

A Geologist's Eye-View  
of a Current Problem.

The problems concerning foreign capital in Canada has been examined in the press by various authors, but in order to form my own opinion, I constructed a pair of charts to illustrate schematically the path of foreign investment. Using these charts as a basis, I found that the key issues became quite clear and I was able to draw some reasonable conclusions.

- Robert O. Cochrane

ON EXPLOITATION BY FOREIGN CAPITALISTS

Introduction

The subject of foreign investment has become very topical not only in Canada but also in many other countries. Invariably the foreign capitalists are painted as the villains and yet reason dictates that the use of capital (no matter whether foreign or domestic) should confer great benefits on a developing country. To examine this paradox, I constructed the following charts which illustrate the path of foreign investment. The method of land tenure immediately rises to the fore and the charts are based on two cases; 1/ where private ownership of land is permitted, and 2/ where the land is owned by the community and administered by the government.

I must admit that I am a disinterested observer (if ever such a beast existed) and have no special qualifications to discuss this subject. The charts are largely self-explanatory and are the most important part of the article because from them the reader can draw his own conclusions. However, for

most authors (and I am no exception) the opportunity to clutter a good idea with too many English words is irresistible and so a definition of terms, comments on both charts and my own conclusions have been added.

### Definitions

Wealth - "All material things produced by human labour for the satisfaction of human desires, having exchange value."

Land - "The entire universe except man and his products." Rent is that portion of the wealth attributed to the use of land.

Labour - "All human exertion in the production of wealth." Wages are that portion of the wealth attributed to labour.

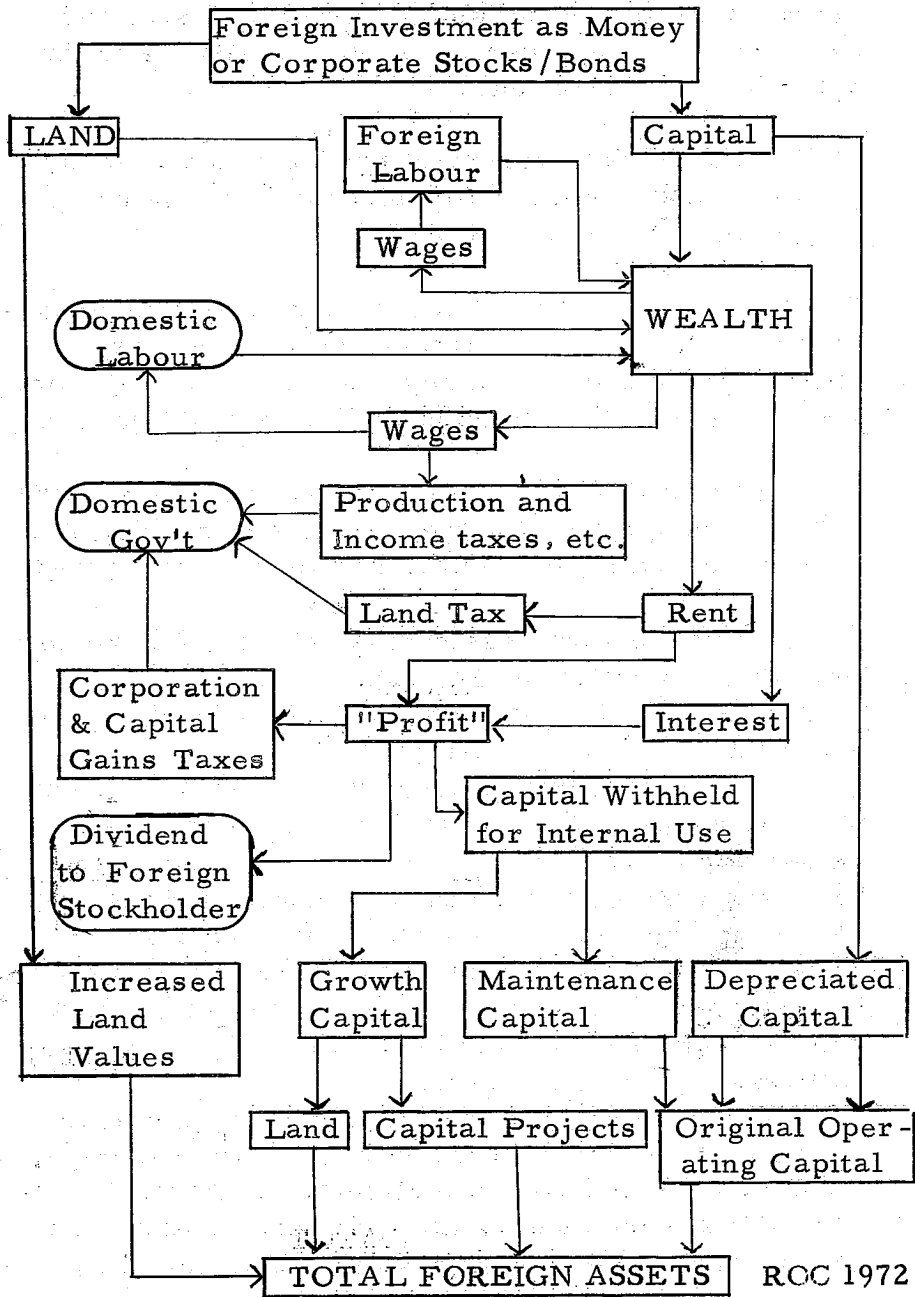
Capital - "Wealth used to produce more wealth." Interest is that portion of the wealth attributed to the use of capital.

### Notes on Figure # 1.

1) A foreign investor will distribute his wealth between land purchases and capital purchases. In a system of private land ownership, domestic land falls effectively into foreign hands as surely as if it was invaded. In fact, by issuing title deeds, the victim gives the invader the right to hold that land.

2) Wages will be distributed between foreign and domestic labour as a function of the necessity of foreign technical expertise and the usefulness of the natives. Only domestic wages are taxable.

Figure #1. Chart illustrating the path of foreign investment in a system of private ownership of land.



3) The ratio of wages/interest will depend on the type of endeavour. For instance an exploration program for oil or gas is highly capital intensive and hence will have a lower wages-to-interest ratio than say a lumber operation.

4) The domestic government has its hands in many pockets but the most easily accessible is the pocket of the domestic wage earner.

5) The economic rent minus the land tax is incorporated into the "profit" of the investor. The word "profit" is deliciously ambiguous and so is appropriate to describe this combination of rent and interest.

6) The "profit" minus the corporate taxes is split to provide the dividend for the foreign stockholder and to provide wealth for capital maintenance and growth.

7) The total foreign assets consist of a good proportion which is not related to capital.

Firstly, a substantial part of the "profit" is actually rent for the use of land.

Secondly, the foreign investor now owns land and will use excess "profits" to buy more land. Land values are more likely to increase than decrease because of the growth of the community and the advancement in technical knowledge and expertise. Thus the "capitalist" receives the benefits of higher land values. Furthermore, speculation on land, a natural feature of private land ownership, will also increase the value of the land.

Because the interest-on-capital is supplemented by the rent-of-land, the rate of return on a foreign investment is usually quite attractive. As well, domestic government usually provides an additional bonus in the form of special exploration permits,

subsidies, etc.

8) The system allows foreign investors to acquire substantial land holdings in a country and with this land, their political power (as well as the influence of a foreign power) increases markedly.

Notes on Figure #2 (next page)

1) Where there is no private ownership of land, foreign wealth can enter the country only as capital and so its political effects are limited.

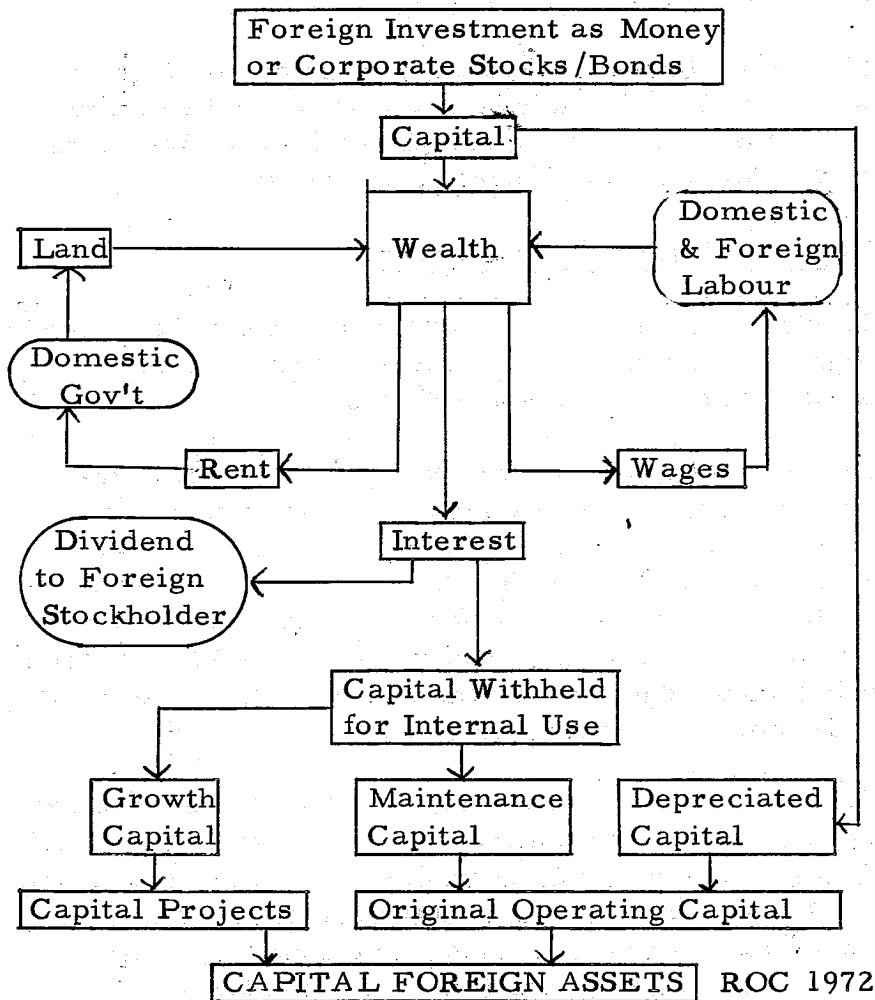
2) The economic rent-of-land goes directly to the coffers of the domestic government to provide services for its citizens. The assessment of the rent is relatively straight-forward and it can be easily collected. The influx of foreign capital will spur the growth of communities and increase the level of technical knowledge; hence, the rent will increase to provide more and better services for the citizens.

3) As the chart is presently arranged the government does not take a cut on the wages. However, it is difficult to conceive of any modern government completely bypassing this lucrative source for financing all sorts of schemes. After all, bureaucracy must be fed! The same applies to corporation taxes.

4) The reward of the foreign investor is the interest. If the interest is not sufficient, he will invest his funds elsewhere.

His political power is restricted. The ownership of capital is not such a politically potent weapon as the ownership of land. More wars and revolutions have been started because of land than because of capital.

Figure #2. Chart illustrating the path of foreign investment in a system of Government Land Leasing.



Because the citizens are not using their wealth to purchase land and because the government will not demand so much of the wages, the developing country can eventually produce its own capital, control its own destiny and is not forever doomed to stand in the shadow.

5) The total foreign assets are limited to the original capital and the earned interest.

6) At present the preservation of the natural environment is a popular topic. As an interesting sidelight, if the domestic government controls the land, it can put restrictive conditions on land use such as landscaping after strip mining. No longer will exploration permits be licenses to rape, plunder, and pollute.

7) The charts illustrate the meaning of the term "exploitation by foreign capitalists." It can be defined as "the appropriation of all or part of the economic rent by the foreign capitalist in addition to his earned interest." The cause of the exploitation is the system of private ownership of land which allows rent (which in principle belongs to the community) to be incorporated into foreign profits and to leave the country.

### Conclusions

In a country with substantial natural resources and a lack of domestic capital, the use of foreign capital can confer a great benefit. The result will be increased production, with higher wages, increasing rent and a higher standard of living. However it must be understood that the investor expects a return for the use of his capital and so part of the wealth will leave the country as interest.

The present system of land tenure fails because it allows a major part of the rent (which belongs to the community) to be incorporated into the profits of the foreign capitalist and hence this wealth also leaves the country. This is true exploitation. The result is that the domestic government must tax the wages of the natives at a high rate in order to provide the necessary services.

The other bonus to the capitalist is the ownership

of land. The land values will increase and so the selling price will be higher than the original price. In addition speculation will artificially increase the value of the land once again as an indirect benefit to the foreign landholder.

Another important consequence of the system is that most of the potential domestic capital is tied up in land holdings.

Politically, one of the greatest threats posed by the combination of private land ownership and substantial foreign investment arises because as more land is acquired by foreign capitalists, their power over the domestic government increases. The exploits of the international majors of the oil industry in South America and in the Middle East provide not a few instances of the subtle use of this power.

The holding of land allows a foreign government to bleed a nation dry by appropriating the rent (like the British in India) and this in turn forces the domestic government to tax the citizens to make up for the lost rent. The system permits an industrial nation to subjugate a developing nation (its supplier of raw materials) as effectively as if it maintained a standing army in that country. The situation is also self-perpetuating because the investor is continually increasing his land holdings, and as long as the natives are appeased (so they don't revolt) the exploitation could last forever and ever. Indeed, the only threat to a foreign investor is the rise of a socialist, a communist, or any revolutionary government which will shake up the system of land tenure.

For a government caught in this situation and unwilling to change the system of land tenure, the

only option is to nationalize (much to the dismay of the international corporations) and even then, this will involve buying back part of their own country (e.g., the current situations in Algeria and Libya).

Historically, foreign ownership of land has given rise to the worst tyrannies because the natives virtually become slaves in their own country subject to the cruelest treatment in order to feed a foreign god. Notably it has bred the violence in Ireland and the widespread poverty in India and Pakistan.

How can the exploitation of the foreign capitalists be prevented? A number of approaches are suggested by figure # 1 and are presented below. However, the only permanent solution which would still provide the benefits of foreign capital as well as eliminate the exploitation is a change in the land tenure system.

1) Foreign investment can be discouraged by government with the resulting decrease in production and a lower standing of living. Are the citizens, even the most ardent and eloquent nationalists prepared to accept the lower standards with increased unemployment, etc. ?

2) Foreign investment can be chosen selectively and directed into those industries where land plays only a small part (I.E. service industries) or into impoverished areas.

Foreign investors are more interested in making money than in performing services. Their capital is usually employed in the exploration and development of natural resources (oil, gas and minerals). They seek primary industries because they are more lucrative (particularly when the rent is included) and

are likely to form domestic holding companies so that they can circumvent government control. An example is the growth of Jersey subsidiaries throughout the world and yet Standard Oil of New Jersey still maintains the controlling interest in each one.

Government occasionally offers incentives to capitalists if they locate in designated parts of the country ("the pockets of poverty"). Industry will use these incentives as long as the "profits" are sufficient. Usually when the incentive program is stopped their operations cease shortly thereafter.

3) Foreign investors could be prohibited from buying land but enforcement of this edict would be impossible. Land would be bought in the name of domestic holding companies and a major portion of the rent would still find its way back to the investor.

4) The other possibility suggested by figure #1 is a special tax on the profits of foreign investment probably in the form of a corporate or capital gains tax.

If this tax is a substantial part of the profit, it will effectively discourage the use of foreign capital. The tax must also be applied to domestic capital for capital has no distinctive national characteristics.

The major problem with a tax on profit is its failure to distinguish between profit mainly due to rent and profit mainly due to interest. For instance, a capital intensive service industry (such as the computer industry) uses a relatively small amount of land, and its profit is mainly interest to which it has every right. On the other hand, a land developer's profit is mainly rent which belongs to the community. Because of this problem, the legislatures find it virtually impossible to formulate a just law to tax profits. A high capital gains tax may curb the

activities of the landholders but drive all the true capitalists into bankruptcy.

A direct appropriation of the rent is the simple solution to the problem but the minds of men are too complex to realize it!

In summary, these four approaches are possible and certainly some of them will be tried by the Canadian government to curb the use of American capital. However, the control of foreign capital will prove to be difficult because domestic capital is also involved and because the citizens may not wish to accept the consequences.

Who is to decide what capital will be beneficial and what will be harmful? With the present land tenure system, all foreign capital involved in primary industry is exploiting the country, but because the government does not seem to appreciate the distinction between rent and interest, the choice can only be based on irrelevant guidelines. Judgement is required, and for every decision, the government will be faced with legitimate criticism no matter what choice is made. Personally, I would feel easier if these decisions were removed as far as possible from the reach of politically-sensitive governments and benevolent and corruptible bureaucrats.

The only effective way to distribute the wealth equitably and to allow the government to extract its share relatively painlessly is to prohibit private ownership of land not only for foreign capitalists but also for the citizens. The capitalist would collect his interest and the community would enjoy the benefits of the rent. Land could no longer be profitably marketed, and because government commands

the full value of the rent, speculation would be curbed. In other words, the situation in figure #1 could be changed to that of figure # 2 by making the land tax equal to the rent. The increase in government revenue from the rent would permit a reduction in the tax on wages. @@

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