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State of the Market 29: The United Cities of America

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A few weeks ago, the Brookings Institution published a spectacular report, *The State of Metropolitan America*[1], that in effect redefines us not as the United States but the United *Cities* of America. Via several hundred pages of concise detailed text and great graphics, the Rockefeller-funded report clusters America's 100 largest metro areas into a new typology that gives a sharp and emphatic picture of where America has gone in the last score of years and where we will go in the next score.

The top metropolitan areas, from Modesto (510,000 people) to New York City (19,000,000), house two-thirds of Americans (66% in 2009), the highest urbanization in our history and still rising: "Cities gained population at suburbs' expense in the wake of the housing crash."

That difference in economic and demographic impact nexus – from state to city – affects how our economy will grow, and with it where our population will grow. These trends have profound implications for multifamily residential property as an asset class, and affordable housing programs as national policy.

Cities of America: seven types

Brookings classified our cities not by geography but rather by socioeconomic prospects and challenges.

1. Industrial cores (18 cities), "in some ways the most demographically disadvantaged of the metropolitan types," are tied to the industrial and not the information age. Memphis, Topeka, Dayton, Detroit, Norfolk, to name a few – have enormous place-based infrastructure, much of it old-tech, and are struggling to define their new identity. They're hurting, losing population over the decade, and won't get better soon.

Are states just boxes to put cities in? From Brookings' report

2. Diverse giants (9) are metro areas whose name is known around the world – New York, Los Angeles, Chicago, Miami, San Francisco. National and even global magnets, nearly all have a world-class core competency (e.g. finance in New York, entertainment in Los Angeles) for which their specialization is a self-reinforcing comparative advantage. Home to 58,000,000 Americans, their cores are growing, going up instead of out. All of them are on bodies of water, in difficult topographies to expand, and with hostile real estate development environments – meaning permanently high housing prices.

3. Skilled anchors (19) are mind magnets – Boston, Philadelphia, Syracuse, Rochester, Cleveland, Milwaukee, even Akron and Worcester – older, slower growing, but with higher than average educational achievement and often a

[1] The report is summarized at http://www.brookings.edu/metro/StateOfMetroAmerica.aspx and may be downloaded (16 Meg) at http://www.brookings.edu/~/media/Files/Programs/Metro/state_of_metro_america/metro_america_report.pdf.

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national-class core economic competency around innovation.

4. Border growth (11) cities cluster along our frontier with Mexico – all except Orlando. Corpus Christi, San Antonio, El Paso, Phoenix, and then Bakersfield, Fresno and others are "marked by a significant and growing presence of Mexican and other Latin American immigrants," and there is a direct connection between immigration and low-skilled labor – and conversely, between high-skill innovation and the emergence of a semi-formal service economy.

5. New Heartland (19) cities are in many ways the report's unannounced story – places that until recently we would never have considered as urban, yet increasingly sprouting vertical central business districts. Charleston and Columbia SC, Kansas City, Sioux City, Iowa City, Nashville, Knoxville, Raleigh-Durham, Salt Lake City, and Provo UT – they are fast growing, highly educated locales, with a lower share of immigrants.

6. Mid-Sized Magnets (15) "have experienced high growth, but exhibit lower shares of Hispanic and Asian minorities, and lower levels of educational attainment." An information and internet economy, where the cost of shipping goods is asymptotically approaching zero, creates opportunities to locate businesses in lower-cost labor markets, and make them into specialist centers themselves. Unlike smaller countries, where the capital city tends to consume everything, America's economic capacity distributes around the land, aided by the world's most mobile labor force. The Mid-Sized Magnets will likely rebound quickly – taking jobs, money, and people from the Industrial Cores – as will the last category, which never actually suffered much downturn at all.

7. Next frontier (9) metro areas are our principal growth engine, as they "exceed national averages on population growth, diversity, and educational attainment. Of these nine metro areas, eight – Dallas, Houston, Austin, Albuquerque, Tucson, Denver, San Jose, and Seattle – lie west of the Mississippi River (Washington, DC is the exception)."

Six national trends and their multifamily implications

Cities are the importation points for the greatest American demographic trend of all: immigration. As America goes global, we are becoming a browner nation: whites represent only 17% of national population growth. Though the current immigration wave has been checked by the recession, people will keep coming. Those who come are younger and more fecund than those who live here, and given a generation's procreation, they will remake the look of our country.

A majority of 65+ Los Angelenos are white; a strong majority of those under 18 are Hispanic. Clint Eastwood's movie *Gran Torino* caught the zeitgeist – cities are the front lines of this most recent wave of great American immigration, and America must adapt to its immigrants even as the immigrants are becoming Americans. Brookings identified five major trends, to which I will add a sixth below.

Trend 1. Growth and Outward Expansion. Our population has topped 300 million, and by 2020 we will add another 28 million Americans – most of them in cities. As America urbanizes, our cities are engines of economic production – and engines of energy consumption, so we want to manage the latter without compromising the former. To grow within a low-carbon city means going up – more verticality – and that takes capital investment on structural technology and municipal infrastructure.

A tax on carbon burning is economically quite different from a cap-and-trade model (with its nasty externalities and dysfunctional administrative system). Its goal is not to reduce greenhouse gases for their own sake, but rather to encourage a more efficient city – and it has the beneficial byproduct of keeping taxes here at home, to trim runaway budget deficits.

Real estate implications. Many of our growing cities are footprint-limited, requiring higher-density but lower-carbon use of the surface area. That means more mixtures: more intermingling of public and private space, repurposing highways into transit lanes. It implies more mixed-use, mixed-income development, more urban workforce housing, more transit-oriented development. To achieve this, metropolitan and regional policy makers will deploy non-Federal resources, making more extensive and better use of inclusionary zoning, density bonuses, real estate tax abatements, sophisticated extended-use land covenants, redevelopment areas (RDAs) and housing set aside funds (HSAFs). It also implies taking a scythe to regulatory barriers to development that choke off affordability even as their supply restrictions price housing beyond workers' reach. The cities that do will win out economically over those that do not.

Trend 2. Population Diversification. America's great strength has lain in its capacity to absorb. The Golden Door remains open, and those who arrive aren't coming from Europe. America's population today is one-third non-white, with those groups representing five-sixths of our *internal* population growth over the last eight years, to say nothing immigration growth. Today nearly one-quarter of US children have at least one immigrant parent. As the report discusses in depth, the challenge of immigration is not change *per se*, but the cultural clash where the elderly are all one ethnicity, and the youth all another.

Real estate implications. Offer more diverse configurations of rental – more than just the 1-BR's and 2-BR's that dominate new construction. Emphasize rental, and strengthen America's stock of permanent professionally operated rental housing across the full continuum from high-end luxury right through special-population properties. Conform affordable-housing rent-setting structures to allow rents to fluctuate as income and household composition circumstances change, and to motivate intra-property moves so that families are not under-housed and the elderly are not over-housed.

Trend 3. Aging of the Population. As the nation's 100 million baby boomers grow old (despite all our best denial mechanisms), we are remaking cities: the 55-to-64-year-old populations of America's cities grew 45% in the last eight years. Compared with youth, older people are richer, slower, more cultural, more socially and economically conservative, and with more assets to protect. Smaller childless households – either the aging or those who support the aging – mean workforce housing. They mean employer-assisted housing. They mean group living innovations like modern rooming houses that are neither flophouses nor SROs. They mean transit-oriented development – not to cut down on carbon, but to save us from traffic jams and impoverishing and enervating commutes.

Meanwhile, retiring baby boomers will take their wealth from where they earned it (the cities of yesterday), and they will move it – south, west, and wet – to where they want to spend it (the cities of tomorrow). These aging people represent a huge demographic challenge, and also an economic opportunity, especially for America's recent immigrants, old or young, high-skilled or low-skilled.

Real estate implications. Design properties that can add service enrichment and a continuum of care, as their population ages in place. Recognize that renting, congregate living, assisted living, and nursing homes should all be in reasonable proximity to one another to accommodate shifts in a person's capacity for independence without uprooting her from her community and family. Retrofit existing multifamily properties, particularly affordable housing, to cope with an aging population. Bring services into developments rather than making people go to them; use common space as a service nexus for the broader community, including neighbors who do not live in the property. Develop, standardize, and consumer-protect financial products, like reverse mortgages or life tenancies, that enable the elderly to monetize a portion of their savings in exchange for lower occupancy cost and higher services during their lives.

Trend 4. Uneven Higher Educational Attainment. In a knowledge economy, good ideas become new money. Twenty-first century America will lead the world with our intangibles: our popular culture, our liberty-oriented value system, our financial innovations, our entrepreneurial ethos and capabilities, and our delight in the next idea. As education and knowledge become distinguishers, they drive separation of incomes. For America to thrive, we need a smarter workforce.

Real estate implications. Design apartments as if they will be capturing an increasing share of the resident's total waking hours. Focus on strengthening home-office and telecommuting capacity. Add rooms that can be flexibly purposed either to family or business requirements. Add broadband, preferably wi-fi.

Trend 5. Income Polarization. For the first time in my life, real American incomes have declined: by more than $2,000 per household from 1999 through 2008 – *and* there is divergence, with the higher-income/ higher-skilled holding their ground and the lower-skilled falling behind. Metropolitan areas with low average wages (Bakersfield, El Paso, Scranton) suffered losses; those with polarizing income did better. As education, location, and skills create economic winners and losers, our population's economic prospects disperse. The mantra for people – and for cities – is simple: *get skilled, or get poor*.

Real estate implications. Incentivize smart-youth magnets like universities. Create early-workforce-entrant rental configurations like service-based rooming houses. Introduce or update low-cost workforce homeownership alternatives like shared-appreciation mortgages, limited-equity co-operatives, and first-time homebuyer programs with the ability to recapture extra appreciation upon market resale.

This leaves us with one more trend Brookings didn't highlight but I will:

Trend 6. The housing policy innovation inversion. With a federal system, money and policy can flow either of two ways: top down, from national government through states to localities, or bottom up, from metropolitan areas and states to Washington. With our national real estate shakeout so unevenly distributed, mainly hitting five states (California, Arizona, Nevada, Michigan, and Florida), and the wildly varying finances of state governments, key housing issues are increasingly diverse at the state and metropolitan levels. Inclusionary zoning, redevelopment areas, workforce housing, transit-oriented development – all these become meaningful only when applied locally.

Real estate implications. Metropolitan areas should tackle their problems themselves, instead of depending on Federal bailouts. That will require weaving together transportation infrastructure and public-space greenery and amenities into a city built around internet shopping more than malls, clicks instead of cars. As this spans multiple localities, it will require effectiveness at metropolitan government – that is, across cities and towns within the same metro area – that has heretofore generally been lacking.

All this is easier said than done – but every quest begins with a vision of the goal.