

## Lesson 6 — Depressions - recessions; Proposed Remedies (a Synopsis)

Based on Progress and Poverty Book V, especially chapter 1; and Book VI, chapter 1 only.

This lesson explores the cyclic expansions and contractions of employment (recessions / depressions) within the economy; and six commonly proposed remedies for the elimination of poverty.

In concept, a depression is a severe form of what is now called a recession. Recessions and depressions are simply intensifications of the general problems of unemployment and low wages. There are several factors which tend to intensify and expand the effects of a recession. Important among them is the interdependence of producers and consumers, in which workers who become unemployed reduce their demand for the products of other people's labor. There is the consequent sharp decline in the velocity of money (number of transactions), which has the same effect as reducing its supply. This dynamic has the opposite effect as inflation where the value of debts is diminished.

In a recession those who owe money find that everything that is paid for, including wages, are worth less in terms of money, but what they owe in terms of real wealth is much more than it was before. In inflationary times prices go up. If corn sold for \$1 a bushel, the farmer who borrowed \$100, owed 100 bushels of corn. If an increase in the money supply bids up the price of corn to \$2 a bushel the farmer only owes 50 bushels of corn. Conversely, if corn sold for \$2 a bushel, the farmer who borrowed \$100, owed 50 bushels of corn. If a recession causes people to slow their spending, and corn falls to \$1 per bushel, now the farmer who owes \$100 owes 100 bushels of corn. This intensifies the cycle by increasing the value upon which debts and obligations are based. Recessions also trigger a reduced volume of credit, which is an intricate part of financing capital formation — buildings, machinery, and inventory. Protective tariffs are often enacted during recessions to counter unemployment, but by increasing the cost of imported products they lower purchasing power. However much these factors make a recession worse, the fundamental force in bringing about the recurring cycles of increased unemployment is labor and capital's inaccessibility to land.

Unlike a mobile home that can be moved if the land rent becomes too expensive, those who invest in new buildings want to make sure that at no time in the future, can the land rent be raised above the value of the site; or if the locational value does go up, they want to make sure that the land rent will not be raised beyond their buildings ability to capture that rent above and beyond the return on the building itself. Otherwise, the lessee (building owner) would lose on her investment.

Borrowing money, buying the land, and paying interest on the loan, especially if only the interest is paid, is almost the same as fixing the rent once and for all. The payments do not go up even if the value of the land does. However, one might ask: how is a price placed on something that has no cost of production, cannot be reproduced? A parcel of land may offer an advantage and have an income, but how is that monthly or yearly income potential transformed into one payment once and for all?

### The Selling Price Of Land

Land, which has an income, but no cost of production is equated to capital, which has an income and a cost of production. The exchange value of capital regardless of its income (interest) will equal its cost of reproduction. Therefore, a parcel of land that yields \$100 in income would exchange for the same value as an item of capital yielding \$100 in income. If interest were 5%, then the selling price of the capital and the land would both be \$2,000. The process is called capitalization. That is to say: at 5% interest, you would need \$2,000 worth of capital in order to receive \$100

Rental Value of Land	\$110
Current Taxes paid	\$10
Unearned Income	\$100
Current Rate of Interest	5%
(Fee Simple) Selling Price	\$2,000

in interest income.

Although the value of capital and interest do not generally increase with the march of progress, the potential value and income of most land do. The price of land is based on its expected income in the future. There is no way to calculate the selling value of land based on its current income. The person who has the most money to bid and the greatest expectation about its income in the future sets the selling price of land.

### **Land Speculation**

As technologies advance, the same amount of labor and capital yield greater results and greater incomes from any particular piece of land. In many cases by reducing the price of products companies can so increase their volume of sales that it more than compensates for the lower profit per item and further increases their overall profits. However, it often requires more land to expand production. During periods of great technological advance like the railroads of the nineteenth century or cars and trucks of the twentieth century the unearned income of land increases rapidly and creates the expectation of even greater increases. As businesses strive to expand, to increase their profits the increased demand and expectations bid up the price of land. More and more money is offered for unused land, but many landowners are encouraged by this not to sell. Although they get no income from the land the value of their asset tends to increase. As long as it increases faster than the interest on a capital or monetary investment the idle land is a more profitable asset. Suppose someone owned a piece of unused land, and she was offered 10% more than she was offered the year before. Even if the real estate tax took 2% of the land's value, she would have enjoyed an 8% return on her asset. If the current rate of interest was 6% without inflation she would have enjoyed a higher return by holding idle land.

### **Reverberations**

The more the economy expands, the higher the price of land is bid, and the more profitable holding it as an investment becomes. At some point businesses find it more profitable to lay off workers rather than expand production. In short, when new inventions reduce the labor necessary to produce a product the natural tendency is not to lay off workers, but to lower prices, expand production, and increase profits through increased volume. But, when not enough land is offered for sale (too much land held for speculation) the alternative is to lay off the workers.

In turn, the unemployed carpenters stop buying new cars; the reduction in the demand for cars requires less people to make them; the unemployed auto makers stop buying refrigerators; the unemployed refrigerator makers stop buying new houses and so on. The reduction in demand reverberates throughout the economy in a cycle of recession or depression.

As unemployment reduces the demand for goods and services not only do wages and interest fall, but so does the demand for land. The price that's being offered for land stops increasing and begins to fall. At that point capital at any rate of interest would be a better investment. Therefore, one could expect that land would be sold, capital would be bought, and the recession part of the cycle would be over. However, land speculators like other investors consider short term versus long term. Consider the rapid increase in land values preceding a recession and the government's projections of economic recovery soon after a recession is confirmed; it is logical that many who can afford to, chose not to sell, but to wait for the end of the recession and the rise of land values again.

The selling price of land, like anything else, is set by the buyers. The reason we have a recession is that too many landowners refuse to sell. In other words, it's not the price, but the refusal to sell that causes the recession. Once the recession develops and the economy stops expanding, the price that's being offered for land begins to fall. At that point It seems most of the owners of idle land are willing to sell, but too many are not willing to sell for the highest price being offered. The more land that's held out of

use the more people are unemployed. Until land is sold unemployed labor and capital cannot engage in production.

### **Requisites To End A Recession / Depression.**

In order for the price of land to be affordable and workers to be reemployed one of three things could happen: Wages and interest could fall; the results of labor and capital could increase; or the price that is accepted for land could fall. In the course of every recession the general rate of wages and interest fall (Even if the lowest paid workers are getting nearly the same pay as before, the lowest paid jobs are often taken by more productive workers as the previously lowest paid workers become unemployed); every invention, innovation, and new discovery increases productivity and the rental income from land, narrowing the difference between the income from owning land and the previously unaffordable selling price of land; and finally, the price at which the owners of unused land will sell also falls in every recession.

By some combination of lower wages and interest, greater productivity, and reduced land prices land becomes affordable. People go back to work and the recession is over. As the economy grows and expectations increase, the selling price of land is bid up again, and the seeds of the next recession are sown.

### **Ameliorations of Recession / Depression**

When companies buy a piece of undeveloped land they not only have to acquire enough money to pay for the land, but they also have to acquire enough capital (buildings etc.), to maximize the potential of that land. If they borrow any part of the price of the land or the capital the rate of commercial interest on that loan will affect the profitability of their venture. Sometimes the Federal Reserve increases the supply of money and banks lend at lower interest rates. This lowers interest payments on buildings as well as the price of land and makes the price of land more affordable.

Sometimes one country invades another, as the Japanese invaded Manchuria or the Germans invaded Poland. This makes new resources available and puts their people back to work. In time of war governments sometimes require people to sell land for defense industries and the war effort. This gives labor and capital access to land.

### **Depression Caused By A Premature Extension Of The Margin**

In Progress and Poverty Henry George describes the free land margin as having been just barely capable of providing an opportunity to make a subsistence living. Along with the railroad came a great expectation, a surge of land speculation, and a premature extension of margin to land that would not support subsistence. Unemployment and the depression of 1873 were the result. In time the railroads and other inventions increased production, the marginal land became productive, people had a place to live and work, and the depression was over. Today, for all intents and purposes there is no free land margin. Therefore, it is necessary to understand recessions by way of the selling price of land.

### **Six Proposed Remedies For The Elimination Of Poverty**

There are six measures frequently proposed for the elimination of poverty. They are economy in government; increased education and better habits of industry and thrift; labor unions; cooperation instead of competition between labor and capital; governmental direction and interference; and land redistribution.

**Economy In Government** would permit lower taxes. In the absence of Min. Wage laws employers would soon find that workers who now paid less in taxes would continue to produce as much with lower pay. They would not get weak or sick, as they would be getting the same quantity of food clothing and shelter after taxes as before. As skilled workers began enjoying a greater reward for their superior productivity others would learn the same skills and knowledge. The supply of superior workers would

increase until the competition for the same number of jobs brought wages back to the previous after tax level. All the savings would go to landowners and other monopolists.

**Increasing The General Level Of Education** would be possible by either diverting government revenue from wasteful expenditures or by shifting the individual focus from recreation to study. Unlike the exceptional individual who increases her personal level of skill and knowledge and enjoys a higher wage, an increase in the general level of education will have no such effect. Under the present no free land circumstance wages tend to a bare minimum for the least productive workers — no matter how much they produce. Increasing the education and productivity of the least productive workers does not raise their pay. It simply raises the minimum level of productivity required for employment. When the vast majority of people could not read and write those who could commanded measurably higher wages. Now that more than 95% of Americans can read and write those skills are basic requirements for even the lowest paying jobs. All higher wages are based on those of the lowest and the supply and demand for superior workers. The same thing would apply to better habits of industry and thrift.

**Labor Unions** have often succeeded in raising the wages of their members. Generally, it has been in industries where there was a monopoly like the railroads or the Telephone Company or, more recently, state and local governments. In mining, workers have gotten some of what would have otherwise gone to land rent. Sometimes there are partial monopolies like the auto industry and the steel companies. In those cases, patents and tariffs against foreign competition enable higher profits out of which they can pay higher wages.

Theoretically, a union of all American workers could affect the general level of wages, but without such a comprehensive organization, because labor unions do not affect the margin of production, they cannot raise the general level of wages.

**Cooperation** is sometimes proposed between labor and capital. Risks would be shared and benefits would be pooled as is the case with profit sharing companies. However, the contest is between labor and capital on one side and landowners on the other. Labor and capital compete for natural opportunities, which are in short supply. Although the lack of competition in food cooperatives rarely deliver products cheaper than the free market, if they did, the increased productivity would in time bid up the price of land.

Share cropping is a case of cooperation where the producers and landowners have eliminated much of the risk and the necessity of producers advancing the land rent, but it has in no way increased wages. Nor has it given workers more of what they produced.

**Governmental Direction And Interference** have alleviated poverty. State run farms in other countries have fed large numbers of people. Social security and Medicare payments have been a blessing for many poor people who were too old to work. However, if these programs became large enough to eliminate poverty, it is believed that collecting the enormous revenues necessary to fund them might also engender great inefficiencies on the part of producers and attempts at evasion.

**Land Reform** or land redistribution has helped many people in impoverished countries. Where it has been implemented it has increased the number of landowners, but everyone did not receive land. Even if everyone gets land unless everyone gets land of equal value it is not equitable. Agriculture land is not all equally fertile or equally close to the markets. The value of residential, commercial, and industrial land is constantly changing as communities evolve. If the land is divided into individual parcels it would have to be re-divided every time the population increased. Although not irreconcilable, individual parcels of land would not likely be the most economical size. In agriculture individual plots would usually be too small for mechanized farming.