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OIL & THE PETTY EFFECT

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1. A theory will be elaborated which I shall call The Petty Effect (after Sir William Petty, the 17th Century English Economist), to illuminate a variety of contemporary economic phenomena which, traditionally, are uncharacteristic of periods of recession. The analysis relates to the exploitation of a natural resource (oil) and the international flow of funds.

2. The largest proportion of revenue from the sale of crude oil constitutes economic rent. Oil-rich nations acquired dramatically-increased incomes after 1973 by exercising their monopoly power. The overall economic effects are explored, the analysis decomposed into two parts:

(a) The monetary effects What happened to economies whose exchequers were suddenly swollen with income from what amounted to a tax on land? Inflation was induced, for the domestic output of goods and services could not increase with commensurate speed to meet the challenge of the unexpected surge in demand from consumers, and the gap could not be wholly met through imports.

(b) The "real" effects Under the existing land tenure system, the pattern of investments arising from development programmes was not entirely rational (based on the needs of the community as expressed through the market). They were, and still are being distorted by the manipulative economic and political power of landowners. Land which formerly had little use value (e.g. desert sands), let alone value in exchange, suddenly acquired a large value. Command over rights to this land became a mechanism for influencing the allocation of the community's income.

3. The empirical evidence is examined by separating countries into two groups:

(i) The oil-endowed OPEC countries quickly committed themselves to industrialization. Kuwait and Venezuela will be taken as case studies. The lesson learned ought to assist in defining development programmes for the other Third World countries; their severe shortage of cash makes it imperative to formulate a strategy which maximises the benefits derived from the use of scarce resources.

(ii) The oil-importers Because of their investment opportunities, industrial nations became repositories of a considerable part of the surplus oil revenue. The USA and UK will be studied. The present high price of land, despite the serious and protracted depression of the '70's (the worst since the '30's), will be explained in part by the demonstration effects of speculators, financed by oil money, buing land as a long-term asset. Many domestic users, such as farmers, have been outbid. The volume of investment in land in this period has been larger than has been the case in the recessions which have peppered 200 years of industrial society.

4. Conclusions The world-wide speculation in land in 1970-73 guaranteed a serious slump, and the dramatic rise in oil prices, beginning in late 1973, merely reinforced what by then was an inevitable fate for the industrial economies.

To cushion the depression, governments at first resorted to Keynesian tactics to artificially buoy up their economies. Money which flooded out as increased payments for oil imports, a process which ought to have been deflationary, was partly offset by deficit financing. As a result -

(I) Financial adjustments as between the factors of production, a feature of previous slump and recovery phases of economic cycles, have been obstructed. Wage negotiations were constrained by legal controls, while the value of land has been kept up despite the diminished proportion of GNP which can be categorized as economic rent. This has generated social friction leading to large-scale protests (such as the union-led marches in Dublin in March, 1979), and reactionary strikes against the state (such as the Proposition 13 movement in California in 1978).

(II) Structural adjustments have also been thwarted. The recovery of profits has been postponed; consequently, there has been a slower rate of new capital formation and job creation, and an increasing reliance on public subsidies to disguise the true underlying level of unemployment.

Thus, some of the effects of land speculation in the 1970-73 period have been deferred. These, however, must finally work themselves through the system if industrial economies are to adjust themselves sufficiently to permit the start of another long cycle of economic growth. The refusal to confront the impact of the world-wide speculation in land in the early '70's does not auger well for the 1980s. For while governments may now have realised that a disciplined monetary policy is an essential feature of sound economic practice, steps are being taken to offset the implications for employment of such a transformation in policy. Protectionism is finding favour despite the nominal commitment to free trade espoused through international agreements and the creation of regional alliances such as the EEC. Before industrial nations can return to the path of sustained growth, they will have to adjust the present pattern of factor incomes. Land values and rents will have to be reduced or stabilized. Will the landowning class permit this? If they do not, the prospects for employment and living standards are grim.

The onset of the "energy crisis" in late 1973 enabled politicians and academic economists to blame OPEC for the world recession. To blame a particular system of land tenure would be, and indeed is, considered to be eccentric. Yet (a) the recession was primarily induced by the traditional form of land speculation, i.e. the exploitation of values created by locational advantages; and in any event, (b) the "energy crisis" of 1974 is a useful illustration of a general phenomenon: the arbitrary exercise of power over natural resources by a group of monopolists. So the "energy crisis", in fact, illuminates the thesis advanced by Henry George 100 years ago - that capital and labour are, or ought to be, bound together in an alliance against the common enemy: land monopolists who disrupt the smooth operations of the world's economies.