IlLUminate Blog Transcript: **Georgette Phillips on Clues to a COVID Comeback**

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ANNOUNCER: 00:02	[music] This podcast is brought to you by ilLUminate, the Lehigh Business blog. To learn more, please visit us at business.lehigh.edu/news.
ROB GERTH: 00:13	Welcome. I'm Rob Gerth, Director of Marketing and Communications for Lehigh University's College of Business. Today is September 21st, 2020, and we're talking with Georgette Phillips, Dean of the College of Business. The dean's research and teaching is focused on the intersection of law, economics, and public policy, within the context of the built environment. She has published in the areas of urban and regional planning, local government law, real estate, and housing. And it's really the commercial real estate part of your experience, Dean, that brings us together here today. Welcome.
GEORGETTE PHILLIPS: 00:45	Thanks so much, Rob. I'm just so happy to do this.
GERTH: 00:48	We talked about it, and you came up with this kind of cool idea of the problems that happened in the early '90s and in 2007 to 2009, what we call the Great Recession, that there's some parallels there. And I was like, "Oh, well, do tell," and that's how we ended up here today. So [crosstalk]--
PHILLIPS: 01:06	Yeah. Rob, if you remember, the original conversation began with me saying, "Being in real estate, I tend not to panic a lot--"
GERTH: 01:16	[laughter] Yeah. That's right.
PHILLIPS: 01:17	"--because part of what we do is we go through these cycles, and we know that things always come back. And so we're a little bit more sanguine about the issues."
GERTH: 01:30	Tell me where you were during the previous downturns.
PHILLIPS: 01:35	Very interesting question because I got to see the downturns from very different vantage points. In the '90s, I was still doing deals. I was actively closing deals. And at the peak, I was closing, oh, a deal a week easily in mainly office, some retail. And I took maternity leave, came back after my son was born, and there were no deals. It was almost like someone had turned off the lights and walked away, and I thought, "What is going on here?" Then in 2007, 2008, 2009, I was in academia, and I got to see that recession from the vantage point of a more scholarly looking at the underlying causes, not having the direct effect on what I was doing. And so both vantage points allowed me to really experience what it is to be resilient in the middle of an economic recession.
GERTH: 02:50	Now, you say in your business, you're sanguine about the pressures and the changes and everything's going to go back. But during those times, what was the general outlook? Was it bleak like it is today?
PHILLIPS: 03:03	Yeah. As a matter of fact, I can remember in the '90s when we were just all kind of looking at each other, going, "Well, what's next?" And we had a slogan which was, "Stay alive till '95." [laughter] That if we could make it until '95, if we could keep the

businesses going until '95, things were going to be okay. And guess what? They were. Things turned out fine.

GERTH: 03:32

In either case, was there any kind of denial that's going on? We have denial today, and I'm not trying to make it political. It's just some people think it's a crisis. Some people think it's not a crisis. Was that the same back then, that some people were like, "Nah, this isn't so bad"?

PHILLIPS: 03:47

Oh, we all knew that it was a crisis. But we came at it from very different vantage points than we are today because, both in the '90s and in the 2000s, there were underlying business issues that caused the recession. Today, the pandemic was the cause of the recession, not the underlying business dealings. And so there were no deniers. There were some fundamental things that had to be solved, market-driven problems that had to be solved. And for each of these recessions, both in the '90s and in the 2000s, the underlying problems were resolved. Now, ironically, as we can probably touch on later if you like, the resolutions that happened from the '90s subsequently caused what happened in 2000. But each of them had an economic problem that was solved with an economic solution.

GERTH: 04:49

Can you give the basics of what the causes were?

PHILLIPS: 04:52

In both cases, it was overlending and exposure to risk. So in the '90s, there was a lot of building that took place. Again, I can remember with some of these closings that I was doing. I would look at this, going, "Wow. How is this ever going to work? These rent rolls are - let's use the word - interesting." [laughter] I don't want to say falsify. Let's just call them interesting. And how is this going to work? And I remember when I came back, there were several loans that I had very recently closed that had never made a payment. They never made a payment. And so there were all of these bad loans just sitting out there. And the lenders were burdened with this debt that was uncollectible. And so that turned into the CMBS market, the commercial mortgage-backed security market, which tranched debt, which allowed the lenders to now choose their risk profile for their debt. "Instead of doing whole loans, maybe I'll only buy the top part. Maybe I'll buy the middle tranche," whatever it was. It's segmented risk.

GERTH: 06:14

And then what about in the 2018-- or 2008 period, as far as how things came back? What was the secret to that?

PHILLIPS: 06:23

Well, it's interesting because it was the same root cause - right? - overlending. There was just too much money out there that was based on rather dubious income statements. But in this case, it was the residential market. It wasn't the commercial market so much. It was the residential market. And the residential market blew up because when interest rates rose, people were unable to refinance their debt. And when they couldn't refinance their debt, they defaulted. What happened? We had all of these lenders who were sitting on a lot of loans. Now, ironically, one thing that played into the recession in the 2000s and the blow-up in the 2000s was the advent of a risk-segmented market. So it was the rise of synthetic products such as CDOs, collateralized debt obligations, that took the bottom piece of a deal and spun it off and resold it and repackaged it as a AAA obligation. And that's really what blew up the market. The linchpin between both of these, besides the exuberant lending that took place, was the resolution of the crisis in the '90s, which then led to the crisis in the 2000s, was the advent of massive computing power. We couldn't have solved the '90s

- the CMBS market would not exist - if we didn't have the advent of exploding computing power, which then led to the Wall Street versus Main Street lending practices that took place that led to the 2008 recession.

GERTH: 08:26 And the computing power was used to make deals, and so many deals could be made. It was historic as far as the number of-- is that what the computer power did?

PHILLIPS: 08:37 No. It allowed you to do what's known as tranching. Tranche is French for slice. So instead of whole loan lending, which is the traditional you go to a lender, you take out a mortgage for the whole amount, and the lender carries that debt on its books. What we were able to do now with the advent of massive computing power is we were able to slice and dice each individual loan and then sell that as a piece according to an investor's risk profile. So people who had a higher risk profile would buy the lower tranches of the deal. The people that had a higher risk profile-- or a lower risk profile would buy the more secure, the top ends of the deal.

GERTH: 09:24 And so during both of those times and now as well, there's arguments over stimulus and what should be the financial stimulus, like how much you should give and what's the limit and how long it should happen. I assume that was the same during those times as well, that that's something people argued about.

PHILLIPS: 09:47 Oh, absolutely. You're absolutely right about that. The government had a role to play in many, many ways. One thing it can't do today that it was able to do in prior recessions was lower the interest rate. I mean, we can't get much lower.

GERTH: 10:03 Because it's so low already, yeah.

PHILLIPS: 10:05 Yeah. So that's not really a tool available for this economic recession. But in both cases, government intervention was absolutely necessary. Now, what can the government do now? You see there is some government intervention but on a far more fragmented and less federally oriented perspective, which are things like rent moratoriums, that if you are unable to pay your rent and you fall into a certain category, you can't be evicted. Okay? The ability to forestall payment on your loans-- now, this is not debt forgiveness for your mortgage. I mean, you still have to make it up, but if because you've lost your job you can't pay your home mortgage. But this is really just for the homeowners.

GERTH: 11:47 Right. What about on the bigger scale? Are there any tools? Have you seen anything that people are talking about that's similar to the stimulus package that the banks got?

PHILLIPS: 11:56 No, I haven't, and it's kind of scary. One of the largest retail REITs is in really big trouble right now. They defaulted on a loan payment back in July, I believe. And the special servicer on this REIT has been able to make interest payments to the bondholders from money it held back in prior months, but that money is running out. So this will be very, very interesting to watch.

GERTH: 12:31 It feels like everybody's focused on the COVID-19 part of it, the disease part of it, and not focused on what's going to be the outcome-- what else it's affecting. You look at things like-- what people say to me-- what I've heard people say is the pandemic is speeding everything up. So everything bad that was going to happen is happening faster, like shifting to e-commerce or department stores going out of business or buying all your food, shopping, doing it all online, or even transitioning to working remotely. Were they these kind of predictions that experts were making back in the '90s and in 2007, 2008? Were they predicting those same kinds of things? Was it speeding things up as well?

PHILLIPS: 13:17 Well, it did speed things up in terms of the way that mortgage debt was issued. It sped things up in the homogenization of loan product. It used to be that on a commercial deal, it was unique to that property. I mean, you could really do a lot of wheeling and dealing and changing of the loan documents. Now your documents are pretty homogenized across the board. What is interesting about this recession is that it wasn't caused by real estate, but real estate is taking the brunt. And the reason real estate's taking the brunt-- I mean, not just real estate. There's so many sectors that are taking the brunt. But the way that we are taking the brunt in real estate are lifestyle changes. So you remember what happened to newspapers when things started to go digital. A lot of newspapers are out of business now. But the newspapers that pivoted, that embraced technology, that embraced new ways of interacting - I think the New York Times is probably the best example here, or the Washington Post, clearly the Los Angeles Times - they are more than just that newspaper that's delivered every morning. They get you soup to nuts. I mean, how many times have we gone to the New York Times cooking app?

GERTH: 14:42 Right. [laughter]

PHILLIPS: 14:42 I mean, yeah. But it's still the New York Times, but now it's my cooking app. And I think that, in real estate, we have to start thinking about these lifestyle changes and what does this mean? I am still confident in the market. I'm confident in both the retail and in the office market. I'm a little bit more confident in office than in retail. But the reason I'm so confident is that we just have to adapt. We just have to find where things are going, not necessarily that it's going away forever, but how can we harness the change that's occurring? So when you talk about the office market, instead of leasing X square feet for 15 years, 20 years, whatever it may be, is there a partnership that occurs between the tenant and the landlord in terms of redoing the office space and thinking about the tenant not having X square feet in use every day? I think that's one of the big changes that's going to happen. We're going back to work. We are definitely going back to work.

GERTH: 15:56 Do you think that--?

PHILLIPS: 15:56 I don't know that we're going back to work every day in the same way.

GERTH: 16:00 Do you think that just-- hold on to that before we come to working from home because I want to touch on that. But before we get there, do you think there's going be seller's remorse at the other side of this when Amazon has bought up all the malls and all the office buildings for their centers or for their office people? The people will be like, "Jeez, I wish I hadn't sold all my buildings to those people."

PHILLIPS: 16:22 I don't know if there's going to be any remorse because-- remember, you said something earlier that I'd like to come back to. We are seeing an acceleration of things that were already in progress. Malls were already suffering from the effects of e-commerce. So how can we think about using that space as more of a community space? The advent of community malls was a direct response to the rise in e-commerce. You're not going to the mall now for a pair of jeans. You're going to the mall for an experience and, oh, and by the way, if you need a pair of jeans, you can do that too.

GERTH: 17:09 Right. Yeah. Well, speaking of going somewhere for the experience, how do you like working from home?

PHILLIPS: 17:19 Hmm. I miss my coworkers. I do.

GERTH: 17:21 I know. I know.

PHILLIPS: 17:23 I know. I miss the interaction with the students. Oh my gosh. That's why we do what we do. Right?

GERTH: 17:33 Right. That's a lot of energy in those hallways.

PHILLIPS: 17:35 Yeah. I mean, Lehigh has such wonderful students. And things that we used to do, like we started every semester with Donuts with the Dean and couldn't do that. All of the symposia that we have that we bring the industry leaders and the students together, we can't do that. I really do miss that face-to-face interaction. But being an academic, I worked from home a lot more before I became dean because I did all of my research at home. So other than my dean position, I worked at home a lot already. So yes, I miss the student interaction. I miss my coworkers. I miss the things that we're able to do that we can only do in a group. But--

GERTH: 18:25 And everybody seems to be talking about working from home, but some of the surveys say that most people plan to-- the majority of people plan to go back to the office. So I don't know--

PHILLIPS: 18:35 Right. Right. Because we're social beings. Human beings like being around other human beings. Right?

GERTH: 18:45 And it's funny that the whole remote working was a thing, and IBM was doing it, and Yahoo was doing it. And now it's kind of reversed, where they actually were calling people back in the last five years. Yahoo had said, "No. We're not having people work from home anymore. It's not working out." Same with IBM. They said they were missing all that interaction you get in the hallways. And now it's like, "Oh, no. We're all working from home again."

PHILLIPS: 19:11 Well, here's the difficulty in working from home: culture. As a manager or as an organization, we work very, very hard in creating a culture of work, a culture of support, a culture of inclusively, all of these things that we hold very near and dear to our mission that just you can't do if you're online, especially with somebody who's new, somebody who hasn't lived in the culture. And then you hire them online. They never meet anybody face to face. It becomes far more transactional. And that's not the type of culture, at least, that we try to create at Lehigh Business.

GERTH: 20:04 Talk to me a little bit about agglomeration. That's a word I learned when all this started happening.

PHILLIPS: 20:12 [laughter] Agglomeration is the idea that there is a synergy that is created with colocation. So that's why you get places like Silicon Valley. It's not just that the tech companies are there. It's that the add-ons from the tech company and then the third- and the fourth-order companies are also there. So from the middle of the circle, you have the tech companies. You have the knowledge transfer. You go out and you meet somebody. You learn more. It's the chance meetings that we were talking about that you don't get if you're a work from home. But then you go out from that, and you need a worker. You need somebody that has this specific skill. In that type of environment, it's a very deep pool that you have to choose from. Likewise, if I'm looking for a job, I have a number of employers, not just one or two, to choose from. And so that draws other people which draws other people. And then you get out to the service providers. And one of my favorite examples is the people that make radios for cars were located in Detroit just like the car manufacturers were located in Detroit. Why? Because that's where they sold their goods. Lawyers. If you are a lawyer in Silicon Valley, you have your pick of companies that you can establish a very niche practice. I don't know what's going to happen with this whole theory of agglomeration economies because it is so deeply rooted in our economic system. I mean, it's not just Silicon Valley. It's why cities grow to begin with. That's why we have cities, because of the collocation and the advantages of collocation. It will be interesting to watch in the future.

GERTH: 22:26 It's definitely somebody's thesis. That's for sure.

PHILLIPS: 22:29 Yes. Yes.

GERTH: 22:30 [But let?]--

PHILLIPS: 22:31 Oh, there's a lot of work that's being done on this. A number of scholars are very deeply into this. Urban economists are all over this.

GERTH: 22:43 Let me ask you this. Is there a difference now from your perspective, or what is the difference, of an economic crisis caused by poor decisions that businesses made compared to one that's caused by a pandemic?

PHILLIPS: 22:57 The solution.

GERTH: 22:59 Ah. Tell me how.

PHILLIPS: 23:00 Well, when we make "bad" quote-unquote business decisions, we could stop making those decisions. [laughter] Okay? You caused a problem. We're going to solve the problem by not making that decision anymore and rectifying what went on. When the recession is caused by a pandemic, that's not a business decision. We can't, in the real estate sector, rectify the coronavirus. We just have to sit and wait for it-- and wait for the health officials to figure out how we're going to solve that problem. And then we can get back to what we're doing. That's the big difference in my eyes.

GERTH: 23:49 Now, we started out by saying that people in real estate are very patient people. Do you have any lessons that you can pass on from your perspective as someone who was doing what you were doing in the '90s and in the 2000s that will calm people's nerves, or like, "Oh, no. Here's what I learned that--" and fill in the blank, that get us back to business or weathering the storm, as we're trying to?

PHILLIPS: 24:21 It will work out. [laughter] It always does. The worst recessions that we can ever imagine, it worked out.

GERTH: 24:31 What was the saying you had?

PHILLIPS: 24:31 It's hard.

GERTH: 24:32 Hold on till--

PHILLIPS: 24:34	Pardon me?
GERTH: 24:35	What was the saying you had? Hold on till--
PHILLIPS: 24:37	Stay alive till '95. [laughter] You just have to hold on and believe. Now, you can't keep doing the same old thing and thinking that it's going to-- when I say it's going to work out, I think this is perhaps one thing that people are going to have to wrap their arms around. We're never going to go back to the way it was. It's going to be different, but it's going to be good again. It will happen. You just have to have the faith that today is not the way that we're going to live for the rest of our lives.
GERTH: 25:15	That is a perfect place to end. Thank you, Georgette, for talking to us today.
PHILLIPS: 25:19	My pleasure.
GERTH: 25:20	I've been talking to Dean Georgette Phillips, the Kevin L. and Lisa A. Clayton Dean of the College of Business. She's a professor in both the Perella Department of Finance in the College of Business and the Africana Studies Program in the College of Arts and Sciences. This podcast is brought to you by ilLUminate, the Lehigh Business blog. To hear more podcasts featuring Lehigh Business thought leaders, please visit us at business.lehigh.edu/news. Follow us on Twitter @LehighBusiness. [music] Thanks for listening.