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CRASH

There is growing realisation that the latest economic figures, stripped of the spin and interpretation applied to boost trust and protect interests, reveal a fast approaching economic storm which will bring the first global housing market crash.

An increasing number of mainstream analysts, commentators and advisers are seeming to see the true nature of the trouble coming. But no-one wants to scare the horses.

The evidence is mounting of the way things will go. Still public statements are dubious. Order of the day is business-as-usual PR swagger, presented for market confidence, coupled with straight-talking warnings delivered *sub voce* in the small print. The US and Europe are at the sharp end of events.

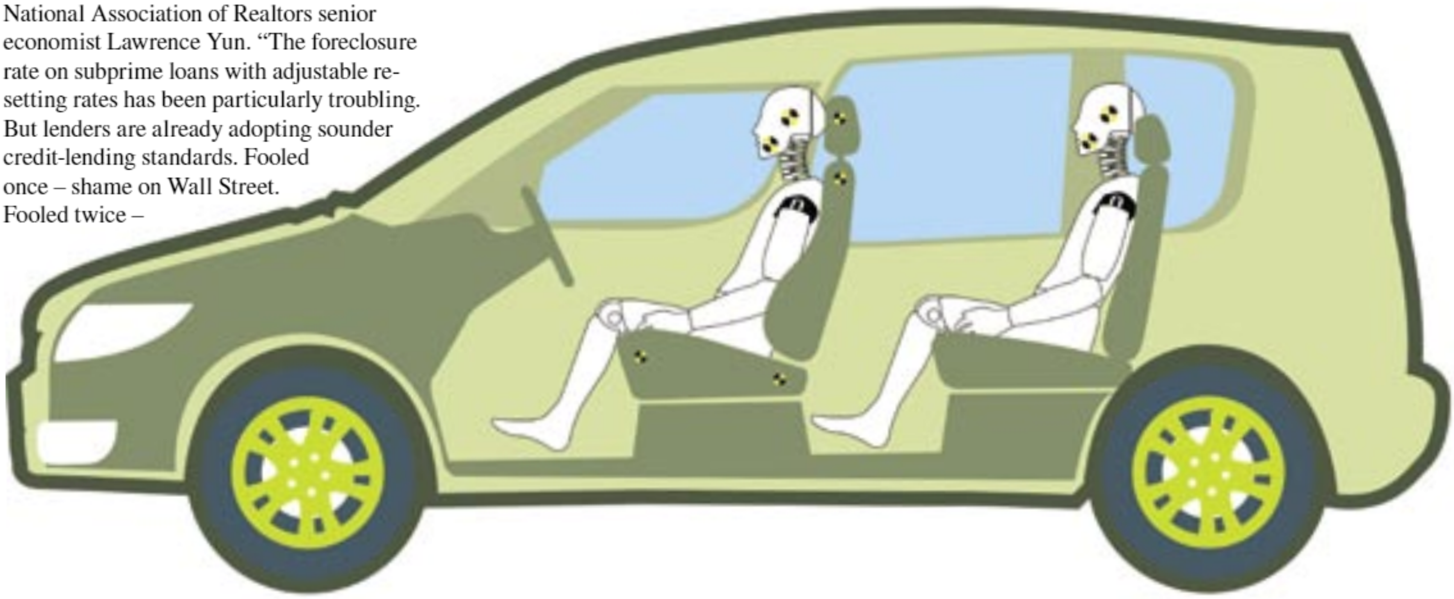
In the US "rising delinquency and foreclosure rates are big concerns" says National Association of Realtors senior economist Lawrence Yun. "The foreclosure rate on subprime loans with adjustable re-setting rates has been particularly troubling. But lenders are already adopting sounder credit-lending standards. Fooled once – shame on Wall Street. Fooled twice – shame on Capitalism. Where money is involved, mistakes do not get repeated." It's a case of "lesson learned" says Yun. So, with 'sub-prime borrowers', it's another day, another fall guy.

Price trends are actually "encouraging", according to Yun, yet the small print in NAR's latest *Housing and Economic Indicators* recommend a "sharp cutback" in housebuilding.

In Europe dubiety is perhaps less prevalent. In the *FT* Ralph Atkins and Ivar Simensen have reported new Eurozone house price forecasts from Barclays Capital. "The latest data suggest that the European Central Bank may have underestimated the extent of the housing market slowdown, as well as its implications for future economic growth and interest rate decisions."

And back in the US some are being even more straightforward. Investment U, for instance, have had a change of heart since last year, when they said "real estate is still a good long-term investment". They're not saying that just now. "Personally, instead of taking equity out of my house to buy more properties, I'm doing exactly the opposite", says Dr. Steve Sjuggerud, adviser to the investment network. "I'm not interested in looking at any US housing property, period. It may sound crazy to you, but I'm comfortable with it. I'll have a pile of cash available to buy up the bargains when prices are cheap and landowners are ready to just get out."

The world's first-ever global housing crash will hit in 2008 and unfold to its worst in 2010. Some commentators are saying it could all have been avoided. But we're all now just sitting waiting for it to happen. Around the world forecasters are dropping talk of a "soft landing".



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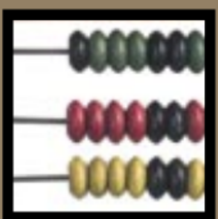

does democracy require land value data?

privilege and a protected free market

1219 vol 114 AUTUMN 2007

Arctic landrush

Lovely spot for an oil rig

Following in the footsteps of Cook and Peary, a race for geological information is being run between scientists from Russia, Canada, Denmark and the US. The four nations are all forcing scientific excursions north of the Bering Strait – not competing for the right to issue Father Christmas stamps, but in order to claim the geological riches under the ice cap. On the 2nd of August the Russians planted a flag on the North Pole in order to lay a claim to its gas and oil reserves. The Americans are understood to be in hot pursuit. Canada and Denmark are also making claims, based on the line of an obscure underwater ridge, and the geological subtleties of whether Greenland is in fact linked to the North Pole.

By 2014 the UN will be looking at the scientific evidence gathered by the various national expeditions. Ultimately it is the UN's International Court of Justice in The Hague that could decide who gets to sit on top of the world.

The great haul of China

China's crazy real estate boom has led to an escalation of illegal land grabs, chiefly administered by local Communist Party officials. Of the 14,700 hectares of land illegally appropriated in the first four months of 2007, a staggering 80% was stolen by local government bodies, and in many cases given to friends and business partners of Party officials. In a system that is rife with corruption, only the small fish are punished, says Li Yafang, a standing member of the Chinese People's Political Consultative Conference. "The more powerful officials were 'overlooked', and that has led to more land grabbing" he told *Asia Times*. [*The last issue of* **L&L** *reported China's forthcoming Real Rights Law, which will establish a unified system of private property and a land-use rights scheme. Ed*].

Greek landlords linked to arsonists

There is mounting evidence that this summer's epidemic of forest fires ravaging Greece has been an extreme consequence of a well-known local problem: developers, dissatisfied with local planning decisions, turning arsonist. Land razed of protected forestry might find development consent more easily.

The government has offered up to €1m in reward for information leading to arrest. Tragically, there may be murder charges. The state has a poor record of dealing with such arsonists.

The obscurity of political strategy

Scottish Parliament, Edinburgh. June 21, 2007, 17.04. Abstentions: Harper, Robin (Lothians) (Green), Harvie, Patrick (Glasgow) (Green).

The Presiding Officer: "It has gone very quiet all of a sudden. The result of the division is: For 64, Against 62, Abstentions 2. Motion, as amended, agreed to. Resolved, that the Parliament believes that local income tax, which is based on ability to pay, is a fairer system of local taxation than the discredited and unfair council tax and notes the position of the Green Party in regard to land value taxation."

Brian Hodgson

Brian Hodgson, chair of the Labour Land Campaign and former Labour group leader on Oxfordshire County Council, has died from a heart attack after a short illness. From 2001 Hodgson was the political driver of the Oxfordshire land value taxation trial project.

Friend and colleague Dave Wetzel, President of the Labour Land Campaign, said that Hodgson "will be sadly missed, not only because of his immense contribution to socialism and the land tax campaign but because of his humour, his honesty and also because he was a smashing bloke."

Sunshine estate

Florida's land preservation programme is running out of money. The funds allocated were supposed to last until 2010. "But the state's wallet is empty", says programme director Keith Fountain to *St Petersburg Times*. The land is turning out to be too expensive to buy.

Property tax goulash

The 386 members of the Hungarian parliament, the Országgyülés, will be voting this autumn on a number of bills prepared by the Finance Ministry. Perhaps the most significant of these is the introduction of a general property tax which will combine a number of existing taxes on land and property. The reform is not intended to bring in any greater revenue than the €¼b brought in by the current taxes – around 1% of government revenues.

Finance Minister János Veres said to the daily paper *Napi Gazdaság* that there is still a lot to do to meet the provisions of the contract between Veres' Socialist Party and its coalition partner, The Free Democrats. The nature of the proposed property tax is still undecided. Indeed, the lawmaking schedule does not yet mention the property tax by name.

Miklós Tátrai, Secretary of State at the Finance Ministry, said the property tax – which will be strictly value-based – would be levied by local governments using a unified methodology. However, it would be the task of local governments to decide on tax rates, allowances and exemptions.

The law is expected to take effect from 2008, but the actual reforms will not be introduced until 2009.

After a mid-nineties economic recession, Hungary's government has concentrated on a number of reforms of the tax system, public services and local government finance. These have had the overall goal of preparing the country for its entry into the European Union, and the possibility of joining the Eurozone sometime between 2010 and 2014.

Historicallly, between 1848 (when serfdom was abolished) and the Communist takeover a hundred years later, a great number of land reform schemes were proposed and implemented. Most adhered to Marxist doctrine. But there was also a strong contingent of land reformers influenced by the American economist Henry George. The leaders of the 1918 republican revolution included land value taxation in their programme, but the counter revolution a year later abolished their reforms.

The Országgyűlés will be voting on tax

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letter from the editor

"Fooled once – shame on Wall Street. Fooled twice - shame on Capitalism. Where money is involved, mistakes do not get repeated." So says Lawrence Yun in our cover story.

But what is happening in the global economy is not happening because of 'mistakes'. The subject and nature of the 'fooling' are not as Yun assumes. In his error Yun stands side by side with the majority of his conventionally-thinking mainstream economist colleagues. Their profession, and its collective failure to exercise its work for the science that it should be, has brought the world to the lamentable point at which it now finds itself.

We are about to experience the violently painful and now unavoidable outcome of running our economies as we do. This crash will not be a 'fool's' 'mistake'. It will be an intended feature, a design, of our chosen set of economic rules. The pain and the suffering are part of the system: the violence is in the system: the crash will be the inevitable consequence and a necessary component of the West's prevailing macro economic and fiscal policy orthodoxy.

But be in no doubt, some – certainly most of the powerful and wealthy – will do not so badly out of the impending chaos. The losers will be the more ordinary folk: families will lose their homes; hard workers will lose their jobs; worthy enterprises will go under; good reputations will be darkened; pensions and savings will evaporate; inheritances will vanish. The whole cycle will repeat.

This is not how it should be.

In this very place, three years ago, in our summer 2004 issue, we brought readers' attention to the cutting-edge work of reformers. We stand by the conclusions we came to back then. The first global housing crash will hit in 2008 and unfold to its worst in 2010. We have at least two years of economic hell in front of us.

We cannot avoid it now. If there is not a 'major readjustment' of the market, dumping a massive portion of its value, and trashing homeowners' assets – how would ordinary families without property inheritances ever be able to afford their own homes? – what would happen to future levels of tax receipts, considering the increasing portion of national 'wealth' deriving from the unearned gains in the housing market – universally lightly taxed?

Of course the global nature of this crash does not mean a universal market outcome for all players everywhere. Instead, simply, it will be one that is globally-linked: the usual regional re-balancing of locational resource value will occur, as usual at this point in the cycle, but it will happen on a planetary level. As the impact of the crash destroys values in Western markets, some part of those values will re-manifest themselves in land value gains in the emerging new superpowers of India, China and elsewhere. Soon Chinese and Indians will be sitting down to enjoy land value gains which were the subject of a decade's dinner party table-chatter back West.

We should pity the property-rich Western homeowners relying on their property assets for their pensions. But, first time buyers, rejoice. Your time is nigh.

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Counting the land

The running of a country relies on having to-hand the right sort of information. **Duncan Elliott** argues that on that score the UK government is working in the dark.

Way back in the early summer of this year, Britain found itself with a new Prime Minister, Gordon Brown, and a new cabinet. Alistair Darling was assigned the tough job of replacing Brown as Chancellor of the Exchequer. Brown had enjoyed a fairly sustained period of relative prosperity while in charge of the purse strings. But how will Darling fare under the leadership of someone who spent such a long and arguably successful time as Chancellor? Darling, as with his predecessors in the post, will to some extent be able to perform only as well as the information with which he is provided allows him. It is this information and the advice he receives based on it that should inform his decisions.

Society and the economy are analysed in many ways and by many interests – government departments, independent policy groups, academics and so on. The decisions that are taken as a result impact upon the economy, society and the environment. Decision making in some quarters has a greater impact on more people than in others. From this perspective, and in terms of running the country, two important public sector institutions whose work has a direct impact on people in the United Kingdom are the Treasury and the Bank of England. Whilst the Bank of England is officially independent of government, ultimately it has tasks set by the Chancellor. This contributes to the importance of the Chancellor's role in terms of running the country.

Clearly we need information to make decisions. There is an untold amount of information to aid decision makers, generated across all sectors of the economy. But it's not just the quantity of information which is important: in fact, it is often said that we suffer from information overload. It is above all the *quality* of the information which is key. We must ensure that it is fit for purpose.

The focus of this article is the issue of what data and information is required to run the country. My purpose here is to highlight a glaring omission. It is one that needs to be addressed if the country is to be run effectively for the common good. This is not to say, of course, that if this information was available, the country would automatically be run well. We would still rely on the right decisions being made. Nevertheless, without the right sorts of information it is unlikely that good decisions can be made at all.

Statistics are an important source of information. They are used and abused to support different theories, to criticise arguments and, importantly, to inform decisions. Statistics are also integral to the different models used to understand the economy, for instance by the Treasury and the Bank of England.

> **“a vital source of information for running the country is currently missing”**

For example, the retail price index, one measure of inflation, is used by government to index pensions, state benefits and index linked gilts. A slight rise in inflation may trigger a decision to increase interest rates. Deviations in the economic cycle might result in fiscal policy decisions designed to get the economy back on track. In both instances information is key to trying to deal with expectations in order to steer the economy on the apparently right course.

There's a lot of data available, and while there is often concern over its quality, on the whole the government has a massive body of useful information to aid its decisions.

All sorts of models are constructed to understand what is happening in the economy and the implications for policy. However, let us turn to a very simple economic theory of the production function: the theory includes three factors of production: land, labour and capital. Often economists omit land (or at least fail to distinguish it separately from capital) – perhaps to simplify the issue. Yet natural resources and man-made capital function differently in economic terms. This common omission should give a clue as to part of the problem with much of what is currently done.

We can ask two key questions. First: are the models that are being used sufficient for understanding the economy as a whole – can they be used as one of the tools required to run the country? Second: are the indicators that are currently used to analyse the economy fit for purpose – do they provide the correct information for the assumptions which underlie whatever model is being used?

The Treasury and Bank of England are generally looking at the economy at the macroeconomic level. But if we consider this is simply an aggregation of the microeconomic level, how then do things measure up against our most basic of economic models? If we look at what is analysed by the Treasury and the Bank of England, there is a big focus on capital, in terms of productivity and prices, and perhaps a slightly lesser focus on an analysis of labour, in terms of wages and employment.

To understand the economy as a whole one requires information on the whole economy. In this respect data on land is the glaring omission. On one level then, the answer to the first key question is that the models used – for even basic analysis of data – are not sufficient for understanding the economy as a whole.

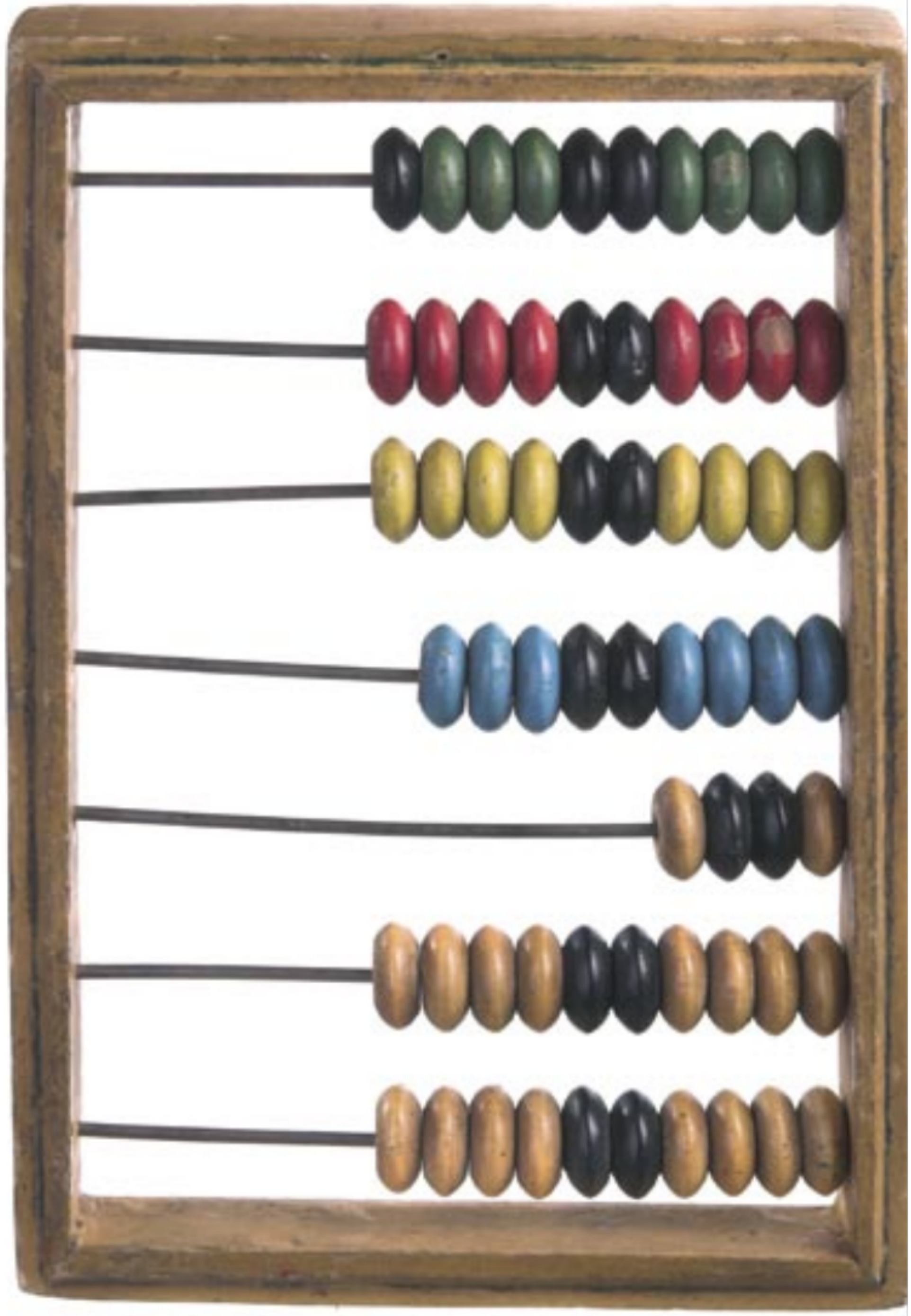
What about house prices, as a measure of land value? The Treasury in their summary overview of the economy publish movements in the Halifax house price index; the Bank of England uses a number of housing market related data from different sources, including the Halifax, the Home Builders Federation, the Nationwide and the Royal Institution of Chartered Surveyors. Here the two questions posed above are relevant. First, is sufficient weight given to this data in terms of understanding what is going on in the economy,

> A recent overview of the economy published by the National Institute of Economic and Social Research suggests that insufficient attention has been paid to house prices over the past few decades. Since 1987 the total return on housing is estimated conservatively at 7% per annum in real terms, on which tax does not need to be paid. This is higher than the return on other assets upon which tax in general must be paid. One problem with this is that it is effectively borrowing on a large scale from future generations. So whilst the government sets targets with respect to its own borrowing (below 40% of GDP) it completely ignores the borrowing that is resulting from the returns on housing. While in the short term increasing house prices don't seem to be a problem, in the longer term they certainly are.

and second, are these indicators fit for purpose?

There have been significant rises in UK house prices in the past two decades. If saving is replaced by investment in housing this can cause a problem in terms of diverting resources from capital stock. Hence it creates a problem for the economy in the longer term. How can this problem be highlighted? Increases in house prices are generally not due to increased wages for labour or prices for materials required for housebuilding. Those have indeed increased, but by nowhere near the rate that house prices have. So an important issue is that in terms of data currently used to analyse the economy there is no separation of capital and land value in terms of assets.

This means that in the data currently used, it is not possible for advisers and decision makers to distinguish clearly between productive returns to investment – such as making improvements to a house – and the returns from rising (or falling) land values. (In terms of economic theory, such land value returns are known as economic rent or unearned income). In other words the data are not really fit for purpose. It is important to distinguish land value with separate information.



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While there are some sources of basic land value data, such as the Valuation Office in England and Wales and the Registers of Scotland, these are not detailed enough to properly analyse what is going on in terms of the whole economy. Therefore a vital source of information for running the country is currently missing. The lack of detailed land value data also poses problems for the correct estimation of capital stock. This means that the quality of important national statistics such as GDP is likely impaired by the fact that there is not a proper understanding of what portion of income is economic rent.

Finally, the example given *(see box)* of the study by the National Institute of Economic and Social Research, estimating the return on housing since 1987 as around 7% per annum – if given a sufficiently detailed regional breakdown of data – could have shown the big differences between (and even disparities within) regions. However, such data is not available.

More and more information is available in terms of statistics for particular regions within the UK. These include regional estimates of GDP, and a variety of Neighbourhood Statistics. But, for the same reasons as at the national level (ie understanding the regional economy as a whole, and improving the quality of other data), there is a clear need to plug the hole that exists in terms of measuring the value of the land. This information is also essential because understanding social and economic regional disparities is necessary for focussing productive investment.

While the practical aspects of getting this data is beyond the limits of this article, there is clearly a need for such data to be available.

We can draw two main conclusions. First, that there is a need for land value data. Second, that it is essential to stress the importance of land value data. The challenge is to start collecting and analysing data on land value. It is required by those who run the country. It is also required by those who want to analyse and critique the running of the country in order to more fully comprehend the impact of policies and the socio-economic situation of society. **L&L**

Duncan Elliott is an economist with the UK Office for National Statistics, based in Wales.

The effect of privilege

In part two in this series **Ole Lefman** tallies the good and bad effects of privileges, including their contribution to the protection of trade freedom

The story so far…

All sorts of privileges are allowed in Western societies. They can be categorised broadly as privileges granted because of the need for regulation of certain activities, so-called privileges that in fact are rewards for service and should be honoured by wages, and 'intellectual property rights'. Privileges can have real value, which people are willing to pay for. Those values are an element of what economists call economic rent.

(L&L spring 2007)

The existence of privilege in society has many effects, some of which are good and some bad. A main area of their influence is how business and trade can be conducted. The balance of their effects is the consequence of the efforts of the power-brokers in society.

In most modern societies exclusive rights or entitlements are enjoyed over many things. A clear and strong philosophical defence can be made for exclusive rights to manmade property. No privilege is involved or invoked in such rights. The effects of those exclusive rights are reckoned to be good. Privileges – exclusive entitlements – must be invoked in all other situations. Sometimes, privileges are granted *to use or dispose of land* or other natural advantage.

Some places are rich in the resources that human beings need for their survival and comfort. Some locations provide advantages strongly sought after by human beings. Other areas are poor in resources: they may provide only little or no advantages to those who occupy them. In primitive societies the more sought-after areas will be occupied by the more powerful individuals and groups, who then exclude those who are less powerful.

In organised societies the government by its supreme authority makes and enforces the rules and laws which govern the territory. Government guarantees exclusive entitlement to use and dispose of lands or the resources they contain, to those who are able to pay the highest tributes – in exchange for an annual rent or a once-and-for-all lump sum. This is a country's system of land tenure.

Advantages available on or beyond the tide line – at sea level or under or above it – are dealt with in the same way. In recent decades other resources such as positions in space, and the radio spectrum have been dealt with similarly.

Advanced societies need such rules. Without exclusive entitlement to the use of land and other natural advantages,

Privilege

A privilege — etymologically 'private law' or law relating to a specific individual — is a special entitlement or immunity granted by a government or other authority to an individual or a restricted group, either by birth or on a conditional basis. A privilege can be revoked in some cases. In modern democracies, a 'privilege' is conditional and granted only after birth. By contrast, a 'right' is inherent, irrevocable and held by all humanity or all citizens from birth.

Wikipedia.org

competition between human beings who want to use natural resources could turn into social unrest. But even if people restrained from violence, the absence of security of tenure would make modern production and commerce near impossible: without security people would not be as confident to initiate development fixed by location – such as the erection of buildings, fixing of plant, installation of infrastructure, or the cultivation of longer-term crops.

Society has a common interest in the best possible use of the advantages provided by nature and society. So these exclusive entitlements – which are privileges – are reckoned generally as being of good effect.

Sometimes privileges are granted *for the purpose of regulation and control.*

In order to safely, efficiently and equitably manage certain activities, substances or processes, the government may wish to regulate by general prohibition. By issuing licences which privilege identified parties, these things can be dealt with according to rules and regulations given and controlled by government.

The subject of such privileges might include things like polluting processes, nuclear activity, genetic modification, certain sorts of scientific research; trade in medical drugs, explosives, weapons, dangerous products and services; handling of waste water, rubbish, disposal of corpses; exertion of physical power within and beyond the realm; and putting money into circulation.

Without such restricted privileges the alternatives would be either total prohibition – meaning nobody taking advantage of the possibilities in question – or unrestricted and unlicenced free activity – uncontrolled handling of waste water, rubbish and dead bodies, and the uncontrolled exertion of power.

The effect of allowing privileges granted for the purpose of regulation and control is reckoned generally to be good.

Some privileges are granted *as rewards* for meritorious services.

The government may give privileges to people who have served it or the people. These privileges may give their holders advantages over their competitors who then suffer from the privileges. The privilege holders would find the effect of this to be in their own interests – so for them a good effect.

Without exclusive entitlements granted as rewards for services, the government would have to pay money. The government that saves expense by pushing the cost of such rewards on to future governments may consider this a good effect. Future governments may find the effects bad. People in general may find that postponement of expenses to be a good effect. But in general the good effect would actually be very limited.

Some privileges are granted as what are known as *'intellectual property rights'.*

Creators of 'intellectual property' can enjoy protection over their work. Inventors, composers, artists, writers, designers and other such people may have copyright over or apply for a patent to the product they have brought forward. Patents are privileges meant to enable the inventor to receive commercial reward in proportion to the value of the advantages that their inventions have provided for the public.

Without doubt the beneficiaries of intellectual property rights enjoy their good effects. But it is unclear whether denying these rights would hamper the development of creative output, and whether the effects of intellectual property rights are in fact good for society at large.

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But the institution of privilege can also have bad effects.

One bad effect of privileges relates to *competition.* The enjoyment of a productive monopoly or the holding of a privilege can confer a commercial edge over competitors, or can hamper competitors' endeavours to compete. Both these benefits are appreciated by the privilege holder. But their consequence is that goods and services are produced in smaller quantities, in inferior qualities and at increased prices – with excess profits on top of what the monopolists and privilege holders would have been content with, had they not held their privileges.

Monopolists and holders of privileges may find competition-checking effects to be good – but for society at large they will be bad effects.

Another bad effect is *exclusion.* Monopolists and privilege holders, whether productive or non-productive, exclude others from some advantage of nature or society; exclude producers from production; and prevent citizens from enjoying life to the full. The result of such exclusion is that the demand for access to the advantages of nature and society increases – and consequently that the price of access increases. It also means that there are fewer products for sale, and fewer homes for sale or rent – and therefore also increased prices for these things.

Furthermore, an effect of increased prices caused by exclusion by non-productive monopolists and privilege holders is that employees may have to accept living farther from their places of work. This wastes time and money on commuting, uses fuel unnecessarily, contributes to pollution of the environment and adds to congestion. Extended distance between the home and work is reckoned to be a bad effect too.

Both the exclusion of people from areas where jobs could be created, and the exclusion of people from areas for homes near their jobs, mean a waste of resources and possibilities.

Increased prices of goods, services and homes may be appreciated by the sellers, but society at large will reckon them to be bad effects.

Similarly with unemployment: its effect of lowering wages will be appreciated by employers, but generally it is reckoned as a bad effect.

A third bad effect of privileges can be to enable some *to accumulate wealth from unearned income.*

Though some privileges are without exchange value, other privileges and monopolies can be extremely valuable. Valuable privileges can have several consequences:

- They can build up fortunes to a few persons. Using their excess-profits or windfall-profits as purchasing power, they take out products and services from the market without supplying to the market in reciprocation. This practice leaves a reduced quantity of goods and services for unprivileged and under-privileged citizens to choose from, and those at increased prices.
- They deprive the government of the income it creates by using governmental power to protect private monopolies and privileges. This makes it necessary for the government to collect from the producers (through the tax system) the revenue it needs for the administration of society and for the provision of public services and infrastructure.
- They cause a deadweight on production. The effect of taxes on production and consumption is that demand and supply cannot meet at prices for optimal production; fewer consumers will accept the higher prices and fewer producers will accept the lower income, meaning reduced production and trade, and reduced employment.
- They create poverty among unprivileged and under-privileged citizens who do not receive big salaries or profits for supplying specialised services or goods – whether to the government or to the wealthy holders of monopolies and privileges, and their supporters.
- They increase the gap between rich and poor people. This can destabilise society. It creates a class of very satisfied wealthy citizens living lavishly, a satisfied middle class, and a growing class of very unsatisfied, insecure and alienated citizens who have to accept low wages for their work, or the alternative of unemployment.
- They destroy self-confidence and self-respect among people who are deprived of their equal share of the value of nature and society; they are denied free access to nature and the advantages of society without compensation; they are obliged to accept unfair working conditions and low wages; they have to accept dwellings in disadvantageous locations; and they have to put up with their landlords' inefficient

administration and careless maintenance of their premises.

• In the longer term they sweep our civilisation back to barbarism. This is what happened to Rome and the other ancient civilisations. The felling of great civilisations – sometimes catalysed by natural events – is invariably the result of power and wealth concentrated within a select privileged class of citizenry – leaving the multitudes without possibility to provide or fend for themselves, dependent on private charity or social support.

While some of these effects of the holding of a valuable privilege or monopoly may be positive to the interests of those who hold them, society at large will reckon them all for bad effects.

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The effects of privileges – good or bad – are all the result of the exercise of power in society. The use of power may be protective, which in general will be a positive thing; or it may be aggressive, which is usually reckoned to be uncivilised and reprehensible. Sometimes the use of power is protective to some people, but aggressive against others.

When power is used by aggressors they usually make big efforts to describe it as protection. So, when we hear about protection it might in fact be aggression. This is particularly so when speaking about trade. 'Protectionism' may be a blessing to some people, but may at the same time be a curse to others. Trade is a major beneficiary of privilege in society.

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In an ideal market, equal actors would exchange their goods and services without problems, satisfying all parties in the market by the provision of economic advantages to them all. However, in reality, without powerful regulation and protection of the market, the conditions of deals would be determined by whoever exerted the strongest physical power. This would often mean the downright capture of goods, or threats which would discourage suppliers from joining the market.

Early in history, rulers and local governments understood that by using power to keep piracy and bullying dealers away from the market, trade would be conducted much more freely. Everyone's profits would be increased over what they would have been without protection. Protected market places became so successful that traders agreed to pay to the protector a fee out of the profit they could make, which made free market protection a lucrative business for all parties.

It would have been a great advantage for all citizens had these experiences from local market places been copied onto the world market of daily trade and industry. But that is not what happened. Some of the players on the international stage are still able to enjoy protection of their individual trades or industries in the form of tariffs and taxes on others' goods, or privileges and monopolies (*see* L&L 1217).

The most common understanding of 'free trade' is of it simply being a market without any governmental regulation, restrictions or taxation. This idea became widespread in the closing phases of the mercantilist period in the 18th century. Mercantilism urged that a nation should maximise export of domestic products, and minimise the import of other countries' products. That policy was based on the idea that a large quantity of precious metal, gold and silver, received in exchange for export, proved economic success and political strength (strong armies being paid in gold and silver). However mercantilism proved to be a fiasco, creating international tensions and aggressions.

It was followed by the idea of liberalism, including the liberation of international trade by the gradual reduction and final abolition of custom tariffs, taxes and restrictions on international trade.

Originally this free trade policy only applied to international trade; but some liberals also urged for abolition of government regulations in domestic trade and industry. It was this post-mercantile understanding of free trade that spread over Europe and the USA during the 19th century. During the same period, socialists and communists garnered supporters from the suppressed working class. They raged out against free trade and made it their prime argument for unification of workers in trades unions and political parties. Many suppressed working class people had experienced free competition as a very destructive power. They found that it urged workers to compete against each other, forcing them to accept employers' unfair conditions of labour – often extremely risky and unhealthy work at low wages. Workers wanted protection against this exploitation and found it to a considerable degree in trades unions and political parties.

The post-mercantile understanding of free trade continued to be a much-used argument for trades unionists and supporters of socialist politics. Even today most socialists are convinced that free trade means unregulated trade and industry, which they strongly oppose.

Liberals of today are no longer fighting mercantilism; they fight the ideas of socialism and communism. They understand free trade in the same way as the socialists. But unlike them, liberals think its effects are positive and urge for the abolition of all regulations and restrictions and for low taxes on trade and industry.

Anti-socialists are also opposed to taxes on the unearned income of landownership and on other privileges. They argue that there is no difference between land value taxes and other taxes, and urge that taxes should be spread to as many different sources as possible – except investors, enterprises of trade and industry, and privilege holders.

Anti-socialists look away from the fact that taxes on wages are taxes on production. They deny that they are urging against the interests of producers when protecting the 'free lunches' of unearned income that 'non-producers' capture. They choose to ignore the fact that all taxes burden trade and industry except tax on privilege-profits including rent of land.

But there is another way of looking at free trade: namely, trade freed from monopolies and privileges, as far as that is possible, and freed from restrictions, regulations, and taxes – other than those protecting lives, health, equal rights, and the environment. In order to realise this approach to free trade it is necessary annually to collect the rental value of land and other privileges which have to be tolerated. This revenue could be used for the betterment of all citizens on an equal footing.

The three kinds of free trade I have summarised are, in brief:

(1) 'Free trade' on the world market. This brand of free trade would need only a small customs administration strong enough to cope with illegal trade in drugs, weapons, piracy, etc.

(2) 'Free trade' in foreign and domestic trade and industry. As the aim here would be to avoid any governmental interference in private traders' businesses, only a small governmental administration is necessary. However, one might foresee a strong confrontation between the holders of privileges and those who are without.

(3) Free trade without privilege holders' withholding of the excess profits of privileges, and without restrictions other than those that protect human beings' lives, health, equal rights and the environment. This genuine free trade needs a strong government administration able to cope with monopolies and privileges which arise. It must also be able to collect the rental value of tolerated valuable privileges – including landownership – and to use the revenue for the betterment of all citizens on an equal footing.

So we see that the success of free trade relies on the good effects of necessary privileges. L&L

Part three in this series will appear in the spring 2008 issue of L&L *and will look at how we can eliminate the bad effects of privileges.*

Ole Lefmann was Deputy President of the IU 1993-2001, since when he has served as the Union's Honourable Assistant Secretary.

Hey big spender

Living with Leviathan
by David B. Smith
IEA, 2007. 190pp
ISBN: 0255365799, £12.50

It is a great pity that David Smith did not read an earlier IEA publication, *Wheels of Fortune*, by Fred Harrison before he sat down to write this book. He states the problems and Harrison gives the answers.

Smith's theme is public spending, taxes and the size of the state and its economic performance. In 1913 UK public expenditure as a percentage of GDP was 12.7 per cent, in 1937 it was 30 per cent, and now it is around 45 per cent. Sweden with its high spending experience peaked at 72.4 per cent in 1993 but this is projected to fall to 55.5 per cent in 2007. The author is unclear what effect such figures have on economic performance. He quotes studies that indicate that 30 - 35 per cent will achieve most of the social and political objectives that justify government intervention. In attempting to do too much, modern Western states may well neglect their core functions such as law and order, and military preparedness.

What is important in the equation is how the tax is raised. Harrison very clearly indicates the negative impact of bad taxes and suggests better ways of raising money. Public spending on infrastructure benefits the private sector. The London Underground Jubilee Line extension increased adjoining land values by close on £3 billion. A land tax on this increase would have recouped this public expenditure. Smith sees that high government spending does not lead to the eradication of poverty and that the cost in terms of economic growth forgone has been considerable. He says "it is highly likely that societies are poorer than they would have been if low spending ratios had been maintained."

He briefly examines different forms of taxation and notes that Britain in the eighteenth and nineteenth centuries saw rapid economic growth when most taxes were levied on fixed assets, such as houses. He doesn't differentiate between property and land in the way that Harrison does but concludes that a mature debate about, among other things, the forms of taxation, should be a priority within parties and between parties. "Sadly," he ends, "there is little sign of this debate beginning."

Geoffrey Lee


Australia's housing bubble may be about to burst

My world!

Who owns the World
by Kevin Cahill
Mainstream, 2006. 640pp
ISBN: 9781845961589, £25

Kevin Cahill is a cataloguer of wealth and an inquisitor of privilege. He first nailed his colours to the mast with his early work on *The Sunday Times* Rich List. His latest book sits at the present end of a line of investigation starting with McEwen's *Who Owns Scotland* (1977), Wightman's subsequent *Who Owns Scotland* (1996) and then Cahill's own *Who Owns Britain* (2001).

For Cahill and for his predecessors it is the 'who' that is key. The major part of *Who Owns the World* is a country by country catalogue of the major landowners of the world. This may indeed be a necessary and – as the author claims – long overdue piece of work. Many argue that publicly available and complete registers of natural and common resources, including the facts and nature of all titles to land and burdens upon them, is an institution necessary for modern democracy and efficient governance [*see* Counting the land, *p.4. Ed*]. The result of Cahill's work is to reveal that concentrated patterns of land ownership are prevalent all over the world. He resents the situation. Cahill's concern is that these patterns be "dissolved".

Cahill's historical analysis describes the increasing spreading of 'ownership' of landed resources over the past century: his political perspective applauds "land redistribution". He commends the vision of Hernando de Soto; but he does not share that economist's enthusiasm for Western "private-property laws and recording systems". Cahill argues that "property law in the developed world is at best internally and institutionally corrupt, having been created by thieves trying to legitimise theft and maintained by the descendants of the original thieves, for their private benefit and no-one else's". Cahill holds that around the world present-day property systems are for the most part "destructive to both democratic and political progress". He believes "economic progress in the West has been in spite of, and not because of, the structure of property law in most Western states".

In this book however, in a way more than in all the earlier '*Who Owns*' work, Cahill is also interested in the 'how' of ownership. The other major part of *Who Owns the World*, over twelve chapters, is a historical overview and analysis of world landownership. Some readers may sometimes find the author's analytical predisposition prejudicial. Certainly unrequited monarchists will find no succour here. Nevertheless the texts are fascinating. Disappointingly, his efforts regarding the 'hows' remain more in the nature of surveys than proposals.

In the end, for Cahill, it is information – land registration – which is "the key requirement" for reform. The reform itself he advances is the dissolution of "the monolithic legal forms of ownership" which his book discloses, and the establishment of "a proper free market in land…in every country in the world". The author does not much go into what he means by 'proper': the reciprocal obligations to the community which the owners of land may be due are not discussed. The author's demotion of the great reformer Henry George (who so clearly laid bare humanity's responsibilities in this regard) to no more than a common witness of the Irish Famine of 1845-9 is disappointing from a writer who would seek to banish unjust privilege from the world and who claims to know the land.

Isabel de Menenez

Bubbly

Unlocking the Riches of Oz
by Bryan Kavanagh
Earthsharing Australia, 2007. 28pp
AUS$10

This short book is subtitled 'A case study of the social and economic costs of real estate bubbles (1972-2006)'. In it, Bryan Kavanagh provides a concise exposition of how property bubbles – which can easily arise in the current Australian system – cause economic recession. He also suggests what otherwise might have been, if the fiscal regime had not been, as he characterises it, 'the Mad Hatter's Tea Party of taxes'.

The book is based on a careful analysis of data and builds up a picture of the economy in classical terms, of earned (labour and capital) and unearned (land) incomes. At this point I would have liked more information on how this had been done: it is interesting to note the increase in privatised rent (from 8% of resources in 1911 to 27% by 2005). However, the detailed analysis of the real estate market helps to fill in the picture. So whilst I would have liked to explore further the methods used in determining classical components of Gross Domestic Product, the omission does not detract from the overall message.

In a counterfactual, Kavanagh estimates what income might have been, in terms of GDP, had the tax regime been organised in such a way that it prevented these real estate bubbles; that is to say, if a proportion of the rental value of land were captured for public revenue.

I'm not a great fan of counterfactuals. They tend to have so many unknowns. Nevertheless even the conservative estimates the author presents are staggering. If the property bubbles that occurred between 1972 and 2006 were to have been eliminated, it is estimated that Australian GDP would have been AUS$700 billion greater than currently it is (ie 75% higher). This amounts to AUS$35,000 per year per person.

All in all this short book sets out an interesting analysis. It demonstrates why we should be concerned that sufficient attention is paid to the issue of land values. In conclusion I should like to note that such analyses as this could be much more readily facilitated if there existed clear and detailed information on land values.

www.earthsharing.org.au/unlock

Duncan Elliott

Charging for landing

(continued from the back cover)

However, crudely, the charging formula is actually based on passenger numbers. Long established major airlines with grandfather rights – if you had them last year, you get them this year – are able to monopolise valuable runway space with small aircraft, and pay only low charges for doing so.

The system causes unnecessary inefficiency and congestion. It also fails to collect the fullest revenue for the use of a scarce resource. However an examination of the present system also reveals a more fundamental question which goes to the bottom of our public finances.

BAA is a child of the Thatcher privatisation years. In 1986 the original British Airports Authority, a public body, was dissolved and all its property, rights and liabilities were passed to the new company, which was floated on the Stock Market the following year. The company has since been delisted and is owned by a consortium led by Grupo Ferrovial, the Spanish construction giant.

Perhaps the terms of the 1986 privatisation should be revisited: perhaps certain assets held by the British Airports Authority properly should have been retained in public possession. Because that underlying question is – why is BAA, a private company, permitted to charge and collect landing fees in the first place? Charges for runway slots are charges for the use of a resource whose scarcity and value is created by the democratic will of society when it limits the development and use of airports. Air traffic landing slots are a public resource. On point of principle, as well as for the sake of industry competitiveness, their value should be collected and returned to the public purse. In taking on the case of BAA the Competition Commission will have to move into a new area of thinking. **L&L**

lars rindsig: the view from the right

I routinely stand out as the most rabid, market worshipping right-winger in any crowd – except when I'm around my rabid, market worshipping right-wing friends who think I'd be alright if it wasn't for my leftie views on land.

I expect Fred Foldvary maybe shares that feeling from time to time. Foldvary teaches Austrian economics (that is, in the tradition of Friedrich von Hayek and Ludwig von Mises) at Santa Clara University in California – as does, incidentally, David D Friedman who is the son of Nobel Prize winner Milton Friedman. Son David has taken his father's libertarian economics to their logical apex and proclaims himself an anarcho-capitalist. Foldvary, too, is a no-holds barred libertarian. He is a fan of privately owned local communities and a regular speaker at conferences of groups like the International Society for Individual Liberty and the UK based Libertarian Alliance. He is also a former Congressional candidate of the California branch of the Libertarian Party and a contributor to online journals with names like *Anti-State.com* if the above wasn't enough to rattle you.

Of course Foldvary is not just your average libertarian academic boffin. His particular brand is the fusion of Austrian economics with a fundamental tax reform based on resource rents – taxes on land, natural resources and pollution (rather than legislation) – which he calls geo-anarchism or geo-libertarianism. Foldvary's latest publication, a small pamphlet called *The Depression of 2008*, was published this summer. In it he examines the business cycle of the property market. Foldvary's conclusion is the same as the cover story in this issue of **L&L**: it's all going down in a cloud of dust. So, the conclusion of Foldvary's analysis does not differ fundamentally from that of other economic researchers like Fred Harrison. His route, however, does.

The concept of money is central to Austrian economists – and not just because they all want more. 'Austrians' ardently favour a totally privatised and non-regulated monetary system issuing gold-backed, non-inflatory money. Consequently, Austrians do not treat all capital goods as one variable – like most economic analysts – but treat money and financial capital separately from other capital items like cars, houses and typewriters. This is all very theoretical stuff but important because under a free banking regime, changes in the interest rate would not cause problems since it would move naturally. Whereas with a government central bank, adjustments to the interest rate are artificial and distort the economy.

So a key aspect, in Foldvary's view, of countering the harmful boom/bust effects of the property business cycle is the introduction of a free banking policy. Since the market would prevent inflation this move would, by itself, dampen (though not prevent) the real estate cycle. Equally important, says Foldvary, is the introduction of a radical tax reform that replaces taxes on income, goods and sales and profits, with a levy on the value of land. The real killer, though, is the two initiatives working in tandem. One without the other won't make the cut; even with an artificially lowered interest rate, government controlled money will continue to work against the true free market.

And this is where Foldvary's take on economics truly shines. Focussing too narrowly on one aspect of the solution – whether it is a tax shift or free banking – only gets us half the way. We'd be better off, sure, but not nearly there.

Charging for landing

Jo Stocks thinks the Competition Comission should tell BAA how to land its planes

The UK Office of Fair Trading has referred BAA to the Competition Commission for investigation. BAA styles itself "the world's leading airport company".

OFT's concerns centre on possible monopolies on the supply of airport services. BAA owns the London hubs of Heathrow, Gatwick and Stanstead, and three of Scotland's four main airports. Questions are being asked about passenger consumer choice and airline competitiveness. BAA provides the marketplace for the exchange of an annual 144 million passengers and 620,000 airline flights.

On the passenger side, BAA is one of the largest commercial landlords in the UK, owning a £1.4 billion portfolio of airport properties. Over 900 organisations trade from its premises. This area of its business is little different from other commercial landlord operations - although the monopoly issue might loom larger than usual.

On the airline side, BAA's role is much more particular. The company manages, and profits from its role as gatekeeper to, the runways. BAA's present-day revenue from this side of its business is unknown, but likely to be in the region of £1b a year. This aspect of BAA's activity will be a different matter for the Competition Commission to grapple with. The Commission's success will come down to whether it is seriously capable – as the Enterprise Act requires of it - of "making and implementing decisions on appropriate remedies" on questions of competition and monopoly.

BAA says Heathrow, Gatwick and Stansted are operating at or near capacity. OFT concurs, and believes "capacity constraints are a feature of the market that restricts, prevents or distorts competition".

Operational capacity is determined firstly by the dimensional constraints of space and time. Public opinion acting through the planning system, and initiatives like this summer's Camp for Climate Action, set the effective limits on these. But also critical to capacity is the operating system in place which manages the effectively-finite resource of runway space.

Access to their passengers is granted to the airlines via a system of landing and take-off 'slots'. Allocation of those slots is made by Airport Coordination Limited – in effect a cartel of the major airlines. So access to the assets which arguably are the airline's most precious resource is directed by the airlines themselves. ACL seems magnanimously comfortable with the existing arrangements.

Allocating the slots

"No member airline receives direct benefit, in terms of preferential treatment in slot allocation decisions made by ACL. All airlines are treated the same, in accordance with UK and European Slot Regulations which ensure that decisions made by ACL are made in a 'neutral, transparent and non-discriminatory' way. Members believe that it is reasonable for them to contribute to the cost of slot allocation in the UK, since the cost of the coordination task in other countries is borne by their Governments or national carriers. Contributing to the cost of ACL avoids the need for Government intervention of [*sic*] control of slot allocation and ensures that all the airlines receive a high quality coordination service. Any airline may apply to join ACL, and the Company is pro-active in seeking to expand its membership base."

Airport Coordination Limited

Under the regulation of the Civil Aviation Authority, BAA has the exclusive right to fix prices and charge airlines for landing and takeoff within the slots at its airports. CAA caps prices, and according to OFT "the fact that Heathrow and Gatwick price up to their price caps suggests that price controls hold prices lower than would otherwise be the case."

(continued inside on p11)

THE FUTURE - the Competition Commission should consider

- reallocating BAA's asset rights rather than breaking up its property portfolio
- abandoning the anti-competitive privilege of 'grandfather rights'
- establishing an annual public auction system of tradable slot permits - a free market pricing mechanism - promoting competition and eliminating monopoly within the air travel industry
- renewable slot permits to apply to the use for a certain duration of a particular runway at a particular time of the week and in a particular season
- establishing an arms-length public 'air traffic charging authority' with the task of regulating the initial allocation, pricing and trading of landing and take-off slots
- permit-holders to pay annually to the Treasury the value of the slots they hold, boosting public revenues and paying for administrative costs
- airlines relieved of the burden of operating Airport Coordination Limited, which should be disbanded
- and, consequently, bringing about enhanced democratic decision-making in the future development or delimiting of air travel - enlightened by public concern for the consequent impact on the public finances of increasing or decreasing revenues from the use of a scarce public resource (and, also, balanced by carbon trading which should be extended to air travel).

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NEXT ISSUE

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