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URBAN DEVELOPMENT

*An unabashed advocate of “walkable neighborhoods,” Christopher Leinberger practices as founding partner of the development firm Arcadia Land Company what he “preaches” as director of the real estate graduate program at the University of Michigan and as a visiting fellow at the Brookings Institution. Leinberger joined Robert Charles Lesser & Co., one of the first real estate consulting companies in the United States, in 1979 and bought Lesser out in 1982. He has written several books and articles on new urbanism themes, including a March 2008 article in **The Atlantic** entitled “The Next Slum?” The article identified the flaws in what he calls “the built environment” and called attention to some fundamental shifts in urban development. Leinberger spoke recently with BNA’s Richard Cowden about prospects for renewed interest by localities in “smart growth” strategies when the economy emerges from recession.*

Proponent of ‘Walkable’ Urban Areas Sees Tide Moving Away From Suburbia

Could America finally be sick of sprawl? Or maybe it’s like the weather: Everybody complains, but nobody does anything about it.

Christopher B. Leinberger, a noted real estate developer, author, researcher, and all-round land use guru, said recently the latest—and now quite dead—push into exurbia could well signal the high water mark of American residential excess.

The past decade’s housing bubble inflated at a time when the emerging paradigm of urban development espoused approaches under the rubric of the “new urbanism” such as “smart growth” and “transit-oriented development.” Predictions suggested cities would favor development that preserved land and transformed consumers’ ideas about what constitutes a desirable neighborhood. BNA asked Leinberger about the status of the anticipated shift in development patterns.

BNA: A few years ago everybody was saying everything is going to change to smart growth and more compact development. Yet in this latest go-round, there was

a good deal of not only suburban development or exurban development, but exurban development on steroids. How did that happen?

Leinberger: Actually, I don’t think it was people saying there is a market for smart growth; it was people promoting smart growth over conventional development, wishing that it would change. I don’t think anybody I’ve heard saying smart growth is what you should expect in the first decade of the 21st century. What I do know is that most of the [chief executive officers] of many major development organizations that are engaged in commercial and residential development on a national, even international level, will tell you the age of unmitigated, low-density sprawl is over. What this last decade has showed is, in essence, the last gasp of low-density development. It took place because we in real estate got really good at building low-density development. Wall Street got really good at financing it. It’s legal to do . . . And it’s also significantly subsidized, so what’s not to like? If the easiest thing to do is conven-

tional development, and it's legal, and everything else isn't, why not do it? Why it was on steroids was because we didn't know much else to do.

Housing Market Meltdown. But that was then, before 2007, when it all began to unravel. Housing starts plummeted from more than 2 million total units in 2006 to a rate that has hovered around 500,000 for this year. The inventory of unsold homes has declined from highs that exceeded 4.5 million in mid-2008 to about 3.6 million in September of this year, but even at the more recent levels, the country has a 7.8-month supply of unsold homes.

Leinberger acknowledged that the collapse of new home sales, particularly in the suburbs, has been much more dramatic than it was during other housing market slumps.

"This is not a cyclical downturn in real estate," Leinberger said. "This is a structural change in how we build the built environment. I liken it to a pendulum that was pushed all the way to one side . . ." which is the traditional approach to development that he has labeled "drivable suburbs." At the opposite end are "walkable urban places," which he regards as the direction in which the pendulum will swing now.

Leinberger qualified that prediction, noting that, "I'm not saying that the pendulum is going to swing all the way back to the other side because there certainly is a definite and significant market for drivable suburban development. It's just that we happen to have overbuilt it and we've structurally overbuilt it, not cyclically."

Certainly the same forces that have always been at work in real estate development played out during the latest boom, and the current oversupply of homes at the urban fringes eventually will be absorbed by the marketplace this time too, Leinberger said. However, following the boom-and-bust cycles of the latter 20th century, the industry eventually recovered and proceeded apace.

"But that ain't gonna happen this time," Leinberger said. "At least that's my impression, based on the numbers I'm looking at and based upon the underlying demographics going forward."

Recent reports document instances of newly built neighborhoods with lavish, unsold homes that have been boarded up; in some cases groups of squatters have moved into homes designed as single-family residences. Certainly the latest crop of large-lot exurban housing, often characterized as McMansions, eventually will reach a clearing price, Leinberger said.

"Where the market price is below replacement cost, it will stay below replacement cost in certain suburbs," Leinberger said.

What's Next? Leinberger is hardly the only urban expert to criticize suburbanization or to have a vision for better ways to plan and build the next generation of communities. But he brings to the discussion his own experience as a developer who has few illusions about the games localities and special interest groups play during the process.

Due to backlashes against property taxes, such as the Proposition 13 movement in California, Leinberger said, many jurisdictions sought to better understand the costs of development and internalize those costs in the projects themselves through impositions of impact fees.

"That was an attempt to begin to make development pay for itself, but still in no way would it pay for itself,

especially over the long run," Leinberger said. "Basically, development over the last 50 years has been sort of a Ponzi scheme. New development generates up-front monies. It depends on the jurisdiction—each jurisdiction has a different tax regime. It could be sales taxes on the acquisition of construction goods. It could be the income tax on the part of the workers on the site. It could be building permit fees. But those are up-front, one-time things. They then have to maintain that property over a long period of time, and the property taxes that were levied on the homeowners in no way made up for the gap."

Many communities have come to understand the weaknesses of this "more-is-less" approach to development and yet appear addicted to it, Leinberger said, adding, "it is especially true for bedroom communities, which have no other way of raising money. Every time I'm talking to a city manager or a mayor, the first thing I want to understand is, 'What is your tax regime? How do you make a buck as a city?'"

Drivable suburbs may seek to earn the bulk of their revenues from commercial space users, thereby subsidizing homeowners who, after all, make up the electorate. Ultimately, many of these schemes have proven unsustainable, Leinberger said.

Although shifting to development models that result in a higher tax revenue return for each unit of land appears an obvious choice for municipal governments, getting a community buy-in may not be that easy. In addition to short-sighted policies for managing the cost of cities, local perceptions about development often militate against sound land use decision making.

BNA: When someone brings a development proposal to a planning commission or zoning body that envisions high-density properties, they are much more likely to get rejected than someone who proposes building one house for every 10 acres. That seems to turn good environmental planning on its head because people don't want to look at tall buildings. Can anything be done about that or are developers going to have more confrontations with that point of view in the aftermath of the latest boom and bust? Now people are going to be looking at abandoned McMansions because they allowed this to run rampant, right?

Leinberger: Yes, you certainly see it the way that I see it. NIMBY [not in my back yard] opposition is probably the number one issue we have to contend with to develop what the market wants and what the environment demands. But we have seen many ways to address NIMBY opposition. For one thing, we see that there is a convergence of market desires with environmental necessity. This has not been the case up until now. The two went in opposite directions over the last 50 years.

You can look at lots of market surveys and see a lot of evidence of this, but the real evidence of this is that walkable [developments] in high-density locations have, generally speaking, maintained their value. Maybe they've dropped 5 to 10 percent, but they basically went flat. And the vast majority of property price declines have been in drivable-only, low-density housing. And that's the market yelling and screaming in our ear.

I was just on the phone with a developer this morning who is a far-out fringe suburban developer and he's seen land values that are negative. You'd basically have to be subsidized, just like 30 years ago you'd have to be subsidized to do anything in the city. Now you have to

be equally subsidized to do sprawl, low-density development on the fringe.

Environmental Considerations. Among the factors that are likely to counter NIMBY opposition in the coming years, Leinberger said, are environmental considerations. Until now groups with concerns about energy consumption and detrimental land uses have not spoken out enough about the need to take smart growth issues seriously, he said.

“Many environmentalists now understand that they can’t just say no to new development without also saying yes to walkable, transit-oriented development,” Leinberger said, adding that he had recently spoken with representatives of a major international environmental organization “about the need for environmentalists to go onto the barricades and say to regional bodies and maybe, if they have membership organizations, go to planning councils and say, ‘Do you want to maintain the status quo in your little downtown, or save the planet? Your choice.’”

But perhaps an even more powerful force in convincing localities to support development of walkable neighborhoods will be the economic interests of individual families, Leinberger said.

New Interest in Higher Density. Although smart growth remains more a goal than a reality in many areas, Leinberger says he can point to examples that demonstrate it can be both feasible and popular among nearby residents.

Leinberger highlighted the experience of Tyson’s Corner, a burgeoning development node in Northern Virginia on the Capital Beltway that is already the largest suburban downtown in the United States. A coalition of neighborhood organizations in the area recently agreed to an increase in the development density of the site from its current 44 million square feet to 100 million square feet.

The coalition acted in concert “with the landowners and developers to work with the county supervisors to allow that to happen,” Leinberger said, noting that they had been influenced by other walkable neighborhoods that have emerged along the Metro line in nearby suburban Washington communities.

“They wanted to live near something like that too,” Leinberger said. “And they understood that the way to decrease traffic congestion and increase quality of life and walkability was by having more development, not less.”

In another example in the Washington, D.C., area, Leinberger met recently with local officials in Montgomery County, Maryland, along with several White Flint Mall area developers who represent about 70 percent of the local land ownership. Also around the table were representatives of five neighborhood groups.

“And I thought, oh, no, not another battle,” Leinberger said.

Instead, Leinberger found the neighborhood advocates pressing the county executive “saying, ‘You must allow higher density. We want our kids to be able to walk to a great downtown, to be able to ride their bikes. We want three times the density that’s there now.’”

In this case, it was the county executive who was “pushing back,” Leinberger said.

“As I told them, ‘Look, guys, you’ve got a drivable suburban mentality that you’ve got to overcome. With

drivable suburban, you get less quality of life,” Leinberger said.

“Walkable urban development works under the principle of more is better,” Leinberger said. “As you build more, you get a better quality of life. That next restaurant; the rental apartment you add into a high-density, walkable place puts more people on the street. It means there’s more retail options; you’re safer.”

Other compelling reasons for those living in close proximity to transit hubs to support high-density development, Leinberger said, are the effect it has on property values and on local government revenues.

“What we’re now seeing over the last 10 to 15 years is that property values [near transit-oriented developments] skyrocket and for that matter property taxes skyrocket . . . It’s what I refer to as an upward spiral of value creation that occurs due to walkable urban development. But the NIMBYs are fighting the last war; they still have in their heads . . . ‘more is less.’”

BNA: They seem to ignore that you can’t really contain overall demand for housing. If you could somehow suppress the demand, that might work, but if the demand for housing continues to grow, it’s simply going to go somewhere else if it doesn’t go in your neighborhood, right?

Leinberger: Well, that’s certainly been the American way of dealing with things for the last 50 years and it’s led us to a very sad point in our country’s history. The more-is-less principle has led us to become an exclusionary society. ‘If we can just get away from those people, we’ll have better schools, higher property values. We’ll have the quality of life we were promised in the suburbs; just get us away from those people. Zone them out of our lives.’”

The Benevolent Recession. Leinberger acknowledged the pain that the recession has inflicted on families and communities, but his vision focuses beyond the current downturn to the next growth cycle. “I personally think recessions are very positive for the economy—they’re painful but positive,” he said. “They force everybody to reconsider everything they’re doing . . . This ‘Great Recession’ in particular has just been intriguing to watch—this price collapse on the fringe.”

As suburban Virginia residential prices have corrected in recent months, Leinberger said, they have slumped to \$100 to \$125 per square foot, “well below replacement cost.” That contrasts with prices in some Washington, D.C., neighborhoods, which even at this point in the recession range from \$500 to \$700 per square foot.

“Thirty years ago, that relationship was reversed,” Leinberger said. “That’s the market telling us something very significant.”

BNA: We’re becoming Europe.

Leinberger: Yes, exactly. Unfortunately, we don’t have enough walkable urban product. That’s what’s driving this. And where it shows up is in land prices . . . Land values, of course, are the most extreme way that you can measure urban economic cycles because all value puddles in land. That’s why there’s a thing called residual land value analysis. So, 70 percent of profit made in real estate is made on land and virtually all value puddles in land because sticks and bricks are fungible.

It costs so much to build a building, whether it be out of steel or reinforced concrete or stick and all value is

in the land. And walkable urban land is at \$400, \$500, \$600, \$700 a square foot because there's a shortage of it. But there's no shortage of land; there's just a short-

age of places that are walkable, urban, safe, vital places. The market wants it; it's our challenge as an industry to give the market what it wants.