How Inflation Postpones Depression, or Is Inflation Better than Site Value Taxation?

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We, who are concerned with the state of the nation and watch in chagrin as the currency is debased and vested interests deplore the right to tax land, are also surprised at the apparent vigor of the economy in face of its expected downfall. We should remember that the Roman empire enjoyed at least 400 years of inflation before its demise – and today's bankers are much more sophisticated. On the plus side there has been some increase in land value taxation, mainly through higher assessments, and therefore we have this hue and cry about the injustice of supporting education via property taxes.

The historical facts notwithstanding, it seems that the economic mechanism of inflation has not been presented clearly in its macroeconomic context. We all understand that when a government spends more money, we appear to have more money to spend for a while and this increases the momentum of the economy. What is not understood is how some of this momentum is maintained for a country as large as ours in the face of anticipated severe depression because of the great amount of land speculation.

Let us postulate that we have a gold standard economy as existed in the U.S. prior to 1930. In those years the prosperity-depression cycle appeared to be in force. Starting with the "expansion of business activity," the cycle runs something like this.

1. *Business is expanding*. Employment increases and demand for land increases. Things are improving for everyone. As long as the economy is improving we call this period "Prosperity."
2. *Land speculation increases*. This is not really Step 2 as much as the undercurrent of the business cycle.
3. Land speculation has risen to the level where business expansion becomes unprofitable.
4. *Business expansion stops*. At this point we say the depression begins.
5. *Demand for labor decreases*; unemployment increases.
6. *Demand for goods decreases*.
7. Employment and business activities decrease until the speculative price of land is pushed downward.
8. When land for the expansion of business again becomes available at a price which encourages business activity, the cycle repeats with Step 1, the expanding economy.

Using this picture of the business cycle as the body of the economy, we may readily see the effects of government intervention. Henry George suggested the intervention by government at Step 2 to prevent, retard or eliminate land speculation, depending on the strength of application of the site value tax. The drawback to this is the unconventional nature of this tax in an era which considers land speculation a fair business activity.

In a booklet entitled "Gold," issued by the Federal Reserve Bank of Philadelphia in 1963, the case for monetary intervention in the business cycle is simply and clearly stated: "One disadvantage of the Gold Standard was that less money in circulation within a country – which meant lower prices – also could mean less domestic business activity and more unemployment." This general observation was transformed by Keynes into what may be called the science of monetary theory as it is used today. Repeating this principle in utter simplicity and stating it positively: an increasing money supply increases business activity.

It is in application to the business cycle that this simple principle becomes complicated. It is theorized that if we understood and could measure economic forces perfectly, we could then use the principle of expansion and contraction of the money supply to keep the economy going steady with only very minor and localized ripples in the pattern of "prosperity." In theory, what the monetarist wants to know is the exact moment in time when Step 4 begins in order to inject the monetary boost. As the reader can readily fathom, the amount and timing of the monetary expansion are at best difficult to determine.

Assuming the business cycle under a gold standard as correct, we can now deduce how inflation postpones depression.

A. That expansion of the money supply *postpones* depressions is a historical fact.

B. In order to act as an interruptor in the business cycle (postponing a decline of business activity), monetary expansion must reduce the effect of or actually reduce land speculation.

C. Since business contracts and leases are time based, and land leases in general are for the long term compared to other business contracts, an expanding money supply (inflation) favors the industrialist and businessman over the land owner. The land owner is stuck with a long term, low interest arrangement.

D. With an expanding money supply, normally interest rates increase, diverting some savings into investments other than land, also reducing the speculative pressure on land.

In order for Steps C and D to take place, there are tow requirements that must be met. These are secrecy and irregularity of time and amount of monetary expansion. This follows simply from business logic. If I am a landowner and I *know* there will be inflation, I will automatically hold out for a higher price or a shorter lease. If I am *uncertain*, I may settle for a lease or sell at a particular price. Unless my own circumstances demand it, I do not have to lease or sell a piece of land. As an investor, if I were certain that monetary expansion followed a very predictable pattern, I would have to discount the return on my investments and look for greater yields and/or increase in capital value to maintain my purchasing power. Since the criteria of secrecy and irregularity are met somewhat by the Federal Reserve Board's activities, inflation does postpone depression in the U.S. *until everyone knows there will be a continuous increase in inflation.*

Ed. Note: The News occasionally receives articles like this one, but unfortunately most are too lengthy for publication in the present format. Articles can be considered for the News if they are no longer than five typed (double-spaced) pages; they should contain a minimum of quotations and illustrations. Readers whose articles are published should write to the News if extra copies are desired.

Tax Reform Group *(cont. from p. 1)*

(D., Wis.), and Vanik (D., Ohio). 44 others joined in signing a public letter of opposition.

Issue number three is closed rule. Closed rule is a device by which tax policy bills are kept in the House Ways and Means Committee, thus depriving the rest of the House many decision-making powers – and of course concentrating those powers in the hands of a few. Closed rule was attacked in an amendment by Reuss (D., Wis.) and lost by 206-180.