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Housing affordability - Economic feasibility - by Brett Pelletier

May 11, 2018 - Appraisal & Consulting

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Reports throughout the Boston commercial real estate markets are positive and the outlook for the year is, as ever, cautiously optimistic; nothing new there. Rents are up, pricing is up, occupancy is up, the pipeline is full, and employment is near full. The Warren Group recently reported that median sales prices of condominiums in Massachusetts increased 20% year-over-year to reach $389,000 in March, compared to that of single-family sales of $354,000. There were fewer single-family transactions year-over-year and relatively the same amount of condominium sales. That bears emphasizing in case it's not apparent that this is a strange dynamic. On average, condominiums in Massachusetts now cost more than single-family homes. There are larger detached and semi-detached condo products being delivered in the suburbs, luxury/high-rise condominiums coming on line in Boston averaging $2000-$3000 per square foot and just generally increasing pressure on housing prices and a reduction in overall housing alternatives.

Construction jobs gains in New England are outpacing the nation, non-farm job gains are softer, but their trough was shallower than the nation, unemployment in Massachusetts is hovering around 3.5%, and nearly full employment, and wage and salary growth is strong. Most sources have indicated continued increases in construction costs throughout the region and no end in sight. I won't try to quantify the impact that any trade tariffs on building materials might have, directly or indirectly, on the cost of building housing in an already high-cost market, but there's certainly a cause for concern. This is especially of concern in markets that need affordable housing and don't currently have enough, markets that don't support the economics of new construction of modest housing alternatives, and markets where alternatives are not available along a broad spectrum of price points.

On April 13th, Harvard's Joint Center for Housing Studies (JCHS) hosted a group of academics, practitioners, and innovators to ask 'How Could Changes in Design, Construction, and Regulation Reduce the Cost of Housing?' The major takeaway from those conversations was innovation. At least part of the reason that housing is so expensive is that the way housing is built today is effetely the same way it has been built for generations. And that's a problem. The materials haven't changed much and the methodologies and labor techniques haven't either. However, regulatory burdens, entitlement costs, land costs, compliance, labor supply and costs, and other development costs subject to governmental and inflationary pressure have, by a lot. Fritz Wolff of the technology-driven offsite construction company Katerra estimates that if the tech sector had experienced the same productivity losses as the building and construction industries over time, the iPhone would cost somewhere around $750,000 today. We're losing ground and it's clear there's an opportunity for innovation, growth, and thoughtfulness in the market; and one the market will likely reward.

On April 27th, Historic New England's conference entitled Preserving Affordability, Affording Preservation asked a number of the same questions. There are a lot of smart, sophisticated, thoughtful people thinking very hard about these issues. How can we observe what exists currently and craft policy and action around the problem that needs to be solved? How do we create high-quality affordable housing options for all age groups, all residents, and all income cohorts that are sustainable and responsible; and that gets the job done and will become major assets to the community.

The one topic that wasn't discussed with much granularity was the economic feasibility and financing of housing. As appraisers and valuation professionals, we have a front seat to the action. It all boils down to value. If you can create value, you can create. If you can't, the project doesn't get off the spreadsheet. For all the innovations in finance over the course of the last three decades, some good, many not-so-good, the commercial real estate capital markets haven't changed all that much in approach or application. Reducing risk, increasing sustainability and predictability of cash flows, and capturing cost savings in the underwriting is a productive step in monetizing innovation, albeit gradually. Whether incentivizing energy savings through LEED, Passive House, and Deep Energy Retrofits by underwriting some or all of the projected savings, will help deliver housing more affordably. The appraiser must understand the upside and the vulnerabilities within the underwriting model and be able to take a holistic view of the market. It's an exciting time to be in the mix and I like what I see coming down the pike. Summer is just around the corner!

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