THE FRIENDLY ENEMIES

Planners can benefit developers by encouraging controls in real estate.

by Henry Hart Rice, CRE

It is time to rethink the old concept that real estate developers and planners are natural antagonists committed to destroy one another. The fact is that where developers have been unopposed, i.e., in Houston, Denver, New Orleans, they have destroyed themselves. Although the oil boom collapse was a major factor in these cities, the phenomenon of overbuilding has been repeated nationwide where planning has been lenient. The result has been office vacancies hovering around 20 percent. The healthy pockets of investment opportunities exist where planning controls and restrictions have been most severe. Nevertheless, efforts to protect the environment and the public interest have proven expensive for the consumer.

Whenever demand for real estate pushes rents up to where new construction becomes economically feasible, it is a sure bet that developers will fall all over one another trying to get into the action. Land prices will bid up, sub-contractors will have more work than they can handle and the foreseeable result will be overproduction at high prices. The outcome is weak rentals in an overly competitive market.

Restrictive zoning in a mature community plus the scarcity of urban land has kept development within viable limits in New York, San Francisco and Washington. Until very recently, Boston was another favorable rental market. Boston's vacancy rate which stood at 5.9% in 1988, the third lowest in the nation, is expected to double this year to 11.4% due to the construction of $4.1 million of new office space. Local developers, including Spaulding & Slye, Ellis & O'Connor and Cabot, Cabot & Forbes, have called on The Boston Redevelopment Authority to tighten up on its regulations. According to one firm,

> "Without the Boston Redevelopment Authority, we would have another Houston here. The soundness of Boston's market has been maintained because of barriers set by the BRA."

It is no coincidence that the cities with strong restrictive zoning have remained the strongest markets in the country. Investors in existing properties in these cities have been protected from excessive competition, and developers who successfully threaded their way through the minefields of regulations are virtually assured of success. The four cities—New York, San Francisco, Washington, D.C., Boston—commanded the highest rental rates in the nation.

Theorizing that industry locates near its most essential raw materials, it seems probable that back office operations will move to where people live. This trend for back office operations to move to the suburbs is probably irresistible. During a three year period (1985 through 1987), New Jersey, for example, built 51 million square feet of office space, whereas 17 million square feet was erected in Manhattan. The massive development in New Jersey was possible because zoning controls were widely dispersed, and each community wanted some commercial tax base. Within Manhattan tight regulations along with residential rent control severely restricted opportunity. The predictable result was that the New York buildings were absorbed at profitable rents, and many of the New Jersey developments remained vacant.

This pattern of development distribution is being repeated across the country. Suburban development outpaces the central business district. Despite strong absorption and steady growth, suburban vacancy consistently exceeds the urban center. Although long range trends favor the suburban markets, the less stringent restrictions on development are encouraging overbuilding. This pattern of growth without profit is extending to many metropolitan areas, with Phoenix as a prime example. The exact opposite is true of Toronto, which also has grown explosively but always in accordance with tight planning controls.

The economics of real estate are the same as in any other business. Prices and profits are set by the interplay of supply and demand. To the extent that supply is restricted, an artificial relative shortage is produced to the advantage of the seller and to the disadvantage of the consumer.

If developers get together and agree to limit production, their action will violate anti-trust laws. When similar limits are imposed by a community, developers and investors should appreciate the protection rather than protest. Perhaps developers and investors in existing structures should organize an annual celebration to restrict zoning and rigidly enforce planning standards.

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