

ECONOMICS AND REAL ESTATE

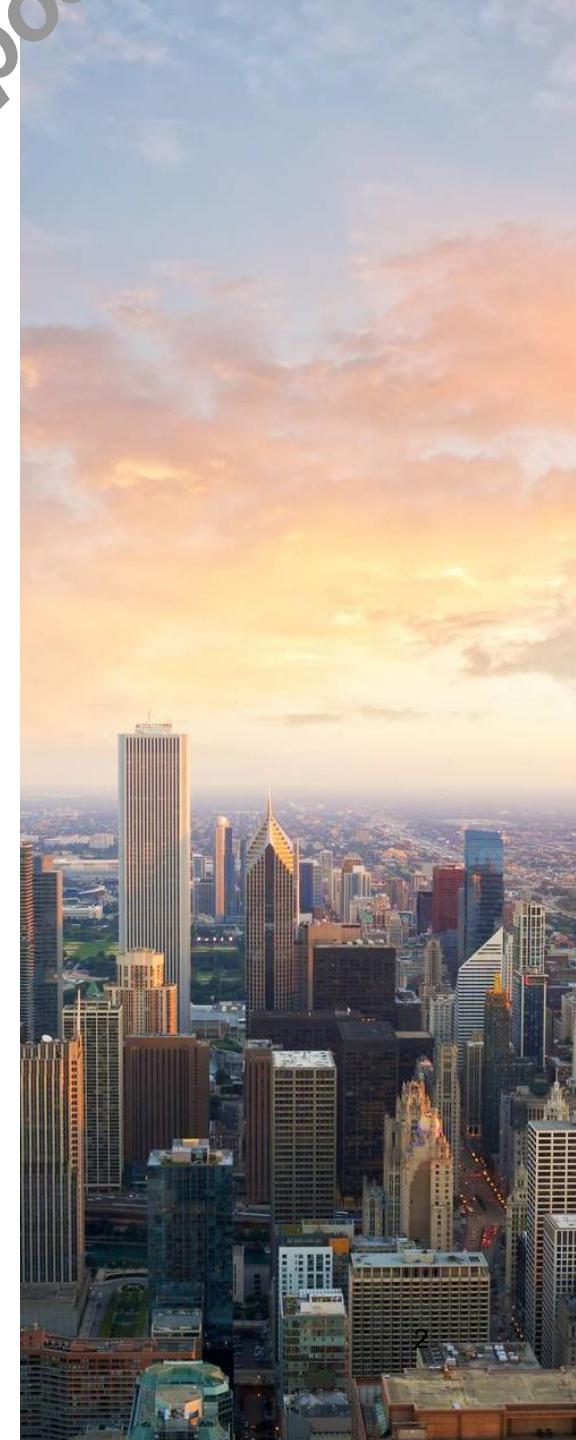
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AGENDA

Discussion of political and economic history for the last 100 years

**A real estate CE
program by
Melanie McLane
McLane Solutions
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melanie@themelaniegroup.com**



Economics



Sooner or later we all sit down
to a banquet of consequences.

Robert Louis Stevenson

quotefancy

Why study Economics?



Business cycles influence value



Economics provides the 'big picture' for everyone in real estate



Knowing how cycles behave allows you to prepare for changes in your real estate market

Major Events

Great Depression

1973-1975 Recession

Double dip recessions of 1980, 1981-82

Great recession 2006-2012

Currently: inflation down; prices still up

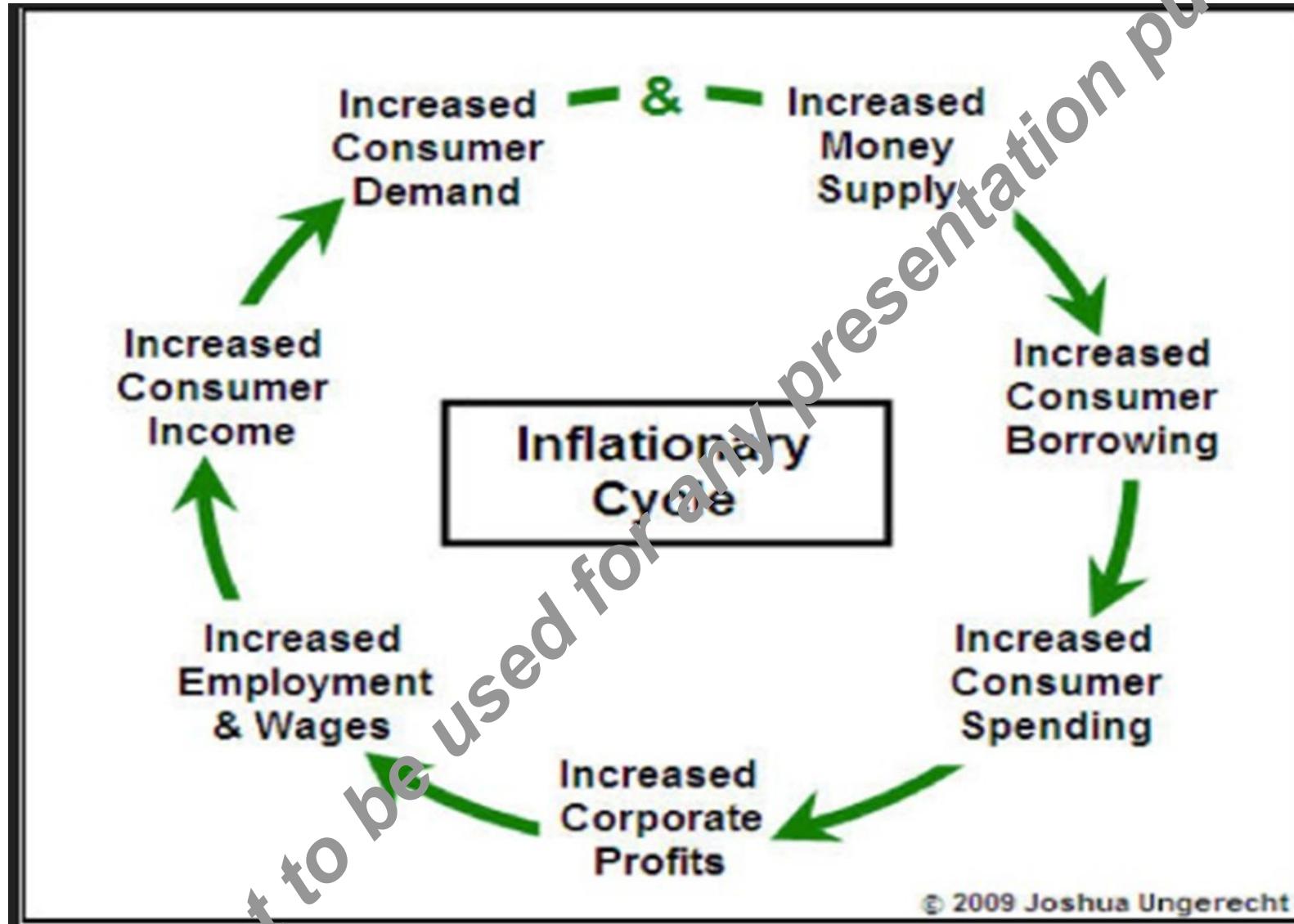
Real Estate in the US. . .

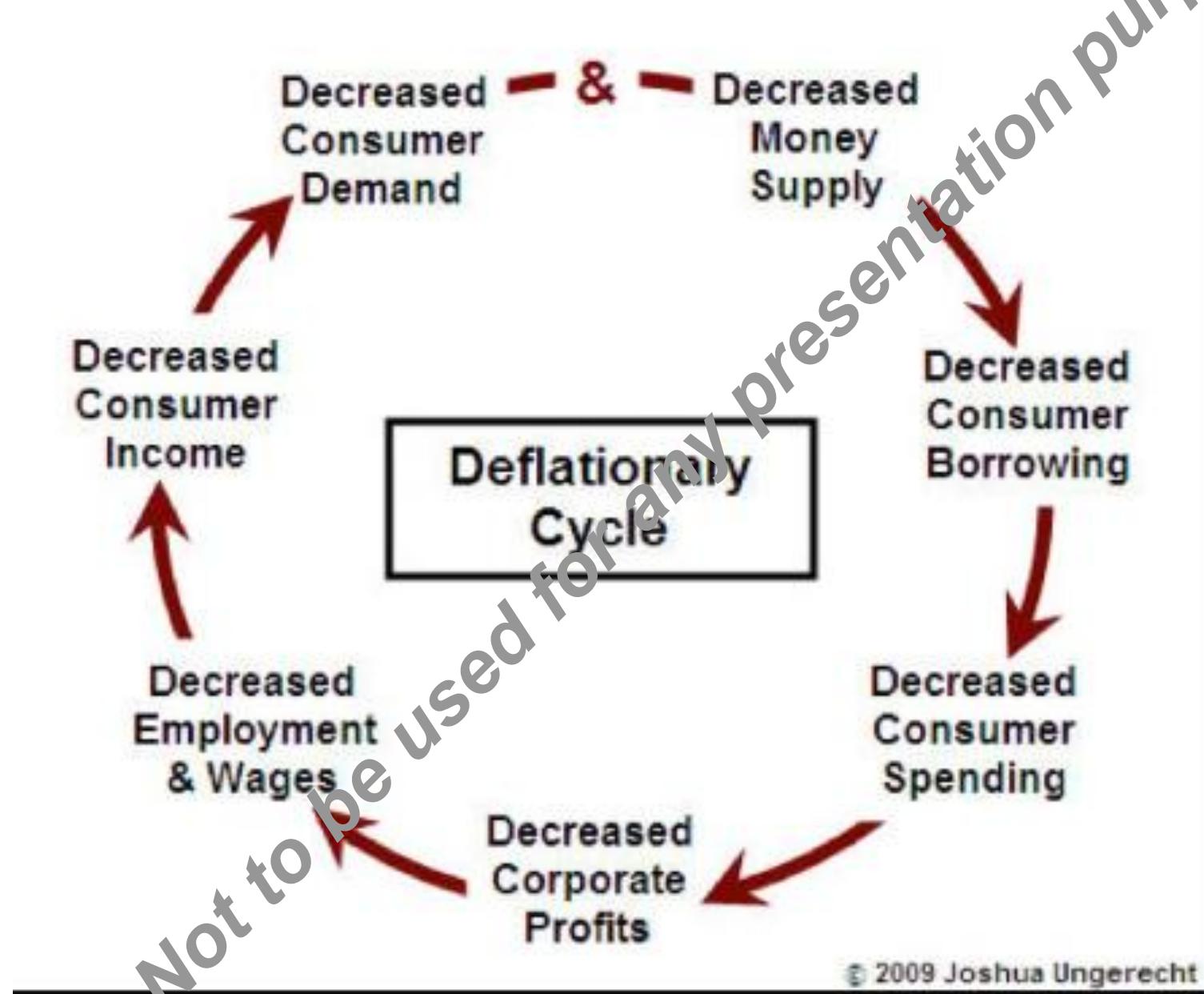


- From Homestead Acts
- To FNMA
- Real estate is a big part of our economy
- Public policy has encouraged home ownership

Private Land Ownership in US

- 60.1%





Deflationary Cycles

Great Depression

Can be when a “Bubble”
bursts

Can be extremely
localized

Affected by overbuilding,
oversupply



Speaking of Taxes...circa 1913

**Federal Income Tax
made permanent
(had been in place
during previous
wars)**

**7 brackets—1% to
7%**

1913

1913

- Federal Reserve was created
- Following the “panic of 1907”
- By Congress
- “To make the American Banking system more stable”

What Does the Fed Do?

Regulates banks

Lender of 'last resort' to member institutions

Open market operations

Discount rate
Reserve requirements

Reserve Requirements

How much banks
must keep in
reserve

Which means they
can't loan it out



Federal Reserve Sets Interest Rates

**On reserve
balances (IORB)**

**Overnight reverse
repurchase
agreement (ON
RRP) rate**

Discount rate

**These 3 influence
the Federal Funds
Rate, the Rate at
which banks loan
each other money
overnight**

Bond Rates are YIELD for Investors

**Mortgages track
the 10 year bond
rate**

**There is usually a
'spread' between
the two rates**

**Spread is historically
around 1.5 to 2
percentage points to
compensate investors for
the higher risk of
mortgages. So if the bond
yield is 4%, mortgage
rates might be around
5.5% to 6%.**

Speaking of the Fed...

- "Regarding the Great Depression ... we did it. We're very sorry. ... We won't do it again."
- –Ben Bernanke, November 8, 2002, in a speech given at "A Conference to Honor Milton Friedman ... On the Occasion of His 90th Birthday."

Taxing Times



1916–1921

Roaring 20's:
Top rate around 78%



1929–1931

Great Depression
DROPPED to about 20%



1944

W. W II
OVER 80%



Currently

Currently:
Under 40%

Will Rogers:



**“The difference
between death and
taxes is death
doesn't get worse
every time Congress
meets.”**

Roaring Taxes in the Roaring 20's!



By 1921, Federal Income Tax had 56 brackets, from a low of 4% to a high of 74%

74%



By 1924, the brackets “only” numbered 43, from 2% to 46%

1924

1920-1930 House Prices



Average price in 1920
= \$6296

Average price in 1930
= \$7145

**Up almost 14% in this
decade**

1920's

**Home Ownership
was limited to a
small percentage
of the population**

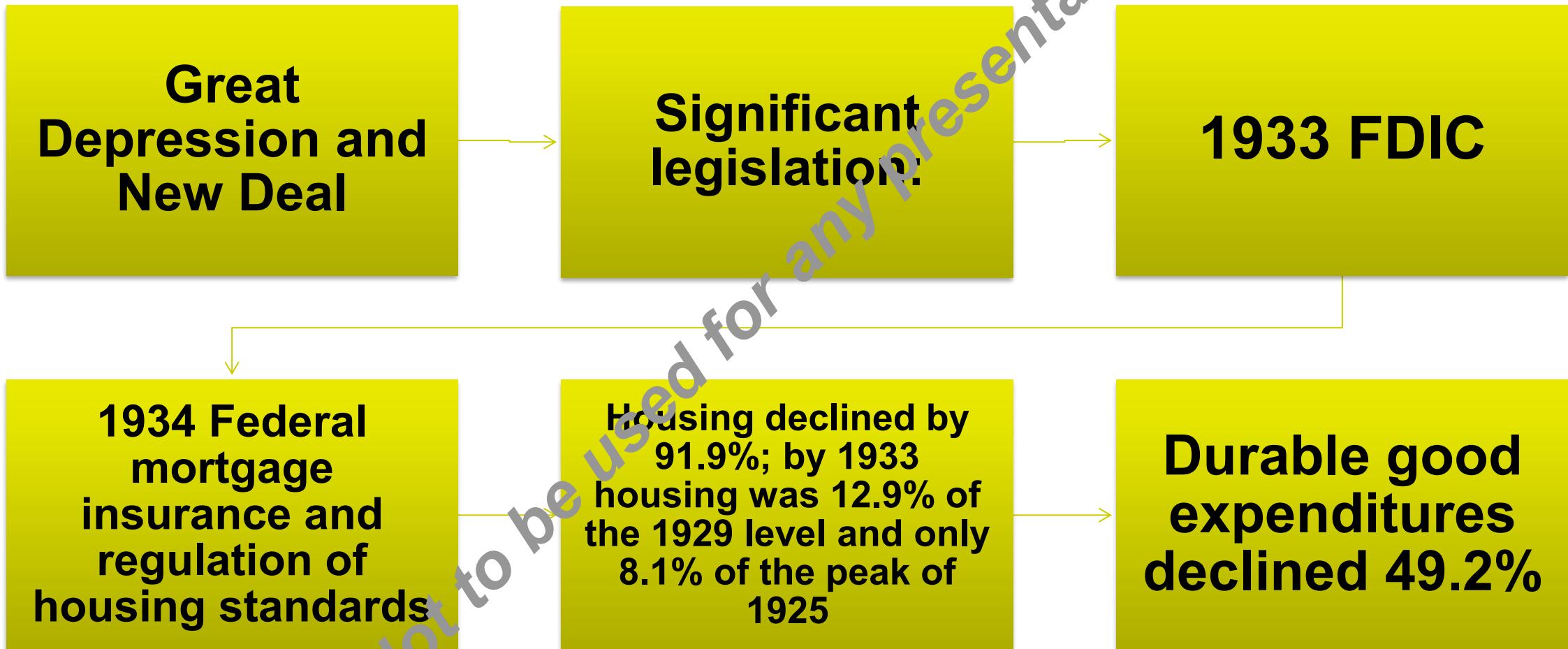
**Down payment
requirements
high—50% plus**

**Term very short—
5 years**

**Many people
bought with
cash**

**Housing increased
during mid1920's---
until the crash; levels
in 1925 were 58.7%
higher than in 1929**

1930's



1932

**Federal Home
Loan Banks were
created**

**Federal National
Mortgage
Association
(Fannie Mae) begin
buying mortgages**

**Until 1968, Fannie
Mae was the sole
institution buying
mortgages**

Investment declined 68.6%

GNP declined 27.7%

Deflationary cycle

Mortgage terms increased to 20 years

FHA created

Stock market declined 89%

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1930's



- Roosevelt suspended Gold Standard
- 1937: “Roosevelt Recession”
- 1940: wartime production began

\$4197.30 Ounce price 12/6/25



In 1933, FDR issued Executive Order 6102, making it illegal for U.S. citizens to own gold coins or bullion.

You had to turn it all in to the government or face 10 years in prison. The government paid you \$20.67 an ounce. Once they had all the gold, they immediately raised the price to \$35 an ounce, instantly devaluing everyone's paper money and making the government rich. It was the greatest wealth heist in American history.

By Law:

**Gold at Fort Knox is
valued at \$42.22 per
ounce**

By law

**“Book value” around
\$11 billion**



Who was Henry Morgenthau?



- FDR Secretary of Treasury
He said: “Never in the history of the world has there been a situation so bad that the government can’t make it worse.”

Taxes in the 1930's

- Reached a peak of 59 brackets (1933)
- From 1935-1939, rates ranged from 4% to 79%

1930-1940 House Prices



\$7145 in 1930

\$2938 in 1940

**Lost almost 60% of
value**

1940's

WWII

Did WWII end the Great Depression?

Would the Great Depression have ended sooner without government interference?

Housing growth between 1945 and 2nd Quarter 1948 strongest of 20th century

Taxes in the 1940's

1940 rates went as high as 79%, but in 1942-1943 hit an all time high of 19% to 83%

War is expensive

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1940's

- Surge of housing construction 1947-1951
- Consumer Price Index increased by 2.9% between June 1946 and June 1948
- Truman took office April 12, 1945 following FDR's death
- Tried to reinstitute "New Deal" as "Fair Deal"
- Blocked by Republicans

Truman

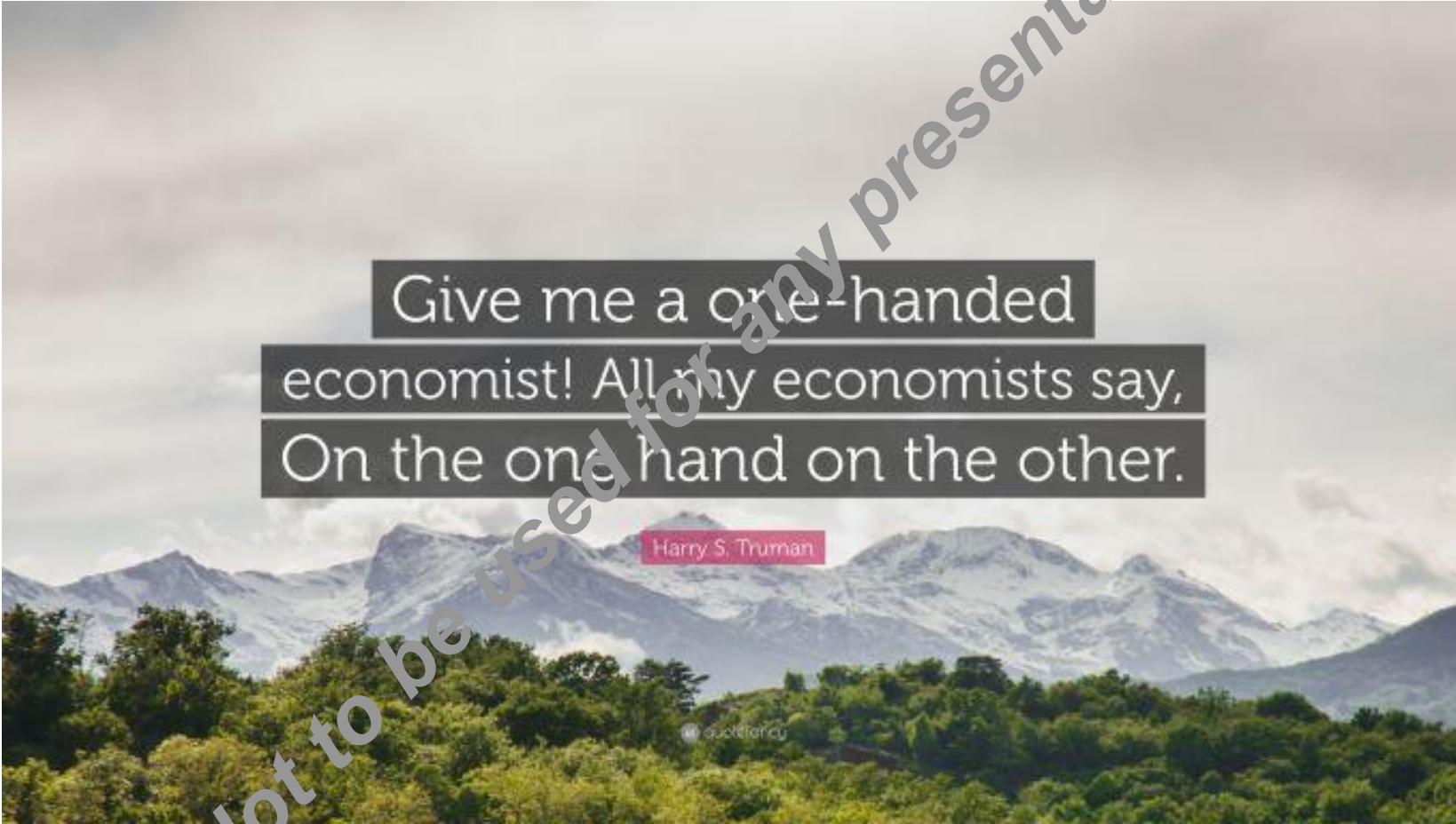
- Price controls, inflation, unemployment
- Beginning of “benefits” (no raises)
- Taft-Hartley “Right to Work”
- Truman vetoed
- Congress passed over his veto
- Price controls ended post WWII

1940's--Truman



- Eventually lowered taxes: growth started
- Extended rent control for 15 months in June of 1950
- Home ownership rates at 43% by near end of decade

Harry Truman's Quote:



Give me a one-handed
economist! All my economists say,
On the one hand on the other.

Harry S. Truman

quoteforu

1940 to 1950 House Prices



\$2938 in 1940
\$7354 in 1950
Up 150%

1950's

1957 MGIC Corporation formed

**Offered Private Mortgage Insurance which
competed with FHA MIP**

Home ownership rate increased to 55% by 1950

1950's

- 1953-1954 recession—fourth largest of post war era
- Substantial decline in housing
- Korean War anticipated to be another long war



1950's

Inflation came back

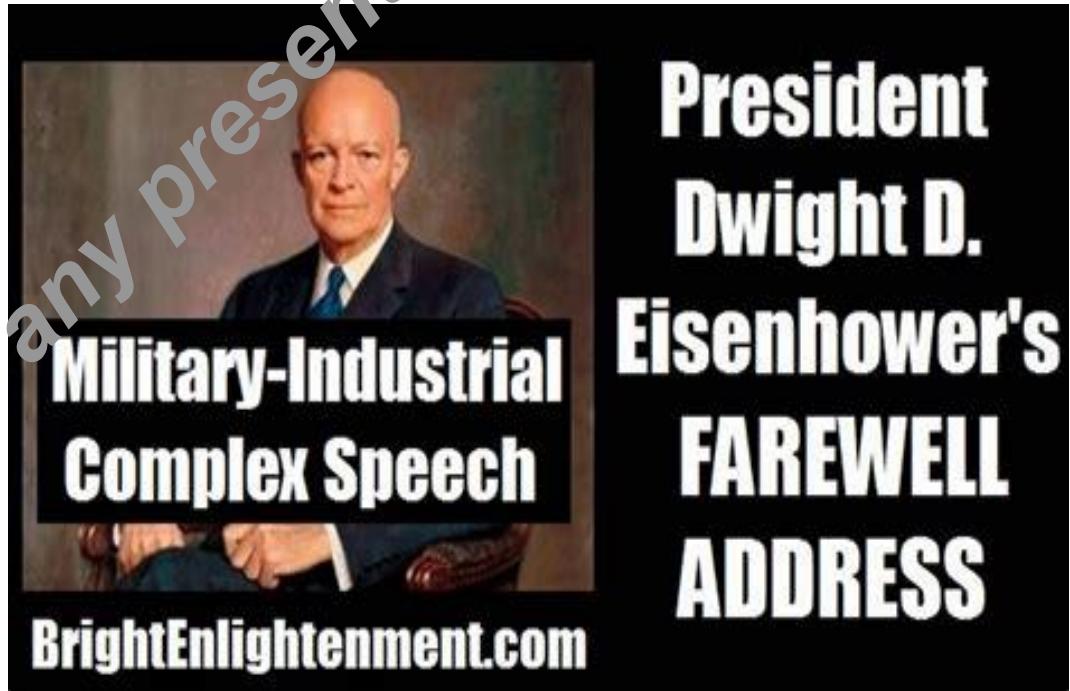
Fed increased reserve ratio

Wage & price controls were started in January of 1951

Housing increased rapidly in the middle of 1954, again leading economy out of recession.

1950's

- Truman did not run again
- Eisenhower elected twice
- “Peace Dividend”



Taxes in the 1950's

- Highest rates historically were 1952-1953, rates went from 22.2% to 92%

Arthur Oken American Economist



- **“High tax rates are followed by attempts of ingenious men to beat them as surely as snow is followed by little boys on sleds.”**

1950's

 **Eisenhower: Interstate highway system**

 **Reduced Federal debt**

 **Unemployment dropped to 4%**

 **Virtually no inflation**

 **Dow hit 400 in '54; closed at 679 on 12/31/59**

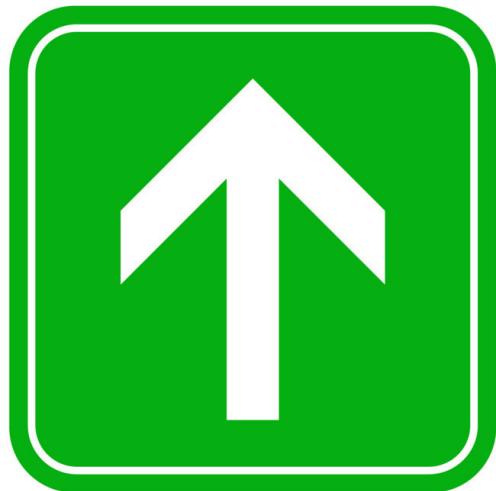
 **“Military Industrial complex”**

1960's

- JFK elected
- Youngest President
- First Catholic
- Unemployment at %
- State of the Union in 1963
- “Cut taxes to increase jobs”



1960's



Unemployment
dropped to around
4%

Minimum wage
\$1.25 in 1961

Stock market
724.71 on 1/2/62;
947.74 on 1/1/69

1960's

JFK Assassination

Space Age

Johnson: “Great Society”

Social Security expanded to age 62

Home ownership levels hit 62%

Vietnam and “Guns v. Butter” (he tried to do both)

1960's



“New Frontier” Housing Act 1961



\$5 billion for urban renewal & new construction



Home ownership rates hit 62%

1960's



- Median price of a home in 1960 = \$16,500
- By 1970 = \$26,600
- Up 61%

1960's Taxes



By 1964, top rate had dropped from 91% to 77%



1965 through 1981 rates remained from 14% to 70%, with a total of 15 tax brackets

1968

Fannie Mae was split into a private corporation and a publicly financed institution

To provide competition for Fannie (now private) and to increase funds for homeownership, Congress established Freddie Mac (Federal Home Loan Mortgage Corporation) through Emergency Home Finance Act of 1970

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Price Controls

Nixon elected 1968

**August 1971 90 day
freeze on prices
and wages**

**Which exacerbated
the oil crisis**



1970's=Inflationary Cycle

- Remember the '70's?
- Gas lines
- Inflation
- GREAT TIME to own real estate!



1970's

-  1971—lending limits changed, allowed S & Ls to make loans of 95% (formerly 90% LTV)
-  Limits on dollar amounts of mortgages raised
-  Decade ended with high interest rates—18% to 20%
-  ARMs introduced
-  Housing fell 20.2% during 1969-1970

1970's

- 🥇 Nixon took us off the Gold Standard
- ¥ Nixon opened China; more trading
- 📉 Recession 1973-1975
- 🏡 Housing declined for 2 quarters before the Arab oil embargo
- 🏡 50.6% decline in housing
- \$ Inflation surges from under 4% to 10%

1970's



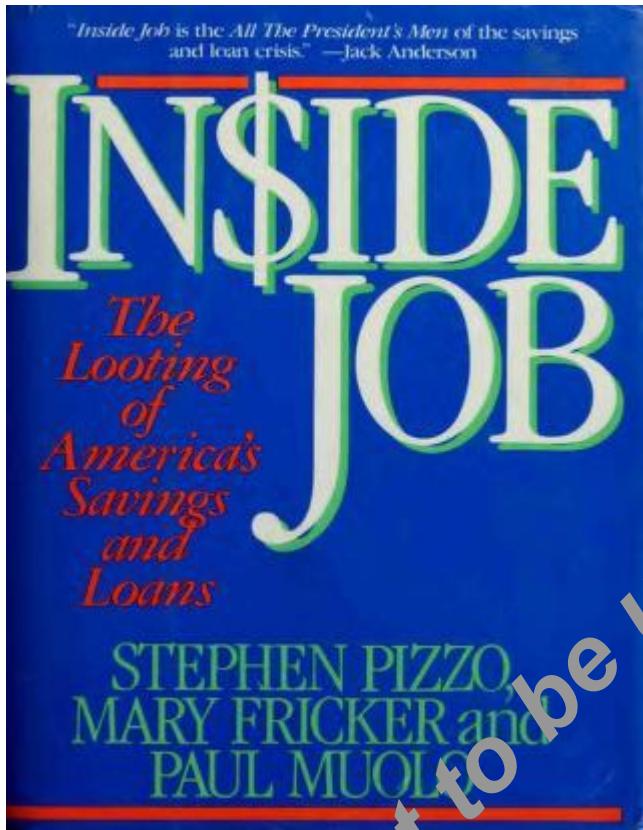
Housing again recovered first, after federal funds rate was reduced to the 1972 level

Nixon resigned; Ford took over

Stock market declined from Watergate to Nixon's resignation

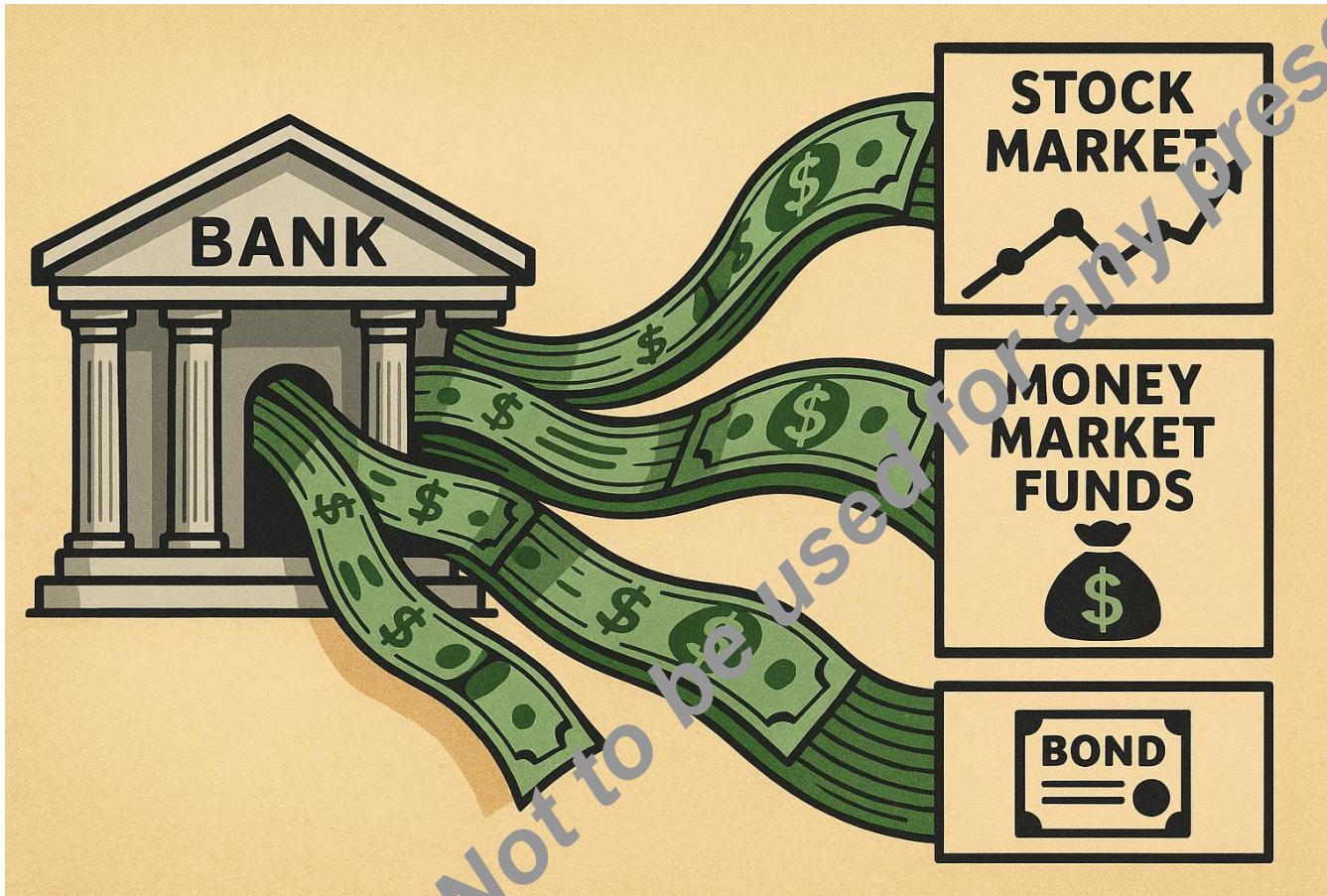
Carter elected 1976

1970's



- Began the loosening of requirements for S & L's
- Allowed them to expand into commercial loans, consumer loans etc.
- Government pushed this "reform"

Disintermediation



Flow of funds
from one entity to
another

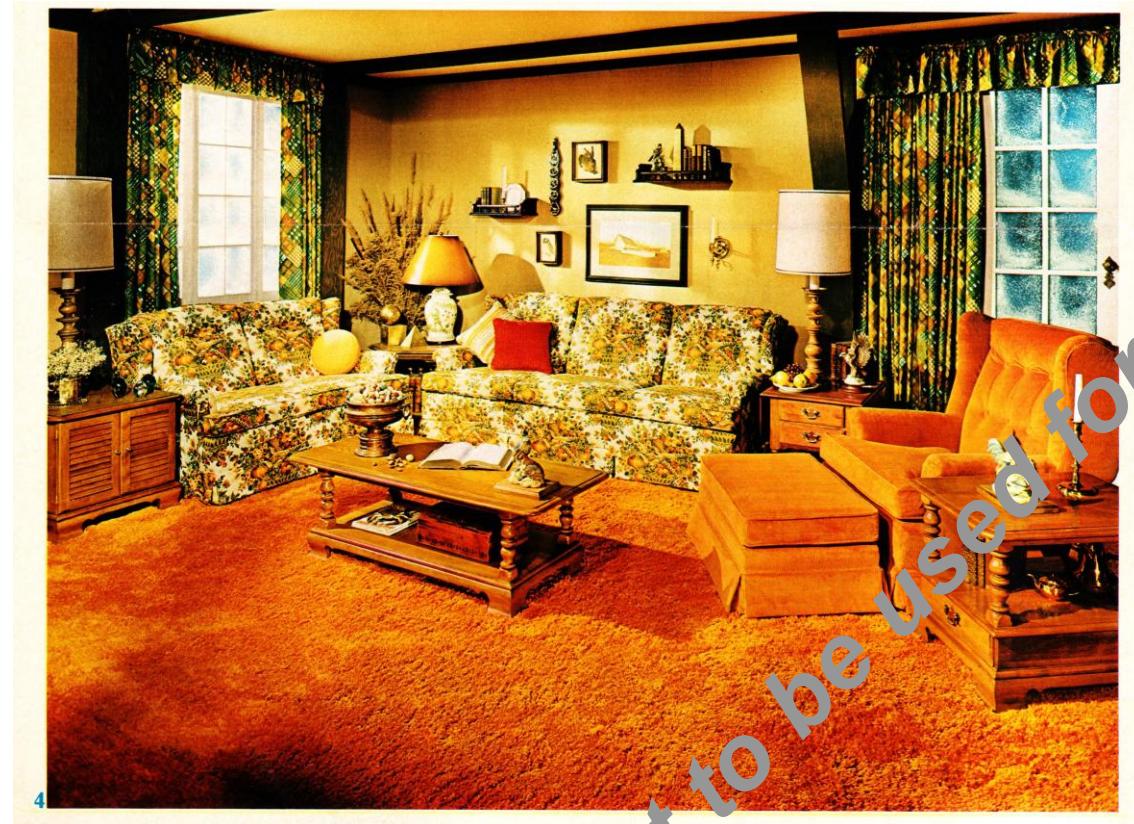
Money market
funds

Siphoning off
bank and S & L
deposits

1970's

- ⌚ Dow crossed 1000 for first time
- 🏧 Disintermediation begins
- ¥ Nixon: price, rent, wage controls
- \$ Ford: inflation at 7%, unemployment at 9% =
- 🦌 Stagflation
- 👤 Carter elected 1976

The 70's were great because. . .



- Real estate was appreciating rapidly
- Borrowers were paying back their loans with dollars which were worth less

1970 to 1980 House Prices



**Average in 1970 =
\$23,400**

**Average in 1980 =
\$64,900**

**Appreciation rate =
177%**

Politics

- Nixon
- Price rent & wage controls
- Watergate
- Resignation
- Ford assumes office



Ford

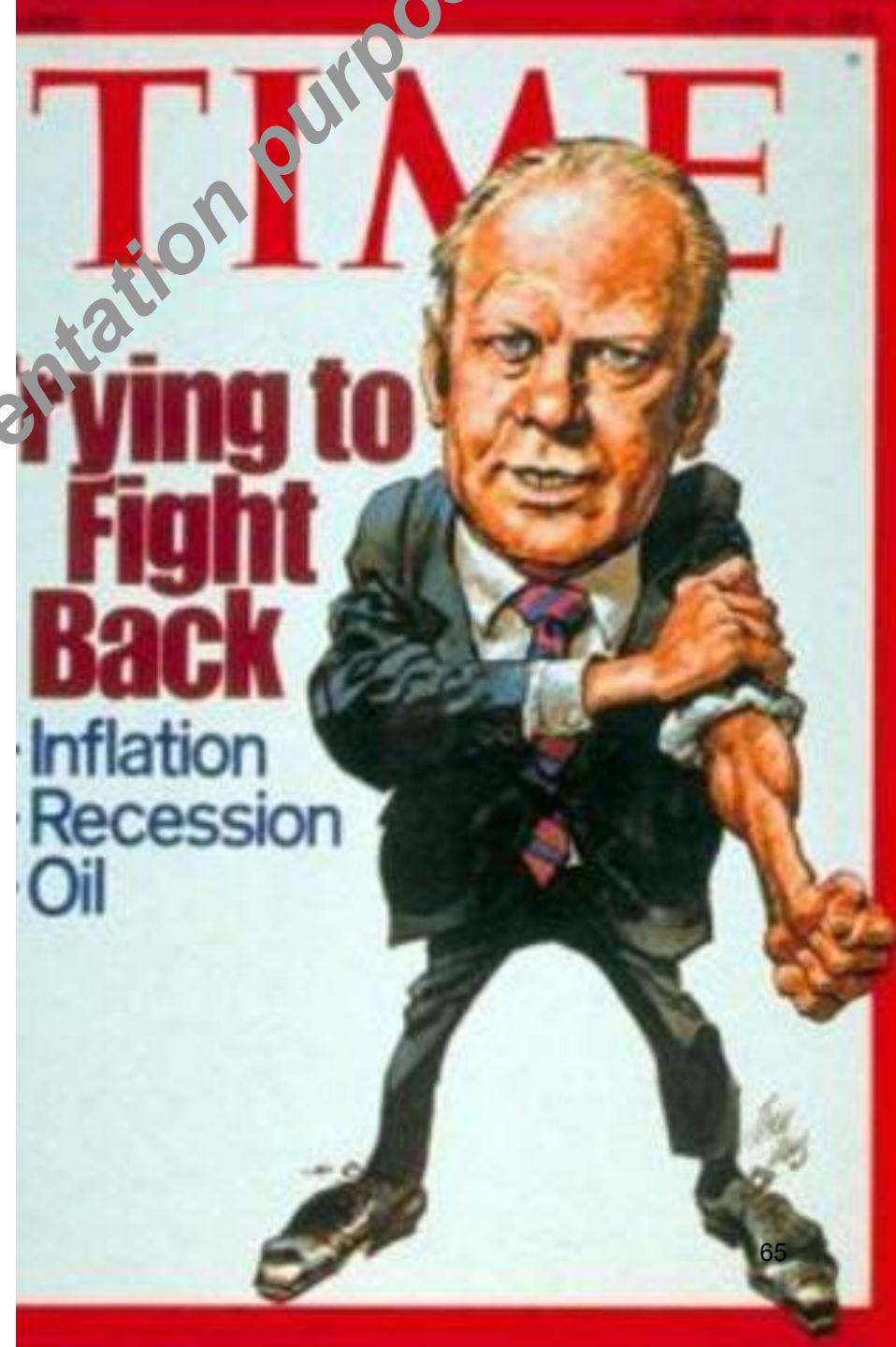
High inflation

High unemployment

“WIN” buttons

Pardoned Nixon

Not re-elected



1970's



Carter started Community Reinvestment Act



Covered all lenders insured by FDIC



Gave feds ability to “muscle” lenders

1970's

Carter did not cut taxes; vetoed his own spending plans

Volcker rates up 9% in 8 months

Reagan defeats Carter with: “Are you better off today than you were four years ago?”

1980's

- S&L bailouts
- FIREEA legislation passed (leading to certification of all real estate appraisers)
- Interest rates decline
- Credit requirements relaxed
- **Community Reinvestment pushed**

1980's



- 100% loans introduced
- 125% loans introduced
- Waves of refinancing
- Wall Street Collapse;
22% loss 10/19/1987
- Disintermediation
continues

1980's



1981-1982 recession was the second most severe of the post-war era



3rd Quarter 1978 to third quarter 1980 housing fell 40.6%



1st Quarter 1981 to 2nd quarter 1982 housing fell another 36%

Fed Chairs In This Era



William Miller's last 3 months registered a 13.521% annualized inflation rate



He was replaced and Volcker beat inflation



Paul Volcker's last 3 months registered a puny 2.220 % rate.

Tax Changes—1980's



**Tax code changed—
taxpayers could no longer
deduct**



**What could they
deduct?**

**Credit card interest
Car loan interest**

Mortgage interest!

Taxes in the 1980's

- After cutting top rate in 1981 from 91% to 70%, Reagan kept cutting
- 1982-1986 rates were from 11% to 50%
- 1987: only 5 brackets, for the first time—11%, 15%, 28%, 35%, 38.5%
- 1988 True simplification: 2 rates: 15% and 28%

1980 to 1990 Average House Prices



\$64,900 in 1980

\$120,000 in 1990

84% + appreciation

1990's



- Average price of a house 1990: \$120,000
- Average price in 2000: \$171,100

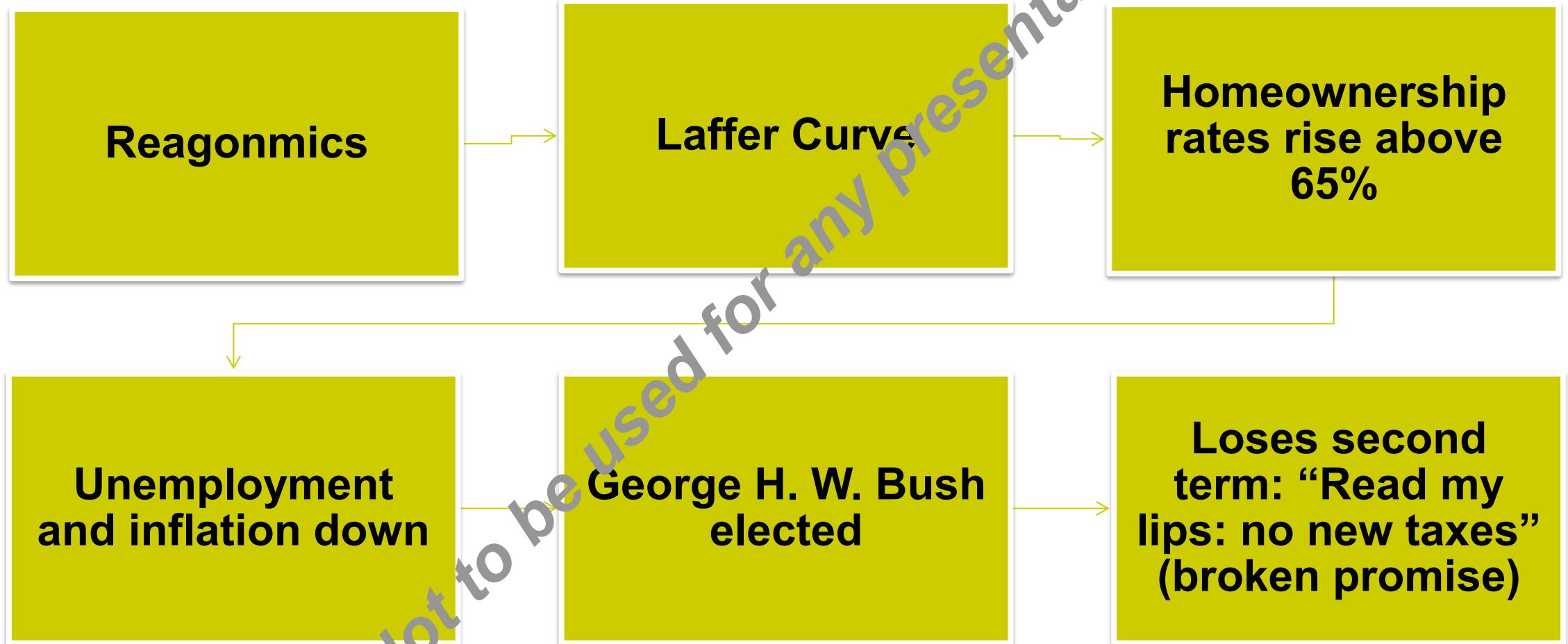
1990's

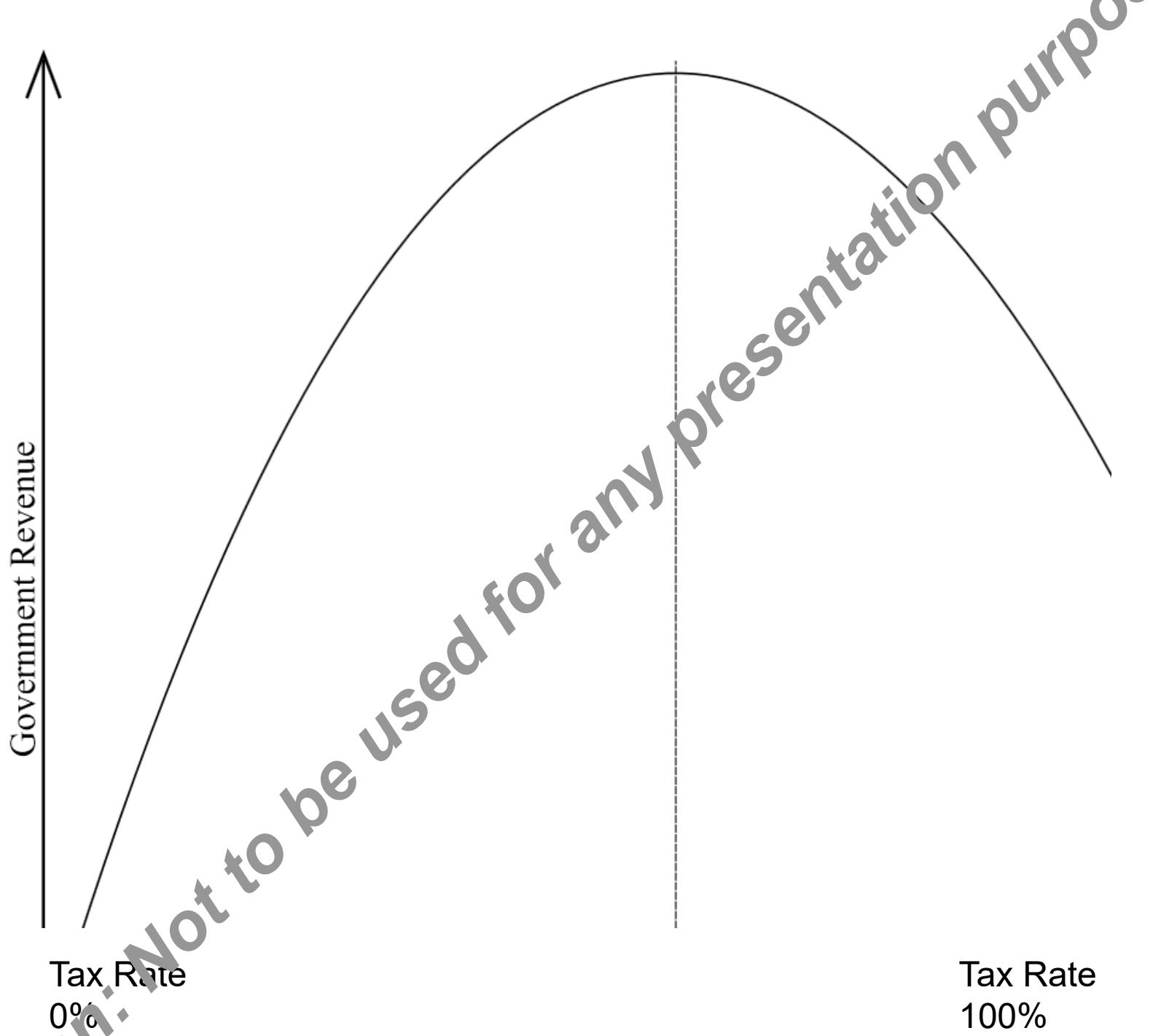
- More Community Reinvestment Act
- Hybrid loan products introduced
- Economy grew rapidly
- Stocks up –Dow hit 11,000
- Low unemployment

Political and Economic History

- Reagan's promises: lower taxes, decrease federal government & spending, increase domestic energy services; increase military; balance budget
- Did all BUT balance budget

1980's





1990's

"All the News
That's Fit to Print"

The New York Times

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DECLARING DEATH OF SOVIET UNION, RUSSIA AND 2 REPUBLICS FORM NEW COMMONWEALTH

Frantic Moves Came to Light In Days Before Maxwell Died

As the Empire Was Crumbling
A special report.



By STEVEN PROKESCH
Special to The New York Times
LONDON, Dec. 8.—At the time of his mysterious death on Nov. 5, Robert Maxwell almost certainly knew he was about to be caught.

He had drained hundreds of millions of dollars from his own English public company and from employee pension funds in a frantic attempt to keep his heavily indebted publishing empire afloat.

The leaders of the Maxwell empire, Coopers & Lybrand Deloitte, were to conduct their next regular audit of the pension funds in a couple of months. And Coopers' auditors have since discovered the transactions, said a person very familiar with the details of a specific financial examination of the empire conducted for the banks after Mr. Maxwell's death. He was asked to discuss the report only if his identity was not disclosed.

"Basically Grabbing Cash."

The Coopers team also found evidence that some of the diverted money went to The Daily Mirror in New York to cover its losses. That raised more doubts about the future of the newspaper, which Mr. Maxwell acquired in March.

According to Mr. Maxwell's plan to prop up the private companies that controlled his empire "was doomed to failure," the person familiar with the Coopers' report said.

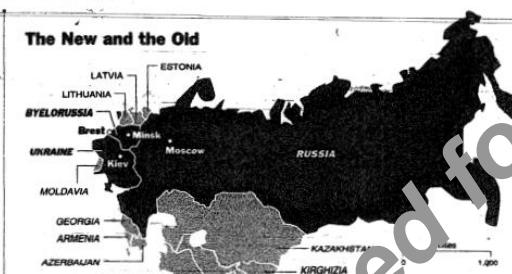
"It was a sophisticated fraud like B.C.C.I.," he said, referring to the scandal surrounding the Bank of Credit and Commerce International. "The guy was basically grabbing cash and putting it in his pockets."

In the Coopers team was led by Richard Stone, the partner in charge of the accounting firm's corporate finance division.

The discovery led the major holding companies of the Maxwell empire to

By ALAN RIDING
Special to The New York Times
MAASTRICHT, the Netherlands, Dec. 8 — In an atmosphere of anxiety and

The New and the Old



Latvia
Estonia
Byelorussia
Russia
Ukraine
Moldova
Georgia
Azerbaijan
Turkmenia
Uzbekistan
Kazakhstan
Kirghizia
Tadzhikistan
Minsk
Moscow
Brest
Kiev

70.6 million
8 million
148 million
51.8 million
10.3 million

Population
January 1990
Others
Baltics
Russia
Ukraine
Byelorussia

16%
28.2%
47.0%
16.4%
5.4%

Consumer Goods
Share of production, 1988
Other
Baltics
Russia
Ukraine
Byelorussia

21.4%
4.4%
46.7%
22.1%
5.4%

Agriculture
Share of total output, 1988
Other
Baltics
Russia
Ukraine
Byelorussia

1.5%
16%
47.0%
16.4%
5.4%

TAKE OVER A-ARMS

Newborn Bureaucracy Is Inheriting Functions of Old Authority

By SERGE SCHMIDMANN
Special to The New York Times
MOSCOW, Dec. 8 — The leaders of Russia, Ukraine and Byelorussia declared today that the Soviet Union had ceased to exist and proclaimed a new "Commonwealth of Independent States" open to all members of the former union.

In a series of statements issued after a two-day meeting at a Byelorussian government retreat, the leaders of the three Slavic republics declared void all efforts to create a new union in the ruins of the old one. But they called for the formation of a "common defense" and "common" for defense, foreign affairs and the economy that would have their seat in Moscow and would assume the international obligations of the Soviet Union, as well as control over its nuclear arsenal.

They declared that the "norms" and activities of the former union ceased as of the moment of signing, and that the new union would assume the international obligations of the Soviet Union, as well as control over its nuclear arsenal.

Gorbachev's Move

The U.S.S.R., as a subject of international law and geopolitical reality, is ceasing its existence," the leaders declared.

The action essentially stripped President Mikhail S. Gorbachev of his office and authority, and the immediate question was whether the new and tenuous Soviet leader would remain in power and if he did, whether the military or other levers of power would support him.

The three cofounders of the new Commonwealth — President Boris N.

"We, the republics of Byelorussia, the Russian Federation and Ukraine . . . state that the U.S.S.R. is subject of international law and geopolitical reality, is ceasing its existence."

— Brest declaration, Dec. 8, 1991

The Union Is Buried: What's Being Born?

By LESTINE BOHLEN
Special to The New York Times
Moscow, Dec. 8 — Ever since the August coup d'état, the Soviet Union

he keeps warning about what has already happened. This is a fact they can't ignore with their daily lives, as they go to factories that have run out of materials

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1990-91 recession
housing fell 34.8%

Collapse of Soviet Union
= more markets for
capitalization & trade

Trade opportunities

Technological advances

1998 first budget surplus
in 30 years

1990's



Clinton years: 1992 Democrats had control of all 3 branches

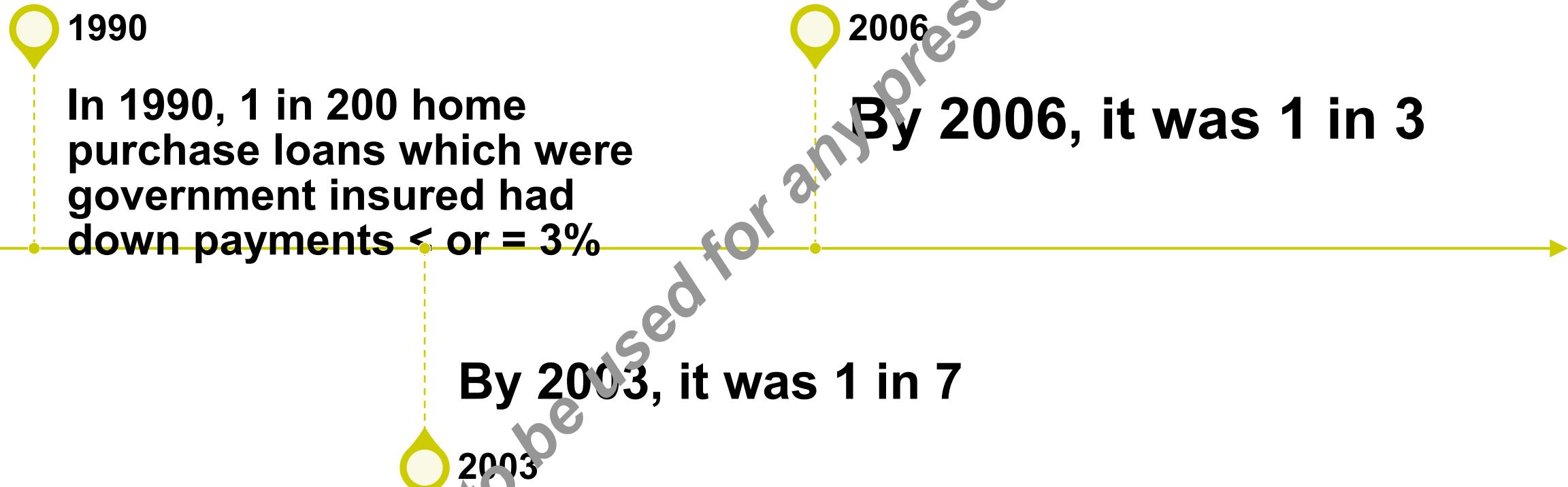
1994: Republicans “Contract With America”

1998 First Balanced Budget in 30 years

Good decade for stocks and real estate

DJIA hit 11,000

Compare:



1990's



**Congress pushed
“reform” for
Fannie & Freddie
Creating the sub
prime monster**

2000's



Early 2000's, market went up and up

Owners became speculators

Some markets had triple digit inflation

Huge demand for mortgage-backed securities; tranches and other exotic things introduced

2nd Quarter 2006, first decline

2000's



George W. Bush

9/11

Two wars in the mid east

Capital gains rate cut to lowest historical level

Home ownership hit almost 70%

2008 Barack Obama elected

Housing crisis kicks into full gear in 2006

Political and Economic History



**Clinton & Republicans cut taxes & spending;
balanced budget in 1997**



First balanced budget in 3 decades



**George W. Bush—tax cuts went into effect in 2003—
followed by 46 consecutive months of growth**

2000's



Foreclosures up
Fraud revealed
Wall Street collapse
Bail out of AIG
Collapse of many lenders
Still reeling from foreclosures

Timeline

April 2007 New Century Financial declares Chapter 11 Bankruptcy (sub-prime lender)

October 2007 Dow hits 14,164

Jan 2008 Fed drops rate AGAIN to 3% (had been 5.25% in Sept 2007)



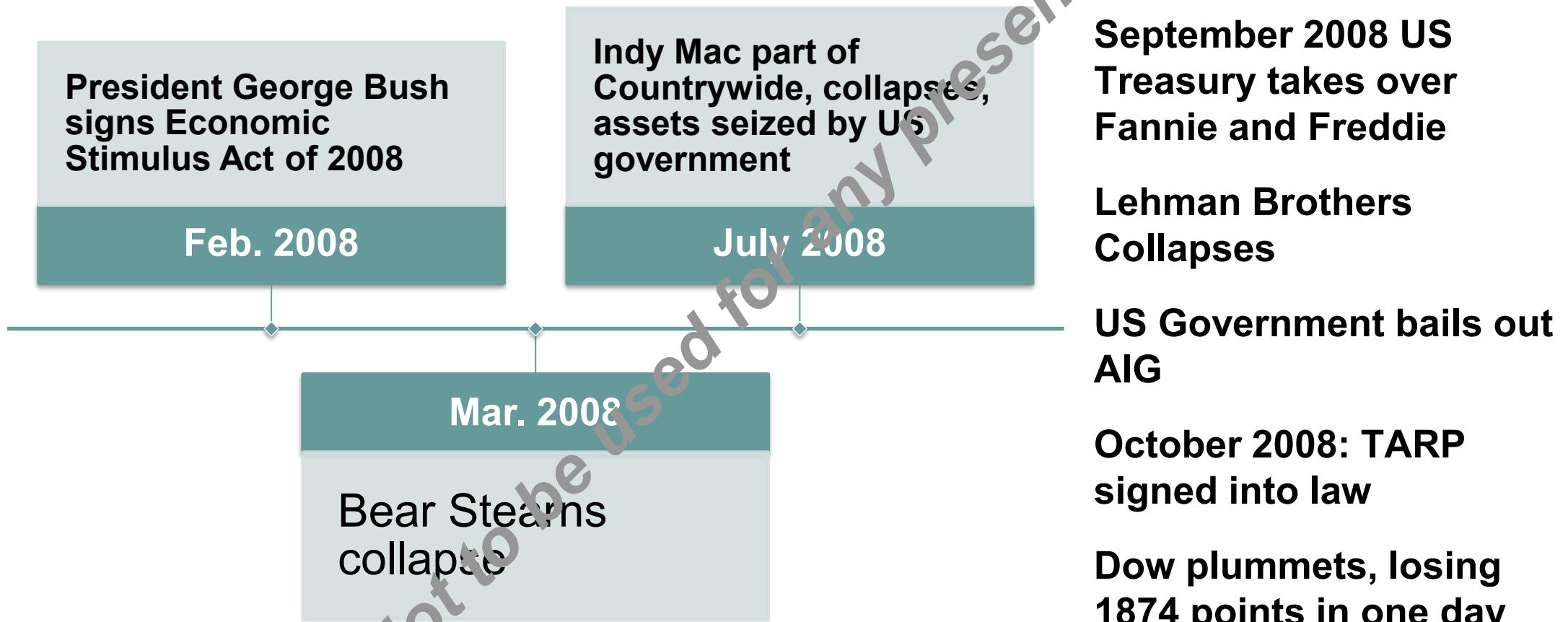
The Great Recession

(the 'grāt rē-sə-shən)

The economic downturn from 2007 to 2009 resulting from the bursting of the U.S. housing bubble and the global financial crisis.

Investopedia

Timeline



Timeline

November 2008 US Government bails out Citigroup

December 2008 General Motors and Chrysler get \$80.7 BILLION TARP funds

Fed reduces interest rates to 0%: first time in US History

January 2009 Bank of America bailed out

New President Obama approves a \$787 billion stimulus package, contains some tax relief

Dow plunges to low of Great Recession, ending at 6547, more than half of October level

June 2009: National Bureau of Economic Research says “recession over”

“It ain’t over till the fat lady sings...”

June 2009 GM files for bankruptcy

October 2009 US unemployment hits 10% first time in quarter-century

Foreclosures hit record levels, 2.9 million in 2009 alone



2000-2010 House Prices



- \$171,100 in 2000
- \$222,900 in 2010

Obama



Stock market up



Many new taxes



Unemployment down, but labor participation rate down (fewer people looking for work)

Obama



GDP 'sluggish' at best



Obamacare raised government spending and taxes



Real median income down



More financial regulations passed:

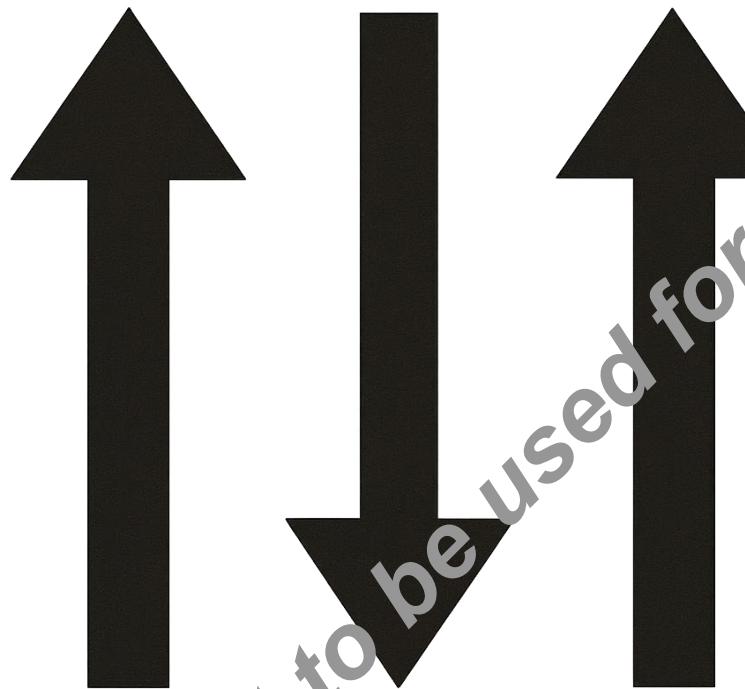


Dodd-Frank



CFPB changes real estate settlement procedures

Taxes



2001 top rate
39.1%

2002 top rate
38.6%

2013 top rate
39.6%

Trump followed Obama



US unemployment hit a 50-year low of 3.5 percent in December 2019

Black and other minority unemployment hit new lows

Black teenagers experienced more employment than at any other time

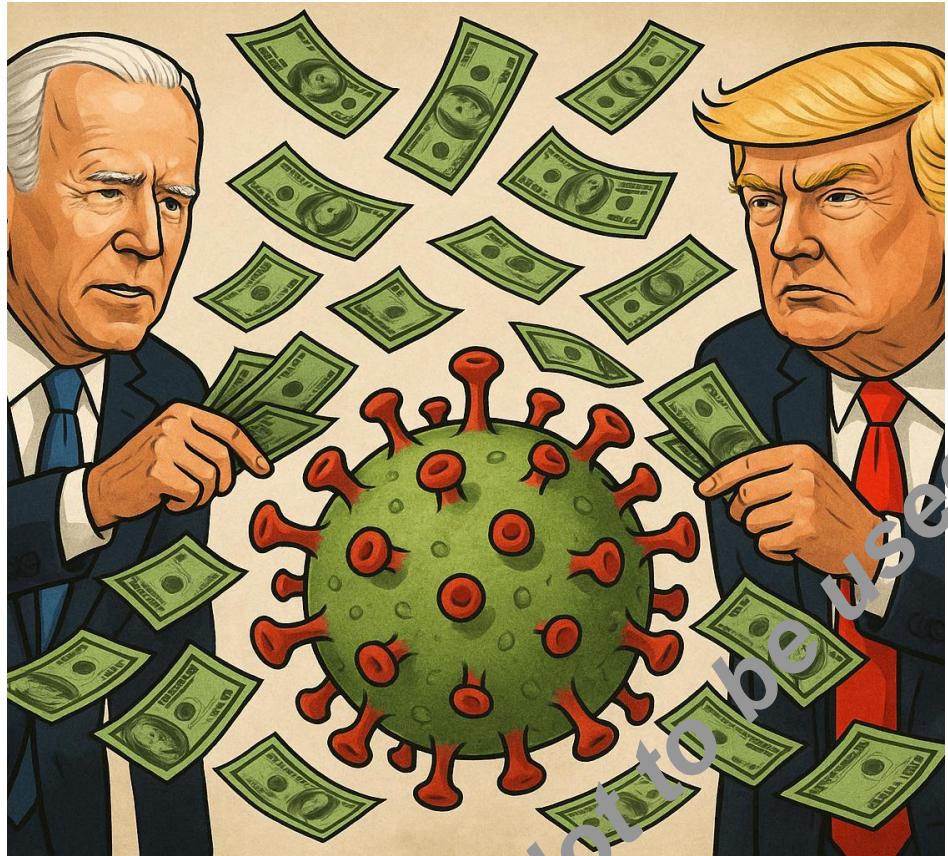
Corona Virus set all employment back

Then: Covid!



- Historic highs in stock market
- Up 111+% 2017-2021
- Tax cuts
- Coronavirus!

Coronavirus



**Congress and Presidents
Trump and Biden began
throwing money at this
problem**

**June of 2021 a trillion of
this remained unspent**

Biden



Tax and Spend bills

“Build Back Better”

Green initiatives

Record inflation

Stagnant employment gains

Recession: 2 quarters of declining GDP

Student loan forgiveness

2010 to 2020 House Prices



2010
\$222,900
2020
\$338,600
Up 51.9%

Government & Inflation



Which 'basket'
are they using?

Summer of 2022
feds conveniently
left out food and
fuel CPI because
they are 'volatile'

Bank Failure: First Republic 2023



**Made low interest
mortgages to wealthy
people**

**Paid high interest to
clients**

**Many account balances
exceeded FDIC coverage**

First Republic Investments

**Heavy investments in
commercial real estate**

**Invested in Silicon Valley Bank &
Signature Bank**

**Investors got worried
Over \$100 billion of deposits
withdrawn in one week**



What Happened?

**FDIC seized First
Republic Bank**

**Sold to J P Morgan May
1 ,2023**

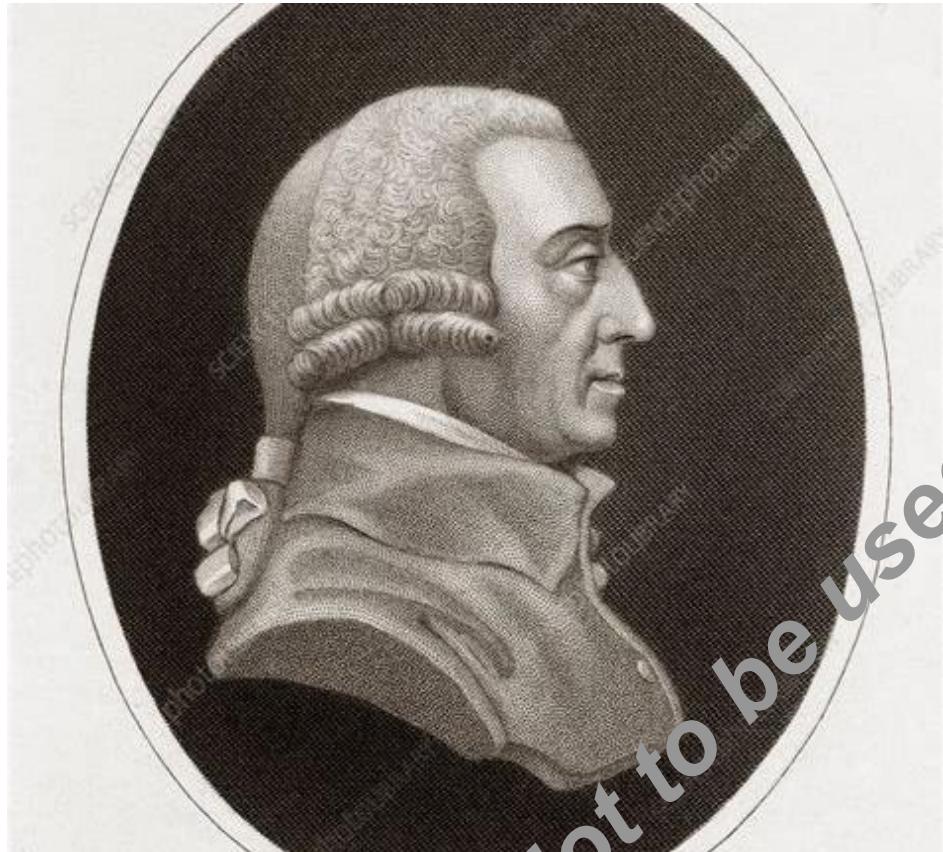
“Fire Sale”

To protect depositors

Keep panic at bay



Adam Smith



An Inquiry Into the Nature and Causes of the Wealth of Nations

Self interest will cause people to prosper

Limited government

Individuals would invest resources in the manner which would yield the highest return

Free market: supply & demand sets price

Adam Smith

- Quote: “It is not from the benevolence of the butcher, the brewer, or the baker, that we can expect our dinner, but from their regard to their own interest.”

John Maynard Keynes



Father of Modern Economics

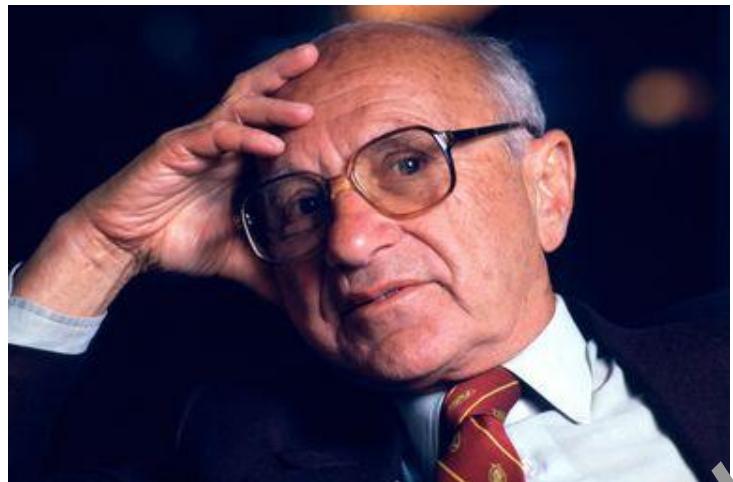
Governments can influence macro economics

Government intervention

Believed in a multiplier effect for government spending

Quote: “In the end, we’re all dead.”

Milton Friedman



Capitalism and Freedom published in 1962

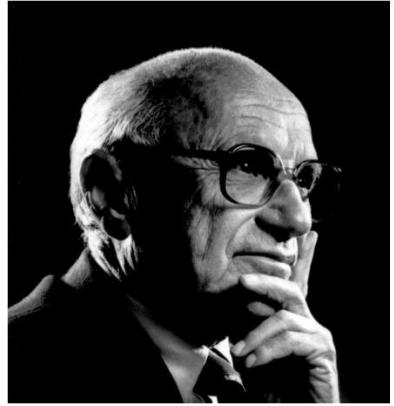
Political freedom & economic freedom go hand in hand

Believed we should go off gold standard

Demonstrated that government spending resulted in an equal change to GDP, not a multiplier (refuted Keynes)

Believed in flat taxes

Milton Friedman



“Underlying most arguments against the free market is a lack of belief in freedom itself.”

Milton Friedman (Capitalism and Freedom)

Argued that many government programs have “unintended consequences”

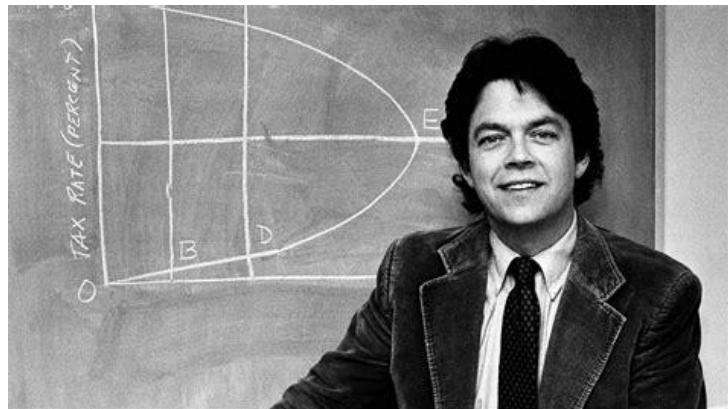
Quote: “There is nothing so permanent as a temporary government program.”



Arthur Laffer

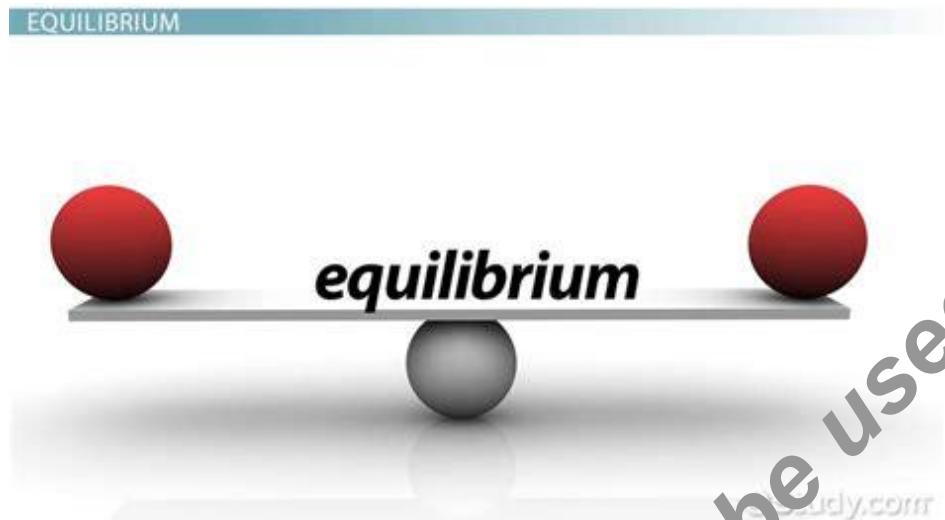
- **Laffer Curve: raising tax rates will eventually *lower* tax revenues because tax payers have no incentive to earn more money**
- **Supply side economics**
 - Remove barriers, reduce taxes, businesses will create jobs

Arthur Laffer



Quote: “And you can’t have a prosperous economy when the government is way overspending, raising tax rates, printing too much money, overregulating and restricting free trade. It just can’t be done.”

Equilibrium



In economics, equilibrium is defined as when supply equals demand (they are in balance).

Real estate is an *imperfect market* (rarely in equilibrium)

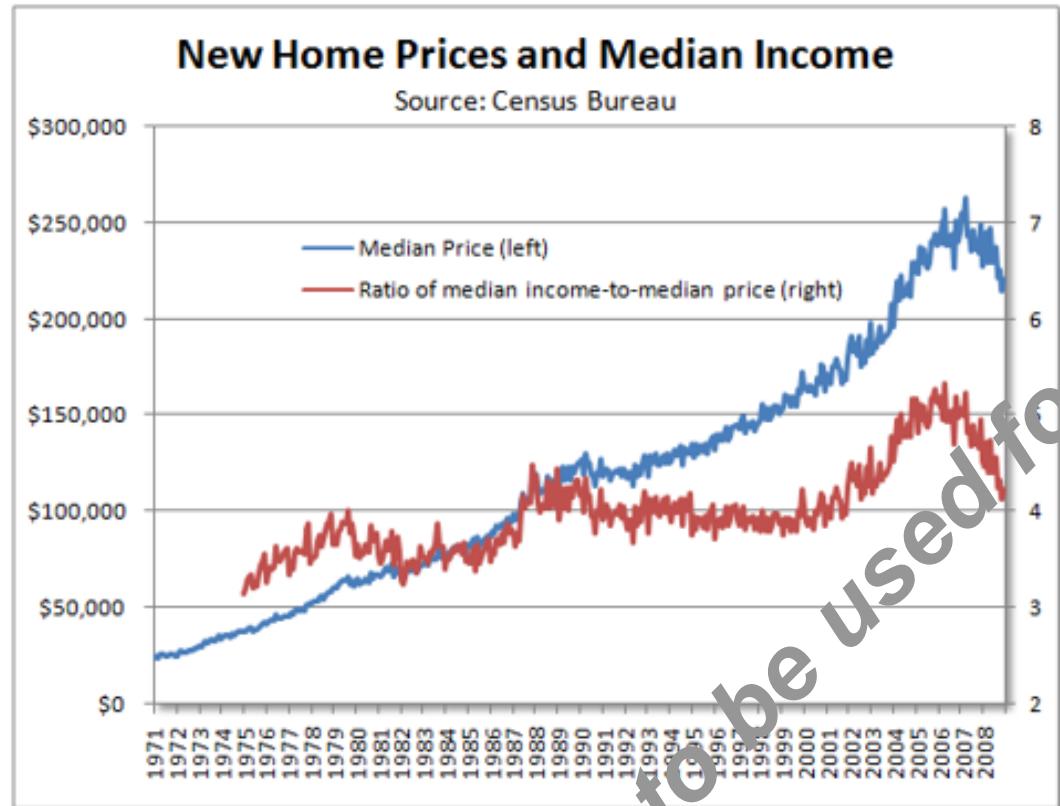
Why?

Equilibrium (Point & Price)

- In a free market, an equilibrium will be established at a price which will result in a supply that will satisfy the demand of buyers



Demand and Money



Housing has to correlate to median income

Relationship between rental rates and income; mortgage payments and income

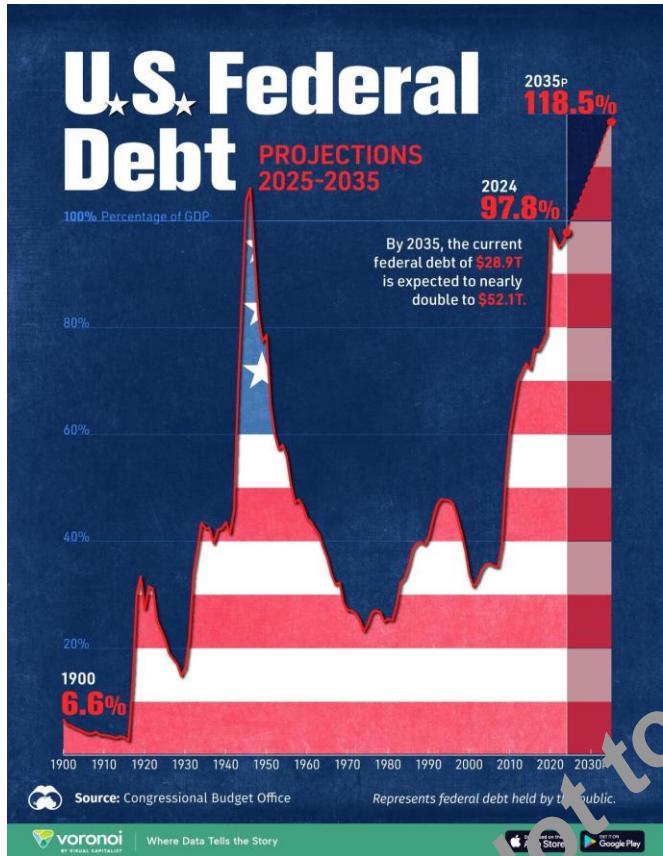
In many markets, median income earners can't afford houses

The Real Estate Market is Imperfect



- Real estate does not lend itself to perfect economic supply and demand models

Monetizing Debt



Government buys back its own debt
Can lead to inflation
Can devalue the dollar

Beyond our control. . .

Interest rates

Supply

Demand

Unemployment rates

- Demographic changes
- Local moratoriums
- Negative external influences (new roads, etc.)

Real Estate Markets are influenced by. . .

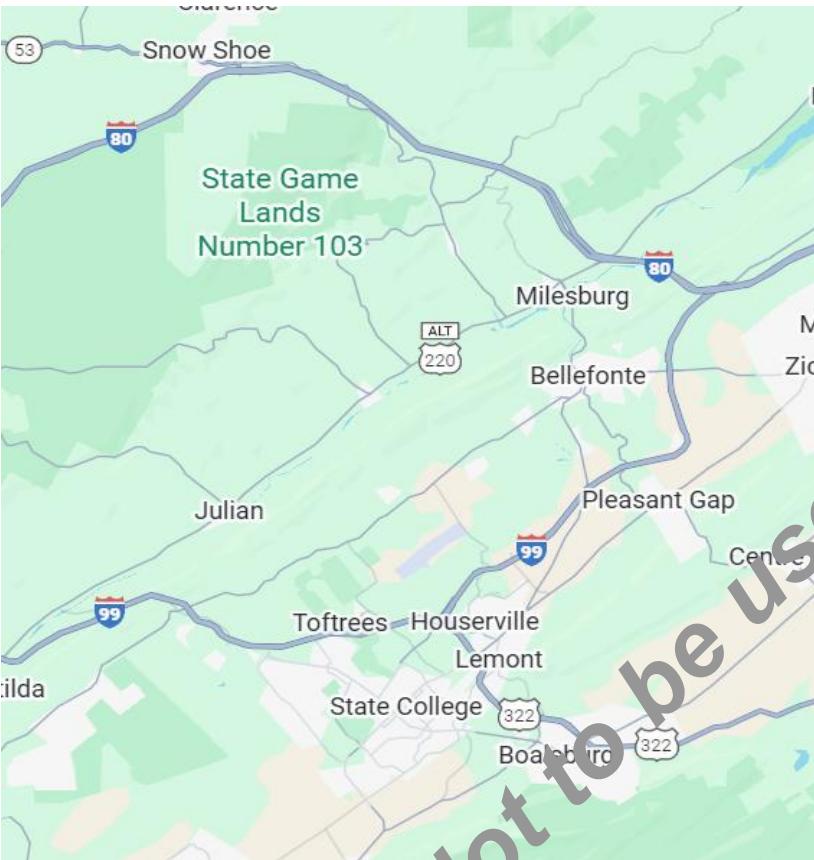


Federal Laws & Policy
e.g. the Fed, interest rates

State Laws and Policy
e.g. state's economy, tax structure, how certain things are funded

Local e.g. local employment, local taxes, local moratoriums, etc.

Local Economy



- Can have large variances within a region**
- Communities which rely in whole or part on one employer are vulnerable**
- Demographics can vary greatly within county or region**
- Tax structure, tap on fees, local moratoriums, all contribute to affecting this market**

Other Factors:



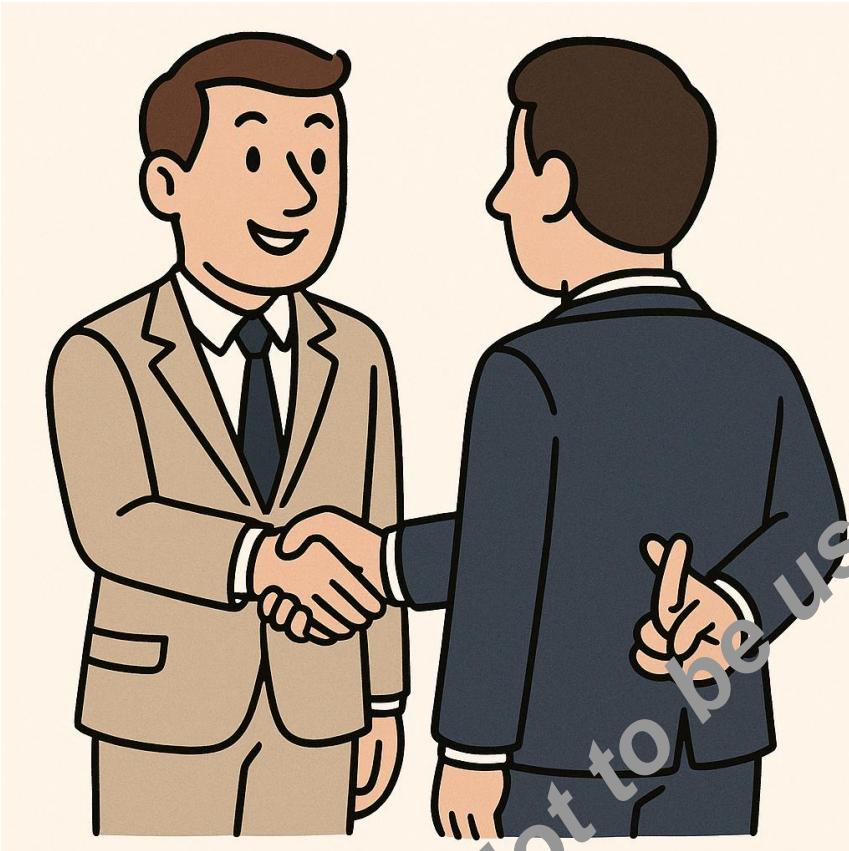
- **Demographics:**
 - **Age**
 - **Educational levels**
 - **Household formations**
 - **Family size**
 - **Income levels**

New Jobs Multiplier



- Dollars spent in a community are generally multiplied in effect by a factor between 2 and 3
- Net effect of \$1,000,000 per year payroll is 2 to 3 million

Summary



Politicians make policy to try to influence economy
Doesn't always work
Unintended consequences abound
Watch what is going on!

**THANKS FOR
COMING!
MELANIE MCLANE**

Open: Not to be used for any presentation purpose

