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Construction That Fueled Growth in the Sun Belt Slows

By JOHN COLLINS RUDOLF

PHOENIX — For years, business boomed at Gilberto Preciado’s home-furnishings store in a working-class neighborhood near downtown Phoenix. But on a recent afternoon his showroom was deserted. Other businesses in his strip mall have been shutting down at a brisk clip.

With a big grocery store nearby gone already, the parking lot was an empty field of asphalt baking in the sun. “You stand out there a couple of hours and you hear crickets,” Mr. Preciado said.

In a little more than three years, the Phoenix area has gone from the hottest of Sun Belt hot spots to one of the nation’s economic disaster areas. It is not alone in its rapid fall.

After riding high during the boom, the Las Vegas area, parts of southern Florida, and Southern California’s inland counties have also been brought low by plunging payrolls, billions lost in housing wealth, a continuing epidemic of foreclosures, record government budget deficits and stagnating populations.

These areas share one thing besides their warm climates. To a degree unmatched in the rest of the country, their recent prosperity was built not on manufacturing, technology or natural resources, but on construction and real estate — growth for its own sake.

As other areas tasted the excesses of the housing boom, they gorged on it. From 2002 to 2006, about 20 percent of private industry growth in the United States was tied to real estate and construction. In the Phoenix area, almost 36 percent of growth in the private economy during that period — more than $34 billion worth — came from real estate and construction.
That expansion was driven in large part by capital flows from Wall Street and abroad, which financed a wave of speculative residential and commercial development. Overbuilding, in turn, accelerated the region’s already rapid population growth.

In essence, many people began moving to Phoenix and other parts of the Sun Belt to build houses and stores for the next wave of people who would move there. Now, that influx has slowed or, in some places, stopped entirely.

“We’ve been on a growth sugar high, and you know what happens when a sugar high runs out,” said Scott Smith, mayor of Mesa, Ariz., a once-small Phoenix suburb that has become the nation’s 38th-largest city. “When it stops, the punishment is severe.”

Now, the long-term prospects for these regions are cloudy.

Their political leaders think that migration from the Rust Belt will inevitably rebound, in turn reviving residential construction. But some experts are skeptical, warning that a housing boom that was fed by reckless lending will prove difficult to resuscitate.

“Places that were built on real estate speculation or as retirement and second-home communities are going to have a harder time, unless they double down and begin to build real economies,” said Richard Florida, the urban theorist and author.

Even those who are relatively bullish on recovery for the former hot spots, like David Denslow, a professor of economics at the University of Florida, doubt that the extraordinary population growth seen in past decades will return anytime soon.

“Growth will never be what it was in the 1990s, and by no stretch of the imagination what it was in the early 2000s,” Professor Denslow said. “That is gone.”

It is clear in retrospect that in parts of the Sun Belt, the economic dependence on construction reached unhealthy levels in recent years.

In Orlando, Fla., for instance, construction and real estate accounted for almost 33 percent of all economic output by private industry in 2006, compared with a national average of about 20 percent, according to data from the United States Bureau of Economic Analysis. In the Miami, Las Vegas and Phoenix metropolitan areas, as well as California’s San Bernardino and Riverside counties, it was near or above 30 percent.

By contrast, in the Dallas-Fort Worth area, 18 percent of economic activity was in real estate and construction at the peak of the housing bubble. In Charlotte, N.C., it was just 15 percent.
Those cities have suffered during the recession, but not as much as the former boomtowns. Home prices in Charlotte are down only 11 percent from their peak, compared with 54 percent in Phoenix. And Charlotte’s job losses, while severe, are also spread almost evenly across several sectors. That is unlike Phoenix and Las Vegas, where job losses in construction have far outstripped those in other industries — down by 45 percent from their peak in Phoenix, for instance.

In Arizona, the construction job losses helped drive the unemployment rate to 9.2 percent this July, up from 3.7 percent the same month two years ago. Florida and Nevada, with unemployment at 10.7 percent and 12.5 percent respectively, are also struggling with high rates of joblessness.

While central Arizona has other economic pillars, including a substantial technology and aerospace industry, some experts say only a revival in residential construction can provide enough employment to return the region to strong growth.

“I really think we have to start building houses again to get the economy rolling,” said Marshall Vest, a University of Arizona economist who has written closely watched economic forecasts of the state for more than 30 years.

A strong housing recovery faces serious obstacles in all the former Sun Belt hot spots, however. Among them is the prospect that the population growth to which they have long been accustomed is stagnating, or even beginning to reverse.

Florida’s population shrank recently, for the first time since 1946. According to estimates by the University of Florida’s Bureau of Economic and Business Research, the state lost more than 58,000 residents in the year leading up to April 2009.

According to estimates by demographers in Clark County, Nev., Las Vegas also experienced population loss, about 9,000 people from July 2007 to July 2008. The shift amounts to a sea change for the city, which has had average population growth of 5.2 percent annually since 1991, one of the highest rates in the country.

(Other population estimates for Las Vegas, including those by the Census Bureau, show some growth during this period, in part because the formulas used to produce them are less responsive to rapid change in housing occupancy rates. Local demographers have adjusted their methodology to account for the increased number of homes built but never occupied, or left vacant by foreclosures.)
Stagnant and falling populations will further complicate efforts to dispose of the large inventory of unsold homes in these regions. The housing markets in all of them are saturated with foreclosures.

Even after housing inventories return to normal levels, builders face another hurdle: a banking industry that has been burned by construction bets in these former hot spots.

“I think the lenders are going to be very, very cautious,” said Jack Kyser, founding economist of the Kyser Center for Economic Research in Los Angeles.

Indeed, the role irrational lending played in driving economic growth in these regions was pronounced. Speculation led to a spree of overbuilding, drawing thousands to cities like Las Vegas and Phoenix for construction jobs. As these new arrivals themselves bought homes, the building boom took on a life of its own.

Retail spending surged, spurring a wave of commercial real estate development, in turn further lifting the construction industry. “We had growth based on growth,” said Keith Schwer, director of the Center for Business and Economic Research at the University of Nevada, Las Vegas.

When the boom ended, thousands of people were caught in the aftermath.

Brandi and Eric Wynne, with four children, bought a new home near Buckeye, Ariz., one of the most distant Phoenix suburbs, in 2007. Not long after they closed on their house, Mr. Wynne, 33, lost his job installing cabinets in new homes, and the couple fell behind on their mortgage.

On a Friday afternoon this July, Mrs. Wynne, 28, sold bric-a-brac in a yard sale while her husband packed boxes inside. On the curb sat a large yellow moving van. The bank was seizing the house the next Wednesday; by that time, the family would be on their way to St. Louis, where they had decided to move.

“This was our dream home,” said Mrs. Wynne. “Now we’re giving it back.”

The bust has also hit the immigrant-heavy working-class neighborhoods in the inner city. The Arizona Department of Health Services, using a formula based on birth trends, estimates that about 120,000 to 260,000 Hispanics have left the state since late 2007. Falling school enrollments and rising apartment vacancies in Hispanic neighborhoods also suggest a large out-migration is under way.
Gilberto Preciado’s home furnishings store, located in a working-class Hispanic neighborhood in central Phoenix, catered to the immigrant market, selling things like bedroom sets and refrigerators. The flow of new arrivals slowed sharply in the summer of 2007, Mr. Preciado said, and by the beginning of 2008, people were leaving the neighborhood, as job losses in the building trade rippled through the broader economy. Food City, a grocery store in his strip mall that had lured many shoppers, closed in July.

“Construction, the service industry — all that started trickling down,” Mr. Preciado said. “It was a domino effect.”

Mr. Preciado worked at his father’s furniture store during the last severe downturn, in the early 1980s, before striking out on his own 15 years ago. By his estimate, even the 1980s recession pales in comparison with today’s problems.

“Back when I opened up the business, I knew there were going to be bad days,” he said. “I never expected it to be this bad, though. I’ve never seen anything like this before.”

This article has been revised to reflect the following correction:

Correction: August 31, 2009
An article on Friday about the slowing influx of people and industry to Phoenix and other parts of the Sun Belt referred incorrectly in some editions to the losses in Arizona’s Hispanic population. The Arizona Department of Health Services estimates that 120,000 to 260,000 Hispanics have left the state as a whole, not just the Phoenix area, since late 2007.