PRACTICAL POLITICS

April 2011 Issue No. 189

Elections to the Scottish Parliament, the National Assembly for Wales, and the Northern Ireland Assembly are set to be held on 5th. May. Whilst in this Issue (double our usual size) we have some items specifically related to their concerns, we also look at a government policy aimed at one particular English region. It is our claim that all our commentaries, wherever ostensibly rooted, are of general validity and reference. We begin, however, not by looking at dry land, nor yet at the waters, but by raising our heads.

RADIO SPECTRUM: rivals agree with each other and (in part) with us!

Shortly before the prorogation of Parliament in 1997, the Conservative government was contemplating collecting land value for public revenue purposes. The radio spectrum is classed as land in economic analysis, the air being part of the natural order outside of man and his products. The scheme to auction the air waves "is compelling…Few means of cash-raising, after all, can be so easily defended on economic grounds" [a]. A government source believes that "charging for the resource will result in more efficient use, with parcels of spectrum being freed up for new competitors" [b].

In 2000, the Labour government brought this prospect to fruition. After an auction spread over 8 weeks, 5 companies, from a starting list of 13, each won a 20-year licence to use part of the radio spectrum. The proceeds totalled £22,500,000,000. The winners were able to offer so-called third generation mobile phone services: "With internet, television, video, music, financial services and e-commerce to be available via handsets, the network operators will be a business conduit" [c]. The auction receipts were not a windfall, nor were they a sell-off. They are a legitimate rent, indeed a ***land rent***, capitalised in this case over 20 years, for the right to enjoy exclusive use, over that period, of a natural resource – a small part of the radio spectrum. Thus did the principle of LVT become within three years the bipartisan policy of both the Conservative and Labour parties. The Treasury used the money sensibly (those were the days!) to reduce the national debt. If a thin slice of air spectrum is worth £1,125,000,000 per annum, how vast must be the yield from the nation's land area as applied to the earth's surface where land really is land, to economist and layman alike!

With hindsight, the successful bidders paid too much. They were not, however, able to “pass on” the land value duty (for such it is) in extra charges to consumers, because competition ensured prices stayed at acceptable levels (and users would not have paid more anyway). This neatly vindicates the arguments that LVT can not be “passed on” in the form of higher charges to occupiers and higher prices for goods and services [d]. Instead, the shareholders (company owners) took the knock, which is what equity risk is all about, and we have seen “supply-side consolidation” (especially takeovers by those who did not bid so highly for licences in the first place).

There is a further lesson here. We have, since Issue No. 4, consistently favoured basing assessments on annual value (rentals), not on capital value (selling prices). These licences involve what amounts to up-front payment on a 20-year lease. Inevitably the cash flow arrives later, not early on. Perhaps worse, there is no recourse if the payment proves excessive, as here. Annual rental, charged on frequent revaluations, satisfies the public interest fairly.

Against this background, then, the Conservative and Liberal Democrat coalition government is to oversee a further auction of the airwaves next spring. Ofcom, the market regulator, has said that 4G (the fourth generation of mobile telecommunications services) can make use of that part of the spectrum that becomes available "as a result of the decision to end analogue TV broadcasts in a switch to digital transmissions" [e]. "Ofcom chief executive Ed Richards…admitted that slicing up the spectrum was a 'fiercely contested area' as the airwaves were 'strategic assets for the market for the next 20 years…I hope the debate does not spill over into litigation'…To maintain competition Ofcom will impose limits on the minimum and maximum amount of spectrum that bidders can win" [f]. Reports suggest that this will hand the Treasury between £2bn and £10bn, a range vague enough to raise quizzical eyebrows – surely something fiercely contested and determining the use of a strategically significant asset for the next 20 years should do better than this?

[a] and [b] Respectively Lex Column, "Financial Times", 22nd. March 1997, and Michael Prescott, "Sunday Times", 16th. March 1997, cited in "Practical Politics", Issue No. 70 (April 1997) [c] Robert Lea, "Times", 11th. April 2000, cited in "Practical Politics", Issue No. 97 (May 2000) [d] *Vide* "Practical Politics", Issue No. 37 (June 1993) [e] Sean Poulter, "Daily Mail", 23rd. March [f] Simon Duke, "Daily Mail", 23rd. March

GONE WITH THE WIND

"The UK government is encouraging 'green energy' by compelling suppliers to buy 11.1 per cent of their electricity from renewable sources. This official 'renewables obligation' which added £1bn to consumer bills in 2009-10 according to Ofgem, the energy industry regulator, has helped to make wind power a profitable business" [g]. No. It has made it a profitable racket, a legalised theft of cash from defenceless consumers' wallets. If windmills were profitable, they would be bidding for rights to the free air!

[g] David Blair, "Financial Times", 16th. April

DEPRESSION

Land is the ideal object of speculation. Nothing can take place without it. No more of it is being made. There are virtually no outgoings on it if one has no intention of doing anything with it, nor is it likely to deteriorate if left in the open. On the contrary, it is more or less guaranteed to rise in value without the slightest expenditure of effort on the part of its owner. It becomes, for all of these reasons, expensive to buy. As expectations of future gains rise, it is seen as an even more desirable possession. Money is being made from land deals. The sight of all this, verifiable in the daily newspapers, the weekly magazines, and the trade journals, breeds confidence. Less allowance is made for risk (risk? what risk?). Illusion takes over. Land speculation has taken off.

Landowners feel rich. The term, landowner, covers not only freeholders, but anyone who enjoys a beneficial interest in land, anyone who could make a profit from the simple process of further sub-letting his holding, whether he chooses to do so or not. Thus giant companies feel rich, big private landowners feel rich, many homeowners feel rich. He who feels rich from appreciating land values, feels no special urge to save from out of his ordinary income. He thinks he may safely consume more and save less. Are not land values doing his saving for him? Thus consumers wish to borrow, intending to repay from future gains from land holdings – provided that lenders can be found who will have confidence in land as collateral.

Building societies (in the domestic sector) and banks (in the important commercial sector too) delight in playing the pawnbroker and lending against complete security. They see in land all the advantages set out above, and, like everyone else, lose sight of the waiting traps. Bloated land values are mistaken for real wealth. Credit is extended. Later, as the thirst for apparently profitable lending increases, credit is allowed to rip. Consumers go on a credit-buying spree.

It cannot continue indefinitely, and it does not. The bubble bursts. The slump in land prices now throws the system in reverse. Easy credit is no longer available. Homeowners who bought at the peak with high mortgages, are caught with properties worth less than the amount of the outstanding loan. Falling land prices have removed the entire basis of the credit boom. There is now a rapid downward adjustment of expectations. Interest rates hurt. Lenders are in trouble. Borrowers do not meet repayments, and the collateral for the loans is not there. Investor borrowing and consumer borrowing are depressed. Recession depresses land prices still further. Entrepreneurs face ruin. Unemployment rises. The paradox is complete: the boom combined a falling savings ratio with artificially stimulated capital-intensive investment, and now there is a slump with investment depressed and savings rising as a proportion of income [h].

Cue printing of paper money (quantitative easing), spending cuts, rising taxes. The menu consists of large dollops of hope and exhortation, without even a side plate of willingness to learn lessons. 1974, 1992, 2009……2026?

Footnote:– There is a bright note. "I think we should deal with land speculation. I believe that now is the time for land value taxation. If we tax the wealth in land, we will encourage development rather than preventing it" – John McDonnell, M.P. (Hayes and Harlington) [j]

[h] This introduction has been extracted and condensed from a lengthier essay on the evolution of the boom/slump cycle, "Landing In Trouble", which appeared first in "Practical Politics", Issue No. 29 (July 1992)
[j] Extracted from his speech in the Budget Debate, House of Commons, 24th. March 2011

MORE DEPRESSION

Since our last Issue **gold** has broken through the $1,500 per troy ounce barrier, to $1,512.50 (eat your heart out, Gordon Brown!), underlining the markets' lack of faith in all the major currencies and thus in the economic policies of all the major governments. The **U.S.A.** "risks being stripped of its prized AAA credit rating…Standard & Poor's has warned…The rating agency cut its outlook on the US from stable to negative in a powerful shot across the bows of politicians in Washington…America's position as the world's biggest economy, and the dollar's role as a reserve currency, has afforded politicians a breathing space not enjoyed by smaller economies such as Britain" [k] but now "S&P has blown a hole in the traditional assumption that there is a 'risk-free' return sovereign debt, such as US Treasuries…There has to be a higher risk premium for holding US Treasuries, another expense Americans can ill afford…a stark reminder that if you rely on borrowing to fund your lifestyle then you need to have policies to make sure someone will keep lending to you. Banks discovered this the hard way in 2007/08. Now politicians are discovering it for themselves" [m].

Europe of course is in a mess. "The total exposure of foreign banks to the struggling quartet of Greece, Ireland, Portugal and Spain tops $2.5 trillion once all forms of risk are included, according to…the Bank for International Settlements. The BIS...said…that Germany had $569bn of exposure to the quartet, France $380bn, and the UK $431bn. A chunk of British exposure is on behalf of Mid-East and Asian clients banking through London. Italy has just $81bn at risk and seems uniquely insulated from the crisis all around it… British-based banks and subsidiaries have$225bn at stake in Ireland, and $152bn in Spain…France is up to its neck in Greece with $92bn; a Benelux-led group has $180bn in Spain, and Spain itself has exposure of $102bn to Portugal. The complex web of lending shows how hard it is to contain the problem to one country at a time" [n].

"Greece, Ireland and Portugal are all bankrupt. However hard these countries try …they will never, ever be able to pay off their debts…The tried and tested response is to default, then reschedule debts by reducing coupons (ie interest payments) and extending maturities, while allowing the national currency to depreciate, so that the economy can once again become competitive. Their membership of the euro zone, however, means that none of this can happen", not least because "massive sums would have to be written off on the balance sheets of many of European banking's most famous names, sending some spiralling towards bankruptcy…It is all too easy to understand why the European Union has gone into collective denial" [p].

"Interest rates on 10-year Greek bonds hit 13 per cent…By contrast, rates on similar German bonds are around 3 per cent. Credit default swaps, financial products that offer insurance against the risks of a government failing to repay its loans, later hit record highs for **Greece**" [q]. "Greek savers have withdrawn deposits amounting to more than €40bn over the past year – equivalent to about 14 per cent of total deposits held in Greek banks" [r]. "Mounting fears that **Portugal** may have to seek financial assistance drove the yield on the country's ten-year government bonds above 8 per cent to euro-era highs" [s]. Days later, with the budget in deficit and "household and corporate borrowings equivalent to two-and-a-half times national output", economists feared Portugal would be unable to escape its debts [t]. Portugal finally admitted defeat, and joined Greece and Ireland in requesting a bail-out. Talks were subsequently begun about "the terms of an €80bn rescue package" [u]. "There will be a pause for breath but attention will soon turn to **Spain**. Its exposure to Portuguese banks will be of increasing concern. But so too will its own banks, particularly its savings banks, or cajas…Madrid needs to come clean on exactly how big its own bail-out of these deeply troubled institutions is going to be" [m]. "Britain's lenders have a total of £93.3 billion of Spanish-related loans and assets. These would turn into losses in the event of a default by Madrid" [w].

Meanwhile, following the announcement of the results of a series of stress tests conducted in the **Republic of Ireland** for the Central Bank of Ireland, four major banks have to raise, in total, "€24bn in new capital, which is expected to lead to the almost complete nationalisation of the country's banking system" [y]. The Anglo Irish Bank is already completely nationalised. The Bank of Ireland must raise further €5.2bn, Allied Irish €13.3bn, EBS €1.5bn, and Irish Life & Permanent €4.0bn. Anglo-Irish later announced it will be making 2,000 of its staff redundant after a loss of €10.4bn in 2010, and said the losses had arisen from " writedowns on residential and commercial property lending" [y]. Of the new capital to be found, one commentator noted that "the Irish said they would pour another €24bn they do not have into their banks" [z]. "The Irish government admitted the final bill for bailing out its stricken banks would now top €70 billion" [aa]. "These continue to be worrying times for British banks and savers, as they remain the most exposed of any European nation to the fortunes of Ireland" [bb].

It is needful to record these steps to misery because, as we have asked previously, **"Do academics, politicians, civil servants, commentators, businessmen, and bankers still not see how important is the rôle of land in the economy, and how corrosive the effect of ignoring it can be in, to take but one example, the boom/slump cycle?"** [cc].

[k] Richard Blackden, "Daily Telegraph", 19th. April [m] Damian Reece, "Daily Telegraph", 19th. April *[U.S. Treasuries are the equivalent of U.K. gilts – ed.],* 8th. April [n] Ambrose Evans-Pritchard, "Daily Telegraph", 14th. March [p] Peter Oborne, "Daily Telegraph", 8th. April [q] James Kirkup, "Daily Telegraph", 15th. April [r] Kerin Hope and Ralph Atkins, "Financial Times", 16th. April [s] "Financial Times", 2nd. April [t] Philip Aldrick and Bruno Waterfield, "Daily Telegraph", 8th. April [u] Louise Armitstead, "Daily Telegraph", 19th. April [w] Geoff Ho, "Sunday Express", 10th. April [y] Harry Wilson, "Daily Telegraph", 1st. and 4th. April, 13th. April [z] Lex Column,"Financial Times", 2nd. April
[aa] Andrew Johnson, "Daily Express", 1st. April [bb] Harry Wilson, "Daily Telegraph", 1st. April
[cc] "Practical Politics", Issue No. 188, March 2011

SOUTH-WEST ENGLAND TO BE GIVEN WATER AID

South West Water "has spent £1.5 billion revamping the region's sewage system" [dd]. The Chancellor has described the area's water bills as "unusually high", and money is to be set aside for relief payments. "Home owners…have been paying the price of cleaning up the region's coastline." We examined this at some length at the scheme's inception [ee]. Bill payers argued it was unfair for them to pay to clean the beaches to benefit tourists. We agreed that the inhabitants of the interior had little direct interest in the coastal holiday resorts and would be paying disproportionately to the benefits they themselves would obtain. The advantages would indeed seem to accrue primarily to people and businesses operating in the main tourist resorts, or rather to the lucky landholders who ultimately rake in those benefits. Tourists bring their own land values with them too, though, for without them the resorts would not last five minutes. All of this, LVT would pick up naturally, as land values react to the gains and, occasionally, losses sustained as a result of the economic activity of private persons and public bodies collectively. There is no incentive for those of us unfortunate enough to reside outside the south-west to urge financial help to the region – unless of course we could be sure that the location benefits would be returned to us later via LVT, just as we are content to share our land value with the south- westerners. However, we definitely do resent contributing to the bank balances of landholders.

[dd] "Daily Telegraph", 24th. March [ee] "Practical Politics", Issue No. 34, March 1993

LVT AN ELECTION ISSUE IN SCOTLAND – and some food for thought

"A Group representing rural landowners and property businesses has described Green party plans to introduce land value taxation as horrific" [ff]. Representatives of the main political parties had attended a hustings debate in Edinburgh, "but it was the Greens' plans to tax land rather than property, that caused the most concern. Former Green MSP, Robin Harper defended the tax". Jim Hume, for the Liberal Democrats "swiftly distanced the party from the proposal…Lib Dem policy is not for LVT". Sarah Boyack said she did "not anticipate LVT being a big priority for Labour" but avoided outright condemnation. "Conservative candidate Miles Briggs was silent on land value taxation". The report made no mention of the Scottish Nationalists.

The SNP has never to our knowledge explained what it wants independence for, if not to give Scotland to its citizens. This is achieved by collecting the annual rental value of all land for public revenue purposes, in place of contemporary taxes. The Hamilton Grand hotel at St. Andrews is currently being converted to unashamedly grand apartments "on a 99-year lease…for £5.5 million" [gg]. The attraction is its location, with "stunning views of the 18th green". The workmen's wages are taxed, their purchases are taxed (including the cost of a home), their savings are often taxable; and their employers are likewise plagued by tax. Yet labour and capital are the wealth creators! What does the landowner, as mere holder of a piece of paper, actually do – except get out of the way and let others work? "One of Edinburgh's most striking buildings, the former Donaldson's College, is being put on the open market…[It] is set on 18 acres of land near Haymarket…It has planning permission for 63 apartments for the existing building and a further 72 to be built within the grounds" [hh]. No guide price has been disclosed, but the estate agency has hinted that prime properties in prime locations attract buyers from across the globe, indicating a record sum.

[ff] "Daily Record", 19th. April [gg] Cathy Hawker, "London Evening Standard", 16th. March [hh] Andrew Bolger, "Financial Times", 2nd. April

ENDING THE SCOURGE OF THE UNEVEN PLAYING FIELD

A house hunter starts by working out how much he can afford to pay. He has the sales value of his present place plus what he can afford from his savings plus what he is likely to want (and get!) by borrowing. He deducts agent's and legal fees, allowances for moving costs, new curtains and carpets, and a healthy contingency allowance. He will assess changes in such costs as council tax, mortgage payments, insurance, and travel to work and to shops. From this he assesses the maximum affordable purchase price for his new house plus of course the attendant SDLT (stamp duty).

A businessman conducts much the same sort of exercise when selecting a location for his activity. His significant costs are likely to be wages and capital on site, plus transport of inward supplies and outward goods. On top of everything else, he must pay the payroll taxes (income tax plus National Insurance) together with enough to enable his employees to take home a net living wage (*i.e.* covering their VAT, council tax, *etc.*) plus the fully built-up post-tax costs of his company's transport needs (including motor fuels).

Sites in Northern Ireland, Scotland, and Wales are prone to be remote from the big markets in south-east England and at the continental heartland. To-day's taxes bear on production and cripple or kill marginal businesses. That is the stark truth. A switch to land-rent capture (LVT) is crucial – **crucial**. Land value is a surplus, representing the advantage a site enjoys in relation to the poorest land in use, and LVT would thus hit the remoter regions least.

JUST A THOUGHT (nothing at all to do with LVT)

The voting system known as first-past-the-post is used exclusively for elections to Westminster (as the alternative vote variant of it will be, if it wins the day in the referendum on 5th. May). The Scottish Parliament and the assemblies in Wales and in Greater London, use a hybrid of first-past-the-post and a proportional regional top-up taken from lists supplied by the parties. For the European Parliament in England, Wales, and Scotland, it is done entirely by proportional voting from regional party lists. What is the point of giving party bureaucracies the power to determine who gets on the list and in what immutable order? How does that produce a better quality of representative? There is one part of the United Kingdom which really does have a much superior system, and that is Northern Ireland, where all elections, except for Westminster, are by the single transferable vote in multi-member constituencies. Parties put up lists, but voters are free to deploy their preferences in any order, and across any parties (including independents and party recalcitrants) they want. The implications for democratic choice are many. Power to the people! [jj]

[jj] Extracted from "Practical Politics", Issue No. 175 (July 2009), with minor adaptations

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