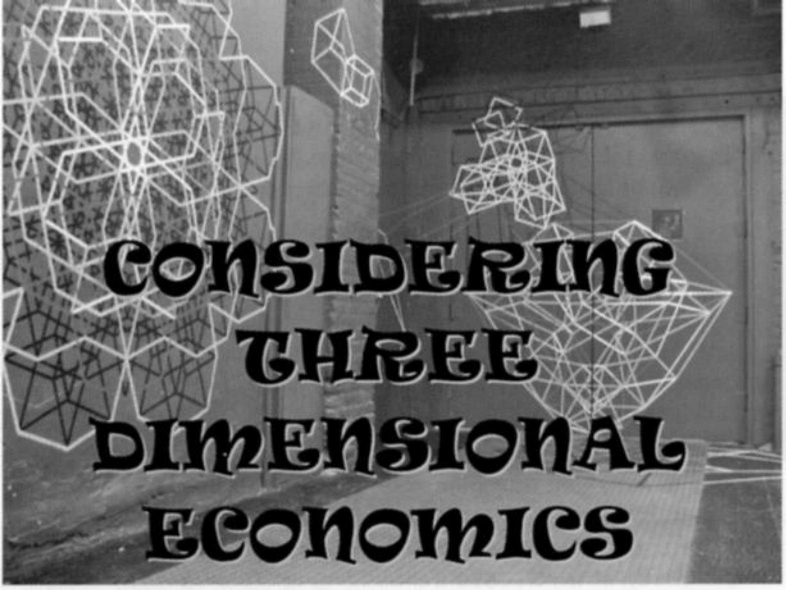

Considering Three Dimensional Economics

By **Karl Fitzgerald**,
Project Coordinator,
Earthsharing Australia

Ed: Our own "K2" had this wonderfully-provocative piece published in the Feb-Mar edition of Arena Magazine.

In a period where the twin crises of global warming and the wealth gap are attacking society from both sides, policy makers are continually limited in their effectiveness by a two dimensional approach to economics.

Land prices have increased at 4 times the rate of GDP and dwarfed wages growth by 1000 to 1 since WW2[i]. Such damning statistics beckon the ALP to take a hard look at the economic fundamentals undermining union wage demands. For Julia Gillard's 'War on Poverty' to be successful, policymakers must look outside the square.

2008 marks the half way point in our promise to halve world poverty with the Millennium Development Goal's 2015 deadline. With the wealth gap accelerating in both Developed *and* Developing countries, a serious flaw is evident in modern economics.

The two-dimensional approach to current economic analysis sees the first priority of policymakers as inflation, representing 'capital'. The second is high wages, representing 'labour'.

A third dimension in classical economic analysis did once exist, at least for a short period of time in the 19th century. This third dimension was represented in economic terms as 'land'. Land represented the planet itself. It focused on the ground we stand on, but also included all the natural resources that seem to be so profitable in a world of growing scarcity – oil, coal, water and minerals. Not only all the resources below us, but the important ones above us, the electromagnetic spectrum, and in this day and age, carbon.

During the formative years of economic theory there was an understanding that natural resources had an advantage over all other forms of property rights. As society developed and populations expanded, the resultant natural scarcity would see the 'owners' of resources delivered profits 'in their sleep', as J.S Mill quipped. These were called 'economic rents' and are the holy grail of super normal profits for corporations such as Macquarie Bank, BHP and the Carlyle Group.

The 'law of rent' ensures that any improvements in hospitals, computing productivity, lower crime or better parks are captured in higher land prices. Population growth levels give a further fillip to the runaway land prices we now face.

The pursuit of these hand delivered profits is called 'rent seeking'. The danger of this pursuit is a central premise to classical economics. Unfortunately it is rarely discussed.

Those in the know understand that there is no alternative to land – we need somewhere to have a roof over our heads. Similarly, there is no alternative to water, thus the neo-liberal drive to privatise it. Oil has few alternatives and so can also demand high prices because of its monopoly rights as the cog in the middle of what should be called 'monopoly capitalism'.

So how does this relate to us in this day and age? Much is revealed by visiting a 'Tax Minimisation for Lawyers' seminar. One can hear how the top end of town engages in 'asset protection', a euphemism for tax dodging. Few from the working classes have knowledge of this modern technique for passing the buck.

At this seminar one will hear how over the last decade cash has returned 6%, international shares 8% and Australian shares 10 – 12%. Then the bell tolls and the crowd is told that land has delivered 15.5% over the last ten years. The biggest return with the least risk.

Those in the know, know.

Prime Minister Rudd has promised a discount on first home savings, giving buyers additional purchasing power. Like the First Home Owners Grant, when the marketplace gains additional purchasing power, such policies end up fluffing the pillows of the wealthiest people in Australia, the landed gentry.

> One can hear how the top end of town engages in 'asset protection', a euphemism for tax dodging

Similarly, the $500 million dollar infrastructure fund announced by Rudd will make surrounding properties more valuable, enabling owners and developers to sell them for higher prices. Speculators know this and are first in line, outbidding families for property surrounding infrastructure, as they know the returns will be higher.

Taxes paid by working Australians fund the infrastructure, compounding the injustice. With global warming threatening, speculators shouldn't be encouraged to drive urban sprawl into our green fields.

Will the ALP's Commonwealth land release assist affordability? The one-eyed invisible hand will see speculators hoard the land and drip feed it to the market at just the right level to ensure first home owners are willing to meet their blackmail price.

Contrasting the one-way street of economic analysis, Earthsharing Australia's 'I Want to Live Here' report[ii] found that the much vaunted vacancy rates only include properties presently on the rental market. Thus speculative vacancies held off the market are not included in the 'official' vacancy rate. The Real Estate Institute of Victoria published its' vacancy rate at 0.8% in September[iii]. The IW2LH report calculated a genuine vacancy of 11.7%.

Earthsharing conservatively found that during a period of 'record low vacancies', 1058 people could live in just one area of Melbourne. Why are vacancies at a record low?

Of the 430 vacant properties found empty, 399 were vacant land allotments. Some had been vacant for over a decade. Holding property empty acts to enforce scarcity, pushing prices up higher. Conveniently for owners, this then raises their borrowing capacity to purchase additional land.

Looking deeper into the affordability issue, the Richard Pratt School of Price Fixing would be impressed with the openness that prices in the land game can be monitored. Both the UDIA[iv] and HIA[v] publish Land Price Indices that monitor the supply of vacant land sold to the market. Keeping the profit maximising incentive in mind, the astute investor would monitor these indices to limit supply and maximise profits.

Much vaunted vacancy rates only include properties presently on the rental market. Thus speculative vacancies held off the market are not included in the 'official' vacancy rate

A recent visit to the Newcastle CBD saw similar doughnut development traits. A walk through its mall revealed vacancies at close to 30%. High rents had forced people and businesses to operate on the urban fringes. Here the same landlords conveniently built new shopping centres, with a clause. Freedom of speech is curtailed for retailers due to the contractual requirement that tenants do not discuss rents with their neighbours.

The speculative vacancy trend is worldwide. New York's Office of Borough released the "No Vacancy?" report in 2006[vi], finding 492 million square feet of residentially zoned vacant land. Pacific Islands such as Vanuatu are suffering from the speculative plague too; with traditional lands carved up for empty holiday villas.

Ignorance of the third dimension in our economic analysis sees a distortion underwriting the boom-bust nature of the growth model. When too much money gets spent on land, technically known as 'rent', there is less left for both capital as investment and wages for labour. When the cycle is crushed by excess rents, we see the first domino fall i.e. the US housing market. From there jobs are lost, consumption falls and a 'correction' is needed.

On the precipice of the largest combined asset bubble in history, we must find a way to rebalance the playing field between land, labour and capital.

Classical economists favour the adoption of a Resource Rentals system. This sees taxes shifted off our hard work and onto our precious resources. Then holding costs for resource ownership see them used productively, not speculated upon greedily. Water trading in Victoria has seen a coterie of wealthy investors snavel up water rights at $80 per mega litre. Now valued at over $500 (and reportedly as high as $10,000), one must ask how selling at the top of the market is a productive activity?

Similar trends will inevitably to emerge with Carbon Trading. The New World Order allows for speculation as the last remaining fast track to wealth whilst multinationals have mass production stitched up through China.

If a holding charge was placed on land by reforming Land Tax into a flat Site Rental, the 430 speculative vacancies in Maribyrnong could no longer be held vacant. At present their holding charges are a miniscule $1000 p.a. whilst they appreciate at closer to $50,000 p.a. If the holding cost was to become $10,000 (or preferably set at 10%) the land would soon be sold. Importantly, land prices would drop and remain at levels closer to what our productive rather than speculative incomes could afford.

Bryan Kavanagh from the Land Values Research Group calculated in his recent 'Unlocking the Riches to Oz'[vii] report that Australian GDP could be boosted an extra $35,000 for every man, woman and child if the more efficient Resource Rentals system was adopted. This is possible through the elimination of deadweight taxes and the smoothing of the economic cycle through the deterrence of speculation.

This path would please the left by encouraging the efficient use of resources and keep business happy by reducing taxes. This comparative advantage would help improve exports and pay off foreign debt. Lower compliance costs would give small business development a fillip, in turn raising wages. Future generations would regain some faith that they could afford the great Australian dream of home ownership whilst simultaneously benefiting from employment in small business and improved public services.

Will Mr. Rudd look outside the square to the bigger picture? If so, he could look up the history of the seat of Griffith[viii] he occupies. Samuel Griffith was a supporter of classical economy.

1. [1] http://www.reiv.com.au/news/details.asp?NewsID=589
2. [1] The Poverty Inquiry to end all Inquiries, Tony O'Brien, Figure 1, p5
3. [1] http://earthsharing.org.au/IW2
4. [1] http://www.reiv.com.au/news/details.asp?NewsID=589
5. [1] http://www.udia.com.au/resource/UDIA%20Land%20Supply%20Study.pdf
6. [1] HIA - APM Land Monitor: http://economics.hia.com.au/publications/land_monitor.aspx
7. [1] http://www.gothamgazette.com/article/issueoftheweek/20080107/200/2394
8. [1] http://lvrg.org.au/Text/1185757317668-1924/Unlocking-Riches-of-Oz
9. [1] http://grputland.com/classics/griffith.htm