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Free Fall's Over, but Where Are We Landing?

By PETER S. GOODMAN

BOISE, Idaho

BACK in September, when financial reality was still merely horrible but not yet catastrophic, a local software start-up called Balihoo was poised to expand.

It already sported the outward trappings of tech world success: an airy space in an old brick warehouse downtown, renovated with recycled wood and glass; a roomful of 20-somethings in fleece pullovers, their mountain bikes hanging from wall-mounted racks; and a hot new product.

All that Balihoo needed was more money, and it was about to get some. Three venture capital firms beckoned with offers to invest a fresh $3 million in the young company.

Then Lehman Brothers collapsed, beginning a string of spectacular Wall Street failures. As primal fear seized the financial system, money suddenly became as difficult to secure as true love on a reality dating show. The venture capitalists changed their minds.

“All that interest disappeared,” says Balihoo’s chief executive, Peter Gombert. “It was nuclear winter.”

In October, Balihoo laid off 10 people in Boise and braced for more painful days. But in the last several weeks, the venture capitalists have returned, enticed by Balihoo’s strong sales, and also by something infinitely more valuable: glimmers of renewed faith in parts of American commerce. “Risk” no longer seems like a radioactive word.

“The spigot turned back on,” says Mr. Gombert, who now expects to raise as much as $5 million. Some of that money will allow him to hire four or five people who will help Balihoo continue to make software that enables national brands to customize local advertising campaigns.

“We still will be pretty conservative in our growth,” he says. “The economy still hasn’t rebounded, and one of the worst things we could do is spend that money fruitlessly. Everybody’s still feeling the pain, but we’re starting to see a little creep up in confidence.”

Three months into a new presidency begun in the midst of deepening economic desperation, the myriad programs of the Obama administration appear to have taken the edge off the financial crisis while generating momentum toward economic recovery that remains, by most estimates, at least several months away.

After the convulsions of last fall, when seemingly impregnable financial institutions fell and cash all but vanished from many areas of commercial life, borrowers with decent credit — from home buyers to corporations — are finding money available on increasingly attractive terms. Home sales are up in many markets, albeit at sharply lower prices. Consumer spending, still shrinking, has nonetheless halted its panicked retreat.

Yet the economy remains pitifully weak, with distress abundant from strapped households to anxious corporate boardrooms. More than two million jobs disappeared over the first three months of the year as the unemployment rate soared to 8.5 percent. With wages still shrinking or evaporating, stock portfolios and savings accounts ravaged, and the future still uncomfortably uncertain, millions of households are likely to keep scrimping, challenging any potential recovery.

"We've just had the worst hit to wealth in the history of the data," says Robert Barbera, chief economist at the research and trading firm the Investment Technology Group. "The labor market data is unambiguously horrible."

So will the Obama administration's apparent achievement in arresting an economic free fall yield a sustainable revival, creating millions of jobs, generating fresh business opportunities and restoring a sense of optimism?

Can programs aimed at reinvigorating the financial system make money flow, allowing companies to expand and hire? Will federal spending amount to something like a piñata at a children's birthday party, with the proceeds scattered willy-nilly? Or will that money help catalyze a genuine economic renewal?

BOISE, a metropolitan area of 600,000 people set in the high desert, is as good a place as any to try to figure this out. In many respects, the local economy presents a microcosm of the recent American experience, making it a useful laboratory.

A former trading post on the Oregon Trail, Boise now has microbreweries, coffee houses and bohemian chic boutiques inhabiting brick storefronts downtown. Beefy men in chamois shirts debate fishing tackle over steins of beer, while others with goatees and pierced lips sip chai lattes and discuss herbal medicine.

A lattice of trails threads into the surrounding Rocky Mountain foothills. A combination of outdoor appeal, local technology jobs and affordable homes has attracted thousands of families to the area. Many have escaped expensive, traffic-filled lives in cities like Seattle, Los Angeles and Phoenix. Some have settled in Craftsman-style homes north of downtown. Many have landed in suburbs west of town, where vast stretches of farmland have been carved into subdivisions.

In what now stands as the guiding narrative of precrisis American life, abundant land fertilized by easy finance delivered a local construction boom, much as it did in Florida, California and elsewhere, on seemingly every patch of soil not occupied by a toxic waste dump. Speculators poured in on organized bus trips, driving prices skyward.

But after too many homes were built and prices had climbed beyond any rational connection to local incomes, Boise suffered the same punishing pullback that has afflicted much of the country.

Prices of existing homes in the Boise area leapt from an average of $130,000 in 2003 to $206,000 in 2007 but fell to $170,000 by the end of 2008, according to Moody's Economy.com.

Building construction jobs in the Boise area plunged to 3,000 in March from 5,000 in the summer of 2006, according to the Labor Department. Over that same period, the local unemployment rate soared to 8.6 percent from 2.4 percent.

Exacerbating that picture is the crisis confronting Boise's largest employer, Micron Technology, a manufacturer of memory products used in cellphones and other electronics. In the face of a global production glut and weak consumer demand, Micron has lost more than $2.7 billion over the last two years.

Layoffs have shrunk the company's local work force to about 6,000 today from 10,000 three years ago, with another 1,000 jobs to be excised this year.

"We're spending very, very conservatively," says Micron's president and chief operating officer, Mark Durcan.

Micron's headquarters feel like a dusty trophy from another era — a campus of boxy buildings ringed by parking lots, with reception areas reminiscent of hospitals, and carpeted floors chopped into cubicles. Among locals, one hears talk that Micron, despite the company's assurances to the contrary, cannot possibly remain here much longer.

"Micron is a big scare," says Danielle Cullip, a Realtor at Serenity Real Estate. "The fall of Micron is going to be horrendous."

Micron's troubles help explain why Paramount — a suburban development with plans for 1,500 homes — remains only one-third built five years after it was begun. "THIS STREET IS TO BE EXTENDED IN THE FUTURE," read placards affixed to barriers where pavement gives way to empty, scrub-covered earth.

Paramount is the work of a local developer, the Brighton Corporation, whose principal, Peter Oliver, grew up in a hippie commune in New Mexico. "All I ever wanted was indoor plumbing and cable television," Mr. Oliver recalls.

Now he makes his living peddling the comforts he once craved, offering a quintessential slice of American suburbia. Yet the credit that nurtured this lifestyle for decades is gone, putting his homes beyond reach of many families. In this new, post-easy-money era, many households are relinquishing aspirations for more, bigger, newer.

"This isn't a correction," Mr. Oliver says. "It's a full-blown reset."

Still, at a recent showing of Paramount's model homes, nearly 500 people arrived for a look at gleaming kitchens and family rooms.

"People with decent jobs and decent credit are saying, 'It's time to buy,' " says Mr. Oliver. "People get to a certain point where they're just sick of feeling bad about stuff."

Real estate agents and mortgage brokers say they have seen renewed interest from first-time home buyers. They credit lower mortgage rates — the result of the Federal Reserve and the Obama administration pumping cash into markets — as well as another administration initiative unleashed in February: First-time home buyers are eligible for tax credits up to $8,000.

"It's gotten buyers off the fence," says Suzi Boyle, a mortgage originator at Evergreen Home Loans in downtown Boise.

Last month, Jason Sears, an easygoing, single 31-year-old, offered $140,000 for a four-bedroom house in a gentrifying part of town. Ms. Boyle secured him a 30-year fixed-rate mortgage at 4.7 percent.

Mr. Sears works as the operations director at the local Boys and Girls Club, an organization financed largely by corporate donations. Back in January, with donations withering, he was too frightened about his own job security to buy a home. Things have changed. "I do feel a little more secure," he says.

In March, sales of area homes leapt 48 percent compared with the previous month, though that was still down 8 percent compared with a year earlier, according to the Ada County Association of Realtors.

"We know it's not getting worse, and that's almost enough," says Marc Lebowitz, the association's chief executive.

BOISE still faces hurdles. So much lending poured into real estate development that the area is encircled by a kingdom of empty lots, making banks on the hook for those loans reluctant to take risks on other ventures.

"There's probably an eight-year supply of building lots," says Dave Player, senior vice president in commercial lending at Mountain West Bank, a regional lender.

As speculators absorb losses, breadwinners surrender wages, and low introductory rates on mortgages reset higher, a foreclosure wave appears to be gathering force. In some suburban areas, like Meridian, foreclosures increased nearly 75 percent over the first three months of the year, according to RealtyTrac.

"If we don't get those foreclosures stopped, this is going to be long and painful," says Ms. Boyle of Evergreen Home Loans. "Foreclosures are killing us."

The federal government has long portrayed foreclosures as a crucial national problem, but ever since the financial crisis began, it has failed to find solutions.

In February, Treasury Secretary Timothy F. Geithner announced a plan aimed at sparing as many as four million distressed homeowners from foreclosure by rewriting their mortgages. Only a few thousand have been modified so far, the Treasury says, though the department has signed contracts with the nation's five largest mortgage servicers obliging them to consider modifying delinquent loans.

The agency says it expects to see the pace pick up soon, but analysts are worried that the Treasury program may never provide enough help. Moratoriums on foreclosures adopted by some institutions are now running out, long before the Treasury program gains momentum. If banks suffer new losses as homeowners run into trouble, they could tighten their lending anew and further suffocate the economy just as it is showing signs of improvement.

“This is shaping up to be a disappointment,” says Mark Zandi, chief economist at Moody’s Economy.com.

Another crucial initiative has also been slow to develop: a Treasury plan to encourage investors to buy bad bank assets using government loans and thus free banks to lend more aggressively. That program isn’t expected to become operational until the middle of the year, and many investors are wary of the assets.

Similar troubles confront a program aimed at freeing money for auto loans, credit card lending and other consumer finance.

“Investors are worrying about the government’s penchant for changing the terms of the deal,” says Alan S. Blinder, a former member of the Federal Reserve and an economist at Princeton. “The belief is there’s a danger that the government’s going to put more restrictions on you if you participate.”

Andrew Petrehn isn’t sure about the details of the programs being unleashed in Washington, but he is certain that no benefits have reached him. In December 2007, he and his wife, Saundra McDavid, expanded their popular barbecue restaurant, Andrew’s Rib Shack, leasing a 3,500-square-foot space in Boise. They borrowed $150,000 from a local bank. A private equity firm discussed expanding their brand as far as San Diego.

But as the recession unfolded, the new restaurant drew few customers. The private equity firm went away. The couple cut staff to 6 from 25 and reduced hours. In February, they shut the doors. These days, they cater out of a rented church kitchen.

Mr. Petrehn is keen to own a restaurant again. “There’s prime locations that are vacant right now and potentially very cheap,” he says. But no one is willing to lend him the money. “The banks are still shut down.”

Even successful ventures are feeling the crunch. Kevin C. Settles, co-owner of Bardenay, a chain of restaurants known for distilling its own rum, vodka and gin, has seen sales slide only about 1 percent at its two Boise-area locations. Yet his banker recently bumped up the interest rate on his line of credit by 2.5 percentage points — “for no apparent reason,” he complains.

Food costs have fallen and high unemployment has made it easier to hire quality people — ideal conditions for expansion, says Mr. Settles. But he doesn’t think he can get capital.

Bankers are unapologetic. “We’re doing commercial lending, but they’re going to have to make sure they have cash flows,” says Joey Perry, vice president at D. L. Evans Bank, an Idaho lender that received $20 million in federal bailout money.

AMONG some economists, a sense has taken hold that the Obama administration’s plans have been unduly shaped by political pragmatism: Given public disgust over bonuses paid to executives at bailed out financial institutions, Congress is reluctant to hand over more money, forcing the administration to resort to gimmickry in an effort to repair lenders without further nicking taxpayers.

Others say that focusing too narrowly on the immediate financial and economic programs misses the true significance of the Obama administration's undertaking. Not since Franklin D. Roosevelt stepped into the White House in the Great Depression has a new president confronted such a stark challenge.

In addition to his financial system and federal spending initiatives, Mr. Obama has already annunciated a "long-term strategic vision" for the economy, centered on expanding health care and education while embracing renewable energy, argues David M. Kennedy, a historian at Stanford University, whose book, "Freedom From Fear," recounts Roosevelt's New Deal.

"They understand the task is not just to restore the economy to business as usual but to put it on a sounder footing going forward," he says.

In the first weeks of Mr. Obama's tenure, he persuaded Congress to approve $787 billion worth of federal spending to stimulate the economy — $288 billion in tax cuts plus $499 billion to aid states and local governments.

In crucial ways, this spending has already had an effect, say economists. It extended unemployment benefits and food stamps, while cutting by nearly two-thirds the amount that laid-off workers must pay to retain their health insurance.

But whether it revives economic activity remains unknown. The tax cuts are only now being distributed. Only about $75 billion has been dedicated, mostly to public works projects like road-building.

"The moment of truth is coming soon," says Mr. Zandi. "If we don't see something real in the data by June, then I get very nervous."

Boise's mayor, David H. Bieter, is hopeful. The federal stimulus package includes $2 million for energy efficiency projects in Boise, like retrofitting buildings.

And the recently passed federal budget includes $2 million to extend the reach of the city's geothermal system, which taps groundwater to heat downtown buildings. The mayor portrays that project as a crucial piece of Boise's efforts to position itself as a center of clean energy.

At the United Brotherhood of Carpenters union hall, George Suite, a father of seven, hopes all of this federal spending will translate into a steady paycheck. He has worked only three weeks over the last year and is struggling to pay his mortgage while living on a $371-a-week unemployment check — which has replaced the $720 in weekly take-home pay he once enjoyed.

"The banks are getting all that bailout money," he says. "What about working people?"

Others here are more confident that the funds streaming out of Washington will eventually make a difference.

Tony Robinson, who was laid off from a sales job at a local division of Microsoft in January, recently took a new position at a local start-up, Inovus Solar. The company makes solar-powered street lights and high-efficiency conventional lighting — the very products communities across the country are adding with their stimulus money.

“The potential of this is unbelievable,” he says. “It’s going to be the tech sector over the next decade.”