



The Impact of Land Speculation on Land Utilization

By Dr. Mason Gaffney

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PROJECT OUTLINE

"The Impact of Land Speculation on Land Utilization"

Mason Gaffney

I. The Subject: (Salter's "Problem")

Land speculation appears, to empirical observers, to be undesirable land use. Economic theory, on the other hand, teaches that in the absence of monopoly elements, free market forces will allocate resources to their most socially productive uses. Further, some observers think the speculative motive is an incentive that leads to developing lands. This study will examine these conflicting viewpoints and of course the subject on which they are given, and try to find the truth.

II. Defining & elaborating the subject.

A. What is "Land"? Some recent economists deny that resources can be differentiated. (Knight, Fetter, e.g.) Their arguments are primarily just to stress the common characteristics of land and capital and labor, and to ignore the differences. Land differs from capital in that:

1. It was not produced by man, is not being produced by man, and so far as we know cannot be produced by man. Capital, by contrast, results from a, production and b, saving.

2. Land has a definite location and relation to its environs, whereas capital can be placed in a variety of places and much capital remains mobile even after production. Indeed, it is convenient to distinguish two aspects of land: location, and "stock". Once capital is created and affixed to land, it acquires ~~many~~ many of the characteristics of a stock resource, save that the stock resource was not placed there by man; and that the stock resource is not usually useful until moved or processed, while the capital is useful where it is, that is why it was placed there.

It follows that capital and labor can migrate from place to place, whereas land cannot. Land can shift among different uses only insofar as this does not require

migration.

Land as space or location cannot be destroyed or depleted, unlike capital. Land as stock can be destroyed and depleted. It differs from capital in that it is the original source of matter which constitutes capital, was not created by production and saving like capital.

3. Land in the sense of location and space is expected to last forever, unlike capital. Land in the sense of matter and energy, the basic constituents of the earth, is also expected to last forever, unlike capital. Capital is simply particular matter and energy on which the impress of production and saving has been made. It lasts for a time and returns to the land. Land is not only the original source of capital, but the graveyard to which it returns.

Capital, even during the span of its life, is partly land. The labor and capital services which went into it do not account for all its value. There is a land element: the material of which it is constructed, and the energy which is embodied in its form. The only part which is properly "capital" is the excess of the value over the stock resource embodied in it. The matter of which capital is composed is still land, divorced from its original site.

4. Land, being stationary, is the trap to which localized values are imputed. A highway may make land, labor, and capital in an area more productive; but labor and capital can immigrate, bringing local values down to those of the economy as a whole. Land cannot immigrate, except as stock resources can be carried in, so benefits are imputed to local land values, not local wages and interest.

5. The total supply of land is fixed, whereas labor & capital vary, are affected by incentives.

service

6. Landowners render no productive ~~return~~ to society for their incomes; they simply appropriate the income from a resource they did not create.

7. Capital depreciates with use, and with time. Land as a flow resource does not, and is normally expected to appreciate.

8. Land supplied freely by nature is so great that much of it is unused and valueless at present.

B. What is Rent?

Some modern economists assert that all resources receive rents. By rents they mean payments greater than necessary to induce the resource into production.

Lerner and others correctly answer that this is only true from the micro-economic viewpoint, from which land is much the same as other resources. From the macro-economic viewpoint, ~~ALL land payments are~~ payments for land use are rent in that they are not necessary to bring the resource into production. Whereas none of the payments to marginal labor and capital are rent, and only part of the payments to inframarginal labor and capital.

The case may best be tested at the margins, where none of the payments to resources can be rent. Labor and capital at the margins receive payments, none of which are rent; land at the margin receives no payment at all, since there is no rent at the margin.

There has also been much overestimation of the importance of the above question, whatever its outcome. The important distinction to be made between land incomes and other incomes is that land income is in return for no productive service to society, whereas other incomes are from contributing capital and labor to society.

Again, as the practical consequences of the outcome of the above discussion, all parties agree that there are no rents at the margins, so that the supply of labor and capital is reduced by reducing their rewards at the margin, other things being equal; whereas the supply of land is fixed, by nature.

C. What is Speculation?

We tend to think of speculation in extreme terms, as when land is held by absentees, or is held idle. But there is no clear line between speculation so conceived and other ownership. It is impossible to own land, or any other asset, without speculating. Land speculation, therefore, I define as land ownership. I shall preserve the name land speculation to serve as a constant reminder that ownership is speculation.

Modern economic theory teaches that resource allocation is perfect, in terms of satisfying given money demands, save for the following elements: Monopoly; governmental restraints on free movement

of resources; external economies and diseconomies. Speculation, it teaches, merely aids other market forces in perfecting allocation. But it only deals with commodity speculation, not with land speculation. My hypothesis is that there is a fourth market imperfection in land speculation.

III.

HYPOTHESIS:

Land speculation distorts land allocation from the norm.

IV.

Testing the Hypothesis.

I shall test it in several stages, starting with the simplest case, and building to the more complex.

A. Land allocation under the assumptions of perfect competition.

These assumptions do not include the assumption that capital markets are costless; nor that all individuals are identical. Hence even in "perfect competition" different individuals will discount future values at different rates. Simultaneously, different individuals, being differently equipped, will anticipate different net yields from the same land. The one who will get the highest yields should get the land; but if his individual discount rate is higher than some others, he may be outbid. Thus land speculation distorts land allocation.

B. Land speculation contributes to monopoly.

In agriculture we observe the existence of functionless absentee landownership or speculation, springing from the differences in access to capital among individuals. In industry, too, we see consolidation of ownership in few hands leading to monopoly. This consolidation is normally effected thru centers of capital, like Wall Street. Holding companies can buy up operating companies at a financial profit because holding companies, with more diversified risks, can borrow at lower interest rates, i.e. can sell stocks and bonds at higher prices. The consolidation that leads to industrial monopoly is thus effected thru industrial absentee landownership. Such absentee ownership would be functionless (save when its express purpose is to create monopoly) were it not for land speculation. Otherwise the resident owners and managers would be in a better position to maximize the

firms' profits. Holding companies are said to effect economies, and thus be economically justified, because they can supply capital to operating firms at lower rates than they could get for themselves. But much of this supposed economy is just in the superior power to buy land, which is not a social economy, but the opposite.

Land speculation indirectly contributes to monopoly because many government restraints, which aid monopoly, are reactions to land speculation. Labor unions are a prime example. They could hardly exist without land speculation, since they require some localized asset to which to fasten themselves. Capital can emigrate to escape them; land cannot.

Land speculation further distorts resource allocation by preventing impartial recognition of external economies, or extended benefits, by government. For particular external economies and diseconomies will accrue to particular lands and, as long as these are owned by particular individuals, there can be no impartial public determination of maximum social benefits from public works.

C. Land Speculation distorts intertemporal relationships.

Absentee landowners frequently, when the costs of landlord-tenant relationships are considered, take less net income from the land than the tenant would directly. Some of this waste takes the form of the absentee's being careless of what the tenant does to the future of his land; and tenantry is correlated with erosion.

Speculation in stock resources results in a pressure to extract now, instead of in the future, that varies with the interest rate. So that stock resources are mined at very different rates, depending on the individual rate of the owners. So that at an early stage in our history they fell into the hands of many who exploited them very swiftly, due to their high rates; and later they tended to fall into the hands of those with very low rates, who hold them out of use for their future values and use them to create monopolies. If they were subject to a severance tax, on the other hand, interest rates would cease to affect mining rates.

V. Extending the Hypothesis *dynamics* Dynamics of land speculation.

A. Land Speculation affects interest rates by drawing money from investment.

B. Land Speculation affects capital formation by providing a substitute for capital in individuals' balances, reducing their desire to save.

C. Land speculation causes excess subdivision, both rural and urban, with attendant waste of resources. It contributes to the miscalculations of future values that cause business cycles.

D. Land Speculation is integrally connected with "boom and bust", in misguiding investment. The biggest business cycles are in construction, which is associated with land speculation.

E. Land Speculation affects the money supply, providing the base, thru real estate loans, of an undependable money.

F. Land Speculation must be considered in modern "employment theory", or "macro-economic" theory. For "full employment" is not a concept separate from perfect allocation. Resources are not fully employed unless perfectly allocated. "Unemployment" is simply the extreme form of misallocation, as idle land is the extreme distortion of land speculation. Labor unemployment results in part from land unemployment, as they are complements.

VI. Extending the Hypothesis into Politics

Land Speculators create local governments as their agents. As labor and capital are migratory, they have less reason to be interested in local government, and landowners dominate. Labor and capital can only benefit from local government if they keep outside labor from migrating in to share the benefits they create for labor and capital. Hence labor unions and political machines.

Local government, thus constituted, breeds restrictive elements which contribute to distorting allocation.

Causes of local restrictivism:

A. To restrict access to common property of the community, like parks, streets.

B. Attempts of relatively wealthy landowners to divide their part of town from that of relatively poor, to reduce their taxes.

C. Attempts to exploit the monopoly position of the town.

These are expressed thru local tax policy; zoning; city planning; licensing; and to some degree in all local functions.