Comments on "Cities, Information, and Economic Growth"

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One goal of the Regional Growth and Community Development Conference was to learn more about the "new regional economics" and what it offers to the discussion about regional and community economic development. Some have drawn an analogy between this literature and the debate within the international trade literature. Proponents of the "new international trade" have challenged one of the most basic beliefs of economists, the primacy of free trade. Do proponents of the new regional economics have something similar to say about regional and community economic development? Also, is the literature ready to enter a normative stage in which it recommends specific government policies?

The bulk of my comments are organized around these two questions, but they are prefaced with praise for Glaeser's article, an excellent contribution to the conference and to the literature on the new regional economics. The author offers a close look at the intellectual roots of the new regional economics and its linkage to earlier work in urban and regional economics. He courageously offers a list of "stylized facts" about urban growth and an inventory of reasons why the city may well be important to economic growth. Finally he provides a lengthy example of the logic underlying the new regional economics in a stimulating discussion of the dark side of agglomeration, the potential for crime and riots.

What Is the New Regional Economics?

Glaeser's definition stresses four points. First, the questions being addressed are about the determinants of urban growth. This focus returns the field to its earlier roots and differs from the new urban economics of the past 20 years or so that placed great emphasis upon intrametropolitan location and suburbanization.

Second, the driving force behind economic growth is the role of information externalities, of which he offers many excellent examples. Let me offer a simple one of my own: the value of an individual's decision to participate in an organization's EMAIL system. An individual's decision to join the network will naturally place great emphasis on the costs and benefits of participating in the system. However, the benefits to the individual are likely to extend to many others as well. The marginal cost to the individual and to the group of joining the network are assumed to be small. In any event, the individual is likely to delay the decision beyond the optimal time because the external benefits will not be taken into account. More generally, too few people will join the network if left to their own calculation.

Third, cities can and do play a critical role in the creation of information externalities by allowing for more and better communication among individuals. This enhanced communication generates many new ideas, which lead to economic growth. The new ideas and the ability to learn from others provide workers with an excellent opportunity to build their human capital and earn higher wages.

Fourth, both the level of economic output and the rate of economic growth depend upon historical forces. In particular, cities that experienced good fortune at some point in their history tend to have an advantage over other cities for a substantial period of time. I do not disagree with the importance of "history," although I do take issue with Glaeser's association of this concept with the new regional economics. The urban economics literature has long included the concept of the "malleability" of capital and the structure of urban growth with and without a malleable capital stock.

The author's description of the new regional economics is similar, but not identical, to others I have heard recently. In the spring of 1993, Paul Krugman and Vernon Henderson presented seminars about the new regional economics at Syracuse University. Krugman seems to place greater emphasis on the importance of economies of scale in production than on information externalities per se. He also stresses the technical advances in modern trade theory that facilitate the analysis of models with imperfect competition and economies of scale. As such, his description closely parallels the international trade discussions about strategic policies to provide one region with an advantage over another.[1]

Henderson places the new literature in the context of a long literature about systems of cities and the contribution they can make to the economic growth of a national economy. "Systems of cities" refers to the optimal size and function distribution of cities and, among other things, seeks to explain why city size matters to an economy. According to Henderson, the new regional economics is an attempt to clarify the microfoundations of agglomeration economies and the many forms in which they may come. In this context information externalities are an important example of agglomeration economies, but not the only one.

Policy Implications

Is the new regional economics ready to move to the normative stage? For the most part, I find the field, and especially Glaeser's description of it, quite stimulating and believe it will only grow in importance in the coming years. Nonetheless I doubt that the new regional economics is ready to provide policymakers with a detailed list of policy recommendations, and I suspect Glaeser agrees. He is surely careful to point out, as did many other conference participants, that the task of generating growth within some of our cities appears daunting and fraught with problems.

My major concerns are three. First and foremost, Glaeser's discussion seems to downplay the many ways in which the market and its institutions may internalize the knowledge externalities that he and others have identified. I have several examples in mind, in addition to my belief that individuals seem to have a significant incentive to invest in their own human capital. My primary example is that of the firm. Why cannot a firm capture many of these externalities by its own organizational structure? Such action might take the form of a large research staff, frequent seminars and training, and possibly diversification. This latter point is one in which financial economists may be quite interested, as they seem always to be looking for ways to justify that which many corporate managers seem to have taken for granted, at least until recently: diversification is good business. Another example of internalizing market externalities includes the structure of real estate development, such as the "Edge City" so many have discussed. Still another, more general, example is the land market itself. If this market has the potential to internalize the externalities by generating higher land prices in those areas where externalities are prevalent, then the importance of the city per se is reduced.

A second, related concern deals with the response of the political system. Glaeser notes that the institutional structure is a key determinant of the production of information externalities. Unless the institutional structure allows individuals or groups to capture the benefits of these externalities, there is little incentive to produce them. I suspect that the structure of local government is an important element in the institutional structure, although it receives little attention in the article. Indeed a long-proposed solution to some of the problems of central cities is a system of metropolitanwide government. Bahl mentions it in his article, and the idea has recently been espoused by Rusk.[2] My own guess, and that of many others, is that full-scale metropolitan government is unlikely to occur in the near future. Perhaps Glaeser provides us with a new rationale as to why this is so. Suburbanization may be a partial response by the political system to the need to provide the benefits of agglomeration to a large portion of the population in the workplace without unduly exposing them to the dark side of agglomeration in their places of residence.

My third concern about the new regional economics relates to the quality of the empirical work on the topic and applies to "old" regional economics as well. I am less optimistic than most in the field about the use of employment as the measure of economic growth. Although Glaeser is right in arguing that income per person is probably not the right measure in an open urban model, something like gross city product (GCP) is appropriate. This is surely a difficult concept to measure, and we have only recently begun to struggle with the definition of gross state product. But until we do our empirical work, measures of the success of economic development programs are seriously deficient. Timothy Bartik offers some suggestions on this subject in his article.

Another potential source of information about the power of information externalities is the responsiveness of other institutions to their presence. As noted above, firms, land prices, and real estate may be structured in ways that internalize the information externalities. If so, the valuation of these institutions and assets may provide clues about the value of the externalities. Perhaps studies of firms stratified by their efforts to internalize these knowledge spillovers can be informative. They may also show us whether land prices appear to be influenced by the size and composition of the industrial structure. An even more narrowly focussed source of information may be the real estate projects themselves. Do new real estate structures provide a better environment for the creation of information externalities than old real estate structures? If so, they ought to be more highly valued, all else being equal. All of these sources of information represent serious data challenges, but they may also represent an alternative to the unsatisfying standard of employment as the measure of economic growth.

Author

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Notes

1. See Krugman, Paul. 1991. *Geography and Trade*. Cambridge, Massachusetts: MIT Press.

2. Rusk, David. 1992. *Cities Without Suburbs*. Washington, D.C.: Urban Institute Press.