heraldsun.com

Professor warns of 2nd wave of foreclosures

BY MONICA CHEN : The Herald-Sun
mchen@heraldsun.com
Jun 4, 2009

BOOKMARK

DURHAM -- Despite glimmers of optimism about consumer confidence recently, the fundamentals underlying the recession are still unable to support a sustained recovery, warns Campbell Harvey, international business professor at Duke University's Fuqua School of Business.

In fact, because of the surge in unemployment in recent months that are expected to continue, Harvey said there could be a second wave of foreclosures.

"The first wave was caused by people buying a house well beyond their means in terms of their income," he said. "The second wave could be people with prime mortgages that can't pay because they don't have a job."

According to Duke's quarterly survey of chief financial officers worldwide, while more American and Asian CFOs were optimistic about their respective national economies, constraints in the credit market and concerns about the greater economy are leading them to make more cuts in their companies.

In the next 12 months, CFOs at 540 U.S. firms reported they expected the following: an average of a 4 percent decrease in earnings, an 11.5 percent reduction in capital spending and a 5.6 percent cut to their respective work forces.

"These CFOs have these planned a year in advance. This is not just talk," Harvey said.

The national unemployment rate for April was 8.6 percent.

The CFOs surveyed expressed concerns about consumer demand, credit markets/interest rates, federal government policies and the housing market fallout.

Results of the survey also pointed to the continued impact of credit problems for companies. Fifty-nine percent of CFOs said the credit crunch is directly hurting their firm, with many having drawn the maximum on their credit lines.

The credit crunch is creating a "dramatic split of haves and have-nots in the credit market," said John Graham, a finance professor at Fuqua and the director of the survey.

Those companies, with AAA/AA/A credit ratings, that have an easier time of getting loans have seen their cash increase from 16 percent at the start of 2008 to 19 percent. Meanwhile, firms that haven't been able to get loans have seen the cash they hold fall from 16 percent to 13 percent.

The credit crunch has continued to affect mostly smaller, medium-sized companies with poorer ratings, according to Graham.

"Banks have really tightened up standards and are making it much more difficult to borrow," he said. "For banks, their capital is limited. They're recovering from their own problems and they're not willing to take certain risks."

Graham said the tightened standards should only be temporary.

More CFOs were optimistic about the economy this quarter rebounding from the all-time low in the first-quarter 2009 results.

About 54 percent of U.S. and 63 percent of Asian CFOs were more optimistic than last quarter. Only 30 percent of European CFOs were more optimistic.

BOOKMARK

© 2009 by The Durham Herald Company. All rights reserved.