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Why Big Cities Matter More than Ever

Seven reasons

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The information revolution, we used to hear, would break the shackles of geography and make cities irrelevant. Thanks to e-mail, the Internet, and an ever-widening array of technological devices, you would be able to work just as effectively in South Podunk as in the Big Apple. A new, post-metropolitan era would open in which creative and flexible firms could locate their operations anywhere. The age of the big city would come to an end.

But that hasn't happened. Big cities have continued to grow. In rich nations today, urbanization levels are on the order of 80 percent or higher. China and India are urbanizing at breakneck speed, with Shanghai and Bombay racing each other to become the world's largest metropolitan area and eclipse Tokyo (currently 33 million strong). Why is it that cities have lost none of their powers of attraction, despite the new freedom that information technology brings individuals and firms? The economic advantages of cities—of urban “agglomeration,” in the language of the people who study these things—are difficult to measure precisely and not the same for all firms. But they are quite real, and we can capture them in what I call the Seven Pillars of Agglomeration.

Let's start with the most basic pillar, one that has historically supported the great manufacturing economies of big cities: *economies of scale in production*. That is, as the scale of production increases, unit costs fall. That basic rule of economics makes it profitable for firms to manufacture goods in just a few large factories, rather than in many smaller ones. And if you're going to have just one or two big plants, it makes sense to locate them where you can find a lot of workers: densely packed urban areas. This logic explains the growth of large manufacturing cities like Detroit in the earlier part of the twentieth century. Nowadays, though, it applies most readily to midsize cities, because real estate in larger cities often costs too much to build big factories (see the sidebar below).

Smaller Cities Matter, Too

Consider a remarkable fact: over the long run, the growth rates of American cities in various size groups tend to be about the same. That is, over the last century, the country's distribution of small, midsize, and big cities has remained stable. This stability intrigues economic geographers. Why aren't all cities converging toward one ideal size—whether large or small?

Part of the answer is that the attributes that make big cities attractive to some industries make them less attractive to others—and every industry gravitates to locations where its comparative costs are lowest. For example, providing environments for rapid, diverse, face-to-face contacts is a comparative advantage of big cities, while physical space is more readily available in smaller ones. If the demand for face-to-face contacts increases, real-estate and wage costs will rise in the largest cities, crowding out industries for which those costs carry—comparatively—less weight. We

understand intuitively that Manhattan isn't a good location for manufacturing airplanes or laptops. But it's excellent for management consulting and producing operas. So urban systems have a self-regulating nature: certain industries emerge (or centralize) in the largest cities; others move to smaller ones.

So small cities, no less than large ones, fill an essential economic need. The more attractive big cities become for some industries, the more alluring small cities will be to others.

The second pillar, however, tends to push firms back to larger cities: *economies of scale in trade and transportation*. Just as larger factories lead to lower unit costs by making manufacturing more efficient, fully loading a truck, an airplane, or a cargo ship leads to lower unit costs by making delivery more efficient. And filling up those trucks, planes, and ships—both coming and going—is generally easier if they're delivering to the largest ports, airports, and other distribution centers. That means the bigger urban areas.

Reinforcing this tendency is the third pillar of agglomeration: *falling transportation and communications costs*. Throughout history, transportation costs—not only monetary outlays but also lost time and the frustration that can come with trading with distant partners—have been a barrier to market expansion. It follows that a fall in transportation costs will stimulate trade, enabling the lowest-cost producers to improve market share. And the steeper the drop in transportation costs and the greater the weight of scale economies in production, the greater the potential for centralizing production in one or two places. Henry Ford could locate automobile production in Detroit because paved roads and railways allowed him to reach the entire American market.

Indeed, if scale economies are infinite and transportation costs are close to zero, all production will be centralized in one place, with the first (lucky) producer to have arrived on the scene. Such an extreme case probably doesn't exist in the real world, but the film industry comes close. Scale in the industry is vitally important, with its enormous sound studios and vast budgets. It costs little to ship a film—and even less if done electronically. The centralization of the film industry in Southern California is the result. With transportation costs removed as an economic factor, competitors had no way to match the scale economy that Hollywood had established early in the twentieth century.

What about the argument that falling communications costs actually undermine urban concentration? For example, didn't the existence of e-mail encourage Silicon Valley companies to outsource computer programming to Bangalore, India? The truth is that this shift did foster urban concentration—in Bangalore. Think of communications costs as tariffs: competition intensifies when they fall. If one city is already more efficient at producing a particular good and then the barriers are removed, that city's market share will expand accordingly.

The centralizing influence of technology is consistent with history. The advent of the telegraph—as revolutionary in its time as the Internet is today—not only failed to slow the growth of London and New York; it enabled financial firms and corporate offices in those cities to extend their reach. The arrival of radio and television in the twentieth century replaced a lot of locally produced entertainment with programs produced in New York or Los Angeles.

Scale economies are only part of the urban-expansion story. Most city dwellers work not in massive

plants but in small and midsize firms in a wide array of industries: legal services, shirt-making, financial counseling, and on and on. Why should these companies set up shop in cities? Pillar four—*the need for proximity with other firms in the same industry*—provides part of the answer.

Proximity brings numerous advantages. To name just one: face-to-face contacts remain essential for the most valuable and sensitive information. Finance, among the most spatially concentrated of industries, is an obvious example. Trust must be constantly renewed; millions of dollars will be committed based on a brief encounter. The greater the risks and sums involved, the greater the need for relationships built on something more than e-mail exchanges. Body language, facial expressions, and eye contact are among the signals that financial workers use to judge others.

Personal contact is also crucial in industries where creativity, inspiration, and imagination are vital inputs. For firms working in these rapidly evolving industries—high fashion, say, or computer graphics—the surest way to stay on top of the latest news is to locate near similar firms. The more that information can be transmitted electronically, it seems, the more valuable becomes information that cannot be so transmitted. Electronic and face-to-face communications tend to be complements; business travel, for example, has accelerated since the advent of the Internet. The more people communicate, the more they want to meet in the flesh.

Lower recruitment and training costs are additional advantages of proximity, particularly in highly specialized fields. A firm clearly benefits if it can hire from a pool of available workers with relevant training acquired at previous employers. The chances of finding a first-rate, experienced screenwriter will be a lot better in Los Angeles than in Baton Rouge.

Companies that require a wide array of talents, across a broad range of industries, will be drawn to big cities as well. Thus pillar five: *the advantages of diversity*. Consider advertising, a field whose products are constantly changing and come with no blueprint. Successful ad firms must rapidly assemble dizzying combinations of expertise and talent according to various clients' needs. Each ad campaign, after all, is unique: one may call for animation, another for symphonic music, a third for trained chimpanzees. Where better to find the necessary components than in big cities, with their myriad industry clusters? Of the world's top ten advertising agencies, it is no surprise that three are in New York, three in Tokyo, and two each in London and Paris. The entertainment industry, publishing, and many other fields feel the same pull.

Firms—above all, general-service businesses, for which customer access is important—naturally want to locate in the geographic center of their markets, which brings us to pillar six: *the quest for the center*. What economic geographers call “centrality” varies by industry, however. For companies with low-scale economies—a gas station, for instance—a central location can simply be a busy street, where the potential number of customers driving by is sufficient to ensure profitability.

But the centrality principle also holds at the national and international levels, and it makes large urban agglomerations particularly appealing. The performing arts are a good example. Broadway, the largest cluster of theaters in America, is in New York City not only because of the sizable local population but also because of all the potential theatergoers within a manageable distance of the city. Greater Philadelphia, with more than 5 million residents, is a mere 90-minute drive away; and don't forget Gotham's many rail, air, and bus links to other cities (including distant ones), which bring in countless more potential theatergoers. Centrality is often a legacy of history. Paris, shaped by many

centuries of investment in roads, rail, and other transportation modes converging on the capital, remains the undisputed center of the French market.

Finally, there's pillar seven: *buzz and bright lights*. Talented and ambitious people benefit from being in a big city, just as firms do—in part because the companies can hire talented and ambitious workers. Some people move to cities not just because they need to make a living (though being in a metropolis does offer all the advantages of a diverse labor market) but also because they want to be where the action is. Ambition, dreams, the need for recognition—all are powerful forces in human behavior. Many a young man or woman will ask: Where are my chances best of meeting the right people and doing exciting things? The answer, for good reason, will often be the big city. Why, indeed, are some people willing to spend small fortunes for apartments on Fifth Avenue or homes in Beverly Hills if not to feel that they are truly at the *center*?

Cities face many challenges in the coming years: municipal debt, onerous taxes, the cost of living, and crumbling infrastructure, among others. But whatever the genuine threats to urban prosperity, human contact is more important than ever in the age of information technology, and people will continue to seek places where they can share ideas, make transactions, and pursue their dreams. There's nowhere better to do these things than big cities.

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