Q&A...

with Kyle Mangum, a senior economist here at the Philadelphia Fed.

Kyle Mangum

Senior economist Kyle Mangum grew up in exurban Philadelphia, watching developers turn his neighbors' farms into housing subdivisions. This triggered a lifelong interest in how markets work for specific physical locations, how people choose where to locate economic activities, and how locations themselves are priced. After earning his master's and doctorate degrees from Duke University, he taught economics at Georgia State University. Since 2018, he has conducted his economic research at the Philadelphia Fed.

Where did you grow up?

I grew up about an hour outside Philadelphia. It was a farming community when my grandparents lived there—they would come down to Philadelphia and sell their farm goods—but now it's a suburb, and I saw that transition happening. Houses going up. Farms being converted to housing development.

Is that when you became interested in housing market investors?

It made me interested in the spatial organization of land development—and in how that development depends on the way things were in the past. In a community like the one I grew up in, it was easy to convert a barely profitable farm into 500 single-family homes. You can't add 500 homes nearly as easily in Philadelphia.

You majored in economics at Taylor University. What drew you to economics as early as age 18 or 19?

I had two majors: economics and political science. I thought that economics would be a good way to understand how to make good policy. As I got deeper into economics, I thought, these are fun problems. I drifted from policy analysis into economics. But since grad school, I've drifted back into thinking about policy.

In your *American Economic Review* article, "Speculative Fever: Investor Contagion in the Housing Bubble," you suggest that investors are sometimes naïve and prone to error. The profit motive, in other words, does not necessarily induce rational behavior. Does that mean that naïve investors are irrational?

Broadly, "rationality" is a matter of how you collect and synthesize information. You can be rational with a limited information set and make what turns out to be the wrong decision. The paradigm in economics is an agent maximizing an objective, subject to their constraints and their information set. That's criticized as being too robotic, but people do what they think is best. That's true by definition. And their information sets are sometimes limited. I think the "Speculative Fever" article gets to the heart of this issue. People see their close-by neighbors investing in the housing market, and they take that as a signal that this is a good idea. They can end up losing, but at the time, they did not have full and perfect information about the future.

So, what makes an investor naïve?

"Naïve" means you don't have a lot of information and don't know how to acquire it. It doesn't mean you're a bad person. It just means you could do a better job of acquiring information. In a model, we want to distinguish the actors who have more information from those who have less, but in real life it's the behaviors that matter most. You can't observe the information someone has, but you can observe the behaviors, and usually it's the behaviors that impact other people. And that's what policies should care about. So, if someone is naïve but doesn't harm society, then maybe there's no point in restricting their behavior.

What is the best way for a prospective investor to avoid being naïve?

This isn't business advice, it's just my thoughts. Investors should have knowledge of the market or diversification of their portfolio. If you're buying only one house and flipping or renting it, you need a business plan. When something breaks, who's going to fix it? Am I doing renovations myself? If not, how will I contract those out? Some of the frothiness of the housing bubble came from this idea that you don't need to worry about those things. You'll just ride the wave. If there's no business plan for the individual investment, maybe it'll work out. But that's a naïve way of behaving. Some of the more socially undesirable behaviors associated with small-scale investors, like capacity underutilization or market fluctuations, result from a lack of planning by those naïve investors: They're just holding property, keeping it vacant, doing nothing with it, not improving it, just waiting for a market wave to take them to a big payoff at resale. That can work out, but you're not guaranteed. Those investors are taking a big risk, and that can be socially undesirable.