INTERNATIONAL AFFAIRS at
THE NEW SCHOOL

Working Papers

Thinking Outside the Bubble:

The Urban Crises of Land, Labor, and Capital

Michael Cohen
The New School, New York

International Affairs Working Paper 2007-05
October 2007

Paper prepared for Lincoln Institute for Land Policy Symposium, Rio de Janeiro, October 1-2, 2007

Thinking Outside the Bubble:

The Urban Crises of Land, Labor, and Capital

Michael Cohen
Professor of International Affairs
The New School
Cohenm2@newschool.edu
www.gpia.info

International Affairs Working Paper 2007-05
October 2007

ABSTRACT

Many analyses of urban phenomena in developing countries occur in an intellectual and urban policy bubble which ignores the impacts of global economic phenomena. "Urban conventional wisdom" ignores the role of global capital flows in urban capital formation in housing and infrastructure. This narrative neglects the central role of urban employment in the generation of urban incomes and livelihoods. Urban policy debate has thus ignored three fundamental crises affecting cities: land, labor, and capital. While some institutions and analysts have studied these issues, their messages have not been heard by influential actors in the wider urban debates. Empirical cases from urban China and urban Africa illustrate these crises.

Thinking Outside the Bubble:

The Urban Crises of Land, Labor, and Capital

by

Michael Cohen

Introduction: The Bubble of Conventional Wisdom

In the last several years there have been a growing number of books and reports about the urbanization of the planet. While some are grounded in careful demographic analysis[1], others are more focused on the physical form of housing and infrastructure, particularly of the poor.[2] Some portend "the urban future" is already upon us; while others can see the migrants coming over the next hill. Still others use technology and geographical information systems to record the past and to predict inexorable urban spatial expansion.[3] Together, they contribute to a growing conventional wisdom about cities.

Among the new urban explorers are those who celebrate the ingenuity of the urban poor in so-called "shadow cities",[4] while others stand back from any particular set of cities and proclaim that we are now a "planet of slums".[5] This condition is decried, without acknowledging, in this book, the enormous efforts of people in slums themselves to improve their circumstances.[6] These authors fail to examine often hostile public policies, severe economic deprivation, and technical and institutional problems which slum dwellers face, some of which are often compounded by the very institutions which seek to provide urban assistance.

Another set of studies focus on "global cities" and their role as centers of management and control in the global economy.[7] These studies have sought to identify

[1] National Academy of Sciences, Cities Transformed: Demographic Change and its Implications in the Developing World, (Washington: National Academies Press, 2003), United Nations' Population Fund, State of World Population 2007: Unleashing the Potential of Urban Growth, (New York: UNFPA, 2007)
[2] UN Habitat, The Challenge of Slums, Global Report on Human Settlements 2003, (London and Sterling, Virginia: Earthscan, 2003), Millennium Development Project, Home in the City, Report of the Millennium Development Project Task Force (2004)
[3] Shlomo Angel, "Measuring Global Sprawl: The Spatial Structure of the Planet's Urban Landscape", (Washington: The Cities Alliance, 2006)
[4] Robert Neuwirth, Shadow Cities: A Billion Squatters, A New Urban World, (New York: Routledge, 2005)
[5] Mike Davis, Planet of Slums, (London and New York: Verso Books, 2006)
[6] See David Satterthwaite, "Asking the Right Questions about Slums", a review of Davis, ibid.
[7] Saskia Sassen, The Global City: New York, London, Tokyo, (Princeton: Princeton University Press, 2001, updated edition)

urban networks and linkages within the global economy, and how these have become embedded in local urban spatial and economic structures, such as infrastructure.[8] This analytic work helps to explain the emergence of differences and disparities within urban spaces, among people and places. It focuses particular attention on how global capital generates employment in specific high-end sectors, namely the financial sector and technology. However, it does not explain overall patterns of capital formation within cities nor of city-wide employment creation itself. For example, it tends to exclude the housing sector from its analysis.

Another approach to urban growth has been through urban geographical studies, showing how city form has changed over time in relation to city function. This work has been helpful in explaining changes to city form over time, showing the value of a historical perspective. But this focus on space has not identified the economic mechanisms and processes of building cities.[9] Thus, the questions remain: how is urban capital created? or put another way, how is the city built? who does it? under what conditions?

Within the conventional wisdom about cities are some advocates whose work is characterized by single perspectives and frequently oversimplified – if not reductionist - solutions to curb the ills of cities. For example, the magic bullet solution of land tenure and property rights alone, suggested by Hernando de Soto,[10] is flawed, because property rights without infrastructure does not guarantee improved housing, neighborhoods, or access to credit. Similarly, simple celebratory notions of privatization of urban services were sold on the grounds that privatized services such as water supply would provide more efficient services to ever-growing numbers of potential clients. This has proven problematic in cities as diverse as Buenos Aires, Cochabamba in Bolivia, Atlanta, and Jakarta. Another urban magic bullet which circulated within the international community after the Rio Environmental Summit of 1992 was that community participation would be effective in addressing high priority urban environmental problems, ignoring the need for science to prioritize health threats and economics to determine the cost of solutions.

The making of conventional wisdom does not come from any one source; necessarily it involves one book, report, conference, and project experience built upon each other. In the urban field, following fifty years of professional work going back to the United Nations' Centre for Housing, Building, and Planning, through the World Bank's entry into the urban sector in 1972, bi-lateral growth from 1970 to 2000, through the Vancouver I and II meetings, Habitat II in Istanbul, UN Habitat Commission meetings in Nairobi, and now the Cities Alliance, as well as projects in 11,000 cities and towns by 2000[11], urban debates continue to be framed in a highly global formulation of urban phenomena. This formulation tends to fail to acknowledge and much less capture

---

[8] Saskia Sassen, ed., Global Networks, Linked Cities, (New York: Routledge, 2002), S. Graham and S. Marvin, Splintering Urbanism: networked infrastructures, technological mobilities, and the urban condition, (New York: Routledge, 2001)
[9] Edward W. Soja, Post-metropolis: Critical Studies of Cities and Regions, (Oxford: Blackwell, 2000)
[10] Hernando de Soto, Mystery of Capital, (New York: Basic Books, 2000)
[11] Michael A. Cohen, "Urban Assistance and the Material World: Learning by Doing in the World Bank"; Environment and Urbanization, Volume 13, No.1 (April 2001)' pp.37-60

important regional, national, and local differences. Despite a growing literature and awareness of "the local"[12] – and the extensive lip-service that it receives in international meetings -- the global formulation of "the urban" hinders and limits the ability to anticipate and respond to emerging local conditions.

This global formulation focuses heavily on a limited number of subjects: demographic growth, housing, infrastructure, land, governance, civil society, environment, slums, urban poverty, the informal sector, and security and safety. However, this conventional wisdom suggests a view of the city which is independent of time and space and, despite the emphasis on demographic and spatial growth, is relatively static. It ignores other changes at different scales, whether at the global, regional, national, or local levels, and fails to acknowledge their impacts on cities through changes in prices, value, and costs. This view of cities is perceived and articulated as relatively independent and insensitive to major phenomena such as global financial crises, national political change, or local disasters.

What is also quite striking in the absence of linkages to events and processes at other scales is the continuing independence of this model of cities from economics, whether in the form of global economic forces or the characteristics of local economies such as their sources of capital formation, productivity, employment, and incomes. At some intuitive level, most urban analysts are still entering the city through the house and the bathroom, rather than through the workplace, the market, or as a site of creating long-term assets.

While it is true that the 1960s and 1970s dominance of the urban field by the architects and urban planners has given way to other disciplines, such as demographers, political scientists, and environmentalists, there remains a fundamental gap in the international conventional wisdom about the economy of cities. This is not to say that there are not urban economists, or that they are not working as academics, in government, or in financial institutions. Rather their perspective has not really been integrated into many current urban policy debates.

Looking Beyond Conventional Wisdom

Looking beyond this conventional wisdom, three major conceptual, policy, and operational challenges exist which have not been sufficiently addressed: First, how will investment in housing and infrastructure for growing urban populations be financed in the future? Secondly, how will jobs and incomes be generated for these populations? And thirdly, what is the role of land in helping to address the first two? These challenges can be described as the crises of urban capital, labor, and land.

[12] Lucy Lippard, The Lure of the Local, or Edward Goetz and Susan E. Clarke, eds., The New Localism: Comparative Politics in a Global Era, (Newbury Park: Sage Publications, 1993), Manuel Castells and Jordi Borja, Local y Global. La gestión de las ciudades en la era de la información, (Madrid: Taurus,1997)

On the first question, it is known that in most developing countries, domestic economies finance most urban housing and infrastructure. However, it is difficult to identify which institutions or agents actually finance these investments. For example, it is hard to imagine that national governments have the financial resources needed to finance urban housing and infrastructure. At present, they face serious budgetary constraints and are in most cases unable to finance the existing backlogs even for public infrastructure. Nor is it likely that local and/or municipal governments will have the needed resources for these purposes. Most municipalities, in both rich and poor countries, devote a large share of scarce municipal revenues for the salaries of municipal employees. Further, it is also difficult to imagine either the international private sector or the domestic private financial sector providing finance for the needs of the urban poor. Clearly they believe that there are other more secure and higher return activities deserving private investment. If this general characterization is true, what can then be expected in terms of the housing and infrastructure conditions in the future?

On the question of labor, it is also difficult to imagine that national public sector employment policies will generate jobs and incomes at a scale and rate commensurate with urban growth. Debates about employment creation extend back for two generations – to Keynes, to ILO reports on the informal sector, and later to the United Nations Social Summit in 1995. Not having identified effective policy and program solutions, many specialists on employment have been left to celebrate the positive features of the informal sector, without completely acknowledging the many disadvantages that the informal sector brings with it, whether in terms of security of employment, benefits, regulatory protections, and professional growth. Successive summits on employment policies have not yet generated a set of policy recommendations or actions which have had much impact on this problem.

Finally, how is urban land related to these problems? Is urban land a necessary or sufficient condition as a platform for either capital formation or employment creation? Is land use policy an independent or dependent variable in this equation? How critical is urban land to determining the dynamics of value, cost, and price in other sectors of urban activity? What are the possible combinations of land with these other production functions?

There are no magic solutions to these problems. Rather, we need to examine more deeply, in a broader comparative, empirical framework, what is happening to capital and labor in relation to urban growth. Further, I believe that capital and labor need to be linked together to generate urban economic multipliers which can help to create new kinds of employment while also allowing the deepening of local financial sectors. The role of land and land policies necessarily is central to this process.

Among the many suggestions about land is a recent proposal by Shlomo Angel and his colleagues in Ecuador, reviving a proposal which was discussed, for example, in Tanzania in the 1970s, that residential areas for future development be “traced” in order to “guide” urban development and to provide a framework for future investment in urban infrastructure networks. Infrastructure investment, such as roads, drains, telecommunications, electricity, water supply, and sewerage, is an example of how land development policy can support the process of urban capital formation.[13] This approach may help avoid the scenario in which many new urban residents will find themselves living in settlements unconnected to trunk infrastructure networks, beyond municipal jurisdictions, and inhabiting "de-linked" urban communities on the urban periphery. There are many examples already of this type of settlement in Latin America and other regions.

In order to explore these twin issues of urban capital and labor in more depth, two examples - urban China and urban Africa - may be helpful in thinking about what might be called the "urban crises of capital and labor" in cities in developing countries.

- Urban China:

Any contemporary Marco Polo visiting urban China in the last few years cannot help to be impressed by the enormous construction boom in Beijing or Shanghai, a dramatic indicator of China's extraordinary economic growth. Beijing now has more than 200 multi-storey buildings over 50 floors under construction, while Shanghai has had 4,000 multi-storey buildings built since the mid-1980s[14]. Observers of China's macro-economic performance recognize that the urban share of China's GDP is increasing, much like European countries throughout the 19th and 20th centuries and other East Asian economies since the mid-1970s.[15] This growing urban role is even more extraordinary given the aggregate growth of the Chinese economy, which has increased from a GDP of $150 billion in 1978 to $2.2 trillion in 2005.[16] Indeed the rate of urban economic growth has exceeded the rural sector, as China has become the factory of the world. One study notes that, "although only 42 percent of China's population is classified as urban, 88 percent of the GDP is generated through non-farm activities, the bulk of which are located in urban areas."[17] This pattern is similar in Japan, Korea, Singapore, and Thailand, where, for example, Bangkok already was contributing 36 percent of GDP in 2000.

Projections of Chinese urban growth indicate that by 2020, more than 55 percent of the total Chinese population will live in cities, or about 800 million persons.[18] The rural-urban migration process will continue, if not accelerate, as the rural *hukou* permit scheme will be increasingly difficult to enforce, given rural-urban income differentials. This migration process involves many interesting issues, but for the purpose of this paper,

---

[13] Shlomo Angel et al,….
[14] Edward Denison and Guang Yu Ren, Building Shanghai: The Story of China's Gateway, (London: Wiley-Academy, 2006), p.15
[15] Shahid Yusuf and Kaoru Nabeshima, Postindustrial East Asian Cities: Innovation for Growth, (Washington and Stanford: The World Bank and Stanford University Press, 2006)
[16] World Bank data
[17] Yusuf and Nabeshima, op.cit., p.75
[18] Mats Andersson, China City Development Strategy Program 2000-2005, (Washington: Cities Alliance, 2005)

what is significant is a continuing stream of rural migrants looking for urban employment.[19]

One of the most visible indicators of this urban growth is the construction boom. The case of Shanghai illustrates this most vividly. As noted above, since the opening of the Chinese economy in the mid-1980s, more than 4,000 multi-storey buildings have been built in metropolitan Shanghai. Construction and real estate now account for more than 12 percent of Shanghai's GDP, with the construction sector averaging growth rates of 23, 16, and 14 percent for the periods 1990-95, 1995-2000,and 2000-2003.[20] Five factors have contributed to this phenomenal growth: heavy investment in urban infrastructure and housing as China's population undergoes an urban transformation; heavy requirements from the design, engineering, and construction materials industries; industrial restructuring in the Shanghai metropolitan area; construction has become a leading sector in the macro-economy as a whole, thereby generating backward linkages; and that the construction sector allows firms of all sizes.[21] Indeed, most startling of all is that "almost 20 percent of China's GDP is absorbed by construction and real estate."[22] The home-building market grew by 18.7 percent annually from 2000 to 2004.[23]

Any observer of this situation, however, is prompted to ask whether and how this growth will be sustained in the future? Is this performance actually a relatively short-lived housing bubble, fed by foreign direct investment? Is high investment in urban housing and infrastructure the only possible outcome of the combination of large-scale flows of FDI, high savings, low wages, and low consumption? Or, put differently what are the downsides of this combination of factors? And what are some of the negative externalities which it is producing, such as increasing inequality between rural and urban areas, as well as within urban areas? Despite its phenomenal growth, China still has some 600 million people living below $2 per day, or 21 percent of the world's total.[24] While these questions lead to worries about over-leveraging of the financial system and over-investment in housing, they also suggest that there may be some problematic aspects of the labor situation in this sector. For example, is this a process fundamentally of underpaid illegal migrant labor building luxury apartments for the upper-class Chinese elite? If so, what are the social and even political limits to this situation? And, from another perspective, what might be the consequences for the quality of construction of these projects?

Asking these questions helps to place this phenomenon into a more dynamic perspective in which the composition of the Chinese economy itself is changing, and particularly in urban areas. At the same time that high growth is occurring in the construction and real estate sectors, employment in manufacturing is beginning to level

---

[19] Gordon McGranahan and Cecilia Tacoli, Rural-Urban Migration in China: Policy Options for Economic Growth, Environmental Sustainability, and Equity, Rural-Urban Interactions and Livelihoods Strategies Working Paper 12, (London: International Institute for Environment and Development, 2006)
[20] Ibid., pp.241-242
[21] Ibid, pp.243-245
[22] Ibid, p.244
[23] Ibid., p.242
[24] Quoted in Nancy Barry, -----

off or decline in some Asian cities, such as Tokyo. Manufacturing is being replaced by services, with gradual increases in finance and higher technology industries. The composition of urban GDP is thus shifting. In addition, higher urban land values and negative externalities in the largest cities can lead to their de-concentration to smaller urban areas where costs are lower. These negative externalities include urban pollution. The issue here is that there will be a high demand for jobs from growing urban populations and the challenge will be how to manage employment growth within individual sectors, within particular urban areas, and within countries.

If Chinese economic growth has been impressive since the late 1980s, how susceptible is this growth to changes in global financial and economic conditions? By 2006 FDI flows reached US$63 billion[25]. China accounted for 16 percent of the total GDP of countries classified as emerging markets.[26] Like other East Asian economies, China suffered in the 1997-1998 financial crises, although much less at the time than the highly open and liberalized economies of Korea and Thailand. But what will happen to flows to China if crises of the type we are currently experiencing in the sub-prime mortgage markets in the United States continue? How sensitive will be urban investments to the price and availability of capital if there is truly a global credit squeeze as seen in August 2007? Phrased more broadly, how will countries with liberalized financial sectors feel changing prices in global credit markets? How will these changes affect the pace and composition of urban investment and urban capital formation?

While the Chinese case raises many questions, it suggests the following conclusions which challenge urban conventional wisdom:

- high rates of capital formation are possible in cities in poor countries
- housing and infrastructure sectors can attract global capital and local savings
- growing urban incomes can allow growing effective demand for housing and hence spur housing investment
- the construction sector can become a major engine in the urban economy, again confirming that an important "business of the city" is "building the city", as suggested by American economist Laughlin Currie in Colombia in the 1950s
- the construction sector can absorb large quantities of labor as well as ancillary services in the engineering, design, and construction materials sectors
- the construction sector can generate urban economic multipliers which can stimulate other forms of urban investment and consumption,
- this process of capital formation does not necessarily involve tradeables
- <u>however</u>, high levels of capital formation may also bring other problems, such as unfair wages and growing inequality
- patterns of capital formation will depend on a combination of factors, some local and some possibly global, and may also be susceptible to exogenous sources of volatility

[25] Xinhua News Agency, January 15, 2007
[26] Nancy Barry, op.cit.

These observations can be useful in considering other regions as well, including Latin America. If this process has transformed urban China, what are the constraints to it occurring in other countries? While no countries are receiving the same magnitude of foreign direct investment and other flows as China – and China may be *sui generis* in other respects as well -- there are other sources of these flows to developing countries – such as remittances -- which also deserve consideration in the capital formation process.[27]

- Urban Senegal:

The case of urban Senegal is at the other end of the spectrum of economic growth and opportunity. The process of urban growth in that country was described by Senegal's Deputy Director of Urbanism as "*urbanization dependant*". He explained that urban public investment in Senegal – in water supply, roads, public spaces, schools, clinics, and other facilities -- came from the international community, from the French Government, the European Union, or the World Bank, while private investment, mostly in housing, came from remittances from the many Senegalese working abroad in France, Italy, or the United States or from foreign investors from the Middle East.[28] The Government of Senegal had very few of its own resources to invest in urban infrastructure or social services.

In contrast to this highly dependent situation, there were almost no locally-generated investments. With high urban unemployment and low rural productivity and incomes, the Senegalese economy was unable to generate surpluses which could be invested in the city. Despite macro-economic performance which was above average in Africa – with GDP growth at about 5 percent from 1995 to 2004 – the country could not generate funds to meet its needs for capital. In contrast, the 1994 devaluation of the West African CFA had meant that dollars or *euros* earned outside Senegal are worth more than twice than they were before, adding further incentives for migration in search of remittances. This explained in part the tragic risks which many Senegalese accepted in traveling in dangerous boats to the Canary Islands as an illegal route of migration to Europe and a better economic life.

While the Senegalese situation differs from other African countries, for example large economies such as Nigeria or South Africa, the phrase "*urbanization dependant*" could also easily apply to Sahelian countries such as Mali or Burkina Faso, or to other smaller economies such as Cote d'Ivoire, Benin, or Togo. Most importantly the phrase focuses attention on the urban capital formation process and raises the obvious question of what needs to be done to make the urban growth process more endogenously-driven. One component of this dilemma is how infrastructure can be developed to support productivity of economic activities in Dakar and other African cities. At present there appears to be attention given to the economic costs of urban form, including travel time, energy costs, and other issues related to mobility and possible economies of

[27] World Bank, Global Economic Prospects 2006: Economic Implications of Remittances and Migration, (Washington: The World Bank, 2006), p.88
[28] Interview with Deputy Director of Urbanism, Dakar, June 28, 2006

agglomeration and proximity. Thinking strategically about land use is a crucial part of this puzzle.

Here the Senegal case – and specifically the city of Dakar with about 3 million inhabitants and very high male and youth unemployment – focuses attention on what might be called the crisis of labor. City infrastructure and land use policies must be part of a strategy to generate productive employment. Even if the absolute numbers of urban unemployed are tiny compared to urban China, they are nonetheless critical in terms of the lives of Senegalese and highly suggestive of the urban employment problem facing youth all over Africa. Simply put, how long can we reasonably expect that increasing shares of the urban population to accept not having jobs and not being able to generate incomes for their families and themselves? If this situation is tragic for individuals and households, it is also wasteful and inefficient for countries and economies.

Conclusions and Questions for Latin America

The above analysis suggests the following conclusions and some questions for research in Latin America:

Urban Capital:

- Urban capital formation is possible.
- There is a need for more research and policy attention to specific constraints on capital flows for urban uses.
- Can remittances to Latin America be used for urban investment?
- There are huge benefits of urban investment in construction for urban economic multipliers.

Urban Labor:

- Some economic research in Latin America suggests that the informal sector brings high macro-economic costs and is a major drag on return to investment and economic growth.
- Urban employment policies have been given low priority by governments.
- Informality appears to reduce the productivity of labor and capital.
- Intra-urban inequality requires more economic research.
- Growing urban crime in Latin America brings high macro-economic costs.

Urban Land:

- How can urban land policies help address the crises of capital and labor in Latin America?
- Can urban land policy discussions shift from being ends in themselves towards appreciating their integral role in macro-economic performance?

- How can urban land strategies help reduce the polarization of metropolitan areas into slums and gated communities?
- How can urban land be bundled with capital and labor to increase capital formation and employment generation?

These conclusions and questions for research are neither comprehensive nor definitive, rather they suggest that urban land is part of a wider process with capital and labor and that land policy studies need to make a greater effort to link with these challenges.