

# Australia's Rent-Seeking: Anatomy of a Depression?

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## **Australia's Rent-Seeking: Anatomy of a Depression?**

**ECONOMIC FORECASTS:** Although accurate forecasting is the test of any valid scientific explanation, it is not a characteristic one relates to the study of economics. Treasury's latest econometric model "TRYM" conjures up its m<sup>th</sup> try to find out what is happening to the Australian economy. If TRYM does not integrate the productive and speculative aspects of the economy, it is also doomed to failure.

There is absolutely no evidence that federal Treasury, the Reserve Bank, nor business analysts bothered to quantify the funds that flowed into real estate throughout the 1980's. They majored on figures and indices on the productive side of the economy, but had no interest in the destructive figures on the speculative or rent-seeking side.

The late doyen of the Australian property valuation profession, Dr John Murray, saw this blind spot in economics, saying:

*"Valuation is the most important subject in the social sciences, but it has always been outside the scope of economics as taught in the universities ..... a re-integration of the theory of valuation with the main body of economic theory would lead to an advancement of learning and to a soundly-based national economy."*<sup>1</sup>

One body which did take in the whole picture was able to forecast major economic recession from 1991 - in a submission to the Economic Planning Advisory Council (EPAC) dated as early as 1 May 1984.<sup>2</sup> Whilst EPAC still tries to fathom what has happened to the economy, the lonely and unsophisticated submission presumably moulders within its own archives.

The following details, collated by the Land Values Research Group, reinforce Dr Murray's opinion and show that escalating land prices act, even more than taxes, to divert capital and thereby curb effective demand and productive investment - with corresponding implications for economic activity and employment.

## THE FIGURES:

### **Aggregate Sales and Values of Australian Real Estate**

<u>FIN. YEAR</u>	<u>SALES (1)</u>	<u>No. SALES</u>	<u>TOTAL VALUES (2)</u>
1984	\$36,338,617,503	556,145	\$464,792,311,695
1985	\$38,445,314,898	538,136	\$520,573,620,800
1986	\$42,308,078,259	513,473	\$553,869,594,512
1987	\$50,020,185,622	514,932	\$639,548,486,280
1988	\$77,003,258,965	654,106	\$785,884,232,799
1989	\$87,709,069,753	661,503	\$1,021,427,550,000
1990	\$65,454,422,569	486,412	\$866,665,800,000
1991	\$61,992,604,105	490,267	\$824,670,000,000
1992 (est.)	\$57,000,000,000	-	\$715,000,000,000

#### **Mean Break-up of Sales by Value :-**

NSW	40%	SA	6%
Vic	25%	Tas	1.5%
Qld	16%	NT	0.5%
WA	10%	ACT	1.0%

### TABLE A

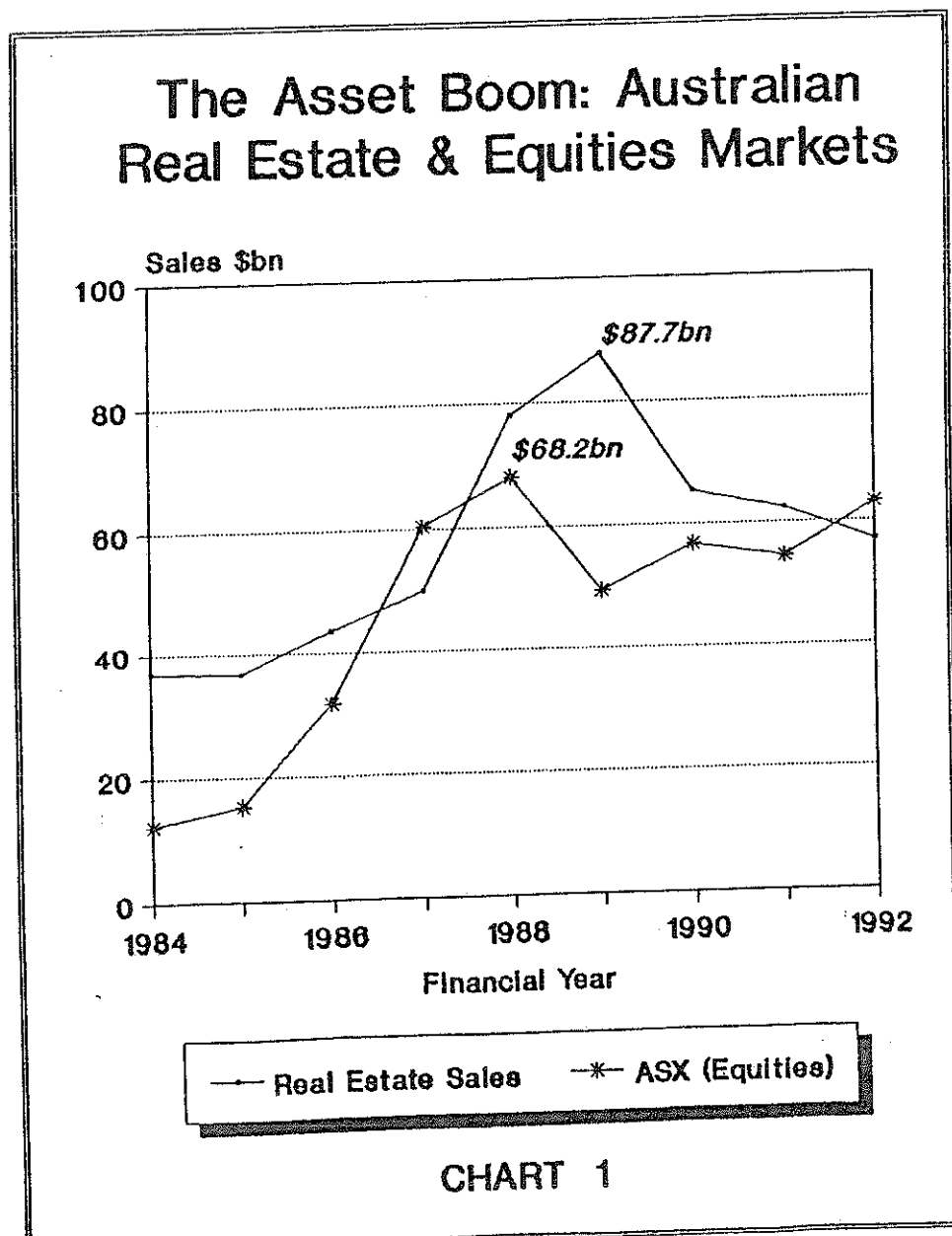
The most outstanding thing in connection with the total volume of real estate sales (Table A) is that it doubled between 1986 and the peak in 1989 at \$87.7 billion. Total values did not quite double, but they rose 1.84 times in the same period: and they rose to a significant figure. We are not used to the word "trillion" in Australia, but we reached \$1.021 trillion in total real estate values in 1989. That is, one million million dollars, or  $10^{12}$ . Average turnover was just in excess of 8% of the total value of real estate each year during this period.

Following the collapse, a figure equivalent to one year of the national income has been written off the value of Australian properties.

Furthermore, due to massive levels of private debt accompanying the boom, it seems that the market will continue to decline for a number of years yet.

On average, New South Wales accounts for 40% of Australian real estate sales by value - a surprisingly high rate considering its population relative to Victoria. Prima facie, this appears to indicate higher private debt levels in New South Wales.

Chart 1 is a more interesting representation of the figures, together with Australian sharemarket sales (ASX) for comparison. Viewed together, this has become known as the '80's "asset boom". Both markets were irrational and ultimately unsustainable. They were encouraged by a tax system which scarcely interferes with rampant speculation, yet levies a myriad of fines upon productive activity.



The speculative binge is comparable to those of the 1880's and 1920's, and the sales "bubbles" which burst are clearly evident. Between 1986 and 1989 we sank \$469.2 billion into both markets. This was equivalent to 51% of our national income for the same period.

Unlike the 1920's, the sharemarket "went" first. There was a 550% increase in the volume of sharemarket sales in the 3 years to the peak at \$68.2bn in 1988, and a lesser increase of 240% in real estate for the 4 years to its peak at \$87.7 billion.

The shape of the two graphs is remarkably similar, because there is a closer relationship between the two markets than is generally admitted - much of the value of shares being underpinned by real estate. One market tends to feed off the fortunes of the other until a "correction" is made. For example, the ASX actually outdid the property market in the financial year before the October '87 "bust", which then reinforced the property market. Shares have surpassed real estate sales again in 1992, capitalising to about one third of the real estate market - when they are more traditionally no more than one quarter. This is suggestive of the future direction of the stockmarket when it factors the property collapse back into the value of shares.

Both the share and property markets perform valuable roles, but neither are well served by such periods of mindless speculation.

## Real Estate Sales and National Income: Australia

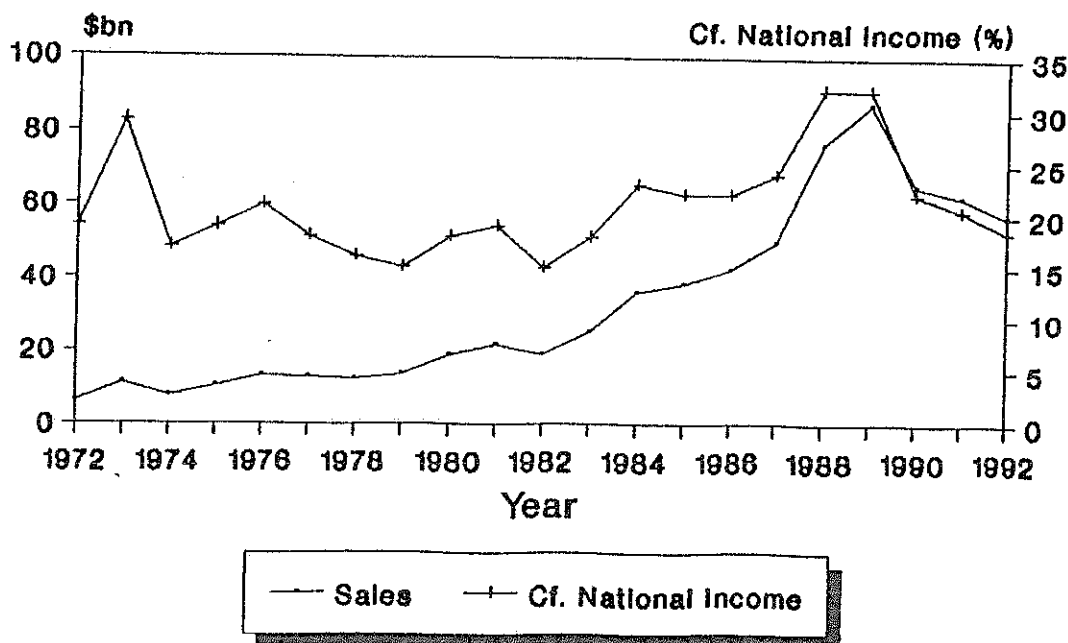


CHART 2

As Victoria's real estate transactions are comprehensively recorded by the Valuer-General's office since 1972, it is possible to extrapolate sales for Australia back to that year, using the fairly consistent nexus of 25% that exists between Victoria and the whole of Australia. They are shown in real terms at Chart 2 against national income, for comparison.

Real estate sales moving up from less than 20% as against national income to 30% at the peaks of land booms tend to confirm that speculative periods are at the expense of national productivity. So, contrary to popular mythology, it seems healthier for the prospects of the general economy when real estate prices are flat, or down - as they are now.

Empirically, it seems a good indicator that we are on course for difficult economic times when real estate sales go beyond 25% as against national income, as they did in 1973 (29%) and also in 1988 and 1989 (32%) ..... or, where the number of sales gets beyond 500,000, as in 1973, and from 1984 to 1989:

## Number of Real Estate Sales Australia

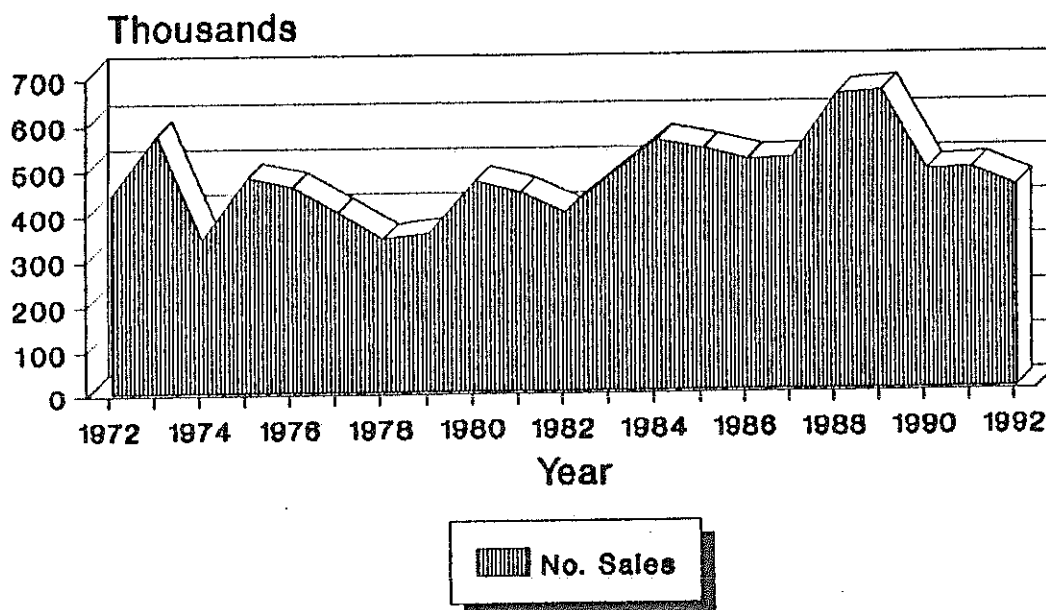


CHART 3

The similarity of shape of the *value* of sales as a percentage against national income (Chart 2) and of the graph for *number* of sales (Chart 3) shows the value of sales to be extremely numbers-sensitive. This would appear to be worthy of further investigation, in order to see if a formulaic relationship can be established between number and price.

As ever, the dynamic in the property market was the land component. Chart 4 shows that land prices grew even more quickly against national income than they did as a proportion of total real estate sales:

## INCREASING LAND PRICES

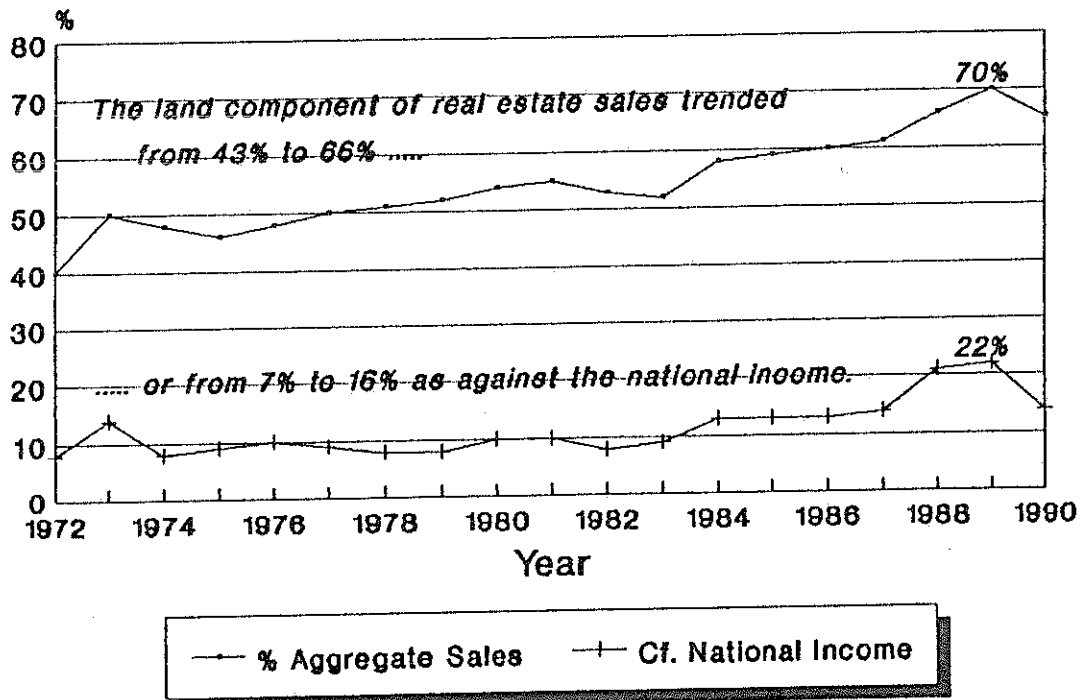


CHART 4

**CONCLUSIONS:** Chart 5 gives the whole picture, back-indexed for inflation in terms of the 1972 dollar - so that we have consistent comparison; it is arguably the ultimate economic indicator. We can see immediately that the '90's will be no simple recessionary period:

# Australian Real Estate Sales As an Economic Indicator

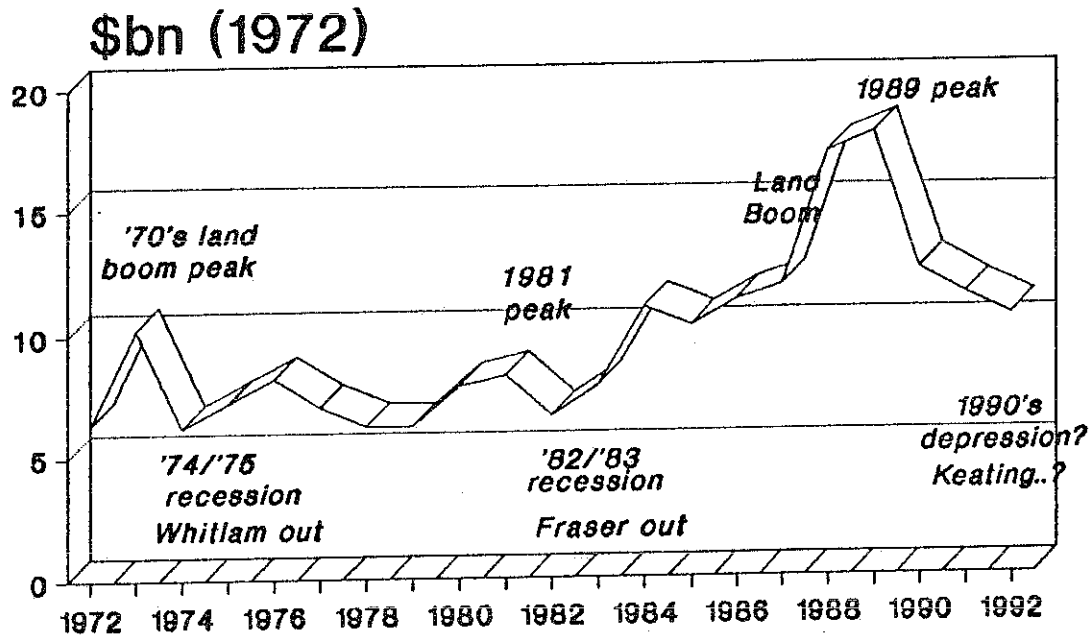


Chart 5

What are the implications of these figures for public policy, then?

Would Mr Keating have re-introduced "negative gearing" in August 1987, thereby adding fuel to the Inferno, if Treasury had this data?

Could he have said, as he did as late as June 1989, that the flow of funds through the late '80's was largely the gearing up of our capital stock?

Where has the Reserve Bank been without the critical information that these statistics contain?

The figures show the process by which capital has been highjacked for the purposes of speculative rent-seeking in real estate. The sheer extent to which capital investment has suffered as a result, appears to lay bare the anatomy of a depression.

The two hundred years since the Industrial revolution has shown consistently that every economic recession and depression is preceded by a land boom.....but to date we have chosen to ignore this rather obvious fact.



## U.S. ECONOMIC & POLITICAL CYCLES

Land Boom Peak	Building Cycle Peak	Economic Recession	Political Upheaval
-	-	-	1788
1818	-	1819	1824
1836	1836	1837	-
1854	1856	1857	1860
1872	1871	1873	-
1890	1892	1893	1896
WW I	1916	1918	-
1925	1927	1929	1932
WW II interrupts cycles			
1955	-	-	-
1972	1973	1974	-
1989	1990	1992	1996*

\* *Economic Intelligence* prediction <sup>3</sup>

### TABLE B

Although Table B provides US dates, they are very similar to those of Australia. <sup>3</sup> We could perhaps note that the mid to late '50's property boom in Australia was brought to a halt by the '61 "credit squeeze". Similarly, the events of 11 November 1975 attest to political upheaval in Australia in the wake of the '74 recession.

By continuing to blame a passing parade of politicians and entrepreneurs for the cycles of recession and depression, we grab at the sensational and miss underlying causes.

Unless valuers and economists combine to study the "Invisible" half of the economy, in order to establish what is happening to the rent of our natural resources, our chance of regulating the Australian economy seems to be on a par with King Canute in controlling the tides. At the threshold of the 21st century, we remain in the dark ages in economic terms.

There is no better time to cut taxation and take a greater part of the economic rent of our natural resources, in order to reduce speculative proclivities and return people to work. However, political inertia and a lack of awareness at the grass roots of the process described, still provide major stumbling blocks.

British property developer and foreign exchange dealer, Ronald Banks encapsulated the current world economic situation most succinctly: "The time has now come to retrieve the theory of rent from its obscurity, and to re-affirm the role of nature in the destiny of mankind".<sup>4</sup>

If we wish to break the socially devastating cycle of speculation and economic depression, he is decidedly correct.

#### *References*

- 1 *Murray, JFN, Valuation And The National Economy, Connecticut, USA, John C Lincoln Institute, 1967, p.2.*
- 2 *Association for Land Value Taxation, submission in connection with 1985 National Tax Summit, 1 May 1984*
- 3 *Economic Intelligence # 31, Centre For Incentive Taxation Newsletter, London, March 1992.*
- 4 *Banks, R, (ed) Costing The Earth, London, Shephard-Walwyn, 1989, foreword p.x.*

#### *Other Sources*

##### *(1) Property sales data:*

*Office of State Revenue, New South Wales  
Office of the Valuer-General, Victoria  
Department of Lands, Queensland  
Office of Titles, Western Australia  
Land Titles Office, South Australia  
Commissioner of Stamp Duties, Tasmania  
Valuer-General, Northern Territory  
Land Information Office, ACT*

##### *(2) Land values data:*

*Commonwealth Grants Commission reports*

##### *Other:*

*Australian Stock Exchange Limited Annual Report 1991-92*

*National Accounts - Australia*

*ABS: CPI All Groups Time Series Report*

(1) AGGREGATE OF ALL AUSTRALIAN REAL ESTATE SALES

STATE/TERRITORY	1984 Sales	No. Sales	1985 Sales	No. Sales	1986 Sales	No. Sales	1987 Sales	No. Sales	1988 Sales	No. Sales	1989 Sales	No. Sales	1990 Sales	No. Sales
ACT	\$15,400,000,000	180,000	\$16,000,000,000	170,000	\$18,000,000,000	171,000	\$20,000,000,000	165,000	\$28,000,000,000	160,000	\$33,275,760,000	180,838	\$24,048,910,000	137,468
NT	\$9,202,013,185	14,822	\$9,129,984,958	12,322	\$10,894,819,454	12,813	\$14,083,733,084	11,070	\$21,793,298,279	18,424	\$19,097,812,118	13,750	\$13,931,222,450	10,415
NSW	\$5,680,287,984	10,107	\$5,149,911,467	10,148	\$5,539,493,376	8,270	\$6,845,678,589	8,438	\$12,856,918,855	14,203	\$16,676,782,708	15,571	\$12,628,568,548	11,449
QLD	\$2,880,951,715	6,016	\$3,558,875,261	7,048	\$3,672,593,498	6,270	\$4,502,618,589	6,526	\$7,056,254,263	8,819	\$10,680,848,305	10,129	\$7,881,563,252	6,445
SA	\$2,000,000,000	4,000	\$2,132,000,000	4,000	\$2,520,000,000	4,200	\$3,008,261,848	4,314	\$4,941,174,401	4,870	\$5,209,879,421	5,829	\$4,711,171,417	5,019
TAS	\$548,000,000	1,000	\$702,000,000	1,800	\$825,359,812	1,883	\$905,853,333	1,807	\$1,163,564,639	2,041	\$1,353,360,130	2,003	\$1,117,275,949	1,823
VIC	\$236,584,359	2,000	\$205,041,212	2,400	\$324,012,119	2,400	\$252,405,121	1,800	\$297,558,527	2,100	\$395,987,071	2,700	\$434,450,953	2,600
WA	\$390,000,000	6,000	\$467,500,000	5,600	\$532,000,000	5,800	\$541,740,000	5,834	\$594,480,000	5,454	\$1,037,660,000	7,982	\$903,454,422	6,431
ACT & NT	\$36,338,517,503	55,143	\$38,445,318,898	53,165	\$42,108,078,259	51,473	\$50,020,183,632	51,432	\$77,003,259,985	65,106	\$87,709,059,753	61,203	\$85,454,422,569	48,412
ACT & NT	\$71,076,388,132	582	\$72,582,733,790	534	\$75,384,846,936	604	\$80,514,313,729	612	\$80,872,150,917	628	\$81,398,348,827	763	\$83,199,318,886	652
ACT/TERRITORY	Mean	% Sales	Mean	% Sales	Mean	% Sales	Mean	% Sales	Mean	% Sales	Mean	% Sales	Mean	% Sales
NSW	\$55,000	42.10%	\$54,118	41.67%	\$104,283	42.55%	\$121,212	39.88%	\$175,000	36.36%	\$183,911	37.94%	\$188,565	36.74%
NT	\$51,104	25.37%	\$71,708	23.75%	\$55,025	23.75%	\$107,601	28.12%	\$118,304	28.10%	\$142,787	21.77%	\$133,793	21.28%
QLD	\$54,567	15.63%	\$50,599	16.00%	\$58,978	15.09%	\$78,325	13.79%	\$90,482	16.70%	\$106,512	19.01%	\$110,286	19.09%
SA	\$47,814	7.93%	\$50,511	9.26%	\$58,509	8.68%	\$68,651	6.02%	\$89,408	8.47%	\$105,325	12.15%	\$119,173	11.74%
TAS	\$30,000	5.50%	\$32,000	5.53%	\$36,000	5.96%	\$39,710	6.02%	\$39,408	6.47%	\$37,203	5.94%	\$39,832	7.20%
VIC	\$36,000	1.78%	\$39,000	1.83%	\$43,755	1.95%	\$50,276	1.81%	\$57,216	1.51%	\$67,624	1.54%	\$67,213	1.71%
WA	\$118,432	0.63%	\$127,101	0.79%	\$133,005	0.77%	\$140,225	0.50%	\$141,893	0.38%	\$146,662	0.45%	\$167,097	0.86%
ACT & NT	\$55,000	1.07%	\$55,000	1.22%	\$55,000	1.26%	\$110,000	1.28%	\$120,000	1.62%	\$130,000	1.62%	\$140,000	1.58%

LAND VALUES RESEARCH GROUP 1992

STATE/TERRITORY	1984 Sales	No. Sales	1985 Sales	No. Sales	1986 Sales	No. Sales	1987 Sales	No. Sales	1988 Sales	No. Sales	1989 Sales	No. Sales	1990 Sales	No. Sales
ACT	\$109,000,000,000	44,482	\$119,078,600,000	42,852	\$127,450,700,000	42,19%	\$156,280,500,000	44,652	\$224,486,700,000	47,612	\$274,447,500,000	47,612	\$320,000,000,000	52,000,000,000
NT	\$80,123,000,000	24,532	\$73,834,000,000	26,442	\$82,609,200,000	27,342	\$98,444,800,000	27,732	\$123,571,900,000	26,212	\$142,787	21.77%	\$133,793	21.28%
NSW	\$31,573,000,000	12,802	\$33,733,300,000	12,682	\$35,551,800,000	11,772	\$38,472,700,000	10,832	\$48,909,000,000	10,372	\$58,325	16.70%	\$106,512	19.01%
QLD	\$17,456,100,000	7,122	\$20,974,800,000	7,512	\$22,593,400,000	7,482	\$25,213,900,000	7,112	\$34,915,800,000	7,402	\$42,787	11.74%	\$119,173	11.74%
SA	\$19,386,000,000	7,912	\$22,816,000,000	8,172	\$24,222,800,000	8,022	\$25,634,900,000	7,232	\$27,672,400,000	5,872	\$32,672,400,000	5,872	\$32,672,400,000	5,872
TAS	\$3,365,100,000	1,372	\$3,750,100,000	1,422	\$4,022,100,000	1,332	\$4,328,400,000	1,222	\$5,114,800,000	1,082	\$5,114,800,000	1,082	\$5,114,800,000	1,082
VIC	\$1,369,100,000	0,562	\$1,577,000,000	0,562	\$1,861,500,000	0,562	\$1,864,500,000	0,512	\$1,753,400,000	0,372	\$1,753,400,000	0,372	\$1,753,400,000	0,372
WA	\$3,000,000,000	1,222	\$3,447,000,000	1,232	\$3,999,500,000	1,372	\$4,551,400,000	1,282	\$5,106,700,000	1,082	\$5,106,700,000	1,082	\$5,106,700,000	1,082
ACT & NT	\$245,072,300,000	12,222	\$279,702,800,000	12,332	\$302,121,700,000	12,332	\$354,723,200,000	12,332	\$471,530,700,000	12,332	\$550,000,000,000	12,332	\$620,000,000,000	12,332
ACT & NT	\$369,578,530,000	12,222	\$397,123,080,000	12,332	\$432,121,700,000	12,332	\$504,206,520,000	12,332	\$620,000,000,000	12,332	\$715,000,000,000	12,332	\$820,000,000,000	12,332
ACT/TERRITORY	Mean	% Sales	Mean	% Sales	Mean	% Sales	Mean	% Sales	Mean	% Sales	Mean	% Sales	Mean	% Sales
NSW	\$208,724,146,200	\$222,022,039,700	\$233,658,607,330	\$281,758,293,740	\$274,144,372,781	\$274,144,372,781	\$274,144,372,781	\$274,144,372,781	\$274,144,372,781	\$274,144,372,781	\$274,144,372,781	\$274,144,372,781	\$274,144,372,781	\$274,144,372,781
NT	\$114,026,383,871	\$117,663,493,850	\$151,450,193,942	\$151,450,193,942	\$177,468,129,920	\$177,468,129,920	\$177,468,129,920	\$177,468,129,920	\$177,468,129,920	\$177,468,129,920	\$177,468,129,920	\$177,468,129,920	\$177,468,129,920	\$177,468,129,920
QLD	\$39,500,519,621	\$52,077,092,850	\$53,107,514,600	\$53,107,514,600	\$54,408,464,890	\$54,408,464,890	\$54,408,464,890	\$54,408,464,890	\$54,408,464,890	\$54,408,464,890	\$54,408,464,890	\$54,408,464,890	\$54,408,464,890	\$54,408,464,890
SA	\$33,106,397,876	\$38,107,514,600	\$42,544,161,000	\$42,544,161,000	\$44,408,464,890	\$44,408,464,890	\$44,408,464,890	\$44,408,464,890	\$44,408,464,890	\$44,408,464,890	\$44,408,464,890	\$44,408,464,890	\$44,408,464,890	\$44,408,464,890
TAS	\$36,382,085,482	\$38,107,514,600	\$42,544,161,000	\$42,544,161,000	\$44,408,464,890	\$44,408,464,890	\$44,408,464,890	\$44,408,464,890	\$44,408,464,890	\$44,408,464,890	\$44,408,464,890	\$44,408,464,890	\$44,408,464,890	\$44,408,464,890
VIC	\$2,596,589,089	\$2,940,316,500	\$3,426,931,500	\$3,426,931,500	\$3,999,500,000	\$3,999,500,000	\$4,551,400,000	\$4,551,400,000	\$5,106,700,000	\$5,106,700,000	\$5,106,700,000	\$5,106,700,000	\$5,106,700,000	\$5,106,700,000
WA	\$5,689,655,400	\$5,426,931,500	\$5,999,500,000	\$5,999,500,000	\$6,426,931,500	\$6,426,931,500	\$6,999,500,000	\$6,999,500,000	\$7,551,400,000	\$7,551,400,000	\$8,026,931,500	\$8,026,931,500	\$8,501,400,000	\$8,501,400,000
ACT & NT	\$466,582,311,835	\$520,573,620,600	\$553,883,584,517	\$553,883,584,517	\$620,000,000,000	\$620,000,000,000	\$715,000,000,000	\$715,000,000,000	\$820,000,000,000	\$820,000,000,000	\$920,000,000,000	\$920,000,000,000	\$1,020,000,000,000	\$1,020,000,000,000
ACT & NT	\$78%	7.1%	\$78%	7.1%	\$78%	7.1%	\$78%	7.1%	\$78%	7.1%	\$78%	7.1%	\$78%	7.1%

Stated areas describe estimated figures

Kavanagh, Bryan

March 4, 1993

TO: Harry Pollard  
John Burger  
Stan Frederikson  
✓ Robert Clancy  
Steve Cord  
Dan Sullivan  
Mitch Chanelis  
Alanna Hartzok  
Sam Venturella  
✓ George Collins  
Mike Curtis

FROM: Oscar Johannsen

I thought you might be interested in the paper which Bryan Kavanagh of Australia did on the effect of real estate speculation on Australian economy.