UNDERSTANDING TODAY'S ECONOMY

Student's Workbook

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UNDERSTANDING TODAY'S ECONOMY

THE PURPOSE OF THIS SEMINAR: To give an introduction to the concepts of economics first developed by the Classical Economists Smith, Ricardo and Mill, and the remedy for the perennial problems of poverty, maldistribution, and economic stagnation. The classical economists defined political economy (or economics) as the study of the production and distribution of wealth in society. Henry George's remedy focuses on the effects of land and taxation on the efficiency of production, and the distribution of wealth.

THE BASIC QUESTION: Why is there such great disparity between wealth and poverty - a gulf that always seems to widen as inventions and societal advances make it easier to produce the things we need?

OVERVIEW: To present fundamental economic principles which may explain the persistence of poverty and many other problems.

DEFINING THE TERMS

Economic analysis depends upon understanding relationships of things and their effects on each other. We can't do that without clear and unambiguous definitions of the things we are talking about.

Many of the terms used in this seminar are words that we use in our everyday speech - but that have a different meaning to economists. Since we are going to use those words, today, as economists, we should agree on their meanings. So, let's look at some of these words and seek their economic definitions as opposed to their common meanings, and then analyze the relationships among the terms.

WEALTH

Wealth, to an economist, has **all four** of the following characteristics:

1. It is produced by labor.
2. It satisfies human desires.
3. It is material and tangible.
4. It has exchange value.

PRODUCTION: The creation of wealth. More precisely: Whenever human labor changes matter in form or in place so as to satisfy human desires, wealth is produced.

DISTRIBUTION: The division of wealth among the factors which produced it. In other words, Who gets the wealth that is produced.

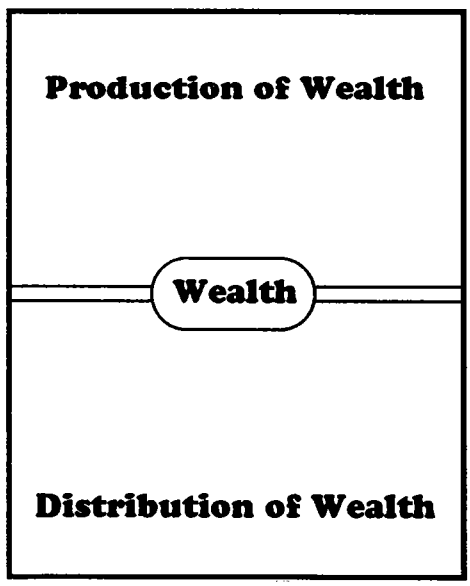


Figure 1

THERE ARE THREE FACTORS IN THE PRODUCTION OF WEALTH:

LAND: The whole material universe except for people and their products. This means that a school of fish in the ocean is land, a wild (uncultivated) tree is land, a river is land, and the air is land. Land is necessary for all production.

LABOR: Human effort, both physical and mental, used to produce wealth.

CAPITAL: Wealth that is used to produce more wealth. Capital is the tools that we use in production: a shovel, a computer, a delivery truck, a baking pan, a bull dozer. Capital is also wealth that is in the course of exchange, such as a loaf of bread on a grocer's shelf.

Project #1

THE FACTORS OF PRODUCTION

Below is list of items. Classify each term as LAND, LABOR or CAPITAL

computer	hammer	wild flowers
salesperson	taxicab	wild deer
teacher	iron ore	vacant lot
manager	cornfield	desk
fertilizer	cow	typewriter
river	CEO	foreman

LAND	LABOR	CAPITAL
_____	_____	_____
_____	_____	_____
_____	_____	_____
_____	_____	_____
_____	_____	_____
_____	_____	_____

Distribution: Wealth is distributed to each of the factors of production in compensation for that factor's role in production. Since there are three factors of production, there are three categories of distribution:

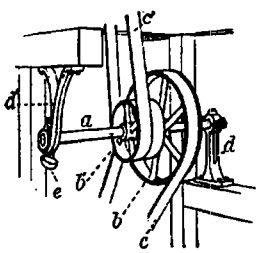
Wages: Labor is compensated by wages, labor's reward for producing wealth. Labor expends energy in making the products and is paid for its work. Wages can take many forms: money, a part of crop given to a sharecropper, or shares of stock as a bonus.

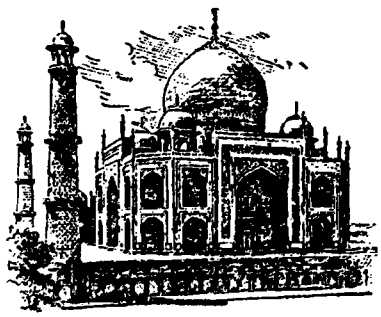
Interest: The payment for the use of capital. The owner of capital has a tool that will make labor more productive. If the owner lends the tool, the owner expects a payment for the use of it.

Rent: Payment for the use of land. Economists often refer to this as "economic rent" or "ground rent" to distinguish it from the everyday meaning of rent. We must remember, for example, that part of the "rent" paid for a building, or space in a building, is actually economic interest, because the building is capital, not land. So, when economists talk about rent, they mean the return for the use of land, not the return for the use of the building or any other improvement on the land.

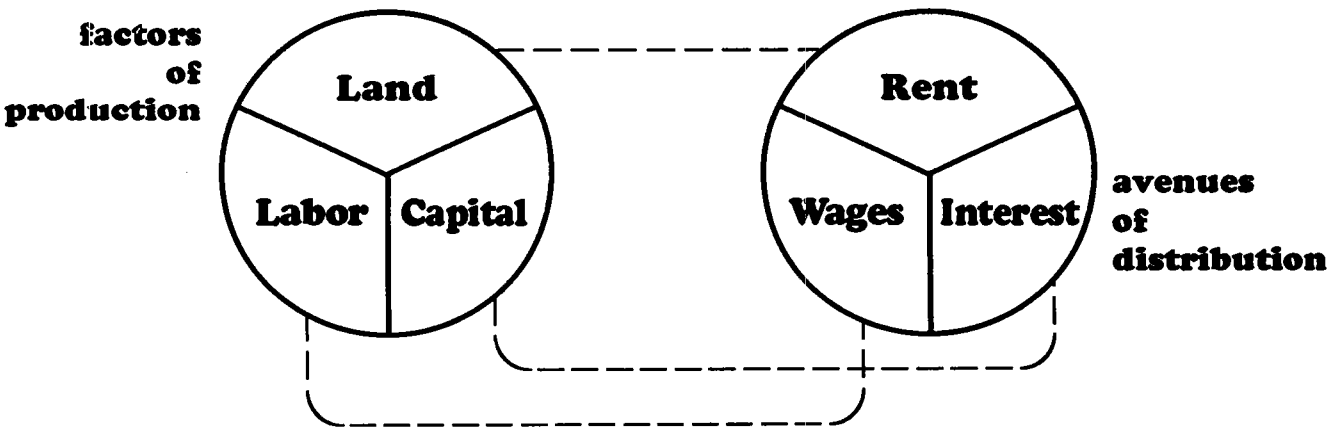
Identifying Production and Distribution







LAND + LABOR + CAPITAL = WEALTH



Land and Value

Now that we have defined what wealth is, the ingredients necessary to produce it, and who gets what, our next step will be to see whether there are natural laws of distribution: principles which determine how wealth is divided among the three factors of production. Because land is essential for all production, we will first examine the economics of land, and how land gets its value.

Things have (economic/exchange) value when someone is willing to pay for them (or give up some labor to have them, which amounts to the same thing). How does a human-made product get its value?

Labor uses capital and land to make the product. A human-made product has a cost of production and this cost must be paid - or production will cease. Costs of production may decline with efficiency and new technology, but it is clear that all human-made things (and services) have value directly related to the costs of the three factors used in producing those things. And people are willing to pay that price (in most cases) because they would have to spend much more time and effort were they to make the thing themselves.

But where does land gets its value? It is not made by anyone, and it does not have a cost of production. So, how is land value determined?

Like anything else, land starts to have value when someone is willing to pay for it. We all need access to land; it is a necessity of life. We live on it, we work on it, we need the resources from it. Unlike chairs or cars or shoes, when there is greater demand for land, there is no land factory to crank out more of it. So, following the rules of supply and demand, as more people bid on it, its price must go up.

Originally land had no market value, although it may have had a high use value. The first person over the hill, surveying the empty land before him or her, could make use of the land but could not get any money for it. Who would pay for what was out there free for the taking? But today, that same land is worth a fortune. How did this happen? Let us begin the journey.

Figure 2

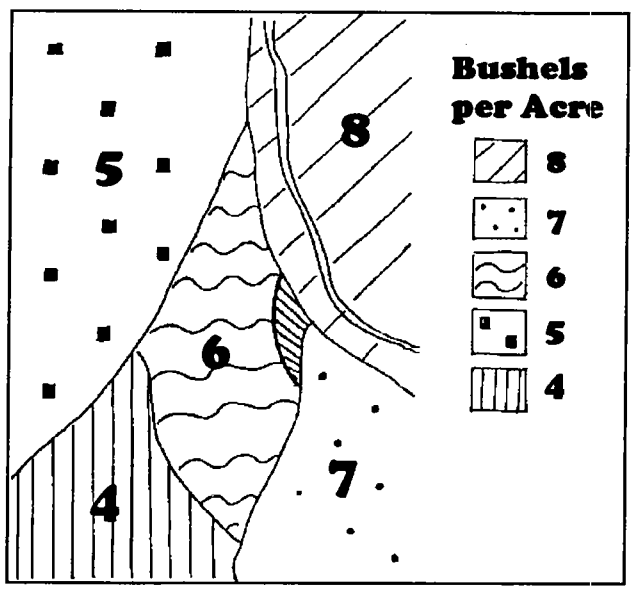
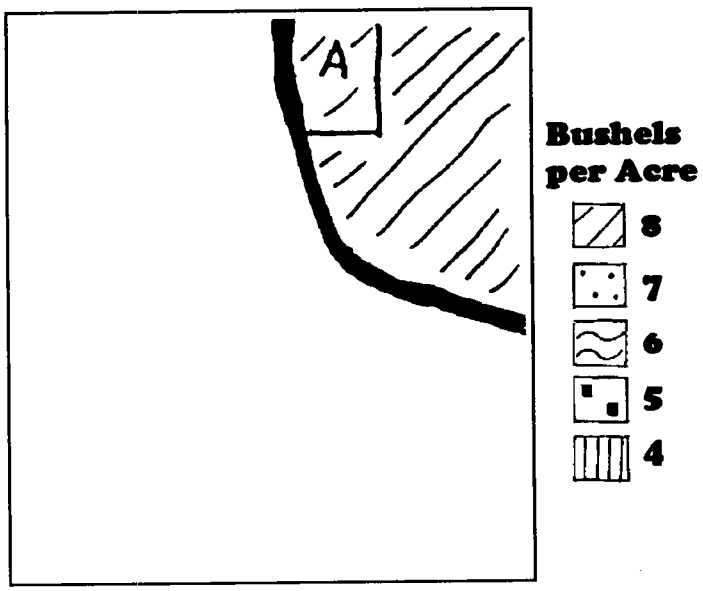


Figure 3

How much wealth is produced? _____
What part goes to wages? _____
What part goes to rent? _____



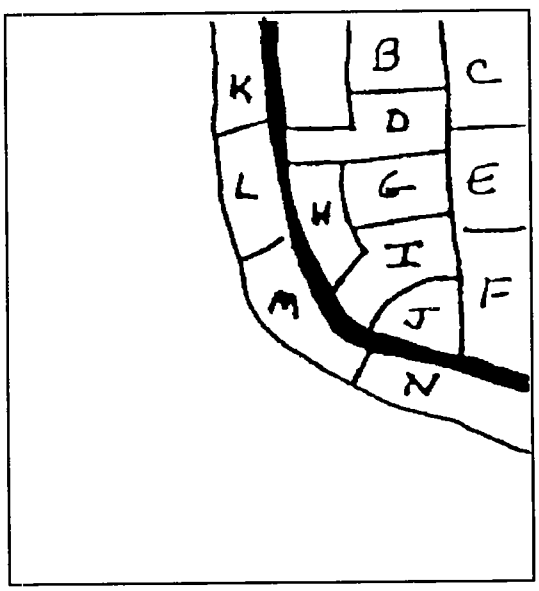


Figure 4

How much wealth does each settler produce? _____
What part is their wages? _____
What part is rent? _____

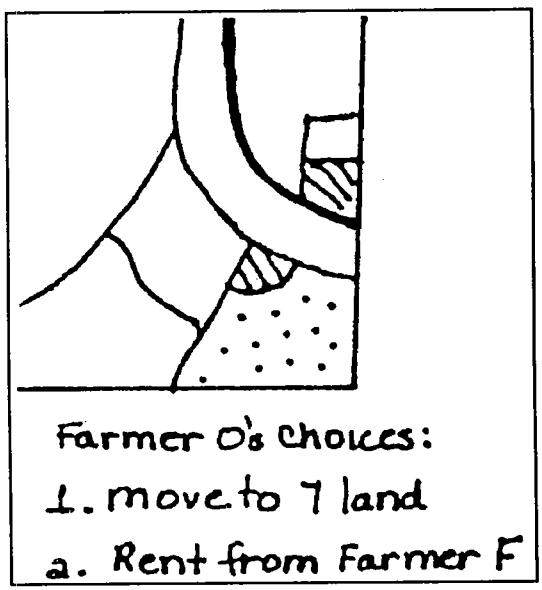
Figure 5

In this map, after all the 8 land is occupied, Farmer F has some land left over. Farmer O, the newcomer, has several choices where to go. If Farmer O moves to 7 land:

How much wealth will he produce? _____
Wages? _____
Rent? _____

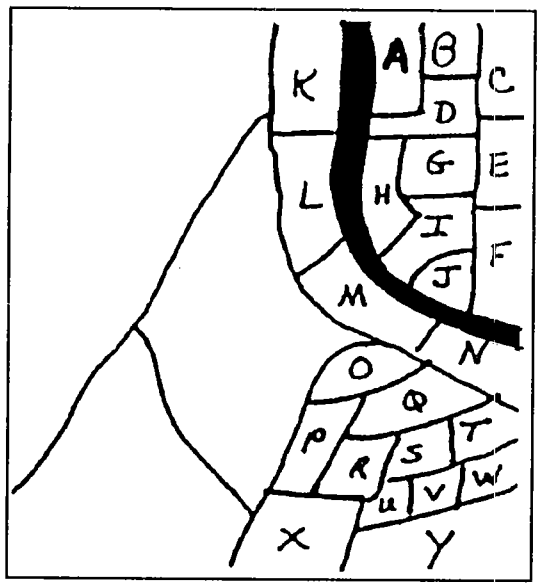
If Farmer O goes to F land:

How much wealth will he produce? _____
Wages? _____
Rent? _____



As time passes, more and more settlers come to the area. Eventually the area looks like this:

Figure 6



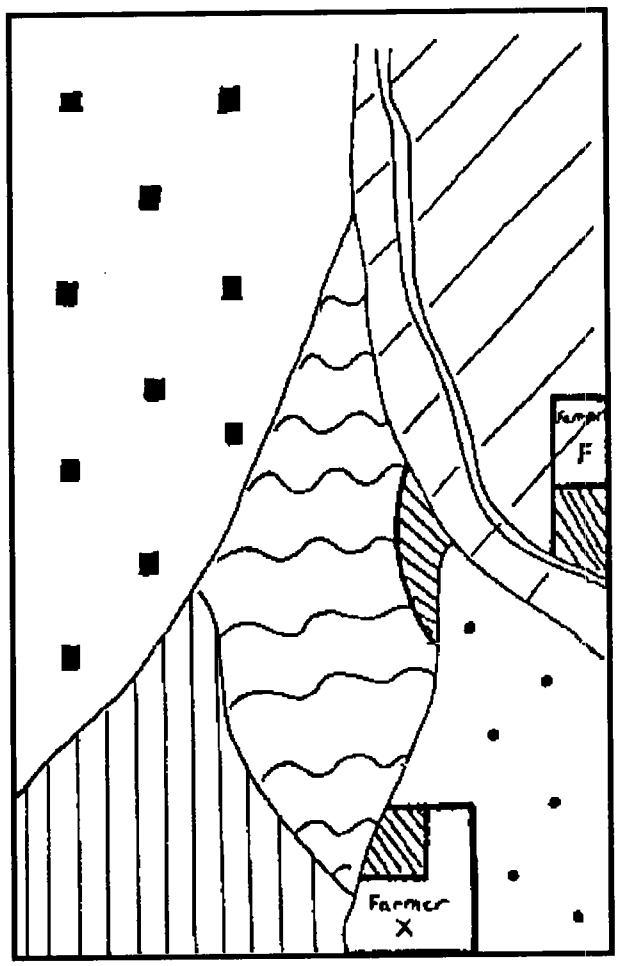
The 7 land has been completely settled. There is no free 7 land left. That means when Farmer Z comes over the hill, he now has three choices.

HERMAN



"Sorry, pal. I just bought the planet. I want you and all your buddies off by next Friday."

Project 2



Yield per acre in bushels:

= 8

= 7

= 6

= 5

= 4

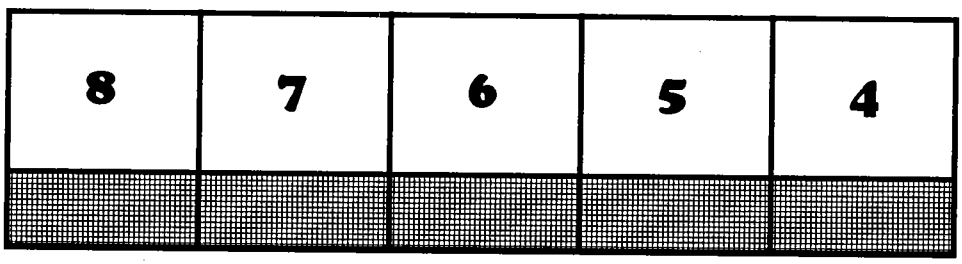
FARMER Z'S CHOICES:	**CONSEQUENCES:**
1. Move to 6 land	**Wealth produced _____** **Wages _____** **Rent _____**
2. Rent land from Farmer X	**Wealth produced _____** **Wages _____** **Rent _____**
3. Rent land from farmer F	**Wealth produced _____** **Wages _____** **Rent _____**

SPECULATORS are people who acquire land, hoping that they can rent or sell it at a later date when land values have gone up. Often they will hold the land without putting it to use, or use it in a minimal way, far less than its potential. Their primary interest is in profit from selling land at a higher price - and only secondarily, if at all, are they interested in putting the land to productive use.

On the map we have been using, there were ten plots of the 8 land. Suppose three or four of these choice plots of land were held out of use by speculators. They would not be in production, so workers who wished to use them would have to resort to 7 land. But perhaps all of the 7 land, as well, would be in use, or held for speculation. They would have to look to the 6 land - and so on.

Project #3

What are the consequences when land is held out of use for speculation?



land held by speculators

How does land speculation affect

wages? _____

rent? _____

employment? _____

distribution of wealth? _____

production? _____

urban sprawl? _____

THIS IS THE STORY OF WHAT HAS BEEN GOING ON AROUND US.

Contrary to the widely-held opinion, capitalists do not set wages. The capitalist may take advantage of low wages, but the capitalist is not responsible for setting the wage level. What sets the general level of wages is the worker's best available alternative for self-employment. And that is what we call the margin of production: the best land available that can be had without the payment of rent. Where the land can be had for free, workers and capital owners may keep all of the wealth that they produce. But whenever more land is taken into private ownership, less free land is available, and the proportion paid to rent goes up. Then, the proportion paid to wages and interest (the compensation to capital) must go down.

Today many people understand this scenario and take far more land than they need. They hold it out of production: they speculate in land. When the value of land goes up, which it will, as soon as the population increases and more people are bidding for the land, the rents go up.

SOME RESULTS OF LAND SPECULATION:

HIGHER LAND COSTS - less land is available. When supply goes down, prices go up.

INCREASED HOMELESS POPULATION - when housing prices go up, many people lose their apartments and can not find new ones within their budgets.

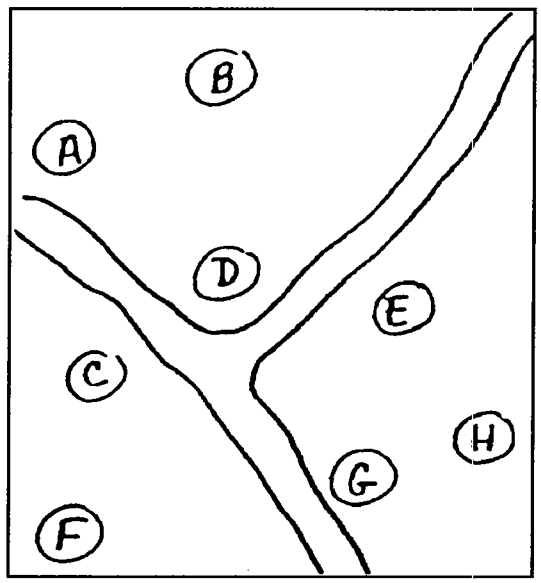
URBAN SPRAWL - if plots of land within the city are held for speculative increase rather than made available for efficient use, residents and businesses have to move farther out from the center to find available land at the price they can afford.

HIGHER TRANSPORTATION COSTS - as city limits expand, the city's transportation network has to cover more miles. Each additional mile adds greatly to the costs.

SPREAD OF SLUMS - slum landlords who are waiting for land vales to rise before selling have no incentives to improve or even maintain their properties. In fact, if they do make improvements, their property taxes go up!

On the first map, we examined these economic relationships for farm land. Now we will apply them to an urban setting.

Figure 7



This is an overview of a flat piece of land where two rivers meet. It is the early 1800s. Most of the surrounding land has been settled by farmers. A new group of settlers are interested in setting up businesses that meet the needs of these farmers. Each of these new settlers has bought land (Letters).

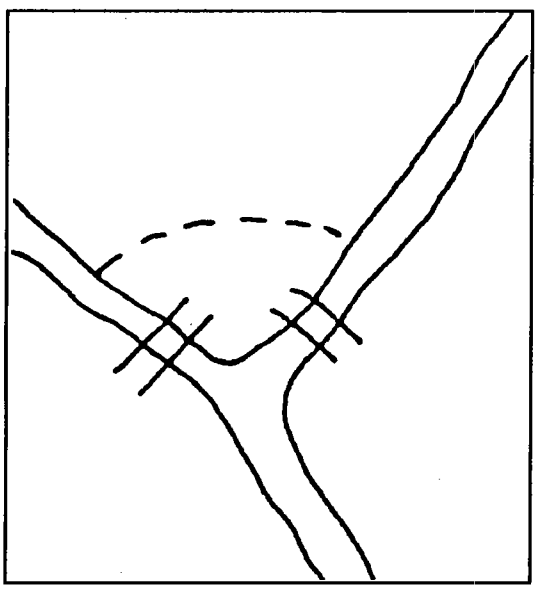


Figure 8

One of the first decisions that the new town makes is to build bridges, which vastly increase the villagers' ability to trade.

Which areas on the map will be most affected by the bridges?

What will happen to land values? Why?

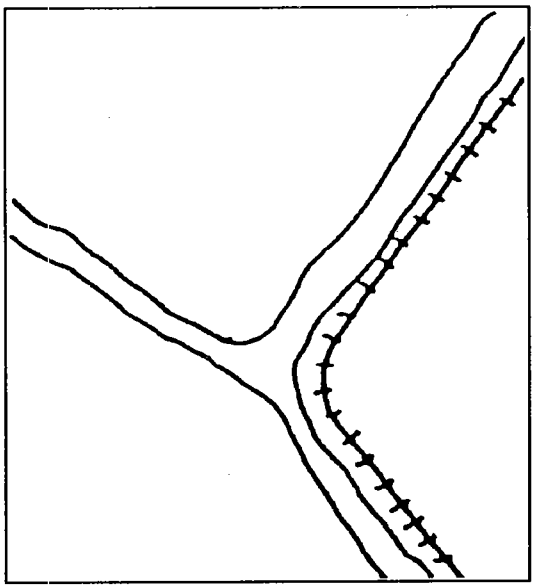


Figure 9

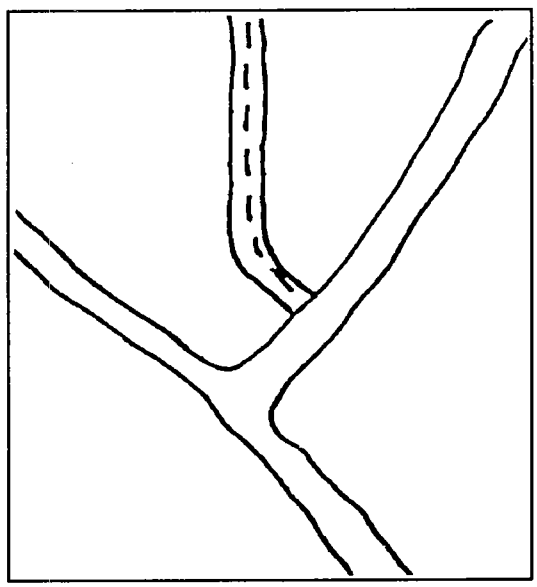
Not long after, the federal government subsidizes the constructionof a railroad. The track borders the town.

Which areas will be most affected by the railroad?

Which other areas will feel some impact?

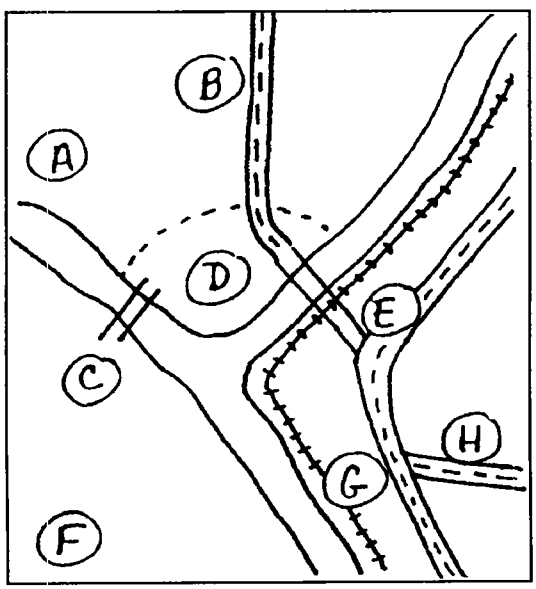
What happens to land values? Why?

Figure 10



The next big improvement is a road entering the town from the north.

Figure 11



Now more new roads.

Which areas are most affected by these latest improvements?

You may recall, in Project #2 (page 8), that we discussed what happens when the yields are different. We were working with this map:

Taxation - Federal, State and Local

The United States has a federal from of government in which the different levels of government - local, state, and federal - share power. This is especially evident in the area of taxation. All three levels of government have the power to levy taxes. Types of taxes are denoted in the Constitution. Several of the most common types are:

Sales: Generally levied by state governments, but occasionally by cities and counties as well. It is placed on the price of a good or service, and paid at the time of purchase.

Property: The major source of revenue for local governments. Taxes are placed on the value of real estate (land and buildings) and personal property. Some states also get revenue from property taxes.

Personal and Corporate: Levied on the income of individuals and corporate profits. Can be collected by all three levels, but a major source of federal funds.

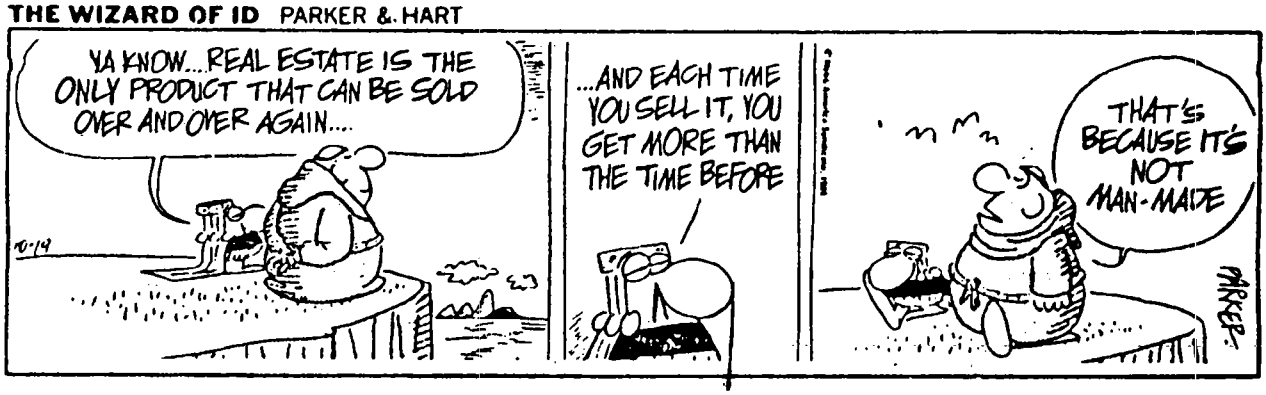
Gasoline: A special type of sales tax, which is often levied by all three levels of government on gasoline purchased at the pump.

Capital Gains: Placed on an increase in the value of an asset from the time of purchase to the time of sale. Capital gains could come from stocks or other securities, or from real estate.

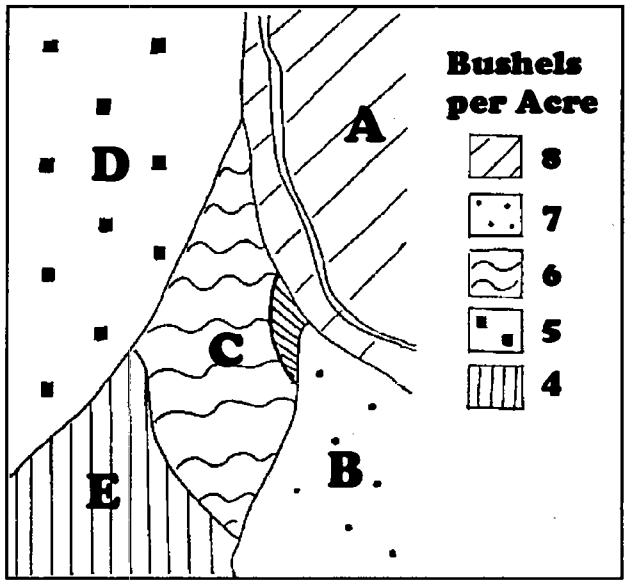
Project #4
In a scale from 1 to 5, show how the following taxes meet the mentioned criteria: (1, very little and 5, very much):

Tax	Encourages production	Easy & Cheap to Collect	Certain	Fair (does not confer individual advantage)
Sales				
Property				
Income				
Gasoline				
Capital Gains				

THE WIZARD OF ID PARKER & HART



Let us assume that all the inhabitants have occupied the plots that produce eight bushels, seven bushels, six bushels and five bushels, leaving the **four** land unoccupied. Based on the Law of Rent (Rent equals the difference in production between the land in question and the best available free land,) please indicate:



A yields a rent of _____

B yields a rent of _____

C yields a rent of _____

D yields a rent of _____

E yields a rent of _____

Under a land value tax - a tax placed on the value of land, excluding any improvements - the **rent** is the amount paid in taxes on the wealth produced on that piece of land. The rent, or land value tax, for the best land on our map is the same as the answer to question A above. Remember, we are discussing a tax on the **value** of the land, not the land *per se*. A small acreage could have a great value, or a huge tract of desert could be worth very little.

A land value tax has a different effect on markets than other taxes. Generally, a tax discourages the use of the thing being taxed. If labor and capital are taxed, they will cost more - the tax will be passed on to the consumer - and therefore they will be used less. However, a tax on land value encourages land use. If a landowner has to pay a tax that reflects the value of his land, the land owner will use his land to produce the wealth needed to pay the tax. That means that landowners will hire labor and capital to work on the land. The land value tax ends up reducing unemployment and stimulating new growth.

Land speculation would become less desirable because the holding cost of land would go up, thus decreasing the rent that landowners can keep. Tax on land value also tends to drive the market value of land down so there is less profit (or, ideally, no profit) to be made on mere ownership of land.

An effective land value tax would eliminate the need for many other taxes. It would also take us far toward eliminating the huge bureaucracy of tax collectors, lawyers, accountants and judges devoted to enforcing or avoiding the wide variety of taxes that exist today. It is a tax that is easy to collect - and impossible to hide.

Project #4

In a scale from I to 5, show how the following tax meets the mentioned criteria: (1, very little and 5, very much):

Tax	Encourages production	Easy & Cheap to Collect	Certain	Fair (does not confer individual advantage)
Land Value				

Land Value Taxation Around the World

The following gives a brief account of various places throughout the world where land value taxation is partially applied and improvements partially or fully exempt. Nowhere has the principle of exclusive land value taxation (approaching the full economic rent), with abolition of all other taxes, been applied on a large scale. But partial applications indicate results commensurate with the degree of application.

Denmark - Although Denmark collects much revenue from taxes on incomes and products, she still collects about 50% of the total annual ground rent through various methods. A land valuation is held about every 5 years. Danish methods are as follows:

1. Rental of government-acquired land to farmers at 4% of its selling value. About 12,000 small farmers rent their land in this way.
2. Local and national taxation of land values, with consequent reduction of taxes on improvements.
3. A national tax on increases in land values.

Results are impressive. Danish farm tenancy dropped from 42.5% in 1850 to less than 5% today. Productivity is high and a high standard of living prevails.

Australia - All six states and a majority of the municipalities in the Commonwealth of Australia tax land values to a certain degree, and some exempt improvements in whole or in part. However, there are many other non-real-estate taxes.

The Capital Territory - The Commonwealth owns most of the land in the Capital Territory, including the city of Canberra. The government leases this land to indivuduals, and also levies a tax on its value.

Queensland - Most of the land in Queensland is owned by the state and is leased. It is also subject to local land value taxes. There is also a state land value tax on privately owned land. Improvements are not valued for tax purposes. More than 50% of the ground rent is collected. All local communities tax land values only.

New South Wales - All local taxing units tax land values only. There is no state land value tax, but the state collects royalties on minerals. The City of Sydney is the largest city in the world to derive all its municipal revenue from land value taxation. Building has been encouraged, slums eliminated and the price of land stabilized.

Western Australia - Of the 147 local taxing units (municipalities and road districts) 32 tax land values only. The remainder tax both land and improvements, but in the 128 road districts, 84% of the revenue is from land values only. There is also a state land value tax which is heavier on absentee owners.

Other Australian States - South Australia has a state land value tax, with an additional penalty on absentee landholders. In addition, 8 incorporated cities, 11 counties and 8 district councils have adopted land value taxation. Victoria has a state and local land value tax. Twenty-four out of 198 local taxing units tax land values only. The result has been to bring idle land into use. Tasmania has a state land value tax but no local ones.

New Zealand - Like Australia, New Zealand has local taxes on land values. Local taxing units adopt it by local elections, and the majority of local units tax land values only. It has encouraged the good use of land and has helped break up large estates, assisting the small farmers. Recent complications in rating legislation have mitigated some of the good effects.

SOUTH AFRICA - Of the 60 cities in the Transvaal, 20 tax land values only. In the other 40, the tax on land values is higher than on improvements. Of the 65 municipalities in the Orange Free State, 15 tax land values exclusively for all city needs except water and sanitation. In Natal, 23 of the 35 municipalities tax land values at a higher rate than improvements. Results are impressive in Johannesburg which has new building continually going on. The system of land value taxation has contributed much to the economic strength of South Africa despite that country's unfortunate racial policies.

CANADA - Various cities in western Canada tax land values at a higher rate than improvements. In british Columbia, 54 of the 104 municipalities exempt improvements 50%; 13 exempt them more than 50%. In New Westminster, 86% of the householders own their own property and land speculation has disappeared.

Alberta requires its 7 cities to exempt improvements 40% from taxation. The province taxes land values to some extent, including a land-transfer tax called an "unearned increment tax". The province obtains considerable revenues from oil leases, rentals and royalties (a form of land rent, which has made possible a "Heritage Fund.")

In Saskatchewan all but one of the cities and towns exempt improvement values 40%; Regina 70%. In rural municipalities land value taxation is the primary source of revenue. In Manitoba cities and towns exempt improvements one-third.

UNITED STATES - The general property tax and the real property tax, insofar as they fall on land values, take for local or state purposes part of the ground rent in the U.S. In many cities the cost of streets, water mains, lights, etc., is charged to adjoining properties through special assessments. Government collection of royalties on mineral land, oil fields, etc., as well as public lands, recoup some ground rent. The federal government is obtaining an increasing revenue from these sources, amounting to many billions of dollars.

PENNSYLVANIA - Seventeen cities in Pennsylvania now apply what is termed the "graded tax plan" whereby land is taxed at a higher rate than improvements, and the two largest among them, Pittsburgh and Scranton, have both raised the land tax considerably in recent years. This has been an important factor in Pittsburgh's "Renaissance II". The state permits cities of the third class (all the remaining cities except Philadelphia) to tax land and improvements at different rates. As the benefits of the graded tax, namely, more new construction and lower housing costs, become more and more apparent, many other Pennsylvania municipalities are examining the graded tax plan.

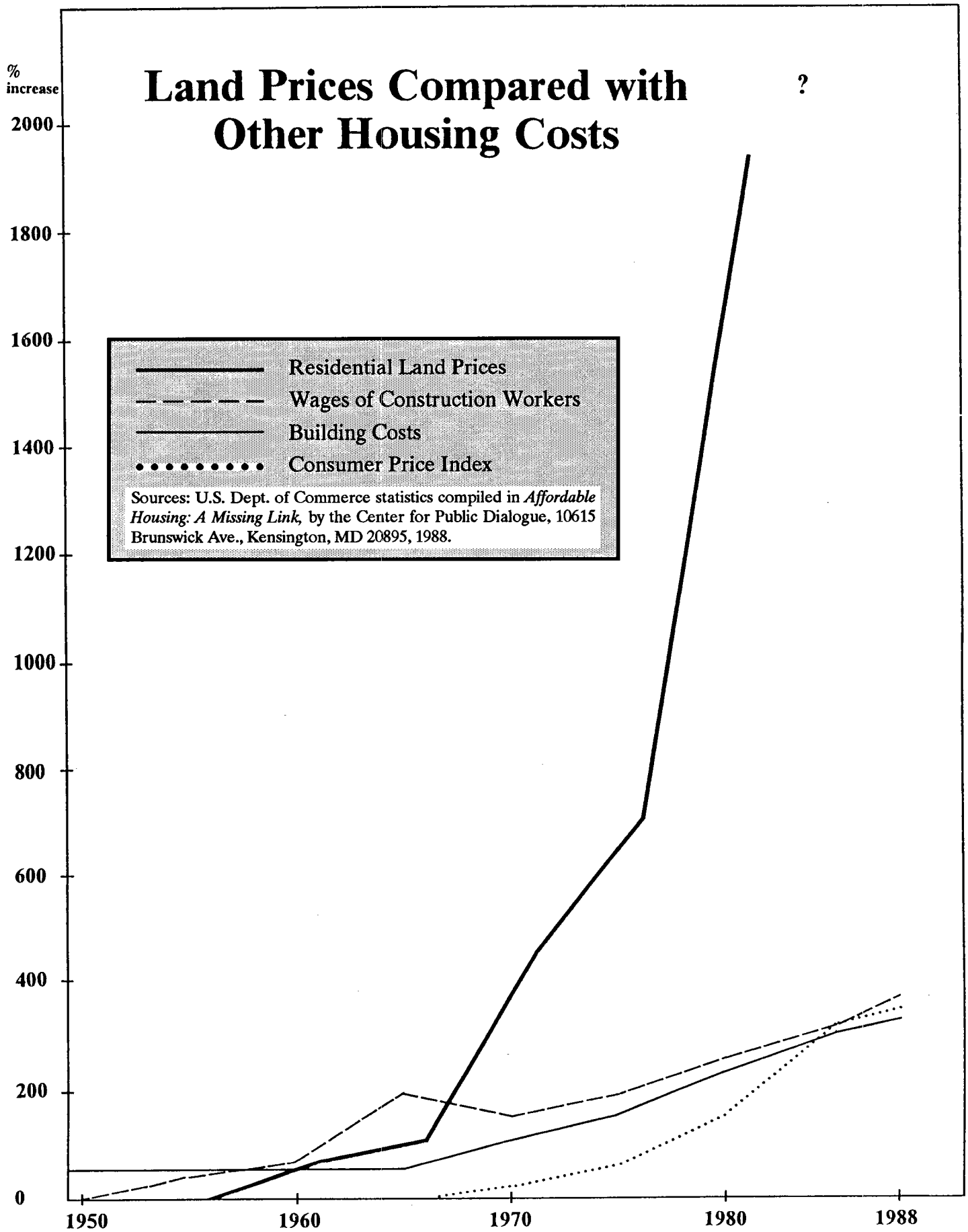
CALIFORNIA - In 1909 the California legislature required new irrigation districts (and gave the option to established ones) to tax land values only, exempting improvements, crops, etc. Today over 100 districts, serving four million acres of the best farmland in the state and raising about 75% of its crops, follow this system. Speculation has been eliminated and agricultural production has been greatly encouraged.

ALASKA - The state owns much of the oil land around Prudhoe Bay, and collects a 12% royalty. This has resulted in abundant revenues beyond public expenses, and has made possible a per capita dividend and a cancellation of the income tax.

FAIRHOPE, ALABAMA - This is a colony operated by the Fairhope Single Tax Corporation which owns the land in Fairhope and leases it to its residents. With the economic rent it collects, the corporation pays property taxes levied by the state, county and city, and the remainder is used for public improvements. Fairhope has far outstripped its neighboring towns in growth.

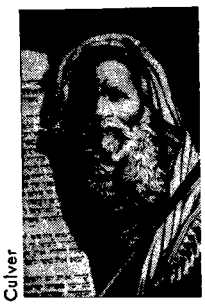
THE THREE ARDENS, DELAWARE - These are Arden, Ardentown, and Ardencroft. The land is leased to its users, and, as in Fairhope, local taxes are paid and the balance of the rent is used for public improvements. These towns are well-known as beautiful residential communities.

Land Prices Compared with Other Housing Costs



NOTES

Many great lawgivers and economists have said landed property is different

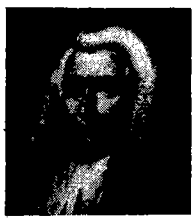

Culver

MOSES (1400 BC): The land shall not be sold forever; for the land is Mine; for ye are strangers and sojourners with Me. *Leviticus XXV.*

JOHN LOCKE (1632-1704): God gave the world in common to all mankind. Whenever, in any country, the proprietor ceases to be the improver, political economy has nothing to say in defense of landed property. When the "sacredness" of property is talked of, it should be remembered that any such sacredness does not belong in the same degree to landed property.



KARL MARX (1818-1883): Assuming the capitalist mode of production, then the capitalist is not only a necessary functionary but the dominating functionary in production. The landowner on the other hand is superfluous in this mode of production. If landed property became *people's property* then the whole basis of capitalist production would go.



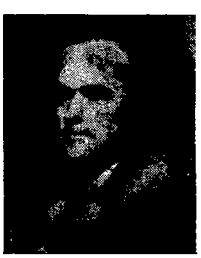
WILLIAM BLACKSTONE (1723-1780): The earth, therefore, and all things therein, are the general property of all mankind, from the immediate gift of the Creator.



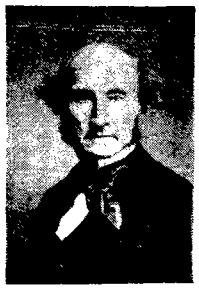
ADAM SMITH (1723-1790): Ground rents are a species of revenue which the owner, in many cases, enjoys without any care or attention of his own. Ground rents are, therefore, perhaps a species of revenue which can best bear to have a peculiar tax imposed upon them.



TOM PAINE (1737-1809). Men did not make the earth. . . . It is the value of the improvement only, and not the earth itself, that is individual property. . . . Every proprietor owes to the community a ground rent for the land which he holds.



THOMAS JEFFERSON (1743-1826): The earth is given as a common stock for men to labor and live on.



JOHN STUART MILL (1806-1873): Landlords grow richer in their sleep without working, risking, or economizing. The increase in the value of land, arising as it does from the efforts of an entire community, should belong to the community and not to the individual who might hold title.



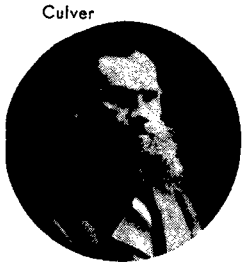
ABRAHAM LINCOLN (1809-1865): The land, the earth God gave to man for his home, sustenance, and support, should never be the possession of any man, corporation, society, or unfriendly government, any more than the air or water, if as much. An individual, or company, or enterprise requiring land should hold no more than is required for their home and sustenance.

All that is not so used should be held for the free use of every family to make homesteads, and to hold them as long as they are so occupied.


Elliott & Fry

HERBERT SPENCER (1820-1903): Equity does not permit property in land. . . . The world is God's bequest to mankind. All men are joint heirs to it.

Culver



LEO TOLSTOI (1828-1910): Solving the land question means the solving of all social questions . . . Possession of land by people who do not use it is immoral—just like the possession of slaves.


Keystone

HENRY GEORGE (1839-1897): Our primary social adjustment is a denial of justice. In allowing one man to own the land on which and from which other men must live, we have made them his bondsmen in a degree which increases as material progress goes on. It is this that turns the blessings of material progress into a curse.



DR SUN YAT-SEN (1866-1925): The (land tax) as the only means of supporting the government is an infinitely just, reasonable, and equitably distributed tax, and on it we will found our new system. The centuries of heavy and irregular taxation for the benefit of the Manchus have shown China the injustice of any other system of taxation.