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If you can't afford the rent, it's my problem, too

Improving the quality of life in cities matters to more than just the people who live in them.

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It is a commonplace observation that **the rent is too damn high**, at least in Manhattan, San Francisco, London, Vancouver and many of the world's other glamour spots. Not only is this observation true — it's worse than you think.

Complaints about the status quo tend to focus on how much renters have to pay out of pocket, or how hard it is to get on the home ownership track, or the problems businesses have in attracting talent. But another huge problem is one of political economy: As time goes on, governance in high-rent cities is likely to get more and more dysfunctional.

To see why, step back and consider two 19th-century "classical economists" who focused on high rents: David Ricardo and Henry George. Both built models where land is so scarce that the cost of renting land absorbs most of the social surplus. We are not (yet?) at that point, but these models give insight into where today's most expensive cities are headed.

Consider an increase in the quality of public services — say, garbage collection, or perhaps in San Francisco the elimination of public urination. You might think that would make life much better for everyone. But in a Ricardo-George model, that is not the case. Mainly what happens is that rents go up and landowners capture most of the newly created surplus.

How would this work? Take the example of San Francisco; with nicer streets, even more people might want to move there. That would push up rents by an amount roughly equal to the value created — putting the gains from the higher quality of life into the pockets of landowners. In a normal market economy, those higher rents would then induce more construction and, eventually, a corresponding decline in rents. But San Francisco is a "not in my backyard" locale where the amount of new construction just isn't that high, for legal and regulatory reasons. Again, as both Ricardo and George realized, the incidence of the benefit falls upon the very scarce factor, namely land.

The political economy problem now should be obvious: Why exactly would non-landowners press for improvements in their cities? The value of those improvements will be captured mainly by other parties.

By the same token, the incentives are skewed when it comes to the cost of problems. Say air pollution or homelessness gets worse. You might think that would degrade the quality of life in a city. But don't leap to that conclusion too quickly: To the extent land is truly scarce, the main effect would be a decline in rents and real estate prices. Landowners would be worse off, but the typical city resident might find that the cheaper cost of living offsets the deterioration in conditions.

The political economy problem here again is that residents just won't care enough about the quality of life in their city. A ride on the New York City subway system, or a walk through central San Francisco, will confirm the view that two of America's greatest cities are grossly underinvesting in the quality of life.

You might think that landowners would care about urban quality, and use their clout to push through all sorts of policy improvements. Partly they do, but landowners are not such a numerous group, and they tend to focus their limited political influence in support of NIMBY policies most of all.

Once you think about these cities in terms of the Ricardo-George model, it is remarkable how many orthodox views get revised. What about an increase in the minimum wage, for example? Any initial gains for workers will eventually be offset by higher rents.

Like most economic adjustments, these effects are more potent in the long term than in the short term. But the upshot is the same: In a NIMBY-controlled world, many of our most glorious cities will slowly but surely fall apart. Voters just won't care enough about the quality of public services, and furthermore many voters might end up using their votes to express their ideology (even more so than usual) rather than to elect leaders to solve problems.

Fine, you might say: So what if major cities decay, especially if most of the burden is borne by landowners rather than workers. Unfortunately, dysfunctional major cities have negative effects on the nation as a whole. America needs its best cities to be centers of national and international innovation — to serve as role models and sources of new ideas. A rotten San Francisco or Manhattan is not acceptable simply because otherwise, the rent would be even higher.

If America's cities continue to deteriorate in so many areas, the social costs of building restrictions and high rents will spread — even to the most development-friendly parts of America and the world.

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