Migration and Municipal Bonds

The slowdown in migration in the U.S. has significant consequences for municipal finance. Local population growth has been a fundamental propellant for bond issuance: borrowing for roads, water and sewer systems, not to mention housing, to meet the needs of new migrants is the classical function of municipal finance. Regional shifts in migration patterns will likely affect the geographic distribution of bond volume in the near term. In the new environment of budget gaps and dwindling resources, governments that have been magnets for new growth, particularly in the south and west, need to make a quick hat switch to manage through the downturn. Borrowing to meet growth is politically easier when expectations for repayment fall on the new beneficiaries. Borrowing for maintenance of infrastructure is more challenging and will be competing with the din of other budget demands. In addition, problems from high foreclosures and developer bankruptcies have cropped up on the suburban frontier, where the migration slowdown is pronounced. A look the recent census report and related analyses adds an important dimension to our understanding of state and local fiscal condition.

The Long and Short of It

In the "Mad Men" decades of the 1950's and 1960's more than one in five people moved from one place to another in the U.S. Three out of five moves were local, mostly from city to suburb or from one suburban location to another as the American Dream of homeownership gained traction. Local moves picked up a bit in the 2005-2007 years when easy credit, low mortgage rates and federal policies were directed to making homeownership easier. Exurban expansion accelerated, parodied by another TV show, "Weeds" which takes place in the gated California community of "Agrestic". "Little Boxes", a song that was written about 1960's cookie-cutter suburban development is the theme.

While people who move locally are first time homebuyers, mover-uppers, and those whose family circumstances have changed (births, deaths, divorce), people make long distance moves primarily for jobs. "…Long-distance migration acts as an engine of growth in many metropolitan areas…younger adults are far more likely to move than older individuals," according to William Frey of the Brookings Institution. (There is a small peak in migration among people in their early sixties who move for retirement.) Long distance movers tend to be college educated and professional.

The Biggest Losers

All this moving around has slowed dramatically in the last two years. According to the recent census report, we've hit the lowest migration levels since World War II and some states, like Florida have shown net out-migration for the first time. In post war 1955-56 about 17.3% of all households changed residence locally and 3.7% made the long distance move. Economists forecast a slow recovery in employment so long distance moves are unlikely to pick up in the near term. Short moves have slowed as well, given the abundance of housing on the suburban frontier, tight credit and the neighborhood challenges of high foreclosures. By 2008 only 9.9% of all households changed residence locally while 2% made the long distance move.

The greatest changes in migration have taken place in states that had benefitted the most from the recent housing boom, "especially the southern and Intermountain West states of Florida,

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Arizona and Nevada. Among the 28 states that gained migrants in 2006-2007, 21 gained fewer migrants and an additional four (including Florida) flipped from gaining to losing domestic migrants," according to Frey, Aside from Florida, the other three states that lost people were Mississippi, Missouri and Indiana.

Arizona and Nevada's dependence on construction will hurt in the current environment. Arizona's net in-migration, while still positive, has fallen by more than 54% from its peak in 2005 -2006 to 2008. Nevada's net in-migration has fallen more than 75% from its peak in 2006 to 2008. "In the heady days of the housing bubble, some Sun Belt cities – Phoenix and Las Vegas are the best examples – developed economies centered largely on real estate and construction. With sunny weather and plenty of flat, empty land, they got caught in a classic boom cycle. Although these places drew tourists, retirees, and some industry – firms seeking bigger footprints at lower costs, much of these cities' development came from well, development itself," according to Richard Florida in the March 2009 *Atlantic*. Florida is professor at the University of Toronto who chronicles the geography of change. At the peak of Nevada's building boom in April, 2006, more than 11% of all employment in the state was in construction. This compared with a U.S. level of 5.6%. Arizona's construction employment was next highest at 9.3% followed by Florida at 8.6%.

Heading Inland

Home buyers who bought in the 2000-2007 period were attracted to more exurban, inland areas and away from high cost coastal areas. Sustained growth of inland areas such as Riverside County in California depends on good roads, affordable gasoline and of course, enough jobs to support the commute, mortgage payments and trappings of the exurban lifestyle. For those fleeing the high cost of California altogether, the most likely destinations were Arizona, Texas, Nevada, Oregon and Washington. Favored destinations for Florida refugees were Georgia, North Carolina, Tennessee, Texas and South Carolina. The demographic of these migrants reflects an important change. "The shift from net in-migration to net out-migration in Florida was especially strong for whites, Hispanics, younger people, married couples and persons with some college education…Despite its total net out-migration, Florida still attracted people ages 55 and over in 2007-2008," as Frey analyzed. Sales taxes and health care services may perform satisfactorily under a demographic shift to older residents, as retirees are in the consumptive period of life. However, older migrants on fixed incomes will reinforce anti-property tax sentiment in the state and will be little interested in supporting already stressed school systems.

In California the pattern is a mirror image to Florida – a reflection of softening real estate costs. During the boom years California exported people, as mentioned above, to the northwest and inland states. Frey points out: "Migration away from…San Francisco to San Diego, where high housing prices fueled 'middle-class flight' to the interior west, has now retrenched as home foreclosures rise and job opportunities diminish in states like Nevada and Arizona."

Metropolitan areas with the greatest declines over the last three years include Riverside, California, Phoenix, Arizona, Las Vegas, Nevada, Tampa and Orlando in Florida and Atlanta, Georgia. San Francisco and San Diego each actually showed some gains. Other gainers where the job market is still strong include Dallas, Austin and Houston.

International migration more than made up for domestic declines in Miami and Washington, D.C. and strongly added to the demographic profile of Dallas, Houston and New York. On the state

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level, international migration exceeded domestic migration in Texas and Virginia in the 2000-2008 periods. International migration significantly offset declines in domestic migration in seven states: California, Connecticut, Indiana, Maryland, Minnesota, Pennsylvania and Wisconsin.

Trouble in Suburbia

The outer suburbs are suffering the fall in migration with increased crime and squatters in empty houses. Some writers even declare that exurban communities will become the next slums. Changes on the suburban frontier not only affect municipal government but water and sewer systems and healthcare systems as well. Healthcare groups that expanded into exurbia to follow new migrants and increase their competitive market share may not see expected growth and bad debts could rise in these outposts. "The experience of cities during the 1950's through the '80's suggests that the fate of many single-family homes on the metropolitan fringes will be resale, at rock-bottom prices to lower-income families – and in all likelihood, eventual conversion to apartments", according to Christopher Leinberger in the March, 2008 *Atlantic*. If this seems unusual, many European cities are modeled with affordable housing on the fringe, preserving the historic center for commerce, tourism and wealthy apartment dwellers. Leinberger described the rise of crime in the starter home development of Windy Ridge, in northwest Charlotte, North Carolina. He also reported the empty homes, graffiti, broken windows and gang activity in the Franklin Reserve community of Elk Grove, California where 10,000 new homes were built in four years. Frey wrote: "…fall-offs are evident in peripheral suburban counties within metropolitan areas of Chicago, Philadelphia, Washington, D.C., Dallas and Houston…21 out of 26 counties in the greater Atlanta metropolitan area showed reduced migration.."

Last April, ABC Australia covered this U.S. phenomenon, "Fifty-four kilometres from downtown Washington, (D.C.) it is easy to find signs that America's relentless suburban expansion may have petered out….Streets remain incompletely paved and poorly lit, the legacy of a builder that declared bankruptcy. And transient renters have replaced homeowners who were forced out by the foreclosure crisis." Prince William County, where this subdivision is located, has seen nearly a 40% drop in property values according to the county's 2010 budget message. The "Aa1" rated county is entering the year well-positioned for the challenge, but has cut the budget across the board, eliminated services and increased classroom sizes. The county has taken down its capital improvement budget by 64% since last year.

Been There, Done That

Ironically, the suburbs around Detroit were the scene of the worst municipal defaults following the Great Depression. In the 1920's people flocked to Detroit for new jobs created by the nascent automobile industry and the city experienced significant expansion. Detroit's population grew from 286,000 in 1900 to 1.5 million by 1930. The city's assessed valuation grew from $238 million in 1900 to $3.7 billion in 1930. Richard Florida wrote: "Suburbanization was the spatial fix for the industrial age, the geographic expression of mass production and the early credit economy…'Fordism' the combination of mass production and mass consumption to create national prosperity, didn't emerge as a full-blown economic and social model until the 1920's and the advent of Roosevelt's New Deal programs." Borrowing in suburban communities was particularly active. Some communities had borrowed so heavily that they had debt burdens greater than 50% of their value. A decline in value on new buildings began to emerge in the late

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1920's particularly on properties built on speculation. By 1935 Michigan had the highest amount of municipal debt in default of all the states. According to one study, more than 66% of general obligation debt, 86% of special assessment debt and 72% of the short term debt defaults were concentrated in the Detroit metropolitan area.

Back to the Cities

The "New Urbanists" who favor denser, walkable, multi-use communities are having their day in the sun. Richard Florida cited the importance of "talent-clustering" as an engine for economic growth. Mega urban clusters are expected to be best positioned to emerge from the current downturn. "Migration matters," according to the December 19, 2009 *Economist*. "Economic growth depends on productivity and the most productive people are often the most mobile… When clever people cluster they can bounce ideas off each other. This is why rents are so high in Manhattan. Robert Lucas, a Nobel economics laureate, argues that the clustering of talent is the primary driver of economic growth."

"Chicago has emerged as a center for industrial management", Florida wrote, "Los Angeles has a broad, diverse economy with global strength in media and entertainment. Miami, which is being hit hard by the collapse of the real estate bubble, nonetheless remains the commercial center for the large South Florida mega-region and a major financial center for Latin America…" Florida points out that the geographic sorting of people by education and talents has diverged. "Cities like Seattle, San Francisco, Austin, Raleigh and Boston now have two or three times the concentration of college graduates of Akron or Buffalo. Among people with postgraduate degrees the disparities are wider still…" While the once depressed urban core of New York, Boston, Chicago and Los Angeles will be beneficiaries.

What's an investor to do? Check to see whether the majority of growth in the community took place in the 2004-2007 periods. If so, look deeper. Look at wealth levels relative to original home values to get a picture of affordability. Get as much anecdotal information about foreclosures and vacancies as possible. How leveraged is the community? A municipality's budget message is often revealing about its fiscal issues and approach. You can find some answers on-line; most municipalities post their budgets these days. The budget message will give you an idea of how well the community is managing deficits, liquidity and balances.

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