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Washington's Economic Boom, Financed by You

1986: Michael Horsely; Now: Michael Horsely for The New York Times

The corner of N Street and 15th Street, NW Washington.

By: Annie Lawrey - January 10, 2013

One damp morning this winter, Jim Abdo was looking through architectural renderings at his office in Logan Circle, one of the many leafy Washington neighborhoods anchored by a statue of a long-dead guy riding a horse. Abdo got his start as a property developer by buying decrepit buildings and modernizing them, and his headquarters shows off the trick. The adjoining storefronts had been stripped bare and rebuilt, all warm wood and cold glass with exposed brick and beams. It looked like a Brooklyn design studio or a Silicon Valley start-up, or at least how those offices might look in a Nancy Meyers movie. But Abdo has built his business in the unstylish land of think tanks and tepid salmon lunches and boxy women's suits.

Abdo, a lithe and neat man with salt-and-pepper hair, was wearing jeans and a trim pullover and excitedly explaining how he was going to raze the office we were sitting in and replace it with more of his signature "luxury but affordable," as he put it, rental units. He showed me a photograph of our location, a corner with a busy coffee shop with outdoor seating, a high-end rug store and the Abdo Development office. In the next slide, the buildings had been replaced by a handsome new glass-and-brick stack of a building, custom-built for white-collar professionals paying $3,000 in rent, all made possible by their low-level but cushy private-sector jobs. "We're looking for those kids just out of law school who've come to Washington and they're working 14 hours a day, but they want a place that isn't a group house," he said. "It's for people who want to say, 'I've arrived.' "

Eager to show what arriving in Washington looks like these days, Abdo escorted me into his hulking Range Rover with a two-digit license plate — assigned to him by the former mayor Anthony Williams, who is godfather to his son — and we barreled south across the Potomac. The first destination was Gaslight Square, a pair of condo buildings featuring units with double-height living rooms and Wolf ranges, just across the river from the high-end shopping district of Georgetown. (There's room for a third building, which Abdo plans to break ground on soon.) Abdo pushed open the door to a model unit, and we walked in on a sandy-haired 20-something in a fleece jacket signing papers. "I didn't plan that," Abdo said, feigning a red-handed gesture. "We get lots of first-time buyers from Northrop Grumman, CEB" — the massive defense contractor and the corporate advisory firm — "places like that."

Washington wasn't always the place where young professionals plunked down $3,000 a month to announce their arrival. When Abdo founded his business, in 1996, the United States was enjoying around 4 percent economic growth, but in Washington, dysfunction and Mayor Marion Barry Jr. reigned. The city government was locked in a mismanagement-driven fiscal crisis: traffic lights were malfunctioning; garbage trucks stopped picking up trash; District residents were advised to boil their own water; President Clinton and Congress placed the city into federal receivership. During the 1990s, while employment in Washington declined, Northern Virginia added 300,000 jobs, and the Maryland suburbs added about half that. "Washington was a national embarrassment," Abdo said back inside the Range Rover. "There was all this aggressive panhandling, all these vacant burned-out buildings. But I knew the city could only go so low. It's one of the least cyclical economies in the country, and it has this tremendous urban fabric."

Abdo figured that federal employment would remain relatively stable, even in recessions. The continued opening of Metro stations would also allow for transit-driven development. And of course, there was that tremendous urban fabric — the brick row houses that make up the bulk of the housing in the city's center, from Georgetown in the west to Anacostia in the southeast, and give it some of its genteel European feel. Abdo's timing, it turned out, couldn't have been better. Billions in federal spending, largely a result of two foreign wars, were pouring into the local economy by the early 2000s. Then came the housing bubble. But after it burst, a remarkable inversion occurred: as the country withered, Washington bloomed. Since 2007, the regional economy has expanded about three times as much as the overall country's. By some measures, the Washington area has become the richest region in the country. It is now home to the three highest-income counties in the United States, and seven out of the Top 10.

The growth has arrived in something like concentric circles. Increased government spending has bumped up the region's human capital, drawing other businesses, from technology to medicine to hospitality. Restaurants and bars and yoga studios have cropped up to feed and clothe and stretch all those workers, and people like Jim Abdo have been there to provide the population — which grew by 650,000 between 2000 and 2010 — with two-bedrooms with Wolf ranges.

During our drive, Abdo narrated this revival with such intensity that he took a few wrong turns, despite the fact that downtown is just a grid dotted with traffic circles. Near the George Washington University campus, he pointed out a cheap hotel that he plans to turn into a pod hotel. Over by H Street, a neighborhood just a few years ago virtually untouched by gentrification, he pointed out a former convent that he converted into apartments. Abdo announced that he helped develop "thousands" of such tasteful, expensive though not outrageously priced units during the past decade and a half, for "people of substance," he said, "people who want to participate in this city." Mayor Williams had already bought a unit in H Street. Sheila Johnson, the philanthropist and co-founder of Black Entertainment Television, bought a chapel in the convent.

How Washington managed this transformation, however, is not a story that the rest of the country might want to hear, because we largely financed it. As the size of the federal budget has ballooned over the past decade, more and more of that money has remained in the District. "We get about 15 cents of every procurement dollar spent by the federal government," says Stephen Fuller, a professor of public policy at George Mason University and an expert on the region. "There's great dependence there." And with dependence comes fragility. About 40 percent of the regional economy, Fuller says, relies on federal spending.

Congress may have passed legislation to avert the middle-class tax increases of the so-called "fiscal cliff," but it has only postponed what is known as the "sequester" — $1.2 trillion in budget cuts. And that's on top of several hundred billion dollars in cuts that the Pentagon has already agreed to. The capital's boom days, in other words, might be over. "Rather than leading the nation, we're going to be lagging it going forward," Fuller says.

Peak Washington of the early 2010s, many economists believe, got its start during the Reagan Revolution of the 1980s. Reagan's messianic push to get government out of the way of private-sector growth famously led to lower taxes and reduced regulation. It also led to a subtle change in the way government did business. Hiring became secondary to contracting, and more and more public projects were outsourced to private firms.

Washington's economy did well under Reagan (added military spending gave it a boost), but the move to contract out more and more government work proved to be a crucial long-term change. In 1993, Bill Clinton announced a "reinventing government" initiative, which ultimately included cutting the federal work force by about 250,000 positions. The agencies winnowed their rolls, but over the course of the Clinton years, their budgets expanded, and in many cases, the work just went to contractors. Those contractors often came at a bloated cost, too. In a study released in 2011, the Project on Government Oversight found that using contractors can cost the federal government about twice as much as federal employees for comparable work. According to the study, the salary for a federally employed computer engineer would be about $135,000; a contractor might bill the government around $270,000 for similar work.

It was not until the Bush years, though, that this increasingly wealthy not-federal-but-still-government work force truly metastasized. The amorphous war on terror and the creation of the Department of Homeland Security — plus the wars in Afghanistan and Iraq — bloated the country's spending by about $1 trillion. The contracting dollars that were pumped into the local economy, Fuller says, more than doubled between 2000 and 2010, when it reached $80 billion a year. This, in turn, created hundreds of thousand of desk jobs and fostered a sprawl of nameless, faceless office parks lining the roads out to Dulles Airport.

In the process, tens of thousands of new workers, often well-paid young white-collar professionals in areas like technology, bioscience and engineering, also entered the local economy. And many of these young professionals, as Abdo hoped, worked 14-hour days and wanted to live near work, friends, coffee shops and yoga studios. This infusion of human capital, combined with proximity to the Federal tap, proved attractive to a huge number of other businesses looking to hire. Google has opened an outpost in Washington. LivingSocial owns a huge, hiply decorated space downtown. Audi, Intelsat, Hilton Worldwide and dozens of other firms have opened up offices or moved their headquarters to the region. The health care sector, with its proximity to the National Institutes of Health, has greatly expanded, too. “Maryland got the life sciences, and Virginia got the death sciences,” Jim Moran, the Democratic congressman who represents much of the military corridor in Northern Virginia, said. “Of course, NoVa, given the two wars, it’s done even better than suburban Maryland.”

But the contours of Washington’s wealth are far different from those in other boom towns. In New York or San Francisco, inequality has become fractured: the upper middle class has pulled away from the middle class, and the rich from the upper middle class, and the really rich from the rich and so on. Washington, though, has become an increasingly two-class town. About a third of households make less than $60,000 a year, while around 45 percent make more than $100,000 a year. Relatively few are what might be traditionally considered middle class.

Perhaps that, more than anything, explains the appearance of the new gilded-age Washington, which is less about wealth than it is about the growth of one of the most ascendant petite bourgeoisies that the United States has known. In the five years since I moved to the city, the transformation has been visible, palpable and sometimes astonishing. Washington has become a place that sports a decent turnover in multimillion-dollar homes, a Tesla dealership and a dozen fabulous new restaurants a year. You can even purchase a $69 tasting menu of craft cocktails at a speakeasy, if that’s your thing.

More prosaically, though, new residents have flocked to the city for its profusion of jobs and stayed on account of its bars and restaurants and its cheap rents, at least compared with New York. In 2007, David Alpert, a former Google employee, and his wife, a lawyer, decided to move to the District rather than staying in the New York area. “When I first moved here,” Alpert, the proprietor of the yuppie urbanist blog Greater Greater Washington, told me, “complaining about how terrible D.C. was was something everybody did. You’d move here for some government job and then talk about how it’s a terrible place. I think that has changed. Maybe it’s that I’m six years older, and my friends are six years older, and people have been here longer. But I don’t think it’s so common to come in and say, ‘Everything sucks.’ ”

Perhaps that’s because Washington is changing in their image. Oramenta F. Newsome, who has worked in community development in Washington since the ’90s, told me that while longtime residents benefited from new jobs and businesses, many eventually left. “If the market moves, it moves,” explained Newsome, now the executive director of the Washington office of the Local Initiatives Support Corporation. And these days, many lower-income families have moved from the District altogether, often to the suburbs of Maryland, like Prince George's County, or even farther out. Newsome stressed that the change has been economically driven, but there are some racial overtones too.

"People will tell you it's not about race, but it is," said George Pelecanos, a Washington native, novelist and screenwriter who worked on "The Wire." "It's no longer a black city, and a lot is going to be lost because of that. But the flip side of that is, I try not to get too nostalgic about what Washington was."

The transition can be jarring. A few blocks from Abdo's office are cheap Chinese joints, a large homeless shelter and empty buildings. But cranes and luxury condos have sprouted up in between, along with a four-story furniture emporium, Room & Board, which sells $2,500 sleek wood dining tables just a block or two away from a pawnshop. There is Estadio, a high-end tapas bar that makes its own tonic water. On a cross street sits Whole Foods. It's no surprise that penthouses in the area often go for well more than $1 million.

According to the Federal Reserve, 2013 is supposed to be the year that the U.S. economy approaches normal growth, around 3 percent. Housing prices are rising, unemployment is at the lowest level in four years. And yet there is a sense that the capital is headed for a slowdown. Among the Pentagon's plans to cut nearly $500 billion over the next decade could be reductions not only in matériel but also to all manner of support staff. The homeland-security budgets look certain to see significant reductions, too. One recent estimate noted that more than two million jobs would be at stake if the sequester comes into effect.

The big contractors and their lobbyists are already fighting back, and there is little doubt that years of rampant military, defense and security spending will be hard to curtail. "This whole nontransparent military-security buildup has created a lot of pressure on — or opportunities for — a variety of politicians and policy makers to misbehave," says Daron Acemoglu, a development economist at the Massachusetts Institute of Technology. "Nobody's blinking an eye at having the same thing done by seven different agencies. And there's no way to know whether the spending is necessary or not." Still, fighting the majority of the cuts seems futile. The wars are winding down, and the whole country is being asked to sacrifice through entitlement cuts and increases on income and capital-gains taxes. "My reading is that the defense industry is not going to get what they want," says William D. Hartung, a defense analyst at the Center for International Policy. "There are going to be more cuts. I think they're starting to realize that."

As it turns out, though, those cuts might only be following a much more subtle and already extant trend. Despite Jim Abdo's optimism, despite the Tesla dealership, the homemade tonic water and the $2,500 wood tables, Washington has actually been slowing down since the Bush years. The dollars devoted to federal contracting have declined in the past two years of the Obama administration. Job growth has been lagging in recent quarters, and offices are renting less space than they used to. "I think that the growth rate," Fuller says, referring specifically to federal spending, "is going to be something like 1 percent a year over the next five years. But for the past 10, it's been something like 8 percent a year. Going from 8 to 1, that feels like more than a cutback."

It is not hard to imagine how this marked decrease in federal spending might ripple through the regional economy. Scant job growth will mean lower wages, meaning slower consumer spending, meaning less demand for new bars and clubs and stores and luxury apartments. But just how deeply this will affect the economy is unclear. It's possible that federal budgets might never get cut outright, with Congress instead slowing the path of spending growth. That might mean slower growth for Washington, but hardly a contraction or a regional recession of the kind that plagued Detroit after the auto industry shrank. And even if the sequester cuts are more drastic, it might take years before the local economy feels them. "People are saying, 'We're going to lose a million jobs here,' " says Gordon Adams, a professor of international relations at American University. "That's not going to happen, and it's not going to happen because contractors are working on existing contracts financed with prior-year dollars. We're going to be working through this for some time, and there's going to be a very slow roll to actual projects. The implications aren't for current work, but the next round of work."

For some economists, though, this course correction — while miserable in the short term — could provide a long-term benefit. There's something unsavory about having a capital city doing outrageously well while the rest of the country is limping along — especially when its economy is premised in part on capturing wealth rather than creating it. The enormous profusion of military spending drew money from other priorities, and those dollars might find better uses elsewhere, says Robert Pollin, an economist at the University of Massachusetts at Amherst. "If you look at military spending, it creates about 11 jobs per $1 million of expenditure," says Pollin, who grew up in the region. "Infrastructure investment, in things like the green economy, it's 17 jobs per $1 million in spending — that's 50 percent more. And education? Education is 27 [jobs] per $1 million."

David Boaz, executive vice president of the Cato Institute, told me: "Washington's economy is based on the confiscation and transfer of wealth produced elsewhere. Out in the country they're growing food, building cars and designing software — all these things that raise our standard of living. Here in Washington, everyone is writing memos to each other about how to take some of that money and which special interest should get it." I asked him if he liked living in the city, which has become undeniably nicer. Boaz sputtered a bit. "I can't walk to lunch from my office without having to avoid the construction projects!" he said. "For Washington, it does mean better restaurants and better entertainment, and the potholes get filled faster. But for the country as a whole? I don't think it's a good thing for America."

If there is a broad sense that peak Washington is already past, it's hardly perceptible in the city itself. Dozens of cranes dot the skyline, and construction projects snarl major intersections downtown. This past summer, if you had swung by Capitol Hill on a particular Saturday evening, you might have found yourself among scores of 20-somethings in black tie and flapper gear for a ball given by the city's craft bartenders' guild that costs $100 for a two-hour open bar. Or you could have recently wandered through the Ritz-Carlton, which is currently setting up for Obama's second inauguration. For $100,000 you can stay, shop and eat the salted caramels that the president himself apparently adores while watching the inaugural festivities.

Abdo admitted that he, too, expected that the city's extraordinary growth would slow down, but he suggested that the change would be a soft landing rather than a crash. The city had been so revitalized that the new workers and consumers would keep drawing in businesses that would keep drawing in new workers, he theorized, in a virtuous development cycle that might allow the region to stop leaning so heavily on federal money. That happens to more or less jell with Fuller's prediction. During the boom years, the metro area had diversified enough into technology, bioscience and other industries to withstand the shock. It has started to resemble vibrant, heterogeneous capitals like London and Tokyo more than dry, homogeneous capitals like Brasília and Ottawa. “We’re shifting from a top-down economy to one based on spending by residents,” Fuller says.

Moran, the Democratic congressman from Northern Virginia, is cautiously optimistic, too. “As we’ve grown, we’ve been the beneficiary of what Richard Florida calls the ‘rise of the creative class,’ ” Moran told me. “The lifestyle built around Metro stations, the ability to work and play without the automobile, the tremendous collaboration taking place among young technology professionals. That may have a life of its own. It remains to be seen how self-sufficient we can be without the continuing growth of the federal government.”

On the final spot on our tour, Abdo took me to his newest, biggest project. We drove north on North Capitol Street, as if we were driving out of the District, to a shabby and decidedly unhip neighborhood called Brookland. It is a mostly older, mostly lower-middle-class neighborhood, underserved by grocery stores and restaurants and overlooked by many of the young professionals farther south in Bloomingdale or Shaw or Capitol Hill. Abdo was undeterred. He said that Catholic University and the young families nearby needed new places to go, and that hip youngsters were being priced out of neighborhoods downtown. He had already purchased and leased nearly nine acres for a number of apartment buildings with sidewalk cafes and art studios. “This is going to be an arts walk,” Abdo said, pulling his car up to point out the hollow building shells. One building faced a set of train tracks, and he styled the back of the apartment building to look like a factory that had always been there, even though it had only just arrived.

Whatever happens to Washington, it seems hard to believe that there won’t be enough people willing to pony up $3,000 a month to inhabit Abdo’s latest vision, to drink lattes on his sidewalk cafe and walk on his arts walk. Perhaps more valuable than the hundreds of billions in government money, the boom years introduced the capital to tens of thousands of young and educated workers who arrived for the promise of some job — any job — and, in the process, married, had a kid and needed to upgrade to a bigger place. In order to survive the cuts, sure, Washington’s economy will need to diversify and attract new businesses. But perhaps the best thing that has come of the past decade is that the city has proved, unequivocally, that it’s not just the province of think tanks and tepid salmon and boxy suits anymore.