

## Debt and the Fiscal Crisis: the Rentenmark lesson

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*The world was driven into a depression of 1930s proportions when the financial crisis struck in 2008. Assessments by the IMF and the OECD warn that the global economy is still weak and incapable of recovering to pre-crisis levels of income and production. Can lessons be learnt from the tragedies of the 1930s? The fiscal boost from World War 2 helped to push America's GDP per person back to pre-1929 levels by the 1960s. But why endure the intervention of another world war, when there is a peaceful way to restore productivity, growth and full employment?*

**E**UROPEAN governments are reducing expenditure on public services in response to the debts they accumulated during the boom years. Austerity policies are depleting the productive vitality out of economies like Spain and Portugal. Greece has learnt what it means to live on a financial life-support machine administered by the IMF and the European Central Bank. There is an ever-present serious threat of civil strife as increasing numbers of people shift their allegiance to fascist-like political parties.

In Britain, the Cameron Government embarked on the replacement of the Welfare State with something called "the Big Society". Spending on the welfare of low-income families is being curtailed, ostensibly to balance the budget and reduce the sovereign debt. Civil society, meanwhile, is tormented by the ethical and economic dilemmas faced by cash-strapped governments:

- ❖ raise taxes (which damage the economy), or
- ❖ cut welfare spending (which damages the lives of vulnerable people).

This is a false dilemma. There is an alternative route to prosperity. Debts can be funded, and then paid down, by fostering growth on terms that would enhance productivity while protecting the natural environment. Furthermore, that formula would automatically build in the guarantee that Britain would never again fall hostage to a land-led property boom/bust.

The starting point is the realisation that taxes on incomes from working, from savings and from production combine to burden the economy with enormous "deadweight losses". And yet, Britain could just about double its national income if Parliament restored the time-honoured way of raising its revenue directly from the rents of land and natural resources. I illuminate this strategy with the financial numbers in [Would Exiting the EU be Disastrous for Britain?](#)

But the transition to the benign way of raising revenue to pay for public services would take time. Meanwhile, creditors need reassurance. One way to buy time is to employ a device developed in Germany in 1923.

### **The Weimar Connection**

Following the First World War, Germany experienced a massive depression. With no gold backing for the Deutsche Mark, the population lost confidence in their currency. They re-named it Papier Mark. Consumers were forced to buy bread by waiting in long queues with their bank notes bundled in wheelbarrows. The long queues often meant that the price had gone up by the time they got to the front, so no bread! But one bank found something that the German people did have confidence in – *land!*

The Rentenmark (literally, "Security Mark": RM) was a currency issued on 15 November 1923 by the Rentenbank, to stop the hyperinflation of 1922 and 1923. It was backed by the bank's assets of mortgaged land and property together with industrial goods.<sup>1</sup>

The Rentenmark was accepted by the population and it effectively stopped the inflation. It continued to circulate until 1948. Parallel with the Rentenmark, the Government introduced a new currency in 1924, the Reichsmark, which lasted until 20<sup>th</sup> June, 1948.

The Rentenmark gives us the clue to our dire financial circumstances today – *confidence!* We *can* cut "bad" taxes now, to stimulate growth, and we *can* use the German experience to cover the deficit.

By beginning to cut the rates of Income Tax (say, by 5p in the £), we have to make up the revenue shortfall. To cover the deficit, Government could issue a Land Rentals Bond. The security of this bond is British land, and the income generated by the proposed Land Rentals Charge.

I must stress the key role played by confidence. It would be easy to sell those bonds in the market, assuming that investors believed the government when it declared its commitment to a root-and-branch reform of the fiscal system. Why? Because land is the asset that offers the best security. This strategy *does* constitute more public borrowing, but the advantages are enormous. The cut in income tax of 5p in the £ would simultaneously

- ✓ jump-start the economy onto a path of virtuous growth, while
- ✓ elevating the spirits of the people.

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<sup>1</sup> Fred Harrison (2015), *As Evil Does*, London: Geophilos, pp.124-126.

Now, working harder or more efficiently, people would raise their productivity, which would yield higher rewards. And at the same time, *land values would rise to provide more revenue and enable government to institute further cuts in the taxes on earned income.*

Commentators are generally agreed that the UK needs “balanced growth”. But to get at its value, the solution is not to nationalise the land – that was the failed strategy of successive Labour governments in the post-World War II era.<sup>2</sup> The failure of fiscal policy in Australia’s new capital is a salutary lesson (see *Box*).

### **Canberra, Australia: the Privatisation of Public Value**

A ‘greenfield site’ was acquired by the government of Australia for a new federal capital. Land parcels were leased for 99 years for residential development and for 50 years for commercial development.

The leasehold rents were set by auction, but rent reviews were to take place every 20 years. The defect in that arrangement became obvious: for 20 years, the increase in the location values were reaped by leaseholders. Those rising rents ought to have been recycled back into the public purse, to pay for the infrastructure and public services that were coming on stream.

At the first rent review, the increases were so great that there was a political storm. It was not long before the combined rents and property taxes were about half of what would be collected if the property tax had been sensibly related to the market value of each location (excluding the value of buildings).

An exercise that was intended to ensure that all of the value of land accrued to the public purse, to be invested for the common good, failed. This would not have happened if rental values were revised on a 3 or 5 yearly basis, with corresponding reductions in taxes. Although leaseholds still exist in Canberra, the fact that rentals and property taxes are low means that the leases have acquired a market value. Capital premiums are required to purchase the leases. The rent of land in Canberra – *publicly owned land* – has been privatised because of the failure to collect all the rent from the outset.

### **The Courage of Conviction**

Governments appear to believe that they can help their economies to recover from the post-2008 depression by cutting spending on services like schools and hospitals. That is a false prospectus: it reminds us of the medieval doctors who believe that they could cure their patients by bleeding them; the end result, usually, was death.

Today, in Britain, there is a growing awareness of the wisdom of shifting the fiscal structure in the direction of rents. Publications like the *Financial Times* and a number of think-tanks from both the political left and right have praised the

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<sup>2</sup> V.H. Blundell (1994), “Flawed Land Acts 1947-1976”, in Nicolaus Tideman (ed.), *Land and Taxation*, London: Shephard Walwyn.

policy. But they usually couple their comments with a resigned fatalism: that the political will is absent. In an article in *The Guardian*, Matthew Taylor, who heads the Royal Society of Arts, reflected on the problem of the housing crisis in these terms:

“There is, for example, a strong case to be made for a land value tax, something that would both be a better way of bringing in revenue than other forms of tax *and* provide an incentive for landowners to develop their land. Many people, on the left and right and in august bodies such as the Institute for Fiscal Studies and the Organisation for Economic Co-operation and Development, recognise this case, but the political consensus is that it is just too difficult to implement and there are too many losers. If we continue with this defeatist mind-set we have no chance.”<sup>3</sup>

In all such cases, the pessimism of the expert analysts stems from the lack of confidence. In Taylor’s case, he lacked the confidence to propose this policy when he was advisor to Prime Minister Tony Blair in the Downing Street Cabinet.

Confidence is the missing link in the political puzzle of how to build political support for change. Interim solutions are part of the challenge of building confidence, and the Rentenmark model provides the clue to one of the tools. The democratic consensus for change would emerge if statesmen can be found to explain that

- ✓ the Land Rental Bond would help government to bring budget deficits under control;
- ✓ the services people need – like public libraries, the employment of teachers, more policemen on the beat – would not be savaged; and
- ✓ growth would be stimulated, by rewarding people who work for their living.

To cap it all, the policy would also set in train the rebalancing of the economy in ways that would terminate the rewards garnered by the land speculators. It is their activities that over-extend the economy, causing indebtedness and unemployment.

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<sup>3</sup> Matthew Taylor (2015), “Housing is the nation’s most urgent and complex challenge. Yet we are paralysed, *The Guardian*, August 16. [http://www.theguardian.com/commentisfree/2015/aug/16/matthew-taylor-we-must-face-difficult-truths-to-solve-housing-crisis?CMP=share\\_btn\\_link](http://www.theguardian.com/commentisfree/2015/aug/16/matthew-taylor-we-must-face-difficult-truths-to-solve-housing-crisis?CMP=share_btn_link)