Faculty Profile

James Follain is an economist with extensive experience in the analysis of housing and mortgage markets. He is currently the principal of James R. Follain LLC, whose recent contracts have been with the U.S. Department of Housing and Urban Development, the Massachusetts Attorney General's Office, and the Lincoln Institute of Land Policy. Follain is also a senior fellow at the Nelson A. Rockefeller Institute of Government at the University of Albany/SUNY, and an advisor to FI Consulting, a financial services firm headed by his son, Tom, and a former student, Roman Iwachiw.

Prior to the establishment of the LLC and his move to the Capital Region of Albany, Follain was a tenured professor of economics at Syracuse University from 1988 to 1998 and also worked with various business, government, and policy-oriented organizations. He has conducted research on the risks of mortgage lending, the tax treatment of housing, mortgage choice, suburbanization, property and land taxes, and the current mortgage crisis. He has authored and coauthored numerous publications for academic and broader audiences and served as the president of the American Real Estate and Urban Economics Association (AREUEA) in 1988. He received his Ph.D. in economics from the University of California at Davis and his B.A. from the University of San Francisco. Contact: jfollain@nycap.rr.com.

James R. Follain

LAND LINES: *How were you introduced to the Lincoln Institute?*

JAMES FOLLAIN: My involvement with the Lincoln Institute has spanned 30 years and has provided me with the opportunity to meet many top people in the field of public finance. Roy Bahl, now a Regents Professor of Economics and Founding Dean of the Andrew Young School of Policy Studies at Georgia State University, introduced me to the Institute in the early 1980s, when we were both on the faculty of the Maxwell School of Citizenship and Public Affairs at Syracuse University in New York.

We worked together on a major study of tax reform in Jamaica, and I was fortunate to participate in a study of the country's land tax with Professor Daniel Holland of Massachusetts Institute of Technology, who also has a long affiliation with the Lincoln Institute. One of the outputs of that larger research project was a book, *The Jamaican Tax Reform*, edited by Roy Bahl and published by the Institute in 1991. The book is now out of print, but some information is available at the GSU Web site.

LAND LINES: *What are some other highlights of your work with the Institute?*

JAMES FOLLAIN: In 1988 I participated in the annual TRED Conference that for many years was held at the Institute's offices in Cambridge and focused on various aspects of taxation, resources, and economic development. Professor Edwin S. Mills and I later coedited a special issue of the *AREUEA Journal* (1989) based on the six papers and discussant comments presented at that conference, which was titled "Interactions between Finance and Urban Development." The participants included many public finance economists including Karl Case, Patric Hendershott, John Kain, Rudolph Penner, John Quigley, Kerry Vandell, and William Wheaton, as well as people relatively new to the profession who have gone on to become leaders such as David Geltner and Dan Quan.

LAND LINES: *I understand you also have worked with Gregory K. Ingram, the Institute's current president and CEO.*

JAMES FOLLAIN: Yes, that's correct. Early in my career I had the opportunity to work closely with Greg when he led the World Bank City Study project in Bogotá, Colombia. Greg and his team collected data that were used in a number of studies that I coauthored with Emmanuel Jimenez, Steve Malpezzi, and others. In a paper on housing characteristics in developing countries (Follain and Jimenez 1985), we used the data set assembled by Greg's team. I remember, for example, having access to data with geo-coded locational coordinates, which was quite unusual at that time for the kinds of hedonic price index studies we were doing in the United States or elsewhere. The broad topic of the work and the project was also at the frontier and dealt with ways in which squatter settlements could be improved to become better homes for their residents.

LAND LINES: *How did you become involved with the Lincoln Institute more recently?*

JAMES FOLLAIN: I reconnected with Greg at the 2010 meetings of the Weimer School when he was honored as a Halbert C. Smith Honorary Fellow at the Weimer School/Homer Hoyt Institute in Florida. Established in 1982, the Weimer School is a unique and effective forum for fostering academic work that improves the quality of decision making in real estate and land economics. I became a Weimer Fellow in 1991 and currently serve on the faculty. We host two meetings per year to discuss recent research by new and current fellows and to recognize others who are working on related topics. During that 2010 meeting Greg and I initiated a conversation about our common interest in investigating what is different and important about the most recent house price bubble-bust. This discussion continued for some time and led to my involvement in a research project sponsored by the Lincoln Institute.

LAND LINES: *What research are you working on currently?*

JAMES FOLLAIN: This has been a most interesting year for me. It began with publication of a paper supported by the Research Institute for Housing America entitled "A Study of Real Estate Markets in Declining Cities." A second paper, coauthored with Seth Giertz of the University of Nebraska, entitled "Using Monte Carlo Simulations to Establish a New House Price Stress Test," was just published in the *Journal of Housing Economics*.

My most recent assignment with the Lincoln Institute of Land Policy has resulted in a Lincoln Institute working paper, also coauthored with Seth Giertz, entitled "A Look at U.S. House Price Bubbles from 1980–2010 and the Role of Local Market Conditions." We explored a variety of models to explain house price growth at the MSA level over the three decades since 1980. Our findings support and champion a theme quite consistent with those supported by the Lincoln Institute over the years—the importance of recognizing the wide variability of housing markets and the role of local conditions. We are currently moving forward on two new projects sponsored by the Lincoln Institute that focus on the most recent house price bubble and bust period, using data from the past decade.

LAND LINES: *What are some of the potential policy implications of this research on housing bubbles?*

JAMES FOLLAIN: One has to do with the development of policies by the Federal Reserve Board and other agencies to combat house price bubbles before they bust. My sense is that the Fed understands the limits of standard monetary policy for this purpose, as evidenced by the growing literature on this topic. It is in the process of considering a wider array of macro-prudential tools that might be used for this purpose. The tool that I have in mind is one that I have written about and championed in earlier times—geographical variations in the pricing of mortgage credit risk that take account of local housing market conditions.

LAND LINES: *Is this work likely to be useful and relevant to housing market policy in other countries?*

JAMES FOLLAIN: I think so. The literature on house price bubbles is enormous and includes many recent papers about conditions in China and Europe. In addition, one of the key results of empirical work on urban economics over the past few decades is the similarity of findings across large cities in different regions. The spatial distribution of development, decentralization of employment and residences, declining central densities, and determinants of travel and mode choice show consistent results across large cities in the world. These similarities carry over to many housing market outcomes, indicating that one country can learn from another's housing policy experiences.

LAND LINES: *How does your work at the Rockefeller Institute relate to these investigations?*

JAMES FOLLAIN: My current focus there is on the impact of the Great Recession and the house price bubble-bust cycle on local property taxes. My concerns are twofold. First, property values have declined in many areas and reduced the value of the tax base. Second, the number of sales available that can be used to value properties is greatly diminished, which can reduce the precision of assessments and increase horizontal inequities. I have written a couple of case studies using data from New York State and I am in the process of developing a larger project on the topic.

LAND LINES: *What prompted you to move from academia to policy making, and can you share some experiences as a housing policy analyst in Washington?*

JAMES FOLLAIN: I was attracted by the possibility of working within an institution, Freddie Mac, with a dual mission to expand the securitization of mortgages and access to credit to low- and moderate-income households. The first part of my time with Freddie focused on the affordable housing goals it was mandated to achieve. The latter part focused on the development of capital rules for the credit risk embodied in the mortgages included in its securities. I moved to the Federal Reserve Board in 2003 to continue work on capital adequacy for large financial banks that invest in residential mortgages. I testified before Congress in late 2005 and have written about some of these experiences. One key insight has to do with the challenges faced by both individuals and corporations, especially large financial institutions, in coming to grips with the risk of extreme and difficult-to-predict events.

LAND LINES: *What is your view about the likely pace and character of the housing market recovery after the recent decline in prices and construction activity?*

JAMES FOLLAIN: I emphasize in my recent research that house prices have declined dramatically during the past five years in many parts of the country, wiping out massive amounts of wealth among homeowners and lenders. These declines may well be justifiable for those areas particularly hard hit by the crisis such as Arizona, California, Florida, and Nevada. In my article about declining cities, I discuss what I refer to as "emerging declining cities" because the current housing stock may exceed what future demand will support. Full recovery in these places will take many years since house price levels at their peak reflected wildly exaggerated expectations of future growth. L

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