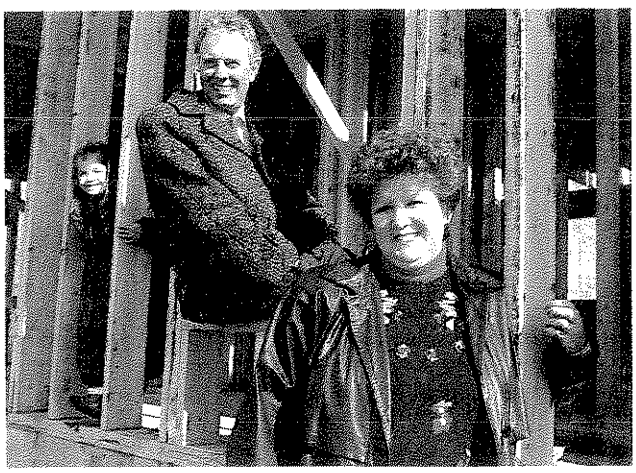
Astronomical housing costs make it difficult for employees to move into the Northeast. Take the experience of John and Barbara Jago-Ford. John, a national sales manager for Rostra Tool Co., moved from Florida to Connecticut last fall. They took a net $8,000 loss on selling their four-bedroom colonial for around $100,000 in the weak Orlando market in February. After months of searching for a comparable house they could afford, they finally found a builder willing to erect one in Madison for $264,000—after he cut the price by $30,000 to get the work. Even then, the Jago-Fords barely qualified for an 8⅞% ARM that adjusts upward in six months.

Many employees living in other regions are refusing to relocate. Some companies have decided that if their employees won't come to them, they'll move. J. C. Penney Co., for one, left New York City for the Dallas area.

It's not just a Northeastern problem. "Moving employees into California is very tricky," says Leonard Troutner, an executive at Coldwell Banker Relocation Management Services Inc. in Laguna Hills, Calif. In the so-called Research Triangle of North Carolina, the mayors of Raleigh and Durham recently joined representatives from banking, real estate, and nearby universities to form the Triangle Housing Partnership. Its mandate: help create affordable housing for moderate-income folks. The *Harvard Business Review* recently focused on the "convulsion in U. S. housing" that's adversely affecting businesses.

America's wealth is largely tied to the home. Some 64% of households own their own home—with a median sales price of $89,100. That compares with the meager 10% that own stock portfolios exceeding $5,000 in value. Americans need not worry that the value of their biggest asset is going to collapse. The worry now is making sure the American Dream doesn't become just a dream to the young and less-than-wealthy home-seekers in strong local economies.

By Christopher Farrell in New York, with bureau reports



STICKER SHOCK IN CONNECTICUT

Relocating to the Northeast was a jolt for John and Barbara Jago-Ford. They took a net loss on the sale of their Orlando home, spent months house-hunting, and ended paying nearly three times what their old house brought in

PHOTOGRAPH BY MELANIE EVE BAROCAS

THIS HOUSE PARTY IS WINDING DOWN

High interest rates and soft demand are putting a damper on prices

Go, get yourself a piece of ground, and hold possession.... You need do nothing more. You may sit down and smoke your pipe... and without doing one stroke of work, without adding one iota to the wealth of the community, in 10 years you will be rich.

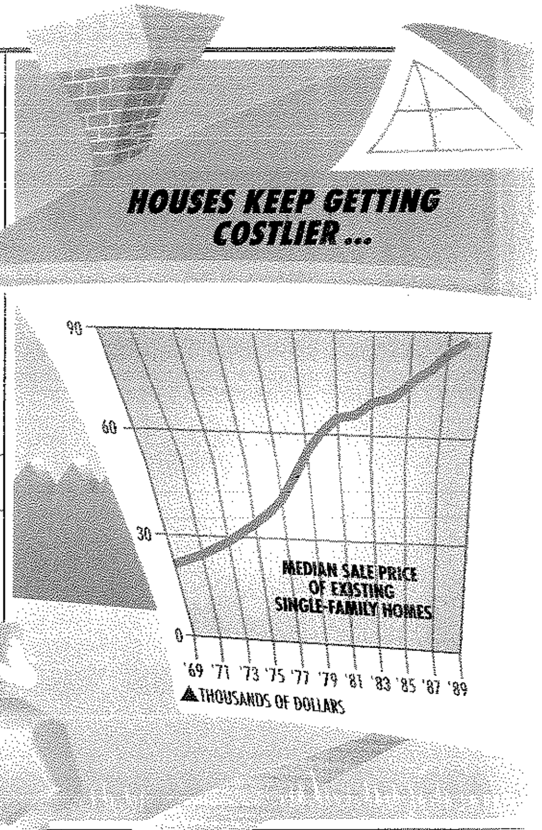
—Henry George

More than 100 years ago, economist Henry George foreshadowed the cocktail-party chatter of a generation made wealthy by soaring real estate prices. Home sweet home has not only been a great place to live but a superb investment as well. The nation's median home price jumped fourfold, from \$21,800 in 1969 to \$89,100 in 1988, while consumer prices generally tripled. There has been no place like home, at least as an investment.

Housing mania is peaking, though, despite inflation's recent resurgence. The rate of price hikes for single-family homes has declined significantly during the 1980s (chart). Short-term, rising interest rates could put further pressure on the market as homeowners struggle to meet their interest payments on the more than \$500 billion in adjustable-rate mortgages (ARMs) outstanding. Ditto for debtors owing nearly \$100 billion on home equity loans. In the longer term, demographic and economic forces will keep a lid on real estate appreciation.

Higher interest rates are already worrying home buyers who took out adjustable-rate loans during the past few years. "They'll face real payment shock," warns Warren Lasko, executive vice-president of the Mortgage Bankers Association of America. Eric Greenstein, president of a small executive-search company outside Boston, took out a big \$300,000 ARM in 1985. He expects that his mortgage rate will ratchet up by two points come August, boosting his yearly mortgage payment by some \$6,000. "The rate increase is going to strangle me," says Greenstein.

LESS DEMAND. Over the long haul, demographic trends, too, will dampen housing price gains. The 76 million baby boomers born between 1946 and 1964 helped fuel the home-buying binge that began in the 1970s. Home lust among baby boomers will be partly satiated in the 1990s. The baby-bust generation, the 41 million born between 1965 and 1976, will exert less pressure. And mind-boggling home price gains in metropolitan areas could slow local economic growth and contain real estate values. The first-time home buyer, for one, is priced out of a good number of economically important cities and their environs.



That is the bad news for homeowners. Now for the good news: Home prices aren't about to fall off a precipice. National home sale prices will at least track inflation. A BUSINESS WEEK survey of real estate markets around the country shows that most are in decent shape, with modest price increases and reasonably brisk sales. Indeed, there are signs that prices in the major regional markets will move closer together over time, as previously troubled markets recover and the hot markets peak.

The exception is California. It's in the throes of a fever-pitch boom. Prices of homes shot up by 32% in Los Angeles last year, lifting the median sales price to \$180,100. The San Francisco region saw prices rise by 28.1%, to \$206,500. Stoking California's hot market are job hunters and a growing crop of laws restricting development.

SIGNS OF LIFE. Many of the nation's worst markets are starting to show some signs of improvement. Median sale prices overall fell by 5.3% last year in Denver. But "there has been a tremendous improvement in sales of existing homes in the past 10 months," says Tucker Hart Adams, chief economist for Central Banks of Colorado. Just ask Joe Louis Barrow Jr., consultant and author of a

DENVER: ARE THE DOLDRUMS OVER?

■ *One of the nation's most depressed real estate markets seems to be recovering slightly. It took Joe Louis Barrow Jr., son of boxer Joe Louis, just one month this year to find a buyer willing to spend \$280,000 for his remodeled carriage house*

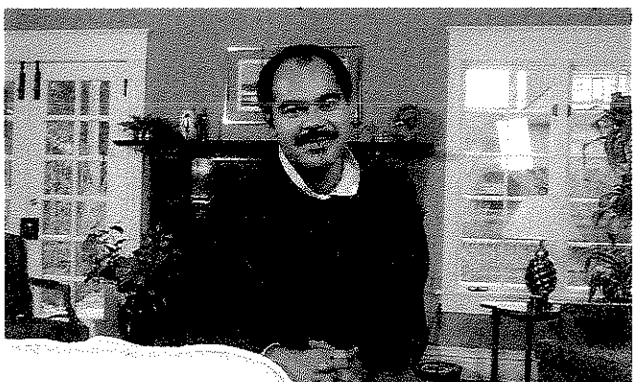


CHART BY ROB DOYLE/BW; PHOTOGRAPH BY ERIC BAKKE