Responding to Urban Decline

By Santiago Pinto and Tim Sablik

In recent decades, a number of once-prominent U.S. cities have experienced economic hardship and significant population loss. Policymakers in those cities want to jump-start growth and improve prospects for the people who live there. But where should they begin? This *Economic Brief* surveys economic studies on a variety of urban policy interventions and provides lessons for policymakers.

Over the past two centuries, the population of the United States has become increasingly concentrated in cities. In the 1800s, only 6 percent of people lived in urban areas. Today, nearly two-thirds of Americans live in cities.[1] Not only is the U.S. population concentrated in cities, the nation's economic activity is as well. Large cities accounted for roughly 85 percent of the country's gross domestic product (GDP) in 2010.[2] Concentrating economic activity in this way produces a number of benefits. Places with higher population density exhibit faster growth in productivity and per capita GDP. Cities are also wellsprings of innovation, accounting for a disproportionate share of new patents.[3]

These benefits make it all the more puzzling that a number of prominent U.S. cities have experienced large population declines in recent decades. St. Louis, Detroit, Cleveland, and Pittsburgh, for example, each lost half or more of their populations between 1950 and 2010. Others, such as Baltimore, Chicago, and Minneapolis, suffered smaller, though still substantial, population losses during the same period.

If these changes merely reflected shifts in population from one city to a more desirable or more productive city, there wouldn't necessarily be any cause for concern. However, evidence suggests that urban population outflows have hurt some lower-income people who have been left behind. Declining city centers frequently exhibit high and persistent poverty rates. For instance, in Detroit and Cleveland, 40.3 percent and 36.2 percent of the population, respectively, were below the poverty line in 2015. Meanwhile, the average incomes of the surrounding suburbs have risen.[4] In fact, the metropolitan statistical areas (MSAs) surrounding many declining cities have grown in population since 1950. For example, the Detroit and Baltimore MSAs each added more than 1 million people between 1950 and 2010.[5] As city centers decline, those people and firms who can leave do, and those who cannot (frequently low-income, low-skilled households) are stuck with dimming economic prospects.

Urban policymakers in declining cities justifiably seek to revitalize their cities and help the people who live there. To do so effectively, it is important to understand what factors lead cities to decline and to examine a variety of urban renewal policies.[6]

The Lifecycle of Cities

Some cities may decline due to the natural aging of infrastructure. When a city is new, buildings near the center are the most desirable and tend to be occupied by a mix of firms and wealthier households. But as those buildings age and deteriorate, those households move to newer developments surrounding the city, leaving behind lower-income households. This process can repeat multiple times, pushing the city border outward as higher-income households retreat to the newest ring of development. Eventually, deteriorated buildings in the city center are redeveloped, once again attracting higher-income households back to the city and starting the cycle anew. This cycle can be seen in cities such as Chicago and Philadelphia.[7]

Because buildings are durable goods, it can take a long time for a city to move through its lifecycle. When a city's population is growing, it is profitable to construct new housing because demand and prices for housing are rising, and the city expands rapidly. But when the population declines, existing housing stock doesn't simply disappear. It can take decades before it is profitable to refurbish or replace a building. The surplus of housing depresses house prices below the cost of construction, and the city stops growing.[8] Moreover, falling rents may draw lower-skilled and lower-income households into the city, intensifying urban sorting by income.

In addition to natural aging, cities experience shocks that alter their composition of firms or people. These shocks can be positive or negative. Cities such as San Francisco, Washington, D.C., New York, and Cleveland, for example, appear to have experienced fairly rapid changes in firm composition. Greater automation at major employers might lead to population losses as local firms demand less labor. This can result in a city with a thriving downtown but a surrounding residential area that is too large for its current population, as seen in Detroit and other manufacturing cities in the Rust Belt.[9] Urban policymakers faced with either a sudden shock or a steady decline have a natural inclination to revitalize their cities. But should they intervene? And if so, how?

Types of Policy Responses

Different wages and housing costs within cities do not necessarily demand a policy response to correct. Some households may voluntarily decide to reside at distant locations despite higher commuting costs because housing prices are lower. Wages and housing prices can also differ between cities for a variety of reasons, such as availability of amenities. These differences don't necessarily justify policy intervention either. However, should policymakers choose to act, economic theory suggests that interventions can have wide-ranging effects in the context of cities.[10]

Cities are built on the powerful economic forces generated by firms and people coming together in one place. Higher concentrations of people and firms have positive effects on almost everyone living in a city. Higher population density means greater learning and sharing of knowledge, more productive firms and workers, and more efficient supply lines and labor matching. Economists call these forces agglomeration economies. Of course, cities do not grow indefinitely because higher concentrations of people and firms are also associated with negative effects, such as traffic congestion and pollution, that may eventually outweigh the benefits.

Investments in a declining city may well "jump-start" positive agglomeration forces in ways that could have benefits that outweigh their costs. In theory, even an announcement that a neighborhood will be revitalized could by itself trigger a variety of positive effects before the government spends any money.[11]

Once policymakers decide to intervene, there are two main types of approaches to consider. One option is to focus on helping households by giving them the tools to improve their situation. This could involve removing barriers that prevent households from relocating to thriving parts of the city, providing housing vouchers to help them move, or improving and expanding transportation networks to reduce commuting costs. An alternative approach is to focus on revitalizing the city itself. This includes reconstructing residential or commercial buildings that have declined or offering incentives to employers to move to the city and hire local people. Economists have labeled these different approaches "people-based" and "place-based" policies, respectively.

Revitalizing Places

Place-based interventions are the most common and widely studied types of urban policies. A good example is the Enterprise Zone (EZ). EZs attempt to revitalize areas by attracting new businesses through tax credits or providing grants for development projects. EZs have been implemented at both the state and federal level. Connecticut established the first state-based EZ in 1982, and forty states had some type of EZ by 2008. At the federal level, Empowerment Zones (which are similar to EZs on the state level) were used from 1993 to the mid-to-late 2000s.[12]

Investment in EZs has been substantial, but measuring their impact has been challenging. One problem is that targeted areas often don't align neatly with census tracts, zip codes, or other standard geographical boundaries used for collecting data. Another challenge is controlling for other factors that influence local economic conditions and finding appropriate control cases for comparison. A third difficulty is that any benefits attributed to the EZ may come at a cost to other regions. For example, persuading a business to relocate from one city to another city benefits the latter at the expense of the former. On the other hand, promoting development in one part of the city may spur private investment that benefits nearby, nontargeted areas. Any empirical study looking to measure the benefits of these programs must account for these positive and negative spillover effects.

Given these challenges, it is not surprising that studies have found mixed effects from state and federal EZ programs. At the state level, an examination of California's EZ program found no evidence of a significant impact on employment, while an analysis of Texas's EZs found a positive effect, particularly in lower-paying industries.[13] At the federal level, some studies have found positive, statistically significant effects on employment and wages from Empowerment Zones.[14] On the other hand, there is also evidence of significantly negative spillover effects on areas geographically near or economically similar to the Empowerment Zones, suggesting that at least some of the "gains" may simply be shifted economic activity.[15]

Other place-based urban policies focus on improving residential buildings and infrastructure. Examples of federal urban renewal programs include the Housing Act of 1949, which provided loans to cities to acquire and redevelop decaying neighborhoods, and the Model Cities Program of the 1960s, which focused more on renewal of neighborhoods rather than wholesale reconstruction. Evidence on the impact of these projects is also inconclusive. Studies don't suggest they had a meaningful impact on population growth or per capita income, but that may be due to their relatively limited funding.[16] Urban renewal projects do seem to generate higher land values—even in nearby neighborhoods not directly targeted, as found in one study of the Neighborhoods-in-Bloom program in Richmond, Virginia.[17] One of the main findings of that study is that after accounting for all the external effects generated by this kind of program, the overall benefits may more than compensate for the costs of implementation.

But to the extent that urban renewal programs generate higher land values, many of the benefits may accrue to landowners rather than low-income households if those households are mostly renters. For example, one study of the federal Empowerment Zone program found that it had no effect on poverty and employment for residents but a large effect on property prices.[18] Successful urban renewal projects also may end up displacing those households if neighborhoods become more desirable because of new construction.[19] An influx of higher-income households may bid up rents and price out the low-income households the renewal projects were intended to help.

Investing in People

Place-based policies are not the only way to improve the welfare of households living in declining cities. To the extent that those households are constrained from leaving and seeking better opportunities, policymakers may be able to help.

In the mid-1990s, the U.S. Department of Housing and Urban Development took this approach with the Moving to Opportunity (MTO) program. The program was implemented in five cities—Baltimore, Boston, Chicago, Los Angeles, and New York—and it provided housing vouchers to families living in high-poverty neighborhoods to help them move to low-poverty neighborhoods. While participation in the program was voluntary, the eligible applicants who received vouchers were chosen randomly, making it a good case study of this policy approach. Some households (the treatment group) received housing vouchers that could only be used in census tracts with poverty rates below 10 percent; others received vouchers with no geographical restrictions (Section 8 vouchers); and the control group received no vouchers and continued receiving public assistance.

Some research has found that for adults, the program seems to have had no lasting effect on earnings or economic self-sufficiency.[20] Moreover, of the households offered a voucher to move to lower-poverty neighborhoods, less than half accepted, and some that did move later moved back.[21] For children, the evidence was mixed. Those who were younger than thirteen when they moved to a lower-poverty area seemed to benefit. Compared with children in the control group, they had incomes that were about $3,500 (31 percent) higher on average in their mid-twenties, were more likely to attend college, and were less likely to become single parents. On the other hand, children who were older than thirteen when they moved suffered worse long-term outcomes, possibly because they already had established social networks in their old neighborhoods and disrupting those networks caused more harm than good.[22]

More recent research examines the outcomes of similar housing voucher programs and finds more favorable evidence of this type of policy. From a research standpoint, the fact that participation in the MTO experiment and the use of the housing vouchers was voluntary introduces potential self-selection bias into the results of the experiment. Some children who could have benefited from the relocation to a low-poverty neighborhood did not participate in the program because their parents were not motivated to move. To overcome this problem, one study focuses on the outcomes of a specific program that involved the mandatory relocation of households to other neighborhoods because the public housing where they lived was set to be demolished. This study concludes that the relocation of households had large and positive effects on children (they were more likely to be employed and earned higher wages as adults), and these effects were substantially larger than those found in the MTO experiment. This suggests that the children who did not participate in the MTO experiment were very likely those who could have benefited most.[23]

Rather than attempting to move residents to more prosperous areas, another people-based approach is to improve residents' human capital. Certainly, investing in education and human capital has benefits on the individual level. But having a more educated, more productive urban population has positive spillover effects on the city as a whole, too. In fact, these spillover effects seem to play a key role in defining modern successful cities. In the early post-World War II era, city growth was tied to high concentrations of physical capital, like the car factories of Detroit or the steel mills of Pittsburgh. But since 1980, human capital has become a more reliable indicator of a thriving city. Average wages in cities with highly educated populations, such as Boston or San Francisco, are much higher for both college graduates and high school graduates than in cities with low levels of college education.[24]

There may be other spillover benefits as well. Individuals with more education are significantly less likely to commit crimes. Thus, increasing high school graduation rates (for men in particular) seems to provide substantial social savings to cities in the form of less crime.[25] Raising human capital levels and the number of high-skilled jobs in a city also has a multiplier effect. One study found that for each new job in an innovative field added to a city, five additional jobs were created. This includes high-skilled jobs (such as lawyers, teachers, or nurses) and lower-skilled jobs (such as waiters, baristas, or taxi drivers).[26]

Cities with higher levels of human capital also tend to attract more individuals with high levels of human capital, creating clusters of innovation, such as Silicon Valley near San Jose or the Research Triangle in Raleigh, Durham, and Chapel Hill, North Carolina. What is less certain is whether policymakers in declining cities can create new innovation clusters by investing in universities or other research institutions. Empirical evidence does suggest that such investments could have lasting benefits for a city, but many of these studies examine the effects of well-established universities on a region. It is more difficult to say for certain what leads individuals and firms to cluster around certain institutions and not others, and it is unclear whether attempting to create such clusters out of whole cloth would succeed.

Taking a Balanced Approach

The economics literature provides a number of important lessons for urban policymakers. First, agglomeration economies are powerful forces that have led to the dramatic urbanization of the world's population over the past two centuries. These forces have fed into each other to generate remarkable economic growth. These feedback effects mean that even small changes to a city can have a large impact over the long run. Urban policies are often thought of in terms of large-scale projects: building a new sports complex or business center, redeveloping whole neighborhoods, or adding new public transportation infrastructure. But small-scale projects could be just as effective at promoting city growth.

Another takeaway is that cities are far from identical. The forces that gave rise to the movie industry in Los Angeles or the auto industry in Detroit may not be replicable elsewhere. Moreover, policies that generated a positive response in one city have no guarantee of doing the same in another. As the studies highlighted in this *Economic Brief* illustrate, policies implemented in the complex social environment of cities may trigger all sorts of unanticipated responses. This doesn't mean that policymakers can draw no lessons from experiments in other cities, but the key lesson is to proceed with caution.

Finally, place-based and people-based approaches should not be viewed as mutually exclusive. There may be practical limitations to how far city leaders can take any one approach. Emptying out a declining neighborhood may seem like the efficient choice in an economic model, for example, but it may not be a realistic solution. Rather, policymakers should consider a mix of responses that would be most appropriate for their respective cities. Two main questions should guide their choices. First, are there policies that can potentially improve the well-being of nearly all residents? Second, to what extent do more targeted policies help their intended recipients?

Santiago Pinto is a senior policy economist and Tim Sablik is an economics writer in the Research Department at the Federal Reserve Bank of Richmond. The Bank published a more comprehensive version of this article as the featured essay in the Bank's *2016 Annual Report*.

Endnotes

1 Darryl T. Cohen, "Population Trends in Incorporated Places: 2000 to 2013," United States Census Bureau Report P25–1142, 2015.

2 James Manyika, Jaana Remes, Richard Dobbs, Javier Orellana, and Fabian Schaer, "Urban America: U.S. Cities in the Global Economy," McKinsey Global Institute, April 2012.

3 Enrico Moretti, *The New Geography of Jobs*, New York: Mariner Books, 2013, p. 84; and Adam B. Jaffe, Manuel Trajtenberg, and Rebecca Henderson, "Geographic Localization of Knowledge Spillovers as Evidenced by Patent Citations," *Quarterly Journal of Economics*, August 1993, vol. 108, no. 3, pp. 577–598 (article available with subscription).

4 More recently in the 2000s, following the nationwide trend, poverty has been rising in the suburbs as well. However, poverty is still highly concentrated in inner cities.

5 The Census Bureau began tracking "standard metropolitan areas" with the 1950 census. These were later renamed MSAs, and the boundaries have changed over the decades following the fluctuations of cities. Data are from the 1950 census and 2010 census.

6 This article is based on an essay that appeared in the Federal Reserve Bank of Richmond's *2016 Annual Report*.

7 Stuart S. Rosenthal and Stephen L. Ross, "Change and Persistence in the Economic Status of Neighborhoods and Cities,"

Handbook of Regional and Urban Economics, 2015, vol. 5, pp. 1047–1120 (article available with subscription).

[8] Edward L. Glaeser and Joseph Gyourko, "Urban Decline and Durable Housing," *Journal of Political Economy*, April 2005, vol. 113, no. 2, pp. 345–375 (article available with subscription).

[9] Raymond Owens III, Esteban Rossi-Hansberg, and Pierre-Daniel Sarte, "Rethinking Detroit," National Bureau of Economic Research Working Paper No. 23146, February 2017 (article available with subscription).

[10] Patrick Kline and Enrico Moretti, "Local Economic Development, Agglomeration Economies, and the Big Push: 100 Years of Evidence from the Tennessee Valley Authority," *Quarterly Journal of Economics*, November 2013, vol. 129, no. 1, pp. 275–331 (article available with subscription).

[11] Patrick Kline and Enrico Moretti, "People, Places, and Public Policy: Some Simple Welfare Economics of Local Economic Development Programs," *Annual Review of Economics*, August 2014, vol. 6, pp. 629–662 (article available with subscription).

[12] The Empowerment Zone designation generally expired in 2009, though it was subject to a series of case-by-case extensions.

[13] David Neumark and Jed Kolko, "Do Enterprise Zones Create Jobs? Evidence from California's Enterprise Zone Program," *Journal of Urban Economics*, July 2010, vol. 68, no. 1, pp. 1–19 (article available with subscription); and Matthew Freedman, "Targeted Business Incentives and Local Labor Markets," *Journal of Human Resources*, Spring 2013, vol. 48, no. 2, pp. 311–344 (article available with subscription).

[14] Matias Busso, Jesse Gregory, and Patrick Kline, "Assessing the Incidence and Efficiency of a Prominent Place Based Policy," *American Economic Review*, April 2013, vol. 103, no. 2, pp. 897–947 (article available with subscription); and John C. Ham, Charles Swenson, Ayşe Imrohoroğlu, and Heonjae Song, "Government Programs Can Improve Local Labor Markets: Evidence from State Enterprise Zones, Federal Empowerment Zones and Federal Enterprise Community," *Journal of Public Economics*, August 2011, vol. 95, no. 7-8, pp. 779–797 (article available with subscription).

[15] Andrew Hanson and Shawn Rohlin, "Do Spatially Targeted Redevelopment Programs Spillover?" *Regional Science and Urban Economics*, January 2013, vol. 43, no. 1, pp. 86–100 (article available with subscription).

[16] Edward L. Glaeser and Joshua D. Gottlieb, "The Economics of Place-Making Policies," National Bureau of Economic Research Working Paper No. 14373, October 2008 (article available with subscription).

[17] Esteban Rossi-Hansberg, Pierre-Daniel Sarte, and Raymond Owens III, "Housing Externalities," *Journal of Political Economy*, June 2010, vol. 118, no. 3, pp. 485–535 (article available with subscription).

[18] Andrew Hanson, "Local Employment, Poverty, and Property Value Effects of Geographically-Targeted Tax Incentives: An Instrumental Variables Approach," *Regional Science and Urban Economics*, November 2009, vol. 39, no. 6, pp. 721–731 (article available with subscription).

[19] Several studies show that EZ programs could have generated demographic changes in affected neighborhoods. See David Neumark and Helen Simpson, "Place-Based Policies," *Handbook of Regional and Urban Economics*, 2015, vol. 5, pp. 1197–1287 (article available with subscription).

[20] Jeffrey R. Kling, Jeffrey B. Liebman, and Lawrence F. Katz, "Experimental Analysis of Neighborhood Effects," *Econometrica*, January 2007, vol. 75, no. 1, pp. 83–119 (article available with subscription).

[21] Susan Clampet-Lundquist and Douglas S. Massey, "Neighborhood Effects on Economic Self-Sufficiency: A Reconsideration of the Moving to Opportunities Experiment," *American Journal of Sociology*, July 2008, vol. 114, no. 1, pp. 107–143 (article available with subscription).

[22] Raj Chetty, Nathaniel Hendren, and Lawrence F. Katz, "The Effects of Exposure to Better Neighborhoods on Children: New Evidence from the Moving to Opportunity Experiment," *American Economic Review*, April 2016, vol. 106, no. 4, pp. 855–902.

[23] Erik Chyn, "Moved to Opportunity: The Long-Run Effect of Public Housing Demolition on Labor Market Outcomes of Children," Working paper, October 2016.

[24] Enrico Moretti, "Human Capital Externalities in Cities," *Handbook of Regional and Urban Economics*, 2004, vol. 4, pp. 2243–2291 (article available with subscription); and Enrico Moretti, "Local Labor Markets," *Handbook of Labor Economics*, 2011, vol. 4b, pp. 1237–1313 (article available with subscription).

[25] Lance Lochner and Enrico Moretti, "The Effect of Education on Crime: Evidence from Prison Inmates, Arrests, and Self-Reports," *American Economic Review*, March 2004, vol. 94, no. 1, pp. 155–189 (article available with subscription).

[26] Moretti (2013)