

NOTEBOOK

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How Long Can Housing Stay **Hot**?

Fears of a “housing bubble” are probably unfounded, but local deflation of housing prices can’t be ruled out

Throughout the recent recession and the current period of sluggish economic growth and bad news from Wall Street, housing has been the brightest spot in the nation’s economy. According to the National Association of Realtors, housing-related spending — which usually accounts for about \$1.40 out of every \$10 spent in the U.S. — last year rose to \$2 out of every \$10. During the first quarter of this year,

national home prices climbed by more than 8% compared to the same period a year earlier. In some particularly fast-growing markets, like metropolitan New York and Washington, D.C., price increases were in the 20% range.

Housing has been so hot, in fact, that it’s making some people nervous. In recent months, the news media has given a substantial amount of coverage to the idea that a “housing bubble” may be developing. What does that mean, and should builders be concerned?

Anatomy of a bubble. In economic terms, a speculative bubble is a wild run-up in prices that occurs when buyers make purchases based on what they believe they’ll be able to make when they sell, rather than for

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Thai Ties Find New Life as Flooring

Recycled railroad ties have long been used for landscaping and other rough projects, but a California company has recently taken recycling to a new level by milling salvage ties into finish flooring. The catch: These aren’t ordinary creosoted ties but tropical hardwood ties salvaged from Southeast Asian railways now in the process of switching over to concrete ties.

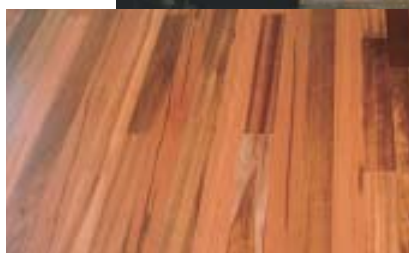
According to Richard McFarland of AsiaRain, Inc., in McCloud, Calif., most of the raw material for his company’s flooring comes from a thousand-mile rail line running the length of Thailand. Construction began in the late 1800s; workers used elephants to move timber that was processed into ties as the line advanced. The durable hardwoods used — including rosewood, narra, merbau, ironwood, padauk, and takien — were not treated with preservative but were replaced as needed during track maintenance, so they vary in age. The newest salvaged ties, McFarland notes, are 15 to 20 years old, while others date back to the original construction of the line, more than a century ago.

Workers in Thailand reprocess the ties into

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ASIARAIN, INC.



Workers in Thailand band-saw salvaged railroad ties into rough boards (top) that will be further processed into high-quality tropical hardwood flooring (left).

How Long Can Housing Stay Hot?

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any intrinsic value. In short, it's investment driven by what's sometimes described as the "greater fool" theory: the idea that it makes sense to pay an unreasonably high price for something as long as there's a greater fool somewhere who's willing to buy it for an even more inflated price.

That can mean big profits for a while, but such episodes always end badly. Those who invest just before the bubble bursts invariably lose their shirts, and often their pants as well. The recent spectacular rise and fall of technology stocks is a fine example of how the process works.

Hot air. Most economists, from Alan Greenspan on down, are convinced that talk of a national "housing bubble" is itself just so much hot air. NAHB economist Stanley Duobinis notes that true speculative bubbles almost always involve things like stocks that can be bought and sold quickly and easily. Housing, he argues, is much more resistant to speculation. "It takes time to sell a house," he says. "People don't get into that 'buy it today, sell it tomorrow' state of mind. Even if they did, closing costs would siphon off much of the profit. It's just not worth it." Localized housing bubbles are not completely unknown, Duobinis concedes — Houston experienced a classic boom-and-bust cycle in the early 1980s, as did southern New England a few years later — but a national housing bubble, he believes, is a practical impossibility.

Another factor arguing against the existence of a bubble, according to Fannie Mae economist Orawin Velz, is a shortage of buildable land stemming from federal, state, and local restrictions on development. In the recent past, Velz observes, a six-month inventory of unsold houses was considered normal; today that figure has fallen to three or four months — a change she ascribes largely to the scarcity of lots in many areas.

"We think this is a permanent phenomenon," she says.

Pent-up demand. If the current surge in demand for housing isn't a speculative bubble, what is it? Many experts believe it's a case of low interest rates reacting with pent-up demand for housing. Mortgage interest rates are currently at a 35-year low, which has permitted many renters to buy homes for the first time. (Ironically, bad news in other sectors of the economy has given housing a boost by encouraging the government to keep interest rates down.) Even though home prices are high, low interest rates have made monthly payments affordable for many.

Permits and jobs. But if the strong demand for housing is unlikely to burst suddenly, it is subject to gradual deflation, especially in regions where much of the current demand is provided by first-time and move-up home buyers. John Burns, a housing industry consultant in Irvine, Calif., explains that housing growth has traditionally been driven by job growth, as new workers coming into an area raise the demand for housing. Housing demand driven by job growth tends to be steady and long lasting, Burns notes. On the other hand, demand that's driven by low interest rates and an abundance of buyers can dry up fairly quickly if interest rates rise or the local supply of buyers peters out.

According to Burns, one way to monitor likely demand in a given area is to track the relationship between building permits and job growth. Historically, he points out, most metropolitan areas have added about 1.2 to 1.3 new jobs for each new housing unit. (Up-to-date figures on both job growth and total residential permits for most metropolitan areas are available at the NAHB website, Burns observes.) "If you're adding twenty jobs and only building twelve homes, it's a hot market," he says. "If you're adding one job and building ten homes, you have to wonder."

Thai Ties Find New Life

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high-quality kiln-dried 5/8-inch tongue-and-groove flooring that is end-matched and back-relieved. The material comes in random widths from 2 to 7 inches and in 12- to 78-inch lengths. It's impractical to sort the finished product by species, McFarland notes, so it's blended into a half-dozen color mixes, including a highly varied Classic Jungle Mix, a reddish Rose Mix that consists largely of rosewood, and a dark-hued Cinnamon Mix.

The recycled flooring is available to dealers for about \$6.50 per square foot, according to McFarland. "Some of it goes into commercial projects," he says, "but most of our output is going into mid- to high-end custom homes. It's a way for environmentally conscious customers to enjoy tropical hardwood without cutting any trees." For more information, call AsiaRain at 800/220-9062 or visit the company website at www.asiarainhardwoods.com.

OFFCUTS

A new antimicrobial paint from the New York-based Alistagen Corp. is said to be 99.9% effective at killing and preventing the growth of more than 20 microbes, including mold. The paint costs \$69 per gallon and is available in ten stock colors, including Trusted Fortress (an off white), Comfort Zone (blue), Twilight Sentry (gray), and Rest Assured (described by the manufacturer as "creme").

The Florida Home Builders Association has announced that it will work with state and regional work force development boards on a new effort meant to encourage high school students to consider careers in home building. The Get Into Building program is expected to inform students about opportunities in construction and provide contacts between high schools and local home builders' associations.

Home safes are emerging as a trendy home accessory, according to the *Wall Street Journal*. Concealed safes are popular, and one manufacturer has launched a line of minifridge-sized Home Appliance safes in a range of decorator colors.

Brick production in 2002 was among the highest in 30 years, according to figures released by the Brick Industry Association. Nearly 80% of the brick was used in single-family residential construction, with the South Atlantic region being the biggest single user.

Developers in Noblesville, Ind., must conceal the back yards of properties that can be seen from main roads. In July, the city council unanimously passed an ordinance requiring builders to orient homes so their front facades face the road, or conceal the back yards with berms or landscaping. The *Indianapolis Star* quoted one city councilman as saying, "Everything unattractive seems to collect in back yards."

Most U.S. homeowners have positive perceptions of treated wood, according to a recent Louisiana State University study summarized in the lumber industry newsletter *Random Lengths*. Despite the press surrounding the recent phaseout of CCA-treated lumber, the study found that only 5% of respondents had negative perceptions of treated wood. About 40% had somewhat positive impressions, and nearly a quarter had very positive perceptions.

Stanley to Stay Put

Stanley Works has abandoned its plan to reincorporate in Bermuda (see *Notebook*, 4/02). The proposed move, which the Connecticut-based tool and hardware manufacturer announced in February, would have saved the company an estimated \$30 million annually by permitting it to avoid U.S. taxes on overseas sales.

The plan proved controversial from the beginning, however, and drew widespread criticism from some shareholders, lawmakers, and labor groups. Although shareholders approved the proposal in May, Connecticut attorney general Richard Blumenthal filed suit to block the move on the grounds that the shareholder vote was marred by irregularities. Stanley sought to explain the reversal by saying that legislation now before Congress could address the tax issues that had prompted it to relocate, although it's not clear when or if such changes might be enacted.

Whatever the reason for the company's decision to remain in the U.S., labor groups and some Stanley employees were quick to declare victory. "The decision by Stanley Works to drop its infamous plan to avoid paying U.S. corporate taxes by moving its mailbox to Bermuda is a promising example of one company rejecting financial gimmicks," AFL-CIO president John Sweeney said in a prepared statement.

Fake Gates Yield Real Benefits

To a developer, gates are a mixed blessing. By some estimates, homes in gated communities sell for a 10% to 15% premium over similar homes in communities without gates. But while they may attract more affluent buyers, gates also impose costs: Because the roadway behind the gates is private rather than public, the cost of upkeep must be passed on to the residents. If the entrance includes a guardhouse, the cost of hiring and retaining security guards also goes on the tab.

The solution? According to recent stories by the *Los Angeles Times* and National Public Radio's *All Things Considered*, developers of high-priced residential communities on both coasts have learned to get the best of both



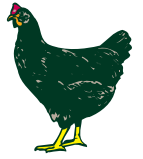
Developers of high-end residential communities are finding that fake gates and guardhouses provide most of the benefits of real ones, at a much lower cost.

worlds by erecting “gates” that aren’t. Such “faux-gated communities,” as they’re sometimes called, are ornamented with unoccupied guardhouses and impressive — but permanently open — gates or traffic barriers. City officials prefer the fake gates to real ones, because they do away with concerns over such issues as access for emergency vehicles. Residents are content because they get the prestige of gates without the monthly assessments — ranging from \$1,000 to \$12,000 a month — that real gated communities extract from inhabitants to pay for guards and street maintenance.

And according to Ed Blakely, the coauthor of a book on gated communities who was interviewed by the *Times*, the residents have good reason to be happy, since studies show that they may actually be safer without guards. Blakely notes that security guards have been known to take advantage of their inside knowledge by stealing from the homes they were hired to protect.

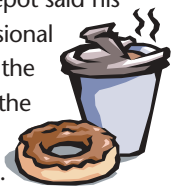
OFFCUTS

Chicken fat makes a fine heating fuel, researchers at the University of Georgia have found. According to *Energy Design Update*, the researchers fired a conventional oil burner with a number of experimental fuels, including chicken fat, lard, beef tallow, and used frying oil. Poultry fat reportedly has 16,500 Btus per pound, compared to 18,000 Btus per pound of fuel oil, at between one-half and one-third the price.



Vinyl siding shipments have declined for the past two years, according to a report in the roofing, siding, and insulation trade magazine *RSI*. Figures provided by the Vinyl Siding Institute show that shipments declined by 6% between 1999 and 2001 and by an additional 0.6% between 2000 and 2001.

Dunkin’ Donuts will be opening full-service donut shops inside Home Depot stores, beginning late this year. A spokesperson for Home Depot said his company’s research shows that professional builders often visit both chains during the morning hours. No word on whether the arrangement will also lead to an increased police presence in the stores.



Builders in Denver no longer have to landscape a new home to receive a certificate of occupancy, according to a temporary measure adopted by city building officials. A long-term drought, coupled with water-use restrictions, makes it pointless for builders to seed or sod new lawns, since homeowners can’t water them. For the time being, building officials are issuing temporary certificates of occupancy to builders who submit letters committing to landscape next summer.

Structural panel manufacturers are producing more 4x9 and 4x10 panels of plywood and OSB, according to the lumber newsletter *Random Lengths*. The trend is said to be driven by strong and growing demand for new homes with 9- and 10-foot ceilings. One manufacturer in the South reportedly predicted that his company’s sales of the larger panels will jump by 30% this year compared to 2001.

Smart Wiring: Growth but No Boom

What if they gave a digital revolution and nobody came? That's the question facing entrepreneurs on the cutting edge of smart-house technology. With the collapse of the dot-com bubble, high-tech hype is sounding a lot more hollow. The continuing stock slump across all industries, coupled with a stuttering economic recovery, has tech heads understandably worried.

"It wasn't too long ago that certain pundits had predicted multibillion-dollar forecasts for home networking components," wrote industry analyst Kurt Scherf in a January web article, "and 2001 was seen as a bellwether year.... In taking stock of the year, however, it is clear that home networking is taking a bit longer than many people had expected to mature and grow."

Scherf works for Parks Associates (www.parksassociates.com), a market research firm that specializes in digital technology for homes. In his article, he said that the explosive growth the smart-home industry is waiting for isn't likely before 2003 or even later. And speaking to *JLC*, he joked, "Ask any analyst, and it will always be 18 to 24 months away."

But seriously, says Scherf, his company's projections are based on a lot of real data. He points to the following indicators:

- PC-based networks will be in 5.5 to 6 million U.S. households by the end of 2002 — about a 5% market penetration.
- Home entertainment networks haven't progressed much beyond simple kits to connect computers to TVs. "The mass



Although smart-house technology has been slower to catch on than expected, it's still a good idea to install basic CAT-5 wiring in advance of the interior finish.

rollout of consumer electronics devices with embedded networking solutions has yet to occur — we sense a hesitancy by the consumer electronics industry."

- Residential gateways that link a house's broadband Internet access to a local network of computers are beginning to emerge, but there's still no convenient way to accommodate other systems such as stereos, VCRs, and appliance and lighting controls.


Given those realities, Scherf advises home builders to keep it simple. "We are recommending structured wiring with two runs of CAT-5 [the data wire used for local Ethernet connections] and also the RJ-6 quad-shielded coaxial cable for video distribution. Most smart solutions would connect to that. Just go ahead and get that behind the walls, with a home run to a central enclosure," says Scherf. People can use the CAT-5 wiring to share computer data, a printer, and Internet access (all common consumer wants), and the coax to connect TVs in different rooms to a single video source. And Scherf adds, "Builders should also look at offering other options that center on entertainment, such as prewiring for audio speakers."

International Codes Continue to Gain Ground

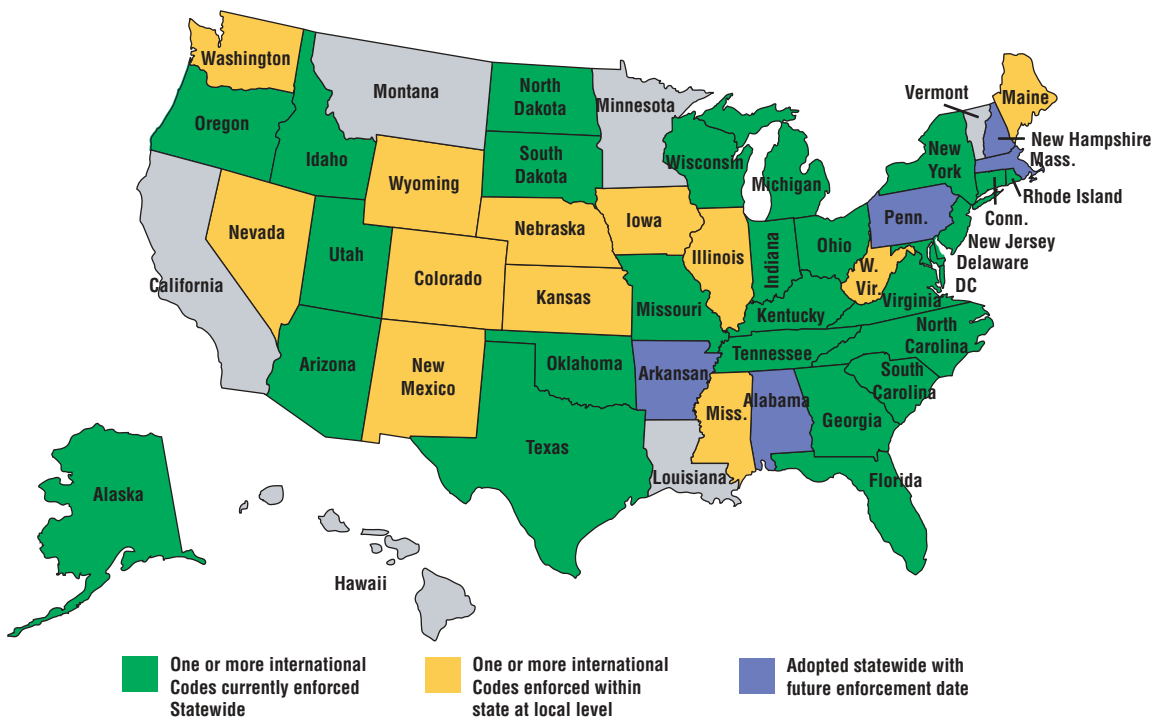
Efforts by the International Code Council (ICC) to unify building codes throughout the U.S. are continuing to make progress. This year, at least four states have adopted the *International Building Code (IBC)* as a statewide code, including two states — New Hampshire and New York — that have never before had a uniform statewide code. A map at the ICC’s website (www.intlcode.org/government/adoptions.htm) now shows only six states that have not adopted any international code at either the state or municipal level.

The newly adopted New York code, however, contains several modifications to the ICC model code. The *International Residential Code (IRC)* stair rule, which specifies a maximum 7³/₄-inch riser height and 10-inch tread width, was amended to allow 8¹/₄-inch risers and 9-inch treads. New York also inserted a requirement for

a 5/8-inch drywall fire barrier between a garage and an adjoining house, rather than the 1/2-inch drywall specified by the model code.

In August, the U.S. Department of Defense (DoD) selected the *International Building Code (IBC)* as a primary reference in its *Unified Facilities Criteria (UFC)*, a new document that governs the construction of facilities used by the U.S. armed forces. Federal law requires the DoD to use private-sector codes and standards as military construction standards wherever practical, in order to improve communication and efficiency. Although the military has modified some portions of the code to meet more stringent design specifications, referencing the *International Building Code* in the military standards means that contractors will be able to use many of the same systems and methods on military projects that they use in the civilian market. 

International Code Adoptions



The map above shows state and local adoption of international codes. An interactive version at the ICC website, www.intlcode.org/government/adoptions.htm, provides details on which codes have been adopted and at what level, with effective dates.