

The Great Crash of 2008



Galloping settlement sprawl, such as that of the last 16 years, has set us up for The Great Crash of 2008. It has the signs of being a Category 5.

There are two main varieties: urban sprawl, and continental sprawl. Let's start with a modest case of urban sprawl.

In Milwaukee County, Wisconsin, there are 17 municipalities. Only two of these are fully built-out: Shorewood and Whitefish Bay, north of the City along the lake. Each houses about 10,000 people per square mile in the green comfort of detached houses on tree-lined streets. The others are full of vacant and derelict land. The Central City itself has hollowed out badly, while also annexing the northwest corner of the County in 1960, still unfilled after 48 years.

At the density of these upper middle-class suburbs, the entire US population, 300 million, would require 30,000 square miles. That is the area of a circle whose radius is 98 miles. Or, if we divide the needed area among 50 states, it is the area of 50 circles of radius 13.8 miles each. Either way you cut it, or any other way, it is lost in the vastness of the USA.

Yet, while the City of Milwaukee hollows out, and the inner suburbs remain unfinished, Milwaukeeans spread into the neighboring counties, where growth is faster: Ozaukee to the north, Washington to the northwest, Waukesha to the west, and Racine

to the south. In addition, some substantial fraction of factory jobs, during times of peak need, go to residents of small outlying towns or farms far away, who move in temporarily when opportunity knocks.

Milwaukee is not growing dynamically, so its sprawl is modest. For immodest, spread-eagle, classic American sprawl, look to new and upstart cities in much of Florida, Texas, Anchorage, Alaska, or Las Vegas, Nevada. Some older cities, however — like Albuquerque or Oklahoma City — manage to sprawl without being dynamic. In California, “From the redwood forests to the Gulf (of California)” urban sprawl inflates the price demanded for nearly every square foot of this land that “belongs to you and me” — or would, if we could afford it. As Woody Guthrie also sang, “Believe it or not you won’t find it so hot if you ain’t got that dough-re-mi”.

Then there is continental sprawl. Old cities and regions stagnate or shrivel, while new ones balloon out of nowhere. Some once-leading cities, and their population ranks in 1890, are St. Louis, #4; Pittsburgh, #7; Buffalo, #9; Cincinnati, #11; Newark, #14; Jersey City, #15; Louisville, #17; and Rochester, #19. These shrinking cities are all in the quadrant northeast from St. Louis, fairly close together, along with surviving but diminished giants like New York, Boston, Philadelphia, Chicago, Detroit, Cleveland, Baltimore, and a dozen middling cities and most of the US. population, as of 1890. People and goods could get from one place to another within fairly short distances, by rail.

Some new big cities today that were not even on the radar screen in 1890 are Los Angeles, Houston, Dallas, San Diego, Phoenix, San Antonio, Honolulu, San Jose, Seattle, Portland, Atlanta, Miami, Charlotte, Las Vegas, Salt Lake, and Jacksonville. These are all outside the northeast quadrant, as the US center of population moves steadily southwestward, from southeast Indiana in 1890 to south central Missouri in 2000. It’s not just the center that counts, though: it’s the dispersion. Populations south and west of the center are widely scattered.

Each of these new cities represents the transfer of an entire

subset of the economy. Cities grow, as Jane Jacobs showed so brilliantly, by import substitution. They and their regions grow more and more self-sufficient as they add people. Repair shops evolve into parts makers, and they into assemblers and manufacturers, some with national and world markets.

At the same time, to tie us together we have the Interstate Highway System, and many state highway systems. Interchanges create hundreds of new commercial nodes. In the short run these may seem to bring urban values to old farmland; in the long run, and in the aggregate, they create an artificial abundance of urbanesque land, an overhang that presages the crash phase of the cycle. They also create an overhang of deferred maintenance and replacement, for highways must in effect be rebuilt every 30 years or so, but at higher prices for cement. Worst of all they create a permanent commitment to wasting energy. These contingent liabilities have been hidden during years of euphoria. Today, as gasoline prices soar and tax revenues falter, they are all too visible. Too much land accessed, and rising costs of accessing it, combine to lower land prices.

We also have our inflated air transport system. The US has 15,000 civilian airports, more by far than any other nation or group of nations. The vastest of these, Denver International, takes 34,000 acres, or 53 square miles. Other oversized ports are mostly in the south and west: Dallas, Orlando, Kansas City, Atlanta, LAX, Seatac, and Miami, for example. Some eastern ports are much smaller: Washington National is 1,000 acres; busy LaGuardia is only 600. Many general aviation ports are smaller yet, down to under 100 acres. Estimating the mean civilian airport area at 400 acres, (military airports, not included here, average much bigger), 15,000 airports would require six million acres, or 9,400 square miles — about the area of New Hampshire.

While surface area is only one of the resources that air travel consumes, it is symptomatic of the daunting resource requirements of spreading people from Nome to Key West, from Eastport to Kauai, throwing in American Samoa and Puerto Rico and The

Virgin Islands, protecting them all with military airports and bases and their logistics, and linking them as tightly as Baltimore and Philadelphia. The soaring costs, led now by jet fuel, and security aggravations, and falling comforts of air travel, are beginning to drive home these rising demands on limited resources. Meantime, though, this nationwide transportation network has brought vast new areas inside the urban ambit. A rich Montana rancher and his wife can wing it into Denver or Vegas in their private plane for a night on the town; but how long can this dream of city-country affluence last?

To highways and airlines let us add the power grid; huge interregional water transfers and systems; several new kinds of radio communication grids in bewildering novelty and abundance; the postal service grid; UPS and FEDEX grids; natural gas lines; the telephone grid; the banking network; the list goes on, and on. Most of these bring service not just to the end-points, but to most of the included interstitial lands.

How can land rents and values fall from oversupply, when land supply is fixed? This fixity feeds the delusion that land rents and values can only rise with population and capital formation. However, people and capital can spread out to encompass and fructify more land. That is sprawl, urban and continental (worldwide, too — but that's not covered here).

Professor Robert Murray Haig theorized in 1926 that if transportation costs fell to zero, there would be no urban land values: one location would be as good as another. That can't happen, of course, but lower transportation costs, as by an abundance of Ford's Model T's, would lower land rents and values. He presented this just as a cautious academic speculation, but did he see something coming? Seen or not, it did come right after he published.

To Henry George, "land speculation" meant holding land off the market waiting for a rise. He likened it to an unconscious "combination" (a cartel) of landowners creating an artificial scarcity. George missed the next trick, however. He attributed industrial depressions to inexorably rising rents and land prices that progressively

squeezed labor and investors off the land and into the unemployment lines. It was too simple. A good explanation must account for land value collapses, like today's, playing a key role in the crash.

Like all cartels, the unconscious combination of land speculators creates a price umbrella under which new resources enter the market. This "price-umbrella syndrome" periodically creates an artificial surplus of land. At the same time, the lavish use of durable capital to bring settlers to all this new land creates a shortage of liquid capital, a shortage of loanable and investable funds, a rise of interest rates and a tightening of credit.

Austrian cycle theorists have dwelt on this tilting of what they call "the structure of production", with too much capital getting sunk irrecoverably in what they call "higher order" goods. Well and good, they are onto something big and vital. Unfortunately, though, they find its cause solely in "forced saving" from bank expansion, with no reference at all to its "geo-economic" roots, and the role of inflated land collateral enabling bank expansion. Worst of all, they see no remedy except forcing down wage rates.

Forces of containment, notably including George's land speculation, have imposed uneconomic scatter and sprawl on settlement. They have held back the logical areas for continuous settlement and forced the pioneers to move around and beyond them. If you examine a map of population density in the United States at any time in history, you see that urban scatter and sprawl have their counterparts in national patterns of land use, and they always have had, in spite of the "Indian menace."*

By 1890 the Census gave up trying to draw a "frontier line". The Director wrote, "the unsettled area has been so broken into by isolated bodies of settlement that there can hardly be said to be a frontier line" — a passage that Frederick J. Turner misread, I think, as he launched from it into his classic "Frontier in American History."

* A series of such maps to 1865 is in John D. Hicks, *The Federal Union*.

It was not the frontier that was passing, but the last vestige of orderly advance into it. The center of population continued to march west-south-westward, as settlements grew ever more scattered. In 1893 another boom ended, evoking the populist plaint, "In God we trusted; in Kansas we busted."

George himself did not, to my knowledge, call the crash of 1893, or explain its causes to his readers. It might have enhanced his reputation among later economists, and justified the subtitle of *Progress and Poverty*. By 1893, however, he was preoccupied with other issues, sick, and four years from death. Perhaps, also, he perceived that the facts did not exactly fit the simple scenario sketched in *Progress and Poverty*, and he lacked time to revise his model, in which by then he was heavily invested.

Georgists of the 1920's did poorly calling the real estate slump that began in 1926, and the stock market crash of 1929. As late as 1932, at the very nadir of The Great Depression, Harry Gunnison Brown, leading Georgist economist of the times, dismissed the wreckage around him as "a period of slack business" (*The Economic Basis of Tax Reform*). Albert J. Nock and Frank Chodorov preoccupied themselves with carping at Keynes and labor unions, preaching free markets as though they had discovered them — and as though the system had not crashed after 1929. They opposed all totalitarians in principle, but aimed most of their shots at FDR and The Allies, alienating a generation of earnest activist reformers.

Career-minded professionals have to pause before issuing pessimistic forecasts about land and securities markets, where confidence hangs by a thread. Senator Charles Schumer warned of the IndyMac Bank collapse, and critics immediately jumped on him for causing it. Homer Hoyt could publish his masterpiece in the deepest trough of depression, when anyone with eyes or ears knew the system had crashed, and revolution was in the air. Twenty years later Hoyt had gone into real estate consulting and land speculation, and declined to see any revival of his own cycle. Many have put down even Robert Shiller for puncturing the euphoria: Michael

Mandel, Chief Economics Editor of *Business Week*, recently published *Rational Exuberance*, whose title telegraphs its message, while the views of his sunny senior columnist Jim Cooper remain reliably upbeat, week after week, as we sink deeper into the mire. No one will fault Mandel or Cooper for pricking the bubble of “confidence.”

I do not know of a single Nobel Laureate in Economics who forecast the present crash, or any other. Two of them, Chicago-Schoolers Robert Merton and Myron Scholes, founded Long Term Capital Management to demonstrate the brilliance of their investment theories. It went down in flames in 1997, saved only by a Federal bailout. Nothing daunted, media and public speakers seeking confirmation lean hard on citations of Nobel Laureates. The media might better consider others with better track records.

Modern Georgists enter this period of danger and opportunity in relatively good shape. Several have outstanding scorecards calling the current crash. These include Fred Foldvary (2007, *The Depression of 2008*); Fred Harrison (2005, *Boom/Bust*); Michael Hudson (2007, “The New Road to Serfdom,” *Harper’s*); and Bryan Kavanagh (2007, *Unlocking the Riches of Oz*). Each has a slightly different take on it, but they all saw it coming and stuck their necks out to forecast it in print. One of their distinctive commonalities is their recognizing that land rent and values are many times higher than most economists realize, and so play a major role in macro-economic ups and downs.

These Georgists who foretold this crash deserve a hearing, in preference to those who failed, and certainly to those who still deny it. What solutions would they offer? I do not speak for them, and they are not of one mind, but the following elements seem reasonable and likely.

One, of course, is to raise more public revenue from taxes on property in general and land in particular. These include property taxes, of course, but in addition a host of other kinds of revenues.*

* See pp. 61-88.

One of them, which Michael Hudson has explained in several articles, is to reform the personal income tax to bear heavier on property income and lighter on wage income.

Another is always to base land assessments on current market value, and update them annually. ‘Expert’ appraisals of land are based on sales of comparables, and upward price trends. These sales, in turn, were influenced by appraisers who based their opinions on earlier comparables and upward trends, and so on. This is because there is no cost of production to check excesses. Thus a herd mentality can take over, divorcing prices from reality: ‘Irrational Exuberance.’

Why, then, would I ask public assessors to join the misguided herd? Because the public assessor is the one valuer whose overvaluation stops the herd. The Assessor by law is supposed to follow a bull market, not outguess it. When the “exuberance” appears in his wisdom to be “irrational,” his job is still to go along, not judge. When private fee-appraisers go along they confirm and reinforce a boom, but when the tax Assessor goes along he douses a boom with cold water: higher taxes. It was the lack of such an automatic remedy that let the farmland boom of the 1970s soar so high above reality, then the urban bubble of the late 1980s, and now, of 2001–07.

The present income-tax treatment of “capital” gains, which nearly forces the elderly to cling to their lands until they die, should be changed to a tax on annual accrual of value, as proposed by our same Professor Haig in the 1920s. The “Unplumbed Potential” article explains practical ways of doing this.

Banks should be regulated away from lending on land collateral. Following the South Sea Bubble (ca. 1720) there was such a movement in England. The emergence of the industrial revolution, flawed as it was, suggests the results were not all bad. Logically there is a powerful reason to regulate banks of deposit. This is because they are always technically insolvent, never able to meet their short-term liabilities from their long-term assets. A related reform might be to make mortgage notes part of the property tax base.

It is tempting to note that public debt has often been a more

stable asset for banks than mortgages. Ever since FDR, banks have avoided the total dependency on mortgage loans that led so many to fail from 1929-33. Should we then limit banks to holding public debt? The problem is, it only takes one wild administration to bankrupt a nation by making a virtue of spending more and taxing less, egged on by certain extremist schools of economic theory. Federal providence is no guarantee of public thrift, either. In the 1920's when Andrew Mellon ran a Federal surplus, local governments and improvement districts ran wild with debt. In the 1830's, when Andrew Jackson ran a surplus, it was state governments that went broke. There is no simple mechanical substitute for sober judgment based on theory, and history, and selfless public spirit.

Meantime, where is hope? Cleaning up the mess left from the last few manic years will cost sweat and tears and fortunes, whoever undertakes it. Lower rents and land prices will finally let us recover, but the process of getting from here to there entails a fall from illusion to reality, from high to low, that will agonize many. New administrations will prolong the agony by trying to defer it. They will bail out a few of the victims and many of the culprits by raising the national debt and inflating the currency to validate bad debts and sustain land values.

Hope lies in observing how many cities and nations have risen from disasters to new prosperity. John Stuart Mill stressed in his *Principles* (1848) "the great rapidity with which countries recover from a state of devastation; the disappearance, in a short time, of all traces of the mischiefs done by earthquakes, floods, hurricanes, and the ravages of war."

Born-again San Francisco, 1907-30, makes a case study in fast recovery after it was devastated in 1906. It had no State or Federal aids to speak of; no oil or gas royalties; no power to tax sales or incomes or payrolls; no lock on Sierra water to sell its neighbors, as now; no finished Panama Canal, as now; no regional monopoly; no semitropical climate; and little flat land. Its great bridges were un-built – it was more island than peninsula. It had eccentrics, drunken

sailors, race riots, vice, vigilantism — and boatloads of illegal immigrants, whose records were lost in the fire. It had fog, the Sierra wall to the east, and the San Andreas Fault, which will never go away. Statewide, mining was fading; irrigation barely beginning. How did a City with so few assets raise funds to repair its broken infrastructure and rise from its ashes? It had only the local property tax, and much of this tax base was burned to the ground. The secret is that it taxed the ground itself, raising money while also kindling a new kind of fire under landowners: to get on with it, or get out of the way. Developments are interdependent, so each owner could improve his land in the knowledge that other owners were subject to the same pressures, so needed complements would arise in sync with his own investment.

In 1907 the City Committee on Assessment, Revenue, and Taxation reported that revenues were still adequate, because before the quake and fire razed the city, 75% of its real estate tax base was already land value. The coterminous County and School District used the same tax base. San Francisco and Henry George were more in tune than perhaps either one realized. They did not rely just on cheerleading; they had a substantive program that worked.

This firm tax base also sustained San Francisco's credit to finance the great burst of civic works that was to follow. People flocked there to open businesses, and find jobs and homes. The City bounced back so fast its population grew by 22%, 1900-10, in the very wake of its destruction; another 22%, 1910-20; and another 25%, 1920-30. It did this without expanding its land area, and while providing wide parks and public spaces. It even pulled back from the treacherous filled-in level lands that had given way in the quake. On its hills and dales it housed, and linked with mass transit, a denser population than any major city except the Manhattan Borough of New York. It is these people and their works that made San Francisco so livable, the cynosure of so many eyes, and the commercial, financial, cultural, tourism, and light manufacturing center of the Pacific coast.

The whole US can follow this model today, but on a grander scale and adapted to modern technology and values. Skeptics will wonder how we can take more taxes from rents when they are falling. Here is the key: the effect of untaxing trade, enterprise, work, and production is to raise and sustain land and resource rents as a tax base. This does not work through raising asking and holdout prices, but rather by raising bid prices, activating the market. Today we recognize a great variety of new ways these rents manifest themselves to be tapped for public revenues. We can seize these opportunities, old and new, and pull ourselves out of the funk left by the great crash of 2008.

— Groundswell, *July–August 2008*. Published as a pamphlet along with “*How to Thaw Credit, Now and Permanently*” by the Robert Schalkenbach Foundation, 2009



