

What Happens When We Build Too Much Space?

*Kirk McClure
Professor of Urban Planning
University of Kansas*

Too many communities confuse growth of supply with growth in demand. This confusion causes communities to favor any proposal from developers to build new buildings. Communities need to guard against this confusion because it can be very harmful to the existing stock of real estate.

This confusion is often made when communities incorrectly believe that allowing a developer to build a project is the same as economic development; it is not. Economic development means expanding the base of jobs and/or the wages levels in the community.¹ Economic development is the expansion of demand. As the base of income grows in the community, the demand for real estate will grow. Unfortunately, the reverse is not true. As the supply of real estate developments grows, the demand for that space will not necessarily grow. The available demand will simply be spread across more space, weakening the level of demand for all space.

The demand for retail space

Retail development provides the easiest example to understand. The demand for retail space is a function of the size of the population in the community served by the retail space, the income of this population, and the propensity of this population to allocate income to retail goods and services. The size of the population and its income are relatively easy to calculate; the Census Bureau provides these numbers.² The propensity to spend this income on retail depends upon the makeup of the population. A younger population will spend more on retail goods and service while an older population will spend less.

All too often, developers make great promises when they propose to build new retail space. The developers promise new jobs, new taxes, and new economic vitality. These are usually false promises.

The number of stores does not drive the system. Building more stores does not create more people. It does not create more income. It does not change the propensity of the population to allocate its income to retail goods and services.

In the short run, there will seem to be new activity as the new store or stores open, but most likely, the aggregate amount of spending in the community has not changed. The spending has simply moved from existing stores to the new ones. This means that there will be the same amount of spending spread across a larger amount of supply. Unless there was a shortage of stores, which is very rare, this means lower spending per square foot. When this falls too low, some stores will fail. Commonly, the older stores are least able to withstand the loss of revenue, and they fail. The new stores simply capture the spending, taking it away from the existing stores.

The new store will hire workers, and in the short run this will appear to add jobs. But in a relatively short amount of time, jobs will be lost at some of the older retail stores as they go out of business. The number of jobs in a retail market is a function of the amount of spending in the market. Adding new stores does not add jobs in the long run.

The new stores will report paying new sales taxes, but the taxes are not really new. Sales tax dollars are paid by the customer and the amount of sales tax dollars are a function of the total spending, not the number of stores or the size of the stores. In the long run, the sales taxes will continue to rise and fall with the changes in the size of the population and its income.

The new stores will pay new property taxes to the community, which will be welcomed. This will, in the short run, be a gain to the community as the older stores will continue to pay their sales taxes as well. However, in the long run, the gain will be reduced or wiped out by the loss in value to older properties that become vacant and less valuable.

There is no new economic vitality with the addition of stores. Only growth in population and growth in its income generates new economic vitality. Communities should not be fooled into thinking that new supply will add to the economic vitality. New stores do not mean more income; too often they mean greater vacancy and blight in the older parts of town.³

The demand for housing

The lessons from retail can be transferred to other sectors of real estate, such as housing.

Adding new homes is not always a good thing. It is nearly always helpful for neighborhoods to attract new investment to fix up older homes and to infill vacant lots. New subdivisions can also add needed new housing if there is population growth to support this new stock of housing. If however, the pace of growth in housing outpaces the pace of growth of the population, then the older stock of housing will suffer.

Neighborhoods tend to be built during a relatively short period of time, thus the housing tends to be of about the same age. This means that the housing units will all age together. As neighborhoods age, the homes need periodic reinvestment.⁴ It is important that a community help aging neighborhoods attract this investment. Frequently through overbuilding, communities inadvertently encourage people to abandon these older neighborhoods and move to new subdivisions. If a community allows new housing subdivisions to be built at a pace that adds housing units faster than the pace of growth of population, then it will encourage this harmful disinvestment and out-migration from older neighborhoods.

What may appear to be a new and helpful addition to the housing stock may actually be harmful. A new subdivision adding surplus units may accelerate the deterioration of an existing neighborhood.

Conclusion

Whether it is retail space or housing units, industrial space or office space, a community needs to keep the supply of that space in balance with the demand for that space. If the community allows the supply of space to grow too fast, then the existing stock of space is harmed. The developers of the new space make money building and selling this new product; thus, they are in favor of the development. But the community should look to the long-term consequences to this growth. It is in the community's interest to resist excessive development and maintain a balance between the pace of growth in demand for space and the pace of growth in the supply of that space.

Notes:

1. Blakely, Edward J. and Ted K. Bradshaw. 2002. *Planning Local Economic Development: Theory and Practice (3rd ed.)*. Thousand Oaks (CA): Sage Publications
2. McClure, Kirk. 2002. "Monitoring Retail, Office and Industrial Markets," in *Land Market Monitoring for Smart Urban Growth*, Gerrit Knaap, editor, Cambridge, Massachusetts: Lincoln Land Institute.
3. McClure, Kirk. 2001. "Managing the Growth of Retail Space: Retail Market Dynamics in Lawrence, Kansas," in *Downtowns: Revitalizing the Centers of Small Urban Communities*, Michael Burayidi, editor, Boston, MA: Irwin McGraw-Hill.
4. Downs, Anthony. 1981. *Neighborhoods and Urban Development*. Washington, D.C.: The Brookings Institution.