ECONOMIC OUTLOOK

WEBINAR
3rd Quarter 2024

with WFG's Patrick Stone
and economist Dr. Bill Conerly

FULL TRANSCRIPT

Welcome with WFG Chairman and Founder Patrick Stone

“Why don't we go ahead and get started. My name is Pat Stone, I'm the chairman and founder of WFG National Title Insurance Company and with me today is Bill Conerly, probably the most accomplished business economist that I know. I have known Bill for 42 years and greatly respect his opinion. So Bill and I are going to address the economy, real estate and a few other issues today and we'll kick it off with Bill. Go ahead, Bill.”

Opening Commentary from Economist Bill Conerly, PhD

“Thank you Pat. Great to be with all of you. Sort of with. Imagine a hug here. I'm going to spend most of my preliminary remarks getting inside the head of the folks at the Federal Reserve. And I'll do that because interest rates are obviously critical for the business that you folks are in. But before I do that, let me give you a slightly broader perspective on the overall economy, and this is the kind of information that would be relevant to your clients' businesses in your community.

“We've had a couple of good quarters for GDP growth. I think that that is going to slow down for some other reasons. Consumers have been growing their spending at a moderate pace, but I think they're going to slow down. There's some sense that they are unhappy with high prices, inflation and will be moderate for that reason. But the bigger factor is those stimulus checks.

“Do you remember back in 2020 and January of 2021? A bunch of checks went out to almost all Americans except those at the very highest level of income. I hope that you guys did not receive a check because that would mean that you had earned a lot of money. But we had a lot of stimulus checks go out, but that money was not spent right away. Almost all of the money in the first year went to savings accounts or paying off credit card bills. It did not go into new spending. About a year later, people started tapping into that savings. But gradually and for the last couple of years we have had the economy being boosted a little bit by those stimulus checks slowly being spent. Well, the money's about gone. By my calculation, we've got two or three months left and then all of that's gone. That won't really be a negative. It simply means people are spending on current income, not past savings, but it's taking a positive away from the economy. So that will be a little bit negative.

“In other negative news, you know that construction of new single family homes has declined through most of this year. Not at a precipitous pace, but down. Multifamily construction is down with the lagged effects of higher interest rates. Non-residential construction has leveled off after a boom from chip fabs and data centers. I believe that business spending on equipment is going to taper down as the overall pace of economic growth slows down. But one of the positive sectors, at least short-term positive, is governments have been spending a good bit of money; both federal as well as state and local governments.

“So with that as a context, what's going on inside the head of the Federal Reserve? You'd like to get into the gray matter of Jay Powell. I've got a gray background and just imagine that is behind me. Not the globe, but the gray behind me is Jay Powell's brain. If I look carefully, I am seeing imprinted on his brain the dual mandate. Apparently the camera is not picking up the dual mandate, but what Jay Powell and the other folks at the Federal Reserve are thinking is that the Federal Reserve Act said that their job is to keep employment at maximum and inflation low. So maximum employment, low inflation. And as you know, they've been focusing on inflation the last few years, pushed interest rates up, and we

have seen significant improvement on interest rates. The measure that the Federal Reserve uses is a little different from the Consumer price index that gets the big headlines. We'll get a new reading on that tomorrow morning. But the Fed has brought their preferred measure of inflation down from about 5.5% to 2.6%. So that's a dramatic reduction of inflation. But their goal is 2.0% and the last little bit has been fairly stubborn. We've been stuck at 2.6% the last few months. The Federal Reserve though thinks, and I agree, that there's more inflation reduction in the pipeline. Monetary policy, the changes in interest rates and also the Federal Reserves' changes to their own balance sheet operate on the economy with a time lag and we're not completely through the time lag. So the Fed is saying they've brought inflation much lower and there's more to come in the pipeline. I agree with the concept. I'm a little bit nervous that they won't be able to get to their 2.0% inflation target. And part of the reason I'm nervous is so much federal stimulus, not from the Federal Reserve, but from fiscal policy, government spending minus taxes. Just a ton of money going in. So the Fed on the inflation side feels confident and I think if tomorrow morning's reading is not bad, they'll feel even more confident. So they're going to start focusing more on employment.

“Now, the employment situation has been good. Month after month we add more jobs. This year, the monthly net addition to jobs has been a little bit lower than it had been in the past, but it's still positive. But those people who go into the tea leaves, the details, are seeing little signs of softening. Things like how many people are voluntarily quitting their job. Usually they quit their job when they think there's another job available to them. The number of quits is down. The number of job openings that companies say they have is down a little bit. The number of people working as a percentage of the population of working age, that's down. None of these are down enough to be disastrous, but they're little signs of weakness. So inside the head of the folks at the Fed, they've got success on inflation with more to come and early small signs of weakness. They think it's time to turn monetary policy around and start easing.

“The Fed decision-making committee will meet next week, Tuesday and Wednesday. I believe that on Wednesday they'll announce a quarter point cut in the overnight interest rate that they manage. And let me emphasize that the interest rate they manage is not the same as what everyday people borrow at. So there has to be a linkage to borrowing rates, and I'll mention that in a moment. But I think the Fed will do like three cuts of a quarter point each this year. Next week, and then they take October off. They'll meet again in November and December. So I think three quarters of a percentage point by the end of 2024 and two or three more cuts in 2025 and then I think they will call it good.

“The other thing to keep in mind is that when they cut the short-term interest rates that does not necessarily feed into mortgage rates, which are the biggest concern for most of you on this call. And mortgages have been a little bit weird the last couple of years. When a mortgage is made, somebody goes to a local bank or a mortgage broker. The money for that is coming from Wall Street and its long-term investors, university endowments, life insurance companies, investors who want to put their money to work over a long-term period. And they can buy things like corporate bonds, treasury bonds, mortgage backed securities, and a mortgage backed security is just imagine a big basket and it's filled with 30 year mortgages. And when interest rates went up, the investors said we want to lock in these high interest rates, and the corporate bonds do that somewhat. The treasury bonds do that really well. But they looked at a bundle of 30-year mortgages issued with interest rates at 7%, 6.5%, and the investors said, you know what's going to happen when interest rates fall? All of these people who wanted to buy a house a couple of years ago and held their nose to pay a 7% mortgage, they're planning on refinancing as soon as they can. So if we buy a package of mortgage backed securities, we're going to get our cash back when interest rates are low. We don't want cash back when interest rates are low, we want to keep it working. So they have said, ‘yeah, we'll buy a mortgage backed security, but you have to pay us a really good yield.’ And that has meant that mortgage borrowers have to pay a pretty high yield.

“I think that spread of mortgage interest rates relative to treasury bond rates will come down and that will be the primary benefit from the Federal reserve cuts. But it's not going to come down like it had been. I'm thinking we get three quarters or a full percentage point cut in mortgage rates over the next year. And Pat, when you get the floor, I'd appreciate your thoughts on that subject as well.

“And let me close. When I give this presentation in person, people often come up to me, they buttonhole me and say, 'Hey Bill, what could go wrong with your forecast?' I'm like, 'What? You don't think I'm perfect? You think something's going to go wrong?' When I think about what could go wrong, yeah, there's a whole list of things that could go wrong and my list begins overseas. The Middle East with Israel. Hamas could expand that conflict.

“Iran is a problem in that area. I worry about that. There's also room for the Russia-Ukraine War to worsen in a way that has economic consequences. And I also worry a lot about China and perhaps using their conflict over Taiwan as an excuse to divert their public's attention from their own weak economy. So there are a lot of ways that the international scene could go wrong. Usually they don't. And usually my worst fears do not come to pass, but it's a possibility and a little bit of contingency planning on your part would make sense. So even though I think the US economy overall will grow at a slightly slower pace the next 12 months, I think that most of you in the real estate business will feel a net benefit driven by those lower interest rates. And with that, I'll turn it back to Pat.”

Opening Commentary from Patrick Stone

“Thank you Bill. And I'll just start off by sharing a message that you left unstated but conveyed there. And that is that we are in an interesting period of time regarding uncertainty and I made a little list of things to think about. Obviously the geopolitical issues, you nailed that. That's hard to plan for, but it is definitely worth worrying about. Inflation. I think you summed that up pretty well. The NAR commission lawsuit. I'll touch a little bit on that. Housing affordability, AI, AOLs (Attorney Opinion Letters) and limited title products, processing efficiency, strategy for the next two to three years, and the election cycle we're in. And then real estate supply and demand. I mean there's a tremendous amount of things to think about and worry about if you want to spend your time worrying. I suggest you spend your time planning, it's more constructive.

“But going through a few things here, the real estate industry is in a period of interesting transition. And I say that because virtually every component of the real estate industry has challenges. If you look at Realtors, the NAR lawsuit, the outcome of that is hard to predict and really uncertain at this point. The title industry. We’ve got the GSEs promoting attorney opinion letters and alternative title products, and I'll touch on that a little bit. The mortgage industry has actually been under fire now continuously since the financial crisis. There are a lot of acronyms around the mortgage industry: TILA, TRID HOEPA, CFPB, and RESPA. I mean there are just a whole bunch of things around the mortgage industry. So the whole industry is in transition, under examination and getting a lot of regulatory oversight.

“Starting with the real estate industry, and I'll keep this fairly brief, but it is kind of interesting. I did a little research on the history of NAR. The first iteration was the National Association of Real Estate Exchanges in 1908. In 1916 it changed its name to the National Association of Real Estate Boards, and in 1972 it became NAR. It's also interesting to look at the history of real estate commissions. Starting in 1913 the first one was at 2%. In 1920 it was raised to 2.5% and you had the initiation of a split in commission between the seller agent and the buyer agent. In 1940 it went to 5%. 1980 it went to 6%. So really a kind of intriguing progression in commission rates.

“If you look at commission rates, the average commission rate over the last 20 years has run pretty consistent between 5 and 6%. And the question now is will it drop because of the lawsuit? And I know that's being appealed with the hopes it'll get to the Supreme Court. We'll see. But there's about 1.5 million Realtors and about 1.3 million active Realtors right now, and everyone is speculating that the impact of this will be that the amount of Realtors declines. I suspect that that's the case because right now you have about 52% of people finding the home they want to buy on the internet and about 28% relying on the buyer agent. So people and the younger generations are becoming much more capable of using the internet and technology to find and explore and make decisions with regard to buying a home. So I think the commission lawsuit, which resulted in buyer agents having to have a contract with a buyer, is going to cause some reduction in the amount of Realtors. The most aggressive projection I saw was a guy named John Campbell who's the managing director of Stephens Incorporated, and he says 50% of agents will go away. I think he's predicting agents being about 750,000. I think that's a little low, to be honest with you, but we'll see what happens.

“There will be some decline and I think we should be really aware of it and be sure that we are planning for it because both title and mortgage are to a large extent depending on a referral and that's initiated by the Realtors. So if there's fewer Realtors, there's going to be fewer vendors. And so really take a hard look at what you're doing, take some time to examine your operation. We'll talk a little bit more about that a little bit later. But please, please, please really look at your operations, start thinking about what you can do with technology, automation, and training to achieve more efficiency and be more successful, because we are going to have some impact from this and it's going to be hard to avoid it.

“It's interesting to me. You look at the impact. Decreasing number of mortgage companies and decreasing number of title companies. What will happen and how do you go about being really competitive? I encourage all of you to really identify top listing agents, really develop relationships. Again, get more intent and more focused on the efficiency of your operation and how you operate.

“On the good news side, the (publicly traded) mortgage companies in Q2 showed earnings improvement almost across the board. So that was good to see. And we are seeing some upticks in a couple things. For example, if you do lower rates by 1%, you have about 7.2 million potential refis. Now, potential refis doesn't mean they're all going to get refinanced, but if you have that 1% reduction in mortgage rate that Bill was projecting, you're going to bring a lot of potential refis to the market. So what would be my best guess on that? Probably about 3 million actually refis, and that's business that you can and should get and pay attention to.

“Now, are we seeing any changes in inventory compared to the last couple of years? The media makes a big thing out of what's going on, but I don't see a lot of change. If you look at the first week of September’s housing inventory, it was up a little bit this year. 703,000 (units) versus 509,000 last year. In 2018 it was 1,195,000 (units). So we're still less than three quarters of what we had right before the pandemic. It's still pretty depressed. The average time on market goes up and down and it really follows seasonality more than anything. You run about 70 to 90 days in January and you get down in the fifties, and that's held surprisingly true even in this market. I think January of this year we were up fairly high. Now in July, we were down in the 50 (day) range. So I don't see a great deal to worry about there.

“I'll give you some numbers that we follow here at WFG just for fun. Something's going on right now, we are seeing a fairly significant increase in activity right now. What did I mean by right now? The first week of September versus the first week of August, our resale orders are up 19%. Versus the first week of September in 2023, our resale orders are up 45%. Versus the first week of September in 2022, our resale orders are up 49%. I mean that is an astounding increase at the wrong time of year. Traditionally in September you start seeing a decline, not an increase. Refis are up 7% over August, up 152% over September of 2023 and up 86% over September of 2022.

“Now that's us, but we also have a national title services function and they do title examinations for our direct operations, for our lender services (division) and for our agents. And NTS orders from agents this month are up almost 20% over the same time last month. So this is not just us, this is happening across the board and it's meaningful. So I think it's encouraging, and I don't want to get overly optimistic, but I think we are seeing a turn and if Bill's right on the 1% drop, I think we're going to get back to the point where the business gets fruitful, if you will.

“One thing I have noticed, and I think it's really worth paying attention to, is the fallout. (There have been) a lot of conversations in the last six months, even the last year to year and a half, about the percentage of deals that people make offers on, then they don't close. They basically fall out. I did a little examination of this just out of curiosity, (to determine) if it was directly related to price range. In other words, directly related to the economic wherewithal of the person buying the home. And to give you an example here, the fallout ratio for three months -- June, July and August of this year for WFG – (for transactions valued from) $0 to $500,000, we had a 33.3% cancellation rate on those orders. So a third of them fell out below $500,000. For deals from $500,000 to $1 million we had a 16.9% fallout rate. So just about half (the fallout rate) of the lower segment. (For deals from) $1 million to $1.5 million, (we had a) 10.5% fallout ratio and (for deals) over $1.5 million, 9.9% (fallout). So there is a direct and meaningful correlation between price range and fallout. Now as a manager, what would I tell people? Let's focus on trying to get higher price deals. (There is a) much higher chance of them closing, and much less chance of us wasting time and money doing work we don't get paid for. Obviously that's a huge difference in the fallout ratio and that directly reflects the affordability issue.

“Last session we talked about affordability and we talked about how hard it is right now in terms of affordability for a lot of people. Right at the current rate, it takes about 35% of the average salary in monthly payments, and that's way too high. It needs to be down around 30%. (If) we get another one point percentage off mortgage rates, we'll get down to between 30 and 31% for mortgage payments on the average salary. So 1% will make a huge difference in our business. It will dramatically increase the volume of business and it will dramatically, I hope, increase the amount of deals closing.

“Real quickly on commercial, I have expressed in the past some concerns about all of the commercial loans that needed to be refinanced by the end of 2025. And I'll be honest with you, I thought there was a lot of money on the sidelines to pick these up or to abate the impact of this. But I also will tell you that I'm a little bit more optimistic now about the commercial market itself than I was before. All segments of the commercial market except office are actually doing fairly

well. Green Street Advisors, which is the leading analytic firm in my opinion on commercial real estate, feels pretty good about everything except major city office buildings. Now that doesn't mean that they are going to completely crash, but that's the one segment that is still up in the air, if you will, a little bit. The commercial loan delinquency rate right now is 1.45%. So I don't think we're going to have a major, major impact from the refinance cycle that will occur in 2025.

“Interesting statistic, and this amazed me, office foot traffic nationwide has reached 72.2% of the July 2019 level. What they're measuring here is the usage of the office and they're saying basically we're back to using offices about 72% of what we used in July of 2019. The top five highest cities with percentage of office visits: Miami, Florida 90.6%, New York City 89.6%, Dallas 76.9%, Atlanta 76.7%, and Washington, DC 73.9%. So we are seeing probably more usage of offices than we anticipated, and I'm cautiously optimistic that we will have a recovery there and we won't have a major calamity with offices or with the refi cycle by the end of 2025.

“Finally, builders are ramping up and (there’s) a lot of talk about this. We are seeing a significant increase in the amount of building permits. One thing that does bother me, and I think bothers every builder in the business, is that the average cost of dealing with the regulators, the counties, the cities, and all the things that it takes to get a permit to build and get it built is running about $98,000 a home and that is absurd. And that is having a big impact obviously on the cost and profitability of building homes. Nonetheless, you are seeing a meaningful increase right now in permits and units under construction. So the question is, are we going to have a shortfall that causes prices to go up again? I don't think so. I think we'll get up to about 1.15 million in new homes by the end of this year on an annualized basis. And that's enough, I think, along with the resale activity and the fact that a lot of homes are owned by older people and they will be selling and moving to retirement centers or basically getting rid of their homes. So I think the amount of supply will be sufficient to offset the increased demand. It's worth watching, but I don't think we'll see a huge price increase. I think prices will stay between 3 to 5% appreciation for the next three to five years. I don't see a crash and I don't see a significant price increase. So knock on wood, I'm relatively optimistic, but probably more optimistic right now than I have been in a long time, especially if I ignore the national and international news, then I do real fine. So with that, we'll get to the question segment.”

Question and Answer Segment

Is the US headed toward a recession?

Bill Conerly’s response:

“I think not, but let me start with a little bit of humility. I went through an exercise some years back of looking at economists' forecasts, the aggregate of all US economists in the years before recessions. And I've got to say we did a very poor job of telling the public whether there was going to be a recession. So don't count on me to clue you in if we're going to have a recession. But recessions are usually caused by overly aggressive monetary policy, interest rates tightening too much. It looks like this time we're going into a soft landing, that we had the tightening not resulting in a recession. And those of you who've been following us every quarter know that I was predicting a recession. Looks like it's not going to happen. Jay Powell at the Federal Reserve says he doesn't use that phrase soft landing. I think he doesn't want to jinx it, but it looks like that's what we're getting. But I would suggest that because it's so hard to forecast a recession, I would suggest everybody do some contingency planning.”

How do recessions typically hit the real estate sector of the economy?

Patrick Stone’s response:

“Well, they dramatically impact the real estate sector. I mean, a lot of people buying homes, and you've heard this expression many times, making the biggest financial decision of their life and they're obligating themselves to a 30-year mortgage. They're obligating themselves to put a significant down payment on the table. It is a huge decision to make if you're concerned about the economy, concerned about your company, your job, where this is all going to go. Rightfully so, your natural instinct is to say, ‘wait a minute, I'm not going to step out and take any risk right now.’ So recessions

always impact real estate. They will impact real estate to the degree that they are severe and for how long they last. So minor recessions sometimes actually lower rates and you don't see a tremendous impact. Long-term recessions and severe recessions impact real estate dramatically."

What are your thoughts on the value of the US dollar? Some folks think that they're bracing for a recession and that'll impact our dollar.

Dr. Bill Conerly's response:

"Yeah, the dollar goes up and down for a variety of reasons. One is if you're in recession, typically the dollar declines. But interest rates in one country relative to other countries affect the foreign exchange rate. And when our interest rates are higher than other country's interest rates, then the dollar is strong and the dollar has been very strong lately. It is not at an all-time record, but it's pretty close to it. I follow a measure that basically looks at an average exchange rate across all the major countries and we have that data back to like 1970 and we are close to an all-time record, not quite there, but pretty close to it. So the dollar is high. Let me tell you how it affects your community. Most of you are working in a business that's tied to local communities. For much of the country, whether the dollar is strong or weak against the euro, the yen, the yuan, whatever, it doesn't make much difference. But if your community has a significant number of import or export companies, it does make a difference. The strong dollar means that it's relatively cheap for Americans to buy foreign imports and it's hard for American exporters to get people to pay when they have to pay a lot to get the dollars to pay. So we're seeing that right now with our imports up and our exports kind of flat. But for most of you, I think you can pretty much ignore the dollar. And if the dollar does come down, I don't think it's going to harm any of you unless your community is dependent on some imports that would be more costly."

There's a lot of attention about this in our NAR settlement. Can you go a little bit deeper on what are the changing practices we're seeing and how it's affecting the real estate outlook?

Patrick Stone's response:

"Well, if you look at it from our side of the business, the placement of title insurance varies by market. For the most part, the listing agent will control the decision regarding who gets a title order. If you're in the mortgage business, the buyer obviously is taking out the mortgage and the buying agent will decide or influence where the buyer goes to get a mortgage. So my personal opinion, and this is nothing but an opinion, is that there will be more impact from this on the mortgage side than on the title side because the bulk of the title orders nationally are tied to the sell side of the transaction. Will it impact the overall business level? I don't think it will. Candidly, one of the reasons I went through the history of the commission rate was that we see that actually we did quite well for a long time at lesser commissions, but also I think the fact that so many people, younger people are accessing information online mitigates some of the impact of the reduction in buyer agents. And I think anybody under 30 or 35, they're going to find their home online. Period. So that's my personal opinion. I think it'll have a minimum impact on us and more of an impact on the mortgage side, at least in a transitionary manner."

Are the numbers we see on unemployment reliable?

Dr. Bill Conerly's response:

"Yeah, it depends on how you're using them. I'll try to stay out of the weeds, but all of our economic statistics, whether it's the unemployment rate, the inflation rate, GDP, are based on estimates that come from a survey. We don't have comprehensive data on everything. When Big Brother starts tracking every transaction in the country, maybe we'll have better data. So is the unemployment rate actually what they publish it? No, but what I do is I'm tracking it over time. So I don't care if the unemployment rate is actually 4.3%. I'm assuming that whatever errors are in there are fairly consistent. So when I see the unemployment rate go from 3.5% to 4.3%, I'm like, okay, the unemployment rate is going up, but it's not too high. So I would suggest all economic data that crosses your desk, you just think, okay, it is not

perfectly accurate. But the trend over time, the change is important. And this is especially important if you look at headlines. Whenever the data comes out, I produce a chart for my own benefit and I'll see wiggle, wiggle, wiggle, wiggle, wiggle, and then I'll look at a headline that says, this measure dropped this quarter. And I'm like, 'Hey man, it's just a normal fluctuation within the range of normal fluctuations, no big deal.' And I yell at the newspaper. My wife is getting tired of that, let me say."

What is the status of title insurance not being required for refinanced government backed primary homes?

Patrick Stone's response:

"Well, there's a lot going on here, and please forgive me if I am cynical about the motivation behind all this and also concerned that the lack of understanding on the part of the politicians is going to cause a problem. So we've had the Fannie and Freddie title insurance waiver program and we have Fannie that did an RFP for a pilot program on refinance transactions with loan-to-value ratios below 80%. So there's a couple things going on there that I don't really like, but I think they're politically motivated under the guise of lowering the cost of home ownership. Truthfully, title insurance is not the major contributor to the cost of home ownership. And there is one thing I don't think the regulators understand, and I'll share this with everybody. If you look at the loss ratio in the title insurance industry, it's been $14.8 billion over the last 20 years. What I'm saying to you here is that our losses run on average over $700 million a year after we do all the risk elimination of title examination.

"So if you take that away, even if you qualify it carefully by (targeting) refinances on homes with a lot of equity, you're still going to have a problem. And I'll tell you why. Because on average, one third of losses are (due to) fraud or forgery. Well, let me be more precise. 30 to 33% (of loss) annually is (due to) fraud or forgery. Now what goes unspoken here is that the title insurance industry and the escrow industry combined eliminate 75% of the risk of fraud and forgery. I did a little study of all the times we caught someone trying to commit fraud or forgery, and then all the times that we didn't, we catch them 75% of the time. So why don't you just eliminate us and see what happens? We're going to take the whole industry down the tube if we do that. So my personal opinion on this is we're going to go through a process where they test this, they try this, they may even implement it for a while on a minimal segment of the market, but I think common sense will prevail, especially after they get whacked a couple times with fraud and forgery. They'll understand that we do have a value and we are essential to the process. So that's my opinion, under the heading of for what it's worth."

Do you think the economy can get out of the circus of the election? Historically, do presidential elections affect the real estate market and how do you think this election is going to affect the mortgage and real estate industry? How will interest rates differ depending on the outcome of the election?

Dr. Bill Conerly's response:

"Yeah, why do I have to deal with the election Pat? So first of all, on the historical questions, I have looked in the past at there's a common belief that the Federal Reserve cuts interest rates before the election to try to influence it for the incumbent. That is not true. I think the Fed will cut interest rates before the election this year, but they have raised interest rates in election years in the past. It goes up, it goes down. There's no pattern. I also looked at the housing market around elections and I don't see any effect at all. I looked at charts going back to the beginning of data and I don't think it has much impact. So I don't think the election itself has an impact. And in terms of the candidates, I'm not going to tell you how to vote, but I am going to tell you that if you asked one of these questions, no insult intended, you're putting too much time and energy and thought into the election. Yeah, it's going to happen. Make a vote when the time comes, but your destiny is not going to be driven by this election. Your destiny is going to be driven by how well you serve customers, how well you control costs, how well you retain your most productive employees. That's your destiny. And the election is just a minor thing.

“One element that is maybe worth paying a little attention to. One of the candidates, President Trump, said he wanted to be more involved in Federal Reserve decisions on interest rates. Now, those of you who have spent time hanging out with real estate developers know that they believe interest rates should be lower all the time under all conditions, and they're not too worried about inflation because inflation tends to boost the values of their properties. And I think that if the new president, whether it's Trump or Harris, said, 'Hey, can I sit in on a meeting of the Federal Reserve?' It's hard to say no to the president who wants to sit in and it's hard to shut the person up if the person wants to talk. But let's review the structure, the policy making. The Federal Open Market Committee makes the policy. It's 19 people, seven who are members of the Federal Reserve Board appointed by the president, but on a staggered term. So the new president will gradually over time be able to turn the Federal Reserve Board over. But depending on early retirements and the like, it may take four years to turn over. The board could take as long as seven to turn it over completely. In addition, there are 12 of the regional Federal Reserve Bank presidents sitting on this committee. They don't all have a vote at the same time, but they are important parts of the discussion. And those presidents are elected by their regional boards of directors subject to approval by the Federal Reserve Board. So you've got a system with a lot of slow, gradual change built in. So even if a president wanted to have a hand in it, I don't think the president would be successful early on and then four years later, who knows what's going to happen. So I'm not too concerned about that, but it is something that I guess I have a little bit of concern that we don't want to get into political control of monetary policy. The countries that have tried it have not fared well.”

What are the recent regulatory trends that agents should try to stay ahead of?

Patrick Stone’s response:

“Well, I think the big thing right now is ABAs. We've seen the Attorney General in Washington, DC entered into a consent order with several title agents engaged in ABAs, which included significant monetary fines. I think that the approach by the DC Attorney General ignores the safe harbor provisions of RESPA and seems to focus on the misguided view that title premiums are too high, so it seems almost politically motivated, if you will. There may be other regulators motivated or influenced or encouraged to take action in their states based on this. What I would encourage everybody out there to do is make sure that if there's interest in forming an affiliated business relationship or a joint venture, that you seek competent legal counsel and construct a relationship that is defensible under corporate law and based on your legal counsel's advice. So it can't be a process to get money back to the Realtor. And I think that's happened in some markets with ABAs and so forth. I think we're going to need to be very, very careful and make sure you've got competent legal advice.

“And then the only other thing on the regulatory front right now that is top of mind is the expansion of the US Treasury FinCEN reporting effective in December of 2025. That requires title agents and others to report on all cash transactions involving equity buyers in all jurisdictions. This is a significant expansion of the FinCEN and geographical targeting orders, which currently require reporting in selected counties for transactions of $300,000 or more. So what has been done on a limited basis is going to become universal and broadly applied. So get ready for that one. You've got a year plus to get ready for it, so it's not right around the corner. In the interim, make sure if you do anything -- JV, ABA, any kind of relationship -- make sure that you have competent legal advice on how to construct it and defend it because it has become fashionable, if you will, for regulators to poke at it.”

What would be the best response when clients ask about market predictions, especially when it's hard to predict?

Dr. Bill Conerly’s response:

“Yeah. Well, and it always is hard to predict. Let me begin by telling you what I have said when I've been asked that question. I've been asked that question, gee, I think I was even an undergraduate economics major and people would ask me as if I knew anything at that point, thinking, ‘well, he studies economics, maybe he knows what's going to happen.’ The advice I give to prospective home buyers first of all is if it's a good house for you and your family at a price and interest rate that you can afford, go ahead and buy it. Don't buy it if you can't afford it just because you think you

will be able to afford it or it will appreciate in the future and don't wait to buy it because you think you'll get a better deal in the future. Interest rates are very hard to predict. And the best thing to keep in mind with respect to that is suppose that everybody in the country said, 'oh, bond interest rates are going to go up in a month.' Well, those interest rates would change instantly as soon as people realized they were going to change in the future because who wants to wait a month when you can arbitrage that change? So interest rates are very, very hard to predict. Home prices maybe a little bit, but not much. And we've seen people look at a trend and say, well, it's been going up 5% or it's been going up by 10%, but that doesn't mean that's going to happen the next month or the month after. So come back to fundamentals. And I would say that's probably true with all steps of the real estate process, including buying the house, getting the mortgage, refinancing the mortgage and all of that."

I talked about interest rates. Pat, do you have any thoughts you want to throw in?

Patrick Stone's response:

"No, I actually worked on Wall Street a little bit and your comment about immediate response to projections or expectations is very true. The amount of arbitrage and the amount of investment dollars that chase trends with regard to interest is very, very, very profound. I would say this, personally, I'm looking at seeing mortgage rates under 6% by the end of the year because I agree with your earlier comment about potentially three rate drops of a quarter each. I think at least two for sure, and quite possibly three. I think even two will result in mortgage rates coming down under 6%, and I see mortgage rates at 5.5% by the end of next year. Now, some of the GSCs and some other people predicting are saying 6% by mid next year. I think they're way, way too conservative. Candidly, I think they'll come down faster than that. As everybody probably knows, historically, mortgage rates are 1.5% to 2% above the 10-year T-bill. If they were one and a half to 2% above the 10-year T-bill this morning, they'd be at 5.2 to 5.7%. So I do think they're going to come down. I think they're going to come down in a fairly meaningful manner.

"Can I go back to something I said earlier, Bill, and correct it? I apologize to everybody. I couldn't find my notes. I was talking about days on market from December of 2017 to December of 2020 and in January it was always 80-plus days on market. In July, for the same period, 2017 to 2020, it was 52 to 55 days on the market. This year, in January, we were 70 days on market. In July, we were 53 days on the market. So July of this year compared exactly to July of 2017 to 2020. So we are, I think, returning to normality in a lot of ways."

Will lenders be open to modifying and extending these commercial loans I was talking about by the end of 2025? And if so, does the Fed interest rate cuts help or hurt commercial real estate landlords over the next one to two years?

Dr. Bill Conerly's response:

"Yeah. Well, for those of you who don't live in the commercial space, let me say that most of the commercial mortgages are not like a fixed-rate for 30 years. They change, sometimes a floating rate, sometimes every five years or so. So the rise in interest rates really hurt those landlords who suddenly had to pay higher interest rates. With the combination of higher interest rates and weak occupancy for particularly downtown offices, a lot of lenders have been doing what we call extend and pretend. You extend the length of the loan and pretend that it's going to get paid. And you don't want to actually say, 'no, this is a bad loan.' And they probably aren't bad loans, but they may be slow to pay and there may have to be some concession on the principle in a few cases. But I think that the banks are recognizing that you can't hold somebody to a deal that is just wholly uneconomic. Even if legally you can, practically it doesn't make sense. So I think there will be some relief. In some cases there will be foreclosures, but I don't think it's enough to take the whole commercial banking sector down as we saw in 2008 with single family homes. And when interest rates come down, if we're right that the Fed cuts interest rates, that's going to be a big relief to these owners of commercial properties."

Do you want to talk about strategic planning? We received a number of questions about that.

Dr. Bill Conerly's response:

"And if you don't mind, I'll give my response to the question of advice for strategic planning.

"One of my consulting clients came to me and wanted help with that, and they were surprised by my first question. I said, 'well, what do you want to do with your business?' This is a company with sales just under $20 million. Husband and wife own it jointly. And I'm like, 'what do you want to do?' And they were surprised. And I said, 'well, do you want to grow the business or do you want to protect it from risk and just keep it the way it is? Or do you want to set it up to sell? And that kind of relates to what do you want to do as people? Do you want to retire early? Do you want to build something you can be proud of? Do you want to just have a comfortable lifestyle that continues on?' That's the first step in strategic planning. What is your goal? And then the second one, I worked some years back on a book called *The Flexible Stance, thriving in a Boom Bust Economy*. I had studied how poor a job we economists do at predicting recession. So I said, 'what do you do if you're doing business planning in an uncertain environment?' And I decided to call up the smart people I knew and I went through my phone list of smart business people and I talked to Pat Stone. And Pat, you want to sort of refresh what you said to me when I was looking for advice and then roll into other advice you have on strategic planning?"

Patrick Stone's response:

"Well, I'll tell you, and I don't remember precisely what I said, Bill, I remember the conversation. But I will tell everybody that I think the first thing you need to do is do an honest assessment of where you are. Almost every manager I know is always thinking up and ahead. And it really would benefit you if you take a few minutes and really analyze your operation, break it down by department, break it down by function, break it down by interface with clients and give everything a rating and be as honest as you can and maybe even encourage some of your subordinates to participate. You need to know exactly where you are because you can have great plans, you could have wonderful goals, but if you are not really cognizant of where you're strong and where you're weak or where you need to improve, you miss opportunities and you may also create a fatal situation. You want to do an assessment, you want to make sure that you put time, effort, and money to make sure that all your components of your operation are operating in a competitive environment and in a competitive manner so that you not only exist, but you win, if you will. One thing, again, doing one, three and five year plans, I wouldn't put too much time on the five year side, but fixing things and getting yourself positioned, and I think you've gotten a good idea today that we expect activity to pick up. We expect refis to pick up. We're pretty optimistic about 2025. I personally think that you're going to see sales over 5 million (units) in 2025, and if I'm right, that's a meaningful increase and that's about a 25% increase in volume. So get yourself positioned to do that and to participate in that market in a very effective and competitive manner. So assessment, plan, and one last thing real quickly. Make sure that you bring your employees into the conversation. I learn something every day that I talk to an employee no matter what level they are. And one of the things that always worked for me was having employees learn where the file came from and where it goes to after they touch it, so they have an understanding of the process and how important what they do is. And you will get ideas from your employees if you include them in this conversation."

Dr. Bill Conerly's response:

"Yeah. Well, I'll remind you what you told me on strategic planning in an uncertain environment. You said that you had looked at how bad things go when things go badly. What is the magnitude of the revenue loss that the company faces when things go down? And you said that at the beginning of the year, you sketch out what you would do if you had that kind of revenue loss. Where can you cut expenses? Where can you not cut expenses? And you may not be able to match the revenue reduction with expense cuts, but at least you know how red it is going to be. And that advice ended up in the book, and I suggest that to people in all industries; how bad could things reasonably be and what's your contingency plan for that happening?"

Patrick Stone's response:

I remember that Bill and apologize for that not coming to the top of mind, but real quickly, one thing that I would add to that for everybody's sake is, if you wait till it happens, you are going to be dealing with an emotional situation. If you plan for it ahead of the time, you can enact changes quickly and unemotionally and be much more effective and much more successful.

Closing Thoughts

Patrick Stone:

"Alright, so I think we're out of time. Bill, any last comments?"

Dr. Bill Conerly:

"Nope, that's it. I look forward to doing this again next quarter."

Patrick Stone:

"Thank you everybody. Thank you Bill. Take care everybody."

# # #

About Patrick Stone

Patrick Stone is Chairman and Founder of Williston Financial Group, the Portland, Oregon-based parent company of several national title insurance and settlement services providers, including WFG Lender Services and WFG National Title Insurance Company. Stone's lengthy career in real estate and related services includes C-level positions with three public companies and serving as a director on two Fortune 500 boards. His senior executive management positions include nine years as president and COO of the nation's largest title insurance company, chairman and co-CEO of a software company, and CEO of a real estate data and information company. Stone also served as vice-chairman of Metrocities Mortgage, a 2005 top-20 mortgage lender, and as chairman of The Stone Group, an Austin, Texas-based tenant-represented brokerage company. In 2013 Pat was named one of the "100 Most Influential People in Real Estate" by Inman News and as one of the "Top 101 Real Estate Industry Doers" in 2015 and again in 2021. Other accolades include receiving HousingWire's coveted "Vanguard Award" in 2019 and again in 2021, Progress in Lending's "Lending Luminary Award" in 2019, 2020, 2023 and 2024, Inman's "Best of Finance" award in 2023 and 2024, and October Research's annual "Leadership Award" in 2020.

About Dr. Bill Conerly

Bill Conerly has a Ph.D. in economics from Duke University and more than 30 years of experience helping companies adapt to changing economic conditions. He was formerly Senior Vice President at a major bank and held positions in economics and corporate planning at two Fortune 500 corporations. He is also an online contributor to Forbes, chairman of the board of Cascade Policy Institute, and the author of The Flexible Stance: Thriving in a Boom/Bust Economy (2016) and Businomics (2007), a book about economics for business leaders. To subscribe to Conerly's monthly newsletter, visit: https://conerlyconsulting.com/newsletter/