THE NATIONAL
MARKET LETTER
PREPARED BY
REAL ESTATE RESEARCH CORPORATION

JAMES C. DOWNS, JR.
Editor and Publisher

ANTHONY DOWNS
Author Special Research Reports

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"TREND, TREND, WHICH WAY'S THE TREND?" That's the absorbing question which is being debated vigorously by the business and investment communities as the economy feels its way cautiously into 1967.

The difficulties of a definitive answer to the question first stated above lie in the apparent contradictions contained in the business and financial news as it unfolds day after day. For example: the rally in the stock and bond markets in the month of January seemed to be saying that the doubts and uncertainties of the year-end were really unfounded; that 1967 was going to be another strong year after all. And yet there was a nagging persistence to bearish bulletins about business itself. Automobile production was down 18% in January and 21.5% in the first half of February. Steel-making thus far in 1967 is off last year's pace, with mills currently operating at only 70% of capacity. Durable goods orders in January were down 5.1% from last year and business inventories were disturbingly high.

Through it all the war in Viet Nam keeps requiring more and more money: President Johnson's messages to the Congress point up the urgency of expanding the perimeters of the Great Society; unemployment in January held at the low level of 3.7% of the labor market (with many cities still below the "point-of-shortage"); and wages are continuing their trend of the past six months.

Although the rally in the bond and stock markets faltered in mid-February and bad news once again seemed to capture the spotlight of the public's attention, we have certainly not turned bearish. We still see no recession in the offing (by our definition) and we still would put 1967 in the "plus" column as a whole.

BASICALLY, OUR FORECASTING FOCUS IS ON CONSUMERS. During most of the year 1966, financial and capital factors were in bad trend. The stock markets were sagging, the money markets were demoralized and the whole real estate sector of the economy was dispirited. Yet consumers were more numerous, more prosperous and more fully employed. And business was good indeed!

In spite of the anomalous developments thus far in 1967, consumers are in better basic condition than they were a year ago! In most metropolitan areas, employment in this January was better than last year's. In all such areas, the average income of consumers is higher than it was at this time last year. And it is moving still higher!

It is true that about October 1, 1966, the chilling winds of doubt blew over the consumers of the U.S. with the result that their willingness to spend (not their capacity to spend) was momentarily curbed. While they waited to experience a resurgence of their buying enthusiasm, they increased their savings. In other words, they rested their buying oars and took advantage of the biggest inventory of their own goods in the history of the American family. But they did not change their fundamental habits! As spring comes --- and if their incomes hold (we think they will) --- they'll get right back into the spending stream to take advantage of the higher living standards which are within their grasp. And once they do that, we'll forget about the dwindling profits in the last quarter of 1966 and the first of 1967.

REAL ESTATE ACTIVITY NOT ONLY FAILED TO TURN AROUND in the first month of 1967, but it slipped further into the doldrums which had marked the last months of 1966. One of the reasons that the year-to-year comparisons with the first month of 1966 look so bad is that --- if you remember accurately --- last year started out impressively on the strong side, at least in the major activity factors of local real estate markets, with sales, mortgage lending and new construction well ahead of the previous year, in most areas.

Here is how these activity factors performed in the latest month for which complete national figures are available (January 1967):

Real Estate Sales

Off a little less than they were in December, sales for the nation were down 14.7% in January, with the following regional comparison with the same month last year:

Region	Percent Change
Northeast	8.0
Great Lakes	15.7
South	6.2
Central Prairie and Mountain	18.4
Pacific West	20.1

The reasons for the slow selling pace were not much changed from those which have prevailed in the past few months. The sharp drop in new home construction and completion was a major factor. Normally the sale of a new house results in from two to five sales of other dwelling units as occupants play a game of "musical chairs" in the upgrading process. No new houses; no occupancy shifts down the line. In addition, the promise of lower mortgage money rates (given wide publicity, especially since October) has caused many prospective buyers of existing houses to wait for better terms.

On the income property side, the rapid drop in money rates acted to lower realistic capitalization rates faster than prospective buyers could adjust their sights. Moreover, improved market conditions in most space markets (especially in the Northeast, Great Lakes and South regions) caused potential sellers to scent higher occupancies and rentals --- thus causing them to firm their ideas of value. Finally, a rapidly rising stock market proved a lure to speculators looking for a fast return on investment.

We look for unfavorable year-to-year comparisons in the sales markets to continue for the first quarter of this year, after which we expect measurable improvement.

Selected NATIONAL Economic Indicators

VALUE OF DOLLAR (1939 = 100) 41.54¢

INDICATOR	% CHANGE FROM A YEAR AGO	% CHANGE FROM A MONTH AGO
PRICES:		
Wholesale Prices	1.5	0.3
Building Costs	4.2	0.0
Farm Product Prices	-2.7	-1.2
Consumer Prices	3.3	0.0
Dow Jones Indl's (as of 2/23)	-11.0	-0.4
PRODUCTION, EMPLOYMENT, INCOME:		
Total Production	4.8	-0.7
Manufacturing	4.6	-0.7
Persons Employed	0.3	-0.1
Persons Unemployed	-0.5	0.3
Construction Employment	-0.2	0.2
Individual Income	8.4	0.9
Wages	2.6	-1.1
MONETARY FACTORS:		
Interest Rates	14.4	-1.6
Currency in Circulation	0.6	0.1
Government Debt	2.1	-0.1
Checks Cashed (Dollars)	15.4	4.6
Value of Dollar	-1.2	0.0

Data latest available for each factor.

Mortgage Lending

The national decline since last year in mortgage lending for the latest month

(January) was 33.5% in the number of mortgage loans closed and 42.4% in the total dollar volume of those loans. While mortgage money conditions continued to improve, the actual volume of lending was still low, due to the highly selective and cautious nature of lenders returning to the markets.

Here are the regional comparisons between the mortgage business in the latest month and that of the same month of 1966:

Region	Dollar Volume Percent Change	Number of Loans Percent Change
Northeast	50.1	29.6
Great Lakes	43.1	26.7
South	0.4	22.3
Central Prairie and Mountain	40.6	29.7
Pacific West	46.8	42.1

It is obvious from the above statistics that, through the month of January at least, the improvement in mortgage money conditions was largely theoretical and technical rather than actual --- as far as real estate lenders and borrowers were concerned.

As noted above, the drop of interest rates in the basic money markets during the month of January was a little less than remarkable. However, at the end of that month and all during February, these trends were reversed. Yields on treasury bills, municipals and corporates were up steadily, week-by-week in February.

This yo-yo action of money rates in the first eight weeks of 1967 was not reflected in the mortgage money rate situation. Reason: the supply-demand ratio in the mortgage money markets did not parallel that in the basic money markets. Here were the differences:

1. The savings flow into real estate-oriented institutions was greatly improved over a year ago. On the other hand, mortgage demand (in the kind of loans scared lenders now consider acceptable) was disappointing. As a result, on balance, there was more money than there were loans.

2. In the basic money markets, demand held high and supply was not meaningfully improved. Money lenders found that they had under-priced their commodity and took a second look at their potentials.

We see no particular "threat" in the February developments to the long-term trend of mortgage money. 1967 will continue to score improvements in this sector.

New Construction

One of the much-touted "bullish" factors cited by those who are optimistic about 1967 is the belief that the ailing home-building industry will stage a comeback in the year. So-called building stocks have shown outstanding strength on the nation's stock markets as speculators have hungrily snapped them up in anticipation of higher sales and earnings.

These sentiments have not only been encouraged by the statistics of housing construction in the past three months (January housing starts were at a seasonally adjusted annual rate of 1,243,000 units --- up 14.6% from December and up a whopping 47% from last October's postwar low), but by the longer range prospects for a dramatic increase in the number of young married couples starting in 1968.

Certainly (as this Letter has pointed out for several months), the residential markets in most local areas have gained strength in virtually all local areas --- and are postured for a burst of new supply in many.

In our opinion, the high expectations of the building industry (like those which have pushed savings and loan stocks skyward since last fall) tend to exaggerate the actual prospects for building profits --- either on the part of the developer or the materials manufacturer. The reason: the costs of money, materials, labor and land are such that development profits must await a higher general rental market to encourage and support a meaningfully higher volume of new construction.

The real profits are to be made in the purchase of good, sound, well-located and well-designed existing property which will experience sharply enhanced earning power before a new building boom can get started.

THE BIGGEST REAL ESTATE PROFITS IN THE PAST FIVE MONTHS have been made in real estate stocks. Our readers will remember that we set up a Real Estate Stock Index in October of 1965. On that date we assigned the figure of 100.0 to the prices of these securities which prevailed on October 1, 1965. Here is the record of those values, monthly, since that date:

Month	1965	1966	1967
January		106.9	101.5
February		110.1	
March		101.4	
April		108.3	
May		96.6	
June		95.1	
July		93.3	
August		83.4	
September		79.7	
October	100.0	75.2	
November	106.9	80.8	
December	105.1	84.4	

Even if these real estate stocks had been purchased on October 1, 1965, their owner would have done better than if he had bought the Dow Jones Industrials on the big board.

REAL ESTATE TRENDS AT A GLANCE

FACTOR	*% CHANGE FROM A YEAR AGO					
	NATIONAL	NORTH EAST REGION I	GREAT LAKES REGION II	SOUTH REGION III	PRAIRIE MOUNTAIN REGION IV	PACIFIC WEST REGION V
REAL ESTATE SALES (Number of Transactions)	17.2	14.0	18.1	9.6	14.8	21.6
MORTGAGE LENDING (Number of Loans Closed)	33.9	33.1	28.4	19.7	31.9	42.1
(Dollar Volume)	38.0	42.6	34.7	15.9	46.8	42.6
TOTAL BUILDING (Dollar Volume)	7.3	11.4	35.0	24.3	22.9	26.1
RESIDENTIAL (NEW) (No. of Projects Started)	35.2	37.2	43.6	19.7	44.2	48.3
(Dollar Volume)	45.5	20.3	47.6	28.2	55.1	60.0
NON-RESIDENTIAL (NEW) (Dollar Volume)	10.0	15.0	102.5	25.8	9.8	40.7
MARRIAGES	7.7	3.7	6.9	11.7	12.8	9.4
EVICTIONS	1.8	8.8	0.9	1.1	0.0	3.5

*Figures are based upon extension to National and Regional Levels of actual rates for QUARTER ending January 31, 1967.

SPECIAL RESEARCH REPORT

A LOOK AT THE "MODEL CITIES" PROGRAM

Last year, Congress passed legislation authorizing a new urban program to be administered by the Department of Housing and Urban Development (known as HUD). Originally known as the "Demonstration Cities Program," it was recently renamed the "Model Cities Program" to placate Congressmen who feared their constituents would think the bill encouraged civil rights marches and other "demonstrations!" Since this program may have important impacts upon big-city real estate markets, we will explore certain key aspects of it in this month's Special Research Report.

The Model Cities Program was originally devised to counteract the following undesirable tendencies which had appeared in the Federal government's attempts to aid cities, especially large central cities:

1. An enormous number of Federal programs were being administered by many different Federal --- and city --- departments without much coordination. A recent Office of Economic Opportunity manual lists over 250 Federal aid programs, most of which are applicable in cities.
2. Funds passed out under these programs tended to be widely dispersed over the urban landscape. Instead of really trying to upgrade a small area by focusing a whole battery of urban renewal, health, anti-delinquency, manpower training, education and other programs on it, the Federal government was scattering its shots too broadly. Hence each slum received too little assistance to counteract the forces "naturally" dominant there.
3. Each program assisted with Federal funds tended to be the same in all parts of a city, and often all over the country, both because one set of Federal rules governed it and because big-city bureaucracies wanted to adopt "uniform and equal" policies in all neighborhoods. As a result, specific programs were often badly adapted to the peculiar needs of non-typical neighborhoods, especially low-income ghettos.
4. A great deal of urban renewal assistance was designed not so much to eliminate blight or improve the living conditions of low-income residents, but to bolster the sagging economies of big-city downtown business districts. Thus the wealthy were the biggest beneficiaries, and the poor were merely shifted from one slum to another.

These complex maladies demanded a complex remedy --- and that is just what the Model Cities Program is designed to produce. In fact, the Guidelines describing how to apply for a grant to plan (but not execute) this program are over 50 pages long. Hence we can only mention their most salient features here, before analyzing some of their major implications.

Participation in the program by any given city involves three stages. The pre-application stage lasts until an application for a planning grant is completed and approved by HUD. No Federal financing is available for filling out an application. Yet it is so complex that many cities have spent months at it and only four have formally filed applications (as of February 25, 1967). HUD is likely to disapprove of almost everyone's application at first until it is adjusted to reasonable conformance with the many criteria described below. After HUD approval is obtained, the planning stage begins. This can last from six to twelve months, and can be financed up to 80% by HUD grants (though the total authorized to HUD for such planning is only $24 million over two years). Finally, for those few cities receiving final approval, the execution stage arrives. In this stage, each city will apply for normal Federal aid for specific programs in the Model City Area (such as 2/3 financing for urban renewal), and can get an additional "block grant" for up to 80% of the local share it would otherwise have to put up. This bonus can be used for additional activities in the Model Cities Area which would otherwise not be eligible for Federal assistance.

The myriad specific criteria which Model City plans must meet include the following major ones summarized from HUD's Program Guide:

1. The program must be comprehensive. Specifically, it should contain the following components: physical improvement, housing, transportation, education, manpower and economic development, recreation and cultural, crime reduction, health and social services and public assistance.

2. The program should provide for administrative machinery at the local level to carry out all its aspects on a consolidated and coordinated basis. Preferably, this means direct linkage to the mayor or other chief executive.

3. It should make a substantial impact on the physical, economic and social problems in the model neighborhood area.

4. It should remove or arrest blight and decay in the selected area or areas of the city.

5. It should be of sufficient magnitude to contribute to the sound development of the entire city.

6. It should make marked progress in reducing social and educational disadvantages, ill health, underemployment and lack of social services necessary to serve the poor and disadvantaged of the area.

7. It should provide for widespread citizen participation.

8. It should provide maximum opportunities for employing residents of the area in all phases of the program and enlarged opportunities for work and training.

9. It should contribute to a well-balanced city with a substantial increase in the supply of standard housing of low and moderate cost.

10. It should contribute to a well-balanced city with maximum opportunities in the choice of housing accommodations for all citizens of all income levels.

11. It should contribute to a well-balanced city with adequate public facilities, commercial facilities adequate to service the residential areas, and ease of access between residential areas and centers of employment.

12. It should provide for a comprehensive plan for the relocation of individuals, families, business concerns and nonprofit organizations.

In addition, each program should require re-examination of local laws, be consistent with comprehensive metropolitan-wide planning, be initiated within a short period of time (under five years), embody high standards of urban design, maintain historic sites, make maximum use of new technology, use cost-benefit analysis, conform to civil rights requirements, encourage maximum private enterprise, not reduce previous local spending in the Model City area, and be backed by adequate local resources.

In setting out this extraordinarily ambitious set of requirements, HUD is like a bachelor stating he will only marry a girl with Jacqueline Kennedy's poise, Jayne Mansfield's figure, Grace Kelly's face, Elizabeth Taylor's allure and Barbara Hutton's money! In fact, he would be fortunate to get any one of these charms, as HUD will be fortunate to get even a majority of its requirements actually met by any given city. Although each individual criterion seems justified, the group taken together constitute too radical a departure from present urban government practice to be fully achieved in any single city.

Specifically, we believe that HUD's program will encounter five major obstacles and will have to compromise with them in many cases. These are as follows:

1. All three of the major objectives of the Model Cities Program --- coordination, innovation and specific adaptation of programs to ghetto areas --- run counter to well-entrenched bureaucratic tendencies in city governments. City --- and Federal --- departments used to carrying out their own functions without much checking with each other will resist intimate cooperation in planning their programs. Moreover, innovation requires changing established behavior patterns, and few things are more difficult for large bureaucracies. Finally, the development of new programs tailored to the needs of ghetto residents, and different from programs in the rest of the city, will run counter to tendencies toward "equal treatment" and "uniformity" long established in some city departments.

   All three of these frictions will probably be greatest regarding big-city schools. Many school boards are relatively free from direct political control by city governments; hence it will be hard for mayors to get them to change their ways to fit these criteria. Yet schools are the most important single public institution in almost all ghettos. They alone have the potential power to make up for many of the home deficiencies suffered by children from deprived families. Hence if they are not effectively integrated into the Model Cities Program in a city, and given part of its bonus "block grants," it cannot really achieve its major goals. So one of the key tactics for any city trying to make this program work must be convincing school authorities of the need to create new programs specifically designed for ghetto areas, including programs which use school buildings for many kinds of non-educational activities (such as recreation, social service distribution and adult vocational training).

2. Concentration of leadership efforts on one Model City neighborhood will be necessary to make this program work; yet this contradicts the fundamental "Law of Over-Dispersion" sacred to politicians. The desire to gain widespread political support naturally leads elected officials to spread the benefits of any program to all areas under their jurisdiction, even though this causes a loss of the economic benefits of concentration. Hence city politicians will be sensitive to the charge of focusing too much attention on the Model City neighborhood, especially since it will be a low-tax-paying ghetto area. So they may provide only half-hearted leadership in support of such concentration.

3. Even if local areas succeed in establishing coordination among their own city departments and related agencies, there is no guarantee that Federal agencies will similarly cooperate in Washington. For example, when a city asks for a grant from the Department of Health, Education and Welfare that is urgently needed for its Model City Program, it may find itself at the end of the long "normal processing line" along with all other requests, including those in no way associated with Model Cities.

4. In large cities, it will be impossible to simultaneously meet the two criteria of significant impact on the city as a whole and intensive impact in the Model City neighborhood. If an area is large enough to be a significant slice of the entire city, it will be too big for this program to effect intensively, since total Model City funds are quite limited.

5. The housing requirement in the Guidelines is ambiguous. At one point, it says that the program must provide "a substantial increase in the supply of standard housing of low and moderate cost." But in the next sentence, it says "The program should add to the overall supply of low and moderate-income housing, not decrease it." The latter requirement is virtually impossible, since any clearance of substandard and deteriorated units, or reduction in overcrowding, will cause a decline in total supply of low-income housing. Even building new public housing will probably not increase this total supply, though it could easily increase the standard supply.

In spite of these drawbacks, the Model Cities Program is definitely a worthwhile experiment which could have significant long-run benefits --- if it is truly conceived of as a means of demonstrating techniques which will later be applied on a much larger scale. Specifically, it may create an incentive for at least some cities to do enough innovating, coordinating, concentrating and adapting of programs to particular needs to give local governments a "shot in the arm." But eventually this tiny shot must be followed by much larger appropriations than those as yet made for Model Cities if the lessons learned are to have any truly sizeable impact upon U.S. urban problems.

(The Special Research Report series on Change in Modern Society will be continued in a later issue.)