

Review of Phillip J. Anderson, 2008, *The Secret Life of Real Estate* (London: Shephard-Walwyn (Publishers) Ltd.)

Review by Mason Gaffney, May 2009

This is an exciting, important and timely work; it will sell well. Anderson has ferreted out and marshaled dozens of sources on the 18-year cycle of boom and bust in real estate, its history, its mechanics, and its dynamics. Some sources are old and neglected; some are current and neglected; but after Anderson it will be hard for macro-economists to continue neglecting them. He melds the dramatic skills of a raconteur with the industry of a scholar and the discipline of a field marshal, to keep readers wide awake while they follow and most likely accept Anderson's take on economic history.

One test of an hypothesis is prediction. Anderson accepts that challenge, even providing us with a "clock" to let us know where we are in the cycle. His theme is "Understanding the Past to Predict the Future". After guiding us through many 18-year cycles, from 1800 to date, he sums up with a chapter disarmingly titled, "Knowledge we Gained along the Way". Here are some major findings.

1. The prices of land peak before other measures do, i.e. it is a leading indicator. Construction peaks after land prices do, but before recession hits, where "recession" is measured in GDP and other familiar metrics used by the NBER.
2. Few people study history, so few under about 42 even know there is a land cycle. All they know is their own recent experience, so in the heat of a land boom, lasting several years, they easily fall prey to projecting the boom indefinitely forwards. Few leading "mainstream" experts forecast crashes, even as they are beginning to happen; quite a few deny them even as they turn catastrophic. Anderson names names, including Ben Bernanke's, and most of us could add more.
3. Bank credit swells and shrinks in synch with the land cycle. The two interact in a positive feedback process: swelling bank credit raises land prices; buyers need more credit to purchase the land; the appreciated land then serves as collateral for more bank loans, and so on.
4. Banks are highly vulnerable to downturns because they borrow short to lend long. In the heat of a land boom they carry inadequate capital reserves to cover the 18-year crash, even though that is, to Anderson, predictable.

Insuring deposits, and bailing out failed banks, creates moral hazard that leads to repeated excesses.

5. Economists recently have programmed their computers not to predict a downturn of more than 25% of the standard deviation (a "black swan" moment). This is only the modern manifestation of a group delusion that has marked every boom in history, a cautious tuning-out of extremes. (This propensity is also manifested in their choice of statistical measures: medians instead of means; standard deviations instead of mean deviations, for example.)
6. Several credit crunches and minor disasters occur before a major tsunami hits. It takes a real estate cycle to generate the proverbial "9th wave". There is usually at least one mid-cycle slowdown from which we recover nicely. Most economists are conditioned to blank out land prices from their analyses, so their histories fail to distinguish major from minor cycles. Accordingly, they (e.g. the NBER) jumble them together indiscriminately, and so miss the 18-year cycle of land prices. Anderson finds, on the contrary, that "land value is the key to forecasting".
7. Anderson gives us dates. There were land-price troughs starting in 1955, 1973, 1991, followed by slow recovery with a "hockey-stick" boom at the end. Accordingly the next trough is due in 2009. Going back to 1800 he gives us peaks: 1819, 1836, 1857, 1873, 1893. The peak of 1911 is curiously muted, and 1926 came a little ahead of schedule, even though one could pick 1929. World War II understandably upset the schedule, which picks up again, however, after the Korean War, from a trough in 1955.
8. The system of government-granted licenses (privatization) is spreading. Privatization is the precondition for trading in and monetizing land titles, which creates the land cycle. He mentions The World Bank making its loans conditional on privatization, and no-bid military contracts, but might have added items closer to home: fishery licenses, pollution permits, spectrum assignments, aircraft slots, water-pumping permits, mining and drilling leases, preferential zoning, subsidies to water licensees, and a host of evolving forms of private privileges.
9. Some reliable indicators of a forthcoming peak are: A, unusually high land prices and price/rent ratios; B, a rash of extra-tall buildings; C, a boom in copper prices; and D, an inverted yield curve.

The NBER cycle-dating committee, led by Robert Hall of the Hoover Institution, did not announce the downturn of December 2007 until 11 months after the fact! That was said to make it

"official". Actually, the NBER is private. Calling it "official" displays an authoritarian cast of mind within the economics profession. Choosing a Hoover Fellow to make the "official" calls betrays an unhealthy dependence on far-right think tanks, whose forecasting record is dismal.

And yet, the "Secret life" of real estate is not really so secret. Anderson has found it from secondary sources, which he simply marshals. What's secret is why this open secret is closed to our most prominent macro-economists. One reason is they choose to ignore economic history, as shown by their rooting it out of their required curricula, replacing it with courses in abstruse theory and econometric techniques that mark modern "mainstream" writers and journals. "...the institutions that teach American elites to think about the modern world are unconcerned with teaching them to look at it" (Ada Louise Huxtable).

Another reason is that they disdain the study of land values and other privileges, lowball their values, and avoid integrating them into their models and hypotheses. This is partly from an overreaction to the historical Henry George, who put land values at the core of his analyses, and bitterly condemned academicians for not following his lead. Being both an intellect and a political force he stirred up throngs of disciples, some of them unlearned and crass, to make of this feud a tradition. That seems too petty, however, to explain such systematic dismissal of the obvious role of land. The greater and enduring reason is probably the defensiveness of rentiers against any challenge to their rents and unearned increments. This has led them to found and fund leading universities, and more recently think-tanks, and to pack the boards of public universities with regents supportive of their views. "Governors of universities fall into their natural place behind the golden calf, bearing shovels" (Tom Beer). Critics label this as "deep lobbying", and it now dominates the intellectual and media worlds.

Another reason is the overemphasis on manipulating data as opposed to gathering and evaluating raw data itself. "Give us data to chew, and we will chew" is the prevailing attitude, even when the data is garbage and the output night soil. There is little work on the quality or relevance of the data, and that little comes from the fringes of the profession without penetrating the core, as engraved in the stone of dozens of new and ongoing textbooks. Few heed Jonas Salk's saying, "I get into a dialogue with nature and put the question to nature, not to my colleagues, because that's whence the answer must come."

On the negative side, "The Secret Life" falls short of being the classic it might be because of Anderson's haste. This is understandable, considering the timeliness of his thesis, but he leaves many loose ends to trouble a critical reader. Worse, they provide fuel for captious critics, who are sure to materialize with arson in mind.

Anderson is an investment counselor and popular speaker, like one of his favorite sources, Roy Wenzlick. Anderson has stitched together many newsletters written over many years, aimed at clients looking for investment counsel, leaving two things unclear. For one, it is not evident whether he is addressing public policy or advising speculators when to buy or sell. His major social value judgment, which appears often, is so drastic, and so vaguely specified, it does not amount to a specific workable idea. He blames private land tenure, which he calls "enclosure", for the boom/bust cycle. One assumes his investment clients filter that out, while appreciating his prescient forecasting. Those seeking a guide to public policy, however, will wish he had attended more to it. He does draw heavily on Georgist sources, especially Fred Harrison, George Miller, and Fred Foldvary, so one could infer that he favors the Georgist policy of taxing land heavily, with the corollary of reassessing it often, to abort incipient booms of irrational exuberance. Or he might favor leasing, which he mentions once, except there he leaves us hanging with "but that's another story".

Secondly, it is often unclear to what year his present tenses refer. The originals, he writes, came from client newsletters he sent out 1998-2004. Some of them read that way. However the book is copyrighted 2008, with some additions up to about 2007, again using present tenses. Worse yet, he "signed off" on the book Sept. 7, 2008. This is curious since the book says nothing about the great crash of 2008, except to claim it as a forecast made earlier. This is probably the result of haste, but seems a little unfair.

He uses too many long quotations. For example, Chapter 2 on the peak of 1818 is built around 9 such long quotes from Murray Rothbard, along with several from other authors. A reader wonders if he is not reading Rothbard's work with filler by Anderson. At the same time, Anderson shows no signs of being a doctrinaire Rothbardian: he quotes J.K. Galbraith as often as he does Rothbard, and draws on an eclectic range of historians including R.C.O. Matthews, Alfred Chandler, Aaron Sakolski, Roy Robbins, H.D. Simpson, Paul Johnson, Clarence Long, Reginald

McGrane, Harriet Martineau, John Steele Gordon, Charles Kindleberger, A.H. Cole, and many others. He has read widely, without an ideological filter.

The coverage is extensive, but the scholarship leaves something to be desired. Some older sources he omitted are Carter Goodrich, Homer Vanderblue, Lewis Maverick, Ernest Fisher, Harry Scherman, Philip Cornick, Alexander Field, and others. On the other hand, to his credit, he has exhumed the neglected research of Roy Wenzlick. Scholars have undervalued Wenzlick because he was, like Anderson, something of a showman and promoter of his consulting business. Like Anderson, he took his material on lecture tours with dramatic display tools, and catered to the self-interest of clients. Yet he, too, discovered the 18-year cycle, and left a trove of research materials, which Anderson has studied, at the University of Missouri, St. Louis.

The more serious omission is the current work of Robert Shiller, Karl Case, Nouriel Roubini, Bryan Kavanagh, Michael Hudson, Piet Eichholtz, Anne Goldgar, Eitrheim and Erlandsen, and others, not to mention the foolhardy optimism of Bernanke, Lereah, Mandel, Greenspan, and other false prophets. It seems that Anderson's extensive reading stopped around 2006. Thus he cites Foldvary's 1997 work, but omits his timely 2007 forecast, *The Depression of 2008*.

On the nitpicking side, Anderson cites several long quotes only to virtual sources, without naming the authors. I searched for one on banking at www.college.hmco.com/history, and found only ads for what look like high school texts, with nothing on banking, and no clue as to whom he is citing. This and other signs of impatience with sourcing need correcting in a sequel or second edition.

He does a good job of hitting the high spots of major land cycles after 1800, along with many vignettes to keep the work readable and entertaining. As much as he may digress, however, he keeps his eyes on the main chance. He marshals all his material to illustrate and confirm his basic thesis about the key role of land pricing in the 18-year cycle. His randomness optimally tempers his single-mindedness.

At one point he calls 1818 the "first" U.S. economic downturn (p.57). Worse than the dating error is the bizarre reason Anderson advances for it, an alleged Federal land monopoly that converted what had been a commons into taboo territory. That is

simply bad history, so bad that Anderson himself later ignores it. Elsewhere he makes out 1792 to have been a major crash.

We can overlook the contradiction as a product of haste. More seriously, though, he omits the major crash of 1798. This is odd, in a work based on the thesis of an 18-year cycle. 1798 is tolerably close to 1818 less 18, but 1792 is not. The crash of 1792 was real enough, but was simply the mid-cycle downturn that Anderson has noted in other 18-year cycles. England's banks survived, and her internal improvements moved ahead. The American crash was abated by application of the cotton gin and expansion of the slave economy of the south. These events in America broke the last bottleneck to applying Arkwright's inventions of 1769-70 to allow the explosive growth of England's cotton industry in Lancashire, archetype of the industrial revolution. Slater's Mill of 1793 in Rhode Island helped bring the industrial revolution to the new world.

As to 1798, though, it was 1797 when the B of E suspended cash payments; when Pitt imposed the first income tax to raise funds to fight Napoleon; when English capital was diverted on a grand scale from America to subsidizing Napoleon's enemies; when Robert Morris, financier of the American Revolution, lost 200,000 acres and went to debtor's prison; when Andrew Jackson lost his lands and conceived his hatred of banks; ... this was a major crash, and the likely reason John Adams' lasted only one term, Hamilton lost favor, and Jefferson became President.

It would be an error to think that economic history began in 1800 or 1798. There were capitalism, land tenure, banking, and boom/bust cycles - all the elements that Anderson analyzes so well from 1800 to date, that one can trace back for centuries: the Mississippi Bubble of 1720; the Tulip Bubble of the 1630's, which Eichholtz and Shiller showed to have been a land bubble; the end of the Great Migration to New England after 1630; the Florentine and Medici banking collapse of 1494; and so on. M.E. Levasseur has traced such cycles back to the year 1200.

Whatever its minor faults, Anderson's *Secret History* is a book to study, remember, and steer by. It reminds me of a German barber I once patronized. However I squirmed to defer the next trim he would repeat compulsively, *vierzehn Tagen, vierzehn Tagen!* Anderson's readers will learn to repeat, *achtzehn Jahren, achtzehn Jahren!* Whoever wins the Presidential election of 2024, Be Prepared! This future President would also be well advised to select economists who, like Hudson, Harrison, Foldvary, Kavanagh, Shiller, Roubini, and Anderson, foresaw the

Great Crash of 2008, rather than insiders like Romer and Bernanke who foresaw only a "Great Moderation" because we had, so they said, "conquered the business cycle".