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**Why Detroit was one of the hardest hit metros by the U.S. housing crash?**

The city of Detroit, the largest city in the Midwestern state of Michigan, developed from a small fur trading post of New France to a world-class automobile industrial powerhouse and the fourth largest American city by the mid-20th century. Now, it became the focus of attention because of its super low housing price. 24/7 Wall St. which is a financial news and analysis website pulled Census data on the 75 largest U.S. metropolitan areas and ranked the cities with the highest overall vacancy rates for both homeowner vacancy and rental vacancy for the second quarter of 2011 and Detroit metro list the 7th place. Why has Detroit so low house price? The reason is automobile industry declined, and people left the city. Next, the Great Recession (2007 - 2009) made things a lot worse. In 2009, almost reaching 30% unemployment rate let more and more people give up their house (Stockdale, McIntyre and Sauter). In Detroit’s housing market, there are too much sellers and continued decreasing buyers. Such relationship of demand and supply lets Detroit’s housing price go to down.

The biggest decline for home prices in Detroit occurred in the second quarter of 2009, with prices falling from a peak in the first quarter of 2006. Foreclosure sales have dropped from around 55% in January of 2012 to around 36% a year later (McIntyre). For example, according to Wayne County records, someone bought 290 Detroit properties for $189,600 at the October tax auction (Christoff). In recent two years, although nearly every important set of government and private-sector figures show a housing market on the rebound, Detroit’s housing price is still very low. 24/7 Wall St. reviewed Detroit was 53.6% drop in home prices the past six years and the median home price is $45,000 which remains the lowest by far of any of the 20 cities in the Case-Shiller benchmark index that is one of the most widely followed measures of home price changes (McIntyre).

Before we figure out why Detroit’s housing price is so low, we should know how the housing price come from. It is the interaction of demand and supply. Here, demand refers to buyers, supply presents to sellers in Detroit’s housing market. According to microeconomics, we can draw the Detroit’s housing demand curve which is a graph that shows the relationship between the Detroit’s housing price and buyers’ quantity. Of course, this demand curve should obey the law of demand which states that, holding everything else constant, when the housing price falls, the buyers will increase; when the housing price rises, the buyers will decrease.

At the same time, we can draw the Detroit’s housing supply curve which is a graph that shows the relationship between the Detroit’s housing price and sellers’ quantity. And this supply curve should obey the law of supply which states that, holding everything else constant, when the housing price rises, the sellers will increase; when the housing price  Figure – 1: Detroit housing market

falls, the sellers will decrease. If we put the demand curve and the supply curve together, they will intersect (see Figure - 1). That is market equilibrium. Only at this intersecting point is the quantity demanded equal to the quantity supplied. That means only at this price, buyers and sellers will make a deal.



Figure – 2: shift demand or shift supply

Only if the demand curve shift left or the supply curve shift right, the price will go down. In other words, when buyers become fewer or sellers are too much, or both of these situations (see Figure - 2), the housing price decreases. In Detroit housing market, the fact is people are leaving this city, sellers are increasing fast and buyers become very little. According to Census Bureau data

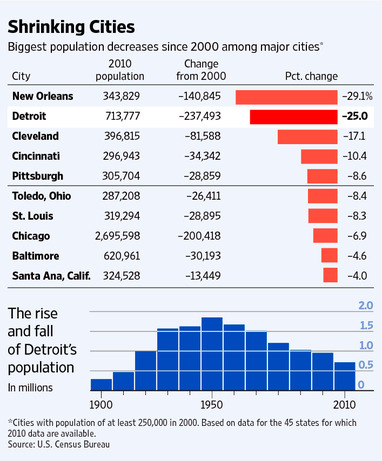


Figure – 3: Detroit population

released on March 26, 2013, Detroit's population decreases 25% in the past decade to 713,777. That's the city's lowest population level since 1910 (see Figure - 3). In all, the city lost more than 237,000 residents, including 185,000 blacks and about 41,000 whites. Roughly one-quarter of Detroit’s housing units are vacant, according to Detro**i**t Future City, a 50-year blueprint for the city’s recovery. In 1950, Detroit was the fifth-largest city in America, behind New York, Chicago, Philadelphia and Los Angeles, and it was in the top 10 as recently as the 1990 Census. Now, Detroit is likely to fall to 19th, behind Indianapolis and Columbus, Ohio. ( Linebaugh)

Why are people leaving Detroit? The key point is the "Big Three" American car companies, General Motors, Chrysler and Ford have based many factories in Detroit metro. Most of this area’s person work for these automobile factories. Because American automobile industry declined in recent decades, many people have to give up their home after losing their jobs.

American automobile industry didn’t collapse in one day. Fifty years ago, United States was the dominant manufacturer of automobiles and trucks on the globe. Now, in 2010 U.S. ran a trade deficit in automobiles, trucks and parts with the rest of the world of $110 billion. The combined U.S. market share of the "Big Three" American car companies fell from 70% in 1998 to 53% in 2008.

What has led to the decline of US car manufacturers in their home market? While it was inevitable they would eventually lose their monopoly position, their failure to adapt their production methods and meet changing consumer tastes has accelerated their decline (Schifferes). In the 1950s and 1960s, US firms failed to innovate in the design of cars, preferring to make money by increasing the size and weight of their vehicles by adding extras like air conditioning, power steering, and fancy sound systems. It was left to European manufacturers to develop disc brakes, rack-and-pinion steering, air-cooled and diesel engines. And the mass production system discouraged innovation because it was so expensive to introduce fundamentally new models. Meanwhile, Toyota was also making a virtue of adversity, changing its production system to

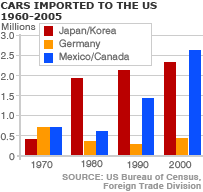


Figure – 4

become leaner and more efficient than its rivals. It was the oil crisis in the 1970s (see Figure - 4) that first illuminated the problems of US automakers. For the first time, smaller cars were the rage, and US consumers found that cars like the Toyota Corolla were an attractive alternative to big American cars. Imports of Japanese cars soared in the 1980s, to the chagrin of the US

companies and the unions alike, taking nearly one-quarter of the US market. And when the

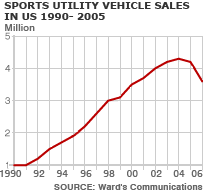


Figure - 5

companies pressured the US government into limiting imports from Japan, Toyota and Nissan started building car plants in the US. By 2005, these Japanese "transplants" were producing 4 million cars a years, one-quarter of US output, and more than GM. In 1990s, with oil back at $18 a barrel, the US companies used the SUV (Sports Utility Vehicle) to face to the Japanese threat (see

Figure - 5). In 2006, the price of gasoline in the US reached a record $3 per gallon in most states. As a result, SUV sales slumped, and the sale of smaller vehicles rose. At the same year, both Ford and GM finally accepted they would never dominate the US car market as in the past. The "Big Three" American car companies cut thousands jobs in Detroit and move to outside the U.S to save the cost. Today, only Chrysler still operates an automobile assembly line within Detroit city limits. Only about 40 percent of Ford's 178,000 workers are employed in North America, and a significant portion of those jobs are in Canada and Mexico.

Later, the Great Recession (2007 - 2009) added to the negative tone. No industry more cyclical or more dependent on the business cycle than the auto industry. According to macroeconomics, Saving = GDP – Consumption – Government Purchases. In the recession, GDP will decrease. That means people’s income will decrease. To keep the enough saving and necessary balance, some of consumption and government purchases will be cut, especially these big shares of the budget like cars. In 2007-2009 recession, cars sale declined rapidly. Profits decline led to cut jobs. One analysis of census figures found that 48.5% of all men living in Detroit from age 20 to age 64 did not have a job during 2008. Since 2005, the metropolitan area has lost approximately 323,400 jobs (Stockdale, McIntyre and Sauter).

In Detroit, the unemployment rate surpassed 17% in 2009 though the nation's jobless rate never rose above 10.1% the past decade. And even though the city's jobless rate has rebounded seven percentage points (10.2%), it remains more than two percentage points above the nationwide rate, which was 7.8% in December and ticked up to 7.9% in January. One of just a handful of large U.S. cities where the unemployment rate remains in double digits, the city's jobless rate has plummeted since its Great Recession peak. But at 10%, the unemployment rate here is higher now than it was during the worst periods for a few of the other cities in the index (McIntyre). So high unemployment push people leave this city and move to other place to find jobs. When they moved, they wanted to sell their houses. In Detroit housing market, there are more and more sellers but buyers are still little. This kind of product surplus makes Detroit housing price go down.

National Bureau of Economic Research show that variation in the cyclical behavior of real house prices across metropolitan areas is attributable to more than just variation in local economies. In Detroit, the price affect by local auto industry. Because American auto industry has fallen steadily in recent years and manufacturing jobs have disappeared, Detroit local people are moving out this area. In the 1950s, Detroit's population was around two million. In 2012, it was 706,585. The number of vacant housing units doubled in the past decade to nearly 80,000, more than one-fifth of the city's housing stock, the Census Bureau reported. Moved people want to sell their houses and the housing market is supply exceeding demand. That is why Detroit housing price is so low.

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