1994

Mary M. Cleveland
1440 Walnut Street, Apt 1
Berkeley, CA 94709-1447

(510) 841-7651
FAX (510) 841-7514

1/10/94

M. Mason Gaffney
PO Box 7998
Riverside, CA 92513-7998

Dear Mason,

I've enclosed a revised version of the piece I sent you some time ago. I distributed it at a seminar I gave yesterday at Gianinni. Enthusiasm from some of the kids, cynicism from the two faculty members who bothered to show. (Oh hum.)

I hope the earthquake didn't knock out the windows Tom cleaned!

My best to Tish, Laura, Patty and Matthew.

Love,

Polly

Mary M. Cleveland
1440 Walnut Street, Apt 1
Berkeley, CA 94709-1447

(510) 841-7651
FAX (510) 841-7514

3/7/94

M. Mason Gaffney
PO Box 7998
Riverside, CA 92513-7998

Dear Mason,

Here's de Janvry's piece. Note especially the paragraph at the bottom of p 10. Except for the jargon, it could almost be right out of the Benefits of Military Spending!

It was good to talk to you yesterday. I'm very eager to see your piece on the difference between land and capital. I've tended to think of the difference as lying on a spectrum, with appreciating land at one end (benefits as far as possible in the future) and unskilled labor at the other (benefits immediate). Capital, as you once said, is stored up land and labor. In dealing with the distribution of wealth, it's not possible to separate the distribution of land from the distribution of capital. The wealthier a person, the higher his ratio of land to capital and capital to labor. Hence the lower his internal discount rate, and the lower the marginal product of his land, which equals the rent he imputes to his land. So I'm not sure what you meant by saying rent goes down when interest goes up, if that's what you said. Given that there is a wide band of rents and interests depending on wealth and other characteristics of individuals, whose rent and whose interest?

My best to Tish, Laura, Patty and Matthew.

Love,

Polly

Mary M. Cleveland
1440 Walnut Street, Apt 1
Berkeley, CA 94709-1447

(510) 841-7651
FAX (510) 841-7514

6/16/94

M. Mason Gaffney
PO Box 7998
Riverside, CA 92513-7998

Dear Mason,

Veh ist mir! I pick up my new June AER and I see an article entitled "Is Inequality Harmful for Growth?" by Persson and Tabellini. I note that the abstract says "Yes" and a footnote thanks Irma Adelman, and I think to myself, aha, finally some people are on the right track! Then I read further. I can hardly believe it. The authors have constructed a model to show that inequality is harmful for growth in a democracy because taxes divert money from productive investment into redistributing income!!!! But at least they have more data linking inequality to lack of growth-- I will use that in due course.

Anyway, I have enclosed a very rough draft of the first three sections of my paper on land taxes, market failure, and Henry George. You need read only the first three pages. I hope you can give me both advice and help.

I need advice as to the best way to present my arguments. I have used Hoff's little piece as a springboard to tackle the issue head on: Henry George was right about a land tax (though partly for the wrong reasons) and here's a conventional model that supports him. Also Henry George was a great economist and reformer who is unjustly neglected. But I don't want to be dismissed as a Georgist flake. And I don't want to (seriously) offend Hoff, who often collaborates with Stiglitz, and is more often on the right side than not. Do you think this is a good approach, or should I be more circumspect? Is there a different approach you would recommend? Have I got my information straight about George? What should I write about George in a couple of paragraphs to hook a well-intentioned (or politically correct) modern economist?

I need help with references, particularly your references, since my copies of your pieces are back in New York. That is, where should I cite you or others and in support of which points? Could you send me an updated vita? Incidentally, your latest on "Land as a Distinctive Factor of Production" gave me a key piece of my models not in my dissertation: land must be sold in minimum size parcels, which leads to land market failure.

This paper has been a nightmare to write so far-- the computer program that does the math (Math Type) is very slow and tedious to work with, and I'm not yet satisfied with the formatting. My numerical general equilibrium model (Part IV of the paper) is sort of running, but not written up yet. I did it on GAMS, the fancy optimization program that Irma Adelman and some of the other Giannini folks like to use. It was developed by the World Bank; it's easy to use and has saved me a lot of programming.

We have to be out of here by the end of July, so I am racing against time to get something that is coherent enough to show to people at Giannini as well as Bardahn. (Did you get to his lecture?)

My best to Tish, Laura, Patty and Matthew.

Love,

Polly

PS. Would Nick Tideman be helpful as someone who can follow the gobblygook?

Mason Gaffney
P.O. Box 7998
Riverside, CA 92513

909/687-1677
OFF 909/787-5037, x1574
FAX 909/787-5685

15 May 94

Dear Polly:

I have no record of having ever sent you the enclosed. I probably have, but perhaps Prof. Wright would be interested in one or more.

1. Taxable capacity of water resources
2. Falling property tax rates and rising concentration
3. Land reform through tax reform
4. Latest version, "Land as a distinctive factor of production."

Fred H. has me on a tight string: must rush to finish.

Also, for amusement, words to "Mad dogs and Englishmen," transcribed from a Noel Coward tape I found at Heathrow last month. I've wanted to learn them since hearing that when I was 12 or so. Recalling your great memory for G&S patter songs, this is just your cup of espresso, too.

Love,

M.

Mad Dogs and Englishmen

INTRODUCTION

FANFARE

In tropical climes there are certain times of day
When the citizens retire
To take their clothes off and perspire
It's one of the rules that the greatest fools obey
For the sun is far too sultry
And you must avoid its ultry-violet ray

The natives grieve when the white men leave their huts
Because they're obviously, definitely nuts.

I

Mad dogs and Englishmen go out in the midday sun
The Japanese don't care to, the Chinese wouldn't dare to
Hindus and Argentines
Sleep firmly from twelve to one
But Englishmen detest a siesta

In the Philippines they have lovely screens
To protect you from the glare
In the Malay states there are hats like plates
Which Britishers won't wear
At 12 noon the natives swoon
And no further work is done
But mad dogs and Englishmen ...

II

FANFARE

It's such a surprise for the eastern eyes to see
That though the English are effete,
     they are quite impervious to heat
When the white man rides the native hides with glee
For the simple creatures hope 'e
Will impale his solar topee on a tree

It seems such a shame when the British claim the earth
That they give rise to such hilarity and mirth
Ha ha ha ha ha ha ha ha ha ha
Ho ho ho ho ho ho ho ho ho ho
Hee hee hee heh heh heh heh heh heh heh
Mm mm mm mm mm mm mm mm mm ...

III

FANFARE

Mad dogs and Englishmen go out in the midday sun
The toughest Burmese bandit
Can never understand it
In Rangoon, the heat of noon
Is just what the natives shun
They put their scotch and rye down, and lie down

In a jungle town, where the sun beats down
To the rage of man and beast
The English garb of the English Sah'b
Merely gets a bit more creased

In Bangkok at 12 o'clock
They foam at the mouth and run
But mad dogs and Englishmen go out in the midday sun

IV

Mad dogs and Englishmen ....
The smallest Malay rabbit
Deplores this foolish habit
In Hong Kong they strike a gong
And fire off a noonday gun
To reprimand each inmate who's in late

In the mangrove swamps where the python romps
There is peace from 12 to 2
Even caribous lie around and snooze
For there's nothing else to do

In Bengal, to move at all
Is seldom if ever done
But mad dogs and Englishmen ...

Mason Gaffney
P.O. Box 7998[1]
Riverside, CA 92513

909/687-1677
OFF 909/787-5037, x1574
FAX 909/787-5685

21 Aug 94

Mary Cleveland
14 W. 68th St.
New York, NY 10023

Dear Polly:

Quick, get your resumé over to Oscar Johannsen, R.S.F., 41 E. 72nd St, New York, NY 10021. Add a short statement as to why you would make a good member of the RSF Board of Directors.

Things are moving. Two Directors have resigned: Tommy Larkin, do-nothing curmudgeon of many years; and David Hapgood, who never did anything for us. There is a lot going for you. Nic Tideman has lined up behind you. We need a female; we need a New Yorker; we need a proven, tempered, battle-scarred Georgist; we need a writer; we need a Ph.D. There is a move going to dump Oscar (nicely, of course). If we can get that moribund gang turned around, we can make constructive use of a significant pile of dough.

R.S.F. is heavily into cash. This has cut income the last two years. Greenspan and the market are turning that around, too.

Yesterday morning at 5:30 I became a grandfather! Meredith Ann Shores saw the light at Marin Cty. General. She will be at home with her parents in Corte Madera.

You will enjoy enclosure written by my Aunt Sally, concerning her uncle, one Selah Merrill Clarke, long-time city editor of the old New York *Sun*.

Give some thought to whether de Janvry, Sadoulet, Wright, Eswaran, and others, are reliable enough to have join our New Committee. We don't want any band-wagon hoppers, just hard-core reliables.

I never read Thurow's Zero-sum Society. What is his thesis?

---

[1]Memorize this address! The P.O. does not routinely deliver mail to our street address.

John Henry sends confirmations that Pareto was even more fascistic than I thought. He was a member of Mussolini's Parliament, among other things.

How odd that our Georgist leadership never made hay of the fact that the goat of the 1930s, Chamberlain, was the one who killed lvt in Britain; the hero, Churchill, was for it; and the villainous fascist Pareto was against it.

Love,

Mase

Dr. Mary M. Cleveland
14 West 68th Street, Apt 4
New York, NY 10023

(212) 873-2982
FAX (212) 873-6125

Saturday, September 24, 1994

M. Mason Gaffney
PO Box 7998
Riverside, CA 92513-7998

Dear Mason,

Re my models. Yes, I have viable parts of micro-macro models, one version of which I used in the paper on "Was Henry George Right?" I am developing another version, with variable land quality, for Great Barrington. (Please send me the materials, etc.) An output (or other non-land) tax should push the margin of cultivation outwards onto lower quality land by lowering the equilibrium wage and discouraging intensive use of central land, while a land tax will pull the margin of cultivation inward by raising the wage and stimulating more intensive use of central land. The implication for banks is that a shift to land taxes will raise central land values, even after tax, but lower peripheral land values. That should make the banks more willing to lend on centrally-located projects, and less willing on marginal projects. I expect the model to show that total land values will *increase* with a land tax ! because less surplus is dissipated.

I have worked out equations, though not programmed them yet, to create dynamic models. Irma's GAMS program will come in very handy, as it allows me to compute a general equilibrium for one period, and use the results as the starting points for the next period. So I expect I can construct models with capital accumulation. The big problem I haven't yet figured out is how to simulate invention of new technology. But I have some leads; possibly the people programming "artificial life" have some useful ideas I could borrow.

Of course you're absolutely right that mathematical models serve to divert practitioners from real issues as well as bamboozle and exclude outsiders. On the other hand, for me at least, mathematical models help me verify that my understanding of the world is logically consistent, and sometimes even give me new insights. Models also give me a clearer understanding of the hidden assumptions that lead so many good economists astray. And on the third hand, mathematical modelling is *fun*. It is both science and art. Science, because you are (or should be!) solving a real-world puzzle. Art, because you create the puzzle in the first place, elegantly or crudely, depending on your skill and imagination.

Who are Charles Haughey and Dan Sullivan? Should I contact them?

I have now received letters of congratulations from Steven Cord and of course Lowell Harriss. But not Boo from Oscar Johannsen or Susan Klinglehofer. What gives? I haven't called George Collins et al because I'm not sure I'm supposed to know yet that I've been elected. What happens next?

Should I call Bob Gilmore in Great Barrington to find out about schedule, motels, etc? Are you sending out a program? Who is coming? How long a paper am I supposed to produce, and how long do I get to present it?

My best to Tish, Laura, Patty and Matthew.

Love,

Polly

Dr. Mary M. Cleveland
14 West 68th Street, Apt 4
New York, NY 10023

(212) 873-2982
FAX (212) 873-6125

Saturday, September 24, 1994

Prof. Kris Feder
Economics Department, Bard College
Annandale-on-Hudson
New York, 12504

Dear Kris,

It was good to meet you last week.

I am enclosing four items for you; comments much appreciated:

1. Mason's new piece, on *Neo-classical Economics as a Stratagem against Henry George*, to be published in England by Fred Harrison.

2. An old semi-popular piece of mine (slightly revised) on "Equality, Productivity and Growth."

3. My dissertation on *Consequences and Causes of Unequal Distribution of Wealth.*

4. A very rough draft of a new paper on "Land Taxes and Market Failure--Was Henry George Right?"

For Mason's conference next month in Great Barrington, I'm working on a version of the models in 4. with varying land quality: An output tax should push the margin of cultivation outwards onto lower quality land by lowering the equilibrium wage and discouraging intensive use of central land, while a land tax will pull the margin of cultivation inward by raising the wage and stimulating more intensive use of central land. The implication for banks is that a shift to land taxes would raise central land values, even after tax, but lower peripheral land values. That should make the banks more willing to lend on centrally-located projects, and less willing on marginal projects.

Please send me your stuff. My regards to your menagerie. See you next month.

Polly Cleveland

SEP 2 9 1994

Mason Gaffney
P.O. Box 7998
Riverside, CA 92513

909/687-1677
OFF 909/787-5037, x1574
FAX 909/787-5685

24 Sept 94

14 W. 68th St.
10023

Dear Polly:

Thanks for the wonderful editorial from *The Economist* about "Jamie" the dissolute landowner. It belongs somewhere in the reading of those conservatives who believe that unequal distribution raises savings rates, and those underconsumptionist liberals who believe it lowers the propensity to consume.

Your impressive bio and biblio is probably what swung the vote your way. (I hope you really <u>can</u> handle Russian, Hebrew, and Arabic, along with the more prosaic French, German and Spanish. How ever do you keep them straight?) I see three items on the biblio I'd appreciate copies of:

"The Research Subsidy," 1971, from Senate Hearings on Migratory workers.[1]

"Parks for fun and profit."

"Making dollars and sense[2] out of fiscal impact analysis."

Back to work for Fred Harrison: what a slave-driver!

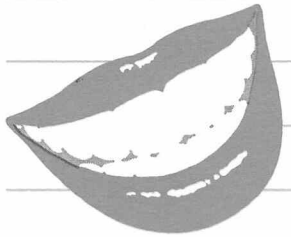
Love,

M.

---

[1]Did you ever meet Jeanne Dangerfield, whose name is used as author of <u>Sowing the Till</u>. I did, and I have serious doubts whether she really wrote it. Wonder whom she fronted for?

[2]Shame on you for using such a cliché!



Smile...

Thanks for ~~last~~ editorial from The Economist. On the mark!

...It'll make people wonder what you've been up to!

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Dr. Mary M. Cleveland
14 West 68th Street, Apt 4
New York, NY 10023

(212) 873-2982
FAX (212) 873-6125

Sunday, Oct 2, 1994

M. Mason Gaffney
PO Box 7998
Riverside, CA 92513-7998

Dear Mason,

I've enclosed the *Planning* piece, -- the editors renamed it. It still reads well after all these years. I can't find a copy of the Pt Reyes piece -- it was a story of shady land deals during the public acquisition of Pt Reyes.

My modelling so far has yielded a surprise: I predicted that a shift to LVT from other taxes, holding collections constant, should *raise* land values, at least in the center, because the surplus increases. But in the simple pure Ricardian general equilibrium model I just ran, with no transactions costs, guess what? Although the surplus increases, *land values fall*. Why? Because *wages rise sharply!* Of course these results may change somewhat with different production functions. Results may also change when I put in transactions costs, by requiring that landowners who hire labor have to supervise it--which will result in underused land in the center. I've enclosed some preliminary graphs that will amuse you.

My best to Tish, Laura, Patty and Matthew.

Love,

Polly

Dr. Mary M. Cleveland
14 West 68th Street, Apt 4
New York, NY 10023

(212) 873-2982
FAX (212) 873-6125

Tuesday, October 25, 1994

Professor and Mrs. Hyman Minsky
The Jerome Levy Economics Institute
PO Box 5000
Annandale-on-Hudson
New York 12504-5000

Dear Hyman and Esther,

I enjoyed seeing Hyman again and meeting Esther. I have sent your regards to Irma Adelman.

I have enclosed a Xerox and the complete reference to Adam Smith's quotation about "other people's money."

Sincerely,

Polly Cleveland

Dr. Mary M. Cleveland
14 West 68th Street, Apt 4
New York, NY 10023

(212) 873-2982
FAX (212) 873-6125

Wednesday, October 26, 1994

Professor Alexander Field
Department of Economics
Santa Clara University
Santa Clara, CA 95053

Dear Alex,

I enjoyed meeting and talking with you at the AEIR.

I found your report of an interest spike just before the crash particularly intriguing. It fits in with Mason's capital market "glitch" due to a rise in interest rates. I have enclosed a two-page rumination on the subject, entitled "RC and the Coconut Crash."

I have also enclosed a copy of Mason's "Neo-Classical Economics as a Stratagem Against Henry George," to be published shortly in England. It catches the neo-classical greats with their theories down and their prejudices exposed, --not to mention the strings connecting them to their financial backers!

Regards,

Polly Cleveland

cc: Mason Gaffney

RC and the Coconut Crash

Alex reports that a rise in interest rates preceded the Crash of '29 and the Great Depression. Mason notes that a rise in interest rates destroys durable capital, possibly causing a 'macro-economic "glitch."'

A rise in interest rates tells owners of *depreciating* capital assets like buildings or machines to junk those assets whose service flow no longer covers the interest on the value of land they occupy, --and replace them with new, more productive assets. That means the owners must borrow, at the new higher interest rate, to pay for labor and materials to create the new assets. Meanwhile, as for owners of *appreciating* capital assets, like trees in a forest, or wine in a cellar, or goods approaching completion on an assembly line,--the rise in interest rates tells these owners to hurry things up: cut the trees sooner, sell the wine less mellowed, speed up the assembly line by putting on the second coat of paint before the first dries, and so on. Ideally, the extra materials, and possibly labor released by the owners of appreciating assets will fill the needs of the owners of depreciating assets. But if a land boom has deceived owners of appreciating assets into investing heavily in assets with a remote payoff that cannot easily be accelerated--such as new subdivisions--then a rise in interest rates may become self-feeding, until a short-term interest spike stops long-term economic activity in its tracks.

Meet RC. RC lives on a large island, where the only food is coconuts. But the trees are scattered over the island; RC must wander all over checking to see which trees have dropped coconuts, and lug the coconuts he collects back to his camp. Moreover, the coconuts don't keep indefinitely. So RC makes two investments. First, he dries coconut meat in the sun, and stores the resulting copra in sheds he constructs from palm thatch. Then he starts a coconut plantation near his camp; a plantation will save him time spent wandering around hunting coconuts, and allow him to harvest more regularly using a ladder. However, the young trees must be carefully tended, as a giant beetle likes to bore into their trunks; the beetles must be found and impaled on a palm spike before they can do much damage. RC "finances" both these investments from a hoard of coconuts he has accumulated by wandering and collecting. That is, he lives off this hoard while making copra, building sheds, and planting and tending young trees.

As the rainy season approaches, RC realizes that his older copra sheds won't adequately keep his copra dry. So he dips deeper into his hoard, nibbles on his copra, and perhaps harvests the first green coconuts from his plantation, to free his time to rebuild the sheds. If all goes well, he will complete the job in time, so that he can sit out much of the rainy season in his shack, eating stored coconuts and copra, occasionally going out to check his young trees for beetles. But suppose, on dipping deeper into his hoard, RC discovers to his horror that rats have chewed up the coconuts inside the pile. In a panic, he abandons his re-thatching and his tending of the young trees, and heads out to collect coconuts fallen from the mature trees scattered around the island. The rains come, destroying part of his copra; and the beetles flourish, tunneling through the young trees

until they fall over. By destroying part of RC's liquid capital, the rats have indirectly destroyed much of his fixed capital as well.

Through no fault of his own, RC has fallen victim to a "wealth illusion," which led him to skew his investments too far towards the future. Had he known about the rats, he could have lined his coconut pit with stones, and all would have been well. The same "wealth illusion" leads landowners in a boom to skew investments too much to the future. When an interest spike pricks the bubble, the whole investment structure comes down. But RC at least can instantly reallocate his efforts from thatching and tree-nursing to collecting coconuts. In a real economy, those who have invested in long-term capital can only slowly recognize what has happened, and even more slowly reallocate their efforts and surviving resources. And of course the slower the reallocation, the greater the damage.

The story of RC strips a capital collapse to its essentials: wealth illusion leading to capital stretch-out, liquidity failure and then collapse. In RC's economy, there is land, labor and capital. However the land accrues no rent, and there is no money! In a real economy, money helps land booms get out of control; it's hard to imagine how land booms could occur without money. But the consequences have nothing to do with land or money. Like rats, land booms create havoc by invisibly eating away liquid capital. Unlike rats, land booms create simultaneous, coordinated havoc for large numbers of people.

Which brings me back to the Great Depression. Perhaps the prolonged slump in housing construction does not reflect any failure of aggregate demand *or* supply. Perhaps it reflects instead a broad impoverishment of society due to the massive destruction of misinvested capital, and a consequent focus on replenishing short-term capital. Poor people put groceries ahead of new houses.

Virginia Tech
VIRGINIA POLYTECHNIC INSTITUTE
AND STATE UNIVERSITY

Department of Economics
College of Arts and Sciences
3016 Pamplin Hall, Blacksburg, Virginia 24061-0316
(703) 231-5688 Fax: (703) 231-5097

Oct. 28, 1994

Fred E. Foldvary
home adr: 709 Circle Drive
Blacksburg, VA 24060

Tel. 703/953-2684
work 703/231-7707
e-mail: foldvary@vtvm1.cc.vt.edu

Dr. Mary M. Cleveland
14 West 68th St., Apt. 4
NYC 10023

Dear Polly,

Your "RC and the Coconut Crash" was interesting, but not convincing to me. Here are my comments.

1) Austrian capital theory has lower and higher orders of capital goods; a reduction of interest rates stimulates investment in higher-order capital goods (more roundabout). An increase in interest rates makes investments in higher-order goods redundant. So it is not merely "durable" capital, as Mase suggests, but high-order roundabout capital that is destroyed in value.

2) You say a rise in interest rates junks assets whose service flow does not cover the interest on the value of land.
This is not obvious. Can you clarify? Is it because rent has changed, or because the service from depreciating assets has been reduced, or something else?

3) As for appreciating assets, a rise in interest rates decreases their present value. This could cause an acceleration of the using-up if the current sale price is greater than the present value of the future product.

4) If appreciating assets such as subdivisions cannot be accelerated, I don't see why a rise in interest rates by itself should do anything other than decrease the present value of the assets and make new investment more costly. The future value of the asset itself should not be affected. It's not clear why a rise in interest rates would be self-feeding. A rise in interest would choke off investments unless it was caused by greater productivity.

5) RC seems to have not so much a "wealth illusion" as a lack of knowledge about his production processes. He committed an entrepreneurial failure. He failed to invest in insurance. Investing in stones is also an investment in the future. He not so much failed to invest as made the wrong type of investment.

6) Landowners in a boom have not so much a "wealth illusion" as a momentum illusion - they think prices will advance in the same direction, when in fact they stop advancing.

7) Builders do invest too much into the future in higher-order capital goods, because a) interest rates are artificially low; and b) land prices are being artificially inflated. The wealth illusion is caused by the low interest rates and by "momentum illusion" - the illusion that past trends will continue.

8) RC does not seem very relevant to me. There is no interest rate reduction or land appreciation. RC's problem is ignorance about his production function. Builders know their production function, but misread the direction of the economic environment.

9) It's not clear why a lack of liquid capital would apply to land booms. There was no shortage of food and other consumables in the 1970s and 1990s recessions. There seemed to be plenty of circulating capital. Interest rates decline in a recession.

10) The poor do put groceries ahead of new houses. But if there is enough food (as there was in the 1930s, when the government was destroying it), why didn't the poor become rich building houses? They could have borrowed food during the time they spent building. The analogy to RC is unclear.

Sorry to be so negative. The RC story does not make that much sense to me. That does not mean your story is incorrect. You may have a great story and good insight here. It may just need more than 2 pages to fully explain step by step to those like me whose linear thinking can't make the needed great leaps of thought. Some gaps need to be filled in.

Sincerely,

Fred

Dr. Mary M. Cleveland
14 West 68th Street, Apt 4
New York, NY 10023

(212) 873-2982
FAX (212) 873-6125

November 22, 1994

Dr. Fred Foldvary
709 Circle Drive
Blacksburg, VA 24060

Dear Fred,

Thanks so much for your comments. I guest my fable of RC was kind of unclear.

I meant it to suggest that it is possible to have a "capital collapse" in the simplest possible economy: one person, no rent, and no money. You are of course absolutely right that RC "committed an entrepreneurial failure." But consider this: RC's entrepreneurial failure would have had far less serious consequences had he been a member of a larger economy. He could have sold his tree farm, or borrowed more coconuts, instead of being forced to abandon his trees to their destruction.

In routine times in our real-life economy, businesses here and there experience "liquidity problems" or "cash flow crises" which force them to borrow more money, or sell some assets, or sometimes even go bankrupt. The physical assets may change hands, and may be marked down in value, but usually they are not abandoned. But in extraordinary times, large numbers of businesses experience liquidity problems *simultaneously*, as happened to the S&L's. They cannot borrow, and they cannot unload assets at prices high enough to cover their obligations. So some assets, like half-built subdivisions or newly-planted vineyards, are simply abandoned. The capital improvements decay, and actually contribute a *negative* value to their sites, as Alex Field documented.

I think I'm trying to get at several questions here:

1. Is it theoretically possible to have a "capital collapse" in a Robinson Crusoe economy? Answer: yes. (Real easy to model, too.)

2. Is it theoretically possible to have a "capital collapse" in a larger economy, if many individuals, simultaneously following the same signals, simultaneously commit the same sort of "entrepreneurial failure."? Answer: I think so; that's why I invented RC. The signals most likely to lead many individuals simultaneously astray are the rising values of a land boom. Even people who do not intend to "speculate" participate by the mere act of buying a home at what turns out to be an inflated price.

3. Is it theoretically possible to have a "capital collapse" without money or rent? Again, I think so. Imagine a remote farming village. Just after planting time, a fire in the communal storehouse destroys much of the food stored from last year. So instead of tending the fields, the villagers scatter to the hills to hunt and gather; consequently the fall harvest is very poor. You could say that, like RC, the villagers "failed to invest in insurance." But that's hindsight. The villagers just followed the "life as usual" signal, which turned out to be wrong in a crisis.

Questions 1, 2, and 3 would not be terribly interesting or relevant without:

4. Does a "capital collapse" of varying severity happen in depressions and recessions? Or are depressions and recessions just monetary phenomena, or what? If "capital collapse" does happen, what sort of evidence should we look for? Now I'm asking for help and ideas.

We should expect, and do find, rising short-term interest rates pre-crash, and abandoned long-term capital post-crash. But what about liquidity? As you point out, "there was no shortage of food and other consumables in the 1970's and 1990's recessions." And in the 30's the government was destroying agricultural "surpluses" in a vain effort to keep prices up (it also created Agricultural Adjustment Act cartels that have been restricting production ever since.) But shortages and surpluses are relative to a price. In the Great Depression, the money supply shrank as credit was withdrawn. Falling prices created apparent surpluses all the way down into the pit. Agricultural suppliers were hit first, since they could not withhold perishable products from market while waiting for prices to improve. Owners of durable goods held out longer, and landowners held out the longest. Workers also held out, refusing to accept the decline in wages.

So if there was a *real* liquidity crisis paralleling the financial liquidity crisis before a depression, what should we be looking for? Rising prices and falling inventories of consumables? Possible actual decline in production of staples? Too high a proportion of luxury consumables, and too great an investment in equipment to make luxury consumables? I'm thinking of the California gold rush. The farmers left their farms for the gold fields. Food production declined, food prices soared, and some of the biggest fortunes were make by the people supplying the miners.

After the crash, prices should fall, but durable prices should fall the most. You said interest rates fell. Real, or adjusted for deflation?

Anyway, I don't know a whole lot about what happens during cycles, so perhaps I'm way off the mark. Models are easy. Reality is another matter.

Regards,

Polly Cleveland

cc: Mason Gaffney

Dr. Mary M. Cleveland
14 West 68th Street, Apt 4
New York, NY 10023
(212) 873-2982
FAX (212) 873-6125

Saturday, Oct. 29 1994

M. Mason Gaffney
PO Box 7998
Riverside, CA 92513-7998

Dear Mason,

Good to talk to you last night.

Visions of Schalkenbach $$$ have inspired in me sort of a dream, maybe nuts:

A new monthly magazine (what???) titled *Progress and Poverty, The Journal of Economic and Social Issues.* Little explanation on title page: named in honor of famous American economist Henry George who tackled all the big questions.

Each issue addresses a major question, with invited essays by major economists, sociologists, anthropologists, historians, etc.,--preceded where appropriate by brief editorial on what HG thought of the subject. For example:

Malthus, Darwin, and the population bomb
Poverty in history
The Great Depression: can it happen again, *has it happened again?*
Territorial warfare in history
The history and evolution of the concept of progress
Why the industrial revolution
Nafta, GATT & the history of free trade v protection
Why Japan developed when China didn't
Slavery in history and in the contemporary world
Rent control around the world
Land reform and land taxes
Urban synergism
What really happened in the S&L collapse?
Technology and productivity
Growth vs the environment
What do all the economic thinktanks do?
Concepts in taxation: wealth, income, sales, Vat, poll
Productivity and the distribution of wealth
Why are some societies so corrupt or why aren't all totally corrupt?
Do the Russians have a chance to get it right?
Intoxicants: social, economic, political, historical

Containment policies for urban sprawl
Race and economics, around the world and in history
Urban slums and bad assessment practices
Economic impact of the Black Death, AIDS
Economics of primitive societies
Why the British colonies developed, while the Spanish and Portuguese ones didn't
The invention of property rights in the ancient Near East
Must America inevitably decline like other civilizations?
Libertarian vs Socialist philosophy
Defining the legal framework for economies
Why has neo-Classical economics become so technical and obscure?
Where have all the Marxists gone?
Marxists and Georgists
The miracle of the US Constitution

In addition, the magazine has regular features: Brief biography of a major economist or historian etc., summary of main ideas. Possibly interview with major living economist. Columns, book reviews, some humor. Advertising: books, magazines, records, other innocuous stuff.

Style: sophisticated, very well-written, but non-technical. Like *New Yorker*, *Harper's*, *Atlantic* or *Economist*. Low-key, tolerant and compassionate tone, understated wit but no sarcasm, let the facts and the people speak for themselves--no shrill yapping like the Libertarians. Appropriate photographs and other illustrations.

Format: Glossy 8 1/2 x 11 monthly like *Reason*, the top Libertarian magazine, which is put out by the non-profit Reason Foundation, partly supported by contributions. Subscription $25, lower rates for students.

Audience: Educated people, high-school and college economics and history students, Georgists, ..(Did you know, the most popular major at Harvard today is economics? Have they managed to make it interesting, or are kids just worried about their future in business? I enjoyed Ec 1, of course, like everything else I took, but the light didn't dawn until P&P.) *Discover*, a first-rate, semi-popular science magazine recently bought by Disney, has over a million circulation, because it targets high-school science classes. *Discover* doesn't back off of controversy either; latest issue: "Race, What is it Good For?" Is it possible to do the same with an economics/social/history publication?

Michigan has dumped its property taxes; Wisconsin threatens to follow suit. Cuomo finds property tax relief urgent because property no longer belongs to the rich! WE GOTTA DO SOMETHING!!!!!!!!!!!!!!!!!!!!!!!!!!!!!!!!!!

Don't miss the November *Harper's* piece by Peter Schrag on "California's Elected Anarchy."

Love,

NOV 08 1994

Mason Gaffney
P.O. Box 7998
Riverside, CA 92513

909/687-1677
OFF 909/787-5037, x1574
FAX 909/787-5685

1 Nov 94

Si Winters
Henry George School
121 E. 30th Street
New York, N.Y. 10016

Dear Si:

Thanks for sending your memo of 16 August to Ed Dodson, and your 6-page Report to the Trustees, and Mike's piece on Roscher.

After some pleading, I got Bob Gilmour to relent and let me stick by my invitation of Mike Hudson to the Great Barrington meeting. It worked out very well. Mike made a good impression, and showed the folks at Great Barrington he knows his stuff in their favorite field, banking and finance.

He also made a great impact on me, much better than at our first meeting with Ed D., when Mike presented a proposal for a macro model. Mike is a little too eager to show how much he knows, and occasionally some recognizable errors slip in, but overall he performs quite formidably. He may be a diamond in the rough, but more diamond than rough, as I now see it.

He drove back and forth with another New Yorker of high potentiality and achievement, Polly Cleveland. Polly lives at 14 W. 68th Street, phone 873-2982. Polly has a Ph.D. in Economics from U.C. Berkeley, has been a Georgist for 20 years, and is the newest Director of RSF. She writes great Georgist tracts, and is ready, eager and able to publish. I recommend her to you highly; her work could fit right into your program, along with Mike's.

Your memo and report give me two ideas. 1, you are looking for a book on "What's wrong with economics." By chance, Fred Harrison and I have finished *The Corruption of Economics* and are about to release copies, November 10, in London. It does not duplicate or compete with what you and Mike are doing (Mike has a copy of my part of the work), but complements it in important ways. I hope you will consider making it part of your program. Fred has an aggressive marketing campaign planned, but we need all the help we can get. Please look it over, and consider adding it to your offerings (Polly or Mike can supply copies).

I have supplied Fred with many names for mailings. I will gladly share these with you, if desired.

2, you are looking for a book on "the role land plays in economics." Again by coincidence of "great minds flow in the same channels," Fred is releasing another book Nov. 10, with Nic Tideman's name on it, including a chapter of mine, "Land as a Unique Factor of Production."

Both these works are done, will be published in a week after you receive this, and are yours for the using. I hope you will see how they might help forward your program. We can help you; you can help us.

I hope that you will use my editorial comments on Mike's work sparingly and constructively. After Gt. Barrington, I now see Mike as having deep insights, along with talents and experience, that will move our cause along.

No doubt Mike has told you about what Robert Fitch is up to in Brooklyn. This, too, may result in a valuable book that you might gain by marketing. It's a matter of selecting the most effective works, no matter who produces them.

Sincerely,

bcc: Polly C.

NOV 10 1994

Mason Gaffney
P.O. Box 7998
Riverside, CA 92513

909/687-1677
OFF 909/787-5037, x1574
FAX 909/787-5685

3 Nov 94

14 W. 68th Street
New York, NY 10023

Dear Polly:

Thanks for "RC and the Coconut Crash." How come you see my points so clearly, when no one else does? I think Fred Foldvary gets it, because it is so Austrian. On the other hand, neither he nor Alex Field seem to have girded their theories against the collapse of Pomona - see enclosed notes on article, which I sent to each of them.

"RC" must stand for something or someone obvious, but I don't get it. Roberts Cleveland?

Please send one to Fred Foldvary for comments. Fred is good about responding.

Love,

M.

EDGE CITY - and Nonrenewal of Old Cities

Davis, Mike, 1994. "The suburban nightmare." LAT 23 Oct M1

Pomona is now in decay. It has a higher incidence of poverty than L.A.; its murder rate is nearly up to Detroit's. From garden city to crabgrass slum - it is like hundreds of other aging suburbs, trapped in a downward trajectory.

"The failure of candidates to address, or even grasp, the acuity *(sic)* of the suburban malaise explains, in turn, much of the populist rage that currently threatens the two-party status quo."

In 35% of suburban cities, md. household inc. has fallen "significantly," 1980-90. They are falling into the same "abyss of disinvestment" that central cities did before.

(Fault lies with NCEists who prate of "quasi-rents" from buildings, likening them to land rents, never thinking how it requires incentives to replace them.)

Parma, OH; University City, MO; Brockton, MA, are inner suburbs now in trouble. (Fred Foldvary take note of Univ. City.)

Firm that left Pomona: Hughes' Missile Division. Firm that left Burbank: Lockheed, with "huge complex."

Who gains? New outer suburbs, or "edge cities" (-Joel Garreau). Or industrial enclaves like City of Industry, pop. 680, with "most of the tax assets of the southern San Gabriel Valley": 2,000 factories, warehouse and discount outlets, golf course (no tax asset!), resort hotel. Starves La Puente, South El Monte.

Simi Valley and Santa Clarita take from San Fernando Valley.

Some old suburbs were built fast with throwaway architecture, life = 30 years. This erodes into slum housing of the year 2000. Northridge earthquake manifested shoddy construction (Alex Field take note).

Morals:

1. Postwar mass construction is not as good as Alex Field may think.
2. Private provision of public services has not lasted as well as Fred Foldvary may think (University City case).
3. Needed and missing: tax policy geared to stimulate replacement, renewal.

Mason Gaffney
P.O. Box 7998
Riverside, CA 92513

909/687-1677
OFF 909/787-5037, x1574
FAX 909/787-5685

4 Nov 94

NOV 08 1994

Michael Hudson
83 Murray Street
New York, N.Y. 10007

Dear Michael:

Si sent me a copy of your paper on "Röscher's Victorian Views on Financial Development." Herewith some comments, which are intended to be constructive, and I hope will be helpful.

1. Si says that Nic says that Röscher was an important critic of H. George. However, the two works cited from Röscher precede 1879, and his criticism of George (or land tax ideas) is not mentioned.

2. This paper continues your rehabilitation of history before The Age of Pericles: a challenging and powerful thesis that holds deep fascination.

3. You make a wonderful point, p.3, that projecting history lets "economists become futurists." That gives meaning and excitement to the whole otherwise arcane enterprise of "looking backwards": we look backwards to help look forwards. Suggest you lean on this more, to motivate readers.

4. P.9, "debts preceded money." This evolution may have repeated itself through several cycles, somewhat on the analogy that "ontogeny anticipates philogeny" (or however that biological bromide goes). The first American "banks" were set up by landowners to monetize their land, rather than as places to deposit money.

5. Your emphasis on the dangers of national debt is timely, as well as timeless. George said little on this, perhaps because in his day the national debt was negligible and local debts bearable (aside from state bankruptcies after 1837, and the Confederate States of America bankruptcy). However, if the nation collects all the rent merely to pay interest on a national debt, of what avail is LVT?

6. Lamberg-Karlovsky's thesis of *rapid* emergence of complexity is important. It has an analogue in Jane Jacobs' chapter on the *explosive* growth of cities, sometimes in cyclical phases, but with a secular aspect: i.e. first City A grows explosively, and later City B does. Ditto for firms, of course.

In support, some say the English political unification of the 16th Century cleared the way for the commercial revolution of the 17th, laying the groundwork for the industrial revolution of the 18th. On the other hand, the 16th was disastrous for wage rates and employment and egalitarianism. Also, the Lombard and Hanseatic Leagues and the bankers of Augsburg and perhaps Amsterdam and Zurich thrived commercially without a central state - does that fit?

Now, being the scion of editors, I will fall into the temptation to nitpick. This draft in its present stage invites it: better it be done *before* something is published.

A. There is nothing on George, seeming to defeat Si's original purpose.

B. p.5, wars cause debt; p.13, wars wipe out debt. Compose these.

C. p.5, i.r. at 1/60 per mo. works out to annual rate of 21.94%, not 20%.

Major thesis here of customary rates set by numerological accident will strike many modern readers as implausible. Therefore it needs lots of bolstering, but gets none. 99% of readers (including me) will know nothing of sources on pre-classical antiquity.

D. p.5, 1980 prime rate rose to 20%; but on p.14, credit is forced into unproductive loans by lack of productive outlets in the 1980s. Compose this apparent contradiction.

E. p.8, Röscher is a Victorian optimist; but on p.1 he has an underlying Ricardian pessimism (although this contradiction is partly resolved on p.1 itself).

F. p.10, I would say privatization results not from debts beyond "ability" to pay, but beyond "<u>willingness</u>" to be taxed to pay.

G. p.13, the core transmitted its technology to the periphery, which was "smaller, less centralized and more 'privatized' ... " Maybe this occurred, Egypt to Greece, as stated, but in European history the core seems to have been smaller and less centralized (city-states and principalities) transmitting to new nation-states on the peripheries: France, England, Spain, Sweden, Russia, perhaps Turkey.

H. Privatizing as "public giveaway" needs support or explanation. Many will point out the assets are sold, not literally given.

Hope this helps, and also that your NYU conference succeeds in every way. Perhaps you heard that the Levy Inst. may host and fund a conference sponsored by the "Geo-economics Committee" next year.

Best wishes,

cc: Si Winters
Nic Tideman
Polly Cleveland

Dr. Mary M. Cleveland
14 West 68th Street, Apt 4
New York, NY 10023
(212) 873-2982
FAX (212) 873-6125

Monday, Nov. 7, 1994

M. Mason Gaffney
PO Box 7998
Riverside, CA 92513-7998

Dear Mason,

I'm glad you found "RC and the Coconut Crash" amusing. More important, does it make sense as a paradigm for the way wealth illusion from a boom can cause massive destruction of capital in a crash? If so, what data should we be looking for to support this hypothesis? Obviously, as we know, rise in short term interest rates just before the crash. Tight inventories before the crash, goods sold before they have been manufactured? After the crash, shift in demand structure from luxuries to staples. Farm prices fell, but fresh produce from California should have fallen harder than wheat from the midwest. What else? Unemployment. We know from Alex it was worst in construction. Should see employment shift from luxuries to staples. Takes time for people to adjust to sudden change in available jobs, and severe drop in real wages. I wish I understood money better. It's in there somewhere, playing a major role in wealth illusion. But I'm not clear just what effect monetary contraction has during a depression.

Of course a computer can easily model RC, but I want to be sure I have the concepts straight and some good real world data before tackling it.

Lowell sent me the enclosed piece. The guy's on the right track, and he's done a very helpful survey of recent literature.

Love,

Dr. Mary M. Cleveland
14 West 68th Street, Apt 4
New York, NY 10023
(212) 873-2982
FAX (212) 873-6125

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Of course a computer can easily model RC, but I want to be sure I have the concepts straight and some good real-world data before tackling it.

Tuesday, Nov. 8th -- Daniel is 15 today!

Received two!! letters from you today. I'm flattered.

In your letter to Mike Hudson you write: "The first American "banks" were set up by landowners to monetize their land, rather than as places to deposit money." I'm ignorant of American banking history; please explain what this means. Can you give me a good reference on banking and monetary history?

I'm glad you liked my ideas for a Georgist periodical. I actually had something broader in mind: a journal that looks to George for inspiration, not because he necessarily had the right answers (though we may believe he did), but because he asked the important questions. I see a journal that makes economics, sociology and history exciting and relevant to a wide audience, high school and college students especially. It cannot be just a journal addressed to those who have seen the Georgist light, and speak a special jargon

that baffles outsiders--though it would offer George's and related books for sale mail order.

My model is *Discover*, which makes the sciences exciting and relevant, including social sciences like psychology, archaeology, anthropology and some history. (You should give Patty a subscription, if she doesn't have one already.) After what I gather were some rocky early years, *Discover* was bought by Disney three years ago, and is now enormously successful, with a circulation over a million--so far without compromising quality. A similar model is *Natural History*, put out by the American Museum of Natural History.

I see a classy publication that might eventually even make money--after all P&P made loads of money. Or less optimistically, like *Reason*, a publication that makes ends meet by asking subscribers to contribute to the non-profit publisher. And yes, it would require a substantial startup investment, some of which could come from Georgist seed money, some from loans, and some from advance sell-in. Now that I have your encouragement, I will speak to the *Discover* staff and others, maybe Hapgood too, to get a fix on costs, size of staff, time scale etc.

Maybe I'm aiming too high, but a little research should settle that.

Lowell sent me the enclosed piece. The guy's on the right track, and he's done a very helpful survey of recent literature.

I should renew acquaintance with Si Winters & George Collins; I haven't seen them since '91.

Wednesday, Nov. 9

What do you think of Lowell's committee? Susan considers Dick Noyes the source of plots against Oscar and the staff.

Boy are we in for it now. Our new governor Pataki favors one strike and you're out. Maybe he'll calm down when he adds up the costs. And you've got 187. What do you make of it? Do Californians really blame lower-class furriners for their problems, or does it mean something else?

Love,

NOV 08 1994

Mary Cleveland
14 W. 68th St.
New York, NY 10023

Dear Polly:

Thanks for your brilliant ideas for a Georgist periodical. Every vital movement has one; our movement just hasn't been up to it, at least for a long time. We have depended on *Land and Liberty*. Fred, with all his virtues, had made that more tabloid than "journal of opinion."

Si Winters at the HGSSS (121 E. 30th St.) is pushing for a *Forum*, to produce conferences and scholarly books. I think a periodical would get quicker results and wider readership.

I don't know about costs. David Hapgood (he whose inactivity and resignation made a place for you at RSF) could perhaps advise us. Glossy is costly, I suspect. How about pulp, like *The Nation*? How about digest format, like *The Monthly Review*? How about newsletter format, like George Seldes' old *In Fact*? All of those made it big with college students.

It would help to get RSF out of the high rent district, where they could spread out some and do more work - like the South End Press of Boston.

I am running your idea past Si Winters. If he could get the HGSSS behind it, it would be a good start. Did you know that the old HGSSS published a monthly, *The Freeman*, from 1938-43 or so? (I have a complete collection - probably one of the few, if not the only one.) It fell into the hands of Frank Chodorov, militant libertarian and pacifist, who fought against the war and lost his paper ration, as well as his support (although the Lincolns may have backed him - an interesting question). Just as well: he was more libertarian than Georgist, and later teamed up with the F.E.E. at Irvington-on-Hudson.

You would make a great Editor! You could get guest editorials from old friends like Peters of the *Washington Monthly*, Mike Kinsley of *The New Republic*, Sierra Club and *Clear Creek* types, and others. It's a natural!

Love,

Mase

Dr. Mary M. Cleveland
14 West 68th Street, Apt 4
New York, NY 10023

(212) 873-2982
FAX (212) 873-6125

November 11, 1994

Dr. Fred Foldvary
709 Circle Drive
Blacksburg, VA 24060

Dear Fred,

Mason said I should send you the enclosed fable about "RC and the Coconut Crash," which I sent him and Alex Field. It's a simple story of how a crash could occur, and what it means-- in a "Robinson Crusoe" economy. The point is that capital structure may get too stretched out due to a "wealth illusion," which can be caused by a land boom. When the bubble bursts, people are suddenly forced to revert to less "round-about" methods of production in order to restock liquid capital, abandoning now worthless fixed capital.

Does this make sense to you? If so, what sort of evidence from the Depression and from the S&L mess and land value fall of the '80's would support this story? RC has a growing economy. Could a crash happen in a static economy, -- some disaster forcing the eating of seed corn, and a reversion to hunting and gathering?

Let me know what you think. Thanks.

Sincerely

Polly Cleveland

cc: Mason Gaffney

Dr. Mary M. Cleveland
14 West 68th Street, Apt 4
New York, NY 10023
(212) 873-2982
FAX (212) 873-6125

Tuesday, Nov. 22 1994

M. Mason Gaffney
PO Box 7998
Riverside, CA 92513-7998

Dear Mason,

I've enclosed the response to RC from Fred, who did not get it, and my response to Fred. I'm perhaps in over my head. I think I understand the theory, or at least a theory that makes sense to me, but my grip on the data is shaky. Help!

I think your speech to the environmentalists is terrific. Will it be published somewhere? I loved the bit about how the rich actually *choose* to live on the East Side of Manhattan because they *like* it there! And you very effectively stick it to the Libertarians on property rights. (When they first came on the scene, it was a breath of fresh air: finally some people associating personal and economic freedom. But then it turned into, I need a good metaphor, a cold shrill wind.)

I enjoyed Michael's conference. The conferees were excellent, and the focus on property rights led them to discuss and connect economic history in a way that I had never seen when I was in the field. It was very exciting for me, though I suspect a bit beyond most of the attending Georgists. I saw George Collins and Si Winters, though I didn't get much chance to talk to them.

Lowell, bless him, has arranged my visiting scholar status at Columbia, so now I can use that luscious library of business and economics!

Love,

Dr. Mary M. Cleveland
14 West 68th Street, Apt 4
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Love,

Virginia Tech
VIRGINIA POLYTECHNIC INSTITUTE
AND STATE UNIVERSITY

Department of Economics
College of Arts and Sciences
3016 Pamplin Hall, Blacksburg, Virginia 24061-0316
(703) 231-5688 Fax: (703) 231-5097

DEC 04 1994

Nov. 26
~~Oct. 28~~, 1994

Fred E. Foldvary
709 Circle Drive
Blacksburg, VA 24060

Dr. Mary M. Cleveland

Dear Polly,

I'm glad my comments were useful.

The question raised by your letter of Nov. 22 is, why is it that at times, large numbers of business cannot borrow?

It seems to me that when there are wide-spread simultaneous liquidity problems, it is due to banking restrictions and interventions, as we have had in the US system since the Civil War, when the currency became nationalized, and by the states before that. Central banking and monetary policy intensified the intervention. In our interventionist economy, major fixed assets are abandoned because 1) economy-wide space/time costs rise (as speculative land values increase, or interest rates rise), or 2) actual or anticipated demand falls.

In a pure market economy, with free banking and no taxes *in substance* (LVT being a tax in form but not substance), and no arbitrary restrictions, a business can always borrow - at some interest rate and risk premium, one can outbid other borrowers. Intervention can cause economy-wide turbulence by: lowering and raising interest rates, controlling credit, fueling speculation with tax-funded public works and subsidies: resulting in economy-wide increases land value and interest rates. As costs rise, profits are choked, investment falls, hence demand falls, further squeezing profits, and down she goes. In the Austrian story, capital goods are malinvested when interest rates are artificially low; the demand for the ultimate consumer goods is unchanged, resulting in a glut of higher-order capital goods. It seem to me that you could well incorporate interest rates into your analysis, as a space-time continuum.

On your points:

1. Of course Crusoe can experience capital collapse.

2. Systematic entrepreneurial failure must be a consequence of government interventions which create false price signals, such as an injection of money by the central bank, or, as you note, a land

boom (caused in large part by implicit economy-wide subsidies to landowners, with government transferring funds from laborers to landowners via public works). An important question, as addressed at AIER, is to what extent a land boom is fueled by money expansion (or whether it instead precedes money expansion).

3. Is it possible to have a capital-goods collapse without money or rent? Of course - nature can intervene instead of government and destroy capital with earthquakes, fire, and locusts. Capital is still destroyed even if it is insured. Technological innovations can also economically destroy previous capital.

4. There is indeed a capital collapse during a depression, caused by malinvestments during a boom. It seems to me the question is not whether the cause is monetary or real, but how the two causes work together. The evidence was visible in the recent depression in vacant, even abandoned, real estate projects. We can also look for evidence in "higher order" capital goods, such as factories and new farmland, that have lost value due to anticipated demand that did not materialize, or previous demand that dropped.

I don't see why there would be a real liquidity crisis, though, if there is enough physical food and other consumables, unless government-induced rigidities are present. In the 1930s there was a macro surplus of food but many micro shortages as people couldn't afford it. The question is, why could individuals not exchange goods and services, thereby increasing utility and providing mutual employment. Part of the answer, I think, is that the system was cash- and credit-constrained due to interventions. Indeed, there were places where locally-created currency circumvented central banking and created some opportunities (which I read about, but don't have handy sources for).

Real interest rates fell during the recent depression, and the FED is now hiking them up. The puzzle is why banks should raise retail rates just because the FED is raising its wholesale rates, since banks depend mainly on savings and their own money creation. Do you think the FED may be a Stackelberg cartel, the FED acting as a price leader, perhaps engineering a political business cycle recession in the midst of the larger real estate upswing?

Sincerely,

cc: Mason Gaffney

Fred

Mason Gaffney
P.O. Box 7998
Riverside, CA 92513

909/687-1677
OFF 909/787-5037, x1574
FAX 909/787-5685

30 Nov 94

Dear Polly:

Thanks for sharing your exchange with Fred Foldvary. Comments follow, keyed to his numbers.

1) "Durable capital" is simply shorthand for "higher order capital goods (more roundabout)." "Durable" means a large share of the value is derived from distant future services anticipated.

4) A rise in interest rates is self-feeding when it freezes up durable capital, keeps owners from recovering its value through CCAs. This is the essence of a capital crunch. See my Gt. Barrington paper, pp. 2 ff. Herewith is one relevant part.

> "3. A rise of real interest rates (i.r.s) destroys part of the real value of existing capital, in increasing measure of its putative longevity.[1] ***This is an economic loss, a loss that is just as real as physical destruction.*** The cash flow from durable capital will, after a rise of i.r.s, be divided more in favor of interest, less in favor of Capital Consumption Allowances (CCAs).[2] The basic mathematics of finance is available, and is quite precise and consistent.
>
> Conversely, a fall of real i.r.s adds to the real value of existing capital, having the same effect as creating capital.
>
> [Both those effects are muted by countervailing effects on ground rents and land prices. This refinement is not pursued here, but that does not mean it is unimportant.]
>
> IMPLICATIONS.

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[1]"Longevity" here means economic life, in the full economic sense. It should not be confused with physical carcass life. The "full economic sense" means the duration and time distribution of cash or service flows, properly adjusted for the time value of money.

[2]The appropriate accounting adjustment on the asset side is called "marking to market value." The loss of value occurs *whether or not it is formally recognized on the books.*

A. The response to a shortness of available (soft) capital is economically to destroy part of durable (hard) capital. This raises the possibility of ***a macro-economic "glitch,"*** (a perverse episode of harmful "positive feedback," often called a "vicious spiral.") This effect, variously described and with varying emphases, has been noted by Ricardo, Jevons, Boehm-Bawerk, Wicksell, Spiethoff, Hayek, and others. Ricardo's Chapter 1, "On Value," and Chapter 31, "On Machinery," are good introductions. They are nominally well-known, and at the same time treated as non-existent: a feat of compartment-mindedness that seems to characterize much economic writing. As Lionel Robbins points out, micro theory after 1870 became one of acapitalistic production.[3] Capital theory simply disappears from the picture.[4]

I think maybe Fred is torn between the Austrianism of Hayek's cycle theory, which includes the possibility of a glitch, and neo-Austrian or libertarian market-faith. In this faith, which may be held as a rigid dogma, markets would work to perfection if buttinsky bureaucrats would keep hands off. Claims of market failure are viewed skeptically and alleged to result from government intervention (whatever that means).

6) A landowner's "momentum illusion" in a rising market is not different from a wealth illusion. As in (1), Fred is introducing a distinction without a difference, an empty formalism that may just muddy the waters and delay a real engagement of minds over the essential points.

9) How does "lack of liquid capital" manifest itself? In shortage of payrolls, most obviously. If banks do not recover money they have loaned, they cannot relend it. If direct investors do not recover capital in higher order capital goods, they have no liquid funds to meet the next payroll.

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[3]Introduction to the English translation of Wicksell's Lectures (p.xiv).

[4]An attempt to reintegrate capital theory with micro and macro theory has been made by the writer, 1976, "Toward Full Employment with Limited Land and Capital." In Arthur Lynn, Jr. (ed.), Property Taxation, Land Use and Public Policy. Madison: Univ. of Wisconsin Press, pp. 99-166. Also in "Capital Requirements for Economic Growth." Joint Economic Committee, Congress of the United States, U.S. Economic Growth from 1976 to 1986: Prospects, Problems and Patterns. Vol. 8, pp. 56-75.

In both works, the effort was to use capital theory as a bridge to unify micro and macro theory.

Once this happens, consumers cannot buy, and unsold inventories appear. As you said, Polly, these may look surplus from a seller's view, but to buyers they are overpriced. There was hunger stalking the land in the 1930s - my mother made me and my brother make 12 sandwiches a week, every week, to feed the poor in the slums of Chicago. There is hunger again today: an estimated 1/6 of Americans are not getting enough to eat.

Why do interest rates fall in a depression? First, they soar just before the recession, playing a role in triggering the upper turning point. Then, **recorded** rates fall, because credit rationing screens out all but the most credit-worthy (propertied) borrowers. The rates for those who are refused loans are not recorded because they do not take place. Volume of loans is leveled downwards. Ben Bernanke made his name by writing on this point. He only rediscovered the wheel, but he deserves credit: that sure beats losing the wheel.

10) The poor could borrow food and build houses? This sounds weird - better think it out again.

You say you don't know what happens during cycles? Who does? Homer Hoyt is a good start. During the 19th Century it was clear as crystal that, during booms, the nation wasted too much capital on "higher order" capital goods of the five kinds I have defined that are spurred by overpricing of land. There was a turnpike boom ending in 1798; another in 1819; a canal boom ending in 1836-37; three r.r. booms peaking in 1857, 1873, and 1893. Then there was the first auto-oriented suburban boom, peaking in 1929.

Hope these thoughts help.

Faithfully,

Love,

M.

cc: Fred Foldvary

Dr. Mary M. Cleveland
14 West 68th Street, Apt 4
New York, NY 10023
(212) 873-2982
FAX (212) 873-6125

Tuesday, Dec. 13, 1994

M. Mason Gaffney
PO Box 7998
Riverside, CA 92513-7998

Dr. Fred Foldvary
709 Circle Drive
Blacksburg, VA 24060

RE: RC and Capital Collapse

Dear Mason & Fred,

As my father says, if it had been a dog it would have bit me. The fall in interest rates in a depression never made sense to me: interest rates should be high, telling people to replace short-term capital. Of course, as you point out, it's only *recorded* rates that fall, that is rates in the official credit markets, where credit-rationing screens out all but the most secure. I should have known, because in my growth model I argue that although poorer people get a lower *cash* return on investments in the formal credit markets, they get overall a higher return on investment due to capital market failure.

I'm familiar with Hoyt's 100 Years of Land Values in Chicago. What I'm not so familiar with are the detailed statistics on business cycles: what rises and falls in which order. And of course these statistics have to be "interpreted" as, like interest rate statistics, they represent only part of the market. I know that, surprise!, the Depression began with a crash in demand for durables. But what happens before and after?

Mason says "lack of liquid capital" manifests itself in "a shortage of payrolls, most obviously." Yes, but there's a chicken and eggishness to that. Payrolls fall short because sales fall short, leaving consumers unable to buy, so that sales fall short. Which sales fall short first and why? What's the weakest link in the chain? Do some sales fall short first because producers have over-projected demand, as for suburban housing? Is that the weak link? I just read a piece by Ceccetti etc. in *Rev Econ & Stat* Feb. 94 to the effect that there was a crash in aggregate demand in 1929, followed in 1933 by a crash in aggregate supply. I don't follow their fancy footwork in separating supply from demand schedules, but assuming they're right, I'm not sure what the results mean, whether they have missed the trees in the aggregate wood. When RC found rats in his coconut pit, his demand shifted away from future coconuts or coconut trees, to present coconuts. Did his aggregate demand change? How do you measure combined aggregate demand for present and future goods? Is there such a thing independent of interest rates? Whose interest rates, given capital market failure?

Now as to the role of bank regulators in the Great Depression: The next chapter in my story is entitled, "RC and the First National Coconut Bank." RC lands on the island, as before, and discovers a large flat area suitable to planting coconuts; however coconuts can be harvested year-round from the rest of the island. But then RC_2 paddles up. RC_1, having but a shaky claim to the flat area, offers to "sell" RC_2 an acre for a nominal amount, 100 coconuts, 10 down, the balance payable over the next year. Then up paddles RC_3. RC_1 sells him an acre for 110 coconuts. And so on. RC_1 has in effect become a banker, lending coconuts to new arrivals to enable them to buy his land. As the population grows, the value of flat land rises. The early arrivals, who at first planted and tended new coconut trees themselves, now hire the new arrivals, at a wage determined by the rate at which coconuts can be harvested from the wild, hilly lands on the island. And RC_1 lends more and more coconuts, first to the purchasers of land, next to the planters of coconut groves. And the price of land rises steadily. As the demands of borrowers rise, RC_1's coconut pile shrinks, and he raises his interest rates. At some point, the inevitable happens...

Question: who's the government, and who's the regulators? RC_1 and other early arrivals are the *de facto* government. Maybe they even elect a Mayor of Cocoville. But the whole precarious structure is created by about as free a market as one can imagine. Is this what Mason means by wildcat bankers monetizing land values?

Mason: thanks for the *Business Week* clipping. I had actually talked to Paul Romer on the phone, and read his dissertation, published in the AER. I thought he had an intriguing growth model, but it wasn't obviously related to distribution of wealth. I seem to have missed something important. I'll give him a call and see if he's coming to the AEA meeting in January. He did another interesting piece recently, showing that conventional modeling tends to underestimate the gains from trade.

Happy New Year!

Regards,

Mason Gaffney
P.O. Box 7998
Riverside, CA 92513

909/687-1677
OFF 909/787-5037, x1574
FAX 909/787-5685

13 Dec 94

Dear Polly:

In yours of 7 Nov you ask about the first American banks. My sources on this are varied. Enclosed are some of my notes, and a bibliography of works cited therein. It's a smattering. I have yet to find a good definitive work on banking history per se. Hammond and Mints both stink. Nettels may be good: I have yet to read it. Also, Davis Dewey.

If you can, roust Susan sometime soon to lay in more copies of Fred's book output. I suspect she has daringly ordered about 10 copies. Then, when she runs out, she will take months to reorder. Meantime, I have put *Land and Taxation* on my students' textbook list for next quarter, in Public Finance, which should eat up 20-40 copies.

I will try a sub to *Discover* for Patty. Another great one is *Earth*, put out by Kalmbach Publishing in Milwaukee.

Dick Noyes is not the source of "plots." He is quite open, and has spoken to Oscar directly. It is obvious to all that Oscar is not doing the job. Susan's paranoid reactions support a view that she is not the person for this job.

Prop. 187 - I am puzzled that it should be called liberally incorrect. There are lots of Yahoos behind it, granted, but that is true of most things that win. César Chavez opposed illegal immigration, and so have most unions. As for calling it racist, what about the blacks? They are all legals. What puzzles me most is that the blacks are so quiet: they of all people have most to lose from illegals. The big supporters of illegals have long been the landowner-employers who use them to beat down wages. They do it at various levels, too: half the college profs. around here are aliens (but not illegals). They are more docile. One dean was known for controlling the votes of his quasi-legal faculty members by reminding them he had to certify their employment each year.

H. George opposed illegal immigration when he lived in California. In NY, he made a pal of Emma Lazarus, who wrote an ode to P&P the year before *The New Colossus*. Somehow they resolved all that. Good: it's nothing we should let divide Georgists.

Speaking of which, the Sapiros are suing Steve Cord for taking their money and failing to perform as promised. Nic T. and Dick Noyes spent "hundreds of hours" (says Marion S.) negotiating, but Steve is adamant (says Marion). God save us from spending our

time squabbling! Whatever I can do I shall do, and not leave money for others to fight over and waste!

Love,

M.

History of Banking, notes extracted from Paxdiv

"1715-. U.S. Craven:323. There were champions of a land bank, to supply money. These grew popular "postwar," i.e. after 1715. [Seems sync with J. Law.] See Nettels, Money Supply; Craven is nebulous.

"1717. Fr. Perk:449. King gives Law's Co. of the West (Miss. Co.) mnpy of trade with La, plus title to all the land, and sovereign powers. 1718, mnpy to mfr. tobacco. Also, all propty of E. India Co. of France, and China Co. - if he assumed debts. Became Co. of the Indies, but called Miss. Co. by all.

To raise K, Law took govt. securities at face, = 2.5x market. Also agreed to fund, i.e. not collect. Thus, had no real K.

1719, prominent persons took chunks of land, sent out colonists. 1717, founded N. Orleans, appealing to vanity of Regent.

1719, p.468, shares now sold on credit, 5% down. But restricted subn. rts. to present shareholders: "mothers, daughters, granddaughters," etc.

"1717. France. NCE:1793. John Law acquires monopoly of La. commerce. 1719, Law's co. absorbed several other orgs. "for the development of" Indies, China, Africa: most French colonial trade. Got right of farming the taxes. Assumed the state debt; amalgamated with royal bank. Large influx French settlers in La. [There was a military motive to settle, also, to thwart Spanish advances. Funny they didn't put more people in Quebec, too, but there were a lot.][This implies real K moved there, too. This would drain disposable K from France.]

Oct. 1720, Miss. Bubble bursts.

"1718. Fr. perk:446. French state buys out Law's Bank; bills become inconvertible, volume reg. by royal council.

"1719. Fr. perk:475. Reckless consumer spending by newly rich from rising shares. P.478, "Sudden wealth ... brought corresponding extravagance." Diamonds, 80 horses, 90 servants, gold and silver plate, constant guests, etc.

"1720. Eng. Versteeg:270. Bubble Act, apparently outlawed land-banking. P. 256, it definitely "prohibited land banks." [Mints is silent; Hammond is supercilious.]

Hammond stresses anti-corporate nature of Act, and of Eng. devmt. ff. Eng. was very anti-corpn., or at least general incorp. There were a very few particular corps.

Hammond overlooks fact that this was period when Eng. raced ahead of world in business innovation. War and small business were associated with rapid advance.

"1720. Fr. perk:495. "Never had murders and robberies been more frequent." Thus, this kind of "prosperity" is divisive.

DATA NEED: crime rates over time.

"1720. Fr. perk:482. Law, having turned Catholic, made comptroller general.
Raised dividends to correspond with high price of shares. However, with dM, i.r. had fallen to 1.5%, lowest anywhere.

"1720. Fr. NCE:793. Crash of Miss. Bubble; in Eng, S.Sea Bubble.

"1740. Versteeg:270. A land bank was organized - no name given. Issued notes with land as security. [This indicates a boom? Possibly, but may also have been a local reaction to tighter money from England.] Versteeg hints the bank was public or semi-public. It was closed down by extending the sway of the English "Bubble Act" of 1720 - apparently that Act outlawed using land as security for money. Gov. Shirley of Mass. let the bank liquidate gradually. Bank supporters soon made a comeback, first in Salem. (Connection between witch-hunters and land-bankers?)
P. 256. 1741 is when England extended Bubble Act to stop land banking in colonies.

"1764. W. Miller:100. Currency Act, demonetized VA legal tender notes, to protect Eng. creditors. Cf. Bubble Act. Cf. Hacker:166. Puzzle: Decl of Indep. is silent on this, why? Need to bring native creditors under the umbrella, probably.
[Theme: constant struggle between equity owners of land titles, and mortgagee-owners, bankers, etc. Hamilton, having won Revn., sided with bankers, just as English had before revn.
A War party would naturally include indebted landowners seeking inflation, although this enthusiasm would be abated by prospect of taxes.]
[Am. Revn., unlike pure class revns., seems to have been aggravated by deflation, not inflation.]

"1764. (Source lost.) In U.S., Eng. Currency Act of 1764 stifled colonial banks from inflating. Creditors in command, not equity holders.

"1780. Jameson, p.64. 1st bank in U.S., Bank of N. Am., Phila. By 1789 there were still only 2 more, one in NY, one in Boston. Thus, here was a boom w/o indigenous banks.
[What does J. mean by banks? He means deposit banks - see Mints:61.) There were earlier land banks, stifled by Bubble Act and 1764 Act. Cf. Bray Hammond.

"1781. Mints:61. Bank of N. Am, 1st instn in U.S. to receive deposits, make loans, and issue notes.
Previously, many banks had simply made loans on security of r.e., issuing bank notes. [I.e., they monetized land; and this preceded receiving deposits!]
1784, Banks of Mass and NY. 1790, still only 3 of what Mints calls "banks," i.e. those resembling Bank of N. Am. In 1800 there were 28. Source: Davis Dewey, Financial Hist. of U.S.

"1781. Jameson:62. Continental bills had fallen to worth of ca. .025. Exchanged for new ones at 40/1. [Cf. German currency reform, 1948; Soviet reform, Jan. 1991.]

"1790. Mints:64. Hamilton, Report on a National Bank, thought lending on land was not feasible because r.e. loans are not liquid. Mints hedges. (On grand scale, Ham had U.S. pledge fed lands for debt.)

"1791. France. Kenn:85. Constituent Assembly seized church lands, issued paper money on the security.

"1791. CHW:791. 1st B.U.S. established. [Just in time to preside over crash of 92. Did it trigger crash by trying to tighten M, serve rent-takers of the 2nd kind?]

"1791. Bowers25:87. Specn in scrip of the new Nat. Bank drives up i.r. to 2.5%/mo and higher, says Jeffn. Logically, though, these are zero-sum xctions, so probably some other factor is driving up i.r. Except that old owners treating gains as income would overconsume. Madison said money "will be unsaved by the public." Ham worries specn goes too far, which it did. P.176, Jeffn had seen money leave remote regions for Phila, l.v. fall steeply.

P.87, Aug, 1791, price of scrip breaks, tumbles.

P.176, April, Duer ruined.

Here seems a case where acute shortage of liquid K betrayed by peak of i.r., triggering slump. Jeff used it as a stick to beat the Nat. Bank he opposes, missed seeing prime causes.

"1792. FWPConn:49. First toll road in CT, Mohegan Rd. from Norwich to N. London. It was a state enterprise; most other tollroads were pvt. corpns. 1792, Greenwich Rd. also opened, (claimed to be the 3d in America, but I doubt this: cf. 1785, NCE:2807, Va. Maybe they mean the first state-owned toll road.)

Thus, one way of freezing K leading to 92 slump was building tollroads. The way things work, probably tollroads were self-liquidating, in rentable regions, while free roads were in marginal, especially developmental regions (frontiers, as opposed to backwoods). NEED INPUT as to whether roadbuilding was major sink of K before 1792; but it clearly was before 1798.

"1792. ohio. Sakolski:105. Ohio Co. petitions Congress for relief from pmt obligations. Cong yields, lowers price to .50$/ac. Its problems were due in part to rise in value of Fed secs, due to Ham's funding scheme. Was also Indian trouble; and Cong might lower price of other fed lands. Sounds a lot like a sharp drop in demand.

"1792. Eng. Mantoux:126. Panic began a year before war with France, war didn't cause panic. [Probly aborted much of it.]

"1792. U.S. Sakolski:153. Financial panic, in NY and Phila. Reign of Terror in France, and suspension by BoE were causes.

(Anachronism by Sakolski? Suspension came 1797. Probably he was stretching for a "good" reason - and missing the one under his nose!)

"1792. U.S. Livermore:142. Wm. Duer goes bankrupt. P.144, so did Platt, his assoc., in "The 1st Wall St. Panic" (altho some of Platt's losses were from short selling.) Rufus Putnam, a ptnr, now gets Congress to complete an originally agreed grant of 1m acs at much lower price. (Does that mean land bubble had burst?)

"1795. Sakolski:165. Mr. James Greenleaf, assoc of R. Morris, had inside with Dutch bankers; but French invasion of Holland meant he could not deliver money to fill contract of buying (and improving!) lots in D.C.

[Nap. control of Eur. K mkts cd. explain slump. War elsewhere could depress investing here. Higher demand, coupled with lesser K, causes subbing labor for K: good for w.r.s, bad for l.v.]

"1797. Chron of Am:226. Bank of England fails, crushing the Atlantic trade, and credit. Robert Morris fails, is jailed.

[1800, Cong. passes Bankruptcy Act, frees him, altho it does not extirpate jail for bankruptcy overall.]

[Thus, crash of 1798 was Eurogenic in part. So was 1792.]

"1807-14. Rothbard:2. Embargo, and Non-intercourse Acts, U.S. imports and exports shriveled toward zero. This greatly fostered domestic industry. Notably textiles.

Fed gov borrowed. N.Eng. banks would not lend, so U.S. encouraged loose money elsewhere, borrowed it.

"1810. Mints:42. Report of the Bullion Committee. Subject: was the paper currency depreciated, and if so, why?

Antibullionists defended B of E, which had followed real bills doctrine. They said the paper currency had not depreciated. P.75, aka banking school, after 1821.

Bullionists said it had depreciated. P.75, aka currency school, after 1821.

"1811-17. WMiller:159. Interbank era, state and pvt. banknotes overissued. Used to buy land. 1817, 2nd B.U.S., but did not tighten up until 1818, when "land boom was already showing signs of petering out." (What signs? What evidence? Cole:233 says peak of sales in 1818.)

"1816. Rothbard:7. 2nd B.U.S. formed, opens 1/1/1817. Loosely run, expansionist. Tsy encouraged this, it received taxes and land sales in frontier banks, wanted B.U.S. to accept them. It did, and stockpiled many, fueling expansion of others.

p.11, strong social pressure vs. making banks pay in specie.

p.9, investment banking grew, too: banks did both.

p.11, specie meant Spanish silver $. P.150, in VT, private Canadian bills used.

(1st B.U.S presided over crash of 1798; 2nd over crash of

1819. Faith in central banks showed amazing endurance!)

"1816. CHW:791. 2nd B.U.S. established. One reason was to help U.S. treasury, "which was financially embarrassed on account of the war." - Bogart:364. I.e., Madison preferred debt-financing: he would.

[So in this boom, banks expanded on U.S. debt, not just land collateral. 1836, by contrast, was no U.S. debt, m was all based on land specn. Here is a prime reason 1837 fall was so steep, and others less steep. Likewise 1929. The Perils of Peace.

Ham. was right about one thing, anyway: public debt is more stable basis for bank deposits than is land.]

"1820-. Bogart:372. State banks came on, new variety. Chartered by States, avoiding Constl. prohibition on states issuing bills of credit. 1837, USSC validates them. (Was this the occasion for McCulloch v. MD? No, that was the other way around, to stop MD from taxing B.U.S. Both cases, banks won, in court at least.)

"1824. Goodrich:125. Was a "Bank Mania" this year, states cd sell bank charters for big bucks. Some did, to finance canals, couldn't have sold them for much the ff. year.

[A purely paper affair, no serious slump.]

"1825. Eng. Mints:124. Some kind of banking "crisis," no details.

"1835. WMiller:180. Nat. debt paid off, surpluses mount swiftly, from land sales. Jackson, feuding with BUS, deposits surpluses in pet banks, which expand fast, lending to buy U.S. land, creating more surplus, etc.!

[Here rise-taker was U.S. govt., used $ to pay debt, thus created pvt. K.]

+ feedback = DANGER! Collect list of + feedback loops.

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DEC 2 1 1994

From my letter to Mase of Nov. 28 (irrelevant material deleted):

On item #10 from our letters to Polly, suppose we have a community with farmers who can't sell their crops, carpenters who have no customers, and shopkeepers who can't sell their goods, because no one has enough money. Why isn't this idle labor employed providing mutual services? If they had cash, then they would start buying from and then producing for one another. So the unemployment seems to be caused by a cash shortage. But cash is just a form of bearer credit. The problem is really a lack of credit. If they extended one-another mutual credit, then the shopkeeper could borrow food from the farmer, the farmer could borrow carpentry services, the carpenter could buy from the store on credit, etc. Why is this weird? To me, what is weird is unemployment, when people instead could provide mutual services.

Fred

Virginia Tech
VIRGINIA POLYTECHNIC INSTITUTE
AND STATE UNIVERSITY

Department of Economics
College of Arts and Sciences
3016 Pamplin Hall, Blacksburg, Virginia 24061-0316
(703) 231-5688 Fax: (703) 231-5097

DEC 2 1 1994

Dec. 18, 1994

Fred E. Foldvary
709 Circle Drive
Blacksburg, VA 24060
703/231-7707

Dr. Mary M. Cleveland

Dear Polly,

Thanks for your greetings and letter of Dec. 13.

In your letter of Dec. 13, you asked who's the government as RCs land on the island. The RCs after the first one are allowing RC#1 to sell land, so they are granting him a gift of authority and ownership. But in a different culture, the new arrivals would realize they jointly have more power than RC#1 and that RC#1 has a shaky claim to the land, as you note, so they would then refuse to buy land, and just take it. This is a free market, as you note, but only because the later arrivals have freely granted the first RC a gift of land. They voluntarily give up their share of the rent. A different culture would have a different free market, in which the later arrivals claim an equal share of the land value, with a different outcome. Of course in today's world, governments enforce land titles, but in your RC example, it is not clear why the newcomers would submit to RC#1 unless he had superior weapons. The government in Cocoville is created either by the agreement of the RCs, or by superior power, so why should they agree that RC#1 has title, other than from cultural habit or RC#1s superior power? So to your model, add (1) culture and (2) power.

I don't think this has any relationship to wildcat bankers. The U.S never had free-market banking. Before the Civil War, the banks were regulated tightly by the states, and this included a prohibition of branch banking in many states and the forced purchase of state bonds by the banks. With branch banking allowed, there would have been much fewer independent rural banks, and without the forced subsidy of state bonds, the system would have been more stable. See George Selgin's "Theory of Free Banking" or Lawrence White's book on free banking in Scotland for the scoop on real free banking.

I'll be in New York City March 17-19 for the Eastern Economic Association, including my panel on "Comparative Economic Theory." Will you be attending?

Happy New Year!

Fred

Dr. Mary M. Cleveland
14 West 68th Street, Apt 4
New York, NY 10023
(212) 873-2982
FAX (212) 873-6125

Monday, Dec. 19, 1994

M. Mason Gaffney
PO Box 7998
Riverside, CA 92513-7998

RE: Schalkenbach, banking

Dear Mason,

Report from the Schalkenbach front. I've enclosed report from Bob Gilmour's investment subsidiary, and stuff distributed by Oscar, including a long and rather interesting report by Mike Hudson. Investments are doing relatively well, following Bob's "Dow Dogs" strategy: collect blue-ribbon stocks with low PE ratios. He says in practice, most of these leave the Dow dogs because stock value rises, rather than because dividends are cut. In any case, earnings are up 20%, prompting Oscar or Lowell (I forget which) to complain that this causes a problem of finding how to spend the money. Oscar reported that Fred Harrison is going under, positively smacking his lips, "That's what you get when you invade capital!" He's really pathetic, frightened, defensive, in over his head and knows it. The committee to investigate the future met, the second time already, following the luncheon.

Some glimmers of intelligence on the Schalkenbach board. Gilmour & others were discussion privatization of land in Estonia, which so far consists of returning land if possible to the squabbling heirs of the original owners. Roy Foulke kept insisting, "What do you mean by privatization? Land to the tillers or land to the feudal landlords..?" Etc. He seemed to appreciate the importance of relatively equal distribution of wealth. Dick Noyes has an interesting scheme for sneaking LVT into New Hampshire to finance state social programs. In fact the only real dim bulb on the board seems to be Bill Davidson, who smoked and dozed his way through the meeting.

I found your notes on banking a little hard to follow, but will check the references you gave me. Business cycles, banking, etc was stuff I had put off trying to understand until I thought I had the rest of the system figured out. But your Great Barrington paper got me interested, so now I'm suddenly picking up bits of information and ideas all over the place. Plus I think I can plausibly model the adventures of RC.

However, my #2 project at the moment (#1 is Xmas & New Year's) is to upgrade the references in my semi-popular paper on "Equality, Productivity and Growth" and get

the thing published. The *Business Week* piece gave me several good new leads. There's a guy called Perotti at Columbia working on the equality question. And I have some quotes from Newt Gingerich that make a great springboard, such as:

> "It is impossible to take the Great Society structure of bureaucracy, the redistributionist model of how wealth is acquired and the counter-culture values that now permeate how we deal with the poor, and have any hope of fixing things...They are a disaster. They have ruined the poor. They create a culture of poverty and a culture of violence. They have to be replaced thoroughly...we have to simply, calmly, methodically reassert American civilization."
> *New York Times*, Nov 12, 1994, p. B3.

New opportunity: Last night I ran into the Chief of Staff for our Congressman Jerry Nadler, Neil Goldstein. He was the Sierra Club Washington rep in the '70's and knows many of the same people we do. I told him how equality is a hot new topic in economics. Turns out Nadler's putting on a conference in April; Goldstein got very excited--a perfect subject for his conference!

Happy New Year! Again!

Love,

JAN 0 6 1995

Mason Gaffney
P.O. Box 7998
Riverside, CA 92513

909/687-1677
OFF 909/787-5037, x1574
FAX 909/787-5685

24 Dec 94

Polly Cleveland
14 W. 68th St.
New York, N.Y. 10023

Dear Polly:

So there is a "chicken-and-eggishness" (wonderful expression!) about my statement that capital shortage is manifested in inadequacy of investing in payrolls. Modern, spending-oriented macro makes everything chicken-and-eggish. The existence of positive feedback loops, real or imagined, makes c&e-ishness. Here are some firmer guidelines.

1, overcommitment of capital to long forms has to cause relative shortness of capital in short, readily usable forms. This has to cause a lesser flow of CCAs. This has to cause a lesser flow of payrolls. The only way to prevent same is with funny money, which leads to inflation.

2, a sure indicator of capital shortage is a fall of land prices (and stock prices). This is complicated (so is everything) by noise in the system. It is complicated by reenforcing expectations (very chicken-and-eggish) that magnify any movement, once exogenously caused. However, land values are reliable guides to real, long-term interest rates. They do not depend on those transactions that are recorded, but apply to all land prices.

Merry Christmas

M.

cc: Fred Foldvary

DEC 27 1994

The Geo-Economics Society

Fred Foldvary, coordinator
Dept. of Economics
Virginia Tech
Blacksburg, VA 24061
Tel. 703/231-7707, fax 231-5097
e-mail: foldvary@vt.edu

Dear Prospective Member:

The Geo-Economics Society is now a reality!

On October 22, 1994, the temporary executive committee agreed to the enclosed draft of a "Statement of Purpose" and "Objectives."

We now invite you to join this new scholarly society. Full membership in the Geo-economics Society requires a master's or doctoral degree in a social science, as well as a publication (which can be a master's thesis or doctoral dissertation) that contributes to geo-economics, within the most recent five years. Others who are interested in geo-economics are welcome to join as non-voting associate members. Annual dues for either class of membership is $20. Your suggestions are welcomed.

I agree with the tenets of geo-economics, and would like to join the Geo-Economics Society. I have enclosed a $20 check payable to the "Geo-Economics Society" and (for full membership) a copy or reference to my publication on geo-economics.

Name: (circle one: Dr., Prof., Mr., Ms.)

_____

Affiliation (e.g. department & university):

_____

Address: _____

_____

Telephone: _____ Fax _____

Internet address: _____

Comments:

_____

The Geo-Economics Society

Statement of Purpose

Geo-economics emphasizes the special properties of scarce natural opportunities, particularly land, natural resources, the electro-magnetic spectrum, and the effluent-absorbing capacity of oceans and the atmosphere. The availability of these opportunities without human effort makes it possible for societies to use them as sources of public revenue without discouraging economic activity. Geo-economics employs the premise that scarce natural opportunities ought to be regarded as the common heritage of humanity.

Individuals are entitled to the full product of their peaceful and honest efforts, insights, and savings, and to the choice of how that product is spent, including the choice to live in communities where individual resources are shared. Community collection of land rent combined with the abolition of taxes on enterprise induces the most efficient use of resources. Geo-economic policies promote environmental well-being, prosperity, and social harmony.

The objectives of the Geo-economics Society are:

1. Promoting and facilitating the publication of geo-economic literature.
2. Promoting communication and collaboration among geo-economic scholars.
3. The development of geo-economic theory.
4. A fuller integration of geo-economics into mainstream economic texts and thought.
5. The inclusion of geo-economics into policy debates.
6. Support for graduate students who are interested in geo-economics.

The means by which we plan to pursue these objective are:

1. Raising funds.
2. Persuading economists to become members of the Geo-Economic Society.
3. Circulating bibliographies of geo-economic literature.
4. Circulating a geo-economic bulletin on paper and e-mail.
5. Organizing conferences and sessions of scholarly organizations.
6. Reaching out to groups with allied interests, such as environmentalists.

Questions for Geo-Economic Research

suggested by Nicolaus Tideman

1. With what accuracy can land be assessed?

2. What is the potential yield of a tax* on land value, and how does that potential yield vary with the levels of other taxes?

3. What is the best way to use taxes on land to finance multiple levels of government, or, to put the same question differently, how should the potential yield of a land tax be allocated among levels of government?

4. To what extent are urban problems caused by land speculation, and what is the impact, theoretically and empirically, of land taxation on land speculation?

5. How does the idea of making the rent of land and other natural opportunities the primary source of public revenue fit with modern theories of social justice?

6. What would be the impact on poverty of shifting from the current tax system to one that made the rent of land and other natural opportunities the primary source of public revenue?

7. How would the idea that land is the common heritage of all humanity promote world peace, including the resolution of ethnic conflict within nations?

8. What compensation, if any, should be provided to those whose land titles lose value when the source of public revenue is shifted from productive activities to land?

9. To what extent is the private appropriation of rent a cause of business cycles and bank failures?

10. How does the idea of taxing land connect with the existing literature on optimal taxation?

11. What reasons do economists give for finding taxes on land unattractive?

12. How would one modify the administration of a land tax to accommodate the objection that a land tax can harm those who have physical or emotional investments in land uses that are less financially lucrative than the uses that yield the highest bids for land, and are there adequate reasons for accommodating this objection?

* Public collection of land rent is referred to here as a "tax" because it has the form of a tax, but differs from other taxes both in its moral foundations and in its incentive effects.

Mason Gaffney
P.O. Box 7998
Riverside, CA 92513

909/687-1677
OFF 909/787-5037, x1574
FAX 909/787-5685

29 Dec 94

Carl Shaw
HC65, Box 148
Mt. Zion, WV 26151

Dear Carl:

Thanks for sending copy of letter from Gary S. Becker. What do I make of it? It is airheaded and inane. It serves to show how careerism and the Chicago School environment can warp the mind even of a Nobel Laureate - indeed, such warping contributes to becoming a Laureate, considering that the judges' minds are similarly warped.

It also shows the error of some Georgists who make much of a few crumbs thrown our way by people with name recognition. We have to get away from that mindset; understand that we Georgists must make our own way, not look for miracles of conversion from people who have won fame by learning to tune out our truths. They may humor us a little to get a fat speaking fee, but they'll deny us as Becker did when put to the test. "With friends like these ... "

I am taking the liberty of sending out a few copies of this infamous letter.

Fraternally,

cc: Richard Noyes
Lindy Davies
Polly Cleveland
Fred Harrison
Ed Dodson

JAN 0 6 1995

Seasons' Greetings, turn of the year, 1994-95

OK, I admit it, this was written for my 50th Reunion, Harvard Class of 1945. Hope you will find it an amusing way to catch up on the Gaffneys on or around winter solstice - Christmas 1994, and New Year's Day, 1995 (5 more years to the *Third Millenium!* - hang in there, fellow old-timers).

Poor old Faust had to sell his soul to enjoy life after retirement. It's worked out better for me. The Federal law against age discrimination originally exempted professors with tenure, so we could be terminated at 65. It did cover those reaching retirement age after Jan. 1, 1994, but that was 5 years and 2 months too late for me. Then the U. of Cal. extended its retirement age to 70 - still two months short for me. Then U.C. interpreted "retirement age" as coming on the July 1 following age 70! I just made the boat! Whew -- Somebody up there must like what I'm doing. Now, if California can just avoid bankruptcy .... I could tell them how to do that, too, but so far they'd rather plead poverty and go begging to Washington.

I've treated my Tish better than Faust did Marguerite, and I like how she treats me, too, so we are still in love and will remain so. That's the core of good feeling, everything else is incidental. We've had a couple of great family reunions here with all six kids together, Tish, plus ex-wife Estelle, all under one roof for two days. How many wives could handle that? That's the kind of lady she is. She's always loved the first brood like her own. They reciprocate, visit us often, and act like older siblings to the younger ones. The tragedy of divorce has been turned into a big, happy family, thanks to her.

My greatest adventure concerned pigs. An old barn came with the place and I didn't like to see it wasting. A young 4-H fellow, a friend's grandson, talked me into buying two sows that he would care for, and we would share the litters. That was my first mistake. He got a new girlfriend who had other notions, and they left me with the lot. "Harvard men don't do pigs," you may sniff, but harken: my brother Matt (Harvard '43) reports from England it is quite fashionable (under some euphemism) among members of the House of Lords.

I drove a barren sow out to get "serviced": that's how it all began. I got her to the church on time, but the next day the farmer called testily and said "Your sow's already pregnant, get your butt out here and take her back before she farrows!" I rented a trailer with high sides and picked her up. I drove slo-o-owly back to the freeway on the bumpy roads, considering her delicate condition, and she looked OK, except she wouldn't lie down. I headed down the smooth freeway with a sense of relief when, glancing back, I saw her hams and tail disappear over the

tailgate! I visualized gore and carnage. Bracing myself, I pulled over to warn traffic not to hit the 600# carcass, but when I started back, there she was trotting calmly along the #2 lane of a six-lane divided highway, the main line between San Diego and Riverside. She had slid along right on her full nipples, and was only scratched. Marilyn Monroe or Jayne Mansfield might not have taken it so well; pigskin is tough!

Yeah, I was dumb, no argument there, but what to do? First I was irked: this would interrupt my Sunday. Then I was chagrined: this was embarrassing. That took two, maybe three seconds, when reality kicked in and I was just a s-c-a-r-e-d child! You think you're a solid citizen, in control of your life, treated with courtesy and respect, when Pow! You're down on a level with roadkill. Suddenly to be helpless and alone and ridiculous and contemptible and expendible and without recourse, it's a catharsis. The good news is, traffic was light on Sunday morning. The bad news, well, have you ever tried to lead or drive a 600# sow? They are <u>big</u>; they are unwieldy; they have their own ideas; they personify inertia, either static or kinetic, depending. You pull them by the ears, then by the tail, but they don't move until they want, nor stop until they want. It doesn't get any easier with 18-wheelers roaring by. Pregnancy and scoured belly did not improve her docility: she was a true road-hog. I wished I were elsewhere, I wished for mother, but there we were, just me and the pig-headed sow and the 18-wheelers. Lordy, Lordy, I should have gone to church.

The sow headed for the median strip and I herded her there for respite. My relief was brief when I realized she wouldn't stand still, and she and I must now cross three full lanes of high-speed traffic. I waved down traffic to stop, but it didn't. I prayed for a black and white, but none came. Suddenly there was a break in the traffic and I pushed her onto the #1 lane. I have no firm recall of how I got her across from there. I remember stopping cars and trucks - they were impressed by her bulk, as was I. I remember pleading with irate drivers, apologizing to some and cursing back at others. I remember abusing her terribly with a stick to make her move. I just knew one thing then, if I could get her to the other side and down the bank I could keep her from climbing back up.

We must have made it, for here I am. At the bottom of the bank was a strong fence, so now we were trapped between it and the bank. I looked up and there, at last, was a highway patrolman, all natty and clean. "Hey, you," says he, "You're violating Code Section ....., etc., get that animal off the road!" "Thanks, officer, I wonder if you could get me some help?" He gets on his blower, and soon there is another black and white, and another, and soon there are seven - count 'em, seven. They group together, boots all shiny, and have a party: *they're <u>laughing</u> at me.* Would they call my friend, who could

bail me out? "Against regs": thanks a lot, fellows. Except I hear one say, "Look at those fangs, I'm not going down there." OK, they have their own dangers to face, why should they borrow mine? How were city boys to know sows won't attack unless you mess with their young? Still, I was not impressed by the courage or devotion in the thin blue line.

In this season here it suddenly gets hot (like 90 degrees) around 10 AM. Swine don't sweat, in the heat they need water to survive - that's why they wallow and root with their snouts, where the cooling warts are. So now I must get her to water, fast. At this point the Good Lord raised his hand and ordered Stop! My servant has suffered enough. A half mile up the road I saw a man standing, watching, on the other side of the stout freeway fence. Even at that distance, he looked more human than an Officer of the Law. Maybe he would stick a hose through for us, and call for help? It took a good hour to get the sow that far. Half that time was spent forcing her out of a culvert where she went for shade, and would have died of thirst. However, as we got there, mirabile dictu!, there was a hole in the fence. Some vehicle had run through it a month ago. Through it we went, too, and The Man With The Hose made us a nice wallow: saved!

His wife wouldn't let me use the phone - I must have looked like the original Man with the Hoe - but called Tish, who called my friend, who came with a proper - i.e. covered - trailer. The sow farrowed that night and we had 7 or so gilts, which she nursed with those very same bruised, cut nipples on which she had skidded along I-215. I sold my friend the sow - enough's enough - and he named her "Freeway." She farrowed twice more before mandatory retirement.

The moral? Don't take up farming for your health, as I did. Manual labor is hazardous. I fell out of a tree I was pruning and broke two ribs; I sliced my foot from toe to heel when a circular blade flew off a weed cutter; I threw out my back lifting a tiller into a pickup; I could have killed myself and several drivers with that sow on the freeway. When I think what might have been, I vow to cultivate Prudence. Being so accident-prone, how have I survived to 70? Remember, there's a reason for workmens' comp! "So be warned of my lot (which I know you will not) and learn about farming from me."

By the time you read this I hope my new book on The Corruption of Economics will have shocked and shaken my colleagues, and they will at least be denouncing it (which of course is better than ignoring it). If it's the latter, however, the worst that can happen is I'll continue to be like Wordsworth's lass who lived among the untrodden ways beside the springs of Dove, she whom there were none to praise and very few to love. Those few will comfort my declining years nicely, however, and I'll trade fame for peace, if that is Kismet. I

really would, however, prefer to strike an effective blow for the good society before I hang it up. Reforming what passes for the "discipline" of economics is what I could contribute, God willing. "The impossible dream" is not for the young alone; perhaps it's what keeps one young. Even if it's only windmills one smites, still "This man is freed from servile bands of hope to rise, or fear to fall; Lord of himself, though not of lands; and having nothing, yet hath all."

Harvard, I am happy to report, is not criticized in The Corruption of Economics. That was not due to bias, although I am as loyal as a proper devotion to Veritas allows, and a shade moreso when there are judgement calls. The fact is, Harvard was clean (although not heroic) in the period I covered (1880-1930). The dirty work was done at Columbia, Hopkins, Cornell, Pennsylvania, Chicago, Yale, Northwestern, Berkeley, Stanford, and perhaps MIT. They have a lot to answer for, if they ever have to answer for anything. The problem with universities, as with corporations, is they have neither bodies to kick, nor souls to damn. Dartmouth College v. Woodward (1819) pretty well settled that.

Tish did so well teaching Spanish part-time they asked her to take the fifth grade full time. She gives it her all, her students adore her, and she really uplifts them. It's a labor of love and conscience, she doesn't get paid half enough for her pains, and not a quarter enough for her productivity. Tads are responsive to the skillful, loving hand. A few years more, and it's too late. Our reward system is backwards. It tells people it is more productive to teach older students. Really, we should pay grade-school teachers more, they're the ones who bend the twigs. By the time they get to college the young are already bent - mostly out of shape. Think about it.

Putting this second batch of three kids through college is tougher than we expected. Tuition keeps rising while my salary is frozen. We used to joke about "motherhood" being sacred in politics, but times have done a "one-eighty" on this matter, and it's no joke for parents. Some of you, well past the parenting years, see this now just as retired property owners, and may shrug it off. You've paid your dues, you think. School taxes are just for parents, right? Let them pay tuition. Next time you read about an urban riot, murder, or mugging, please think it out again. Are all children born with equal rights, or are they not? Is a bastard rescued from a dumpster one of those people Jefferson said were all created equal, or not? We have to face this one: are we one big national family, or not? A lot of things ride on your answer.

Our children are all doing well, thank you, but they cherish their privacy so I'll go light on details. Brad, 40, is now a computer programmer. He worked for some years at "JPL" (Jet

Propulsion Laboratory) in Pasadena, but now has gone into the business. Before JPL he was a chemical engineer, specializing in environmental protection for oil refineries. Our children were born into a new world where one has to change trades a lot, in shifting markets. May the gods of commerce shine a light for them.

My daughter the lawyer, Ann, does real estate deals in San Francisco, anticipating all contingencies, keeping people out of court. She is especially good at keeping secrets, so I have few particulars. One secret not kept, however, is my first grandchild, Meredith Ann Shores, born August 20, 1994. I flew north to check her out this week, and she is a definite #10, A-OK. She came a bit earlier than forecasted, when poor Ann was in the middle of a case, so her first picture shows her on a desk top with her tired mother pecking at a keyboard. Shades of Olan, in *The Good Earth*! It took a day or two to get another partner on the case, but they all survived.

Three years earlier, Ann and her spouse made the papers by crossing the High Sierra in April, camping in the snow. Others had done so before, but Ann is the first to contract pulmonary edema at 12,000'. They descended to 11,500', where she could breathe, but couldn't escape without returning to 12,000' where she couldn't. So she camped alone in the snow for two nights while spouse Tom soloed back in record time to Independence or Lone Pine (one of those jumping-off places in the Owens Valley) where he got a rescue crew to helicopter in and fly her out.

Dad, of course, was the last to know, so didn't have to worry except in retrospect, which was bad enough. He suggested a grandchild be produced before any more such foolishness. He was rebuked for so presuming, and has learned to bite his tongue, but is more than routinely delighted to have Meredith Ann now. With six kids, doesn't a man deserve at least one grandchild?

It was about 12 years ago that Stuart announced he is gay, and a couple of years earlier that I had figured it out. I went through the classic phases: denial, guilt and remorse, lecturing, exhorting, "reasoning together," explaining survival values, retracing childhood influences, looking for a reconversion ... whatever I said, he had heard it all before and had twenty answers. After a while it came down to take it or leave it; naturally I took it. He is the same delightful kid he always was, bright, witty, insightful, warm and loyal. He is, interestingly, the most family-oriented of us all, binding us all with frequent visits, letters and calls.

He has formed a stable relationship with John Lewis, a lawyer from Stanford, whom we have grown to love dearly, too. John is multi-talented, a great pianist, urbane

conversationalist, and a fantastic ping-pong player: almost beats me sometimes, if you can believe it.

Stuart's short video *Virus* recently won the award for Best Experimental Video at the Utah Short Film and Video Festival. *Virus* will screen this fall at the Mill Valley Film Festival and at the Film Arts Film Festival, and will appear on public TV, early 1995. It's about how to face death: not that he is, but he's seen a lot of it.

Laura, a junior at U.C. Irvine, has wonderful stage presence and a glorious soprano. I'm also allowed to report she has played two Ann-Margret roles, only better: Kim McAfee in Bye-bye Birdy, and the adulterous mother in Tommy. My dad would have loved her so: he was a ham with a glorious voice, too, and Ann-Margret, and many other notables, learned their craft in an auditorium named after him at New Trier H.S., Winnetka.

Patty is class salutatorian and Queen of the Senior Prom! She's so boy-sane and studious, like her grandmother Laura, the latter came as a surprise, well-deserved though it is based on looks.

Little Matt got his Varsity Letter for tennis while still a freshman, and a short one at that. He's crafty, and fast as Michael Chang. I can still give him a game on those rare days when I'm in "mid-season form." This, too, shall pass, but meantime there is no greater pleasure than playing your favorite game with your own son, growing up clean and true. Soon I'll just watch and cheer, but that's a thrill, too. We've left a lot of "human capital." You can't spend it, but it's the best.

Bless you all, it's a privilege to be included in your group, Wandersmann though I have been. Knowing you is a great capital, too.