Population, Pigs And Perestroika

PLAINTIFF'S EXHIBIT

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Conditions in real estate, especially housing, have a vital relationship to the region's competitiveness. Those conditions are now providing a lesson in free market economics.

By Karl E. Case

There shouldn't be any confusion about the fact that we have major problems in the real estate industry today. Some very big banks have portfolios with a lot of non-performing loans. Some well known as well as some well capitalized developers are filing for protection under Chapter 11 and Chapter 7. There is a large inventory of unsold homes, and still a larger inventory of unsold condominiums, many of which are vacant. Housing prices in some locations are turning down—commercial and office vacancy rates, while still very healthy compared to national conditions, are also on the rise. The employment picture is also changing. Furthermore, we have over 20,000 people on the wait list for public housing in the city of Boston—affordability is still a very important word in this region. Those who believe in the free market believe that the best way for society to determine how resources are allocated across alternative uses is to leave most of the decisions to private, risk taking independent entrepreneurs. Every economic writer since Adam Smith, including Ricardo, Marx, Alfred Marshall in the latter part of the 19th century and Keynes in the 1930s, has pointed out that one of the prices we pay for the advantages that markets bring is lack of coordination. The lack of coordination and the lack of central planning that markets bring with them lead to mistakes of coordination and cycles.

The 'pigs' in my title refers to what Alfred Marshall called in 1890 the 'hog cycle'—excess demand in period one causes prices to rise, and seeing those nice high hog prices, farmers decide to produce more hogs. But it takes some time to grow them and get them to market—it also takes some time to build buildings (in case you haven't noticed) and to get them to market. Since nobody sits down and plans supply responses and since there is no real coordination, by the time the pigs get to market there is an inevitable glut, too many pigs. If we want the benefits of a free, largely unregulated economy, we must be willing to accept cycles and the pain that cycles bring with them on the downside. It is a lesson that people in China, in the USSR, in Hungary, and in Poland are going to have to learn as prices and production are deregulated. Indeed, there is already some instability showing up in those economies: hence the word 'perestroika.'

What I want to argue is that we are in the midst of a down cycle that is natural and one which was inevitable. It will just as naturally and just as inevitably some day come to an end although there is considerable room for debate and for disagreement about how long it will take and how painful it will be. In 1975 there was a national recession which put unemployment at about nine percent; in the Massachusetts economy it was 12 percent, second highest among all the 50 states, second only to Michigan. Wages in the region were falling, Boston was deteriorating, and except for two urban renewal projects, there hadn't been a new building built in many, many years. Those were the days when the Boston Redevelopment Authority's job was to recruit people to come and invest and to develop properties, rather than to slow things down which seems to be their role more recently. The traditional sectors, shoes, textiles, machinery, furniture, had been in steady decline for more than a decade—housing prices were below the national average.

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