

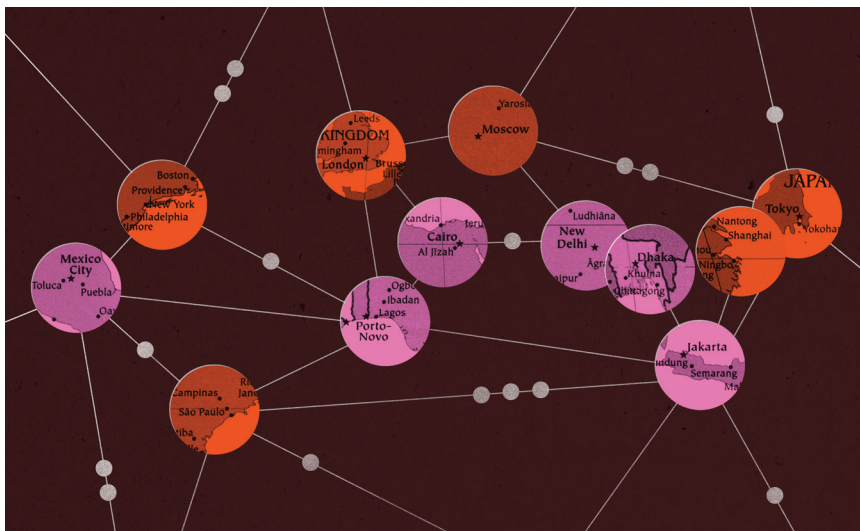
Point of View

The Mysteries of Cities and Economic Growth

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It's impossible to think about economic growth without also thinking about cities' vital role in connecting the world



CITIES ARE THE NODES ON OUR GLOBAL LATTICE

of travel and trade. They are the ports of entry for goods, people, ideas—and for viruses. The second of the IMF's three critical missions is “encouraging the expansion of trade and economic growth.” Given the vital role that cities play in connecting the world, it's almost impossible to think about the expansion of trade and economic growth without also thinking about cities. It is our belief that improving governance of the world's cities and reducing the barriers that artificially divide them can help trade expand and economies grow.

The link between cities and globalization is long-standing. When ancient Athens was the hub of the Mediterranean region, it attracted human capital from across the Aegean Sea. As Athenians learned from outsiders and from each other, they generated a remarkable flourishing of genius in philosophy, sculpture, drama, architecture, and history. But connection to the outside world brought

danger as well as dynamism. As Athens expanded, it went to war with Sparta, a war that halved the city's population. A key moment in that war was the Plague of Athens, which killed perhaps a quarter of the city's inhabitants.

Even today, urbanization is synonymous with economic development. A paper by economists Filipe Campante and David Yanagizawa-Drott showed that areas with fewer flight links to successful cities have less business activity. This is not just because airlines don't fly to less developed areas; the effect works the other way as well. When distance between cities exceeds 6,000 miles, there are more travel regulations, raising the cost of flights and reducing their number. Sure enough, connections and trade between cities drop sharply at the 6,000-mile cutoff.

Within countries there is a similarly strong link between urban neighborhoods' size and integration and their prosperity. A recent paper by one of us coauthored with Radu Barzu, César Hidalgo and Martina Viarengo looks at upward mobility for poor Brazilians who move to urban areas. People who move to cities experience big wage gains, but the effects in southern Brazilian cities are much stronger than in the North. This gap can be explained by the fact that Southern business establishments are much more integrated by skill than Northern establishments.

The same link between economic integration and growth appears to be true in the United States in recent decades. In explaining economic conglomeration, Alfred Marshall, the British economist, perhaps said it best over a century ago: “The mysteries of the trade become no mystery; but are as it were in the air, and children learn many of them unconsciously.”

Face-to-face exchange

One recent worry about cities is that electronic interchange will make face-to-face interactions far less relevant. But this is not true. While electronic interaction substitutes for some face-to-face interactions, it also leads to more relationships, many of which necessitate face-to-face exchange. And electronic interchange makes economic interactions more complex, which also requires in-person connections. The more complex the topic, the more people prefer to meet and discuss in person. We see this in the data. Work from home has boomed since COVID, but it appears to have settled down to a modest rate. In late 2024, 11 percent of the employed in the United States were fully remote and 13 percent did some remote work. Thus, the share of hours worked remotely was about 16 percent. That is of value to workers and their families, but not a sea change in behavior.

The impact on use of existing buildings will be mixed. In many areas, a one-off 16 percent reduction in office space is likely a blip on the road to business growth: the rising demand for office space will offset the desire to work from home in a few years. For some markets where demand is stagnant, however, this spells trouble.

There are three larger risks—war, plague, and climate change—that threaten our urban world much more. Each is centrally related to the IMF and its mission. Three major wars—in Ukraine, the Middle East, and Sudan—impact urban life both directly and indirectly. Cities are being physically destroyed in these conflicts, and it will take many years to rebuild or relocate them. Cities are also indirectly damaged by conflict. The number of foreign

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visitors to Moscow dropped by 43 percent between 2019 and 2023. The number of foreign visitors to Israel fell by an even larger percentage after the onset of war in the Middle East.

The IMF can, and likely will need to, play some role in financing the rebuilding of cities in places such as Ukraine and Lebanon. While the European Bank for Reconstruction and Development and the World Bank are likely to play central roles in physical rebuilding, the IMF has a role in focusing on the finances and governance of the countries as a whole. Fiscal and monetary infrastructure is as essential to economic growth as are bricks and mortar. In addition, the Fund has a diplomatic role to play. The IMF promotes peace when it leans on borrowers who want to spend lavishly on arms and when it stresses positive connections among its members. Global cooperation is made, not endowed.

Existential problem

Pandemic disease is an existential world problem, and the IMF must play a role there too. COVID has subsided into a manageable, endemic disease, but that doesn't mean the world is safe. The question is not whether, but when, there will be another pandemic. COVID was a major economic as well as health event. The IMF responded appropriately with significant lending. If it wants to be

ready for the next event, it must think about future health risks and plan for their arrival.

The IMF can even do more to reduce the risks of future global pandemics by keeping continued focus on these risks. We learned during COVID that many countries were woefully underprepared for a pandemic. Since the outbreak, we have not changed our institutions to plan for and protect against a new outbreak of disease. The IMF is not a medical organization, but as long as health risks create major financial risks, it can continue to shine a light on the topic. It might, for example, work with entities such as the US National Institutes of Health and the World Health Organization to keep the issue of pandemics and the needed response front and center.

The IMF has already embraced sustainable development, but that's not what the world's most vulnerable cities actually need to be safe. Low-lying metropolises in tropical areas are vulnerable to heat and flooding, and they have limited financial resources and public capacity to address these issues. It is only partly known how to keep these places safe from rising seas, water pollution, and large temperature increases. Support for a learning agenda that encourages scholars to develop practical tools that better protect poor world cities against climate change would be an important step forward.

The IMF is a great institution that connects the world. Those connections are critical to the success of cities—our central economic engine. However, the future is full of new challenges. The IMF's core mission is not directly related to the three great challenges currently facing the urban world, but the Fund is not divorced from them either. Sound policy can improve governance, enhance financial stability, and connect the world's leaders in ways that promote their commitment to addressing these common goals. **F&D**

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