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The U.S. and World Economic Geography Before and After the Downturn: Conference Summary

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This conference examined how the recent economic crisis has changed residential and development environments in many parts of the world. For example, the crisis has reduced home ownership and created pressure to increase neighborhood density in the United States. And, at least temporarily, it slowed migration in China to export-oriented urban areas.

The conference was sponsored by the Center for the Study of Innovation and Productivity and was held at the Federal Reserve Bank of San Francisco November 18, 2009.

At the conference, four leading experts on economic geography and urban economics gave talks spanning a wide set of economic geography topics that are relevant in the aftermath of the recent economic crisis. These included the outlook for urban structure in the United States in the wake of the housing downturn, urban policy changes in the United Kingdom, how the geography of China's economic development may have been affected by the global downturn, and the widespread trend toward "green" construction in the face of global warming.

Cities and the housing crisis

Most analysts point to the dramatic correction in house prices starting in 2006 as the catalyst for the wider financial and economic crises that followed. Jan Brueckner of the University of California, Irvine, an expert in urban and real estate economics, looked at what the housing correction means for the future of residential investment, home ownership, and broad trends in economic geography. He focused on possible short- to long-run ramifications of the housing "debacle" on the economic geography of the United States. In particular, he considered the potential effects of the crisis on the location and quantity of residential investment, the social capital of neighborhood life, and intra-national migration patterns.

Brueckner speculated that the large fall in house prices may have caused households to rethink the riskiness of homeownership as an investment. The increase in the perceived risk of owning a home could lead to a permanently lower rate of homeownership, as well as a shift in preferences toward smaller, less expensive houses. These effects, in turn, could have an impact on the geography

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of the nation's housing sector. In particular, shifts toward renting instead of owning and toward smaller homes for those who do own could lead to denser, more compact cities and slow or reverse urban sprawl.

Although some would welcome a reduction in urban sprawl, the social capital of existing neighborhoods—i.e., the value generated by social networks and relationships formed within a community—could be a casualty of the housing crash, according to Brueckner. The enormous loss of housing equity across the nation is forcing many people to uproot themselves and their families, severing bonds with their communities. Secondly, a decline in homeownership rates implies fewer households are firmly planted in their communities. A large volume of social science literature documents that, compared with nonowners, homeowners are more likely to invest in the social capital of the community by voting, participating in community organizations, maintaining their property, becoming active in local schools, and similar acts of social solidarity. To the extent that renters replace owners, the production of social capital could fall.

Potential shifts toward owning smaller homes or renting, however, are likely to be longer-term trends. In the short run, the decline in housing equity may "lock in" households. That is, many households may be unable to move because the market value of their house is below what they owe on their mortgage. Alternatively, their equity may be too small to afford a down payment on a new house, especially given higher down payment requirements these days. This lock-in and a subsequent drop in intra-national migration could hamper the job-matching process, whereby job seekers in depressed areas move to areas where job openings are more abundant. Such job matching is an important dynamic helping to pull economies out of recession.

Lessons from across the pond

Of course, the United States was not alone in experiencing a housing crash that triggered financial and economic crises. Along with other countries, the United Kingdom suffered in many of the same ways. Henry Overman of the London School of Economics discussed how the economic downturn has varied geographically within Britain and how this has affected urban policy. Overman pointed out that, early in the recession, many observers assumed that London and the south of England would suffer disproportionately due to the importance of the financial sector in that region. However, it turned out that the manufacturing-intensive north saw the largest drop-off in economic activity.

Local governments in the hardest-hit areas have responded in different ways, according to Overman. Some have sought to help small businesses obtain loans. Others have increased grants and incentives targeted at such activities as research and development. Still others have tried to create jobs and attract future businesses by initiating large infrastructure projects. Overman argued that local government stimulus is likely to be less effective than national monetary and fiscal support for several reasons: Local policy often is slow-moving. It can end up siphoning off economic activity from surrounding areas. And "leakage" can occur when local government spending goes to out-of-the-area recipients. He recommended that local governments instead focus on helping individuals and families weather the downturn by providing advice and small-scale housing assistance. He also encouraged cities to reconsider restrictive land use policies which have contributed to the tremendous volatility that has characterized British residential and commercial real estate prices in recent decades.

The current downturn has increased calls for national government policies aimed at closing the gaps between rich and poor areas of Great Britain. Overman argued that, in the past, many such policies have been ineffective or have actually worsened such gaps. Policies should instead focus on aiding poor *people* rather than poor *areas*, which would allow market forces to determine the most efficient geographic distribution of economic activity, he concluded.

China and the geography of economic development

The rapid economic growth in China and other emerging markets has led to enormous geographic reallocations of population and production. J. Vernon Henderson of Brown University documented the major shifts in urbanization in China over past three decades, especially the mass migration from rural areas to cities. Despite the vast movement of population, China by many measures remains too rural. For example, based on GDP per capita and the cross-country relationship between per capita GDP and the urban share of the population, China should have a 55% urban share instead of its actual 46% share. Moreover, Henderson's research has shown that China's urban population is less urban than urban populations in other countries. The majority of China's population living in cities with over 100,000 people lives in small cities of less than one million people. Less than 4% live in megacities of more than 12 million. In the rest of the world, a little over a third of the urban population lives in small cities and nearly 10% live in megacities. Henderson estimated that China's output per worker would increase significantly if the urban population were concentrated in larger cities.

One reason why China has not urbanized more quickly is that intra-national migration is severely restricted by the government, Henderson noted. These restrictions prevent rural people from permanently relocating to the cities where jobs are more abundant. Nonetheless, an enormous number of migrants appear to have moved despite the restrictions. The global downturn weakened China's export sector and may have stemmed the tide of urban migration. But China's exports have rebounded and this has led to a revival of labor demand in Chinese cities, spurring renewed migration from rural areas, Henderson concluded.

Going green while in the red

One longer-run trend affecting economic geography in the U.S. and globally is climate change. The recent recession probably had little impact on the underlying warming trend, but recessions often push businesses and households to redouble their efforts to control costs. Faced with the prospects of rising temperatures, commercial and residential property owners in many regions may have accelerated a trend already under way toward making homes and buildings more "green" or energy-efficient. John Quigley of the University of California, Berkeley, examined the extent to which the greening of buildings is being capitalized in rents and sale prices.

Quigley noted that commercial buildings account for a large share of energy costs in the United States and that energy expenditures represent a significant part of the total occupancy costs of buildings. Increasing public pressure on commercial property owners to help reduce energy consumption and carbon emissions has accelerated a trend toward building and marketing so-called "green" buildings. Property owners and developers value a green rating from such certification programs as EnergyStar and LEED. They say they may be able to command higher rents, stemming in part from the ability of tenants to market themselves as environmentally sensitive. They may also get higher sale prices because green buildings have lower energy and maintenance costs.

Quigley and fellow researchers have attempted to estimate what rental and sales-price premiums green-rated buildings get. They compared prices of green buildings with other comparable structures located nearby in cities across the United States. They found that, all else equal, green buildings fetch 2–3% higher rents and 16–17% higher prices than similar non-green buildings. Quigley concluded that these premiums primarily reflect real energy cost savings and are not due merely to the cachet of the green label.

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Conference presentations

Brueckner, Jan. “Cities and the Housing Debacle.”

Henderson, Vernon. “The Geography of Development in Emerging Market Countries: The Case of China”

Overman, Henry. “Lessons from Across the Pond: U.K. Urban Policy and the Downturn.”

Quigley, John. “Green Hype? Green Cities, Green Buildings.”

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