THE URBAN IMPACTS OF FEDERAL POLICIES:
VOL. 1, OVERVIEW

PREPARED UNDER GRANTS FROM THE CHARLES F. KETTERING FOUNDATION
AND THE U.S. DEPARTMENT OF HEALTH, EDUCATION, AND WELFARE

ROGER J. VAUGHAN, ANTHONY H. PASCAL,
MARY E. VAIANA

AUGUST 1980
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This report summarizes the findings of a Rand Corporation study of both the intended and unintended urban effects of federal policies. The study had three purposes: to establish a conceptual framework for assessing the effects of federal actions on urban areas; to synthesize the results of existing research on the subject; and to evaluate the adequacy of current knowledge for anticipating the effects of future federal policies.

The research individually examined three major sectors of the urban economy that are affected by federal actions: the private business sector, the residential sector, and the local public sector. The findings are presented in three Rand reports:

- *The Urban Impacts of Federal Policies: Vol. 3, Fiscal Conditions*, by Stephen M. Barro, R-2114-KF/HEW, April 1978; and

The intended audience for these reports includes federal policymakers and their staffs, state and local government officials, and others who are interested in understanding, anticipating, or influencing federal policy decisions that have consequences for urban areas. The reports should also prove useful to researchers in urban economics and related fields and to public and private agencies that sponsor urban research. The three sectoral reports have been conceived of as resource documents that review evidence from the relevant research literature.

This summary report, less technical and detailed than the others, has been prepared to make the results of the study available to a wide audience of public officials and others concerned with urban affairs.

The research was conducted under a grant from the Charles F. Kettering Foundation, with supplementary funds provided by the Department of Health, Education, and Welfare.
SUMMARY

Federal policies and programs have strongly affected American cities. The consequences of explicitly urban policies, however, have been swamped by unfolding market forces and by the ramifications of programs designed to achieve other ends.

Market forces have stimulated employment and population growth in both the Sunbelt and West at the expense of the Northeast, and in suburbs at the expense of large central cities. Among the major forces behind that deconcentration are technological change, especially the increased use of truck and automobile transportation, and innovations in communications; rising incomes, with a concomitant rise in the value that households place on residential amenities; and changing world trade patterns, in which many industries in the Northeast have lost their erstwhile competitive advantage to foreign nations.

Although decentralization stems basically from market forces, a combination of federal policies has strengthened their effect. The most influential of these policies were not expressly designed to help cities; yet non-urban federal policies have profoundly affected the health of the older urban areas. Though inadvertent, the effects have mostly been adverse. Federal policies have lent further impetus to the movement of jobs and people from the Northeast toward the South and West, and from the central cities to the suburbs. These policies were largely formulated to achieve goals in the areas of transportation, public housing, regulation, taxation, and the like. This report provides an inventory of federal policies that affect cities and shows how the policies are linked to urban outcomes.

Federal urban strategy in the future should try to determine: how much of the urban problem results from "natural" readjustments and how much from the inadvertent effects of government policy; whether the federal government should attempt to ameliorate conditions resulting from market forces and inadvertent policies; and which policy mechanisms are most germane to the chosen federal role. In deciding the latter, policymakers must clearly determine when the problem lies in the clustering of disadvantaged people in urban areas, in the obsolescence of certain urban economies, or in the inadequate tax bases of central cities. Failure to distinguish among these sources of distress can worsen matters.
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Within the Rand Corporation, Stephen Barro provided the analytic structure of the study. Bryan Ellickson, Thomas Glennan, Ira S. Lowry, David Lyon, Peter Morrison, Georges Vernez, and Barbara Williams have helped to formulate the issues and present the analysis.

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¹The positions listed are those that the panel members held during 1976; they are not necessarily their present positions.
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I. INTRODUCTION

THE URBAN PROBLEM

The period since World War II has seen a disheartening decline in the fortunes of many of the nation’s cities. Shrinking populations, job losses, and fiscal weakness are interwoven features of the cities’ plight. Firms have abandoned central city factories to build near suburban freeways. In 1948, the suburbs accounted for one-third of metropolitan employment; that figure is now more than one-half. New businesses have chosen to locate in the Sunbelt rather than in the traditional areas of economic concentration. The most distressed cities, as measured by employment and per capita income trends, are heavily concentrated in the old manufacturing belt: New England, the Middle Atlantic states, and the East North Central states. Affluent households have moved into sprawling suburban developments, leaving the central cities to a growing concentration of the poor. Among the largest American cities, 44 lost at least 10 percent of their population between 1950 and 1975; in the same period, central cities lost 3.4 million white inhabitants and gained 1.2 million nonwhites, who now constitute a quarter of all city residents. Local taxes have climbed. In 1953 in the average state, nonfederal taxes absorbed only about 8 percent of personal income; by 1975, the bite was about 13 percent.

People who live in a declining city are painfully aware of the urban problem. Families face rising crime rates and pay rising property taxes; their children attend deteriorating schools. Firms operate in old buildings, have trouble finding skilled labor, and suffer from inadequate transportation services. Public officials are caught between declining tax bases and growing demands for public services. They have little patience with those who ask whether the urban problem is a federal issue. Enough places and people are affected to make the problem national in scope.

In a sense, leaving the problem unintended makes us all worse off because it inflicts social and economic costs on the nation as a whole. In many municipalities, almost 15 percent of the population is on AFDC. Crime proliferates. In Detroit, almost one in ten black males can expect to be robbed in the course of a year. Vandalism in schools now costs about $600 million annually. Decreased demand for traditional city functions has devalued downtown property. The cost of maintaining public capital, paying public workers, and meeting future civil service pension obligations will fall on a decreasing number of central city inhabitants. And as tax bills rise but school quality and public safety slide downward, all but the most immobilized are pushed out.

Clearly, a large share of urban deterioration is due to changes in consumer preferences and production technologies. But federal policies, as we will see, have also influenced the fortunes of cities. Damage to traditional cities has frequently been the result of policies designed to achieve other objectives. These inadvertent consequences have stimulated demands for new, ameliorative policies.

Urban troubles do not necessarily mean that there should be a federal policy to “save” cities, however; for one thing, help for distressed cities might impose costs on other locations. Consider, for example, a middle-income family that leaves a central city for a suburb. To those remaining behind, the move may represent a
loss: Local firms lose customers, the supply of skilled labor decreases, and the local tax base declines. The suburb, however, reaps a corresponding gain. The very fact of the move suggests that the family itself has gained, or at least expected to.

Thus, to the extent that urban decline reflects household preference for suburban living and the corporate exploitation of the technological advantages of dispersed locations, the case for a major federal effort to save cities—as opposed to helping people who happen to live in cities—must be based upon the explicit judgment that the values of urban life justify the costs of the proposed remedies. If, however, as this report argues, urban decline is not simply a "natural" phenomenon but is partly due to the largely inadvertent antiurban bias of federal policies, then a case can be made for federal urban assistance to redress the bias. The urban policy debate must be informed by a full understanding of how federal policies have affected cities.

THE FEDERAL RESPONSE

The federal role in urban affairs for the past two decades has changed along with definitions of the urban problem. Many federal programs aimed at big-city problems had insignificant effects. A second class of programs succeeded in stimulating growth but, over time, injured either the big cities or the Northeast or both. Yet a third class had no particular urban objectives but worked to the disadvantage of America's central cities. The following abbreviated history of the federal response to changing perceptions of regional and national needs illustrates the interplay of the first two classes of federal programs. The remainder of our study analyzes the third class of programs.

In the 1950s, the urban problem tended to be defined as crowding in the central cities on the one hand, and on the other hand a suburban infrastructure inadequate to accommodate rapid suburban growth. The interstate highway program was designed to achieve many purposes, including civil defense (because it dispersed population), but it was also a response to that definition of the urban problem. Subsidies for the purchase of new suburban housing was a related program intended to reduce crowding. Another was urban renewal, a program designed to improve the physical conditions of cities and to increase the supply of housing for their low-income residents. But many residents were displaced from their original housing and moved to marginal areas, often bordering the original slum, where the cycle of low rents and disinvestment often led to a new cycle of deterioration and eventual abandonment.

During that period, major policy attention was directed to alleviating poverty and stimulating growth in rural areas and in the South. Such policies aided cities only insofar as they reduced people's necessity to migrate. Huge water projects were undertaken to open landlocked Southern cities to supplies of raw materials and to the benefits of international trade. The Appalachian Regional Commission, established at the end of this period of rural focus, built highways and industrial parks in small towns, and funded training programs to help local industry and to staunch the northward flow of rural migrants. It was believed that such problems as cities did experience were transitory, and that rapid national growth would erase urban poverty and unemployment. To some extent, those beliefs were justified. Northern cities generated jobs for most of their in-migrants, and rapid suburbanization eased the problem of overcrowding.
By the mid-1960s, however, it became apparent that national economic growth would not eradicate the swelling pockets of urban poverty and decay. Many large metropolitan areas had ceased to grow. The disparity between affluent, white suburbs and poor, black central cities became an important political concern. One policy response was a war on poverty fought on several fronts: improved social services, education and training programs, antidiscrimination efforts, and, later, increased transfer payments. The policies were “urban” primarily because so many economically disadvantaged people lived in cities. In contrast, the problems of declining urban economies—their needs for capital, infrastructure, market access—got little attention. In fact, most of these programs helped the poor where they lived: Public housing was built in central cities; urban areas offered more training programs, social services, and public transportation subsidies; city governments actively hired minorities. As a result, economically disadvantaged people who once might have located elsewhere were encouraged to move to or to remain in central cities.

By the end of the 1960s, programs to upgrade the tangible capital stock of cities had gained prominence once again. Later, Model Cities funds were used to clear areas of dilapidated housing adjacent to central business districts, and then to build commercial structures and, often, middle-income housing. The Urban Mass Transit Administration provided grants for new rail systems. The Economic Development Administration funded inner-city industrial parks. But such programs were much too small to make more than a dent in the cities’ massive economic problems.

In the early 1970s, the Nixon administration’s New Federalism shifted responsibility for problem-solving back to local governments. The Comprehensive Employment and Training Act (CETA), Community Development Block Grants, and General Revenue Sharing are examples of new federal assistance programs that embodied the shift. Encouraged to assume more program control, local decisionmakers used some part of their newly acquired resources—which came directly to them and not, as before, through state channels—to relieve burdens on local taxpayers. Such uses of federal funds made it clear that fiscal problems had become a dominant concern among local officials.

While the move to fiscal relief and local control was under way, it became apparent that new federal initiatives in such fields as environmental regulation, occupational health and safety, affirmative action, and school desegregation were heavily affecting urban development. Antecedent federal policies in such fields as taxation (e.g., homeowners’ deductions, business investment credits), natural resources, defense procurement, energy and transportation rate regulation, local infrastructure subsidies, and public assistance continually worked to favor some cities and to disfavor others. Thus, the postwar period made evident:

1. That the federal government’s deliberate attempts at urban improvement had achieved ambiguous results;
2. That some federal activities designed with other, often worthy, ends in mind wrought unanticipated and deleterious side effects on particular types of cities; and finally,
3. That many urban economies were peculiarly vulnerable to national business cycles, such as the recession that began in the mid-1970s.
Spokesmen for the big cities' interests began to argue that a real, if inadvertent, antiurban bias permeated federal policy. Some went so far as to label it "implicit" or "hidden." At the least, the situation seemed to call for a reconsideration of how the federal government influences urban conditions.

DESIGN OF THE RAND STUDY

To clarify the issues, Rand undertook a more systematic examination of the ways in which federal policies have affected cities. The study confirms the suspicion that federal policies have contributed to urban problems. The analysis provides the first steps for a strategy to ameliorate this situation. First, it identifies the extent to which urban problems are beyond the remedial powers of local governments. Market forces and the concatenation of federal policies are the fundamental factors in urban change. Second, it describes the range of program levers that the federal government must pull to assist cities. To fine-tune existing urban programs or increase revenue-sharing grants would do little to alter the urban predicament.

As we will see, formulating an effective federal strategy to assist either urban areas or their residents requires an understanding of how federal actions influence the decisions of households and firms about where to locate. A wide spectrum of federal policies and urban outcomes must be considered. The analysis must include the recognition that some of the most important relationships between federal policies and urban effects are indirect. For example, a direct policy such as the decision to expand HUD's Community Development Block Grant program will directly ease the local fiscal burden and add to the inventory of local public capital. These changes could enhance the residential environment in cities and thereby encourage settlement there. The central-city housing market, however, could be more strongly stimulated by an indirect policy: altering the income tax treatment of renters to give them the advantages that homeowners enjoy.

Policies affect locational decisions in ways so complex that it is infeasible to try to analyze either the full range of urban outcomes or the full array of federal policies simultaneously. Therefore, we partitioned the problem in order to establish a manageable research design.

The urban economy, as defined in this study, consists of three distinct but interacting sectors: the private business sector, the urban public sector, and the residential sector. Rand has published three reports corresponding to those sectors (see Preface). This report summarizes their main findings.

Our research consists strictly of analysis of existing data and models. No new data are presented and no new empirical analyses are undertaken. Because little of the existing literature specifically treats the urban effects of federal policies, we have had to exercise ingenuity in winnowing potentially relevant findings. Extant research ranges from case studies of particular cities to sweeping reviews of national urban trends; consequently, it has been difficult to assemble consistent evidence on specific issues or to offer generalizations that apply to entire classes of cities. Since empirical evidence for many of the key relationships is lacking, we developed a conceptual framework to fill gaps and to give coherence to what would otherwise seem isolated and unrelated findings.
This report provides an inventory of federal policies that influence cities, defines how policies are linked to urban outcomes, and draws on both theory and empirical data to assess the likely direction of federal influence. Section II diagnoses the urban problem. Section III presents our conceptual framework and summarizes the urban effects of market forces and of federal policies. Section IV suggests the implications of our findings for both federal and local urban strategies.
II. DIAGNOSING THE URBAN PROBLEM

An effective federal strategy to assist cities depends on how the urban problem is defined. We must first distinguish the targets for assistance. Are we concerned about pieces of geography, entities of government, or clusters of people?

Proponents of the geographic definition of the problem argue that certain cities suffer because they have lost the modern infrastructure, attractive environment, and locational advantages they once boasted. Those taking this position can be divided into two classes according to whether they stress interregional or intrametropolitan dimensions. The regional imbalance is emphasized in the Sunbelt/Snowbelt dichotomy. The intrametropolitan camp argues that central cities simply cannot compete with the suburbs because their housing stock, industrial base, and transportation facilities are badly aged.

Those who adopt the view that the problem lies with outmoded government organization argue that fixed boundaries separate city governments from their tax base, and that local resources in the core entity cannot meet local public service demands.

Proponents of the "people problem" view argue that the urban crisis stems from the spatial concentration of the economically and socially disadvantaged. The demands for social services that must be met, at least in part, from local taxes, combined with the concomitants of poverty—crime, blighted housing, and poor labor skills—diminish the attractiveness of cities as places to live and work. Households that can afford to leave migrate to more desirable environments, thus reducing the tax base and stunting economic development.

There is evidence to support all of these viewpoints. Urban reality is complex, but getting the problem definition straight is a prerequisite to effective policy design. For example, fiscal relief through revenue sharing may be sold as a program to help the disadvantaged. In reality, jurisdictions are more likely to use it as a windfall for taxpayer relief. Manpower training, in contrast, may improve employment prospects for some of the underemployed, but it is unlikely to enhance the quality of the labor pool enough to attract new firms to the local economy. Rarely can a single program address all three sorts of problems. Declining areas can best be helped through programs to improve the residential and business environment; jurisdictional problems respond to fiscal and technical assistance to the local units of government; people problems may require income transfers, training, and relocation assistance.

Here we review briefly some of the more important elements of policies designed to address each of these problem categories.

PLACE PROBLEMS

In recent years, there have been calls for a federal policy of urban conservation
or a national policy on urban settlement to help redevelop declining areas. These are among the federal policies advocated:

- Stimulating the demand for locally produced goods and services:
  - Direct the federal government to purchase goods and services from designated urban areas
  - Augment local purchasing power by pumping in money (e.g., through grants or transfer payments)
- Improving the comparative economic advantage of the area:
  - Construct a new economic infrastructure, including industrial parks, transportation linkages, and capital facilities
  - Subsidize transportation costs for both goods and people
  - Improve municipal services
- Enhancing the urban environment:
  - Encourage housing renovation
  - Reduce crime
  - Control air pollution, traffic congestion, blight

JURISDICTIONAL PROBLEMS

If urban problems are seen as stemming from jurisdictional fragmentation, a different set of federal actions is appropriate:

- Mandating federal assumption of responsibility for welfare, education, and health services
- Encouraging metropolitan areas to share tax bases in order to stem the migration of affluent households seeking tax havens
- Assisting fiscally strained jurisdictions:
  - Increase revenue sharing from the federal government
  - Target other funds more effectively
- Helping local governments to develop more efficient techniques for planning and delivering public services

PEOPLE PROBLEMS

If the basic federal concern is with the plight of certain urban residents, and not necessarily with the economic and political entities in which they happen to live, then the policy implications are far different. In contrast to the geographically or jurisdictionally oriented views, people-oriented policies begin with the view that saving the cities is only a means to an end. Municipal fiscal relief and support for urban economic development would therefore be judged according to whether they help people injured by urban decline. (Two very different types of policies are possible: those that provide additional income for the poor, and those that enhance the employment prospects of the economically disadvantaged.)

1See, for example, the National League of Cities, State of the Cities: 1975—A New Urban Crisis, Washington, D.C., 1976.
People-oriented policies include:

- Assisting the disadvantaged directly through welfare and social security payments and unemployment compensation
- Training and educating workers to enhance their job prospects
- Broadening the economic and housing options of inner-city residents:
  - Provide affordable housing outside the central city
  - Improve transportation from inner cities to decentralized workplaces
- Reducing the concentration of “problem” populations in the declining cities:
  - Reduce the differences in benefits that inhibit movement from the Northeast to the suburbs and the Sunbelt.
  - Provide social services so that residents may cope with a blighted environment.
- Providing incentives to private employers to hire economically disadvantaged workers.

AN INTEGRATED VIEW

Although the policy approach must emerge from the diagnosis of the problem, it is possible to conceive remedies too narrowly. For instance, programs directed at helping people may spill over to improve places, e.g., by expanding local markets. Aid to the business sector alleviates jurisdictional problems by expanding the tax base. Thus the less immediate, less direct, and less visible policy effects, which may be as significant as the direct effects, often receive inadequate attention. Few recent policy proposals, for example, take account of the locational incentives imbedded in many programs. Compared with emerging locational preferences wrought by market forces and by inadvertent policies, flows of direct federal aid may not be very significant.

Policymakers have good, practical reasons for emphasizing programs that work directly to aid people and businesses already in the cities. Some of the reasons are political: Direct programs seem quicker acting, are more visible to voters, and usually place funds in the hands of local public officials who can use the money to ease their fiscal and staffing problems and reap the political benefits of disbursement. But there are also cognitive reasons. It is easier to understand and design direct-aid policies and to analyze their short-term effects than it is to work out locational incentive schemes and trace the long-term consequence of more subtle modes of intervention. Doing the latter means making a transition from asking “who gets how much” to asking how the recipient's behavior will change because of altered circumstances.
III. ANALYZING FEDERAL POLICY IMPACTS

FRAMEWORK FOR ANALYSIS

Our first task in analyzing the effects of federal policy on cities was to construct a framework comprehensive enough to encompass both the wide range of federal policies that might conceivably influence cities and the many ways in which they could do so. We began by disaggregating the nebulous concept of the city into operational sectors—the local public sector, the local business sector, and the local household sector. Each is inhabited by a different decisionmaking unit: local government, the firm, and the household. And each sector is influenced directly by a distinct subset of federal policies.

Besides direct influences, a given sector also responds indirectly to many other forces, including, importantly, the behavior of the other two sectors. For example, when local businesses receive a new federal procurement order, they will fill job openings. Rising local wages may increase labor force participation and attract workers from less buoyant labor markets. The increase in the number of workers expands the local tax base and raises the demand for schooling and new housing. And the increased demand for goods and services stimulated by the swelling population may lead to further expansion of the labor market. Figure 1 summarizes this complex pattern of direct and indirect interaction among the three sectors.

Fig. 1—Conceptual framework
Determining the effects of federal policies on any one sector required that we first identify the set of direct linkages between that sector and the relevant subset of federal policies. Second, we had to identify the indirect set of federal influences that acted through induced changes in the other two sectors.

We attempted to identify these linkages in a three-stage analysis, whose components are shown in Fig. 2 for the case of federal policies that affect the price of labor.

First, we distinguished the major outcomes in each sector (right-hand column of Fig. 2). These outcomes reflect the behavior of that sector and are important to federal and local officials, as well as to the city's inhabitants. For example, when we examine the effects of federal policies on the business sector, the outcomes of primary interest are levels and rates of change in employment, wages, output, and investment—the most important measures of economic activity. In the residential sector, the principal outcome variables are the size, composition, and spatial distribution of the population, and the quality of housing. In the local public sector, the main outcomes are the level and mix of public services and the magnitude and composition of the tax burden.

These outcome measures can be used to answer questions on how development has differed among groups of cities. For instance, how has employment growth

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**Fig. 2—Illustration of three-stage analysis of federal policies affecting the price of labor**

- **FEDERAL POLICIES AFFECTING PRICE OF LABOR**
  - Expenditures
    - Training programs
    - Federal employment
    - Transfer payments
  - Tax structure
    - Personal income tax
    - Business tax
  - Regulations
    - Minimum wage
    - OSHA
    - Affirmative action

- **CHANNELS OF INFLUENCE**
  - Demand for local product
    - Local
    - National
    - Public sector
  - Factors of production
    - Transportation
    - Land
    - Labor
    - Capital
    - Energy
    - Local public services

- **OUTCOMES**
  - Business sector
    - Industrial location
    - Employment growth
    - Investment
    - Wages
    - Output
  - Residential sector
    - Population growth & characteristics
    - Housing quantity & quality
  - Local public sector
    - Level & type of public services
    - Level & incidence of local taxes
differed among Snowbelt and Sunbelt cities? How do central-city and suburban households differ in ethnic and demographic characteristics? How does the tax burden differ between large and small cities?

Next, we identified the channels through which various policies affect the outcomes for each sector (middle column in Fig. 2). Most federal policies create indirect incentives for changes in economic behavior.

Moreover, the sectors are interconnected in complex ways. For example, the local business sector depends on the local household sector because households affect the demand for goods and services and also because households provide the labor force. The actions of local governments influence firms through the tax rate and through the quality of public services such as training programs, loan programs, and sewer, water, and transportation services. But the influences flow both ways. Households respond to the local business sector by migrating toward good jobs and high wages. The local public sector relies on local firms to foot some of the tax bill.

Finally, we examined each determinant to establish those policies that we expected to be influential (left-hand column in Fig. 2). For instance, the price and availability of labor are influenced by federal transfer payments such as welfare and unemployment compensation, by training programs, and by direct federal hiring. Both personal and business tax structures also influence the operation of the labor market. Personal income taxes affect a person's desire to seek work, while business taxes affect the cost of labor relative to capital. Regulations such as the minimum wage law, safety and health requirements, and affirmative action measures also influence business hiring decisions.

We undertook this analytic process for each of the outcomes in each sector. However, our ability to identify the determinants of outcomes differed significantly among the sectors. Analytic models for employment growth and industrial location are relatively well developed, but less is understood about what influences people's choices of where to live. And very little is understood about the factors that affect local government decisionmaking. Thus the tasks for each of the three sectors differed. In most cases, we were able to identify only the direction of the effect, not its magnitude.

This framework made it possible for us to synthesize the findings of many studies that analyzed small pieces of the overall network, even though few of those studies dealt directly with the impacts of federal policies. For example, to connect federal transportation policies with regional shifts in employment, we integrated two bodies of research: analyses that linked transportation policy to changes in transportation costs, and analyses that related transportation costs to the distribution of economic activity. Of course, this synthesis inevitably involved weighing the conflicting results of different studies.

The three Rand studies that this report summarizes tend to confirm the hypothesis that federal programs have stimulated employment and population growth in both the Sunbelt and the West at the expense of the Northeast, and in suburbs and smaller urban areas at the expense of large central cities. Federal policy has also contributed to the growing concentration of the poor in central cities and to local fiscal problems. These federal effects have exacerbated trends that emerge from market forces. We first review the major market forces, then summarize the major findings on federal effects.
MARKET FORCES

The major forces behind the continuing trend toward decentralization have been market forces:

- Technological change
- Rising incomes and changing tastes
- Changing world trade patterns

Below we discuss some of the components of these forces.²

Technological Change

The production of new goods and the adoption of new techniques of production have favored developing areas at the expense of more established industrial centers. It is difficult to quantify the contribution of individual phenomena, but among the most important are:

- Transportation developments. The most powerful single influence on the movement of jobs out of congested urban areas has been the increased use of truck transportation for freight and the automobile for commuting. Because firms are no longer tied to rail spurs and mass transit links, they have greater freedom to locate where land is cheap and plentiful.
- Linear flow plants. Modern production techniques use single-story production facilities. Increased space requirements have encouraged firms to move out of cramped, vertical, inner-city factories to suburban sites where land is cheaper.
- Increased complexity. As products have become more complex, raw materials have become less important than processed inputs. Firms have moved away from the sources of raw materials—e.g., coal and iron ore—in the Northeast toward their growing markets in the South and West. The decline in the transportation component of product cost has made this decentralization efficient.
- Air conditioning. The development of “manufactured” climate has meant a comfortable working environment in the South. In addition, climate control is essential for certain new industries, such as those based on computers.
- Communications. Computer technology has reduced the cost of transmitting, storing, and processing information to a fraction of its former level. Advances in telecommunications reduce the need for face-to-face contact. These innovations have weakened the spatial ties between establishments in multiestablishment firms and among firms, service suppliers, and customers. It has also reduced the need for clerical workers, thus freeing firms from the necessity of locating in high-density centers.

²Of course, these processes have been influenced by federal policies. Federally funded research has spurred technological change, federal management of the economy may have helped the growth in real income, and treaties and agreements with foreign nations have helped shape trade patterns. But federal influences over these trends have been relatively slight, and it is important to distinguish between their effects and those of more weighty federal policies.
Rising Incomes and Changing Tastes

Rising incomes and changing tastes have also contributed to decentralization in several ways.

- Higher income enables more people to own homes and automobiles, and thus increases the likelihood that a household will move to the suburbs where spacious new housing on large lots is available.\(^3\)
- Affluence and education have made households more conscious of the quality of their environment. They are choosing to move away from polluted, congested central cities with high crime rates, even when they must pay a premium for suburban amenities.
- Many households have moved to new urban areas in the Sunbelt that offer clean air, attractive climate, reduced density, and abundant recreational opportunities.

Changing World Trade Patterns

In the Northeast and North Central regions, urban areas producing goods that compete with imports have suffered job losses as world trade has expanded and the comparative advantage for certain products has shifted abroad. Examples are found in the auto and steel industries. In contrast, areas producing exports of computers and advanced electronics have grown rapidly. A disproportionate number of these high-technology firms are located in the South and West.

THE EFFECTS OF FEDERAL POLICY

Decentralization stems basically from market forces, but a combination of federal policies has strengthened their effect.

Federal policies are only rarely designed to affect specific areas; most are national in scope. How, then, can national policies have different effects in different regions? Geographic bias arises in several ways. Most obviously, procurement decisions and formula grants based on need will occasion geographically unbalanced spending. Defense receipts will spur local industrial development in economies specializing in aerospace. Transfer payments will raise local income in depressed areas. High per capita revenue-sharing grants will provide fiscal relief in some places. Imbalance in allocating funds means imbalance in effects.

The remainder of this section summarizes federal contributions to three trends that have contributed to urban problems:

- For the economic sector: the deconcentration of jobs.
- For the residential sector: the selective deconcentration of households.
- For the local public sector: the resulting fiscal problems.

\(^3\)The relationship is not simple. For a low- or middle-income household, an increase in income tends to be associated with an increased probability of living in the suburbs. For a higher-income household, an increase in income sometimes leads to a closer-in location, where residential amenities can be combined with savings in commuting time. The rise of the "non-normal" household—multiple workers, no children—has in some areas actually spurred a return to central city residence. Rising suburban land prices may eventually stimulate such behavior in other places.
Deconcentration of Jobs

Federal policies—capital investments, procurement, the tax structure, and even regulation—have encouraged the movement of jobs from the Northeast toward the South and West, and from central cities to suburbs and even nonmetropolitan areas. This consistent direction of influence has resulted, in large part, from the implicit or explicit favoring of growth and new development over rehabilitation and repair. The result has been that firms in growing areas have been stimulated to grow more rapidly. Some firms have been encouraged to move away from older central cities into these more favored areas. We consider both interregional and intrametropolitan effects.

Regional Shifts. The most obvious channel of assistance is capital investment, particularly the interstate highway system, which involved substantial interregional subsidies. Without this system, many areas in the South and West would remain inaccessible. Massive Corps of Engineers waterway projects have opened up many Southern cities to the benefits of international trade. Government spending matters, too. The rapid growth of defense payrolls has contributed significantly to economic development in areas remote from the old manufacturing belt.

Other nationally applied policies, however, including the tax structure and certain regulatory activities, have had a distinct regional impact on economic development even though economic development has not been a primary goal. The tax structure, for example, has favored growth in three ways. First, investment in new construction has traditionally been accorded more generous tax treatment than comparable investment in rehabilitation. (This differential was substantially reduced in the Tax Reform Act of 1976.) Second, tax-free industrial development bonds reduce the cost of constructing the infrastructure necessary for new expansion. Finally, investment tax credits subsidize expansion in already growing areas where most investment is undertaken.

There is some evidence that certain forms of regulation also affect the spatial distribution of employment, however unwittingly. For instance, holding natural gas to a price below the market rate has led to curtailed supplies in the Northeast. This has encouraged firms that are heavy users to relocate in gas-producing states in the South and Southwest where supplies are more certain.

Regulation of transportation rates and routes has also led to decentralization by artificially raising the cost of long-haul relative to short-haul transport and by subsidizing shipping on less used routes at the expense of those more intensively used. As a result, manufacturing plants have moved closer to their markets. They have redistributed themselves regionally in the process.

Suburbanization. The policies that worked to move employment out of certain regions also encouraged the rapid growth of employment in suburban or even nonmetropolitan areas at the expense of central cities. Again, the chief mechanism has been implicit and explicit subsidies to new investment. Federal subsidies help support the construction of roads, industrial parks, sewers, and rural electrification.

4However, it is largely a myth that the Northeast has been badly hurt by the outmigration of firms. Less than one job loss in 50 in the Northeast is attributable to outmigration. Most jobs have disappeared through the contraction or disappearance of local companies.
However, the most important influences have been inadvertent. For example, in computing business tax liabilities, land cannot be treated as a depreciable asset. Consequently, firms try to find sites where land prices are low—typically, in suburbs or nonmetropolitan locations. This incentive is reinforced through the favorable treatment of capital gains relative to ordinary corporate income, which has led firms to purchase large lots in areas where land prices are rising.

Selective Household Deconcentration

Federal policies have spurred the decentralization of the urban population as well as the decentralization of jobs. But the incentives engendered have not operated on all groups equally. The result: A growing share of the population of older central cities is poor, unemployed, and nonwhite.

Regional Shifts. Federal income transfer payments have facilitated residential movement from region to region. Through Social Security, the elderly have become less dependent on their families and have moved from the Snowbelt to more temperate areas. Interstate highways and flood control projects have opened previously inaccessible areas to residential settlement. Federal support for recreational facilities has been concentrated in the South and West. The location of military bases in the South has also led to an at least temporary relocation of households.

Suburbanization. Federal policies have stimulated selective suburbanization in two ways: They have encouraged the outmigration of more affluent households, and they have discouraged the outmigration of the poor.

While auto ownership has been growing, federally funded highways have expanded the commuting range. Water and sewer grants have reduced the cost of developing the newly accessible land.

The tax system subsidizes homeownership by allowing the deduction of mortgage interest and local property taxes from income tax obligations and by excluding the imputed value of owner-occupied housing from taxable income. This subsidization has reduced the cost of homeownership for those who itemize deductions, mostly middle- and upper-income households. New homeowners have shown a marked preference for a spacious residential environment and have moved away from densely populated central cities. Supplanting these pro-homeowner policies are FHA and VA mortgage guarantees, under which nearly one-fourth of all new homes have been purchased. The subsidies arising out of guarantees have been limited to new housing, which has meant, in effect, suburban housing.

Finally, there is mounting evidence in many big cities that enforced school desegregation through busing has speeded up the suburbanization of white households. “White flight” results in blacker central cities.

Inadvertently, federal policies have worked to keep the poor “in their place.” Because most public housing has been built in central cities, poor households have been discouraged from moving to the suburbs. Subsidies to low-income groups to promote homeownership have generally been available only for very low-cost housing, typically unavailable in the suburbs. At the same time, local building codes prevent the construction of cheap new suburban housing that might have provided, at comparable costs, alternatives to older units in the city.
The absence of uniformity in welfare payment levels and eligibility criteria has led to the concentration of the poor in cities offering high benefit levels. There is no evidence that high benefit levels have encouraged poor households to move to a city—jobs have usually been the goal—but nontransferability and high benefit levels do appear to deter those who have been unable to secure employment from moving to more promising labor markets. Public assistance payments do of course augment the demand for goods and services in the local economies where recipients live.

Local Fiscal Conditions

Federal programs and policies affect the local fiscal balance—tax base, tax effort, and service demands. The policies that directly affect revenues include federal grant programs and federal tax expenditures. Local expenditures are affected by imposed definitions of local responsibilities and by the cost-sharing features of grant programs.

Local revenues are influenced by federal actions in several ways. For instance, the federal government may subsidize ongoing local programs (as in the case of general revenue sharing), or it may assume full program costs (as it did for the Supplemental Security Insurance program), or it may offer cities inducements to assume new local responsibilities. The larger cities in particular are heavily dependent on federal aid. The fiscal situation is also affected by the form of aid (block or categorical, lump sum or matching); by the formula for distribution; and by accompanying state actions (control of “pass-through” funds, assumption of local programs, withdrawal from local programs funded directly by the federal government).

Federal income tax policy provides important, if implicit, subsidies to local and state government. More than $18 billion a year, or 26 percent of the volume of outright grants to state and local governments, arise from the deductibility of state and local taxes from federally taxable income and from the tax exemption of municipal bond interest. Localities are able to collect more revenues because they need not impose the full cost of collection on their residents—i.e., there will be less resistance to a rise in property tax to the extent that the tax payment is deductible on Form 1040. However, only a fraction of this federal tax expenditure translates into additional state or local revenue. The remainder provides benefits to individual federal taxpayers, particularly the high-income households to whom any given deduction is worth more.

There are several areas in which federal regulatory programs have imposed spending obligations on local governments or raised the cost of local public services. Notable examples in the first category are environmental protection, where federal aid for construction of pollution control facilities pays only part of the cost of meeting water quality standards, and treatment of the handicapped, where Congress and the courts have established rights to service without providing all the aid needed to defray the increased costs. In the second category, federal actions that

As we indicated earlier, our research in the local public sector has, of necessity, focused upon identifying the links between federal actions and local fiscal conditions, rather than assessing the impacts. A considerable part of our effort was devoted to identifying how future empirical research could be directed to defining local fiscal conditions, in both service demands and local revenues.
directly affect local service costs include regulation of energy prices and the requirement, under the Davis-Bacon Act, that "prevailing wages" be paid on federally aided construction projects. One proposal that could exert much larger long-run effects on the costs of local government is contained in a bill establishing a national framework for collective bargaining in the state and local government sector.⁶

Finally, the local political structure will help shape the impact of federal policy. When federal programs have loose "strings," local government themselves decide how to spend funds—they choose the projects and the neighborhoods. The capability of municipal and county officials also influences the ease with which the local economy adapts to underlying structural changes that are the result, in part, of federal policies.

⁶However, the Supreme Court's decision in National League of Cities v. Usery has delayed further efforts in that direction.
IV. CONCLUSIONS AND IMPLICATIONS

A proper diagnosis of the nature of urban decline is the essential prerequisite for improved policy. The problems faced by people who are stuck in deteriorating urban environments, and the problems occasioned by declining tax bases or shifts in comparative advantage that damage certain kinds of urban economies, have different causes and require different solutions. And although the business sector, the residential sector, and the local government sector are intertwined in a complex fashion, each requires a different mode of analysis and each demands a distinctive policy treatment. Below we attempt to draw out the essential implications for policy at the federal and local levels.

FEDERAL STRATEGIES

The evidence pieced together in this study suggests that a federal urban strategy must recognize three facts:

- The influence of federal policies over urban development is pervasive, and extends to almost all departments, agencies, and programs.
- In formulating policy, there is a tendency to neglect the effects of shifts in where households and firms choose to locate—the fallout from "non-urban" policies—and to concentrate on effects that alter the places to which federal funds are allocated—the consequences of consciously "urban" policy. Among the most influential determinants in the former category are many "non-budget" programs, e.g., tax expenditures and regulations, which are not typically thought of as development policies and which are not always subject to regular Congressional scrutiny.
- A great deal remains to be learned about the urban impacts of federal policies. We have uncovered no secret store of potentially pro-urban programs. If federal policymakers are to anticipate how policies will shape development in the future, further research must be undertaken on the geographic effects of federal actions.

On August 16, 1978, President Carter took a small but significant step toward improving the federal government's ability to understand the urban impacts of proposed new initiatives. Executive Order H-116 requires that

Urban and community impact analyses are to be prepared on proposed major policy and program initiatives identified by each agency. All types of initiatives should be considered candidates for this type of analysis, including new programs, expansions in budget outlays, program changes leading to shifts of resources among recipients, program changes affecting state and local governments, changes in tax provisions, new regulations, new regulatory authorities, and other changes in policy or program direction.
Two basic questions about Urban Impact Analyses (UIAs) spring to mind: (1) Is the Executive Order the right way to raise federal urban consciousness? and (2) How should UIAs affect policy decisions?

UIAs have been criticized on several grounds: They are prepared by the agency advocating the new initiative and might therefore be self-serving, and because they are not public documents they may disappear during the budgetary negotiation process.

There are certainly grounds for fearing that the analyses may be self-serving. Impact analyses performed by the Corps of Engineers for its major projects have notoriously underestimated costs and overstated benefits. The staff at the Office of Management and Budget charged with the responsibility for reading and evaluating UIAs may not be sufficient for the task. As an alternative, it has been suggested that a separate executive office, similar in structure to the Council of Economic Advisors, be established to analyze urban and regional effects.

The fear that UIAs will not enter the policymaking process should prove less serious. Generally, UIAs promise a more informed debate. They may lead to the discovery of important but inadvertent consequences before they occur. However, we should recognize that the cost of more light may be more heat. Additional information can sharpen the debate between the intended beneficiaries of the "non-urban" programs and representatives of the cities threatened by adverse impacts. The result may be deadlock. Congressmen, for example, will be interested in how new policies influence the location decisions of households and firms. Aware that UIAs exist, they will call upon them during committee hearings on new initiatives. Unfortunately, many of the more important policies are not subject to regular Congressional oversight, e.g., IRS procedures, climate of enforcement for environmental regulations, court decisions on school busing.

How might the nation take advantage of the growing awareness of the complex ways in which federal policies influence the local business climate, local fiscal conditions, and patterns of residential settlement? Obviously, the nation cannot hope to create "spatially neutral" policies. Not only is that impossible, but we believe it is also undesirable. Social policies have many goals other than ill-defined "balanced growth." Many of them were expressly designed to accommodate the revealed preferences of large segments of the citizenry by fostering suburbanization, homeownership, and new construction. For example, even if policymakers had understood in advance the full ramifications of decentralizing population and jobs via the highway program, probably little would have been done to reshape it. Cold War fears, and concern about overcrowded urban housing in the 1950s, dictated a more dispersed population and a transportation network alternative to the railroad. The harmful effects of air pollution may justify the deconcentration of polluting activities.

Many of the programs that we have identified as harmful to central cities are not reversible. The country cannot close down highways nor demolish the suburban housing developments financed through federal guaranteed mortgages, tax-free development bonds, and income tax provisions. It must be hoped that, in the future, awareness of the geographic effects of policies may help the nation to alter them sufficiently to reduce their undesirable, and often unnecessary, effects on business and household location decisions. For example, now that nuclear families make up a smaller fraction of households, it may be politically possible to extend to renters
the favorable tax treatment traditionally provided to homeowners. Regulation of freight rates could be modified to reduce the antirail bias. Tax incentives encouraging sprawl could be reduced to accord with emerging desires for environmental protection. Grants that fund only new public facilities could be extended to subsidize the rehabilitation of existing facilities.

These changes will be neither rapid enough nor extensive enough to cure all the ills of troubled cities. However, they may slowly reduce the adverse environment within which many local policymakers operate, and allow them more time to adapt to the structural changes caused by the inevitable process of development.

LOCAL STRATEGIES

The interactions among the business, residential, and local government sectors suggest some implications for local policymakers. The movements of jobs and people are closely interrelated. Household migration decisions are often based upon a desire to improve employment and income prospects. Simultaneously, firms seek to locate where demand is growing and labor is available. Within this interactive system, household migration is also influenced by such noneconomic considerations as climate, clean air, and recreational facilities. For that reason, although Detroit gained population because of the location of the auto industry, Miami grew first in population and then in economic activity to service its new retired residents, who were more concerned with local amenities than with job opportunities. More and more, these noneconomic considerations outweigh economic ones. Jobs tend to follow people rather than the reverse. The implication is that local economic development efforts may not be successful if they focus entirely on trying to attract or retain businesses. They must be coordinated with efforts to attract or retain households who can stimulate local demand and provide skilled labor. A city park may be as powerful a development magnet as an industrial park.

Surprisingly, there is little evidence that local taxes play a critical role in determining industrial location or economic growth. However, there is some evidence that less quantifiable aspects of the local public sector may matter more, such as the flexibility with which regulations are enforced, and the helpful attitude of local officials. While this finding may be of some comfort to administrators in high-tax locales, it also implies that the rather expensive tax holidays that some areas have offered to footloose businesses may be wasteful.

Household behavior responds to local government actions. Cities offering generous services and welfare payment levels have, as we have seen, experienced a growing concentration of the poor. Suburbs have proliferated to accommodate homogeneous groups of households who seek, among other advantages, to avoid redistributive local tax payments. The implication is that if social segregation along jurisdictional lines is to be avoided, redistribution of income and social services for the poor must be funded at a level above that of the local government.

New policy cannot and ought not try to reverse all the ramifications of trends in tastes and in technology. However, careful diagnosis of the problem to be solved and attention to locational incentives can ameliorate some of the socially deleterious side effects. The mere raising of the issues should lead to more balanced policies.