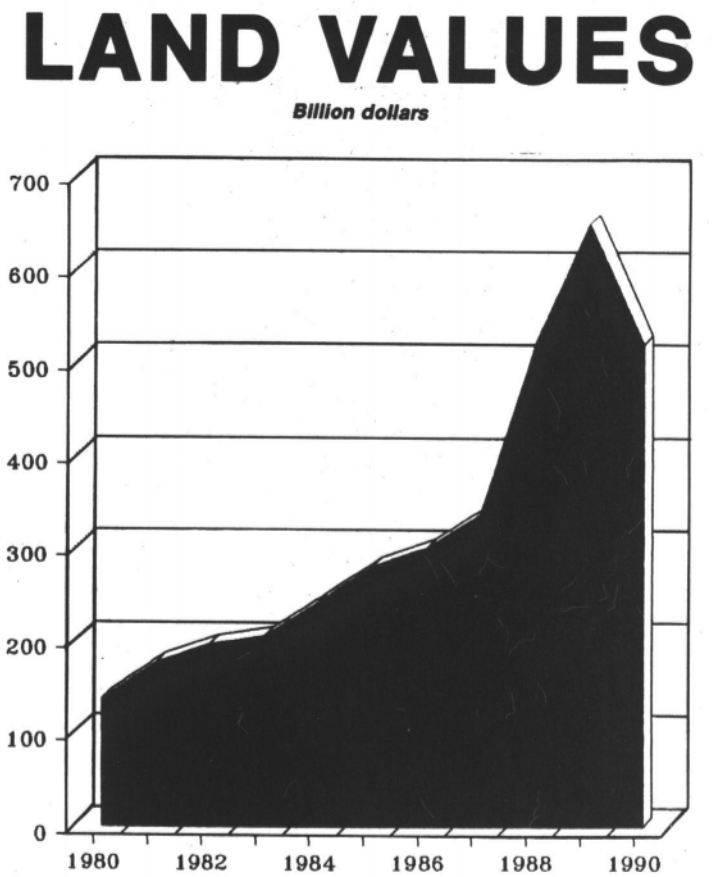


• Australian land value figures, supplied by the Commonwealth Grants Commission; and estimates by Bryan Kavanagh

A bullish outlook

THE Organisation of Economic Cooperation and Development, which represents the industrialised market economies, has a bullish view of prospects for the Australian economy.

• Growth of 2.5% is predicted for 1991, a slowdown from 4% last year.

• Unemployment should increase, and by 1991 is expected to edge above the OECD average of 6.6% of the labour force.

• The government is urged to keep interest rates high, and the budget in surplus.

• Reforms, says the Paris-based secretariat, should focus on the labour market. "The main obstacle now appears to be the attitudes of management and labour and the pattern of unions. Management will need to be more forward looking, better able to manage its human resources and capable of creating a coherent strategy of workplace reform."

Australia and the last taboo

INSITE examines the evidence which puts to the test a classic economic theory which explains busts in the business cycle.

IN APRIL, 1984, a small team of Melbourne-based supporters of American social reformer Henry George were putting the finishing touches to a report which they were to submit to the Economic Planning Advisory Council on Tax Reform.

The Council, which was to report to the Prime Minister and Cabinet, was looking at the ıuture of the Australian economy. And the Georgists felt that the government ought to take a closer look at the virtues of land value taxation. Many Australian municipalities levy a local tax on site values, but this fiscal policy is not regarded as significant for macro-economic purposes.

Before the Georgists finalised their report, a copy of a book published in Britain arrived in Melbourne: *The Power In The Land* had been published a few weeks earlier by Shepheard Walwyn Ltd. Its author, Fred Harrison, had retrieved from obscurity the notion of 18-year cycles in land values. These cycles were originally traced in the 19th century US economy by Homer Hoyt.

Harrison had subjected the cycles to further examination. He concluded that the 18-year

Continued on Page 68 ▶

◀ From Page 67

periodicity was a phenomenon that continued to operate in the 20th century. Furthermore, the cycles were evident in all the industrial countries that he examined: the USA, Britain, Japan and Australia.

The Australian land taxers read the book and decided to back the historical record with a prediction. At the last minute, they incorporated the following statement into an addendum: "The next property boom should peak worldwide in mid-1991."

The report, which was submitted by the Association For Land Value Taxation, justified the risks associated with such crystal-ball gazing in these terms: "It is surely the predictability of recessions following massive land booms which should be the proof of any scientific explanation."

COMING soon after the recession that crippled the global economy in the early 1980s, that prediction was certainly a bold one. It relied on a theory that claimed to foresee a major turning point in the business cycle a full seven years down the line.

Some Australian Georgists were worried. "What if we are wrong?" they challenged Bryan Kavanagh, a property valuer who played a major role in drafting the report.

Kavanagh stuck with the prediction. In his profession's journal, *The Valuer*, he wrote in July 1987: "... as land prices rise sharply across the board, it can be accepted that the productive side of the economy will wilt - that unemployment will increase and the return on capital will wane. It is empirical study of the effects of this natural law which allows Georgists to predict the recession which will follow the peak of the next worldwide land boom in 1991/92."

At the time, land prices were, indeed, booming in Australia (see graph). The cash-rich Japanese were leading the spending spree, followed hard on their heels by Australian speculators.

In 1988, Kavanagh and his associates repeated their prediction in a submission to the Bishops' Committee for Justice, Development And Peace. They declared that a "world recession will follow the bursting of the speculative 'bubble' in land prices in mid-1991.

A year later, in October 1989, Bryan Kavanagh declared in an article in *Progress*, the journal of Tax Reform Australia: "If history is a guide the current explosion in world land prices will come to a sudden halt by late 1991."

He added: "For analysts to glibly assign the cause of the ensuing economic collapse to 'unsustainable debt levels', without acknowledging the critical role played by land price, would be to explain this chapter in our history most inadequately."

LAST YEAR, Australia's residential property market began to weaken. This was to be an early signal supporting the periodicity which Kavanagh and his associates have emphasised.

Ravi Batra, an American scholar whose prediction turned his book *The Great Depression of 1990* into a best-seller, visited Australia. Kavanagh was not impresed, and he reported to *Land and Liberty* in August 1989: "I still think our time frame for the collapse is superior to his. The current situation seems more a function of interest rates than the structural 'crunch'."

Then, early in 1990, events in the Australian property market began to move fast - downhill. And by the summer, the Press published screaming headlines that began to vindicate the Georgists.

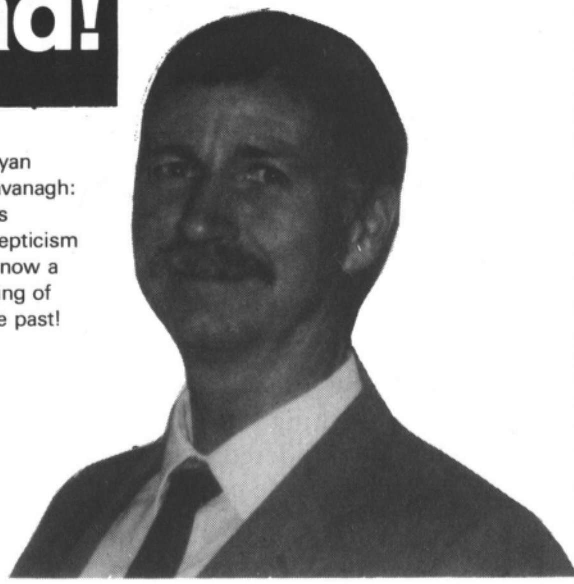
In one report, written by Pam Walkley in the *Australian Financial Review* (May 30), the depression of the early 1970s was recalled: "Forget the Australian property market crash of 1974, the crash of the early 1990s is shaping up to be far worse."

The distressed sale of property worth A$3bn is damaging the market, and analysts say a further $10bn is overhanging the market as terrified owners seek to reduce their exposure. Their fears are traced by new estimates by Kavanagh, who as a supervising valuer with the Australian Tax Office is well placed to judge trends in property values. His latest estimates show that the land market has gone into a tailspin. He informed *Land and Liberty* in June: "Melbourne values have declined 15% to 25%. Commercial and industrial development sites are the most affected." The decline was even more dramatic in Sydney.

What does this mean for the prediction of a depression? In his book, Harrison had argued that the land market reaches its cyclical peak about two years before the onset of depression. If this holds true for Australia, the continental economy will be in deep trouble by the end of 1991 - exactly in line with the prediction submitted to the Economic Planning Advisory Council in 1984!

ORTHODOX economists cannot agree on Australia's medium term prospects. Westpac Bank and the Melbourne Institute of Applied Economic and Social Research, whose index of leading indicators fell by 1.4 points in March, has correctly forecast every major change in the Australian economy since the 1950s. Cautiously, the institute's Dr Ernst Boehm said it was too early to say whether the slowdown would develop into a

Very good read!



Bryan Kavanagh: His scepticism is now a thing of the past!

BRYAN KAVANAGH was working as a property valuer in the Australian Taxation Office when he noticed most of Melbourne's land values doubled between August 1973 and February 1974.

This topped off a remarkable period of escalating prices.

"I had read a bit of the literature of the Henry George League, and, although impressed, was a little sceptical," he told **Land And Liberty.**

"I thought this sharp, frenetic surge in land values would test Henry George's theory on the boom-and-bust cycle."

When the property market collapsed in 1974, "I was by now most impressed! I set about reading George. In the early 1980s, I couldn't help myself. I thought 'If you can't fault 'em, join 'em.'

"Despite the general cynicism of property valuers towards these ideas, I've been a convinced Georgist ever since.

"In the profession I am regarded as a bit of an oddity and have been asked to speak several times on the subject of these arcane beliefs to valuers' groups.

"When it comes to why valuers reject the implications of failure to capture economic rent for revenue, they have an interesting response.

"The same people who are quite analytical in their jobs, make no attempt to argue their case. They resort simply to such as: 'But that's just Henry George'. As though that very statement simply defeats our case!"

Mr Kavanagh eventually became President of the Melbourne-based Tax Reform Australia, which gave him a platform from which to alert the Australian government on the macro-economic consequences of land speculation.

Now, as past-president, he is still urging Australian academics to undertake a thorough study of the value of the continent's land and natural resources.

severe recession. But other analysts now fear that the economy may be near to a technical recession.

What makes the original 1984 prediction all the more remarkable, however, is that the Melbourne Georgists realised that the world economy was so synchronised that the depression would be of global proportions. They forecast the land markets would slump around the world in time for the crash at the end of 1991. The evidence is bearing them out. During the first six months of 1990, land values have seriously weakened in Japan, Britain and the United States.

The asset values on which many firms rely as collateral for loans are being crushed by the downturn in real estate markets, leaving them – and many banks – seriously exposed. Worldwide, the consumption boom that began in 1986 was financed on the back of the land boom. This led to a deterioration in the balance of payments of countries such as Britain, compelling governments to strike back with damaging policies (such as high interest rates, which obstruct fresh investment and destroy jobs).

The small band of Melbourne Georgists have been exonerated for putting their theory to an empirical test. Even if the timing had turned out to be slightly out, their mechanism for the crash is being verified by the turn of events.

HAD THE Australian government taken their advice in 1984, it could have restructured the tax system in favour of a higher tax on land values: the administrative apparatus was already in place for the fiscal reform that would have spiked the land boom which, we now know, was in the offing.

The tax reformers knew their advice would fall on deaf ears. They wrote this assessment into their 1984 report: "It seems land value taxation is the last taboo of the western economist, for, to argue that land booms are an unnecessary knot in our system is seen by many to strike at the very heart of 'free enterprise".

"The cogs of free enterprise can be oiled by recognising the destructive influence of property booms and acting to curtail them. We must be prepared to accept the truism that the so-called property 'hedge' initiates and encourages inflation and unemployment, before we can make significant inroads into our substantial economic problems."