[Economist's View]

Be Prepared

Plan Now for the Next Downturn as Risks Rise

By Hugh F. Kelly, PhD, CRE

Parsing the economy has never been a simple task, but it has become vastly more difficult in the sea change wrought by the shifts in presidential administrations. Donald Trump ran on a platform of "shaking things up," bringing disruption to settled ways in government, in domestic and foreign relations, and in economic policy. Whether you approve or disapprove of his actions during his first weeks in office, it's fair to say that he proved true to his word.

Forecasting in such a period of disruption is fraught with uncertainty, and yet businesses must still do their best to anticipate the environment in which they will operate and for which they must budget. Unless we are to be paralyzed by confusion, the best tack is to adopt a truism attributed to Helmuth von Moltke, a 19th century German scholar and military strategist: Plans never survive the first contact with the enemy.

Another famous general's variation on the theme may be even more pertinent today. As Dwight D. Eisenhower put it, "In preparing for battle, I have always found that plans are useless but planning is indispensable." And the man who served Eisenhower as vice president offered one further insight that bears repeating. "We are all Keynesians now," Richard Nixon said late in his career. (For the record, Nixon was apparently quoting Milton Friedman.)

All in the Timing

For all the *sturm und drang* of this transitional time, the foundation of Trump's economic approach looks remarkably Keynesian, at least at first glance. His platform calls for lowering taxes, deregulating many industries including energy and finance, boosting military spending and infrastructure investment, and using the power of government and the bully pulpit to spur job growth. And given Mr. Trump's own background as a real estate developer, the commercial property industry should reasonably expect that its efforts will proceed relatively unfettered, at least in the short term.

Such a prescription for economic stimulus has traditionally been called a "Keynesian Yank." The problem is that the optimal timing for these tactics is when conditions are like those in 2008 and 2009—high unemployment, depressed asset values, and a private-sector economy struggling with low profits and systemically low demand.

Such is not the case at present, however. Immediately after the election, the stock market voted enthusiastically that the incoming administration would prompt a surge in economic growth from what was already a solid foundation of extended albeit moderate growth. At the same time, the bond market recognized that this increased risks of inflation and anticipated that the Federal Reserve would adopt an accelerated policy of monetary tightening in response.

For some time, I have been arguing in these

Map image by PeopleImages/iStockphoto.com

columns that the Fed's accommodative monetary policy had been pulling hard on its oar while legislative gridlock kept the fiscal policy oar out of the water. No wonder, I believed, that forward movement in the economy was so slow for so many years. That is what you get when economic policy is uncoordinated, as it has been since 2010.

Bumpy Road

Unfortunately, I have to say that policy coordination does not seem to be a high priority within the Trump White House so far. That is what makes forecasting at this time especially difficult. In a period in which a single party controls the executive branch and both houses of Congress, economic policy-making should be relatively clear. Especially during the first 100 days, the proverbial honeymoon period of a presidency, the path forward should be laid out smoothly.

However, that path appears to be unusually bumpy. Among the Republican majority, a significant cadre of conservative members opposes portions of the White House's agenda. Moreover, the president's combative approach could make enactment of a budget and the implementation of appropriations anything but smooth.

Against such a background, I believe the real estate community, and business in general, should be cautious. While economic expansions do not die of old age, we are already in the fourth-longest such cycle in U.S. history. No one has repealed the business cycle, and so at some point the risk of recession must be confronted. The likelihood is that a Keynesian stimulus applied at a moment of relative economic strength will cause some overheating that both normal supply/demand factors and Federal Reserve policy intervention will aim at correcting. I worry that this confluence of conditions raises the probability of a recession and advances its timing.

I have no better crystal ball than the senior real estate leaders who read *CPE*. But it seems to me, as a base case, real estate investors and executives should be developing contingency plans now for a 2018-2019 recession marked by a slowdown in trade, an increase in price inflation and a tightening in credit. If that doesn't transpire, I'll be as happy as the next guy. But sometimes the best offense is a good defense. Right now, I think it is wise to prepare for risks to the downside. CPE

—Hugh F. Kelly, PhD, CRE, was recently appointed Special Advisor to the Fordham Real Estate Institute at Lincoln Center. He previously taught for more than 30 years at the NYU Schack Institute of Real Estate. In 2014, Kelly served as national chair of the Counselors of Real Estate. He is the author, most recently, of 24-Hour Cities: Real Investment Performance, Not Just Promises, *published in 2016 by Routledge.*

WANT THE BEST COMMERCIAL REAL ESTATE NEWS AND INSIGHTS IN THE INDUSTRY?

COMMERCIAL PROPERTY EXECUTIVE™

Sign Up to Receive Our Newsletters!

SIGN UP