Never Underestimate the Housing Multiplier Effect

Housing Is Good for the Broader Economy In Many Ways

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Simply stated, a multiplier effect occurs when one person's spending becomes another person's income. That income is subsequently spent becoming the income of a third person and so on. Multiplier effects are created at virtually every level in the economy. When new jobs are created, those persons spend, thus generating more income followed by more spending followed by more spending, more income and more jobs. That helps explain why job creation and resultant spending are enormously important to local economies as well as the broader economy.

A home purchase always has a ripple or "multiplier effect" in the economy. In other words, for each dollar that is spent, there is an additional amount spent over and above the initial investment that ripples through the economy. Multipliers take many forms but in housing, economists attempt to quantify three fundamental things: **jobs, spending and tax revenues.** Housing multiplier impacts tend to occur in two phases. The first is when the house is constructed and the second is throughout occupancy. While growth critics sometimes opine that housing doesn't pay its fair share, the reality is it almost always does, and then some, except perhaps in times of severe recession.

An existing home sale produces a multiplier effect but certainly not as great as when a new home is constructed and sold. The first impacts in new home construction occur when the home is built. There is spending on the workers who build the homes as well as by the firms that support them. There are usually office staff, cost estimators, buyers accountants and more. This first layer of impact is referred to as *"direct impact."* In addition to the direct impact of home construction, there are the ripple effects; those that ripple through the local economy in some form or another. Generally two forms are measured. One is the *"indirect impact"* which is typically the jobs and spending created from businesses that are suppliers to the construction operation. This impact might include building supplies, architectural and engineering spending, cabinetry, flooring , decorating, landscaping, financing and much more.

Finally there is "*induced impact."* It occurs when workers spend their wages in the local area such as at restaurants, retail, healthcare, services and other establishments. The induced spending tends to create additional new jobs at these consumer related businesses as well. While a sale and purchase of an existing home has a multiplier effect in the form of spending on remodeling, furniture, appliances and, of course, the community tax base, the impact of new construction is even larger due to construction and the jobs it creates plus its addition to the tax base and many impacts, too many to mention here. We witnessed a powerful *negative* multiplier effect with the great recession. As housing collapsed, jobs were lost in construction, sales, financing and many other areas. Those losses reduced spending and led to job losses and then reduced spending in other sectors as the recession rippled through the economy.

A robust housing market leads directly to growth in the commercial real estate sector as well. Builders, developers, suppliers, sales agents all need office space. As homes become occupied, residents need a wide range of support services. They need places to shop, bank, to receive healthcare, obtain services and more. The multiplier effect is powerful and nearly endless. The Great Recession was unusual in that commercial development, which should *follow* residential development, actually got ahead of it. Commercial developers and builders sought to be there when residential development arrived. As we now know, the housing market collapsed and many new homeowners never arrived. The commercial sector collapsed 18 months or so later.

Today, the housing market is rebounding. The multiplier effect will be profoundly positive and its effect will be felt in the commercial real estate markets as old inventory is absorbed and demand for more space emerges. Never underestimate the reach of the multiplier effect, either on the way up or down.

The Ripple Effect

The housing rebound began to show up in allied industries in the fourth quarter of 2012. Not only did construction employment and new residential construction rise but sales of products such as heating and air conditioning systems, power tools, remodeling, carpet and flooring did as well. Moving those goods also had a positive impact on transportation and warehousing as well.

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