

Housing affordability and the economy: A review of labour market impacts and policy issues

**National Research Venture 3: Housing
Affordability for Lower Income
Australians**

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EXECUTIVE SUMMARY

Housing affordability problems arise when a household's income is insufficient to meet the various non-housing costs of living after paying for a dwelling of reasonable basic standard, appropriate to the size and structure of the household. Clearly, one important component of the affordability problem concerns the inadequacy of a household's income, which for most households, stems from position in the labour market, determined in large part by both the skills possessed and effective access to jobs for which current skills are relevant.

If the inability to get and keep a job is purely access related – i.e. is *not* caused by an absence of skills – then the resulting unemployment or underemployment is frictional rather than structural in character. Policy responses would then focus on ways of improving effective access of disadvantaged groups to employment, instead of dealing with the structural sources of the skill deficit.

Inefficient (non-clearing) urban labour sub-markets, in general, ensure that the urban economy underperforms; resources are not allocated to the most productive uses and over time there is a loss in potential economic welfare. These effects are widespread and not confined to the particular group or groups experiencing depressed employment prospects.

In other words, to the extent that urban labour markets under-perform due to locational and access problems, the issue – and challenge for government – includes but extends beyond a distributional concern for the welfare of the people directly disadvantaged to the question of allocative efficiency in the economy at large.

This project:

- Identifies the main issues and policy concerns in relation to housing affordability and regional labour markets, with particular emphasis on the 'key worker' debate
- Reviews policy proposals put forward to deal with housing-related regional labour market failures

and seeks answers to the following **key research questions:**

- How does housing affordability influence labour market decisions?
- How are employment prospects and careers of low and moderate income earners impacted by housing costs? To what extent does the spatial mismatch between housing and job opportunities contribute to urban labour market failure?

New Cities, New Barriers

Major cities, including Sydney and Melbourne (and, to a lesser extent, the smaller capitals), are undergoing significant economic and social restructuring in the current phase of 'Globalisation'. The urban theorist Saskia Sassen identifies a number of large metropolitan regions in the developed world which play an increasingly important role globally. These cities are those that (1) act as command points in the organisation of the world economy, (2) serve as key locations and market places for the leading industries of the current era, notably finance and other advanced business services, and (3) are the sites for production of those leading industries, and the locus of innovation driving growth in these and client industries. The labour market in these cities displays increasing concentration and differentiation, dividing – broadly – into 'new economy' and 'old

economy' jobs. The former are high value-adding, highly skilled and high paid occupations, particularly in advanced business services and other 'knowledge-intensive' occupations. The latter are routine, low skilled and low paid jobs in the service sector, transport and manufacturing.

The new economy is therefore creating a spatially concentrated demand for the services of workers at both ends of the skill and wage spectrum in particular parts of the metropolitan region (especially in the inner core), a phenomenon that entails the emergence of what might be called a 'synergistic dual urban labour market'. For the functional efficiency and growth of the urban economy, an important prerequisite is an adequate supply of workers in both categories, raising questions as to both the necessary skills base of urban workers and their job accessibility.

However, it is clear that declining housing affordability in dynamic 'world cities', apparent over the past decade in particular – and the resulting location of the affordable stock – can result in an increasing 'spatial mismatch' between where many lower paid 'old economy' jobs are located in the metropolitan region and where lower skilled workers live. In effect, urban housing and labour markets may be inefficiently articulated over space with the consequences of shortages and recruitment difficulties in some lower paid but functionally necessary occupations and/or higher wages to offset high housing costs or more expensive commuting. In the latter context, a series of negative second-order externality effects may arise due to the sharp rise in car-dependant commuting. The implication here is that the more successful a city-economy is in the current global environment, the more its success is likely to be undercut by a growing spatial mismatch between housing and job opportunities for lower paid workers.

From this perspective, the location of affordable housing for working households is a critical economic rather than a social welfare issue. There are no powerful mechanisms that automatically ensure that the *residential location* of the functionally differentiated and skilled work force will routinely facilitate their effective access to the range of required jobs at the right locations. In fact, to the extent that urban housing markets are also segmented and – for example, push lower income households towards and beyond the periphery – the opposite may increasingly be the case. An increasing spatial mismatch of housing and employment may undercut the functional efficiency of the urban economy by blocking the productivity-enhancing interactions necessary for industry clusters (and the inter-agency networks on which they are based) to work. Put another way, metropolitan wide polarisation of housing opportunities may destroy the integrated employment mix required for globally competitive production in particular parts of cities (e.g. the central core) like Melbourne and Sydney. The crucial policy significance of this situation is that failing urban labour and housing markets could exact a substantial efficiency cost in foregone growth and welfare on the regional and national economy.

The Spatial Mismatch Hypothesis

Questions surrounding the spatial disjunction of housing outcomes and labour market demands first arose in the United States in the late 1960s. There the emphasis was on the equity or distributional effects of urban concentration ('ghettoisation') of urban blacks in the inner city of large metropolitan regions, in the face of the increasing suburbanisation of employment. Two major conclusions can be drawn from this US research. First, the intensity of spatial mismatch effects vary within large metropolitan areas and impact most in urban sectors where housing segregation on racial lines is most pronounced and poor transport access

(especially for reverse-commuting) most evident. Second, the research seems to show that where spatial mismatch persists over long periods, a combination of barriers – an absence of information on suburban job opportunities, cultural reluctance to search in white areas, pervasive racial discrimination in job and housing markets, etc. – rather than a single cause is responsible.

The New Focus

Over the past decade, research and policy interest has shifted direction, animated not by a renewed concern for civil rights or distributional justice, but by the dynamics of welfare reform conditioned by an increasing concern about the creation of an 'urban underclass' – in European countries termed 'social exclusion' – raising the challenge of how resulting 'welfare dependence' could be addressed. Thus, the particular racial dimension to spatial mismatch has been overtaken by more general forces and outcomes – although, in the US, it is the case that the underclass, so-called, is heavily racialised.

Broader patterns of spatial mismatch emerging in large cities, it is feared, undercut the basis for effective policies in welfare reform and social inclusion favoured by both neo-liberal and 'new labour' governments. If welfare recipients can't meaningfully access suitable jobs in the metropolitan region then policy regimes designed to move people off benefits and into employment will be self-defeating and likely to add to, rather than reduce, problems of social marginalisation and exclusion. In this situation, effective welfare reform will require complementary policies aimed at offsetting or undermining the forces that result in spatial mismatch in particular urban regions. More to the point, failure to deal with work disincentives undermines the efficiency of the lower skilled reaches of the labour market. By dealing successfully with this dimension of urban labour market-housing market failure, marginalised groups will benefit through enhanced economic welfare *and* the regional economy will operate more efficiently through drawing on more responsive labour markets.

Housing markets, it is feared, are pricing low and moderate income households out of job-rich areas and injecting a spatial dimension to supply-side constraints on economic growth. Moderately paid workers essential to the smooth functioning of the urban economy are less able to find and keep employment. Spatial dislocation of housing and labour markets also increases the probability of job informational deficits and asymmetries and job search costs, imposing further efficiency costs on the economy. Poor housing affordability, in this view, results in both increasing housing stress (housing-related poverty) and urban economic inefficiency.

In the United States, recent research carried out by the Essential Worker Immigration Coalition, Urban Land Institute and National Housing Conference points to the shortage of 'workforce housing' for low and moderately paid workers in many large American cities. The occupations identified include, teachers, police officers, municipal employees in both white and blue collar jobs, and workers in health care, retail and hospitality industries. Such households with at least one member in the employed workforce – and hence, not primarily dependant on welfare benefits – are likely to be in housing stress, facing constrained employment prospects and poor access to available jobs. High unemployment and labour recruitment and retention problems are likely to coexist with high job vacancies in many of these occupations throughout the metropolitan region, undercutting the growth prospects of the regional economy.

Whereas attention in the US has been directed across a range of industries and occupations in both the public and private sectors, including but moving beyond 'the working poor' to consider the access problems facing moderate income workers, research and policy action in the United Kingdom has been more narrowly focused on specific public sector occupations in particular regions where high housing costs and rapid house price inflation have created problems of recruiting and retaining teachers, nurses, police and other emergency service officers, municipal officers and health care workers. Many of these occupations are semi-skilled or para-professional with remuneration levels inflexibly fixed on a national basis that does not allow employers flexibility in tailoring salaries to local housing and cost of living conditions.

Members in these targeted occupations are referred to as 'key workers' who are defined as '...someone who is: employed by the public sector; in a frontline role delivering an essential public service, and in a sector where there are serious recruitment and retention problems' (ODPM, 2005c, p. 14).

In March 2004 the UK government introduced a 'Key Worker Living' program (KWL), to assist in the provision of housing to people in these occupations, with central government funding of £690 million committed. KWL was introduced as part of a broader central government agenda to ensure 'sustainable communities' (ODPM, 2004b).

The new £690 million scheme offers four simple options, including home ownership packages and intermediate rental solutions and will be marketed by one-stop shops located in London, the South-East and the East of England, where house prices are high and recruitment and retention is difficult. Eligibility varies across the regions depending on local recruitment and retention priorities (ODPM, 2005a, p. 1).

British research has established that key workers particularly value improved access to home ownership and that this is an important determinant of whether they are attracted to jobs in high house value regions. Affordable home ownership options also influence the decision of key workers to stay in the region or seek employment elsewhere. When key workers have been in their job for around 5 years they are likely to be at a critical juncture in their careers and/or lives. It is at this point that home ownership assistance can make a major beneficial impact.

Morrison and Monk (forthcoming), in their study of Surrey, found a high degree of employer concern about the barriers to getting and keeping lower paid workers in a rapidly growing region attracting high value-adding internationally connected firms and high income earners who commute into London. These concerns cut across public and private sector divisions and included a much broader range of occupations than those targeted by current government policy.

The overriding concern expressed by public sector employers centred on the significant number of applicants either withdrawing their application, or not even making one after inquiring about housing costs in the area. Candidates often turned down job offers once interviewed. The primary reason given was that they could not afford to live in Surrey (ibid., p. 11).

In the private sector, similar recruitment and retention problems were found, particularly in the lower-paying service sector companies – in retailing, entertainment, leisure and hospitality and personal services. These are industries which compete on low margins and depend on a low-paid, flexible, casual work

force. Retailers interviewed reported high turnover among both sales assistants and junior managers. The privatised public transport companies reported similar problems and expressed concern that high training costs were being incurred due to high labour turnover. High local housing costs were seen as a major factor in recruitment and retention problems in these service sector industries. Interestingly, employers in these industries face similar constraints on the capacity to pay higher wages in order to attract and keep workers as do public sector employers. Intense competitive pressures on a national scale in areas like transport severely constrain employers from paying enhanced local wages in Surrey

Conversely, private sector employers in growth industries like electronics, avionics (Gatwick airport is nearby) and information technology reported no significant staff recruitment and retention problems. Many of these companies are large international firms in high value-adding areas. Salary scales were flexible and set taking into account high local housing costs and the housing aspirations of workers. Generous relocation and mortgage assistance packages were available to some staff, as were benefits like car allowances and health care schemes.

The Australian Situation

There has been little research into the spatial mismatch hypothesis in Australia and what has been done is largely indicative or based on essentially anecdotal evidence. This follows, in part from the paucity of relevant data at appropriate spatial scales. However, the results to date, limited as they are, do suggest that larger Australian cities, particularly Sydney and Melbourne, may be experiencing some of the negative impacts of spatially mismatched housing and labour markets, at least with respect to the operation of their economically dynamic inner core economies.

Australian metropolitan regions display high levels of urban containment – i.e. most people live near to where they work, due to substantial employment decentralisation following post-War suburbanisation. However, processes of residential and commercial gentrification over the past 20 years have progressively pushed the stock of affordable housing for lower income people towards the urban periphery. The AHURI study by Yates et al. (2006) found housing stress problems were very high among people like sales assistant, cleaning and hospitality workers working in the highest cost housing market areas. Those lower paid less skilled workers employed in the central city tended *not* to be primary income earners or the partner of the primary earner but secondary income earners likely to be living in the parental home or in shared accommodation. The former group working in the central city were more likely to live further out in the metropolitan area and depend on long commuting trips. This provides some initial evidence for the spatial mismatch hypothesis in the context of the emerging ‘synergistic dual urban labour market’ in central Sydney and Melbourne, at least. It suggests that the supply of lower skilled workers needed to service the high-value new economy industries is strongly dependent on workers living in relatively temporary households, including young renters, more affluent childless renting couples and a stream of temporary visitors or ‘backpackers’. Yates et al (ibid., p. 88) further suggest that ‘employers will be able to address their [recruitment and retention] problems by employing a continuing supply of young, mobile workers by providing better wages and better conditions. The continued costs associated with retraining will be passed on in higher prices.’ It remains an open question, however, whether this potentially very mobile, mixed and uncertain supply of lower paid, ‘flexible’

labour will adequately meet the functional needs of the globally oriented economy centred in the core areas of the major cities.

Dodson (2005), on the other hand, finds little evidence of spatial mismatch in his study of Melbourne. He focused on three outer suburban areas in the west, north and south-east of the metropolitan region in which local unemployment rates were high and housing relatively affordable. He found that areas in which housing was relatively affordable were also areas where employment growth was buoyant. This suggests that other reasons account for higher than average unemployment rates in those areas, for example, skills deficits and poor public transport. He further suggests that many traditionally low status outer suburbs – e.g. in the West – have been recently ‘surrounded’ by new up-market housing developments that have acted as magnets for employers, particularly in the service sector. Hence, lower income workers living near those new high status suburbs have benefited from the local growth in jobs, provided they have had the necessary skills and could access them by private or public transport.

Dodson’s conclusions are constrained by the narrow focus of his study on three arbitrarily chosen cases and by the wide radius (10 kilometres) used to define the local employment area in each case. Thus, his analysis suffers from some of the weaknesses identified in the earlier comparable US research (see chapter 3). In this context, it is not clear that Dodson’s interpretation of the data actually supports his conclusion of limited or no spatial mismatch. In particular:

- Poor job information and transport barriers may still mean that low-wage workers are unable to access local jobs, even when job vacancies are high in the area. There is no necessary relationship between where in the outer areas most jobs are being concentrated and how accessible these job growth precincts actually are to workers seeking affordable housing. The poverty of public transport in outer areas of the metropolitan region, especially in Melbourne and Sydney, make comparisons of physical distances problematic. Hence, continuing high unemployment in broad regions where job growth is strong may still hide localised patterns of spatial mismatch between employment and affordable housing. If this is coupled with poor job information about opportunities further a field and poor inter-suburban transport, the degree of spatial mismatch is reinforced for those households pushed to inaccessible, lower housing cost locations.
- More importantly, Dodson’s analysis focuses – as did Kain’s original SMH – on the socio-economic or equity concerns about employment opportunities for low-wage workers. His analysis does not address the main focus of this report – viz. the functional inefficiency of urban labour markets due to housing market failure.

With respect to the latter point, the fact that Dodson – like Yates et al – found that inner city labour markets are very tight relative to other areas of the metropolitan region, suggests that labour bottlenecks may indeed constrain the most dynamic, centrally located new economy industries and their support service requirements. However, these forces may be more intense in Australia’s largest cities. Nygaard et al. (2005), for example, found convincing evidence that the spatial impacts of the economic restructuring of Sydney and Melbourne, reflected and reinforced through polarising urban housing and commercial property markets, are creating the potential for an intensifying spatial mismatch between where lower-waged workers functionally necessary to support the growth of the new economy live and

where their labour is required. These outcomes were much more muted in Adelaide.

Policy Approaches

The main efforts to address, in policy terms, the impacts of spatial mismatch have been attempted in the United Kingdom. There attention has been narrowly focused on assisting particular categories of public sector employees to access affordable housing in high cost housing regions in and around London in order to ease the labour recruitment and retention problems of public agencies in the education, health and emergency services areas. The emphasis has been overwhelmingly on helping these workers into home ownership. The main program – Key Worker Living – has assisted about 8,000 households, largely through the provision of ‘equity loans’. In early 2006 the definition of ‘key worker’ was broadened a little but still focuses exclusively on the public sector. The research summarised in chapter 3 points to the significant labour market problems that still exist for many private sector employers of lower and moderate income workers in those areas.

There has been virtually no policy interest in key worker issues in Australian housing debates. This appears to be due to a series of factors: first, the particular spatial patterns of economic restructuring and socio-economic advantage and disadvantage characterising Australian urbanisation; second, the marginal status of housing on the agendas of governments in Australia; thirdly, the absence of detailed (as opposed to speculative and descriptive) research on the topic, and; finally, the tendency to see housing issues as primarily to do with social equity or justice concerns rather than economic efficiency and growth.

This issue may have salience beyond the major metropolitan regions in Australia. To the extent that low wage workers are being pushed out of the major cities to smaller towns and regions due to high housing costs, problems of spatial mismatch and declining housing affordability would appear to be reducing – but only in the metropolitan regions and only on the surface. The housing may be more affordable in smaller settlements but job opportunities worse or non-existent, throwing these workers onto the unemployment rolls of their new town rather than in the metropolitan region. This does not actually increase employment and output anywhere, though metropolitan unemployment figures have declined along with the demand there for affordable housing. In reality, all that has happened is that the now hidden problem of declining metropolitan housing affordability has shifted unemployment from one place to another

1 INTRODUCTION

Housing affordability problems arise when a household's income is insufficient to meet the various non-housing costs of living after paying for a dwelling of reasonable basic standard, appropriate to the size and structure of the household. Clearly, one important component of the affordability problem concerns the inadequacy of a household's income, which for most households, stems from position in the labour market, determined in large part by both the skills possessed and effective access to jobs for which current skills are relevant. In a companion report the author (Berry, 2006, p. 2) has argued:

... the delivery and location of housing has important economic implications for both the employment prospects of households and the functional efficiency of regional labour markets. Increasing residential polarisation in the metropolitan regions increases the difficulties and costs of getting workers – especially low-waged workers in the service sector – to and from work. To the extent that there develops a spatial mismatch between where people work and where they can afford to live, regional labour markets will fail to operate efficiently, resulting in labour bottlenecks and surpluses, reflected in higher wages in some areas coinciding with persistent frictional unemployment in other areas. The lack of local jobs can then result in the growth of deeper structural unemployment in marginalised areas, which then assumes an inter-generational character.

If the inability to get and keep a job is purely access related – i.e. is not caused by an absence of skills – then the resulting unemployment or underemployment is frictional rather than structural in character. Policy responses would then focus on ways of improving effective access of disadvantaged groups to employment, instead of dealing with the structural sources of the skill deficit. Inefficient (non-clearing) urban labour sub-markets, in general, ensure that the urban economy underperforms; resources are not allocated to the most efficient uses and over time there is a loss in potential economic welfare. These effects are widespread and not confined to the particular group or groups experiencing depressed employment prospects. In other words, to the extent that urban labour markets under-perform due to locational and access problems, the issue – and challenge for government – includes but extends beyond a distributional concern for the welfare of the people directly disadvantaged to the question of allocative efficiency in the economy at large.

In situations where a 'spatial mismatch' between jobs and people emerges, there are three broad policy responses. *First*, move the jobs to the people, for example by encouraging new firms to locate in or existing firms expand in job deficient regions. Conventional regional development policies stretching back to the 1960s in countries like the United Kingdom and Australia provide examples of this approach. The policy levers applied include industry-specific subsidies, dedicated infrastructure, tax benefits and the like. More recent policies that focus on improving the 'milieu for innovation' seek to make depressed areas more attractive to leading-edge, knowledge intensive firms and may – as a side effect – either improve job prospects for lower skilled residents or help unleash displacement forces that push these households out to areas where they can afford housing. In

the latter case, the problem of reducing labour market inefficiencies may simply be shifted spatially to other parts of the urban area.

The *second* approach tries to bring people to the jobs. It is here that housing policy is most relevant. Interventions through direct social housing provision or subsidy arrangements that encourage private provision of housing at below-market prices and rents or land use planning regimes that mandate the provision of affordable housing can achieve this outcome, as well as other outcomes like improved social mix and greater access to non-work related amenities and services. The *third* approach focuses on improving the intra-urban mobility of disadvantaged households, especially by investing in improved urban transport infrastructure and operation. Time-cost access will depend on where these households live compared to the public transport and road networks (where the roads, rails and electricity wires are installed) and to the operational characteristics of public transport (cost, frequency and reliability of services) and the patterns of car ownership, access and use.

This project focuses on the extent to which housing market and housing affordability issues and policies are relevant to the question of urban labour market dysfunction, in the context of the processes of global restructuring influencing contemporary patterns of urban development in countries like Australia. Hence, housing affordability is here viewed from the efficiency rather than equity perspective. This is not to downplay the distributional rationale for affordable housing policy but merely to stress that these important issues are not addressed in this paper.

1.1 Objectives of the Project

This project will:

- Identify the main issues and policy concerns in relation to housing affordability and regional labour markets, with particular emphasis on the 'key worker' debate
- Review policy proposals put forward to deal with housing-related regional labour market failures

In order to pursue these objectives, the following **key research questions** are posed:

- How does housing affordability influence labour market decisions?
- How are employment prospects and careers of low and moderate income earners impacted by housing costs? To what extent does the spatial mismatch between housing and job opportunities contribute to urban labour market failure?

1.2 Structure of the Report

The debate on the spatial mismatch of urban labour and housing markets, including the recent focus on 'key workers', is addressed in chapters 3 and 4, drawing mainly on existing data and analysis from the United Kingdom, United States and Australia. The point is made that primary concern here is with the possible inefficiencies created for the urban economy as a result of inadequately located affordable housing. However, before this it is necessary to review the extensive literature on the contemporary processes of urban restructuring in the advanced capitalist countries over the past 20 years and the implications for both labour markets and housing markets in countries like Australia. It is the collective impact of these forces that is likely to be creating the current patterns of spatial

mismatch between jobs and housing affordability. This discussion, in chapter 2, is conditioned by alternative attempts to unpack the complex and 'essentially contested concept' of 'Globalisation'. Chapter 5 takes up and discusses the policy responses that might address the economic problems embedded in under-performing urban labour markets, looking in particular at recent British experience. The final short chapter summarises the findings of the report.

2 DIMENSIONS OF URBAN RESTRUCTURING

Over the past 20 years there has been a burgeoning literature on the changing nature of the urban economy and urban society in the current era of 'Globalisation' – e.g. Friedman, 1986; Harvey (1989); Sassen (1991, 1994); Berry and Huxley (1992); Fagan and Webber (1999); Fainstein et al., 1992); Hamnett (1994); Hamnett and Cross (1998); Scott (1988); Amin and Thrift (1994); Musterd and Ostendorf (1998); Marcuse and van Kempen (2002); Walks (2001); Scott et al. (2001); O'Connor et al. (2001). This work, in turn, derived from a slightly earlier focus on the nature of economic restructuring in advanced capitalist countries, in the era of what was variously termed 'Post-Fordism' or 'flexible production' (Aglietta, 1980; Piore and Sabel, 1984; Scott and Storper, 1986)¹.

2.1 Economic restructuring

Although emphases varied in this diverse and complex body of work, the overall thrust was to the effect that the national economies – developed and developing – were being restructured to re-establish the conditions for profitable capital accumulation in a world brought closer together by the increasing mobility of capital, especially finance, and rapid advances in information and communications technologies. The political pre-conditions were crafted alongside these economic changes – and, indeed in some views, were essential to them – expressed as the triumph of 'the Washington Consensus', entailing a neo liberal concern for free trade, small government and deregulated financial markets (Stiglitz, 2002).

Although the predominant dynamic identified was 'Globalisation' – the increasing integration of national and regional economies – it became clear that political-economic integration was occurring in a geographically uneven way. Different 'places' assumed specific roles and functions. In particular, some large city-regions became 'command points' and the activities organised within and between them play a defining role in determining the overall economic (and political) outcomes for the nation states comprising the world economy. For example, Sassen (1994, p. xiv) sets out to show '...how some cities – New York, Tokyo, London, Sao Paulo, Hong Kong, Toronto, Miami, Sydney, among others – have evolved into transnational market "spaces"'. As such cities have prospered, they have come to have more in common with one another than with the regional centers in their own nation-states, many of which have declined in importance.' Sassen (ibid., p. xiii) further stresses that; '(t)here is no such entity as a global economy "out there", in some space that exists outside nation-states. Rather, the location of transnational spaces within national territories defines the current phase of the world economy'.

In this view, 'real cities' are institutional complexes that contain numerous activities and transactions, some of which are purely localised in their form and impact, while others cross regional and national borders and have a determining impact on a large geographical scale.

Processes of economic globalisation are thereby reconstituted as concrete production complexes situated in specific places containing a multitude of activities and interests, many unconnected to global processes. Focusing on cities allows us to specify a geography of

¹ Earlier AHURI research reports have summarised some of this literature: see Dodson (2003) and Yates et al. (2005).

strategic places on a global scale, as well as the microgeographies and politics unfolding within these places.... In the current phase of the world economy, it is precisely the combination of the global dispersal of economic activities and global integration – under conditions of continued concentration of economic ownership and control – that has contributed to a strategic role for certain major cities that I call global cities (ibid. p. 4).

This characterisation of some cities as forming ‘a geography of strategic places on a global scale’ accounts for the seemingly contradictory notion of a global economy in which capital and production is increasingly mobile and national borders increasingly irrelevant *and* which favours the growth in the size, prosperity, function, power and reach of particular cities – and, it might be added, the persistence of the nation-state. Global cities, for Sassen, are those that (1) act as command points in the organisation of the world economy, (2) serve as key locations and market places for the leading industries of the current era, notably finance and other advanced business services, and (3) are the sites for production of those leading industries, and the locus of innovation driving growth in these and client industries.

The earlier work on global cities, including that of Sassen, stressed the emergence of a hierarchy of cities, with some – like New York, Tokyo and London – ‘the first among unequals’. First-order and lower-order global cities could be distinguished not merely by their size and growth but, critically, by the number of head-quarters of leading transnational firms in manufacturing, transport and – especially – advanced business services. It is this later group of industries that increasingly influences the global flows and transactions of modern economies and facilitates the organisation of production on a world scale. ‘Advanced business services’ (ABS: also termed ‘producer services’) include: firms operating in the banking and finance, legal and para legal, accounting, advertising and marketing, design, property and real estate development industries. The products of these industries are strategic and increasingly important inputs to the economic activities of other firms ranged across the economy². ABS tend to be dominated by a small number of large firms, operating on a multinational scale and concentrated in the CBDs of major cities. The types of employment generated by the growth in ABS range from highly knowledge-intensive jobs (e.g. lawyers and chartered accountants) to semi-skilled and unskilled support jobs (e.g. office cleaners and receptionists). Tight co-location in city centres enables these firms to benefit from the communication infrastructures linking them to similar centres in other cities and, more broadly, to world markets *and* the face-to-face contacts with each other, the headquarters of major clients and government. Work in many of these firms is divided between specialists in different fields, enabling cooperative teams to be assembled – e.g. comprising management consultants, financial analysts, technology experts, legal experts, etc. – to add maximum value to their clients’ activities. Co-location facilitates the trust relations necessary to form effective teams and facilitates fast-response and flexible delivery of services to demanding clients, themselves dealing with the highly competitive realities of competing in world markets. Co-location also enables individual producer services firms to accurately monitor and evaluate the performance of both competitors and collaborators and to adjust their

² Most of these industries also provide services to consumers. However, their strategic role and impact in the economy is tied to their location in the value chains of client firms – i.e. to their capacity to enhance their clients’ productivity and profitability (often referred to as ‘value creation’).

behaviour accordingly. Finally, centrality and spatial closeness to markets and regulators boosts access to market-sensitive information and opportunities through tapping into informal information networks that often depend on serendipitous face-to-face meetings in neutral 'third places' (neither home nor work), such as clubs, cafes or cultural and recreational events.

2.2 Occupational restructuring

The growth of advanced business services underscores a more general change in the occupational structure of advanced economies. Following Reich (1991), jobs can increasingly be divided into those requiring intensive training and entailing the manipulation of information or knowledge ('symbolic-analytical services'), those oriented towards meeting the needs of consumers ('in-person services') and those located in traditional manufacturing, construction and transport industries ('routine production services'). The first category of jobs – symbolic analysts – is held to relate to (drive) 'the new economy' comprising the key globally oriented value creating industries – viz, advanced business services, communications, 'the creative industries' and knowledge intensive (elaborately transformed) manufacturing. An overlapping and more recent analysis in this vein has been provided by Richard Florida (2002; 2005), who argues that the new economy is essentially dependent on the mobilisation of the skills, knowledge and commitment of 'the creative class', made up of 'the super creative core' and 'creative professionals', together including Reich's symbolic analyst group. An Australian approach along these lines is provided by Brain (1999), who focuses on the strategic role of the C21s – i.e. the key workers of the 21st century. There is a large overlap between the occupational groupings of Reich, Florida and Brain. The common claim is that these are the jobs and industries that characterise and drive 'the new economy' in the current era of globalisation. Florida (2004) also argues that these creative workers are highly mobile and globally marketable and that capturing them is essential for the economic prosperity and position of particular city-regions³.

In this vein, O'Connor et al. (2001: p. 59) characterise the Australian situation as follows:

Global change, as reflected in the growth of symbolic analysts, the expansion of the services sector, the rise of part-time work, and investment in office and business parks has been seen as evidence of a 'new economy' in Australia. This new economy is anchored in the intersection of telecommunications and computing, so that much of its activity involves information storage, transmission, and analysis along with work in the business services sector. The restructuring of the Australian economy is associated with these activities and has created new types of work, new arrangements for employment, and new ways of doing business ... and results in a powerful set of forces acting on the geography of the nation.

³ The National Institute for Economic and Industry Research (2003) has applied Florida's analysis and categories to all regions in Australia. For a summary of the NIEIR research and a critical review of Florida's work, see Berry (2005).

2.3 Spatial differentiation

According to theorists like Sassen, the growth and concentration of ABS and other knowledge-intensive jobs in the centres of large urban regions increasingly differentiates cities on a global scale with respect to size, function, influence and prosperity. Just as dramatically, the emergence of the new economy is creating pervasive patterns of spatial differentiation *within* these cities. The polarisation of the occupational structure is resulting in increasing economic inequality that is being expressed and reinforced spatially. The growth and central concentration of ABS, in particular, is creating a rising demand for both highly skilled, high-wage workers and for low skilled, low-wage workers. In part this dual demand reflects the internal structure of firms in ABS – e.g. the need to employ secretaries, receptionists, security and maintenance workers, as well as managers and senior partners. However, increasingly many of these inputs are being outsourced, provided by a plethora of small service firms in the building services, hospitality and transport industries. The growth of these support services in areas like transport, retail and hospitality are also concentrated in central areas close to the headquarters of the leading firms in finance, consulting, manufacturing and resources. The new economy is therefore creating a spatially concentrated demand for the services of workers at both ends of the skill and wage spectrum, a phenomenon that entails the emergence of what might be called a ‘synergistic dual urban labour market’. For the functional efficiency and growth of the urban economy, one prerequisite will therefore be an adequate supply of workers in both categories, raising questions as to both the necessary skills base of low skilled workers and job accessibility. Finally, it appears that this pattern of polarisation, resulting in the growth of both high-wage and low-wage jobs, is most prevalent in those cities that are most globally connected. Moreover, Sassen argues, it is in the centre of these cities that economic activities are globally connected, differentiating the city centres from their surrounding suburbs and hinterlands. Centrally located, globally connected firms are also likely to be more profitable than other domestic firms in locally oriented industries, further cementing inequalities within the urban economy. The evolving spatial structure of Australian cities over the past 30 years has witnessed significant ‘gentrification’ of the inner suburbs and CBD. Lower income households have been pushed further out to the periphery and beyond, potentially intensifying the problems of access to routine low-paid jobs in the centre. Australian cities, unlike their US and, to a degree, UK counterparts do not have economically depressed inner areas housing low income households. Nor have high value-adding jobs been decentralised to the suburbs of Melbourne and Sydney as they have in large US cities (Freestone and Murphy, 1998; O’Connor and Healy, 2002), increasing the likelihood of a spatial mismatch between the demand for low-wage workers in the inner city and the peripheral housing locations of these workers.

The fact that globalisation has and is resulting in a more uneven spatial pattern of development both within and between city-regions, seems to contradict the underlying fact that this is occurring in a world that is increasingly integrated, economically and culturally, due to the mobility of financial capital and ‘footloose’ manufacturing, facilitated by major technological advances in communications technologies and the partial, uneven but discernable move towards free trade and financial deregulation; ‘and therein lies a paradox: the enduring competitive advantages in a global economy lie increasingly in local things – knowledge, relationships, motivations – that distant rivals cannot match’ (Porter, 1998a, p. 78).

2.4 Agglomeration

Theorists like Sassen provide part of the resolution – viz. particular parts of certain cities support the directive operations of global firms, especially the ABS sector or ‘creative professionals’, and therefore express a new, hardening pattern of international urban specialisation. However, other ‘logics of agglomeration’ are also at work. Porter (1998a, 1998b, 2000) argues that the agglomeration economies that increasingly construct competitive advantage for individual firms in particular places do not – as in the past – reside at the industry, sector and metropolitan levels but arise from the alliances and networks formed between firms at different points in the value chain (i.e. across different industries) and other organisations whose activities improve the productivity of all engaged in these interactions. For Porter (ibid., p. 197):

Clusters are geographic concentrations of interconnected companies, specialised suppliers, service providers, firms in related industries, and associated institutions (for example, universities, standards agencies and trade associations) in particular fields that compete but also cooperate. Critical masses of unusual competitive success in particular business areas, clusters are a striking feature of virtually every national, regional, state and even metropolitan economy, especially those of more economically advanced countries.

And, again:

A cluster is a geographically proximate group of interconnected companies and associated institutions in a particular field, linked by commonalities and complementarities (ibid., p. 199).

The urban concentration of ABS, in Porter’s view, therefore figures as a component part of a number of specific clusters of complementary agents, all of whom benefit from geographic proximity. Much attention has been devoted to clusters in areas of advanced manufacturing and technologies, like ICT and aerospace. However, clustering also appears to characterise global competition in a whole range of new and traditional industrial fields, including food, tourism and construction⁴. The advantages to individual cluster members are various and include:

- improved access to specialised inputs and workers
- greater (and faster) access to vital information
- the creation and capture of complementarities of operation – i.e. improved performance in one part of the cluster opens up new opportunities for other cluster members
- stronger incentives to perform – and penalties for non-performance

A second generalised advantage of clusters is that regions in which active, overlapping clusters operate seem to encourage *innovation* – to be what have been termed ‘innovative milieu’ (Maillat, 1995) – which, in turn, underpins competitive advantage and drives general economic growth in the local and national economies. Third – and in a related sense – once industry clusters take off in particular places they tend to be self-generating, since they act as magnets

⁴ For an analysis of cluster dynamics in a number of fields, see OECD (2001).

for new businesses and agencies seeking to participate in the mutually beneficial interactions supported.

Economically speaking, the key characteristic of a working industry cluster is that it is greater than the sum of its parts, since it generates recurrent communication and cooperation between cluster members, as opposed to the essentially passive traditional agglomeration economies that arise from co-location near port infrastructures and a large urban labour market. 'For us, innovative industry clusters are not a simple concentration of independent economic agents, but display at an inter-industrial level, underlying networks of interrelated cooperating businesses' (Debresson, 1996, p. 161)⁵.

What this analysis of clusters and urban agglomeration underscores is the highly integrated but segmented nature of urban labour markets. In the first place, urban labour markets are functionally specialised according to skills and the capacity to contribute to the competitive advantage of employing organisations operating within a highly competitive global environment. Secondly, urban labour markets are segmented on a spatial basis, with particular sets of jobs located in particular cities and particular parts of cities. There are no powerful mechanisms that automatically ensure that the *residential location* of this functionally differentiated and skilled work force will routinely facilitate their effective access to the range of required jobs at the right locations. In fact, to the extent that urban housing markets are also segmented and – for example, push lower income households towards and beyond the periphery – the opposite may increasingly be the case. An increasing spatial mismatch of housing and employment may undercut the functional efficiency of the urban economy by blocking the productivity-enhancing interactions necessary for industry clusters (and the inter-agency networks on which they are based) to work. Put another way, metropolitan wide polarisation of housing opportunities may destroy the integrated employment mix required for globally competitive production in particular parts of cities (e.g. the central core) like Melbourne and Sydney. The crucial policy significance of this situation is that failing urban labour and housing markets could exact a substantial efficiency cost in foregone growth and welfare on the regional and national economy.

The next chapter explores this thesis further in the context of a number of international studies.

⁵ The idea behind clusters goes back to the work of Marshall (1921) who introduced the term, 'industrial districts' to capture many of the inter-firm advantages of co-location. More recent research has focused on structure and role of 'networks' in cluster dynamics. For a review of this literature, see Berry (2003, ch.3).

3 THE 'KEY WORKER' DEBATE: INTERNATIONAL PERSPECTIVES

Housing is a crucial component of economic competitiveness. The growing spatial mismatch between where job growth is taking place and where people can afford to live creates costs for employers as the local labour pool contracts and employee turnover rises (Harvard Joint Centre for Housing Studies, 2000, p. 1).

The original critical analysis of the 'dysfunctionality' of urban labour (and housing) markets was advanced in the 1960s by the American urban economist, John Kain (1968), though the germ of the spatial mismatch problem can be traced a little earlier (Kain, 1964). Since then, there have been many attempts to test and refine the hypotheses first advanced by Kain; for reviews of this work, see Holzer (1991); Kain (1992, 2004); and Ihlanfeldt and Sjoquist (1998). The workers identified in this early research were poor urban blacks living in the centres of large metropolitan regions. More recently, the 'key workers' targeted have been moderately skilled and paid functionaries in service (especially public) agencies. The focus of the early spatial mismatch research was essentially distributional, concerned about the welfare of the marginalised urban black population. The recent work is explicitly cast within an efficiency context. Nevertheless, even in the former case, the question of black unemployment and underemployment, and excessive commuting, raised efficiency questions for the urban economy. This chapter will first review key findings from the research stimulated by the original Kain thesis and then focus on the later work.

3.1 Race and spatial mismatch

Kain's original hypothesis was that there were fewer jobs per worker in or near areas where black urban Americans lived, than in white dominated areas, resulting in black workers being paid less or having to commute further in comparison to white workers with similar skills and qualifications. Ihlanfeldt and Sjoquist (1998, p. 851) argue that this hypothesis rests on three premises: first, the claim that jobs have shifted away from black neighbourhoods, historically concentrated in and near the city centre; second, racial discrimination in housing and mortgage markets has prevented blacks from moving out to the suburbs after jobs; and, third, poor job information, limited transport opportunities and customer racial discrimination have restricted work opportunities for blacks in job-rich areas.

Ihlanfeldt and Sjoquist identify four distinct approaches to testing the spatial mismatch hypothesis (SMH) advanced by Kain and highlight the difficulties that arise in providing evidence for this hypothesis in each of these approaches.

1. *Racial comparisons of commuting times.* If blacks and other minority groups have less access to jobs than whites, then this may show up in differential commuting times – i.e. other things, equal, the former workers may, on average, travel further to work than the latter. Thus, McLafferty and Preston (1992), drawing on a national urban microdata set, found that black and Hispanic women had longer journey-to-work travel times than white women. Similarly, Gabriel and Rosenthal (1996), using data from the American Housing Survey, found that black workers had average commuting times 14 per cent longer than whites with similar qualifications and demographic characteristics. Greater commuting can have efficiency costs in the broader urban economy due to the negative externalities associated with intra-urban travel.

However, as Ihlanfeldt and Sjoquist argue, there are a number of difficulties in interpreting the significance of differential commuting times. Spatial mismatch will result in longer commutes only if blacks are able to access employment in job-rich areas, typically in the suburbs dominated by white residents. If black inner city residents have poor job information about where opportunities exist or poor transport access or face discrimination in suburban job markets, then their average commuting distances and times to the small range of jobs they can effectively access will tend to be *lower* than other groups. In other words, their job 'choices' will be severely constrained in number and space. Furthermore, standard models of urban economics point to the trade-off by higher income residents of distance and space/amenity. Higher income people will tend to commute further to work in order to consume more housing space and suburban amenities; this observed tendency is reinforced by the greater access of higher income households to car ownership. Unless income can be controlled for, this effect will bedevil any attempt to infer support for the SMH from differential commuting times, since whites have higher average incomes than blacks and other minorities.

The problem is that residential location is endogenous, at least for whites. Workers may voluntarily choose to make a longer commute in exchange for a lower unit cost per unit of housing or greater environmental amenities. Whites are more able to make these exchanges than blacks because blacks face discrimination in the housing market.... This situation confounds racial comparisons of commuting times or distances and renders them essentially irrelevant to the SMH (Ihlanfeldt and Sjoquist, 1998, p. 854).

In short, it is very difficult to sort out the effects on differential commuting times of spatial mismatch, on the one hand, and the structural impact of racial discrimination in job and housing markets, on the other.

2. *Job accessibility.* Spatial mismatch may exist when there are relatively few available jobs located *near* where particular groups live. The emphasis should be on 'available' jobs – i.e. those jobs for which the target group members are appropriately skilled. This immediately raises data problems. Most of the studies that adopt this approach are forced to use crude measures of job access, like total employment or vacancies by geographic area or proxies like commuting distance. In any event, the problem already noted – viz. the endogeneity of residential location – must be dealt with. For example, Cutler and Glaeser (1997) analysed the following outcomes for under-30 year olds across 204 metropolitan regions – high school and college graduation, idleness (neither working nor studying), earnings and (for women) unmarried motherhood. They found significantly poorer outcomes for blacks, with lack of job access accounting for between 20 and 40 per cent of the differences. However, they did not standardise for job type and mode of commuting which probably led to underestimating the effects of access to employment.

Holzer, Ihlanfeldt and Sjoquist (1994) used data from the National Longitudinal Survey of Youth for the early 1980s to explore the relationships between job search, commuting and the decentralisation of employment in 113 metropolitan regions. They addressed the endogeneity problem by assuming that the residential location decisions of young people are made by their parents, that is, exogenously. In other words, they assumed away the problem. Their measure of job access was crude – viz. the percentage of total metropolitan jobs located

outside the central area. Their findings were that black youth were likely to experience longer periods of unemployment and that blacks do not respond by commuting longer distances, either to search for or undertake employment, controlling for the time costs of travel. The first finding is consistent with the SMH, the second suggests that the persistence of spatial mismatch depends on factors like poor job information, employer discrimination and absence of skills, rather than inadequate access to transport. In a subsequent study, Ihlanfeldt and Young (1996) found that the relative inaccessibility of suburban employment was a significant factor in accounting for the persistence of spatial mismatch. More than a third of the difference in city-suburban black employment share was due to the location of suburban employers beyond walking distance from public transport routes, another third to their distance from the CBD and almost 30 per cent to racial discrimination by employers and customers. 'These results suggest that the physical inaccessibility of suburban job sites by public transit, the length of the commute (which may proxy either commuting costs or information on job opportunities), and labour market discrimination all represent important barriers that prevent blacks from securing suburban jobs' (Holzer, Ihlanfeldt and Sjoquist, 1994).

Weinberg (1998) compared 195 large city-regions and found that an increase in the proportion of metropolitan jobs located in the central city increased black employment rates, as did an increase in the proportion of blacks living in the suburbs. These effects were greatest for black youth, women and those without a college education, precisely those sub-groups that the SMH suggests would be least able to reverse-commute or access suburban housing. Ihlanfeldt and Sjoquist (1998, p. 868) point to the fact that Weinberg's results focus on larger metropolitan regions and strongly support the SMH, whereas a number of other multi-city studies that included small cities found little or no mismatch effect. This suggests that urban scale may have something to do with the degree of spatial mismatch occurring.

3. *Comparisons of central city and suburban residential location.* This approach tests for whether blacks who live in the suburbs enjoy significantly better employment outcomes than blacks located in city centres. This approach has tended to go out of fashion in the field (for the weaknesses noted below) and was mostly utilised in the 1970s and early 1980s (e.g. Harrison, 1972; Price and Mills, 1985). Cooke (1996) has, however, attempted to estimate the probability of employment of black males between 5 and 65, over nine metropolitan regions, including an independent variable for suburban location. The results are mixed and do not offer strong unambiguous support for the SMH, largely because they reflect the weaknesses of the approach noted below.

The first problem is the previously mentioned issue of the endogenous nature of residential location. Although suburban location in the US context may improve job access, it is also the case that people with a job (and income) may choose a suburban location. Any modelling of job access must simultaneously account for locational choice. Otherwise the estimate of the independent effect of job location will be biased. The second problem is that most approaches, including Cooke's, assume that job opportunities are spatially uniform within the central city region and within the suburban region. In reality, jobs cluster unevenly within each region.

4. *Comparing relative tightness of sub-metropolitan labour markets.* This approach seeks to provide support for the existence of the SMH – rather than

quantify its effects – by comparing the level of job vacancies and wages in central, as opposed to suburban areas. To the extent that mismatch exists, the job vacancy rate and/or wages are likely to be lower in central areas dominated by blacks, compared to looser conditions in suburban labour markets. This follows from the likelihood that there will be a surfeit of potential workers locked into the inner city job market and a tendency for rapid job growth in the expanding suburbs to outstrip available workers.

Turner's (1997) qualitative study involved interviews with 59 auto-workers in the Detroit metropolitan area, employed by 13 white and 13 black owned firms. She found that, regardless of race, average wages paid for similar jobs were higher in the suburbs – 22 per cent in the case of white-owned firms and 5 per cent for black-owned firms. Central city employers commented that they could keep wages low because of the excess number of local workers seeking local jobs. This suggests that residential location is critical; it is the fact that blacks are so strongly concentrated in central areas, where workers of all races are in excess supply, that the effects of mismatch bite deeply and disproportionately disadvantage blacks.

Ihlanfeldt (1999) in a comparative study of Atlanta, Boston, Detroit and Los Angeles, found that vacancy rates for low-skilled jobs in these cities were two to three times higher in white dominated neighbourhoods than neighbourhoods with large minority group populations, with the exception of Detroit where the difference was not statistically significant. Starting wages were also higher in the white neighbourhoods in Atlanta and Detroit but the differences were not significant in the other two cities. This study is useful since it controls for most of the key characteristics defining the resident populations, job levels and employer types. The variable results found in the four large metropolitan regions selected indicates that the intensity of spatial mismatch, where it exists, is likely to vary, between cities and over time. A plausible extension or corollary to the basic SMH might be that this effect first manifests as falling vacancy rates in central or minority group dominated areas and rising rates in the suburbs, which over time, leads to employer perceptions of surplus and deficient labour supplies, respectively, putting upward pressure on suburban wages and downward pressures on wages in the centre.

Looking overall at attempts to establish the SMH, it appears that, since 1990, there has been an upsurge of relevant US research, most of which provides varying degrees of support for the hypothesis (Ihlanfeldt and Sloquist, 1998; Kain, 2004). It is also clear that researchers face some major methodological and data problems in teasing out the relative importance of spatial mismatch effects in accounting for relative economic disadvantage across different urban sub-populations. The need to recognise and account for the endogeneity of residential location and the challenge of accurately measuring job accessibility loom large in any such analysis. That said, two main conclusions can be gleaned for the post-1990 research (Ihlanfeldt and Sloquist, 1998, pp. 880-881). First, the intensity of spatial mismatch effects vary within large metropolitan areas and impact most in urban sectors where housing segregation on racial lines is most pronounced and poor transport access (especially for reverse-commuting) most evident. Second, the research seems to show that where spatial mismatch persists over long periods, a combination of barriers – an absence of information on suburban job opportunities, cultural reluctance to search in white areas, pervasive racial discrimination in job and housing markets, etc. – rather than a single cause is responsible. *More importantly for the focus of this paper, it is becoming clear that the SMH may not*

only apply to particular racial or ethnic minorities but increasingly extends to most, if not all, lower income groups, including those in mainstream communities employed in low to-moderate paid jobs (see below).

One study by Jencks and Mayer (1990) that challenges the SMH argues that the observable and persistent differences in the employment prospects of black and white American urban residents are largely explicable in terms of the poorer job skills of the former group and have little or nothing to do with location and, hence, with the housing situation and opportunities of blacks. Kain (2004, pp. 21-24) however, points to the results of his later work in the 1990s that finds evidence for the effect of the locational concentration of black children on their relatively low levels of educational attainment and – hence – job skills and prospects. Indeed, he points to this long-term dynamic as ‘spatial mismatch’s worst case’ and concludes: ‘I continue to believe that we will make very little progress in eliminating the gap between Black and White children as long as housing market segregation continues to confine the low-income Black residents of our metropolitan areas to massive concentrations of poverty’ (ibid., p. 24). Kain’s conclusion echoes European research on social exclusion. For example, van Kempen (2002) has coined the term ‘poverty pockets’ to refer to areas of large segmented or ‘partitioned cities’ in ‘post-Fordist states’ which house large concentrations of low-income, welfare dependent groups. The first of the four mechanisms she identifies as constituting and reinforcing emerging patterns of socio-spatial segregation in large European cities – viz., poor access to job markets – explicitly draws on the SMH. The other three mechanisms noted are: stigmatisation, socialisation and loss of effective social citizenship rights.

An important question to pose is – why has there been a recent upsurge in interest in academic and policy communities in this field of research? Initially, the SMH was proposed during a period of intense scrutiny of cities and racial relations. Federal US programs during the mid-late 1960s ‘war on poverty’ targeted large urban regions in areas like housing, education and employment assistance. The major policy driver was distributional, focused on the broader debates on civil rights and economic citizenship. As these issues receded in the US political landscape, so interest in and research on the SMH declined through the 1970s and 1980s⁶. The resurgence of the 1990s, when it came, was not driven by a renewed concern for civil rights or distributional justice, but by the dynamics of welfare reform conditioned by an increasing concern about the creation of an ‘urban underclass’ – in European countries termed ‘social exclusion’ – raising the challenge of how resulting ‘welfare dependence’ could be addressed. Thus, the particular racial dimension to spatial mismatch has been overtaken by more general forces and outcomes – although, in the US, it is the case that the underclass, so-called, is heavily racialised.

...while the SMH was originally conceived to explain employment problems of inner-city minorities, urban structures have changed and class segregation has grown...so that spatial mismatch applies more generally to lower-skilled workers, regardless of race, whose residence may be outside the inner city. Thus, policies and programs that seek to address the problem of spatial mismatch need

⁶ In his personal perspective on the field of research he initiated, Kain (2004, p 16) commented: ‘(n)either the Reagan or Bush [senior] administrations asked my advice on questions relating to housing market discrimination, or for that matter any other area of housing policy. I offered unsolicited advice on occasion, but I have no evidence that anyone noticed.’

to target a population broader than just inner-city minorities (Ihlanfeldt and Sjoquist, 1998, p. 882).

Broader patterns of spatial mismatch emerging in large cities undercut the basis for effective policies in welfare reform and social inclusion favoured by neo-liberal and 'new labour' governments. If welfare recipients can't meaningfully access suitable jobs in the metropolitan region then policy regimes designed to move people off benefits and into employment will be self-defeating and likely to add to, rather than reduce, problems of social marginalisation and exclusion. In this situation, effective welfare reform will require complementary policies aimed at offsetting or undermining the forces that result in spatial mismatch in particular urban regions. More to the point, failure to deal with work disincentives undermines the efficiency of the lower skilled reaches of the labour market. By dealing successfully with this dimension of urban labour market-housing market failure, marginalised groups will benefit through enhanced economic welfare *and* the regional economy will operate more efficiently through drawing on more responsive labour markets.

3.2 The 'key workers'

Although ethnic and racial differences may loom large in analysing the patterns of socio-spatial segregation in US, European and, indeed, Australian cities – especially in the wake of the continuing immigration of people from less developed and war-torn countries – increasingly debate has shifted to a concern for the increasing difficulties lower income households in general face in finding affordable housing accessible to appropriate jobs. The at-risk households include those with at least one member who is in work, actively looking for work, or discouraged from looking for work. However, in addition to the welfare or distributional concerns for the disadvantaged (excluded) households, the policy focus has also targeted the *efficiency* consequences for local, regional and national economies. Housing markets, it is feared, are pricing low and moderate income households out of job-rich areas and injecting a spatial dimension to supply-side constraints on economic growth. Moderately paid workers essential to the smooth functioning of the urban economy are less able to find and keep employment. Spatial dislocation of housing and labour markets also increases the probability of job informational deficits and asymmetries and job search costs, imposing further efficiency costs on the economy. Poor housing affordability, in this view, results in both increasing housing stress (housing-related poverty) and urban economic inefficiency.

Recent research and policy debate on this topic has tended to target particular occupations, household types, demographic groups, patterns of work organisation and gender issues. An earlier AHURI report by Yates et al. (2005) provides a useful review of key literature in this vein in countries like the United Kingdom and United States. We draw on this review below before considering, in more detail, particular recent relevant studies.

3.2.1 The US situation

Yates et al. (ibid, pp. 9-14) summarise the results of two streams of housing affordability research and advocacy in the US. The first entails national studies of 'essential worker' shortfall by the Essential Worker Immigration Coalition (EWIC), a coalition of industry associations and interests concerned about labour shortages in both skilled and 'lesser skilled' but functionally important areas. The second stream focuses at the urban and local level, associated in particular, with the National Housing Conference (NHC) and the Urban Land Institute (ULI). The term 'workforce housing', rather than 'key worker housing' tends to be used in the US

debates (McIlwain, 2003). The national level concern focuses on immigration policy; however, as Yates et al. point out, the occupational groupings identified by EWIC overlap strongly with those pinpointed by organisations like the ULI as struggling with housing affordability at the local level – e.g. routine workers in hospitality, tourism, retail, construction and health care. The occupations represented are ‘old economy’ jobs, concentrated in Reich’s ‘routine production services’ and ‘in-person services’. These at-risk households have at least one member in fulltime (or near-fulltime) work and are therefore generally ineligible for welfare or housing-related assistance; they are sometimes referred to as ‘the working poor’, though this term is deceptive since many in this situation are well above even liberal characterisations of the ‘poverty line’. The studies noted by Yates et al. – viz. Stegman et al. (2000), Fiore and Lipman (2001), Harkness et al. (2002) and Harkness and Newman (2004) – establish, for a large number of American cities, that households with a single member employed in these moderately paid occupations are highly likely to be experiencing serious housing stress⁷. Nevertheless, it is not immediately clear in the US debates whether the major cause of the labour shortages in high housing cost areas is primarily due to the lack of affordable housing or an overall shortage of people with the required skills in particular occupations.

Workforce housing in the US has been called ‘intermediate housing’ in countries like Britain. ‘Workforce households’ are defined as:

households, with at least one full-time worker, whose members earn incomes that are too low for them to afford to pay market prices for homes or apartments in the communities where they work but, by most definitions, are too high to enable them to qualify for significant federal housing subsidies. The target group includes teachers, police officers, fire fighters, and other municipal employees, as well as health care workers, retail clerks, administrative personnel and other moderate-income workers, all of whom are essential to the economic vitality of a city or region and the success of its corporations, institutions and government functions (Urban Land Institute, 2003).

Organisations like the ULI and NHC are strong proponents of the view that housing affordability matters, both for the welfare of disadvantaged households and for the wider economy⁸. They point to (largely anecdotal) evidence that some employers have found it difficult to recruit particular occupations in some locations and responded by moving elsewhere, with negative development outcomes for residents in shunned locations – and presumably, efficiency losses due to a reliance on second-best locations. Other costs stem from higher than otherwise labour turnover – i.e. extra recruitment and training costs.

⁷ See Yates et al. (2005) for a discussion of these studies.

⁸ Yates et al. (2005, p. 10) quote from a report on a ULI forum convened in 2001 to address the issue: ‘(t)he lack of affordable housing in urban areas is leading many households to locate far from their jobs, creating all problems associated with sprawl, including traffic congestion, air pollution, environmental degradation, and requests for public funds to be used for the construction of new roads, schools, libraries, etc.’. This assertion extends the efficiency argument by highlighting the negative externalities generated by the decline of affordable housing opportunities in job-rich areas of large metropolitan regions.

3.2.2 *The UK situation*

The UK Government's *Housing Green Paper* (DETR, 2000) raised the issue of a group of public sector workers who, it was argued, were experiencing increasing difficulty in accessing affordable housing in some high housing-cost regions of the country, particularly in London and other areas of the South-East. This concern arose as part of a broader policy debate about the need to expand the stock of affordable housing – defined as lower cost, usually subsidized housing available to households who cannot afford market provided housing – in those regions (ODPM, 2003). The target group of key workers generally earned more than those eligible for social housing but not enough to afford market housing in the regional housing markets concerned. Although the term was applied across all housing tenures, there was particular policy resonance around the problem such workers had in accessing owner occupation in high-price markets. Central government saw the overall problem, not in distributional but efficiency terms; i.e. as undercutting the capacity of government at central and local levels to effectively deliver its services to the community, reflected in increasing difficulties and costs of recruitment and an increasing risk of service breakdown or overload.

As such, the key worker focus in the UK has tended to be pitched somewhat more narrowly, at least initially, than in the US and at a point further up the income scale. The British debate has been concerned with what in Australia has been referred to as 'the sandwich class' – in the UK termed 'intermediate housing markets' – rather than 'the working poor'. This narrower focus was evident in the initial identification of particular public sector occupations (ODPM, 2004a): viz. nurses, teachers, police officers and support staff, prison and probations officers, fire and essential services officers, social workers, planners, and some local government health service workers.

In March 2004 the ODPM introduced a 'Key Worker Living' program (KWL), to assist in the provision of housing to people in these occupations, with central government funding of £690 million committed. KWL was introduced as part of a broader central government agenda to ensure 'sustainable communities' (ODPM, 2004b).

The new £690 million scheme offers four simple options, including home ownership packages and intermediate rental solutions and will be marketed by one-stop shops located in London, the South-East and the East of England, where house prices are high and recruitment and retention is difficult. Eligibility varies across the regions depending on local recruitment and retention priorities (ODPM, 2005a, p. 1).

Broadly speaking, the target groups fell into three key public sector categories – education, health and community safety. The overall target profile of KWL is 40/40/20 with respect to the three occupational categories, respectively.

A key worker is defined as '...someone who is: employed by the public sector; in a frontline role delivering an essential public service, and in a sector where there are serious recruitment and retention problems' (ODPM, 2005c, p. 14).

The remainder of this chapter summarises some of the main findings of selected studies that touch on important elements of the key worker phenomenon or address broader questions concerning the relationship of urban labour markets and affordable housing. Chapter 5 returns to the policy question, including the current approach in the UK government's KWL program.

3.3 Specific Studies

3.3.1 Office of the Deputy Prime Minister (2005a)

In August-September 2003 ODPM commissioned NOP World to conduct a series of 10 focus groups of 5 to 6 people in each and 20 in-depth interviews (singles, pairs and triples) with current and ex-employees drawn from the occupations of teaching, policing, nursing and prisons/probation in four locations in London and the South-East. The results of this research informed the subsequent development and launch of the Key Worker Living program (discussed in chapter 5). The main results of this study are summarised below:

- The key workers interviewed valued the excitement of London but saw it as very expensive to live there. Job dissatisfaction, it was suggested, could be adversely affected by poor housing situation and housing was one of the important factors in determining whether people stayed or left the region.
- Interviewees had high housing aspirations but felt blocked by high housing prices and rents. This impacted adversely on their overall quality of life, level of satisfaction and level of perceived security: ‘...if key workers are dissatisfied in both work and quality of life, this can act as a trigger to leave the profession or London and the South East’ (ibid., p.7).
- When key workers have been in their job for around 5 years they are likely to be at a critical juncture in their careers and/or lives. It is at this point that home ownership assistance can make a major beneficial impact. Up until then, most will be willing to trade off poor, expensive and insecure housing situation for the other lifestyle benefits that a London location brings. However:

At the five year stage, many are established in their career and want to settle down, and home ownership is the preferred next step. It is at this point that many start to question quality of life and five years is still considered to be early enough in a career to make a complete change or move out of London/SE completely in search of more affordable housing and a better quality of life’ (ibid, p. 7).

- Young key workers, recently completing training, often have student loans and other debts outstanding and find the high rents in London and the South-East prohibitive. This restricts their capacity to access home ownership, even via shared equity or shared ownership programs. In these latter cases when the rental component is added to mortgage repayments, the total housing cost takes up too much of the key workers’ starter level salaries and they have little savings to fall back on. They are faced with the prospect of either moving out of the region to start their careers elsewhere or enduring poor housing and quality of life conditions or taking on a second paying job, which also impacts negatively on quality of life.
- Key worker interviewees valued having a range of choices with respect to cost, location and type of housing, rather than supporting a one-size-fits-all assistance policy. This followed in part from the heterogeneous nature of the key worker occupations – people at different stages of their careers in different service industries. But even among new recruits, there were pronounced differences in situation and housing preferences. This latter group included the young single person referred to immediately above but also includes older established, single or family-based workers transferring into the region for professional or personal reasons and older single or family-based workers

pursuing a change of career or a second career after early retirement. The researchers also suggested that: '(i)n addition, there is the psychological benefit that having a portfolio of solutions offers, giving an element of choice which is important to key workers in terms of feeling that they have the same opportunities as their peer group in other professions' (ibid., p. 8).

- The earlier government program aimed at encouraging and assisting lower income first home buyers into home ownership – the Starter Homes Initiative (SHI) – was generally perceived to be inadequate by the key workers interviewed. SHI was poorly understood, seen as too inflexible, based on unrealistic requirements regarding the time necessary to find and arrange dwelling purchase, and made no contribution to helping key workers accumulate the purchase deposit.

3.3.2 *Monk and Morrison (forthcoming)*

This paper looks at the applicability of the key worker thesis to an area outside London but still in the South-East – viz. Surrey. They argue that:

Housing and Labour markets need to be examined not as isolated elements, but through their interconnections. Changes in one market affects changes in the other. On the one hand, housing-market pressures, entailing rising housing costs and lack of affordable housing, impact on labour recruitment, particularly of lower-income employees. On the other hand, labour-market pressures entailing high wages and earnings for certain workers worsen income distributions and hence impact on housing costs for those at the lower end of the market (Monk and Morrison (forthcoming, p. 1).

The authors argue that at least part of the disconnect between low-wage workers and affordable housing in high house price regions is structural and will not be resolved as the property cycle turns down, particularly in the case of affordable home ownership (Joseph Rowntree Foundation, 2002). Structural factors resulting in housing shortages and labour recruitment problems also appear to be present in other European countries and the United States (McIlwain, 2003).

The paper focuses on the region of Surrey to the immediate south of London and uses a survey of local employers in both the public and private sectors to gauge the degree to which rising housing costs interact with recruitment and retention problems for those employers. Surrey has higher proportions of the resident population employed in professional, managerial, technical and administrative occupations than in the country as a whole and lower proportions employed in skilled trades, sales and customer services, and process and machinery operatives. Labour in-migration to Surrey over the past two decades has been biased towards the former higher paid occupations, understandable in the light of the manageable commuting times to London. 'Consequently, lower-income households are forced to compete for a diminishing supply of lower-cost housing. This leads to a tension between the needs of future economic growth and the inability of the market to provide sufficient housing, particularly for those in lower paid occupations' (Monk and Morrison, op. cit., p. 5).

Significant land supply constraints in Surrey are reinforcing the effects of rising housing demand, pushing prices and rents beyond the means of many lower paid workers. The number of annual housing completions was about 2,500 in the 1999-2002 period, running behind new household formation; only 13 per cent of

completions in this period were for social housing. The targets for social housing were under-achieved throughout the County and many housing associations reported that they were unable to access suitable land at prices allowing affordable housing to be constructed. Given current housing targets, actual dwelling construction was forecast to fall 21.3 per cent below forecast household numbers (ibid., pp. 7-8). In 2004, the ratio of average house prices to average household income was 7.98 in Surrey, compared to 5.47 for England as a whole (ibid., p. 9). Average private rents did not increase as fast as average house prices but increased more rapidly than social rents in the period of the housing boom, 1995-2004.

The authors interviewed 30 employers active in the County, 17 in the public sector and 13 in the private sector, seeking to understand the links between housing costs/availability and employee recruitment/retention. The former included senior managers in the County Council, police force, ambulance service and educational authority. Private sector employers were drawn from a number of industries, including electronics, retailing, hospitality and privatised public transport firms. Business peak associations were also interviewed.

The key findings were:

- All but four organisations interviewed considered that high local housing costs were a significant factor in local labour shortages. The four exceptions were all in the private sector.
- All public sector employer interviewees reported problems in filling job vacancies for professional and semi-professional staff and retaining appointees. Lower level administrative and clerical positions were less of a problem since they tended to be filled by local people, many of whom were second income earners in the household. With respect to the higher qualified positions:

The overriding concern expressed by public sector employers centred on the significant number of applicants either withdrawing their application, or not even making one after inquiring about housing costs in the area. Candidates often turned down job offers once interviewed. The primary reason given was that they could not afford to live in Surrey (ibid., p. 11).

- The hardest to fill positions were in the critical care areas of health, notably qualified nurses, radiographers and physiotherapists. However, a number of trainee occupations were also difficult to recruit and retain, including trainee teachers, social workers and police officers. One local Health Trust commented: 'We are faced with the prospect of nurses and midwives training in Surrey but subsequently working elsewhere. In effect, we are acting as a training ground for the rest of the country' (ibid., p. 11).
- Nationally set salary scales provide little scope for Surrey's public sector employers to attract and keep staff, especially given the special London salary weightings that encourage Surrey workers to commute or relocate closer to the metropolitan area. This suggests that London's key worker problem would be worse than it currently is if public sector employers there were not able to 'poach' staff from the broader South-East region.
- Younger public sector workers tended to live in poor quality, often shared accommodation or commute long distances in order to buy homes in more affordable locations. The decision to live independently or move into home

ownership was often accompanied by shifting jobs outside Surrey. Long distance commuting was common among workers transferred to Surrey; 'Driving an eighty mile round trip was considered the norm' (ibid., p. 11).

- In the private sector, similar recruitment and retention problems were found, particularly in the lower-paying service sector companies – in retailing, entertainment, leisure and hospitality and personal services. These are industries which compete on low margins and depend on a low-paid, flexible, casual work force. Retailers interviewed reported high turnover among both sales assistants and junior managers. The privatised public transport companies reported similar problems and expressed concern that high training costs were being incurred due to high labour turnover. High local housing costs were seen as a major factor in recruitment and retention problems in these service sector industries. Interestingly, employers in these industries face similar constraints on the capacity to pay higher wages in order to attract and keep workers as do public sector employers. Intense competitive pressures on a national scale in areas like transport severely constrain employers from paying enhanced local wages in Surrey.
- Conversely, private sector employers in growth industries like electronics, avionics (Gatwick airport is nearby) and information technology reported no significant staff recruitment and retention problems. Many of these companies are large international firms in high value-adding areas. Salary scales were flexible and set taking into account high local housing costs and the housing aspirations of workers. Generous relocation and mortgage assistance packages were available to some staff, as were benefits like car allowances and health care schemes.

Surrey may be a special case in the sense that it is a traditional high housing cost area, located within the commuting shadow of one of the world's major cities, undergoing significant growth fuelled by globalisation. Nevertheless, it does bring into sharp relief the potential for a functional mismatch between the diverse and dynamic labour needs of a globally connected regional economy and the capacity of local housing markets to support the full range of workers required. The problems relate to both many sections of the public sector, responsible for providing services like education and health that impinge on local labour productivity and liveability, and to the competitiveness of many service providers in the private sector.

3.3.3 Morrison (2003)

In this earlier paper, Morrison focuses on another region, this time to the north-east of London – viz. Cambridge. Cambridge is an old university town that has undergone significant population growth and economic transformation over the past three decades; indeed the city has been the fastest growing region in the country over that period. The local economy has expanded, attracting new high-technology industries, catered for by a number of science parks with strong ties to the university. Other rapid growth sectors included communications, research and development, higher educational and publishing. The demand for lower-paid service workers has also increased sharply, feeding into an increasingly polarised local labour market. One consequence has been increasing pressure in local housing markets.

Households migrating into the city are likely to lead to further competition in the already constrained housing market, bidding up house prices as

more households aspire to live in or near Cambridge. The contribution of the 'commuting' sector to incomes and purchasing power in Cambridge is also likely to be disproportionately high. This workforce which has moved out of London but continues to commute, is well positioned to afford housing in Cambridge. Similarly, the in-movers taking up employment in the growth sectors, such as high-tech, are also able to bid up house prices and compete with local people in the housing market. At the same time, the constrained land supply within the city, as a result of the tightly drawn Green Belt around the city's boundaries, has further exacerbated the house price rises. Housing demand is likely to continue to outstrip supply into the future (Morrison, 2003, p. 288).

As a further result, housing affordability problems have intensified for an 'intermediate' cohort of working households which earn too much income to qualify for sub-market housing provided by registered social landlords but insufficient income to compete successfully with higher income households in the constrained local housing market. The ratio of average house prices to average (individual) incomes in Cambridge is 8.4 (6.1 if mean rather than median income is used), compared to 6.9 (5) for England overall. Single income households where the income earner is employed in a low to moderately paid job are particularly likely to be in serious housing stress. Average ratios are likely to understate the affordability situation. Morrison quotes data from the late 1990s that shows that house price rises in the lowest quartile – i.e. the lowest priced quarter of the housing stock – were increasing faster than housing overall in the region. 'This suggests that demand is greatest at the lowest end of the market, where property is relatively more "affordable". It also suggests that this demand for lower-cost, smaller units is not being met by increased supply and that the shortage of smaller, more "affordable" units is the most severe' (ibid., p. 290). Further signs of pressure on the local market are evident in the trend over the past decade for average housing costs in both the home ownership and private sector to increase much faster than rents in the social housing sector.

Morrison carried out two surveys to test the degree to which these housing-related pressures were impacting on the intermediate group of 'key workers'. The latter were defined broadly as low-to-moderately paid workers in public sector service jobs (hospital staff, police officers, teachers), private sector service jobs (bus drivers, supermarket workers) and knowledge-intensive growth industries (engineering, publishing, R&D).

The first survey targeted employers of 'key workers', as defined. Around a quarter of the 160 employers surveyed by mail responded. The main findings were:

- 80 per cent of employers responding reported difficulties in recruiting new staff and a half had difficulty keeping them. Labour problems were not confined to those occupations targeted by the central government but also included university staff and a range of care workers in the public sector and transport workers, catering and hotel staff and hairdressers in the private sector.
- Recruitment and retention problems occurred at all levels, from junior to moderately senior grades.
- Almost all employers responding believed these problems related to high local housing costs – both for owner occupation and renting – in the private market. Two-thirds of employers said that they had evidence of increased commuting distances for their staff as a result of high housing costs. Those employers

conducting exit interviews of staff leaving identified local housing as a significant 'push' factor. The problem of unfilled vacancies left some essential services under-resourced; e.g. at the time of the survey, the Cambridge Constabulary was 18 positions under strength.

The second survey targeted 670 key workers directly. The response rate was over 40 per cent. Seventy per cent of employees responding earned less than £20,000 per annum, with supermarket workers the lowest paid and those working in private sector growth companies, the highest paid. The greatest levels of dissatisfaction with their current housing conditions were displayed by the lowest income respondents, especially those renting privately, living in tied accommodation or sharing with friends or families. Most of the respondents aspired to traditional (not shared) home ownership rather than social housing, suggesting that the gap between aspirations and affordable realities was large for the lowest paid households. Over 40 per cent of respondents wanted to live closer to where they worked; of these, 63 per cent nominated high housing costs as the main reason for not doing so. Overall, 84 per cent of respondents believed that high local housing costs would eventually force some people in their circumstances to leave Cambridge.

3.3.4 Meen (2000) Economic Polarisation in London and South East England

Analyses that focus on spatial mismatch and the shortage of job opportunities and take-up in particular areas of large metropolitan regions (at least) implicitly subscribe to a theory of uneven spatial development or polarisation. This, as Meen (*ibid.*, p. 1) suggests can be traced back to the original theories of 'cumulative causation' propounded by Myrdal (1957) and Kaldor (1972), the basic idea being that once set in motion, differences in rates of growth between areas grow further through a series of feed-back processes ('spread' and 'backwash' effects, according to Myrdal). Meen proposes a dynamic approach that takes account of the interactions between housing markets, labour markets and job location and tests it using data on household and industrial location in greater London⁹.

Meen develops a 'nested multinomial logit model' of housing choice to test whether people move to where jobs are locating or jobs follow people or at least, those people who have the skills most in demand by innovating employers. He found that, in addition to stage of the life cycle, housing movement and location is largely driven by the locational preferences of higher income households and not the independent locational moves of employers. Lower income households tend to be 'left behind' in areas losing jobs that chase higher income groups. The former are 'locked' or 'trapped' in declining areas which encourages remaining higher income households to move out, and so on, in a classic pattern of cumulative causation.

Although the story is not complete, we can begin to see how interactions between housing and labour markets may generate dynamic spirals of decline in some urban locations. The low skilled are more likely to be unemployed and therefore, to have low

⁹ Meen (2000, abstract) argues that – '(a) full model needs to take account of housing, labour markets, industrial location and aggregate demand, although only the first three elements are endogenised in this paper'. This raises the tantalising question/challenge as to how the macroeconomic dimension of aggregate demand could be 'endogenised' to achieve a more powerful explanation of the interactions between housing and labour markets across and between metropolitan regions. See Berry (2006) for an initial discussion of the macroeconomic dimension.

incomes. But those on low incomes have a lower probability of moving (or commuting to jobs elsewhere). Furthermore, as high income, employed households move away from the urban core, the unemployment rate in the inner city rises even further which ...makes those locations even less desirable to households who can move. Out-migration, then, increases even further and the end result is the cumulative process of decline described [earlier] (Meen, 2000, p.18).

One reason that lower income households are trapped in declining areas is that credit constraints – the down-payment or deposit requirements of lenders (and up front transaction costs) – assume a higher proportion of the wealth and disposable income of this group, limiting their effective housing choices and locking them into low-cost rental housing for longer periods. One consequence of the existence of credit constraints in housing markets is that lower income households are likely to react more slowly to exogenous shocks like changes in interest rates or patterns of in-migration and inward foreign investment:

If certain locations experience either negative or positive shocks, high income groups will be in a better position to move to alternative locations quickly to take advantage of those shocks. Furthermore, low income households are more likely to become locked into locations of poor quality, not only because of lower incomes but also because of declining relative housing prices. Periods of disequilibrium, therefore, are positively related to the size of credit restrictions and negatively to the level of income (ibid., pp. 13-14).

The dynamic forces of polarisation identified by Meen (and also, utilising a somewhat different approach, by Galster (1998)) can be seen as one important foundation underlying the emerging processes of urban restructuring discussed in chapter 2 and as a driver for the particular patterns of spatial mismatch between labour and housing markets resulting in recent policies designed to house key workers, however defined, in areas of high job growth.

3.3.5 Henley (2004) House price shocks, windfall gains and hours of work

A companion report (Berry, 2006) focused on the wealth effect on consumption of changes in housing prices. However, changes in wealth may also impact on the inter-temporal distribution of leisure; in other words changing wealth brought about by factors like house price inflation or deflation may increase or reduce the supply of labour, the number of hours people work rather than enjoy leisure. In theory, unanticipated increases in wealth should result in a decline in labour supply since the marginal utility of wealth falls¹⁰. In practice, institutional factors, like restrictions on the ability of workers to re-negotiate and reduce their hours worked, or a strengthening of the bequest motive, may offset this effect. As in the case of the consumption wealth effect, empirical analysis is necessary to establish if and to what extent and under what conditions the effect holds. If 'work-wealth effects' exist and are robust, then significant volatility in housing markets, a major (but not exclusive) cause of unanticipated changes in household wealth, can lead to pronounced instability and inefficiencies or bottleneck in labour markets. Changes in the supply of labour can impact on wage levels sending further signals through the urban labour market.

¹⁰ The gain must be unanticipated to have an effect, since if it wasn't, workers would have already factored in into their labour supply responses.

Regions experiencing rapid house price inflation are likely to show signs of declining affordability for low and moderate income households. Hence, housing affordability may be a reliable indicator of work-wealth effects on local labour supply. More importantly, declining affordability may intensify these effects. For example, if rising prices cause the supply of labour to fall, this will put upward pressure on local wages generally (as house owners cut back their hours of work) and worsen any supply bottlenecks in specific occupational areas. Secondly, private tenants, other non-owners and aspiring owners face rising housing costs and a higher hurdle accessing owner occupation. If local wages do not rise enough to offset this cost – or those households do not possess the skills relevant to the jobs in demand – they have a strong incentive to move away from the region in order to access affordable housing and employment, further intensifying labour shortages in their current location. This outcome, if occurring, operates independently from the processes of spatial mismatch discussed above.

Henley's study looks at the effect of both real capital gains on housing and windfall financial gains (like lottery wins) on labour supply. He develops a logistic regression analysis utilising data from the British Household Panel Survey (BHPS), an annual survey of around 5,000 households. This study draws on the first 11 waves, from 1991 to 2001.

The main results are as follows.

- In relation to windfall financial gains, both men and women work less. Thus, for an unanticipated £10,000 gain, women on average reduce their hours of work by two and a half hours per week, whereas the reduction for men is half an hour per week. The main way that this reduction occurs is by cutting out second jobs. This gender difference is consistent with the US study by Imbens et al. (1999).
- In relation to housing real capital gains, again the labour supply responses of women were more pronounced than men. Interestingly, the direction of responses to housing price *losses* differs between men and women. Men tend to work more and women less when the value of their housing falls. On the other hand, when house prices *increase* both men and women work less, though the latter display the largest response; for a 10 percent increase in real capital gains, women work up to half an hour a week less.
- Both men and women would respond more – i.e. would increase or reduce their work hours more – if they had more power over the number of hours worked. This suggests that institutional constraints and employer requirements prevent an 'optimal' response to wealth effects of house price changes – but may have the benign unintended effect of reducing the impact on local labour supply and wages of volatile movements in housing markets.

Henley suggests that the gender differences found may reflect the lower degree of attachment of (some) women to the paid workforce, given their multi-role tasks in domestic production and child-rearing. It is possibly also the case that, in two-income households, the women's income is not the primary income source and, in that sense, is treated as a 'second income' more readily given up. Alternatively, or in addition, it may be the case that the institutional constraints on changing or re-negotiating work hours bite less heavily on women than men in labour markets like the one Henley studied.

4 THE 'KEY WORKER' DEBATE: AN AUSTRALIAN PERSPECTIVE

4.1 Introduction

As indicated above, one of the key concerns with the outcomes of the urban restructuring that has arisen from globalisation has been a concern that the resultant uneven economic development would lead to a spatial polarisation within cities and to a spatial mismatch between where jobs are located and where lower paid workers can afford to live. This, in turn, can contribute to structural inefficiencies in urban labour markets.

In Australia, there is increasing evidence of the growing gap between dwelling prices in central locations, where jobs are concentrated, and in outer locations where an increasing proportion of lower income households live.¹¹ Recent examples of such analyses can be found in Berry and Dalton (2004), Burke and Hayward (2001) and Yates (2002).

Within Australia, the most comprehensive analysis of whether employment of workers in specific occupations has been affected by housing affordability and accessibility problems, particularly in higher cost, job rich locations, has been undertaken by Yates et al (2006). This builds on earlier city wide analyses undertaken by O'Connor and Healy (2002) for Melbourne and Randolph et al (2004) for Sydney and on more narrowly defined within-city studies undertaken by Epic DotGov (2004) and Blunden et al. (2004). O'Connor and Healy's analysis of Melbourne supported the argument that globalisation is leading to spatially polarised cities: it showed that central Melbourne is becoming increasingly separate from the rest of the metropolitan region. Randolph et al's analysis of Sydney highlighted the importance of the Reichian distinctions between different types of workers by showing that outcomes differed by occupation both in terms of the impact that occupation has on household income and in terms of the spatial dispersion of jobs available to workers in different occupations. The remaining two studies signalled the methodological importance of determining whether the workers in question are primary or secondary workers within the household. The broader based Yates et al study reinforced the results of, and reflected the lessons learned from, these studies and is discussed immediately below.

4.2 Specific Studies

4.2.1 Yates et al. (2006)

Yates et al based their analysis on the assumption that potential mismatch would show up in one of two ways: workers would either face high housing affordability problems or they would face significant commuting costs, reflected in the distance they needed to travel to get to work. This, in turn, was underpinned by an assumption that, if high housing costs imposed unsustainable pressures on affected workers, they would encourage workers to re-locate to lower cost areas

¹¹ As discussed above, methodological issues arise in separating out the effects of high income households who voluntarily choose to live in outer locations because their preference for high housing consumption offsets the costs of longer commutes (often made feasible because they have access to car based transport) and lower income households who are constrained to live in locations where housing is more affordable.

and, similarly, that if high commuting costs imposed unsustainable pressures on affected workers, they too would encourage workers to look for employment closer to their current place of residence. Either response is likely to contribute to labour market shortages in high cost areas.¹²

One of the results of the Yates et al analysis of the relationship between housing and labour markets reinforced that derived earlier by O'Connor and Healy (2002): there is a high degree of residential and employment self-containment within what reasonably might be defined as labour market regions with approximately half the workforce living and working locally in most regions. In part this arises because service jobs in particular have moved to where people live. The main exceptions to this generalisation, however, are jobs in the areas identified by Reich (1991) and Florida (2002) as being the engines of growth. These are the new economy or knowledge workers, represented in the Yates et al study by computing professionals (but defined more broadly above as those working in advanced business services).

The relatively centralised location of jobs for some workers and more dispersed for others means that there are considerable differences in the amount of commuting undertaken by workers in different occupations. There were also considerable differences in affordability outcomes.

Housing affordability problems were greatest amongst households where the primary income earner in the household was employed in the highest cost regions in Australia in an occupation which is likely to be low skilled, casualised and part-time. The areas with the highest incidence of household stress are the Sydney metropolitan region, the inner regions of Melbourne and south-east Queensland. The examples given of workers with the greatest housing affordability problems are those with occupations as hospitality workers or sales assistants. The primary driver of affordability problems, however, is household income and household structure rather than occupation.

A more detailed analysis of households with at least one worker employed in the job rich centre of Sydney, selected by Yates et al as the highest cost region of those studied, showed that a disproportionate share chose to live in the higher cost inner region of Sydney than in the more affordable outer regions. An alternative explanation is that employment is feasible for these inner city workers only if they do not have long daily commutes. One of the (untested) hypotheses in Yates et al (p 86) is that:

long distance commuting is problematic because of the employment conditions under which workers are employed, particularly when these involved shift work and unsocial hours. The choice to live close to work is reflected in above average levels of housing stress and, a higher incidence of renting and, associated with this, higher proportions of households without children (specifically, couple only households and group households). Those households with at least one worker employed in the centre of Sydney who have children are more likely to be home purchasers living in the more affordable regions of the city.

¹² The alternative outcome, embodied in the spatial mismatch hypothesis, is that high commuting costs would result in unemployment. Yates et al excluded this option from their analysis because the census data they employed did not have occupation defined for unemployed workers.

Finally, their results show that a disproportionate share of persons in the lower skilled hospitality and cleaner occupations¹³ are neither the primary earner in the household in which they reside, nor a partner of the primary earner in this household. Yates et al suggest “they are likely to be secondary earners in the household. Their affordability problems are therefore managed by their willingness either to remain in their parental home or to share in a group household.” (p82)

They conclude:

low paid workers who are the breadwinners in their household are being displaced from high cost regions. Much of this displacement is because their jobs are also being displaced as a result of high-cost residential development displacing many of the traditional sources of employment for the residents of those areas. With the exception of the CBD, the numbers of persons employed in jobs in high cost regions have declined.”(ibid., p. xi)

They conclude their study with the predictions that the CBD ‘will be populated by young renters, the affluent renters and those without children’ and that ‘employers will be able to address their [recruitment and retention] problems by employing a continuing supply of young, mobile workers by providing better wages and better conditions. The continued costs associated with retraining will be passed on in higher prices.’(ibid., p. 88). It remains an open question, however, whether this potentially very mobile, mixed and uncertain supply of lower paid, ‘flexible’ labour will adequately meet the functional needs of the globally oriented economy centred on the core areas of the major cities.

4.2.2 Nygaard et al. (2005)

This study compares the patterns of socio-spatial polarisation, economic differentiation and integration with the global economy in Sydney, Melbourne and Adelaide and the interaction of these processes with metropolitan housing markets in those cities. Following the lead of Sassen and other urban theorists, noted in chapter 2 above, the authors suggest that cities which are undergoing significant economic restructuring, integrated most effectively into the global economy and growing the new knowledge-based ‘new economy’ industries will tend to also experience the most intense patterns of housing market sorting, segmentation and polarisation. Moreover, these housing market developments are likely to reinforce many of the underlying economic drivers leading to internally fragmented cities.

The key findings reported are as follows:

- In 2001, Sydney and Melbourne were the only regions in Australia with above-national average proportions of their labour forces employed in the key knowledge-intensive occupations – finance and insurance, property and business services. Growth in these occupations was also greatest in Sydney and Melbourne over the 1996-2001 inter-censal period. The concentration and growth of finance and insurance was particularly pronounced in Sydney. These two cities, in contrast with Adelaide, experienced strong growth in the service sector overall. Service sector jobs in both high paid-high skill and low paid-low skill areas increased markedly in the two largest cities. For example, between 1996 and 2001, employment in accommodation, cafes and restaurants grew by 27.9 per cent in Melbourne, compared to 15 per cent (from

¹³ These two occupations were selected by Yates et al as being indicator occupations representative of the lower skilled and less well paid occupations classified by Reich as in-service workers.

a much lower base) in Adelaide. Likewise, property and business services employment grew by 27.9 per cent and 24.1 per cent in Melbourne and Sydney, respectively, compared to 17.5 per cent in Adelaide. For Sydney and Melbourne these patterns of growth over a relatively short period suggest the emergence of the 'synergistic dual urban labour market' referred to in chapter 2.

- New economy-type jobs are strongly concentrated in the inner areas of all three cities. However, the pattern of concentration is greatest in Sydney, then Melbourne. In fact, the CBDs of the two cities contain almost 1 in 5 people employed in these occupations nationally. These industries account for a significantly higher proportion of total value added in the economy than their share of total employment. This suggests that these centrally located industries are likely to be more profitable – and hence able to pay higher wages and salaries – than other industries. This is borne out by the authors' analysis of Australian Bureau of Statistics data on corporate profitability.
- Sydney and Melbourne also displayed pronounced patterns of occupational polarisation and, at the top, professionalisation, a trend identified for Sydney earlier by Baum (1997). The number of occupied professional jobs increased by 16.8 per cent in Sydney and 20.2 per cent in Melbourne between 1996 and 2001. The increase in Adelaide was lower at 9.7 per cent. The difference between the two larger cities, on the one hand, and Adelaide was even greater for managerial and administrative occupations. At the other end of the income spectrum, the lowest paid clerical, sales and service worker category grew rapidly in all three cities; by 12.4 per cent in Sydney, 18.7 per cent in Melbourne and 16.1 per cent in Adelaide. The other growth occupations in Adelaide were intermediate level clerical, sales and service workers, labourers and related workers, and associate professionals. This suggests that, whereas the occupational structure in Sydney and Melbourne was being 'hollowed out' to a degree, with both knowledge intensive-high paid jobs and low skill-low paid jobs increasing relative to middle level jobs, in Adelaide growth was concentrated in the middle and lower occupational categories relative to new economy jobs.
- However, turning from occupational to income differentiation, it appears that Sydney stands apart from *both* Melbourne and Adelaide. Drawing on the ABS survey of income and housing (1999-2000), the ratio of the median income of managers and administrators to the median income of labour and related workers stands at 4.6 for Sydney, compared to 3.4 for Melbourne and 3.3 for Adelaide. Income polarisation, by this measure at least, seems to be more intense in Sydney. A closer analysis revealed that there were statistically significant differences in the average earnings of employees in the top three occupational categories between Melbourne and Adelaide but not Sydney and Melbourne. 'This would indicate that the skills premium is particularly relevant in Sydney and Melbourne, where demand for skilled labour as a result of agglomeration has been higher' (Nygaard et al., 2006, p. 11).

To summarise, they argue:

When examining overall industry of employment and occupation data for the period 1996-2001 it is evident that Sydney and Melbourne have developed along a different trajectory than Adelaide. However, also [evident is] that Sydney differed from Melbourne in crucial aspects. There was higher concentration of

new economy type jobs in Sydney than in Melbourne, wage differentials were higher and the share of employment in the three highest occupation categories was higher than in Melbourne. In terms of female employment the two cities have the same trend [upward] and both cities display trends that would indicate increased professionalisation of the workforce *and* increased lower wage employment. By contrast, in Adelaide the trend towards professionalisation was weaker and there has not been a corresponding concentration of new economy type employment. Finally, wage levels tend to be lower than in the two other cities (ibid., p. 13).

- Rapid growth in the female labour force and a concentration of overseas migrants in the two largest cities provides some support for Sassen's hypothesis that *occupational* polarisation in globally connected cities depends in part of the expanding supply of labour from these two sources pushing wages down. In both Melbourne and Sydney overseas born workers were overrepresented in the bottom two occupational categories. However, given the small sample size of overseas born migrants in each occupational category, it was not possible to establish robust results with respect to *income* polarisation; nor did the individual earnings data allow recent migrants to be distinguished from long established migrants. The authors also note that low wages in low skilled jobs – contributing to increasing income polarisation – can be brought about by a number of other factors, including institutional reforms to wage fixation systems, new forms of industrial organisation such as outsourcing and the competitive pressures imposed by producers in low-wage countries.

The authors then interrogated income data from the Australian Taxation Office, available at postcode level. The Gini-coefficient for total income increased by 40 per cent in Sydney over the 1995-96 to 2002-03 period, by 33.7 per cent in Melbourne and by 16.9 per cent in Adelaide. The Gini-coefficients for the wage and salary component of total income were 21.2 per cent, 16.4 per cent and 5.6 per cent, respectively. 'The income data thus seem to confirm that [income] inequality increased sharper in cities that concentrate a larger share of new economy type industries and that earnings and wage pressures (as a result of a higher skills premium in these cities) may be higher in cities that have a larger service and finance oriented economy' (ibid., p. 17).

- Drawing on ABS data on the profitability, the authors find that *new economy* small businesses received an increasing share of all small business profits in Sydney and Melbourne – but not Adelaide – over the 1995-96 to 2000-01 period. To the extent that these firms tend to cluster in particular parts of the metropolitan region – viz. the inner core – this implies the existence of significant variable intra-urban profit-making capacities which could reinforce intra-urban wage differentials. It also appears to be the case that profit-making capacities vary between cities of different size and function, particularly with respect to how strongly they are globally tied into the new economy. The increasing profitability of new economy firms, according to Sassen, bids up the price of urban land, pushing lower value businesses and land uses generally out from favoured locations. This tends to be a self-reinforcing cycle. As more and more new economy businesses cluster in the centre, the agglomeration economies created increase profits which push the price of commercial space up further and drive lower value businesses further out increasing the latter's

costs and reinforcing the economies of central location. The growing divergence in profitability ensures that central location is increasingly only affordable by new economy businesses the growth of which increase agglomeration economies further, and so on.

- It is also clear that Sydney and Melbourne have functioned as the major Australian gateways to the wider world, with respect to exports, particularly of services, and international migrants. Over the past decade Melbourne has increased its national share of airfreight, educational services and commercial construction, and remained as the nation's largest container port. These trends may help explain why Melbourne and Sydney converged in important respects over that period, reflected in the partial convergence of office rents and housing prices since the mid-1990s.
- Housing markets have closely reflected these changing patterns of metropolitan economic restructuring and polarisation in Sydney and Melbourne but not Adelaide. Gentrification of the central and inner suburbs has been associated with increasing dwelling densities and a more slowly increasing, more affluent residential population. This trend has been associated with the construction of new high cost rental accommodation and rapid house price inflation towards the centre. The price-distance gradient has steepened and the location of the available stock of affordable housing has been pushed to the periphery of both major cities. This suggests that housing markets are more effectively 'sorting' households according to income source, level and security – i.e. that the processes of occupational and income polarisation are increasingly being expressed over space in an expanding metropolitan region.

This last point is critical to the questions addressed in this report. It appears that the spatial impacts of the economic restructuring of Sydney and Melbourne, reflected and reinforced through urban housing and commercial property markets, are creating the potential for an intensifying spatial mismatch between where lower-waged workers functionally necessary to support the growth of the new economy live and where their labour is required. This further suggests why economic policy makers should be concerned with the affordable housing question, at least in Australia's two major cities whose core economies function as the main linkages to an increasingly competitive and integrated global economy. It is precisely in these metropolitan regions that the seeds of urban labour market failure appear to have been sowed.

4.2.3 Dodson (2004, 2005)

Dodson (2004) summarises the earlier Australian research, noted in chapter 2 above, that identifies the spatial segmentation of both housing and labour markets in Sydney and Melbourne, leading to the concentration of new economy jobs towards the centre and the retreat of affordable housing towards the urban fringe. 'If Australian housing markets segregate households on the basis of socio-economic status, and spatial patterns of employment growth do not favour areas where such households are concentrated, then comparable socio-economic opportunity problems to those experienced by US cities are likely to arise, albeit without such a strong ethno-racial dimension' (ibid, p. 19).

Dodson (2005) then attempts to gauge empirically the extent of such mismatch in the case of Melbourne. He first identified the areas of low-rent private housing in the metropolitan region, not surprisingly finding that these areas were located in

the outer ring suburbs and in the northern and western regions of the city traditionally home to old economy industries. These areas were also characterised by the largest concentrations of households with relatively low mortgage repayments; indeed, the pattern of segregation between high and low mortgage areas was even sharper than for private renting. The entire inner core of suburbs and those to the immediate east and south had less than 15 per cent of households paying less than \$600 per month on their mortgage at the 2001 Census, whereas between 30 and 60 per cent of households were in that situation in municipalities like Greater Dandenong in the outer-South East and Hume in the outer-North.

Dodson then looks at measures of labour market disadvantage across the metropolitan region, again as revealed by the 2001 Census. In the case of unemployment, rates were highest in the Northern and Western sectors, from inner to outer, and in the outer South-East. Between 1996 and 2001, the beginning of the current period of rapid economic growth, unemployment fell furthest in the inner and southern suburbs, relative to the rest of Melbourne. Over the same period, employment grew fastest in the outer suburbs and fell in the inner and middle western and northern suburbs.

Dodson then tests the spatial mismatch hypothesis by looking at the changing situation in three statistical local areas (SLAs) – Sunshine (in the West), Dandeong (outer-South East) and Broadmeadows (outer-North). In these cases he found ‘...that the hypothesis that there is a spatial mismatch between housing affordability and employment opportunity in Melbourne is not strongly supported, at least at the level of statistical local area (SLA)’ (Dodson, 2005, p. 27). In other words, Dodson found that areas in which housing was relatively affordable were also areas where employment growth was buoyant. This suggests that other reasons account for higher than average unemployment rates in those areas, for example, skills deficits and poor public transport. He further suggests that many traditionally low status outer suburbs – e.g. in the West – have been recently ‘surrounded’ by new up-market housing developments that have acted as magnets for employers, particularly in the service sector. Hence, lower income workers living near those new high status suburbs have benefited from the local growth in jobs, provided they have had the necessary skills and could access them by private or public transport.

Dodson’s conclusions are constrained by the narrow focus of his study on three arbitrarily chosen cases and by the wide radius (10 kilometres) used to define the local employment area in each case. Thus, his analysis suffers from some of the weaknesses identified in the earlier comparable US research (see chapter 3). In this context, it is not clear that Dodson’s interpretation of the data actually supports his conclusion of limited or no spatial mismatch. In particular:

- Poor job information and transport barriers may still mean that low-wage workers are unable to access local jobs, even when job vacancies are high in the area. There is no necessary relationship between where in the outer areas most jobs are being concentrated and how accessible these job growth precincts actually are to workers seeking affordable housing. The poverty of public transport in outer areas of the metropolitan region, especially in Melbourne and Sydney, make comparisons of physical distances problematic. Hence, continuing high unemployment in broad regions where job growth is strong may still hide localised patterns of spatial mismatch between employment and affordable housing. If this is coupled with poor job

information about opportunities further a field and poor inter-suburban transport, the degree of spatial mismatch is reinforced for those households pushed to inaccessible, lower housing cost locations.

- More importantly, Dodson's analysis focuses – as did Kain's original SMH – on the socio-economic or equity concerns about employment opportunities for low-wage workers. His analysis does not address the main focus of this report – viz. the functional efficiency of urban labour markets due to housing market failure.

With respect to the latter point, the fact that Dodson (and others) has found that inner city labour markets are very tight relative to other areas of the metropolitan region, suggests that labour bottlenecks may indeed constrain the most dynamic, centrally located new economy industries and their support service requirements. The seriousness, impacts and causes of these bottlenecks are matters for empirical investigation. Where the problems are significant, policy makers have a strong interest in determining the causes and acting to overcome the barriers. In such cases, the possibility of both deficits of appropriate skills and a spatial mismatch between housing and labour demand need to be explored.

5 POLICY APPROACHES

This chapter concentrates on the recent attempts of central and local governments in the UK to address the problems of labour supply in the context of the key worker problem identified in earlier chapters.

The approach to key workers in the UK, noted in chapter 3, targets specific occupations in designated regions, viz. the South-East. The British Government, as noted above, introduced a new program in early 2004 – Key Worker Living (KWL) – aimed at assisting this target group into home ownership and sub-market rental occupation. The emphasis, however, is clearly on meeting the owner occupation aspirations of target households, in order to ease perceived staff recruitment problems in basic public services like education.

There are four main products accessible to eligible applicants under the KWL program:

- *Homebuy*. Eligible applicants, including key workers, can receive an equity loan' up to £50,000, which is not repayable unless and until the household sells the dwelling or ceases to be a key worker. Households can purchase all or a proportion of the equity in a new dwelling built by a RSL or an existing dwelling on the open market; in the case of less than 100 per cent equity, the remaining share is normally taken up by a housing association. The amount of the loan repayable is equal to the proportion of the original value of the dwelling paid for by the loan. Households in addition to key workers eligible for assistance include:
 - ❖ *Social Homebuy*: local authority and housing association tenants and those on the local authority housing register who will be able to purchase all or a share of their current dwelling at a discount.
 - ❖ *New Build Homebuy* and *Open Market Homebuy*, relating to new and existing dwellings, respectively: social tenants and other first time home purchasers in groups identified as priority cases by Regional Housing Boards.

The government aims to assist at least 80,000 households, including key workers, through New Build Homebuy and Open Market Homebuy (ODPM, 2005c, p. 7).

- *Key Worker Shared Ownership*. Key workers buy at least a 25 per cent equity share in a new dwelling constructed by a registered social landlord (RSL) and pay rent on the remainder, the remaining share held by a RSL. The key worker can progressively increase his or her share over time. On sale of the dwelling, or exiting the key worker occupation, the household must repay that proportion of the original value of the dwelling still covered by KWL.
- *Intermediate Rent*. Key workers pay sub-market rents at less than 80 per cent of market levels on dwellings developed by RSLs.
- *London Challenge Teacher Homebuy*. This scheme is a subset of Key Worker Homebuy but with the maximum equity loan increased to £100,000 for 'a small group of school teachers in London identified as having leadership potential' (ODPM, 2006a, p. 1).

A review of KWL was carried out in early 2005 (ODPM, 2005b). This review¹⁴ interrogated monitoring data collected by ODPM and a series of face-to-face and telephone interviews with employers and 'zonal agents', the latter being the registered social landlords (RSLs, normally housing associations) charged with the responsibility of marketing and administering the program within their areas. Central government officers were also interviewed. This review found that:

- As at December 2004, 87 per cent of enquiries for the program were about Homebuy, 8 per cent for Shared Ownership and 5 per cent for Intermediate Rent. This suggests that, initially at least, government assumptions about the pronounced home ownership aspirations of target key workers were justified. It also reinforces perceptions that KWL is pitched at the intermediate (or higher) reaches of the market.
- Just over half the enquiries were from London.
- By the end of 2004, 2,236 key workers had accessed Homebuy.
- Across the program, 92 per cent of key workers accessing Homebuy were first-time buyers.
- The average key worker Homebuy grant was £36,381 (£40, 504 when London Teacher Challenge funding is included).
- The majority of interviewees believed that retention, rather than recruitment, of key workers was the critical labour market problem to be addressed.
- With respect to eligibility, central government officers and other national stakeholders were satisfied with existing occupation-specified eligibility criteria and prioritisation based on local recruitment and retention conditions, while local government employers and RSL interviewees favoured widening eligibility criteria and focusing on the relative value of particular jobs rather than recruitment and retention problems, *per se*.

With respect to the four KWL products:

- *Homebuy* was valued for its flexibility in expanding the choice of location and type of housing for key workers. It was seen to be particularly popular with police officers who are 'generally averse' to housing labelled as 'key worker'. Nevertheless, it was pointed out that Homebuy does not, in the short to medium term, increase the overall supply of affordable housing.
- *Shared Ownership* (as noted above) had a low take-up rate, in part due to the fact that it depends on new building which takes time to come on stream. It is also the case that people tend to prefer a 100% home ownership scheme like Homebuy if the mortgage repayments approach that of the combination of repayments and rent in Shared Ownership.
- *Intermediate Rent* has also had a low take up rate and, again, this may be partly dependent on lack of available opportunities rather than simply lack of demand. More seriously, interviewees argued that the scheme which sets rents at 70-80 per cent of market levels may still be unaffordable by many in the target occupations. It is also the case that there is a limited supply of

¹⁴ These are early findings reported from a study being carried out by GHK Consulting Ltd. and the Centre for Urban and Regional Studies, University of Birmingham.

employer subsidised housing at less than 80 per cent of market level that competes with this KWL product.

- *Clawback* – the requirement of KWL recipients to pay back assistance if they move out of the region within 2 years – does not appear to deter or inhibit take-up of the scheme. Most of the employers interviewed supported the clawback provision.
- In general, interviewees considered that KWL was *appropriately targeted*, with respect to both geography and occupation. However, a number of the zonal agents interviewed considered that the target numbers set for the London Challenge Teacher product were unrealistic, given that the extension of eligibility to further education teachers introduced a new client group with which the zonal agents were unfamiliar and who were difficult to identify and reach. The cost of reaching small populations of particular occupational groups is also relatively high, suggesting that broader rather than narrower occupational groupings should be the aim of specific targeting requirements.
- With respect to *marketing* of the KWL products, interviewees largely agreed that the one-stop marketing of the products worked well and that the most effective marketing mechanism was to develop direct links with relevant employers on a face-to-face basis. Conducting and disseminating brief case studies on individuals drawn from the target occupations was effective in publicising the program to both employers and key workers, particularly in relation to teachers. Zonal agent and ODPM websites were also useful sources of information on the program and ways of accessing it.
- Some tension was identified between employers and zonal agents in relation to the latter's practice of imposing defacto limits on the amounts of assistance available in individual cases.
- Employers generally pointed to an improvement in the recruitment and retention of key workers since the early 2000s. At the early stage of the review, it was not possible to sort out the extent to which improved housing affordability contributed to that outcome, as opposed to the impact of other policies (like improved promotion processes and flexible working arrangements) introduced over the same period as KWL. These issues, along with 'value for money' outcomes for both target workers and government, are being addressed at later stages of the review (not yet completed).

Although this review of the KWL was conducted in the first year of the program with a relatively small number of key worker employers and other stakeholders, and hence the results must be seen as suggestive, early signs were that the program was achieving at least some of its goals. With respect to the broader policy canvas:

Nearly all interviewees felt that KWL was contributing to the Sustainable Communities agenda, either in terms of providing mixed income and mixed tenure new-build developments or in allowing key workers to access areas with high house prices and allowing them to serve their community (ODPM, 2005b, 4).

As a result of continuing negative commentary in the media – and claims that a significant proportion of new housing provided under KWL remained empty – the government responded, in late 2005 by claiming that (ODPM, 2006a):

- As at end of October 2005, 2,149 dwellings had been provided for key workers under New Build Homebuy; of the 546 unoccupied, 226 had been completed less than three months earlier and were in the process of being marketed. Over the whole KWL program, only 7 per cent of the dwellings were unoccupied at that date.
- By the end of October 2005, 7,916 key workers had received assistance 6,479 through accessing equity loans.
- The total sum of assistance committed to KWL had increased to £725million

In early 2006, ODPM (2006b) flagged new funding for KWL for the 2006-07 and 2007-08 years, along with somewhat expanded eligibility criteria. Although the geographical focus of the program remains London, the South-East and the East, eligibility has increased to cover:

- All clinical NHS staff (except doctors and dentists)
- Teachers in schools, further education and sixth form colleges
- Police officers and community support officers
- Uniformed staff in Fire and Rescue Services (eligibility may vary across regions in the light of location-specific recruitment/retention priorities)
- Prison and probation service officers
- Social workers, occupational therapists, educational psychologists, rehabilitation officers for the visually impaired, speech and language therapists and qualified nursery nurses
- Local authority employed clinical staff
- Local authority planners

A fifth KWL product has been added. The NHS provides some short-term intermediate rental accommodation that is now accessible to all key workers, whether or not they are employed in the NHS. The expanded eligibility criteria were applicable from November 2005 with respect to Key Worker Shared Ownership and Intermediate Rented dwellings. However, the new eligibility rules did not apply to Key Worker Open Market Homebuy until April 2006, since government funding will be committed for this purpose from that point.

5.1 Key policy issues

It is clear that the British government is concerned about ensuring the viability of essential services in areas where local housing markets are failing to deliver an adequate supply of affordable housing. However, as the studies discussed in chapter 3 and 4 argued, there are many *other* lower income workers in such areas who are equally as important for the efficient operation of the local economy and are struggling to access appropriate housing. These 'forgotten households' tend to be employed in the private sector, particularly in industries like retailing, hospitality and producer and consumer services. The current policy focus ignores these workers and the potentially negative impacts on the local economy. Conversely, the studies found that high income, new economy workers in the private sector were generally well catered for in high housing cost regions since employers had the flexibility and motivation to tailor remuneration packages to cover high local housing costs.

A further weakness of the current British approach to 'key worker' housing is that it is essentially based on tailoring an existing demand-side subsidy program – Homebuy – to the problem at hand. Like all demand-side approaches, the impact in regions where house markets are tight can be to feed inflationary forces – unless complementary policies act to expand the local supply of lower cost housing. In the UK, the use by local government of land use planning powers to mandate affordable housing provision in new residential developments on both greenfield and brownfield sites (so-called 'section 106' powers) does provide the capacity to increase supply or, at least, to offset the decline that would have otherwise occurred in the overall stock of affordable housing in rapidly growing regions. Section 106 developments are increasingly important in ensuring the access of housing associations to land for social housing provision (Whitehead, et al., 2005). Nevertheless, it is also clear that, in spite of the use of section 106, housing markets have not delivered sufficient affordable housing in 'hot spot' areas like Surrey and Cambridge; if they had then there would not be a need to introduce policies like 'Key Worker Living' – although it is likely that affordability problems in such areas would have been even worse in the absence of s.106 powers.

To date, the 'key worker' debate has not gained much traction in Australia. In part, this stems from the very different spatial structures of Australian cities, compared to British and American cities, and in part to limited data and research focused on this problem. The Australian studies discussed in chapter 3 make an initial but limited start in this direction. The possibility that this relatively neglected topic may exercise Australian policy makers more in future is taken up in the concluding chapter.

6 CONCLUSIONS

This report has focused on the issue of (mis)match between labour and housing markets in large, globally connected cities in the current era of globalisation. Inevitably, attention in the Australian context has been directed towards Sydney and Melbourne. The basic argument draws on the urban analyses of theorists like Sassen, Fainstein and Marcuse who see the processes of globalisation impacting very unevenly across and within countries and who point to the primary role of particular cities and within them, particular regions, as the locus of dynamic economic growth.

Urban economic restructuring, according to this view, is leading to a pronounced internal *spatial* restructuring of cities like Sydney, with high-value new economy businesses increasingly clustered in and near the central city, creating a growing demand for *both* highly skilled knowledge workers *and* low-wage workers, especially in the growing service sector of the economy – heralding the emergence of what was called earlier ‘the synergistic dual urban labour market’. At the same time, growing economic inequality, driven by increasing inequalities in earnings, is being reflected and reinforced through urban housing markets. Patterns of ‘urban containment’ – i.e. the tendency for most people to work reasonably close to their homes – have strengthened and been expressed over space, with low skilled low-wage workers pushed by rising housing prices and rents towards the urban periphery where the available stock of low-cost housing is available, while the inner and some middle suburbs have continued to gentrify, attracting highly skilled and high earnings households. The relatively greater rates of capital gain on dwellings in inner areas has further intensified wealth differentials across the urban population (and between the major capital cities and non-metropolitan Australia), further increasing the housing and employment choices of new economy workers at the expense of other workers. The global city thus develops as an internally segregated, increasingly segmented metropolitan region in which particular parts of the city – notably, the central core – are strongly integrated with similar regions elsewhere in the world and other parts – notably, the outer suburbs and fringe areas – are increasingly marginalised reception centres for low-wage workers who ‘trade off’ long commutes or unemployment for access to affordable housing.

The interaction of housing and labour markets over space thus raises the spectre of spatial mismatch, at least with respect to the inaccessibility of the inner suburbs and central city to low skilled service workers. Nor is it clear that the strong outer suburban rate of job growth in Melbourne and Sydney substantially increases the effective accessibility of low-wage workers living on or near the fringe. Poor transport resources and poor job information can lock outer suburban households out of local labour markets, so that high local unemployment exists with high local vacancy rates. These spatially expressed effects can then reinforce job bottlenecks due to inadequate skills in the both old economy and new economy industries.

Initially, concern over the effects of spatial mismatch centred on the welfare of disadvantaged, marginalised groups. In other words, the major policy issue was seen to be about social equity and the appropriate policy initiatives to do with overcoming the barriers limiting employment opportunities for those groups. However, over the past decade, attention has shifted from equity to efficiency considerations. If urban housing markets act to effectively exclude low-wage

workers from central areas of high labour demand, growth industries – e.g. advanced business services – will struggle to operate optimally.

Bottlenecks leading to problems in recruiting and retaining staff impinge negatively on the allocative efficiency of the regional economy, as do entrenched spatial pockets of unemployment on the urban fringe – i.e. labour is not being put to its most productive uses. However, the most damaging impacts of spatial mismatch may relate to the *dynamic efficiency* of the regional economy. Regional economic growth is dependent on continuous innovations that improve productivity and increase the competitive advantage of the globally active businesses located in the strategic central areas of the city. If these firms are underperforming, in part due to labour shortages and bottlenecks, then the whole economy suffers. Labour bottlenecks caused by spatial inaccessibility will team with particular skill deficits at all levels to undercut the competitive advantage of these firms – the dynamic force in the regional economy – with deleterious flow-on effects for the economy at large. Alternatively, these firms may be forced to pay higher wages to attract and keep workers, increasing their cost base and cutting into their competitive advantage. Either way, the capacity of these leading-edge firms to drive local metropolitan growth will be reduced.

In the Australian context little empirical research is available to determine the degree to which these effects are occurring. It may, therefore, be useful to carry out a series of case studies such as those described in chapter 3 for regions in the UK, in order to begin to scope the nature and scale of any problems in Australia. It is also the case that, at least with respect to issues of allocative efficiency, some of the problem may be being exported to non-metropolitan locations. To the extent that low wage workers are being pushed out of the major cities to smaller towns and regions due to high housing costs, problems of spatial mismatch and declining housing affordability would appear to be reducing – but only in the metropolitan regions and only on the surface. The housing may be more affordable in smaller settlements but job opportunities worse or non-existent, throwing these workers onto the unemployment rolls of their new town rather than in the metropolitan region. This has not actually increased employment and output anywhere, though metropolitan unemployment figures have declined along with the demand there for affordable housing. In reality, all that has happened is that the now hidden problem of declining metropolitan housing affordability has shifted unemployment from one place to another¹⁵.

To conclude, the overseas debates and policy developments addressing spatial mismatch, 'key workers' and 'workforce housing' have not, to date, gained traction in Australia. This appears to be due to a series of factors: first, the particular spatial patterns of economic restructuring and socio-economic advantage and disadvantage characterising Australian urbanisation; second, the marginal status of housing on the agendas of governments in Australia; thirdly, the absence of detailed (as opposed to speculative and descriptive) research on the topic, and; finally, the tendency to see housing issues as primarily to do with social equity or justice concerns rather than economic efficiency and growth.

¹⁵ In this context, at the Australian Financial Review Housing Congress, in Sydney (30-31 March 2006), the Queensland Housing Minister recounted the true story of a woman who had approached him at a public meeting in the regional city of Mackay and told him that she and her family were being forced to move to another town because they could not afford to rent a family house in Mackay, even though her husband was fully employed and the household income was in excess of \$50,000 per year.

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