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A real three-body problem - by Thomas House

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We are here in a mathematical distortion field at the heart of chaos theory — the three-body problem. (No, it's not a movie title pun draining the meaning from a serious computational challenge.)

The usual real estate equation is usually of the buyer-seller or supply-demand nature, a two-input binary.

Yes, there are other considerations that have long been on the periphery, but they have generally done little to meaningfully disturb this dynamic.

But with pandemic-induced inflation, this situation has changed - it is the third-body consideration that makes outcomes seem incalculable.

Records are made to be broken

The standard two-input binary looks promising at first. Interest rates have dropped below 7%, and buyers have returned to the market.

True, this is limited to only well-heeled buyers able to afford that rate, and they are shopping amid low inventory. So, for January, single-family homes in Mass. jumped more than 10% year-on-year, a record for the month.

With limited inventory, even a small contingent of buyers puts pressure on prices, especially if these buyers don't blanch at 6%-plus rates.

For Mass. particularly, unit sales are down 17%, but prices are up 5.5%.

Condo prices jumped 13%...but that was a 20% decrease year-on-year, making for a head-spinning conundrum.

The third body

When we introduce the inputs from the pandemic (higher prices, higher wages, and the wild card that may become endemic, remote work) what we see is more pressure on cities, by which we mean expensive ones. Boston particularly, because its costs include painful and expensive commutes. But renaissance cities such as Providence, Portland, Worcester to some extent feel the same pressure - a loss of in-office workers to justify office floor space.

This also reduces the desire for some to invest in the urbanist life, which almost certainly explains the 20% drop in condo returns.

The result of the remote work dimension has led to an exodus of professional workers, which may (and in an age of climate change, perhaps should) embed itself permanently in the economic landscape.

Thus, the differential real estate calculus also includes office space, particularly the sudden surfeit of thousands of square feet of it underutilized — in some cases, not utilized at all.

Boston, we have a problem
A big one.

All this portends diminishing tax revenues for cities like Boston as well as New England's second tier. This is the spring that pays for fire, police, schools, and pavement.

And lest we forget, in Boston crucially, this includes public transportation — the artery that circulates the lifeblood of Boston's professional employees. To describe these arteries as sclerotic is to understate the crisis. (And it's not just Boston: New York City is considering a local tax on self-employed individuals to pay for public transportation shortfalls).

Property taxes represent three quarters of Boston's revenue, and a diminution of returns on office space, and the economic activity a full office tower generates, generates a vacuum on a city's money supply. Unless and until a legislature or city council can (or will) approve 'new sources of revenue', it will be creative accounting until the pencils are worn down to the erasers. This is not the kind of thing that will fill a pothole.

The effect outside the Hub and New England's other hubs
The Columbia Business School notes that the shift to hybrid working has had dramatic impacts outside the cities, as suburban rents are rising alongside house prices.

An exodus of office workers and residents goes somewhere, and in a hybrid environment, that place is the suburbs. The upward pressure on prices is affecting both home prices and rents - and no surprise, affordable housing initiatives continually hit a brick wall. No one invested in their property wants to see something cheaper built three streets over, in theory reducing their investment. A home is often the largest investment a homeowner has.

But just as cities will face severe fiscal challenges in this strange new world, suburban and exurban areas will benefit.

New economic life should bloom this spring
If there is one constant in all our calculations, it's that things will change.

And one of the changes is likely to be shovels in the ground. The answer in all markets is exactly the same: the opportunity is there for development. Housing is in short supply at every turn, in every location.

This spring, in our estimation, is the perfect time to plant housing.

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