

of the expansion, and the secondary mortgage market makes bankers and mortgage brokers loosen lending standards to keep rolling over loans that get sold.

Eventually, land prices rise so high that entrepreneurs who seek sites for investment decide that the real estate and interest-rate costs are too high. As expected profits fall, investment slows down and then stops growing. Investment drives the business cycle, and when investment falls, workers in those fields lose their jobs, and their demands for goods fall, and the whole economy then tumbles into recession. Foreclosures rise even more, and the financial system crashes as banks and other financial institutions become insolvent.

The engine of this perverse cycle is real estate speculation, and the only way to stop it from happening is to take the steam out of it by tapping the rent and land value for public revenue. If most of the rent is tapped for public revenue, there is no profit in speculating on land. Real estate would only be held for actual use or to rent to others for use, not for land-value gains. The land value will be small and not rise if most of the rent is collected for public revenue.

The secondary mortgage market would not be so perverse if most of real estate mortgages were made to purchase buildings rather than land. However, to eliminate distortions in the mortgage market, government guarantees should be phased out. Folks will find real estate much more affordable if they only need to borrow to buy the building and not also for a high land price.

The monetary intervention can be remedied by shifting from central banking to free-market banking, where the money supply is determined by the public demand to hold money rather than by a monetary authority. The supply of governmental currency would be frozen and would serve as a money base like gold did in the old days. Private bank notes would be convertible into government currency, preventing inflation.

The interest rate would then be able to do its job, to equilibrate savings and investment. There would be no more manipulation of interest rates to either stimulate or put a brake on the economy. Without the real estate cycle, there would be no business cycle, and the economy would not recede, and thus not need any monetary stimulus. With no more inflation, the economy would be free to grow as fast as folks want. And with no tax on wages or investment, growth could well be dazzling, limited only by the supply of labour as wages rise and poverty becomes extirpated - pulled out by the roots.

Since such policy changes are not forthcoming, we are unfortunately riding

the economic river to a financial waterfall, a recession and depression. The timing of the real estate cycle has been quite accurately predicted by those familiar with the past pattern. Real estate construction and prices have peaked consistently shortly before the major depressions, with an average period of 18 years. The last real estate recession was in 1990 in the us, so adding 18 years puts the next recession at 2008. Of course sometimes the interval is a bit more or less than 18 years. But it is striking that in 2007 real estate prices in the us were already falling, and the mortgage problem got ugly.

This time around, the real estate boom has been global. The global economy has linked together the economies of the world like never before. While real estate markets still have local variances, the financial markets have tied economies together, and real estate has boomed world-wide with few exceptions. Moreover, fiscal policy is fundamentally similar world-wide, as real estate is explicitly or implicitly subsidised. Such policies stem from quite similar political structures, including rent seeking by special interests.

As the us enters a recession, having been the world's biggest importer, other economies will recede also as sales fall and as their real estate markets also peak out - if they have not already done so. The bigger the boom, the greater the fall, and as this has been the biggest global real estate boom in history, the consequent economic fall will be proportionate.

Crises have one consolation. They provide an opportunity for reflection and a climate for major shifts in policy. Perhaps this time policy makers will see the fundamental causes of the boom-bust cycle - and popular opinion will open to a big shift in monetary and tax policies. Reformers need to be ready to step in and offer the twin remedies - free banking and land-value taxation. **L&L**

*Dr Fred Foldvary teaches economics at Santa Clara University, California, and is a research fellow at The Independent Institute. He is also a commentator and senior editor for the online journal The Progress Report and an associate editor of the online journal Econ Journal Watch. His books include The Soul of Liberty, Dictionary of Free-Market Economics, and The Depression of 2008.*

## good idea bad idea

THIS ISSUE: TAX IN THE UK

### GOOD IDEA ?

According to the UK Pre-Budget Report published in October, "from 1 November 2009, the Government proposes to replace Air Passenger Duty with a duty payable per plane rather than per passenger". Responding to 'Charging for Landing' in our last issue, **L&L** reader Conal Boyle, from Port Talbot in Wales is enthusiastic about the proposal. He writes - "If it's done the right way, this could be a form of land value taxation. Should reformers get involved in these discussions? I hope we can take this forward."

### BAD IDEA ?

The new Scottish Nationalist government has set off down the road of institutionalising modern-day landed privilege. Its 'new' fiscal ethos was set out by Finance Minister John Swinney in his first budget, presented to the Parliament in November. The Nationalists will introduce a new additional tax on earned income, penalising effort, and will abolish Council Tax - the tax on unearned income - the only periodic public charge on publicly created location values. Oh dear Mr Swinney - don't you know the way of the 21<sup>st</sup> century is to "pay for what you take, not what you make"?

What do you think? What good ideas are you hearing aired in public debate - and what bad ones? Let us know. [ideas@LandandLiberty.net](mailto:ideas@LandandLiberty.net)

## Mr Greenspan's

Alan Greenspan was chairman of the US Federal Reserve from 1987 until last year. **Michael Hudson** considers the

IN 1966 I was designated to fire Alan Greenspan. I was Chase Manhattan Bank's balance-of-payments economist at the time, and was writing a study of the balance of payments of the US petroleum industry. Chase and the Socony Oil Company each had paid \$10,000 to finance the study, and Socony had insisted on bringing in Mr Greenspan. My boss in the Economic Research Department, John Deaver, worried that Greenspan was so eager to get business by giving the client what it wanted, that few people had much confidence in his statistics.

Greenspan was supposed to be producing statistics on us oil company capital investment. What he was actually doing was coming up with rough approximations of us figures - basing them on total worldwide investment. He told his statistical assistants to assume proportionality. One of them - Lucille Wu - told me "it's all implicit". By 'implicit' she meant they were to assume that European and Near Eastern depreciation rates and other tax laws were identical to us laws. But this was obviously not the case.

One day Mr Deaver and I were invited up to David Rockefeller's dining room. Mr Rockefeller - Chase's President - told me to inform Mr Greenspan that unless he could provide specifically us figures, and/or be forthright about his assumptions, we would have to leave his contribution out of the study. (I remember Socony's representative was a friend of his, and I think they made sure he got paid as their favorite business lobbyist *du jour*.)

Mr Greenspan was an economic lobbyist for the rich - for large corporations and for Wall Street. That is the job of a Federal Reserve chairman these days. Like a good criminal defense lawyer or the 'expert witnesses' they hire, a good lobbyist makes a cover story believable. Mr Greenspan crafted a myth that many people wanted to believe. The myth was that people (just about everyone) could get rich by going into debt, to buy property whose

prices were being inflated by monetary policies - policies of loose money and the deregulation of the financial system in a period of 'wild financial speculation'.

Mr Greenspan sponsored a study that said that increasing asset prices was 'wealth formation'. It was a myth that Adam Smith called 'wealth of Nations'. Posing as a reformer, Greenspan tried to make a particular kind of inflation seem like a good thing.

The distinguishing feature of the price inflation - the bubble economy - was the price of property rising. This put the class war by another name. This time a class war by another name. This time a class war by another name. This time a class war by another name. This time a class war by another name.

As the most vocal critic of the Bubble Economy, Mr Greenspan was responsible than anyone else for the us economy with a negative equity in his own home. In the first time in history, people could get rich by borrowing. Property were rising in price. The Bubble Economy made America love inflation.

The myth that he created should treat their houses as investments. But borrowing is *not* like a bank account. It leaves a debt that must be repaid. And wages and stocks may go down. The Federal Reserve's interest rates enabled a bubble - personally and nationally. Payments, and even gifts, where banks agreed to interest, is what Hymans called 'Ponzi phase' of the credit cycle. Greenspan's main