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SHARING THE EARTH SO ALL MAY PROSPER

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PROSPER'S SUBMISSION TO THE SENATE INQUIRY INTO AFFORDABLE HOUSING

ACCESS TO LAND • FAIR TAXES • CITIZENSHIP

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Editor
David Collyer

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Send contributions to:
progress@prosper.org.au
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Prosper Australia
Earthsharing Australia
Land Values Research Group

Contact
2/22 Punch Lane
Melbourne 3000 Australia
Tel: +61 (0)3 9077 0999
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Contact Information Related Organisations

ACT
Association for Good Government
www.associationforgoodgov.com.au
goodgov@bigpond.net.au
02 6254 1897
Holt Street Holt ACT 2615
PO Box 4376 Munuka ACT 2603

NSW
Association for Good Government
goodgov@westnet.com.au
02 9698 2436
122 Little Everleigh Street Redfern NSW 2016
PO Box 251 Ulladulla NSW 2539

QLD
Henry George Association of Queensland
HenryGeorgeAssociationQld@gmail.com
0407 210 079
PO Box 3112 Maryborough QLD 9726

Site Revenue Society
dspain@spains.com.au
07 5574 0755
PO Box 8115
Gold Coast mail centre QLD 9726

WA
Georgist Education Assoication
www.gea.org.au
info@gea.org.au
08 9279 5590
5/20 Old Perth Road Bassendean WA 6934
PO Box 472 Bassendean WA 6934

TAS
Prosper Australia (Tas Branch)
foleo55@gmail.com
03 6228 6486
31 Brushy Creek Road Lenah Valley TAS 7008

Useful Websites

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www.earthsharing.org.au
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If a tax were imposed equal to the annual use value of real property ex its improvement, so that it would now have no net earnings and hence no capital value of its own --progress would be orderly and its fruits would be equitably shared.

John Kenneth Galbraith 1908 - 2006
The Affluent Society (1958)

Australia's Land Bubble: The Cause of Unaffordable Housing

by Philip Soos and Paul Egan with David Collyer

PROSPER'S SUBMISSION TO THE SENATE ECONOMIC REFERENCES COMMITTEE INQUIRY INTO AFFORDABLE HOUSING

Introduction

Over the last decade, Australians have debated the causes of the rapid housing price inflation and perceived lack of affordability. Since 1996, prices have outpaced inflation, incomes, rents and GDP, making it difficult for potential first home buyers to enter the market and realise the Australian dream, while increasing shelter costs adversely impact the homeless and lower income groups. These forgotten people are citizens too. Ominously, the Australian housing market shares similarities with countries afflicted by real estate bubbles, such as the United States, Spain, Latvia and Ireland. Around two-thirds of household wealth is in real estate; a large fall in housing prices would adversely impact many individuals, families and the broader economy.

Government officials, the finance, insurance and real estate (FIRE) sector and mainstream economists predictably deny the existence of a property bubble, even though land market bubbles formed during the 1830s, 1880s, 1920s, mid-1970s and late 1980s. The bursting of these bubbles invariably caused economic recession or depression. Contrary to the protestations of government, industry and academia, nine long-term measures of housing valuation demonstrate Australia is in the midst of the largest housing (land) bubble on record. Policymakers are in a bind: either delaying or implementing needed reforms is likely to burst the housing bubble, with severe financial and economic consequences as residential land values deflate to their long-run average. A chorus of critics stand poised to blame policymakers for the bust and deflect attention away from financial speculation.

Previous inquiries in 2004 and 2008 identified both supply and demand-side variables as contributing to high housing prices: availability of finance, lower nominal interest rates, preferential taxation treatment for all land owners, developer charges, the composition and rate of employment, demographic factors (populationw growth, household size and age structure), cash grants to first home buyers, and the returns from other investments. It is argued there are two primary causes for the housing bubble: a rapid acceleration in mortgage debt and tax policies encouraging speculation.

Nine Metrics Illustrating the Residential Property Bubble

A residential real estate bubble forms when housing prices and land values rise sharply. Nominal housing price to inflation/rent/income and mortgage debt to GDP ratios escalate, investors' net rental incomes become persistently negative on aggregate, gross and net yields are negligible, and the turnover rate of housing ('flipping') rises. These outcomes result from banks' willingness to finance investor-led speculation in housing markets, amplified by low property and land taxes. Owner-occupiers and investors ignore paltry (imputed) rental incomes, even though this determines the fundamental value

of land. The following figure illustrates the long-term trend in real housing prices and the household debt to GDP ratio (the overwhelming majority of which is mortgage debt).

A rising trend in real housing prices indicates buyers are favouring housing relative to other opportunities. It took forty years from 1950 to 1990 for housing prices to double, but only fifteen years between 1996 and 2010 to double again. The surge in housing prices is driven by the tremendous growth in household debt, as owner-occupiers and investors take out ever larger mortgages to speculate on housing. The household debt to GDP ratio reached a record high of 98 per cent in 2010, the same yearreal housing prices peaked. In 2013, the mortgage and personal debt ratios were 86 and 9 per cent, respectively, for a combined household debt ratio of 95 per cent.

As mortgage debt escalated, investors' net rental losses increased rapidly from 2001 onwards. In that year, net rental income losses were just over $1 billion, rising to $9.7 billion in 2008 as the cash rate peaked at 7.2 per cent. By 2010, when mortgage debt reached its historical peak relative to GDP, investor losses eased to $5.1 billion as the cash rate fell to a then historic low of 3 per cent in 2009 following the global financial crisis (GFC). The latest data shows income losses rose to $8.2 billion in 2011, the second largest absolute loss on record. Not only is the investment stock incurring net rental income losses; the entire housing stock is in this undesirable position.

The housing price to rent (P/R) ratio is the equivalent of the price to earnings (P/E) ratio used in the stock market, and an elevated ratio is a classic sign of a bubble. From the trough in 1997, the gross and net P/R ratios increased from 21 and 38, to a peak of 35 and 71 in 2007, respectively, before falling to 27 and 54 in 2013. The sharply rising P/R ratio was caused by a period of strong housing price growth coinciding with moderate rental income growth. The ratio fell between 2007 and 2010 due to a surge in rents stemming from a combination of high population growth and a collapse in new housing construction in 2009 after the GFC. Investors' indifference to mounting net rental losses and elevated P/R ratios implies they are fixated upon pursuing capital gains over rents and rental growth. The housing market meets economist Hyman Minsky's definition of a Ponzi scheme, as gross rental incomes minus expenses are clearly insufficient to meet principal and interest repayments. As 67 per cent of property investors are negatively-geared

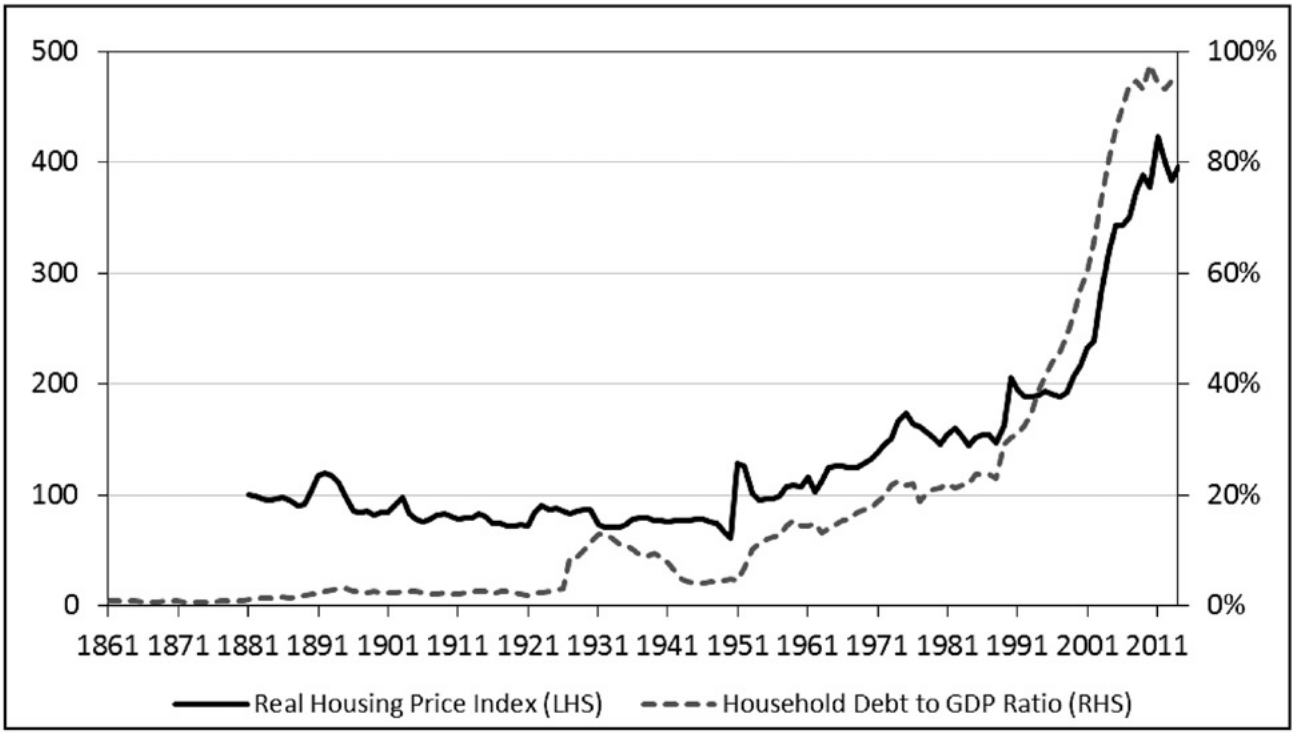


Figure 1: Australian Constant Quality Real Housing Price Index (1880 – 2013; 1880 = 100) & Household Gross Debt to GDP Ratio (1861 – 2013)

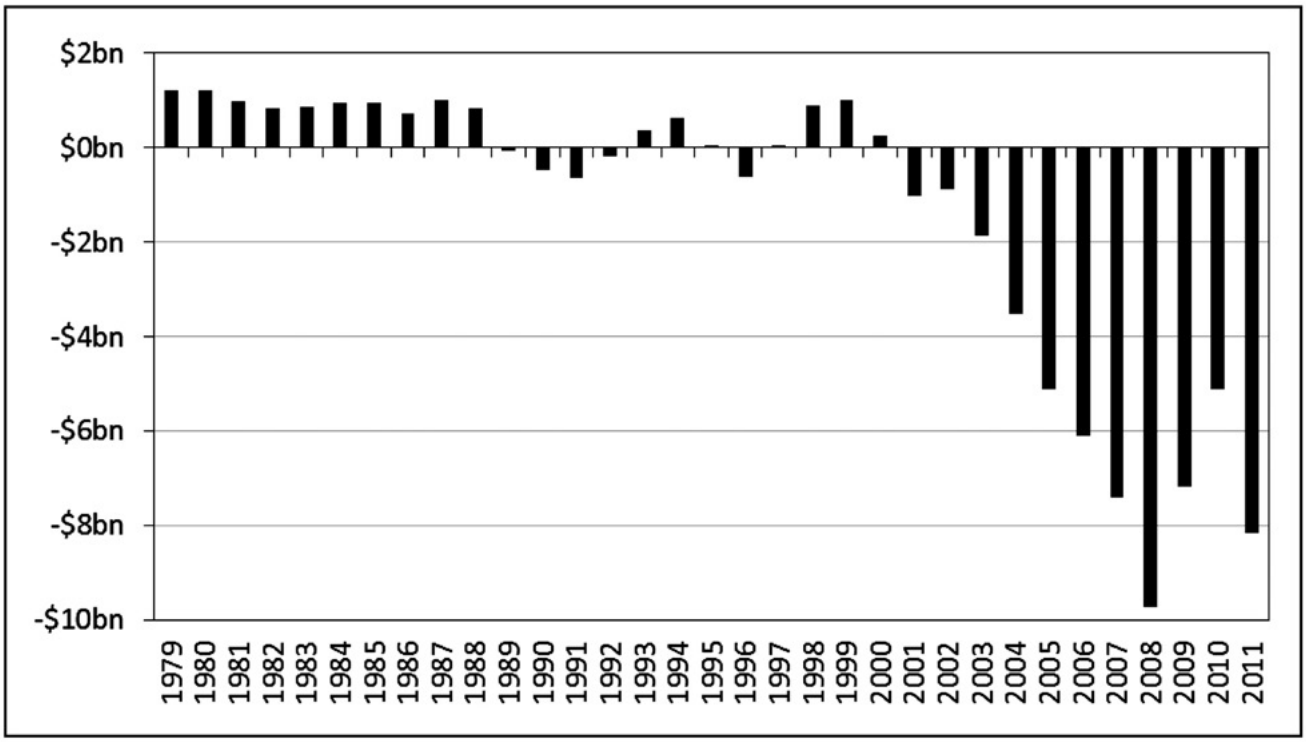


Figure 2: Australian Property Investment Real Net Rental Income 1979 - 2011

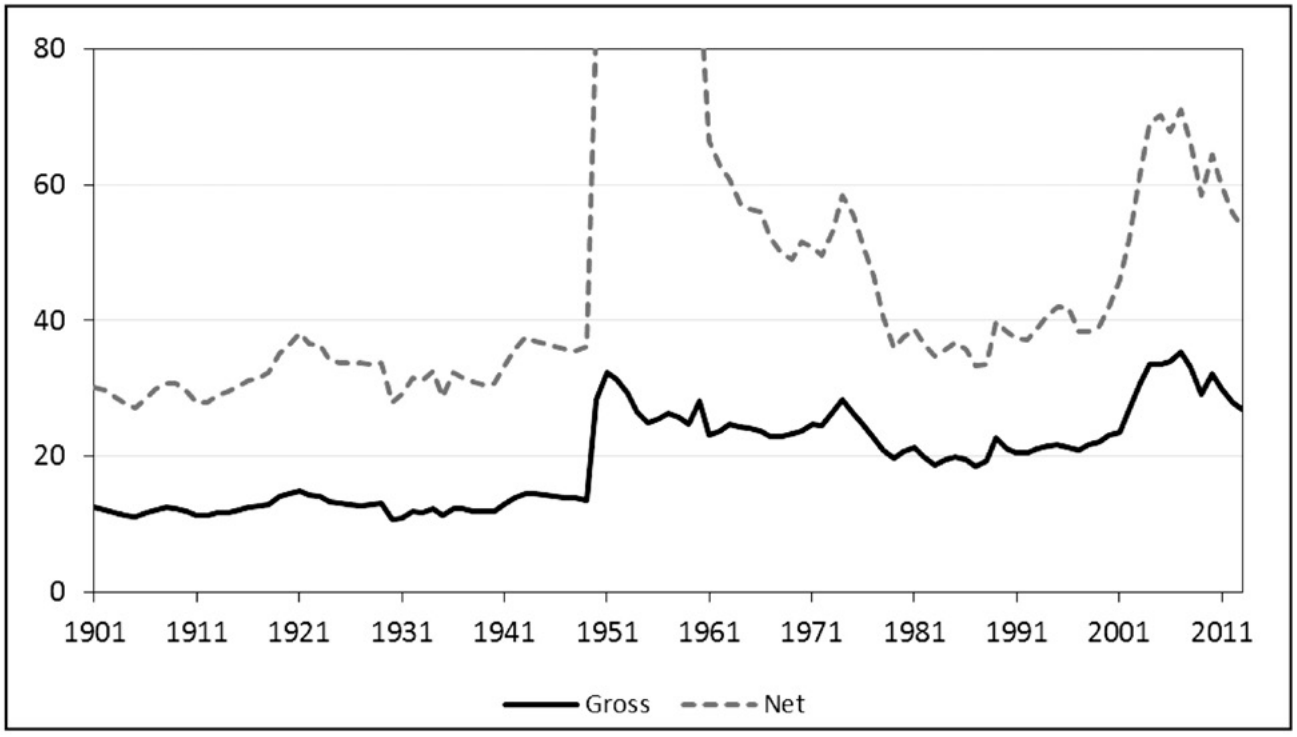


Figure 3: Housing Price to Rent Ratios 1901 - 2013

as of 2011, investment decisions are predicated upon expected rises in land values, not rents. This strategy will inevitably fail, as the escalation in real housing prices can only be sustained by a continual acceleration or exponential rise in mortgage debt.

The price to income (P/I) ratio, otherwise known as the median multiple, is another measure of residential property valuation. It is expressed by dividing the median dwelling price (numerator) by the median household income (denominator), providing a simplified measure of the number of years of gross household income required to purchase a home. From the mid-1990s onwards, housing prices outpaced household incomes, and the P/I ratio increased from 4 to 7 nationwide. It is impossible for household incomes to match the rise in housing prices during the boom phase of a property bubble, as wages grow more slowly, usually just above the rate of inflation.

The Kavanagh-Putland Index (KPI) measures the ratio of the total value of property sales to GDP, and is a leading indicator of housing prices and the broader economy. As irrational exuberance mounts, turnover increases, and the total value of annual sales rises relative to nominal GDP. When the 16 per cent threshold is breached and the ratio eventually falls, a downturn in the property market typically occurs, leading to recession. From 1996, the KPI increased from 14 per cent to a record peak of 28 per cent in 2004, and remained near this level until 2008. The KPI has since fallen to 18 per cent in 2013, a level last observed in 1999. The falling trend signifies waning investor mania and partially explains the recent stagnation in housing prices and sales nationwide, except for pockets in Sydney and Melbourne.

Land is the largest tangible market in Australia. Residential land is the most valuable component, at slightly over $3 trillion, with commercial, rural and other land markets worth $351b, $261b and $225b respectively. Our housing bubble is actually a residential land bubble, as the total land values to GDP ratio doubled between 1996 and 2010, when it reached a record high of 298 per cent ($4.1 trillion). In real terms, residential land values rose from $895 billion in 1996 to a peak of $3.2 trillion in 2010, a relative increase of 262 per cent. This ratio is closely matched by a similar rise in the value of the residential housing stock. The rise in residential land values, rather than structures, is responsible for almost all of the increase in the value of the housing stock. As of June 2013, the total land values and housing stock value to GDP ratios were 256 per cent ($3.87 trillion) and 293 per cent ($4.4 trillion) respectively. The total value of the housing stock surpassed the $5 trillion threshold in December 2013 (around 330 per cent of GDP).

The debt to cash flow ratio (D/CF) provides a

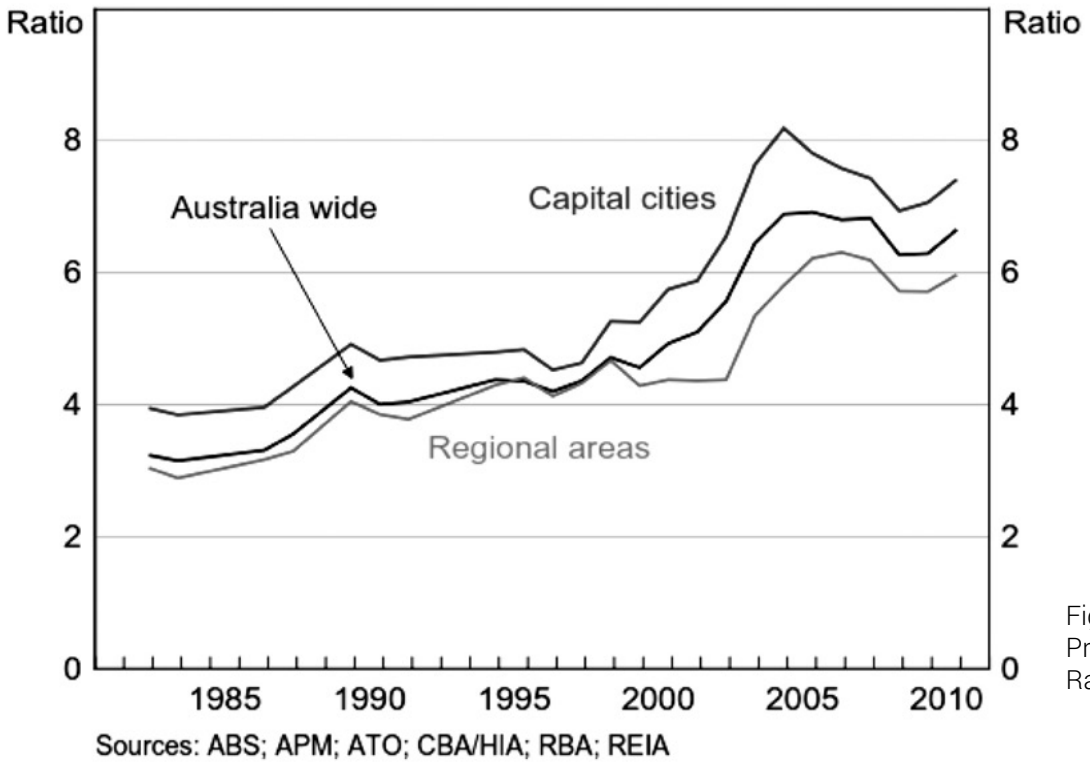


Figure 4: Dwelling Price to Income Ratios 1981 - 2011

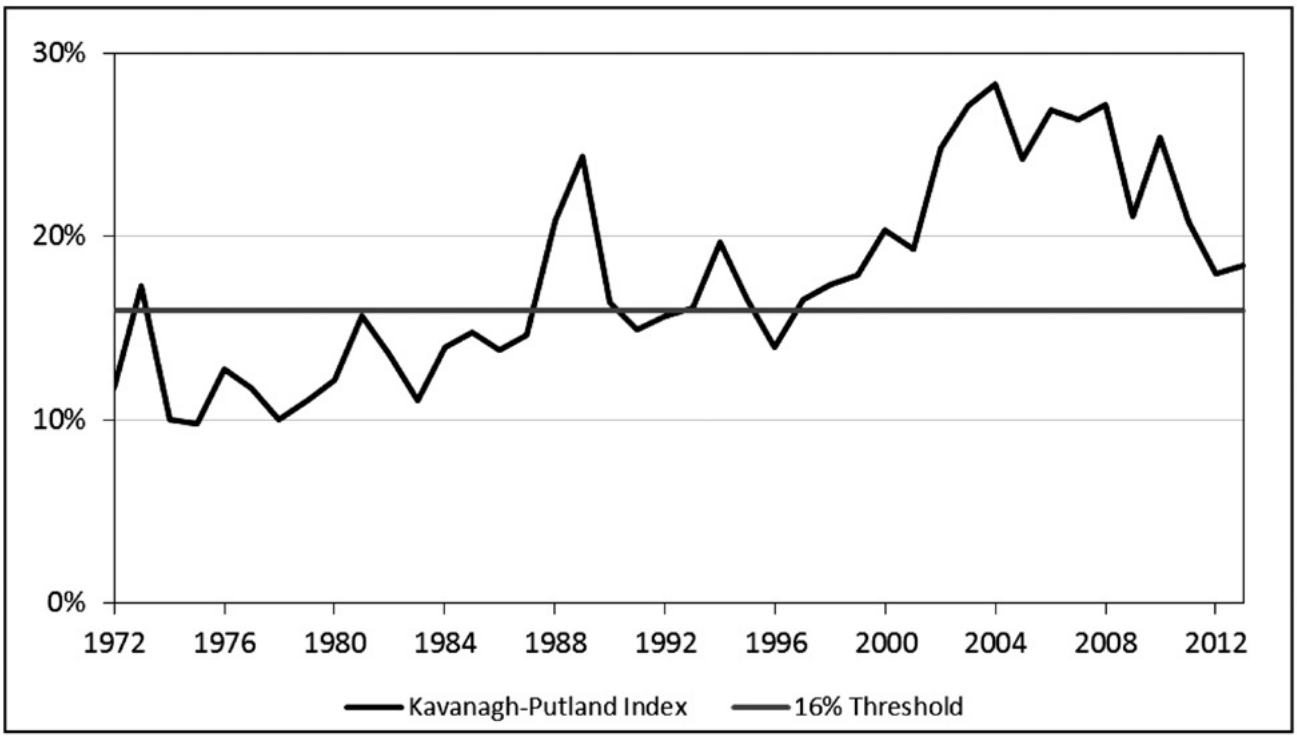


Figure 5: Kavanagh-Putland Index 1972 - 2013

measure of leverage, comparing the stock of debt with the income available to service that debt. The numerator represents household mortgage debt and the denominator, cash flow, is equivalent to net revenue. This metric is a valuable tool of real estate analysis, as the housing sector's financial health is often ignored by mainstream economists who inordinately focus upon government accounts. D/CF ratios are superior to private debt to GDP ratios as the latter assumes an unlimited proportion of national income can be diverted to service debt. The D/CF ratio can be categorized into one of four zones representing relative leverage: inefficient, optimum, warning and calamity. For the household sector, a ratio of 5 or less indicates inefficiency, optimum (5 to 10), warning (10 to 20) and calamity (20 and above).

Theoretically, leverage within the optimum zone maximises returns without adversely affecting stability or increasing risk, whilst lower and higher levels are suboptimal because they either generate poor returns, or conversely threaten household solvency due to the scale of debt burdens. The housing stock D/CF ratio was 4.8 in 1990, doubling

Tax Expenditure	2005-06	2007-08	2011-12
Capital gains tax exemption for owner-occupied housing	29.8	20	14
Discount on capital gains on investor housing	4.2	6	4.4
Land tax exemption for owner-occupied housing	3.5	10	5
Negative gearing for investment property	1.2	2	2.4
Non-taxation of imputed rent for owner-occupied housing	11.7	15	9.6
Home exemption from pension assets test	-	-	7
Total	50.4	53	42.4

Table 1: Estimates of Housing Tax Expenditures ($Billions)

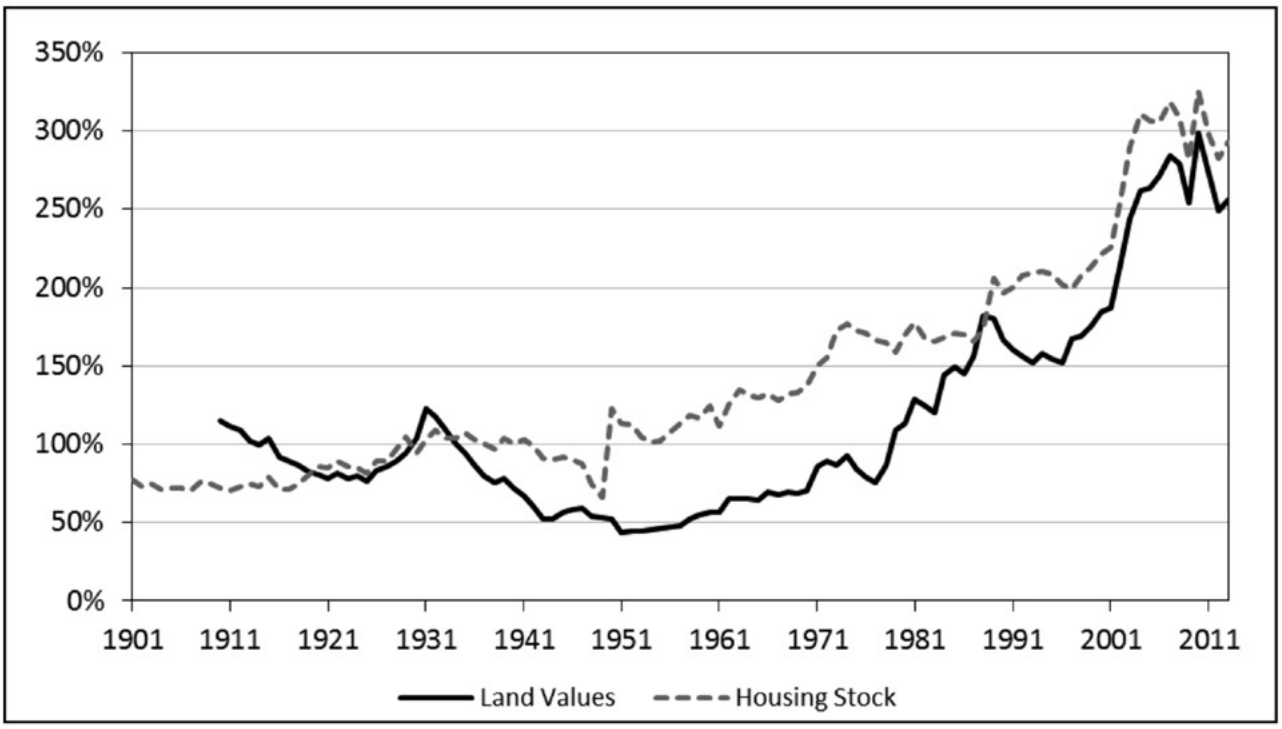


Figure 6: Total Land Values to GDP Ratio (1910 - 2013) & Housing Stock Value to GDP Ratio (1901 - 2013)

to 9.5 in 1999 but still within the optimum zone. It escalated to a peak of 32.7 in 2007, well into the calamity zone. With the slowdown in the growth of mortgage debt since the GFC and rising rents between 2007 and 2010, the ratio has fallen to 21.2 as of 2013. The investment stock fares little better, having peaked in 2006 at 29.2 and has decreased slightly to 25.6 in 2011. Households have taken on onerous levels of mortgage debt while cash flows have barely increased. Without a strong rise in imputed and actual rents or active mortgage debt deleveraging, the D/CF ratio is expected to remain in the calamity zone.

The Role of Taxation, Debt and Land Rent in Declining Housing Affordability

The nine measures of housing valuation provide strong evidence of the formation of the largest land price bubble in Australian history, threatening future financial and economic stability when it deflates. Every measure is at or near a historic peak. A convergence of factors are responsible: a large cohort of irrational investors gambling on housing prices, a FIRE sector willing and able to facilitate a credit boom, and low property and land taxes attracting speculators to this asset class. Contrary to neoclassical economic theory which stipulates private debt has no effect upon asset prices, a trend of accelerating mortgage debt growth has driven up housing prices to a historic peak. A positive feedback loop has emerged between housing prices and mortgage debt, with rising prices prompting the take-up of more debt in an upwards spiral.

An inefficient taxation system, comprised of low property and land taxes, allows landowners to expropriate 'geo-rent' (economic rent derived from land) by capturing the uplift in land values generated by taxpayer-funded infrastructure and rising economic productivity. As noted by property valuer Bryan Kavanagh: "...land price is actually the private capitalisation of imputed site rent remaining on a site, developed or undeveloped, after the deduction of government charges." Government willingness to tax wages and business ahead of land has elevated its privileged status, resulting in larger capital sums being paid by owner-occupiers and investors.

Counter-intuitively, reducing wage and business taxation and increasing land tax would not necessarily lower fundamental land prices, given the offsetting boost to disposable wages, profits and hence rents, but it would certainly lower bubble-inflated land prices. Land tax reform – urged on government by every independent tax review in living memory – would firmly correct the price to rent and income ratios. If Australia wishes to escape or ameliorate the profound financial destruction of a bursting land bubble, the solution lies in this equation.

The generous scope of tax expenditures relating to the housing market has served to further increase prices. Tax expenditures are defined as a deviation from the commonly accepted tax structure, whether it is a tax exemption, concession, deduction, preferential rate, allowance, rebate, offset, credit or deferral. Australia has the highest rate of tax expenditures among our OECD peers, at more than 8 per cent of GDP. Tax expenditures are vulnerable to lobbying, and often compromise the fairness and efficiency of the tax system. Lavish tax expenditures for both owner-occupied and investment property has significantly worsened housing affordability because they allow landowners to capture greater amounts of geo-rent and prioritise unearned wealth and income over what is earned. Existing home owners capture the most benefit, ahead of first home buyers, investors and tenants.

These tax expenditures provide a strong incentive to speculate on housing prices, and are reinforced by already low property taxes. Investors perceive rental income as secondary to expected rises in capital prices, while first home buyers over-leverage themselves to enter a bubble-inflated market. Tax expenditures, combined with the ongoing deregulation of the banking and financial system, has transformed the housing market into a casino. Residential property is commonly viewed as a speculative asset to flip, rather than shelter to raise a family in. The behavior of Australians is profoundly influenced by irrational exuberance, amply demonstrated by a large cohort of negatively-geared property investors; overwhelmingly middle-income earners seeking to escape the PAYE tax system.

Neoclassical economists reduce the functioning of the housing market to supply and demand equations, instead of focusing upon debt-financed speculation and the private capture of land rent as major causes of housing price inflation. Reasons most often cited included population growth, demographic change, housing grants, urban containment policies, low nominal interest rates and inflation, developer imposts, foreign investment, the mining boom and so on. Attributing the rise in housing prices to fundamentals is problematic because the true measure of land value – rental income – has not risen in tandem with prices; also, the rent to income ratio has remained steady. Every time a housing bubble forms, prices rapidly increase but rents tend to track the rate of inflation, resulting in a significant divergence in the P/R ratio.

Australia's current land bubble is the latest in a long line: the 1830s, 1880s, 1920s, mid-1970s and late 1980s. The same pattern of continuous land market cycles has been observed in the UK, US and the Netherlands, often ending in severe recession or depression. History has been unkind to those

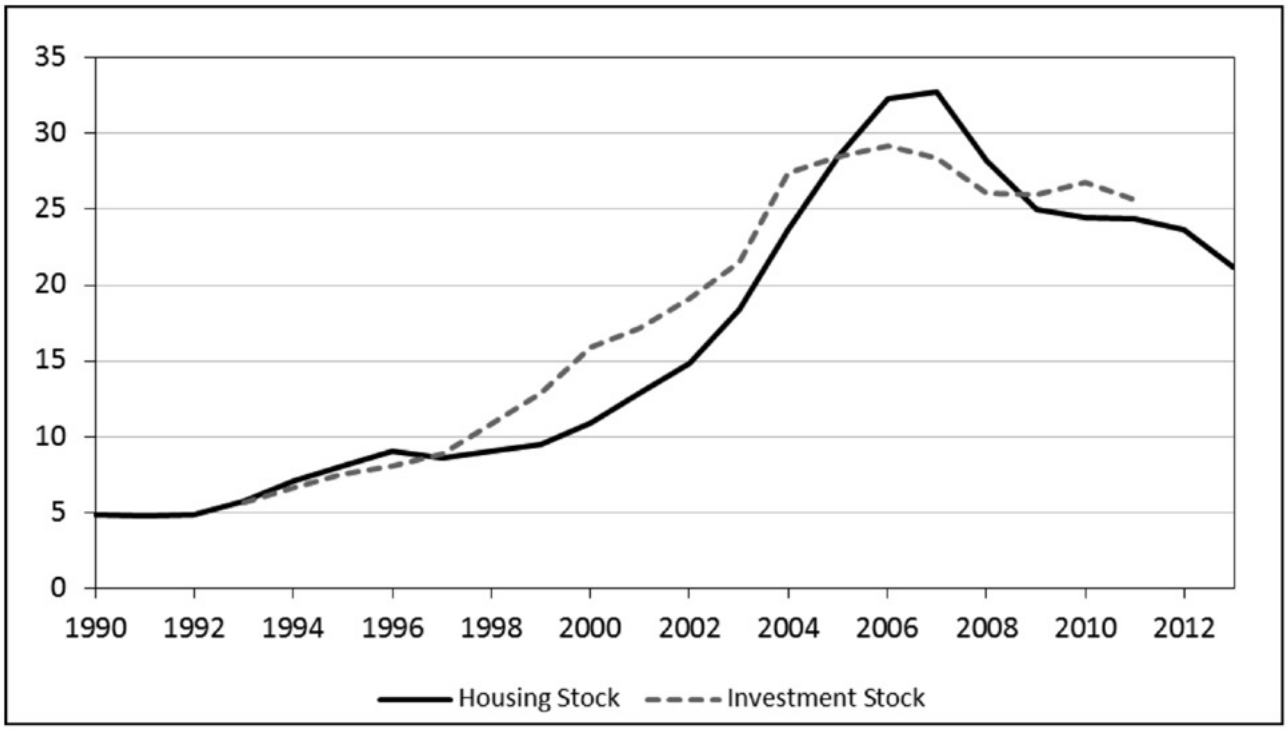


Figure 7: Housing Debt to Cash Flow Ratios 1978 - 2013

gullible enough to believe markets are guided by an 'invisible hand' generating efficient economic outcomes. Yet, despite clear warnings from history, economists appear willing and capable of ignoring the role that inefficient capital markets and the private capture of geo-rent has upon the formation of land market cycles.

The Senate inquiry must critically reconsider simple claims that high housing prices stem from a shortage of housing. If we are faced with a genuine mismatch between supply and demand, rents would have risen dramatically. They have not, except for a short period between 2007 and 2010. A solitary focus upon supply and demand is a convenient distraction from the twin determinants of land market bubbles: liberal lending standards and non-taxation of land. These factors are common threads explaining more than 180 years of land market data and cycles across fundamentally different economic periods: the early decades of the newly established colonies, the late 19th century before Federation, the Roaring Twenties, post-WW2 social democracy and the current era of neoliberal capitalism.

Two Recommendations

The damage wrought by regular land market cycles implies Australia's largest bubble on record poses a significant threat to future financial and economic stability. All levels of government must engage in significant policy reform regarding the FIRE sector and taxation system to supress speculation. A return to housing affordability in Australia requires directly targeting the impulse of the banking system to lend out too much credit and landowners' capture of geo-rent. To affect the greatest possible change, financial and economic reforms must prioritise the implementation of a land value tax (LVT) and macroprudential regulations.

Recommendation 1: Reform Land Value Tax.

The ideal tool to moderate land bubbles and properly fund infrastructure already exists in the hands of state and territory governments: state land tax (SLT). Unfortunately, this tax has been so riddled with exemptions and concessional treatments it must be considered dormant. The states show no interest in, for instance, removing conveyancing stamp duty or payroll tax – both inefficient taxes – and funding this by also removing exemptions from SLT. They fear the political consequences, despite land tax being the most efficient and highly equitable tax.

We suggest the current government introduce a nationwide one per cent federal land tax (FLT) – fully rebatable on SLT paid – to oblige the states and territories to use their taxing powers properly. State governments could adjust their tax rules and keep every dollar the FLT raises, to the benefit of all Australians. The Commonwealth Parliament would be entitled to argue this intervention is for sound economic reasons and dissipate the political fallout. Placing state and territory finances on sound bases would vastly improve the federal system mandated by Australia's Constitution. Transitional arrangements would need to be considered. Rebating all stamp duty paid against a hypothetical past SLT obligation would address concerns of fairness and equity.

Recommendation 2: Macroprudential Regulation.

A range of macro-prudential tools are needed to moderate housing price inflation and subdue credit growth in a pro-cyclical financial system, such as those affecting the loan to value, (LVR), debt servicing (DSR) and debt servicing to income (DSTI) ratios. Quantitative restrictions should be placed on the share of new mortgages with moderately high LVRs (60 to 79 per cent), and significantly strengthened for mortgages with an LVR of 80 to 89 per cent. Mortgages with an LVR of 90 per cent and above, interest-only loans and those backed by parental guarantee should be disallowed. Mortgage debt should be capped at a multiple of ten times the imputed or actual annual rental income of the property being purchased to prevent a positive feedback loop forming between rising housing prices and debt.

To reduce systemic risk, a large rise in capital and liquidity ratios (buffers) is required to ensure banks can withstand a future economic downturn, bank run or large fall in the value of collateral. Research suggests the probability of a banking crisis can be reduced to a 1 in 100 year event by raising core equity (Tier 1) capital ratios to 11 per cent in isolation or raising core equity to 10 per cent with an addition rise in liquid assets of 12.5 per cent (the rise in liquid assets over total assets). For the Big Four banks, this would represent a rise of around 3 per cent in core equity. Liquidity and capital buffers should rise in a counter-cyclical fashion during the expansionary phase of the credit cycle, thus taming the size and duration of a debt-financed asset boom. A transition towards higher backing for deposits would enhance financial stability, reduce inflation, minimise public and private debt, restrict over-lending and promote economic growth. The macroprudential toolbox should empower regulators to compel additional capital requirements in investment sectors prone to irrational exuberance; typically residential and commercial land and the stock market.

Conclusion

In Australia, the FIRE sector is not playing by the rules; bankers are extracting economic rent via wide net interest margins on a colossal stock of mortgage debt, while the unearned increment in rental and land prices flow to those holding property. The popular wealth "creation" strategy of speculating on land prices has dramatically eroded housing affordability and created an almost insurmountable gulf to overcome for many potential homeowners. These outcomes are promoted by a flawed taxation system granting low property and land taxes, a mountain of housing tax expenditures valued in the tens of billions of dollars annually and financial deregulation permitting the issuance of large amounts of private debt. Investor preferences are reinforced by urban folklore backed by government and FIRE sector public relations campaigns stating housing is a solid investment, with a permanent and growing stream of wealth and income. A prohibitive entry point for housing symbolises a triumph of self-interest over the national good, as benefits flow to those Australians who already owned or invested before prices began to inflate during the mid-1990s. Families entering this grossly inflated market bear a heavy burden: decades of dutiful employment and stress to pay down ever larger debts. Enormous mortgages detract from national living standards, given a greater proportion of household income is diverted to mortgage repayments.

Ten years following the Productivity Commission inquiry that recommended reforms to improve housing affordability, all levels of government have worsened market inefficiencies by cynically maintaining and enacting policies which actually inflate housing prices. The inertia regarding housing and taxation policy reform is partially a consequence of the states' over-reliance on conveyancing stamp duty revenue, the fear of a significant fall in housing prices and a serious voter backlash. Political cowardice is expressed in absurd double-speak statements: "Improving housing affordability *does not* mean reducing the value of existing homes, which are usually the primary asset of any individual or family." The tolerance of housing policies that maintain bubble-inflated prices, ignore objective evidence, contradict the recommendations of earlier inquiries, and erode housing affordability, are entirely predictable. Property ownership and speculation has been elevated to the status of religion in Australia, compounded by a perverse culture of homeowner entitlement driven by a degenerate taxation system that penalises effort and innovation, while rewarding speculation.

Long-term vision requires superficial and populist politics be discarded in favour of aggressive taxation and financial reforms that drive down land prices; principally by implementing a comprehensive LVT. As economists Adam Smith and Henry George noted, land is a unique gift of nature whose value is determined by society; its revenues are long overdue to be shared for the benefit of all Australians, not just pocketed by the wealthy. An immediate productivity windfall flows from lower housing prices, improving business competitiveness and lowering cost-of-living pressures. A sufficiently large LVT applied to all forms of land could prevent, or at least minimize, the regular land market cycle observed throughout Australian history since early colonial times. The bursting of land bubbles create horrific costs which most often fall upon the poorest: those who never gained during the boom and have no decision-making power or political influence.

"Cranks? Us? Sure, we're cranks – we believe that taxes are legalised robbery, for one thing! The hired guns of the academic world, bankrolled by bankers and railroad barons, couldn't argue with Henry George on the merits of his arguments, so they kept calling him a crank. But it was George who pointed out that ' ...a crank is a little thing that turns and makes revolutions....' " Mason Gaffney

Financial Rules for Constructing a Strong State

Fred Harrison

China is now in the unique position of being able to learn from the tragedies of Western nations, to create a post-capitalist society based on the freedom and equality of all citizens. This can be achieved if the financial system is constructed on respect for the division between what the individual citizen may retain as private property, and what must be recognised as the property of society. Western nation-states failed to honour that distinction. The result was the evolution of politically Weak States, which were hostages of a statecraft based on greed.

Property rights, and their impact on the distribution of a nation's income, were long ago recognised as being at the root of socially significant problems (like the division of the population into classes, the institutionalisation of poverty, and systematic degradation of natural habitats). That is why Western political philosophers wrestled with the problem of property ever since the ancient Greeks. They attempted to identify the terms on which to combine a strong State with freedom of the individual. How can power be shaped to serve the best interests of both the individual and of the State? Ancient civilisations failed to develop solutions of the kind that could sustain their societies.

Plato, in his *Republic* (Chapter 5), chose to avoid the problem by abolishing property. The power to make decisions would rest with the people who were trained as the guardians of society. In this utopian state, the people had to trust the guardians to act for the common good. But no society has succeeded in creating sustainable arrangements in which private property was abolished. So the problem of how to reconstruct power remains with us. Effective reforms are impossible without first understanding why private property is the cause of problems like endemic poverty. Before we can elaborate an answer to that question, we need to define what is meant by a strong State.

A strong State is one that is not vulnerable to manipulation by influential groups. Or, to put it another way, a strong State is one in which the population is composed of citizens who are equal. No one group of people can exercise undemocratic influence to secure privileges *at the expense of others*.

Military power is not an indicator of a strong State. A State that relies on coercive power to maintain order is in a weak position. It is a weak State because it has to either use force to control its citizens, or to deploy force against other nations to capture natural resources to satisfy the demands of its social elites.

A Strong State, then, is one that evolves on the basis of three principles.

1. It does not need to exercise coercive power over its citizens to maintain civil order.

2. It is authorised by the people to administer civil society on the basis of treating everyone as equals, as determined by the principles of natural justice.

Its mandate is to produce and renew the social infrastructure that people, as individuals, cannot provide for themselves.

Nation building is complex. Social equilibrium, expressed as a practical balance in the distribution of power, needs to be achieved between the public and private sectors in the economy, between government and the population in politics, between materialism and morality in aesthetics. This means that freedom does not turn into anarchy, and order is not imposed by the tools of despotism. This ideal system has not yet been achieved in the West, and the principles for its achievement have eluded philosophers. That is why they have relieved themselves of their frustrations by seeking solace in utopian escapism.

Can we now specify the conditions for emancipating the creativity of all members of society in ways that would constitute a fair and efficient system, as represented by our notion of a strong State?

The Role of Rent

At the heart of the challenge is the way in which a society owns and uses the resource that is needed to create and sustain the culture of the people. That resource is a flow of value, or income, which does not include the income needed to sustain the individual household economy; and the income needed to form capital, which raises the productivity of labour.

What is that flow of value called, and where does it come from? Through the genius of people in the earliest civilisations, a sophisticated market mechanism was created to identify that part of a population's resources that were not the wages of Labour or the profits of Capital. In classical political economy, that third category is called economic rent. The earliest urban civilisations emerged when rents were reserved to fund the infrastructure required by complex settlements.

A healthy society achieves sustainable equilibrium when rents are allocated and used to fund the "common good". It is when rents are privatised that society shifts towards despotism. So it is critical for the long-term survival of society that the correct rules are elaborated to measure and collect rents as they are produced; decide how to spend the rents; and guarantee everyone's equal access to the benefits that flow from the expenditure of those rents.

By studying how a nation resolves these issues, we are able to infer the character of its culture. That information reveals the nature of personal freedoms, the quality of governance, how the natural habitat is treated, and whether the State is fit for its purpose of serving the whole population.

In European, about 500 years ago, a few people (the feudal aristocrats) began to appropriate the rents for their personal use. One result was the perversion of the two pricing mechanisms:

- prices charged in private markets for consumer goods, and prices (taxes) charged to fund public services.

- By resolving the contradictions that create the tensions between these two pricing mechanisms, it is possible to integrate the public and private sectors so that they work together in harmony.

At present, people who earn their incomes by working in the private sector are hostile to government, because of what they perceive as the injustices associated with the taxes they pay. This creates social stresses that weaken the State. The objective of good governance should be to synchronise the two pricing mechanisms so that they complement each other. The goal is maximum satisfaction for individual citizens and the welfare of society.

The Volume of Rent

This thesis places a heavy burden on rent as a stream of revenue. So the first practical question is this: does a population generate sufficient rent to fund all the public services they need? There is no reliable answer to this question in the economic literature. Why? Most governments devote substantial funds to statistically measure activity in their economies, so why is the flow of rent as a percentage of national income a mystery? The answer reveals something important about the distribution of power in society. To work out the facts, we have to go back to the origins of the modern economy and the politics of State formation.

In the 17th century, an English philosopher, John Locke, wrote Two Treatises on Government (1689). This was a seminal document. It influenced the politicians who shaped the formation of the liberal

State. It was quoted by the Founding Fathers of the United States of America. Locke argued that, in the state of nature, every person had a natural right to "life, liberty, and estate" (estate was the old English word for land). He argued that people consented to enter into civil society to protect their property. But nature – planet Earth – could not be privately owned. Why? Because people could only own as private property those things in which they had mixed their labour. So, viewed in terms of a flow of income, according to Locke there were two categories: the income of labour, and that share of income that could be attributed to nature.

To determine the legitimate distribution of income, we need to know the value that has to be assigned to the services delivered by nature (like the fossil fuels that yield energy that can be translated as the rents of oil, or of coal, or of the power of wind). On this issue Locke was less than honest. It appears that he did not wish to disappoint the aristocrats who controlled the public budget. For he claimed, in Chapter 5 of his Treatise, that the rent attributable to nature was just 1% of total income. The rest (99% of the flow of national income) was value created by the labour of the individual. He remained silent on the value created by the services of society. Today, the West's economists claim in their textbooks that rent ranges from 1% to 6% of national income (drawing on USA data).

Nobel Prize economist Paul Krugman claims that, in 2004, the USA apparently generated "rent" of just 1% of total income (Krugman and Wells 2006: 283). Examples spanning the years since 1945 reveal how statistics were manipulated to under-state the quantum of rent.

Nobel Prize economist Paul Samuelson published the first edition of Economics in 1948. Charging rents for the use of natural resources, he explained, "may slow down their rate of depletion and serve to ration out such scarce, exhaustible resources. But in a freely competitive system, the self-interest of owners may well lead to the rapid using up of natural resources…. Unsightly and unhealthy slag piles may also be created…There may be deforestation that causes floods and soil erosion downstream…" (Samuelson 1955: 539). This is a scary prognosis! But aren't these abuses of nature associated with the current fiscal regime, which largely fails to charge rent for the use of those resources? Samuelson does concede that "Pure land rent is in the nature of a 'surplus' which can be taxed heavily without distorting production incentives or efficiency" (1955: 535). But why bother to isolate rent as a special income category when the "Rent income of persons" is shown (on page 182) as just 3% of Net National Product? Not enough revenue here to fund public services!

In a later edition of Economics co-authored with a Yale professor, Samuelson reports the "Rent income of persons" as less than 2% of Gross National Product (Samuelson and Nordhaus 1985: 115). Drawing revenue from pure rents might be fair, and might be efficient, but the sum is obviously too trivial to target!

In 1963, Richard Lipsey's textbook assured students that "an effective tax on economic rent would finance only a tiny portion of government expenditures" (Lipsey 1979: 371). Besides, there was a grave problem with the proposal: "The policy implications of taxing rent depends on being able in practice to identify economic rent. At best, this is difficult; at worst, it is impossible" (1979: 370, emphasis added). Real estate professionals perform this exercise every day for their clients, but in Western universities the students are taught that the task is impossible!

Heinz Kohler, a Germany economist, repeats the myths about not being able to isolate economic rent, and that rents would not yield sufficient revenue to cover government expenses (Kohler 1992: 857). His textbook is an example of the damage such manuals inflict on people who need to live in the real world. He claims that, when California imposed a limit on increases in the tax on real estate in 1978, by the mid-1980s "an unexpected consequence had emerged" (Kohler 1992: 859, n.13). For every $1 decrease in the property tax, property values rose by $7. Why were economists surprised at this outcome? Fiscal reformers predicted that holding down the property tax would translate into higher prices for residential land. They were correct. But for academics in their intellectual fortresses, this result could not be anticipated. So California's voters were not guided away from what proved to be a disastrous decision for families who needed homes that they could afford.

The reality is that rent constitutes something like 50% of a modern nation's income. How can we validate this claim?

To excavate the truth, we have to return to the writings of John Locke. He examined the financial impact of taxes. In Some Considerations of the Lowering of Interest and the Raising the Value of Money (1691), he explained that it would be "in vain" for a country to impose taxes on anything other than land, for "there at least it will terminate". The merchant won't bear taxes, and the labourer on subsistence wages cannot bear them. So taxes are

passed on, through the marketplace, in the form of higher prices. But someone must pay! Who? Locke was emphatic: taxes are ultimately drawn out of a nation's rents (Locke's reasoning appears in full in Harrison 2012: 184). This leads to an important economic insight. Taxes, if they are imposed on Labour and Capital to be paid out of wages and profits, reduce the income left in the hands of labourers and the owners of capital. This means they have less income left to pay as rent to land owners.

Locke's thesis tells us something of vital importance about the nature of the revenue that is collected as taxes on labour and capital. In reality, that revenue is rent in disguise. We see the dynamics of this reality at work every day, as when a government reduces a tax on wages or profits. The net gain does not surface as higher real wages for labour, or real returns for capital. Through the competitive process, the gains are translated into higher rents paid to those who own the land.

In the past, land owners who controlled tax policy did not welcome Locke's insight. They wanted to believe that, by cutting the Land Tax and imposing taxes on their peasant populations (such as the tax on the consumption of salt), they could reduce the share of the rent they paid to the State. That appeared to be the case, but it was all appearances. For, at the same time, the amount of rent the peasants could pay to their landlords was reduced. It was this struggle to control rent that caused social chaos in the form of mass unemployment, the under-production of wealth, debt and inflation and the division of the population into hostile classes. That struggle remains with us in the West to this day.

Adding up Rent

Locke's thesis is most thoroughly explored by Mason Gaffney, who taught economics at the University of California. He formulated an acronym for Locke's thesis: ATCOR. All taxes come out of rent (see Addendum).

The first step in calculating the size of a nation's rents is to establish the amount people pay through "taxes" levied by government. In 2013, tax revenues collected by US federal, state and local governments added up to $5.3 trillion (GDP: $16.2 trillion). Using the ATCOR formula, we may conclude that, if America was a tax-free zone, this revenue would surface in the marketplace as rent. In other words, under present tax policies, about one-third of US income is transformed from rent into "wages" and "profits" via painful political illusions.

But if revenue collected by government is ultimately out of rent, why bother to collect that revenue directly? One reason is that collecting rent directly would raise the productivity of the population. Why? Because (to use the technical term) taxes cause "deadweight losses". The gains from abolishing taxes on wages and collecting rents in a direct way to fund public services would have an enormous impact on people's lives. Nicolaus Tideman, a professor of economics at Virginia Tech and State University, estimates that, after five years into the fiscal reform, the average American family would be better off by $6,300 (Tideman 2013).

Rents in Private Pockets

The next question relates to the proportion of a nation's revenue that is visible as rent. This is rent that is not collected by government. Western economists have no idea how much rent remains in private ownership. The prudent estimate is that rents in private pockets amount to about 20% of national income.

In the UK, researchers found that rent was 22% of national income in 1985, rising to 29% in 1989 (Banks 1989: 40, Table 2:II). But 1989 was a peak year in the property cycle. Rents dropped in the recession of 1992. Allowing for the distortions caused by land speculation, the "normal" year estimate for the UK would be for 1987: 21.8%.

In Australia, researchers – armed with one of the best official data sets in the world – calculated that rent in private hands in 2012 was about 24% of GDP (Putland 2013; Fitzgerald 2013). Rents in that year were inflated by abnormally high urban and commodity prices (this was one of the ripple effects of trade with China).

If we conservatively assume that privately collected rents are about 20% of national income, what would be a robust estimate for the value of all rents generated by mature industrial economies today?

If we take a random selection of 10 rich nations, ranging from Australia through the USA to Sweden, Germany and Japan, the average tax-take as a percent of GDP is 37%. In ATCOR terms, most of this is rent in its disguised form (collected as if they were "wages" and "profits"). If we add to this the rent that is not collected by government, of around 20%, we discover that rent exceeds 50% of national income. This first approximation of rent needs to be adjusted.

Taxes distort the total income. They encourage the

under-use of urban land (which artificially raises rents). Tax policy also motivates behaviour in ways that damage the environment, as when polluters are not obliged to pay for dumping waste into the atmosphere (which artificially reduces rents in some urban locations).

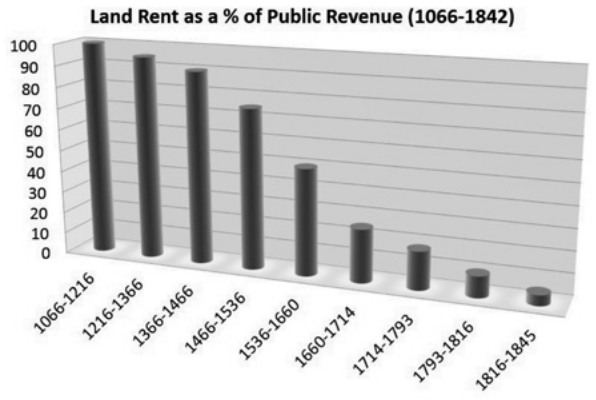
A small part of tax revenue may actually come out of wages, because the workers lack the bargaining power to shift the taxes onto rent.

Revenue currently collected by the property tax falls largely on economic rent.

Taking such considerations into account, we may cautiously estimate that rent is about 50% of total income. This is more than sufficient to cover existing government financial obligations.

History and Public Finance

Citizens are intuitively aware that there is something fundamentally wrong with tax policy. In England a thousand years ago, the State's revenue was exclusively from rent; 500 years ago, the land grabbers got to work. The chart below tracks the reduction of rent as a proportion of public revenue. It records how England became a weak State with a dishonest form of governance. Evidence of this weakness can be inferred from the way land owners exercised power to manipulate laws to secure special privileges from the State.



Europe's weak States were responsible for two world wars. And yet, the knowledge needed to avoid such outcomes was available to statesmen in the 18th century. The Industrial Revolution made it possible for everyone to prosper. What went wrong may be illustrated with the work of Wilhelm von Humboldt (1767-1835), a civil servant who established the University of Berlin. In The Limits of State Action, first published in 1852, he sought to describe how the State could be controlled.

Individual freedom, von Humboldt argued, was maximised when education was tailored to treat people as ends, not means. The State's role was to help people realise their potential. But how could citizens constrain the State, which commanded the instruments of coercion? Von Humboldt is not convincing in his answers. According to my thesis, revenue is the key.

The State needs revenue to fund public services, as von Humboldt noted. But on what terms would that revenue be raised? Who decided how the revenue is raised, and how much is handed to government? The answers are to be found in the unique character of rent, and the social function performed by the land market. Through that market, the people themselves negotiate the rents they are able to pay to use the ecological and social services available at each location. By this process of free negotiation, who paid, and how much they paid, is determined by citizens, not politicians or servants of the State.

In the 18th century, the French Physiocrat school of philosophy explained that rent was the correct source of revenue for the State. Adam Smith repeated this recommendation in The Wealth of Nations (1776). But while von Humboldt confessed his "ignorance of everything concerned with finance" (1993: 134), he felt free to pronounce on tax policy. The Physiocratic rent policy was "unquestionably the simplest" was to raise revenue, he wrote, but "human power" must also be "subject likewise to direct taxation" (1993: 135: emphasis added).

If people like von Humboldt, who contributed to Germany's zeitgeist, had helped to shape the State according to Physiocratic financial principles, that nation would have travelled a different path of social evolution. If everyone in Germany had enjoyed increased prosperity and social security, this happy state of affairs would not have led to the colonial land grab in Africa in competition with other European States (especially the UK, Spain, Portugal and Italy). It was that muscle-flexing mission which (among other reasons) was responsible for drawing a weak German State into war with its neighbours in 1914.

Transforming the Weak State

By restructuring the public's finances, economic growth would be raised above historic rates. The important gains would take the form of more leisure for people, the freedom to deepen human relationships, and a stronger cultural membrane which wraps everyone in its riches (like the arts).

Politics would mutate into an authentic democratic

process. Politicians would no longer be able to buy votes by funding projects which favoured special interests groups. The State would be strengthened on foundations of fairness.

In the West, the trend is in the opposite direction. In the 1980s, the trans-Atlantic nations began to shed their industrial status in favour of a rent-seeking culture. Whole populations now have to try to survive by participating in the arts of cheating. One example: the middle-class exercise in buying and selling houses to accumulate capital gains. This is a culture of cheating because it enables some people to live off the labours of others.

The Western State treats the land market as a slush fund. Either directly or indirectly, this rewards corrupt behaviour in the financial sector, in the media, law-enforcement agencies…. and, of course, in politics. The law on property rights legitimises the transfer of the common wealth to the privileged few, resulting in the rape of culture and the environment. An authentic democracy would not tolerate this tragedy. The People's Republic of China need not become a victim of this social pathology, because it has passed a law which reserves land as public property. Its next step must be to guarantee that the rent that represents the services of nature and society are collected for the benefit of everyone in society.

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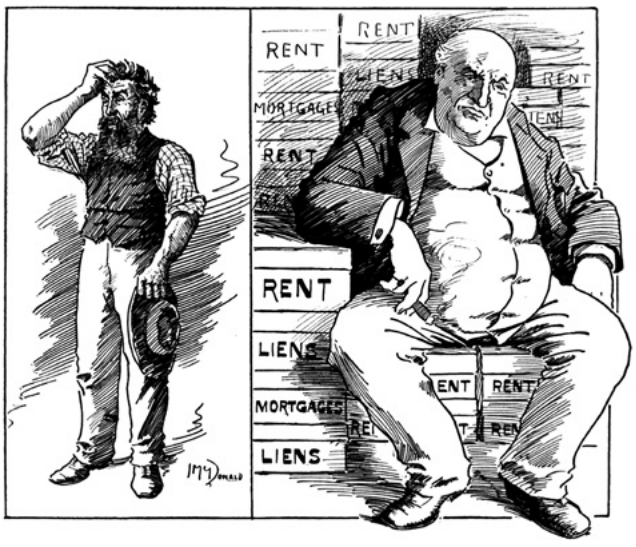
About the Author:

Fred Harrison is a graduate of the Universities of Oxford and London. He is the author of many books on the economics of rent, including The Traumatised Society (London, 2012). He is Research Director of the Land Research Trust, London. He was the economist who gave a 10-year forecast of the economic crisis that began in 2008. He warned the British Government in 1997 that the West's house price bubble would peak in 2007, followed by a collapse that would trigger a global depression.



WHAT'S NEXT- PRIVATISING THE SHADE?

Under the current economic system 'privatising the shade' may well be the next profit-seeking frontier. From water to DNA to our seeds, it's all apparently open to monopolisation.

This doesn't reflect the entrepreneurial culture we were brought up to believe in with the mantra 'the harder you work, the luckier you get'.

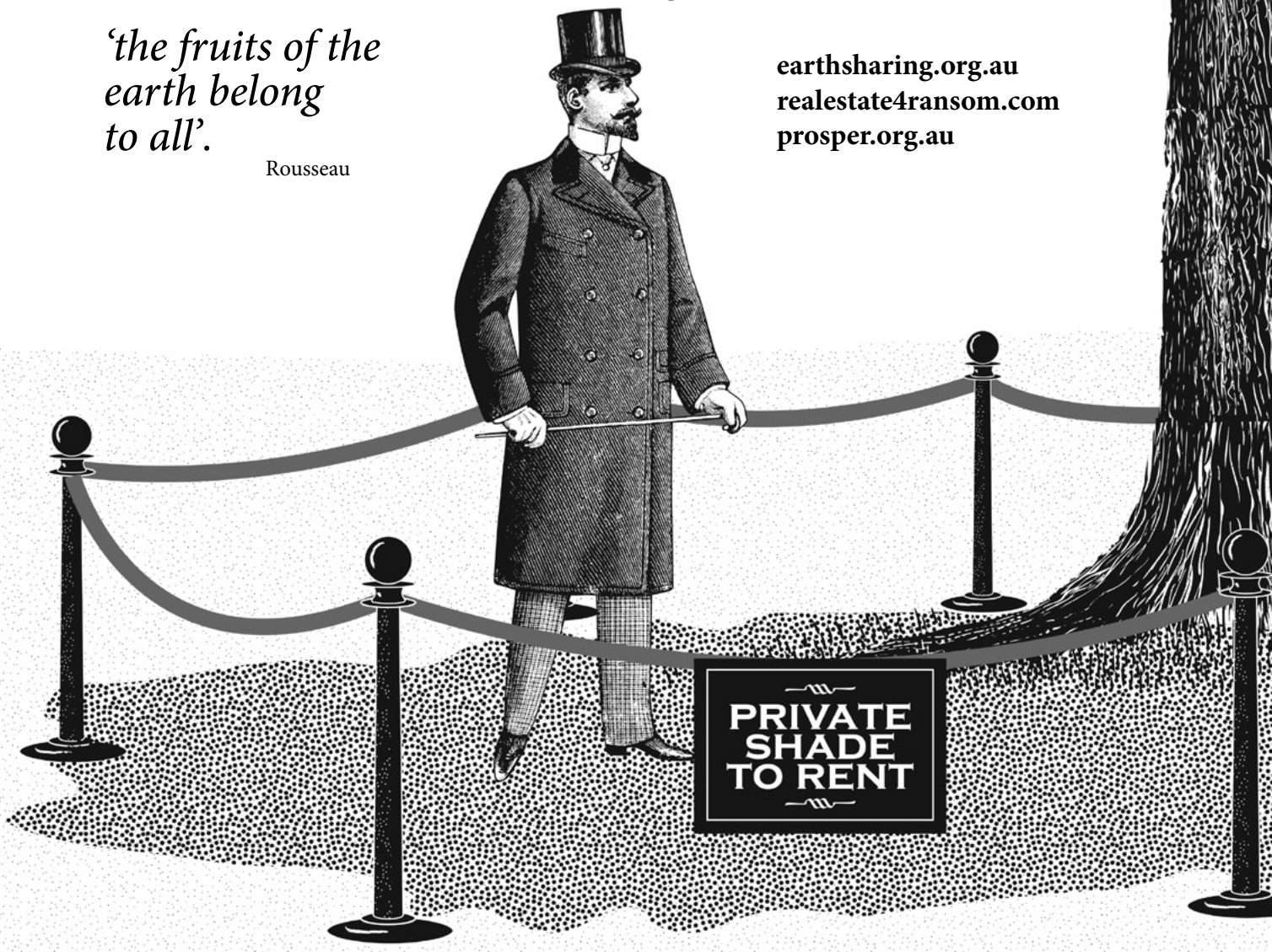
Nature's bounty should not be privatised because:

- It will naturally increase in value - even with no productive work by the 'owner'.
- The access price will increase to cover shareholder returns and debt-based interest.
- Workers are taxed (for being productive) whilst the 'owners' of the earth make money in their sleep → wealth gap, sustainability pressures.

'the fruits of the earth belong to all'.

Rousseau

earthsharing.org.au
realestate4ransom.com
prosper.org.au



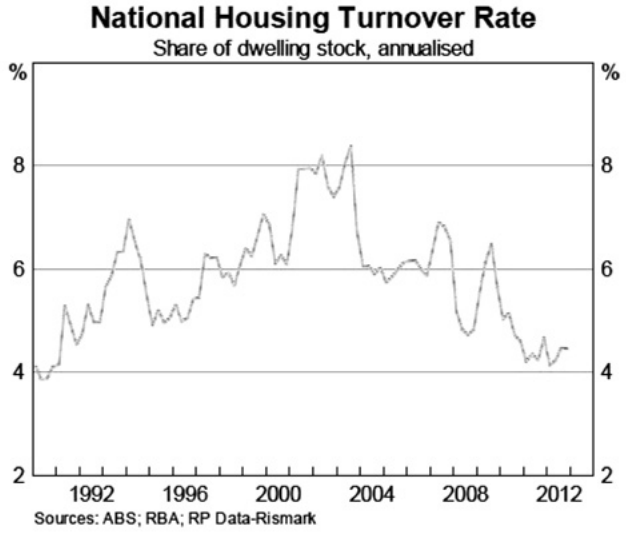
It's Time to Shift States to Land Tax *By Leith van Onselen*

THE DECLINE IN STAMP DUTY RECEIPTS IS POSING PROBLEMS FOR AUSTRALIA'S STATE & TERRITORY GOVERNMENTS.

Stamp duty is an inherently volatile source of taxation revenue, since it is critically dependent on both the volume of housing transfers as well as the price at which those homes transact. During the early-to-mid 2000s boom, when both prices and transactions soared (see next chart), the states found themselves awash with cash, with total stamp duty collections rising by over 150% in the eight years to 2007-08. Since that time, however, stamp duty revenues have fallen by -18%, putting the squeeze on state and territory finances that had become accustomed to the good times.

The volatile nature of stamp duty receipts adds further weight to arguments for reform on both equity and efficiency grounds.

Stamp duties unfairly penalise people that move to homes that better suit their needs. Obvious examples include baby boomers downsizing from large family homes and young growing families upsizing to bigger family-friendly homes. Such disincentives inevitably lead to an inefficient use of the housing stock, such as empty nesters occupying large homes with multiple spare bedrooms. Stamp duties also hinder labour mobility since they discourage workers from relocating closer to employment.



As shown in the above RBA chart, just over 4% of the housing stock is currently transacted annually. Accordingly, we have the crazy situation where a small minority of households are paying taxes that support services for the whole community – all for the privilege of moving to a home that better suits their needs!

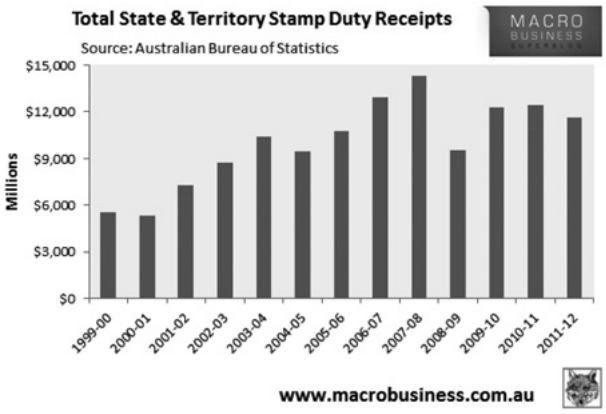
As shown in the below chart, stamp duties can chew-up tens-of-thousands of dollars when purchasing a median priced home. Seeing as we all consume government services, wouldn't it then be fairer and more efficient to levy each household a much smaller amount, rather than penalising only a small minority with huge tax bills?

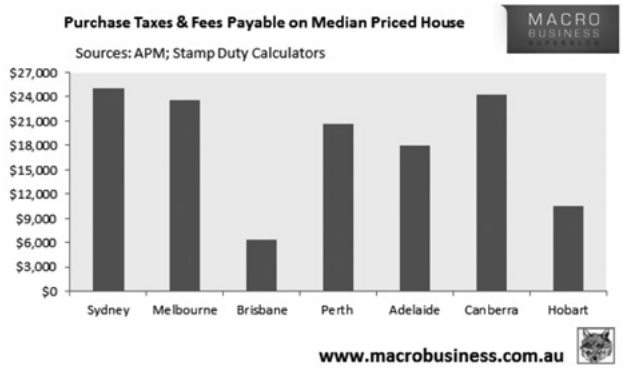
A fairer way of sharing the tax burden would be to abolish stamp duties and extend land taxes currently applied on investment properties to one's principal place of residence. As shown by the next chart, land tax receipts have proven to be a remarkably stable source of revenue when compared against stamp duties, since they are not affected by transaction volumes.

Broad-based land value taxes (LVT) would also assist in the provision of new housing via two channels. First, an LVT would help make infrastructure investments self-funding for governments, since any land value uplift brought about through increased infrastructure investment (e.g. new roads, trains, etc) would be partly captured by the government via increased LVT receipts. Accordingly, governments

would be more likely to facilitate development, rather than act to restrict it in a bid to save on infrastructure costs. Second, an LVT would penalise land banking and vagrancy, effectively increasing the supply of land in the process and bringing new homes to market more quickly.

As with any change to the tax system, there are transitional issues that would need to be worked through in shifting from stamp duties to a broad-based LVT.

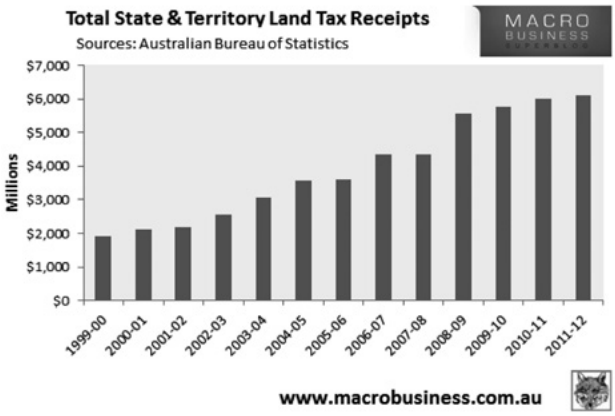




One concern is that those who recently purchased a property (and paid stamp duty) would be double-taxed via an LVT. A logical solution is to credit all landowners with the amount of stamp duty paid and then deduct the hypothetical land tax they would have paid since the date of purchase.

Another concern is that asset rich, cash poor, retirees could be left with LVT bills they cannot pay, requiring them to sell their homes. A logical solution is to allow these people to accumulate their LVT liability, with the bill payable upon death (via the estate) or once the house is eventually sold (whichever comes first).

Last year, the ACT Government announced the bold (and sensible) plan to transition out of stamp duty over 20 years, replacing it with a broad-based land tax levied via an increase in property rates. Reforming stamp duty was also a



recommendation of the Henry Tax Review, which characterised stamp duty as an inefficient tax, and recommended replacing it with broad-based LVT levied on all properties.

The options are there, and with stamp duty revenues shrinking, it is in the state and territory governments' financial interest to pursue reform and change the tax mix.

unconventionaleconomist@hotmail.com

www.twitter.com/leithvo

"The Land Boomers" *by Peter Ryan*

It was my privilege, over almost half a century, to have followed in intimate detail the triumphant "best-seller" course of one of the most remarkable Australian books of all time: *The Land Boomers*, by Michael Cannon. No full understanding of the concluding decades of the Colony of Victoria, nor the subtler character even to this day of its jewelled city Melbourne, is possible without some apprehension of the land boom era, and of its appalling "bust".

For reasons which escape my understanding, the publisher over recent years has ceased to put copies into the bookshops – "Out of print". More reprehensibly, the author himself seems to have been left in the dark about the intended future fate of his great work.

No matter. The publication last month of a fresh edition, liberally illustrated and with a new Author's Introduction makes us look ahead rather than backward, not so much a happy ending to *The Land Boomers* as its resurgent continuation.

Michael Cannon tells his absorbing, often scandalous story with verve and clarity. We see the respectable middle classes hurling their money away as madly as any drunken sailor, frantic to "get rich quick" through wildly inflating land prices and "development".

We see supposedly upright and conservative bankers and other business leaders throwing caution overboard out of similar breathless greed. Some of these were themselves dupes of the delusion. All too many others were mere brigands in shiny silk top hats consciously setting forth to swindle humbler citizens of their lifetime nest eggs.

The Melbourne mood was all wild optimism: "We're all going to be millionaires! Every blessed one of us!" Came the bust. Proudly independent "comfortable" families dismissed their troops of long-serving retainers, and then themselves became dependent on the dreaded "paying guest" to meet their own grocers bills; ordinary workers were simply sacked in their thousands, starving with their families as they tried to beg bread on the streets, or scavenge among the scraps in Melbourne's garbage cans. Lacking any system of organised state relief, churches, charities and citizens of good will tried to sustain them. For example, it was recorded that "200 souls were Maintained at Werribee Sewage Farm at an average cost of Sevenpence ha'penny a week". (One forbears to inquire what they were eating.)

The land boomers themselves seem to have included a remarkably high proportion of what poet Rabble Burns would have called the "uncommon good": stern teetotallers, wowsers, sabbatarians, churchgoers, vestrymen, pew-renters, puritans of every Stripe. Their mortification when their bubble burst was extreme, and their efforts to suppress the story strenuous and largely successful.

Victoria's bankruptcy laws were shamelessly rigged so that outrageous defaulters could escape in secret. Honest judges were threatened with removal. Eighty years later I knew two Melbourne scholars of high achievement and blameless academic reputation who would almost blush if the land boom were mentioned; their well-known grandfathers had played an equivocal role in that boom so long ago.

When Cannon sought help with his researches at the Public Library in 1963 that vast repository could point to no more than a single chapter in H.G. Turner's conservative History of the Colony of Victoria published in 1904. Only that trace remained about a trauma which had rocked the colony to its foundations!

The arrival at the State Archives of a series of wooden crates from the Crown Law Office transformed Cannon's resources. The crates contained dust-coated original records of the

Bankruptcy jurisdiction, court transcripts of evidence, old company files and indeed most of the bare facts needed to piece together the tales of horrid fascination which The Land Boomers tells.

The feat of analysis and reconstruction of all this material would have been a challenge to any mature and hardened research scholar; it was brilliantly performed by a young man who lacked a single hour of research experience or university training.

The outstanding quality of this "amateur" manuscript was testified by two impeccable authorities: Sir Hugh Brain, after nearly a lifetime experience in the Collins House Group of companies, a familiar with the powerful magnate William Lawrence Baillieu and the Baillieu family interests. Brain said that Michael had got the business side right, and furthermore helped him with additional rare documentation. Then Australia's pre-eminent historian Geoffrey Blainey pronounced it to be sound and important history.

With such distinguished support, the manuscript was swiftly adopted for publication by the Board of Management of Melbourne University Press: this despite the unease of the Vice- Chancellor, and murmurs of the risk of the Baillieu family withdrawing its support for the university library and the nascent archives department.

The book was published in 1966 to sensational acclaim, and a fresh printing was required within days — and then promptly another one — to satisfy exuberant demand. It almost seemed as if the sedulous cover-up of the Edwardian years had bottled up latent curiosity under pressure.

Hundreds of copies were sold to lawyers summoned to advise upper-crust families on whether they might sue for defamation, or otherwise put Cannon's "vile book" out of circulation. Over the teacups at Darren Baillieu's Toorak mansion, council of war was held by the family over how "The Land Boomers" might be silenced or smothered.

Not one writ was ever issued by anyone, and for about the next forty-six years, through at least ten different impressions and various editions, *The Land Boomers* has continued to share with its readers its rich freight of wisdom and warning, and the entertainment of a lively, racy yarn.

The author's new introduction to the fresh edition enables him to do not only the usual minor corrections and tidying up, but also to deal with one new matter of substance. A Melbourne academic (encouraged by the Baillieu family) last year published a scholarly volume entitled William Lawrence Baillieu, Founder of Australia's Greatest Business Empire. Says Cannon, the book "seems to me to worsen the case against W.L.'s boom-time activities, making his financial recovery after the crash even more astonishing". Clearly The Land Boomers still surges with active life. To help modern minds grasp the immensity of the disaster of the 1890's, Cannon cites the example of Benjamin Fink: when that super-boomer went bung for 1,800,000 pounds, his debts would have been worth some $300,000,000 today…….

Reprinted with kind permission from Quadrant Magazine, April 2013

The Land Boomers by Michael Cannon. Melbourne University Press 3rd Edition 2014

Geoists in history *by Karl Williams*

Herbert Asquith (1852-1928)

Each fragile, wounded human being is a mass of contradictions and, despite the enormity of his accomplishments, Herbert Henry Asquith was no exception. Until 1988 he was the longest continuously serving British prime minister in the 20th century, is considered the founder of the British welfare state, and was the prime minister who blundered (rather than led) the British Empire into the monumental debacle that was World War 1.

There was nothing particularly noteworthy in his birth and early years, born into an unremarkable middle-class Yorkshire family. Herbert was seven years old when his father died, after which he and his family moved into his maternal grandfather's home. Four years later Fate handed him a break and young Herbert, his keen ambition already stirring, grabbed it with both hands. As we see so often, a solid education often sets up a person for life.

At the age of 11 Herbert was sent to London with his brother to live with relatives and attend the City of London School, then under a celebrated headmaster, Dr. Edwin Abbott. Young Asquith distinguished himself as a classical scholar and, more pertinent to his ultimate career, developed remarkable talents as a public speaker. Winning a classical scholarship, he entered Balliol College, Oxford, in 1870. There he achieved first-class honors in humane letters and, unusually for someone not from the upper class, attained the great honor of being made president of the Oxford Union.

Switching direction, he chose not classical studies but the law for his career and was soon admitted to the bar in 1876, but at first found it difficult to develop his legal practice. He married "well" (i.e. into a fair bit of money), and settled in London.

Ambition inevitably drew him into politics, and he entered the House of Commons in 1886 as Liberal member for East Fife, a Scottish constituency which he represented for the next 32 years. His extraordinary maiden speech, which came under the notice of political power-brokers, marked him out for future greatness. As the shifting sands of British party politics would have it, opportunities would drop into his lap shortly.

When William Gladstone and the Liberals returned to power in 1892, Asquith, now 40, was given Cabinet office as home secretary and soon after became deputy leader. His boss at the time was Sir Henry Campbell-Bannerman, who was known to request his presence in parliamentary debate by saying, "Send for the sledge-hammer," referring to Asquith's reliable command of facts and his ability to dominate verbal exchange.

The Liberals were then the most closely aligned party to geoist proposals, including being staunch free traders. Thus Asquith was sent out to shadow and refute the protectionist arguments of Joseph Chamberlain.

Asquith's personal life wasn't straightforward, either. His first wife died in 1891, leaving him with five young children. Three years later he married Emma Tennant, daughter of a wealthy landed aristocrat and a woman distinguished in her own right in intellectual and social circles. Brilliant, vivacious and witty, she was a person altogether different from Asquith's first wife, and seemed a potent force behind Asquith's surge to greatness.

He didn't have to wait long. Although Asquith's political prospects had seemed dimmed by the long Tory rule from 1895, the Conservatives divided and fell apart over the tariff issue in 1903. With Asquith's oratory an instrument of revival, the Liberals reunited and took power in 1905. Asquith

immediately took perhaps the second most powerful position in the British Empire, that of Chancellor of the Exchequer as well as deputy prime minister.

Asquith's extraordinary capacity in the Commons made him a leading spokesman for government policy, and when Campbell-Bannerman resigned as prime minister in 1908, Asquith's succession to the top spot was a matter of course. The Asquith government represented the transition from Gladstonian liberalism with emphasis upon "Peace, Retrenchment and Reform" to the "New Liberalism" of the 20th century with objectives of social and economic reform. Under Asquith the Liberal party reached the height of its power but also suffered the first stages in its disintegration.

Asquith in many ways pioneered the modern welfare state, legislating old age pensions as well as national insurance against illness, disability and unemployment. His chief obstacle was the Conservative-dominated House of Lords but Asquith initially managed to win over the Lords to accept his welfare proposals.

However the dark clouds of war were looming on the horizon and government expenditure escalated alarmingly to further finance their extensive expensive naval arms race with the German Empire. From where would the revenue come now?

To understand the enormity of what erupted soon after, we need to appreciate how relatively commonplace it was for people – the great and the humble – to understand the land issue at the time. In our arrogance, many of us consider that today's economic understanding has evolved beyond and above that of a century ago – the reality was just the opposite! Henry George had set the world – and especially the English-speaking world – alight in the late 19th century, and his influence was still keenly felt in the UK when Asquith's star was on the rise.

Some newcomers to our movement might not realize that the great Winston Churchill – admittedly a political opportunist later in life – was an outspoken geoist. In 1908, Churchill was promoted to the Cabinet as President of the Board of Trade by Asquith and proclaimed:

"It is quite true that land monopoly is not the only monopoly which exists, but it is by far the greatest of monopolies – it is a perpetual monopoly, and it is the mother of all other forms of monopoly."
…. and ….
"I have made speeches by the yard on the subject of land value taxation, and you know what a supporter I am of that policy."

Lloyd George, who was later to succeed Asquith as prime minister, was also a man deeply imbued with geoist principles. When Asquith became prime minister in 1908, Lloyd George was promoted to Chancellor of the Exchequer, a post he held until 1915. In 1909 Lloyd George announced what became known as the People's Budget, a noble failure in the end but a document that almost turned British politics on its head. Lloyd George said:

"Who ordained that the few should have the land of Britain as a perquisite; who made 10,000 people owners of the soil, and the rest of us trespassers in the land of our birth?"
…and…
"Search out every problem, look into these questions thoroughly, and the more thoroughly you look into them you will find that the land is at the root of most of them. Housing, wages, food, health, the development of a virile, independent, manly, Imperial race - you must have a free land system as an essential condition of these."

And Asquith himself, shortly before he took office as PM:

"There can be no fairer and juster claim on the part of the community than to appropriate to its own benefit for public purposes some part, at any rate, of the added value that comes to land of this kind automatically through no effort of any human being, but which is the result of the general and increasing prosperity of the community."

Among the most controversial parliamentary bill in British history, Asquith and George's People's Budget aimed to systematically raise taxes on the rich through a modest version of land value taxation. With the hitherto untouchable ancestral lands of the Lords being directly challenged, the upper classes pulled out every weapon they could muster to stop Asquith's reforms. The Lords did not traditionally interfere with finance bills but nevertheless this was one bill they could never allow, and they vetoed it. Britain now had a full-blown constitutional crisis.

Asquith hit back hard, prevailing upon King Edward VII to threaten to pack the House of Lords by creating new peers. The Lords bowed to this pressure and passed the budget – an event known since as the Constitutional Revolution in England.

Many other Liberal politicians had attacked the peers to force their retreat at this stage, including Lloyd George who famously proclaimed in a speech "a fully-equipped Duke costs as much to keep up as two dreadnoughts (battleships)" and was "less easy to scrap".

Before the People's Budget could be implemented, the Lords dug further into their bag of tricks and eventually forced the country to a general election in January 1910. This election resulted in a hung parliament, with the Liberals having two more seats than the Conservatives, but lacking an overall majority. The Liberals formed a minority government dependent on the support of the Irish Nationalists. Pressure to remove the Lords' veto now came from the Irish MPs, who wanted to remove

the Lords' ability to block the introduction of Irish Home Rule. They played hard-ball politics with Asquith by threatening to vote against the Budget unless they had their way. More and more peripheral issues thus came to threaten to compromise this, the greatest geoist political reform in history.

King Edward VII did eventually consent to fill the House of Lords with freshly-minted Liberal peers who would override the Lords' veto, but only if Asquith agreed to hold another general election. However Edward VII died in May 1910, before this second general election. Asquith had to use his considerable powers of persuasion to get Edward's successor, George V, to agree to the plan. The new king was hesitant, as packing the Lords would undermine the power of the hereditary aristocracy. Before the December 1910 general election (the second that year but the last held for eight years), Asquith's persuasion paid off, and George V agreed to pack the House of Lords.

The Liberals thus won their second election of 1910, though the balance of power in the government still rested with peers from Ireland, who pressed home their demand for a Home Rule bill as the price of support for Asquith's third government.

A fiercely-determined Asquith was now out to curb the powers of the House of Lords for good through the Parliament Act 1911, which greatly limited the power of the House of Lords. This upper chamber of Parliament was then restricted to delaying, but not defeating outright, any bill passed by the House of Commons.

"We hold, as we always have held, that, so far as practicable, local and national taxes which are necessary for public purposes should fall on the publicly-created value rather than on that which is the product of individual enterprise and industry. That does not involve a new or additional burden on taxation, but it would produce these two consequences - first of all, that we should cease to be imposing a burden upon successful enterprise and industry; and next, that the land would come more readily and cheaply into the best use for which it is fitted. These two things would be two potent promoters of industry and progress."

But later in 1911 the Liberals were weakened by political alliances and how the House of Lords utilized its ability to delay passage of bills for up to two years. In a tumultuous European world, they were playing for time. Only by dropping the land tax proposals would the House of Lords allow a budget bill to be passed without delay. The Lords got what they really wanted.

Asquith paid off the Irish block with the Third Irish Home Rule Bill, which achieved the Royal Assent in late 1914. However implementation of the law was suspended for the duration of World War I, which the UK had become involved in due to a spiderweb of treaties.

The world seemed to slip into worse and worse turmoil, further distracting the geoist ambitions of both the parliament and the populace. Asquith's efforts over Irish Home Rule nearly provoked a civil war in Ireland over Ulster, only averted by the outbreak of the world war. Ulster Protestants, who wanted no part of a semi-independent Ireland, formed armed volunteer bands. British army officers threatened to resign rather than move against Ulstermen whom they saw as loyal British subjects. Asquith was forced to take on the job of Secretary of State for War himself on the resignation of the incumbent, Seeley.

While the war in Europe was raging, Ireland staged its Easter Rebellion of 1916, which would prove to be one for the factors of Asquith's loss of power. The other was the war, for in May 1915 the Cabinet split over a scandal involving the dearth of munitions available at the front. Asquith ultimately was held responsible for the shortcomings in British war production.

Responding to the discord, Asquith formed a new government, creating a national coalition that included members of the Opposition. But the war continued to shed rivers of blood, and the machiavellian Lloyd George undermined Asquith by splitting the Liberal Party into pro- and anti-Asquith factions. In the end, Asquith had no choice but to fall on his sword and resign as prime minister in December 1916, and was succeeded by Lloyd George.

Asquith, along with most leading Liberals, refused to serve in the new coalition government. He remained Leader of the Liberal Party, but found it hard to conduct an official opposition in wartime.

In 1918 Asquith declined an offer of the job of Lord Chancellor, as this would have meant retiring from active politics in the House of Commons. By this time, Asquith had become unpopular with the public (as Lloyd George was perceived to have 'won the war' by displacing him) and, along with most leading Liberals, lost his seat in the 1918 elections, at which the Liberals split into Asquith and Lloyd George factions.

Despite losing his East Fife seat at the 1918 General Election, Asquith remained leader of the Liberal party until 1926 - that is, among those Liberals who did not support Lloyd George's coalition government. Support for the Liberals was now dwindling.

He returned to the House of Commons in a 1920 by-election and now played a key role in helping the Labour Party form a minority in 1924, which gave Ramsay MacDonald (yet another geoist) his first - though short-lived – prime ministership.
The minority Labour government fell later in 1924, and in the subsequent election won by the Tories, Asquith lost his seat in the Commons.

For a man who had fought and, indeed, reformed the House of Lords so gallantly, it's surprising that he accepted two titles in 1925, as Viscount Asquith of Morley in York as well as Earl of Oxford. Asquith in fact moved over to the House of Lords and finally resigned his Liberal Party leadership in 1926

Exhausted by years of tortuous political machinations, Asquith rapidly declined and died in 1928, leaving a remarkably modest estate for such a prominent person. Trivia flash: among his living descendants is his great-granddaughter, the actress Helena Bonham Carter.

He took on not just the establishment but the whole economic system of privileges in land. Sure, he lost in the end, but it took the whole British aristocracy, a looming Irish civil war and a full blown war world to thwart his efforts.

Next issue: Mikhail Gorbachev

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Here and There

by Geoff Forster

The chief Executive of Oxfam called upon the world's finance ministers at the G20 meeting in Sydney in February to crack down on tax avoidance by multinational corporations. The Oxfam report said that national governments lost millions of dollars each year to tax loopholes and avoidance. Sub-Saharan Africa lost through tax avoidance and low rates more than twice the aid it received in 2013. The crucial factor here is resource rents and land values, but this is overlooked by those who should know better.

Union leader Paul Howes expressed the view that some worker' incomes are excessive. One correspondent replied that he apparently ignored a 2013 OECD report that the richest 10% of Australians gained almost 50 per cent of the country's economic growth over the past three decades; 22 per cent of all household income growth between 1980 and 2008 went to Australia's richest 1 per cent; and our income distribution is the most unequal in the Western world. So much for "the land of the fair go".

The annual produce of the land and labour of the society, the real wealth and revenue of the great body of the people, might be the same after such a tax as before.Ground-rents and the ordinary rent of land are, therefore, perhaps, the species of revenue which can best bear to have a peculiar tax imposed upon them. **Adam Smith** - *Wealth of Nations (1776), Book V, Chap. 2, Art.1*

More suburbs have attained the dubious distinction of median house prices above the million dollar mark. As at February 1, Toorak was at the top, followed by Canterbury, Deepdene, Brighton, Albert Park, Malvern, Kooyong, Kew, and on. Ashburton's recent elevation means Boroondara is the first entire local government area with a seven figure median house price. Overlooked is the radical difference in cost between the dwelling and the land on which it is located.

Melbourne's street homeless are living nocturnally. It is safer and more comfortable to sleep during the day. A Melbourne city council survey of about a third of the city's homeless sleepers revealed that many walk around all night because it is too cold to sleep. Half reported being treated badly by a member of the public. Many reported a variety of deprivations in their social backgrounds. Causes of poverty amidst plenty vary, but the structural problem of access to land and our skewed tax system remain central factors. Melbourne may luxuriate in its liveable city reputation, but the continuing injustices cannot be ignored.

It was recently reported that renting is cheaper than buying in all Melbourne's suburbs except three. This contrasts with Sydney, where buying is cheaper than renting in only 30 suburbs, Adelaide 30 and Brisbane 50. One economist remarked that while record-low interest rates and rising housing costs were incentives for buyers to enter the market (the second factor is debatable!), this was offset by the uncertainty of a declining economy and the threat of unemployment.

Underlying all this of course is the official disregard for the steadily rising cost of land in all areas.

Once similar, there is now a $250 a fortnight gap between Newstart and the disability pension. Not surprisingly many unemployed on Newstart getting $35.80 a day are trying to get themselves reclassified as disabled to lift their income to $53 a day. The Henry Tax Review observes that on current trends, Newstart will shrink to one third of the pension by 2050 - one is linked to the consumer price index, the other to faster-moving wages.

Official policy deals with secondary issues, while ignoring basic fundamentals.

Things may seem bad in Australia, but are far less drastic than in Spain where nearly half of those under 30 – almost 2 million people – cannot find a job. Suicide rates are rising and the young fear they have no future in their home land. In January one in four adult Spaniards was out of work. Even after five years of recession, the International Monetary Fund warned that it may be five years before the unemployment rate falls below 25 per cent and the number of unemployed falls below 6 million. Oxfam observed 8 million people or 40 per cent of the population are at risk of social marginalization over the next decade.

The basics of economics are universal. In particular, to disregard the law of economic rent has dire consequences in any society.

In Australia, unemployment levels are bad enough, but usually they conceal the trend of major concern: youth unemployment. For 15-24 year olds, the situation has been described as reaching crisis point. National youth unemployment rose to 12.5 per cent in January, and in some rural areas is much higher – in the Seymour area, it is 17.5 per cent, the worst for Victoria, while in Cairns, Queensland the figure is 20.5 per cent.

Behind these figures are many sad stories. The failure of successive governments to take any remedial action condemns them.

Median house prices (read: housing cost) rose significantly last year in all capital cities. Sydney was worst, up 15.2 per cent, followed by Perth 10.2 per cent, Melbourne 8.5 per cent and Hobart the lowest at 2.9 per cent. As usual, there was the failure to distinguish between the actual dwelling and the underlying land. Bot of course to make that distinction might lead to some awkward questions.

Onward and Upward for Gavin

Prosper's resident number-cruncher and key researcher Dr Gavin Putland has left Prosper to study another degree in Economics.
We wish Gavin every success in his new endeavours. Gavin has been very generous of himself to Prosper and the wider Georgist movement. We all appreciate his writings in Progress over the years. His vast knowledge and unique economic perspective are globally recognised.

Gavin continues as Honorary Director of the Land Values Research Group where we will see his dissections of economics and taxation from time to time.

Land lunacy being encouraged to get in others' way

by Karl Williams

Imagine you've just bought a brand new car, with all the bells and whistles. It cost $60,000 and still has that new car aroma when you step inside. Except you don't step inside – rather, you leave it in the garage, completely idle. And it doesn't sit there unused for days or weeks, but for months.

Imagine now you're a businessperson, proprietor of your own printing firm. You've kept that old banger of a printer going for over ten years but escalating repair costs and maintenance time mean it isn't worth keeping. Replacement printers have awesome advances in technology and, after a lot of research, you lash out more than your accountant thinks you can afford. Yes, you've spent nearly half a million dollars on the ultimate boy's toy from Germany, and finally the container from Port Melbourne is delivered to your premises. After hiring a portable crane, the new printer is moved into position after which it just sits idle for months with the timber, padding and shrink wrap still in place.

Why does such behaviour seem so absurd when the basis of our economic system that of, literally, idle speculation in land? Why do we blindly accept urban land worth untold millions can be devoted to growing grass and thistles?

Our tax system has duped us. Because tax-funded infrastructure and rising population inevitably boosts the market price of land, a land holder knows they can sit on their plot and get rich on the back of others. For every land speculator who gets something for nothing, someone else is getting nothing for something. Society in general is getting ripped off because we have to pay punitive taxes on honest work because the natural source of public finance – land value taxation – is strictly overlooked.

Land hoarding is a totally destructive – and rarely-identified - phenomenon. If you collect and speculate upon works of art, the only people who'll suffer from your gain are those who are forced to bid

Why do we blindly accepting how urban land worth untold millions can be devoted to growing grass and thistles?

For every land speculator who gets something for nothing, someone else is getting nothing for something.

more for what you've collected. But land kept vacant or underused by speculation, gets in the way of productive endeavor. We have to travel around and past this obstacle. New suburbs are unnecessarily pushed out to urban fringes, and all sorts of infrastructure (roads, pipes, cables) have to leapfrog over it and stretch out to distant need.

The photos here say it all. They were recently taken on the major arterial Ferntree Gully Road in Scoresby, 25 km south-east of Melbourne's CBD. The city's sprawl is now reaching absurd levels – the boom suburb of Pakenham is 56 km south-east of Melbourne. We should be making better use of land closer and zoned for development before pushing people, businesses and infrastructure out to such distant locations

There are literally hundreds of hectares lying idle for decades in this Scoresby industrial estate. I suspect the opening 5 years ago of Eastlink, providing rapid access to destinations north, south and west, might have given the landholders the gentlest of nudges to cash in this now-accessible and valuable land.

But such is the brazen attitude to holding land out of production for speculative purposes that the billboard urges buyers to commit the same economic sin themselves and hold land idle in the pursuit of unearned gains.

Our academic institutions have become so intellectually flabby and perverted with neoclassical economic absurdities that this 500-pound gorilla just sits in the corner without anyone questioning it. We desperately need a geoist tax shift that would stop 'fining' business for producing wealth and employing people. And the flipside spur to productive activity is an annual site rent makes it impossible to waste an essential resource such as land because, whether you properly use land or not, you still have to pay your dues.

Shameless billboards like this demonstrate that the 500-pound gorilla is not just sitting in the corner, but is eating all our bananas and crapping on the carpet too.

Michael Hudson: Trade Advantage Replaced by Rent Extraction

KARL FITZGERALD INTERVIEWS MICHAEL HUDSON, RESEARCH PROFESSOR OF ECONOMICS AT UNIVERSITY OF MISSOURI, KANSAS CITY, AND A RESEARCH ASSOCIATE AT THE LEVY ECONOMICS INSTITUTE OF BARD COLLEGE, ON 3CR'S RENEGADE ECONOMISTS. HIS LATEST BOOK IS "THE BUBBLE AND BEYOND."

Karl Fitzgerald: Our favourite guest, the man that Max Keiser from www.MaxKeiser.com described as the world's greatest living economist, yes, Professor Michael Hudson is here to give us a wrap on 2013 and the economic forces that have surrounded us for centuries.

How have you actually seen 2013? What's played out for you in terms of the big trends?

Michael Hudson: Oh, the same shrinkage that you've seen since 2008. We're still in the backwash; the economy is still unable to pay its debts. The difference in trend is that now you have hedge funds coming in to the real estate market here buying a lot of properties from the banks at great discount prices for all cash.

So, for the last 30 years you've had a declining proportion of equity ownership of US real estate. All of a sudden that's turned around and gone up because you have hedge funds buying for cash. Now that you have Treasury Securities yielding only one tenth of a percent, the financial sector says "How are you we going to make a higher rate?" The highest rate they can make is in mortgages, so they're buying the discounted properties and they're renting them.

One of the consequences is that rents are going sharply up for the United States so that not only can people not afford to buy houses now, they can't get mortgage credit, but they can't even afford to pay their rent. So the squeeze is on. Only about 25 per cent of workers' pay cheques here can be spent on goods and services, all the rest is spent on rent and social security, medical care, interest payments and taxes.

Karl: You're talking there about the growth of rental-backed securities and Blackstone Capital buying up properties at $100million a week from what I'm reading?

Michael: That's the big change in the last year. Before 2008 you'd have home owners' mortgages that were being packed and sold and now you have the hedge funds packaging rental properties to absentee owner mortgages that are being sold. That's the change that's occurred in the structure of the financial markets this year.

Karl: And meanwhile in America there's vacancy rates of 10.2 per cent. It's staggering that people are taking this sort of pain and the Wall Street mob must be just laughing saying "Look, we can push this even further than we expected"?

Michael: That statistic you just cited is way under-reported because the banks are leaving a lot of families in the homes that haven't paid mortgages in a half-year or a year. They're not foreclosing because they know that if they do kick the people out of the homes and leave them vacant the homes are going to

be stripped of copper, stripped of any wiring and just stripped and the value will go down.

So the banks are leaving people in the homes that are not paying any mortgages just so that they'll be there and, sort of be the watch guard dogs of the home until they can be picked out and replaced with other people. But nobody sees who's going to replace them because the economy's broke.

Karl: Here in Australia we've just had our housing finance figures that revealed investors are at 38 per cent of all loans being taken out. It's shocking how rapidly this is increasing and first home owners are being crunched. They usually average around 19 – 20 per cent of the market, they're down to 12.6 per cent and in cities like Sydney, the pride and joy of Australia, first home owners are just over 7.5 per cent So we're being crowded out.

Michael: Yes, what you're described is inherently unstable. At the peak of the investment boom in the United States in 2008 speculators made up only a sixth of the market, about 16 per cent. So when you say 38 per cent of Australia, that means people have too much money, to make a long story short. They don't know where to put it, so they're putting it there without much thought of how on Earth can Australians ever pay these rents and get jobs where they have to pay so much for their income in rent? How can Australia compete, whether it's in industry or it's in services or whatever, how can it compete if people have to pay such a big portion of their pay cheque out for housing?

Karl: The wealth gap is expanding at a rate of knots and many commentators, economists are struggling to really get a grip on where this divergence is coming from.

Michael: Yes, it's coming from the fact that for the 99 per cent, their income's going down and for the 1 per cent they're making capital gains and interest. The 1 per cent have the 99 per cent of the population in debt to themselves, so they're collecting and it's like a siphon taking all the wealth upwards. And first the 1 per cent are looking for all the income that the 99 per cent have to be pledged to pay the debt and then they want all the assets. So the wealth gap is coming.

For one thing, now people have to pay for their education and that means they have to pay so much they have to borrow, so student debt is increasing and once you graduate you have to spend the next 10 years of your life paying off the student debt. They can't afford to buy their own homes; they have to live with their parents because if they do buy a home they have to sign away the next 30 years of their life to paying the mortgage. So the entry price to get a job in this society, start a family and getting a home is running into a lifetime of debt to pay the 1%. That's why the economy's polarising.

Karl: Is it not also the element of unearned income that's being bought and sold through property transactions, any sort of buy and sell arbitrage?

Michael: Unearned income sure, if you mean capital gains, riding asset price inflation, financial speculation or just making – unearned income is getting money without working for it, getting money simply by lending money or by owning property and putting up a toll booth and charging people an access price. So the economy is putting up toll booths for education. If you want an education, you have to borrow from the bank. If you want to drive a car on a road, well, we're turning the roads into toll roads. If you want to park your car, we're now putting parking meters on the sidewalks and the parking meters' revenue's sold off in Chicago to Wall Street for the next 30 or 40 years to get money to pay the interest to Wall Street now.

So the economy's getting deeper and deeper into debt while all this is occurring. So if you look at the polarisation of wealth, you can just look at the increase in the debt ratio and that's a mirror image of it.

Karl: What I see that's interesting is that around the world we've got now these bail-in policies where depositors do come second to creditors, which is a reverse of the bedrock of the financial system. The depositors being first in line created a sense of trust

that you would be looked after and now we're seeing that not even our deposits are safe, so we might as well all just go into debt and join this Ponzi game and speculate wherever we can because savings in this day and age is virtually over?

Michael: That's not really around the world, that's in Cyprus and the only reason that was in Cyprus was most of the depositors were Russian.

Karl: In New Zealand this is the case and there are elements of it here in Australia. I've heard that in other countries too this is really moving forward.

Michael: Oh, alright, I didn't know about that. Then indeed, there's no safety. I don't know where to put the money. I would imagine people are beginning to buy gold bars. I don't know what to put it in. In America they're buying farmland, they're buying anything that's tangible that can't be wiped out.

Karl: Well that's right. Isn't it interesting that it comes back to the most trustworthy thing you can have on this planet is land in a prime location that's productive? And much of what I like to talk about here is the unearned income that can be earned by just owning a piece of property, waiting for society to develop and then being able to sell that.

Now, a lot of people have difficulties understanding the difference between rent and price. Michael, could you give us an outline on what the difference is between rent and price?

Michael: Well, this is what classical value theory was all about for about 800 years, especially from our Quesnay in France, to Adam Smith and Ricardo and John Stuart Mill. There's cost value on the one hand and almost all the cost of production, whether it's machinery or buildings or labour, all the costs can be reduced to labour. However, if there's a price that's higher than the cost of production that difference is called economic rent. So that's why people talk about rent extraction in these days.

For instance, in America about a century ago, unlike other countries, we left the electric utilities, gas companies, power utilities in private hands, like the railroads were here, and so the government developed a way of analysing what is a fair price for utilities to charge for gas, electricity, for railroads, and so it was all based on actual cost of production. The idea was you want to get rid of monopoly pricing. A monopoly pricing economic rent, monopoly rent, is when a company charges more than the cost of production, including normal profits, will reflect. And traditionally you have that in land, in real estate, in mineral rights, in finance when banks can create money on their computer keyboard freely and then lend it out to get interest.

So rent and interest are created without any real cost of production, they're simply a result of a legal privilege, whether it's a legal privilege to erect a toll booth or to somehow impose a tariff or a special monopoly price gouging.

Karl: And what is the cause of this market power that gives them the ability to enforce these higher prices?

Michael: Usually, the failure of the government to apply anti-monopoly laws. Until Margaret Thatcher's time, Europe kept its roads, its railroads, its airlines, its gas and power utilities in the public hands. So the whole idea was that basic needs and infrastructure would be supplied to the private sector economy either at cost or at a subsidised price so that you'd made the economy more competitive. If you have to begin selling off the roads and putting toll booths there and people have to pay more for that; if you begin selling off land or real estate and the value goes up and you build public infrastructure and you don't tax it away then all this rent is going to be capitalised into a bank loan and the house is going to cost much more and you're going to increase the cost of living, and if you increase the cost of living, that'll increase the cost of labour and it'll make countries uncompetitive.

So right now you have Thatcherism and neo-Liberalism spreading throughout the world. Every country is trying to be as uncompetitive and high cost than the other country because being high cost means that somebody can borrow money against it and leave somebody else holding the bag.

Karl: So that's why trade theory in comparative advantage has really gone out the window due to this financialisation of the economy?

Michael: Yes, if you have three-quarters of the American budget going for housing, either rent or a mortgage, and for debt service and for taxes and medical care, then you no longer have the price of grain or the price of bread determining the price of labour as it did in Ricardo's day. You have really a financialisation of everybody's income and it's a rent theory of international trade instead of a cost of production theory of international trade competitiveness.

Karl: And it is bizarre when you look at the privatisation arguments that are going on around the

world, it's almost as if economies of scale have been superseded by crony competition?

Michael: It affects the markets, that's right. The whole idea now of economies of scale means the ability to control the market and extort economic rent higher than the cost of production and get a free lunch. So today's economy is all about getting a free lunch. This is exactly the opposite of everything that the classical economists thought they were pressing for.

Karl: So what nation do you see is moving in the right direction in terms of economic policy? Is there any nation, Michael?

Michael: I can't think of anyone particular. All you can say is who's avoiding the problems? China seems to be avoiding the problems for the time being. Everybody else, the Eurozone is a dead zone, they're not doing very much; the US is in the doldrums; the Third World is now in trouble, especially India; Russia hasn't really rebuilt its manufacturing base. The whole world is sort of falling apart.

This condensed interview is from a podcast produced in the studios of independent community radio station 3CR in Melbourne, Australia. The full interview can be found at: http://podcast.3cr.org.au/pod/3CRCast-2013-12-10-93939.mp3

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Letters

THE AGE

13 January 2014

Beneficiaries can pay

John Wilson describes Victoria's infrastructure catch-22: "low levels of government debt attract a AAA rating, meaning government can borrow at very low interest rates, yet governments are reluctant to borrow, due to an obsession with protecting this rating" (Forum, 11/1).

He writes how public-private partnerships can come at a great cost to the community, and considers other means of funding, such as a national infrastructure fund, investment by superannuation funds or government bonds. There is another one, the system that built our roads, bridges and dams: local government and water rates.

The Brisbane to Gold Coast light rail will reportedly increase residential land values by up to $100,000. Why can't local government capture a small portion of that increase to help fund the light rail's cost of construction. Surely the beneficiaries should pay for necessary capital works? My local railway line was extended from Darling to Glen Waverley with a levy that ratepayers were happy to pay. God bless the wisdom of our forebears.

Bryan Kavanagh,
Glen Waverley

theguardian

9 March 2014

Government for whom?

Are homes meant to be investment opportunities or places for people to live? Anyone reading 'Scandal of EU's empty homes' (GW, 28 Feb.) would have reason to wonder as to whose interests Europe's decision makers are serving.

But if one casts an eye at the West's tax systems, one can only conclude that we have governments of the speculators, by the speculators and for the speculators. Honest work is frequently hammered by the highest tax rates, whereas those who "reap where they do not sow" are the beneficiaries of tax favoritism.

Australia's sweeping 2010 tax review recommended that properties be encouraged to be put to optimal use by a substantial federal land tax, which is almost impossible to avoid no matter how large one's battalion of tax lawyers.

Why are we not surprised that our system of lobbyocracy soon committed nearly all of these recommendations to oblivion?

Karl Williams
Melbourne, Australia

The tax upon land values is, therefore, the most just and equal of all taxes. It is the taking by the community, for the use of the community, of that value which is the creation of the community.
Henry George - *Progress and Poverty (1879)*

FINANCIAL REVIEW
THE DAILY HABIT OF SUCCESSFUL PEOPLE.
20 January 2014

Howard blew his capital on Work Choices

"Big majorities never last," writes John Howard ("Howard: A majority should be used to major effect", *AFR*, Letters, January 16), "so political capital should be spent on a good cause."

When the former prime minister finally gained control of the Senate, he spent his capital on Work Choices.

This policy produced no discernible change in the unemployment rate, which continued to trend downward as it normally does during the inflation of a property bubble, until the bubble popped.

Meanwhile, Michael Workman in "Soft wages growth makes the case for reform" (AFR, January 16) talks of "high structural costs, other than wages" without mentioning tax!

If the Tories are serious about job creation, they will stop attacking workers' wages and conditions, and start dismantling the taxes and tax-like imposts that cause the cost of hiring a worker to exceed the worker's take-home pay.

The biggest offenders are withheld PAYG "personal" income tax and compulsory super contributions. Employers should be allowed to offset both against GST, reducing the marginal cost of labour without reducing workers' spending power, their job-creating power.

By itself, this reform would cause GST revenue to be negative.

So the obvious way to replace the revenue is to raise the rate and broaden the base of the GST, so that total GST receipts, and hence the cost of living, stay the same.

Gavin R Putland
Land Values Research Group
Melbourne, Vic

FINANCIAL REVIEW
THE DAILY HABIT OF SUCCESSFUL PEOPLE.
12 January 2014

House prices, not wages, is the bigger issue

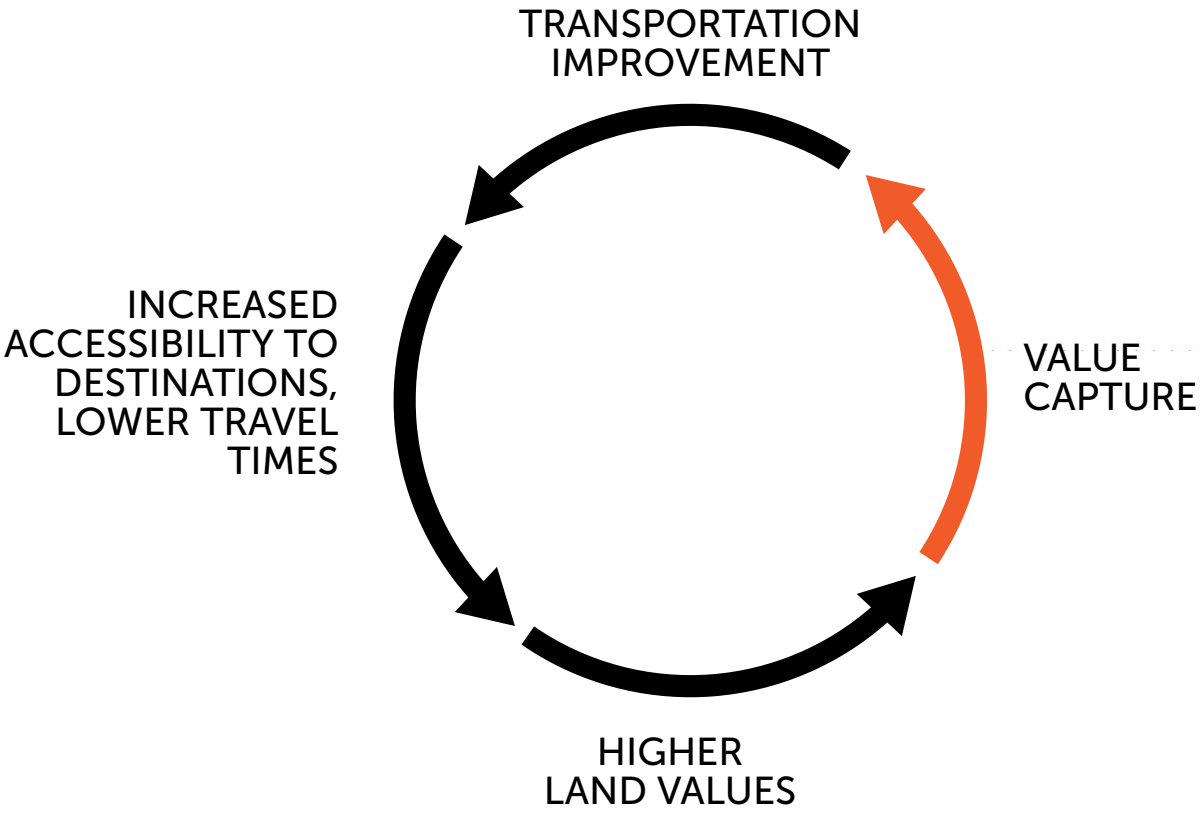
Peter Pitt ("High wages force companies to consider offshore options", AFR January 10) suggests that a lower minimum wage will improve employment retention in Australia. The lower wage countries he uses to support his point include the United States, United Kingdom, New Zealand and Japan.

Of these, only Japan actually has a lower official unemployment rate than Australia. However, Japan uses a narrower definition of unemployment, has a lower participation rate and has around one-sixth of its population living below the poverty line. Given that Australia has some of the most unaffordable housing in the world, fuelled by exorbitant land prices, lower minimum wages are a certain recipe for increasing homelessness and the numbers of working poor.

Australian wages are not too high. Rather, it is the exorbitant price of all types of land that is the real enemy of employment and progress. This problem is perpetuated by a taxation system that punishes effort and rewards unproductive speculation. Australia can increase employment and wages to their full and natural levels by freeing the labour market of land monopoly and other unjust privileges that block fair access to work opportunities. This can be achieved by removing taxes off the backs of wealth producers and returning the unimproved site value of land to the Australian people via the Treasury.

Ronald E Johnson
Association for Good
Government Canberra, ACT

MORE TRAINS?
HERE'S HOW



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