CITIES: STEERING TOWARDS SUSTAINABILITY

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Cities: Steering towards Sustainability
Pierre Jacquet, Rajendra K. Pachauri and Laurence Tubiana (editors)
Delhi: TERI Press, 2010
ISBN 978-81-7993-131-8
© 2010 AFD, IDDRI
© 2010 TERI Press

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Cartography: Benoît Martin, Sciences Po Cartography Studio.


Publishing and administration: Raphael Jozan, Chandni Sengupta.

A Planet for Life would like to thank the Courrier de la planète, the Sustainable Development Center at Sciences Po, the people who agreed to answer our questions, the authors of the Chapters and Zooms, as well as all those who contributed to this work: Paolo Avner, Maurice Bernard, Alexis Bonnel, Lise Breuil, Ayméric Blanc, Frédérique Bouvrart, Christophe Cassen, Catherine Casteran, Jean-Raphaël Chaponnier, Kosmas Chatzis, Béatrice Combe, Bérénice Combette, Nils Devernois, Isabel Díaz, Chahhvi Dhingra, Sandrine Dury, Pénélope Dutet, Eric Fofiri, Sophie Galharret, Benjamin Garraud, François Gemmen, Christian de Gromard, Sabrina Guérard, Vincent Jouglet, Guillaume Josse, Laureline Krichewsky, Sarah Lahmani, Benoît Lebot, Nathalie Ledenmat, Benoît Lefèvre, Samuel Lefèvre, Alexandre Magnan, Sarah Marniesse, Benoît Martimot-Asso, Nicolas Maisetti, Philippe Menanteau, Paule Mourié, Suzan Nolan, Vatche Papazian, Muriel Penaud, Serge Perrin, Brune Poisson, Olivier Ray, Armand Rioust de Largentaye, Julien Rochette, Hillary Sample, Marisa Simone, Ludovic Temple, Jean-François Tribillon, Louis-Jacques Vaillant, Jayashree Vivekanandan, Tancrède Voituriez

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This book is part of a series of annual publications on sustainable development (A Planet for Life) that started in 2007. In this overview, we take a global perspective on 2009, assess the state of collective action required to meet today’s sustainable development challenges and explain why cities have been chosen as the focus of the 2010 edition.

The year 2009 highlighted the many challenges of international collective action in its two complementary dimensions: crisis management and preventive action in the broad sense, including the evolution of global governance. The first aspect emerged in recovery plans responding to the economic and social crisis, as well as in the strengthening of international financial institutions and the emergence of the G-20 as an arena for top-level consultation and co-ordination. The second aspect, prevention, reaffirmed a longstanding paradox—the gap between the urgency manifest in public policy discourse and aims, and the feasibility of action at either the national or global level.

Thus expectations seem constantly plagued by disappointment—the Copenhagen Climate Summit in December 2009 was the most striking example: it typified the problems of collective action in the era of globalization and communication. Growing expectations create the necessary pressure and incentives, but high ambitions make short-term results unattainable; more achievable goals, in fact, would hardly justify the extra effort needed to initiate action. This dynamic, also present in multilateral trade negotiations, might appear as a formidable political problem: governments must implement what they propose and their success or failure depends upon achieving the stated objectives.
This culture of results certainly helps increase government efficiency, but it also leads to a reductionist vision of links between aims and outcomes. These depend on a complex chemistry between multiple actors with differing motivations; governments must guide ever-changing collective preferences and progressively anchor results achieved through laws, regulations or any kind of international agreement. However frustrating, the gap between leadership and validation seems inevitable in any dynamic perspective.

Such a viewpoint necessarily leads to an interest in agents beyond governments alone, and to a focus on the interaction between the different levels of action (individual, local, national, global). In this 2010 edition of A planet for life, we have put the spotlight on cities – at once the actors of sustainable development and emblems of its challenges. More than half the world’s population lives in cities, which concentrate the majority of greenhouse gas emissions. Current demographic, economic and political dynamics concentrate wealth and power around urban hubs, key nodes in the interaction between globalizing trends, societies, economic growth, climate change and protection of the environment.

From a social and environmental perspective, cities often appear as nuisance producers. While one can certainly link growing energy demand and urbanization (Salat 2009), the dialectics involved require careful scrutiny. Studies in geographic economy (Prager and Thisse 2009) illustrate the dynamics of economic polarization, a process that persists despite the spectacular drop in transport costs since the mid-nineteenth century and the near zero-cost of communications. The search for increasing returns, even to the point of congestion, drives the dynamics of agglomeration. Cities are thus central to the processes of growth, innovation and sustainable development. They are also laboratories for observing political and economic dynamics at work and for testing technical solutions and new public policies. It is therefore the type of urbanization rather than the city per se that which will prove decisive for sustainable development.

Yet the current evolution of cities in many regions of the world runs counter to ecological, social and economic requirements. For example, various economic, institutional and legal factors aggravate the fragmentation of cities. There is also a visible divide between the “legal” city – well-equipped, modern and productive – and the illegal or “informal” remainder, sometimes designated by terms such as shantytown, bidonville, or favela. As some of the articles in this edition will show, this trend seems to be spreading, heightening social segregation and ecological problems. Worldwide, more than 50% of new housing is built outside of any legal framework, most often haphazardly and in the absence of any land title. In the least developed countries, the problem of urbanization has reached a critical level: while population growth and the rural exodus are accelerating urbanization, especially in sub-Saharan Africa, the cities do not have the means to absorb this additional population and provide basic services. For all these reasons, the construction of “sustainable cities” stands as one of the main challenges for the years to come, and it is chosen theme for this issue of the series, A planet for life.

This introduction proposes a reading of the events that have shaped the global landscape in 2009, whose effects not only highlight the sustainability (or not) of current development models, but also set crucial challenges for urbanization and other policies. We will identify what
we see as the four key lessons governance may draw from these events as a general framework for the specifics outlined elsewhere in this volume.

THE CRISIS AND A “GREEN AND INCLUSIVE” RECOVERY

The economic crisis of 2007-2009 began when the housing bubble burst in the United States, in the wholesale segment of the (high-risk) “subprime” mortgage market. It soon engulfed the entire global financial system, spawning the world’s worst economic crisis since the U.S. stock market crash in 1929 and causing international trade to decline even more than during the Great Depression of the 1930s (Eichen-green and O’Rourke 2009). American households lost nearly a fifth of their wealth in the space of a year (Federal Reserve 2009), and the U.S. unemployment rate reached 10.0% by December 2009, according to the U.S. Bureau of Labor and Statistics (BLS 2010).

Initial hopes of “decoupling” soon proved illusory. The crisis spread across the planet, extending far beyond the borders of the United States and other Western economies and financial centres. It wormed its way through multiple international transmissions to infect the world economy, causing credit contraction, loss of wealth and confidence, a slump in demand and a fall in foreign trade. Emerging countries, notably in Asia (India and China, in particular) were initially considered immune from contagion due to their earlier banking system reforms and to their accumulation of reserves following the Asian economic crisis of 1997-1998. But fact they suffered severely, affected by the curtailment of international credit and the shrinking of capital inflows, as well as the sharp reduction in international trade and in exports to the United States (Chaponnière 2010).

There were also hopes that poorer countries, notably in Africa, would have some protection against the American financial turmoil, given their financial markets’ under-development and lesser integration into the world economy. But the crisis in fact struck hard in these regions as well. The progressive integration of African countries into international trade over the last fifteen years has made them more vulnerable to any severe curtailment of international capital flows. These flows, whether from foreign investors or remittances transferred by Africans working abroad, have slowed down considerably, mainly as a result of the recession affecting Europe and the United States (IMF 2009). In addition, decreasing prices and volumes of Africa’s international market commodities, such as cotton, copper and tin, has dried up the sources of external financing for their exporters.

CITIES ARE LABORATORIES FOR OBSERVING POLITICAL AND ECONOMIC DYNAMICS AT WORK AND FOR TESTING TECHNICAL SOLUTIONS AND NEW PUBLIC POLICIES

As a result, African countries have had to cope with their own credit crisis, and have had to abandon many development projects in progress over the previous five years – notably in housing and infrastructure, as well as in production activities such as mining (also heavily affected by falling commodity prices). Price instability had a particularly strong impact on African

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3. Initially, the development of the subprime market was aimed at helping low-income households with bad credit records become homeowners. Banks were willing to lend to them using their homes as collateral even though they were much riskier borrowers. Over time, it was thought these customers could repay or refinance their loans by collateralizing ever-increasing home values.

4. According to the IMF, a 1% decrease in a host country’s rate of growth leads to a 4% decrease in the value of remittances sent by migrant workers to their country of origin.
economies given the linkage of their agriculture into global financial markets since 2006. Staple food prices were thus caught up in the storm, increasing sharply in 2006-2008 when agricultural commodities served as a “refuge” value, only to suffer from a subsequent collapse. In reality, Africa’s unprecedented growth since 2000 came to an abrupt halt.

What can explain the onslaught of such a crisis? Consensus on the causal chain of events will doubtless require time (see Benassy-Quéré et al. 2010). The crisis certainly revealed not only rapacity by some financiers (such as the American businessman Bernard Madoff and his Ponzi scheme), but also certain dysfunctions in the world economy and regulatory practices. It has also shown the dangers of excessive complacency. But fundamentally, the crisis reflects the interaction of a wide range of factors. The macroeconomic environment played some part in this; the global savings glut had fed on global current account imbalances encouraged by the lax monetary policies of central banks, particularly in the United States in the wake of the 1987 financial crisis. Moreover, the exchange rate policies of oil and gas exporters and of many emerging countries – designed to prevent any appreciation of their currencies and also sustaining a loose monetary policy in the United States – translated into an abundant liquidity that inflated bubbles in asset prices. In turn, securitization contributed to global imbalances by boosting the supply of “safe” investments available in the United States, in order to meet the incipient excess supply of savings and satisfy the demands of foreign investors, notably foreign central banks (Adrian and Shin 2009). By investing its official reserves in risk-free U.S. Treasury Bonds, China left it to others to take unwise risks (Brender and Pisani 2009), and enabled Americans to live far beyond their means.5 This “equilibrium” has been dubbed a “Revised Bretton Woods System” (Dooley et al. 2004).

In sum, during the 1990s and 2000s, it was believed that lifting restrictions on international capital flows and the balance of payments would accelerate the transfer of savings from developed countries towards developing countries and emerging markets. In fact, quite the opposite happened: Asian savings financed Western consumption to excess.

These macroeconomic factors interacted with a number of microeconomic failures. Investors were led to underestimate and misprice financial risk. The economist Gary Gorton (2009) provides a detailed analysis of how a “shadow banking system” emerged in the corporate world, through which companies could receive cash against securitized assets. This fed a rising demand for collateral assets and nurtured the growth of mortgage securitization to supply such assets through the higher rated tranches of mortgage-backed securities. As long as no shock disturbed the system, the quality of these assets was not questioned. However, subprime mortgage securitization was inherently sensitive to fluctuations in house prices. When the property bubble actually burst, the value of collateral based on subprime mortgage-backed securities collapsed. But no one really knew how

5. For the last 20 years, U.S. household income has stagnated in inflation-adjusted terms, leading Americans to take on debt in order to maintain consumption levels. The debt levels have particularly harmful effects because of the low inflation rate, which itself is a function of the American government’s desire to maintain a strong dollar and the fear of Asian governments to unpeg their currencies from the US dollar and allow their currencies to appreciate.
to assess the quality of the underlying assets, so the subprime mortgage crisis snowballed into a fully-fledged collateral crisis in which no one was prepared to hold securities. The collapse of the Lehman Brothers investment bank compounded the panic, and started a run on cash.

The more or less implicit pact between the Americans and Chinese did not guarantee stability (Aglietta 2007). Over time, and despite their well-known export orientation, the economic growth of China and of Asia has become less dependent on Western consumption. China developed other outlets, notably in Africa (Chaponnière and Jozan 2009); its exports to the United States and Europe represented only 5% to 10% of its GDP and its home market became a major engine for growth (Anderson 2007). The adjustment of international payments imbalances, and the broader exit from the present crisis, hinge on China and Asia: they will need to strengthen this nascent shift towards growth driven primarily by domestic demand, which in turn will become a key driver of the global economy.6

NATIONAL AND GLOBAL RESPONSES TO THE CRISIS AND CHALLENGES

The policy-makers’ response to the crisis was both active and atypical. They put forth measures designed to sustain demand in the economy through expansionary monetary and fiscal policies, and to support the ailing banking system (e.g. by raising deposit insurance ceilings, injecting capital into fragile banks, guaranteeing debt, insuring banking assets or purchasing toxic ones, and even nationalization). The United Kingdom and the Netherlands, for example, injected 3.4% and 5.1% of their GDP respectively to recapitalize their banks. The French government injected 1.4% of GDP into the sector, as well as providing nearly €80 billion of debt guarantees. In spring 2009, budget stimulus packages across the planet were estimated to be worth 3,000 billion dollars. After years of fascination with the notion of macroeconomic discipline, both monetary and fiscal policies turned dramatically expansionary. Central banks began buying assets that would not have even aroused their interest before the crisis; this move, known as “quantitative easing,” both expanded the money supply and gave a strong boost to their balance sheets. Fiscal policies set about substituting private demand and debt with public demand and debt. As a result, according to the IMF, budget deficits in the G-20 countries as a whole jumped from 1.1% of GDP in 2007 to 8.1% of GDP in 2009 (Economist 2009). Such measures were clearly needed to address a slump of historical magnitude. But they will not create sustainable recovery without well crafted “exit strategies,” since the time will come when this excess liquidity and debt will have to be eliminated. Further complications will arise from the crisis’ lasting impact on rising unemployment.

Two questions have immediately come to the fore: will these responses create a post-recession economy that is sustainable in the medium and long term? And would it not be wiser and more efficient to invest now in that future sustainability, at the same time stimulating the economy in the direction of growth, jobs and poverty eradication?

As pointed out in The Economist (2009), Keynes’ ideas have made a clear comeback, although his own reactions to this crisis remain hypothetical. Rather than returning wholesale to Keynesian views, we should incorporate his insights into our understanding of current problems. To borrow Neustadt and May’s terms (1986), “uses of history” fully inform our learning process and decision-making capacity, but do not imply a return to outdated formulae. The combination of

6. China has become the main trading partner of several Asian countries, thus supplanting the United States and Japan.
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Publisher: TERI Press
ISBN: 9788179931318
Author: Pierre Jacquet

Type the URL: http://www.kopykitab.com/product/8496

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