SES talk, December 8th 2007

History/ forecasting how we repeat it.

This presentation will show how, with an understanding of the law of rent, it is possible to gain an understanding of how the economy truly functions, and then apply this knowledge to make some quite astounding observations about how future economic activity will unfold, in particular for both the stock market and for property.

The talk will focus on how history has repeated over past centuries, and how it will repeat into the future, and discuss the economic conditions which make this inevitable under present man made laws we invent to govern ourselves. A far cry from the natural laws given to us.

Persons interested in understanding how property cycles work, and why, will find the presentation particularly useful.

Phil Anderson has run Economic Indicator Services successfully teaching subscribers how to profit from business, real estate and commodity cycles for about 15 years.

Slide: plan for today

Intro Fred, but first, brief definition of Ricardo's law: The rent is not a cost of production.
Explain with The Big Issue sellers of San Francisco

Fred Harrison has authored many successful books about real estate cycles, and has proved himself the only forecaster having been able to correctly forecast this cycle since 1983.

Slide: Some UK figures
(Fred's commentary)

Slide: Draw attention to series of dates, understand this series of numbers and you will see how the world works:

2001/2 1991 1982 1974

1961 (1955) 1949 1937 1932

1921 (1913) 1907 1897 1893

1884 1873 1866 1857

1847 1836/7 1825 1819

Roughly one per decade,
Those in red about 20 years apart, the real estate led downturns

Real estate
slide: Real estate, the US movement inwards
Just a reminder, as the Americans went further and further inland, they discovered the land got better and better

Now to cut a long history short, eventually more and more of the US was settled, the twelve or so eastern seaboard states got together after Independence and elected a federal government, with the states ceding their control of land to that federal body, which began a process of selling title to the land, to all who would come and live there. That was the practice that interested me, because after 1800 this process became measurable, as I am about to show you

slide: real estate; 1810's land speculation, then downturn
Explain how the land was sold off by the government, $1.25 per acre regardless of situation or quality, on extended credit terms, stake out the land, seek title at the nearest title office, take in your freshly printed bank notes for the deposit, and start farming

Speculation in urban and rural lands and real estate, using bank credit, was a common phenomenon which sharply raised property values…
Leading to a peak in sales activity in 1819.

slide: **real estate; 1830's land speculation, then downturn**

At the heart of national prosperity was a land boom developing in the West, financed by the banks. The farmer, the manufacturer, and the merchant, instead of paying their debts, bought land and speculated in land. Villages and cities sprang up overnight in every direction, sites increased at the rate of 200 to 300 per cent per year, fortunes were made and lost in a few moments. Many of the states had slapdash banking laws, and many of these new banks were badly - if not fraudulently - managed, under-capitalized, under-regulated and overly bullish about the future.

The land auctions were attended by veritable mobs. They were scenes of great excitement. Premiums were paid for choice locations near the auctioneers,

From a Wisconsin newspaper came the estimate that in the newer sections of the country, real estate investment for the ten years between 1825 and 1835, paid a 20 to 30 per cent return per annum…

In Milwaukee, it was being reported that land buyers went to bed at night hugging themselves with delight over the prospect that the succeeding morning would double their wealth.

Land sales peaked in 1836, 9 months later, in May of 1837, a heap of bank runs, then panic.
The web site campusprogram.com gives May 10 as the panic day of 1837, though no source is quoted. Using excerpts from the New York papers of the day, they reported John Fleming, President of Merchants Bank "fell dead from excessive anxiety with regards to the affairs of the bank May 4th, from which a run set in on all banks. The failures grew worse over the next two days, and United States Bank stock fell below par for the first time. On May 9th there was a "furious run on all banks", May 10th, "chaos".

Refer to McGranes list of 1837 bank thefts, in handout

slide: **real estate; 1850's land speculation, then downturn** land sales peaked in 1854,
Note the rapid rise in speculation with very low interest rates

Quote of historians writing of 1857: "Nearly the whole West swarms with speculators… who neither intend to cultivate the soil nor settle there, but who expect to realize fortunes without labour. Land speculation, observed many a newspaper editor, had become a mania. 'Merchants have shut up their shops, lawyers have left the bar, farmers have laid down the shovel and the hoe, manufacturers have abandoned their business to turn land agents and real estate dealers.'

slide: 1830's, 1850's acceleration in bank lending

Note the acceleration in lending towards the end of each cycle, at the turn, a bank run, described thus:
On September 25th 1857 yet another leading financial institution, the Bank of Pennsylvania, in Philadelphia, closed its doors. Papers reported 'the wildest excitement' just about in the whole city, as queues of depositors formed at other banks in the city, demanding their money, now!

A teller at the Ocean bank paid himself out some $50,000 of the banks funds, a teller at the National grabbed $70,000. The bookkeeper of the Union Bank stole $200,000 and promptly fled with the loot after it was discovered he had been forging balances for months.

Has much changed? who to blame for the downturn:
"Our present disorders have been provoked by the extravagance of our women."
New York Weekly Times, Oct 17 1857

"What caused trade thus to topple over, almost without a struggle? What hurled to the dust so many stately fabrics of industry, skill and enterprise? The answer is plain enough - we have been living too fast."
Philadelphia Press, Oct 12 1857.

Hunt's Merchants' Magazine listed one of the causes as the telegraph, disseminating the bad news, as it was, 'too quickly'.

And finally:
The *Herald* lays it to wine, women, cards and .... fast horses."
Washington Evening Star, Aug 28 1857

slide: real estate speculation into the 1873 peak

Land sales peaked in 1869. Rail index versus interest rates

A revival of the property market was being anticipated in the autumn, as per usual, however the September 18th announcement in New York of the failure of Jay Cooke and Company startled investors. Indeed, the initial reaction to the collapse of America's most prestigious banking concern was disbelief. In Pittsburgh a paperboy was arrested for shouting out the news, because it was news which police had not yet heard and believed the paperboy was making it up to garner more sales. "Incredulity soon gave way to panic, as the stock market collapsed and daily interest rates rose to 5 percent."

The next day, crowds thronged the financial district to witness the unravelling of the speculative drama that had entranced the nation for the past decade and a half… Vanderbilt's son-in-law, Horace Clark, was found dead after the failure of the Union Trust Bank, from which he had borrowed heavily to finance his margin speculations. Daniel Drew, the Old Man of the Street, took his final curtain call as his brokerage, Kenyon, Cox and Co, was swept away in the panic. Declared bankrupt, Drew retreated to his bed…he died a year later. When the panic continued into Saturday, the President of the New York Stock Exchange announced that for the first time in its history the exchange would close - until further notice."

Historian Alfred Chandler, (page 506), about September 18th wrote: "On the day of the Jay Cooke failure, these shares dropped in price so suddenly and sharply that banks and prominent brokerage houses collapsed like pins in a game of ten-pins. On the street, within the shadow of the stock exchange, some men wept and some attempted suicide at the realization of their financial ruin. I saw all this, as I was in the midst of it and it made a lasting impression."

Slide: real estate speculation into the 1893 downturn
Land sales peaked in 1888, well before the months of panic as usual, with sales falling markedly after 1890.

Slide: sooners; the 1889 land run

The bank run:
The banking panic began this time in the interior of the country - in Chicago. On May 8th, without any prior warning whatsoever (to the public and its depositors at least) the Chemical National Bank of Chicago did not open for business. Its doors never did in fact reopen and depositors were faced with the prospect of losing a collective $1.6 million. “Excessive loans had been made to the bank’s directors and to some of the shareholders.”

Three days later on May 11th In Indianapolis, the Capital National Bank, closely associated with the Chemical National, failed. Depositors here lost $1.1 million. The next day, May 12th, the Columbia National Bank of Chicago failed (the result of rumours caused by the Chemical National failure), with $1.5 million of depositors cash lost. This was a bit more serious, since the Columbia’s deposits were mostly deposits from other banks.

June 3 The largest commercial paper house in Chicago, Herman Schaffner & Co. closed its doors on this day, taking with it depositors money to the tune of $850,000. A private bank, Schaffner & Co. had been speculating in railway bonds, which, as a result of the stock market collapse, were now worth far less than previously. The bank’s president was last seen renting a boat, rowing far out into the waters of Lake Michigan and is then presumed to have jumped overboard, never to return. The panic was on.

Discuss here, why cycle must repeat:
Govt granted licenses, story of Canberra

Highlight the cause of the cycle: speculation in the enclosed rent (a government granted license) funded on credit, created by banks out of thin air. Collecting this rent for government revenue, say through a leasehold pyt, or land tax, would eliminate completely the real estate cycle. Totally. Why, because there would be no value in which to speculate...

Slide: US real estate into 1932
Again, a real estate speculation peak just over 18 years after the last one.

Florida:

A chap named Carl Fisher built Miami Beach, putting his substantial fortune from the manufacture of automobile headlamps into the development. Locals literally gasped as Fisher proceeded to fill hundreds of acres of swamp with sand dredged from the bay, top it with thousands of tons of Everglade topsoil and then build hotels, golf courses, yacht clubs and polo grounds.

Fisher started his working life at age 12 selling newspapers on the railway. Sales soared after he started flashing a photo of a naked woman from underneath his jumper. This time, to draw attention to his 1920's Miami Beach development, Fisher brought in a circus elephant, imported a polo team from England, dressed young women in risqué bathing suits, and started taking pictures. Said Fisher: “We’ll get the prettiest girls and put them in the goddamndest tightest and shortest bathing suits, and no stockings or swim shoes either. We'll have their pictures taken and send them all over the goddamn country!" Soon, every paper in the country was carrying pictures of suitably clad (or rather un-clad) women on the beach in Florida.

Slide: modesty prevents showing the gals, but I can show you the elephant...

Slide: here are the gal's

Fisher's promotions sparked a national hysteria for Florida real estate. Six million people poured into Florida in three years. When they arrived they found a real estate gold rush in progress. Overflow crowds slept in parks, and pored over Sunday papers with 500 pages of real estate ads. Caravans of buses from the upper mid-west brought thousands of prospects on tours of new developments. Seven thousand five hundred real estate licenses were issued in Miami in 1925. Subdivisions sold out the day they went on the market. One office sold thirty-four million dollars worth of property in a single morning. Prices soared, and speculators rushed in.

So many citizens were now pushing Florida real estate that the municipal authorities were having trouble finding staff to carry on essential services; most of the policeman, firemen and other employees had quit to do the same thing, buy and sell land. The Miami authorities resorted to grabbing the sharecroppers from the hills of Georgia and putting them in uniform, despite the fact many, if not all, had never before worn shoes let alone some sort of authoritarian outfit. Towns north of Florida reported a severe slump in the movie business because so many theatre-goers were leaving town to travel south. Warehouse managers even as far away as New York were reporting no space left because of all the furniture they were having to store on account of those who had sold up and travelled south to trade real estate. The Massachusetts Savings Bank Association complained that more than one hundred thousand depositors had taken their money out of the state's banks and headed to Florida to buy land.

1930, the turn after a bank run:

In early November of 1930, the banking empire of Rogers Caldwell, centered in and around Nashville, Tennessee, collapsed. Rogers Caldwell controlled the largest network of banks in the Southern regions of the US and was, as it happens, heavily invested in real estate. Then, on December 11, 1930, The New York based Bank of the United States (in some ways a misleading name since it was not connected with the government in any way) went bust. This, it was said, was due not only to the bank's stock market losses of its affiliates, but also to an over exposure to declining property prices.

Describing the scene as the Bank of the United States closed its doors, James D Horan (*The Desperate Hours*) wrote: "It was one of the most disastrous failures in the banking history of the country…men wept as they tried to rush past the police guards and pounded on the closed doors; women screamed as they held up their bank books. Crowds refused to disperse and stayed outside the doors for days, hoping that their savings were not lost."

Slide: 18 years has a good history, Chicago land value, According to Hoyt, 1966.

Slide: 18 years has a good history, US building construction

The heavy black line is the Warren and Pearson 120-City-Index of building activity
The dotted line is the value of construction contracts awarded in 37 states, F.W. Dodge Corporation, 1925-45.
A stylized 18 years cycle is added in the background.

Slide: 18 years has a good history, US real estate activity

Black line is measuring US real estate activity (indicator died with the death of its inventor, Roy Wenzlick.
A stylized 18 years cycle is added in the background to show what would happen if the cycle as seen then continued...

In years past, the memorable downturns had occurred in an economy without electric light, without telephones or fax machines (or any other fast means of communication for that matter) and in conditions that would seem less than civilized to on-lookers from today's era. What's more, despite the US economy operating either with a central bank, or without one, at a time of inflation or at a time of deflation, under conditions of a government budget surplus or deficit, severe downturns (depressions in fact) have been occurring every eighteen to twenty years.

Current: highlight 2005 Fortune magazine

Slide: The real estate rhythm

Slide: Murdoch quote

Thank-you for your time today