

# 1. Introduction

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Just like cities themselves, urban economics is undergoing a period of resurgence. Yet urban economists have to date contributed very little to the development and evaluation of real-world urban policy. Both historically and currently urban policy has been much more influenced by the disciplines of engineering, architecture, design and planning than economics or other social sciences.

To us this is both surprising and worrying. Cities are social and economic constructs – ‘organised complexity’, as Jane Jacobs puts it in *The Death and Life of Great American Cities* (Jacobs 1961). As Ed Glaeser suggests, cities are probably our greatest invention.<sup>1</sup> Other great inventions – the wheel or writing – arguably derive much of their value from the economic and social success of cities. Take writing: the complexity of urban life makes the efficient coding of information a necessity rather than a luxury, while the economic surplus created by cities in turn allowed the full cultural rewards of writing to be realised. Cities also amplified the impact of the wheel: to feed growing urban populations it was essential to overcome the ‘tyranny of distance’ (Bairoch 1988). Because of that success there were advantages in being able to support an urban population, and because they were more productive those early citizens demanded and could pay for better transport.

Such technological changes have helped cities to grow. But cities also help generate the ideas that make technological progress possible in the first place (Marshall 1918). Cities, however, do not ‘work’ simply because of the technology embodied in their infrastructure, their buildings or layouts. As Alfred Marshall sets out, cities ‘work’ because of the way in which they encourage and support specialisation, social interaction and the exchange of ideas. Infrastructure, buildings and urban form can be a means to these ends, but they are not ends in themselves.

As complex organisms, cities are made visible in their built form – and this is one reason why so much urban policy has been focused on the built

<sup>1</sup> For a lively, informed if picaresque account of the critical role cities have played in human history and economic growth readers should consult Hall (1998). For a lucid and engaging view of cities from the perspective of an urban economist see Glaeser (2011) and Moretti (2012).

environment. One result of this is that many key urban programmes have been largely uninformed by economic insights. The prime movers in developing land use planning, for example, were Ebenezer Howard (unsuccessful farmer, journalist and proofreader for *Hansard*), Sir Patrick Geddes (an academic zoologist who studied mining) and Sir Patrick Abercrombie (an architect). Sir Anderson Montague-Barlow, main author of the *Barlow Report* (1940) and one might say the originator of regional policy, was a lawyer turned politician. Baron Haussmann, the planner of 19th-century Paris, was a lawyer, turned administrator. The inspiration and intellectual roots of the ‘new urbanism’, people like Leon Krier or Christopher Alexander or the drafters of the *Ahwahnee Principles*, were all architects. The one great exception to this list (and the only woman) is Jane Jacobs, pioneer of urban re-use and mixed use – nominally a sociologist but in practice a polymath, drawing on a vast range of disciplines and ideas. Even here, Jacobs’ original thinking on how neighbourhoods and cities operate has often been distilled into fairly arid design principles, with little apparent understanding of the underlying dynamics.

What we might term ‘physical urbanism’ has not just influenced urban policy in Britain and France but all over the world. It has also shaped the education and habits of thinking about cities and regional differences of generations of urbanists, policymakers and practitioners. As a result, it often appears that urban policy is hardly influenced by economic thought. There is no single ‘right’ way to understand cities and make policy for urban areas. The best examples of urbanism recognise this, and bring multiple perspectives to the analysis (for instance, see Hall 1998, 2013 and Storper 2013). Nevertheless, economically informed perspectives on urban policy also need further exploration and development. This book is one attempt to do this, distilling policy lessons from the growing global body of urban economics and economic geography, and particularly from the work done at the Spatial Economics Research Centre (SERC), which was established at the London School of Economics in 2008.

Why does this matter? If conventional urban policy was generally successful in meeting its declared policy objectives it might not. Unfortunately, the evidence we have suggests that this is largely not the case. As this book will set out, many (though not all) of the key tools in the urban policy box have had limited or little positive effect on the economic and social outcomes we all care about. Equally, some of these tools – in the UK, notably land-use planning – have generated substantial economic and social costs for large groups of people. And until recently, a lack of robust evaluation has exacerbated these problems, by leaving ineffective or counterproductive interventions in place.

Making effective policy for cities is extremely challenging. We strongly

believe that urban policy could be improved by bringing a stronger economic understanding into policy design and delivery. In particular, urban policy informed by economic insight can help improve policymaking for individual cities and urban systems as a whole. Of course we also recognise that city leaders and urban policymakers need to balance economic, social and environmental welfare. But we suggest that in at least some cases – planning, again – applying insights from urban economics can improve outcomes across all of these domains.

Three themes recur in this book: the need for realism in the face of strong market forces that drive unevenness; the ineffectiveness of many current urban growth policies and other interventions; and the importance of focusing on outcomes for people not places. The book is organised in three parts that develop these ideas, with Part IV providing some conclusions.

In the first part, Chapters 2 and 3 establish our basic building blocks. Cities both arise from and generate agglomeration economies: people and firms are more productive, all else equal, when they live and work together in cities. Agglomeration economies, as we show in Chapter 2, increase with city size. Although there are also diseconomies of size – mainly congestion, pollution and increasing space costs – recent research strongly suggests these costs have tended to be overestimated and after a certain size rise only slowly. Space costs rise with the size of a city only because it is worth paying extra to live or work there – that is because of the gain in productivity and higher incomes bigger cities generate. Workers and firms trade-off the productivity and amenity benefits of cities against these congestion costs when thinking about where to live, produce and work. Urban economics provides a powerful conceptual tool – spatial equilibrium – for thinking through the implications of these interactions for the development of the urban system as a whole.

The evidence shows that agglomeration economies are much more important in some economic sectors than in others: for example, they are some four times as important in financial or business services as in the manufacturing of wood products (Table 2.5); on average they are almost three times as important in services as in manufacturing. The sector where they are most critical of all seems to be public services: echoing one of the original functions of cities as centres of administration.

More generally, these sectoral differences in agglomeration economies make for one very powerful reason for urban resurgence – especially in larger cities and cities with more skilled and educated populations – seen over the last 20 years. The most rapidly growing sectors in advanced economies have a competitive edge in these locations. Unlike manufacturing, services and the public sector tend to use less physical space, so are

relatively less constrained by higher land or property costs. With less need to ship raw materials and goods, they are also less affected by congestion – although their workforces need effective transport systems to commute.

Service activities have also differentially benefited from one of the most significant technical innovations of the past 25 years, the internet (Ioannides et al. 2008). Online technologies have hugely decreased the costs of finding and sharing information, and this has helped many service sector firms spread their businesses across multiple locations (McCann and Acs 2011). However, services also depend on face-to-face interaction: between firms and their customers and with their specialist suppliers (such as legal services, advertising or finance) and subcontractors. Cities, especially the largest urban cores, help keep these costs down by enabling contact and ideas flow on a grand scale.

Cities are places of culture and leisure, as well as centres of production. And just like workers' productivity, consumption of 'leisure goods' expands and becomes more rewarding with city size. As cities grow, the market for any given cultural activity grows with it: this allows specialisation and enhances choice. As Georg Simmel observed in 1903, city life supports multiple scenes, cliques and subcultures in which attention is part of the currency (Simmel 2013). Culture requires an audience: that is what a city provides. The larger the city (and the better its physical infrastructure), the larger audience it will generate. To put it more formally, choice of cultural pursuit and entertainment is both dependent on cities and is a positive function of their size.

As Chapters 2 and 3 acknowledge, the causes of urban resurgence are still not fully understood. In turn, this makes predicting urban futures a perilous business.<sup>2</sup> We can probably safely say that many of the economic changes we have been observing over the past 20 years are going to continue. Unless something fundamental changes, large-scale manufacturing will have almost no place in the economies of larger cities in rich countries in 2030, certainly not in their urban cores. Emerging technologies such as 3D printing are likely to accelerate this trend. Skills will be even more important than they are now, and economic penalties for the low-skilled will be even greater.

In Chapter 3 we examine how, within cities, the land, labour and housing markets all interact and generate fine-grained sorting between neighbourhoods. This process generates residential segregation, but at the same time, specialised neighbourhoods which often provide benefits to their residents. In some sense these are another manifestation of

<sup>2</sup> Many of the world's key cities are low-lying, coastal or both: they face increasing environmental uncertainty due to climate change. See Smith (2011) for an overview of these issues.

agglomeration economies – not in production but in consumption. In turn this has important implications for policies designed to produce ‘mixed neighbourhoods’. They can have costs in both resource terms and perhaps in terms of one of the attractions cities offer – the ability (subject to income) to choose to live in congenial neighbourhoods with compatible neighbours. Recent evidence also increasingly suggests that policies to mix neighbourhoods may be wholly ineffective at reducing economic inequality. In essence, Chapters 2 and 3 make the case that a better understanding of how city economies function – in particular the importance of the three-way interaction between agglomeration benefits, congestion costs and the sorting of workers across cities and neighbourhoods within those cities – helps explain both how global trends play out spatially and the role that the spatial economy plays in driving national and global macro trends.

A key argument in this book is that urban policy needs to work better with the grain of markets. That does not mean letting markets rip: cities contain many endemic market failures, especially in land and property, where it is often in the wider social interest to override market signals. To do this effectively, however, implies building market signals into the underlying policy framework.

The second part of the book, Chapters 4–6, explores these issues in detail. Congestion and pollution are classic examples of market failure and this diagnosis suggests obvious solutions. The most obvious of all, congestion pricing, has not really been widely applied (certainly not in its ‘pure’ form with prices varying to reflect congestion levels) despite the politically brave effort of Ken Livingstone, the first modern London mayor. But as we argue in Chapters 4 and 5, some of the UK’s most powerful urban policies have the unintentional effect of increasing the costs of urban size while at the same time constraining their growth. The incredible difference in prices across South East England between farmland and land on which it is permitted to build is in effect a signal of foregone agglomeration economies: people and firms would be willing to pay such prices to build if they could, both to gain access to income-earning locations and to popular places to live. In 2010 (the latest data at the time of writing), housing land in the South East was worth 430 times its value as farmland. On the fringes of London, that figure rises to 925 times. So these foregone agglomeration economies are likely to be large. Dealing with this problem in Britain, as elsewhere, will require radical reform of the planning system, a thorny problem that we deal with in some detail in Chapter 6.

In the third part of the book we turn to the governance of cities, and to the evaluation of urban policies. In the UK, one of the most centralised countries in the world, planning powers are part of the package of policy levers being slowly devolved from Whitehall to city leaders. Ministers

hope that devolution will unleash urban economies in a way that helps to narrow spatial disparities. As Chapter 7 makes clear, however, the evidence of any link from governance to economic performance is weak, and international experience is rather mixed. In countries like the UK, there are good reasons to think that devolved governance can improve economic and social outcomes, as city leaders apply local knowledge and develop bespoke interventions. However, there is a real risk that communities with weaker or less experienced leaderships will become worse off, not better. In turn, this implies that central government will need to carefully manage the transition to localism.

Whatever the institutional architecture, improving urban policy requires a better understanding of the causes and consequences of uneven city performance. It requires us to be more realistic about policy ineffectiveness in the face of strong market forces that reinforce unevenness. And it requires us to focus much more on the impact of policy on people rather than places. The importance of cities in shaping the lives of billions makes urban policy vitally important, but as we discuss in Chapter 8, many popular urban policies either do little to achieve their stated aims or have unintended and counterproductive consequences. Our conclusions may appear discouraging. When dispassionately evaluated, the evidence suggests policy can in truth do relatively little to change the basic trajectory of underperforming urban areas, but misguided policies can have very bad unintended outcomes on all cities. In other words, governments have limited power to directly improve urban economies and a great deal of capacity to damage them. Hence, one of the key themes of this book is that policies need to be realistic about the causes of spatial disparities and the lack of effectiveness of many popular policies. In terms of causes, we argue that this means understanding that differences that may appear to be spatial are, in reality, often driven by differences between people rather than places. Realism about both causes and policy effectiveness does not mean there are not lots of very useful things policy can do but the useful things are often not so glamorous: efficient public administration, simple and transparent regulation, policies to reduce the costs that increase as cities get bigger.

Like all scholars, scientists or authors we have learned from and rely on the work of others. This is particularly true of this work. It started out as an attempt to edit the set of SERC *Policy Papers* into a coherent book form.<sup>3</sup> As we did this we found we had to update, discard and edit so much that it has evolved into an authored book. Some chapters had clear lead authors (Cheshire on 3, 4 and 6, Nathan on 7 and Overman on 8), one had

<sup>3</sup> [http://www.spataleconomics.ac.uk/SERC/publications/policy\\_papers.asp](http://www.spataleconomics.ac.uk/SERC/publications/policy_papers.asp).

joint-leads (Nathan and Overman on 2) while we are jointly responsible for 1, 5 and 9. Getting to the final versions has, of course, involved substantial editing of each other's material throughout.

Large parts of the book draw heavily on – even use verbatim – many of the original *Policy Papers*. So we should particularly thank and apologise to the authors of those papers: Steve Gibbons, Ian Gordon, Patricia Rice and Paul Steeples who gave us permission to shamelessly plunder their work. We should also thank the numerous research officers and research assistants – mainly postgraduate students – who have worked on SERC projects. Most of all we should thank Kirsty Kenney, Teresa Schlueter and Sevrin Waights who have helped us directly with material and given outstanding editorial assistance. Finally we would like to acknowledge the inspiration provided by the work of Ed Glaeser. While many great scholars have contributed to the rapidly expanding body of urban economics research, Ed's boundless energy, economic insight and love of cities have been central to recent efforts to take insights from that research to a wider, non-specialist audience.

As with everything in life that is complex, there are few simple right or wrong answers when it comes to urban policy. We strongly believe that urban economics provides many pointers as to how the policy mix might be improved. But some of these recommendations are contentious. Indeed, there are a number of issues on which even we three authors disagree – on aspects of brownfield development and mixed communities policy, for instance – and where we have had to apply the principle of 'majority rule'.

Neither do we claim anything like perfect knowledge. Given the acknowledged gaps in the evidence base, some of these recommendations might not work, hence our emphasis on experimentation and rigorous evaluation to help inform the development of future urban policy.

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