

CHAPTER XXXIII

THE THEORY OF RENT

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Nature of Rent. — The most generally accepted and most firmly established theory of distribution is that relating to rent. Rent is the return on natural resources and, in economics, means the amount of wealth that "land" receives for its part in production. Therefore, from an economic standpoint, "rent" means something quite different from the sense in which the word is used by the real estate broker. The latter uses the

term to represent not only the return on land — the lot — but also the return on capital — the house. Real estate rent, therefore, includes both rent and interest; but economic rent signifies simply the return on land. This distinction is fundamental and must always be borne in mind.

It is equally important to remember that rent exists regardless of the manner in which it is paid or of the person to whom it is paid. For example, land may receive its share of rent in the form of so many extra bushels of wheat as well as in the form of money representing these bushels of wheat.

How rent is paid. Likewise, this rent is paid to land regardless of whether the land is used by the owner or by the tenant. Since land cannot take this rent itself, some one must take it for the land. Therefore the landlord receives the rent. If he uses the land himself, he receives it in the form of extra crops; if some one else uses it, he takes it in the form of money. When the owner and the user are two different persons, it may easily be seen that the payment of rent becomes more marked and more socially significant.

Since rent exists so generally and since it is paid so universally, one naturally asks, "How does rent arise and what reason is there for its payment?" To this question there is

How rent arises: a clear and definite answer. Rent arises because of differences in the productive capacity of various lands. This difference of productivity may be due to a difference in the fertility of the soil or to a difference in the location of the land.

First of all, picture in your mind two separate tracts of land, each an acre in size. Every spring the two farmers owning these tracts go out to plant their grain. They may use the same quality of fertilizer, the same kind of grain,

and the same kind of plow, and have the same efficiency in their labor force. In the fall, one farmer reaps twenty bushels; the other, fifteen. To what can we attribute this difference in yield of five bushels per acre? In all production there are three factors,—
From differences of fertility.
 land, labor, and capital. On these two acres the capital and labor were, by assumption, respectively identical. This being the case, there remains but the third factor to which we can attribute this extra growth of five bushels. That is land. The extra return of five bushels is the income which we can attribute to the better acre because of its superiority over the poorer one. Such an increase is termed "rent." Thus, economic rent arises because "land" aids man unequally in production. In one place it yields fifteen bushels, in another twenty. This difference in the yield constitutes the rent.

Again, let us picture to ourselves two retail stores of equal attractiveness so far as the building and goods are concerned, and each with equally efficient management. One is located on the outskirts or edge of the business district and the other is near the center of one of the busiest thoroughfares. At the end of the year, the net profit of the one store may be one thousand dollars, while the net profit of the other may be two thousand five hundred dollars. To what, then, must we attribute this difference in earning power amounting to fifteen hundred dollars per annum? The labor is equally efficient; the physical equipment of the stores is similar. The difference, then, can only be attributed to the third factor in production, namely, land. The income which we must attribute to this second store because of its superiority in location over the poorer we also call economic rent. In
From differences of location.

the first illustration, the superiority in fertility gives rise to rent, while in the second, the superiority in location has a like effect. Superiority may, of course, be the product of both fertility and of location, as in trucking land near great cities.

Rent, therefore, arises from differences in the value of land, and the rent of any piece of land is the difference between its yield or value and that of a particular piece of land taken as a basis of comparison.

The Grades of Land. — The center of every city is devoted to the purposes of business. Outside this district we find, roughly speaking, the circular belt of the residential district, which, though it has not quite the high social value of the business section, still plays an important part in the use that man makes of land. Then beyond the confines of the city is the land devoted to truck farming; still farther out lie lands devoted to general farming and to grazing.

There may still be land lying beyond the grazing land which is least desirable for any of the uses to which man may put land, but which may serve to catch the overflow of population, or may be used by the less fortunate members of society who are willing to go on this poor outlying land and work there for a bare living. This last type of land has earned the name in economics of "no-rent" land, — a term which implies that a man working on such land will merely get enough from his labor to allow himself his daily wage and to pay for the few simple tools and seed that he may need in cultivating it. Its fertility is so low that, when a definite return from the land is set aside to pay the wages of labor and the interest on capital, there is nothing left for rent. Hence the expression "no-rent" land.

Broadly speaking, that class of land which has the highest social value will yield the largest amount of rent, and, of each class, that land which is superior will yield the higher rent. Accordingly, all land used for business purposes yields a greater income than land used for residential purposes. This latter in turn yields more than land used for trucking, while trucking land yields more than land used for farming. Again, farming land is more valuable than land used for grazing, which, in its turn, brings in a higher return than "no-rent" land.

*Rent varies:
Between
grades.*

It is apparent, however, that though this general scheme of gradation of the size of rents holds good, there are many variations in rent, and no two pieces of land in the same belt pay the same amount of economic rent. Hence, we speak of the poorest land of each belt or class — the marginal land — as receiving a marginal rent. If we take this poorest land as our basis, better land in the same class must pay a higher rate due to its superiority. This additional rate is called the differential rent, so that in theory all land which is better, to however small a degree, than the poorest land pays a rent composed of these two elements, — a sum equal to the amount paid for the poorest land of its class, called marginal rent, and an additional sum proportionate to its superiority over that land, called differential rent. The two together equal the economic rent.

*Within a
grade.*

To illustrate, one can imagine a piece of land just on the margin of the belt between general farming and trucking. It is the poorest land used for truck farming and yields a rent of twenty-five dollars an acre. Half a mile nearer the city there may be a second farm which, because of its superiority, will have to pay an additional sum of ten dollars,

making its full rent the sum of the marginal and differential rent, or thirty-five dollars. Still farther in toward the city we can conceive of the very best land used for this purpose lying adjacent to the suburban district. This farm, being near to the city markets, will have to pay an even greater differential rent, perhaps fifteen dollars, making in all a total rent of forty dollars.

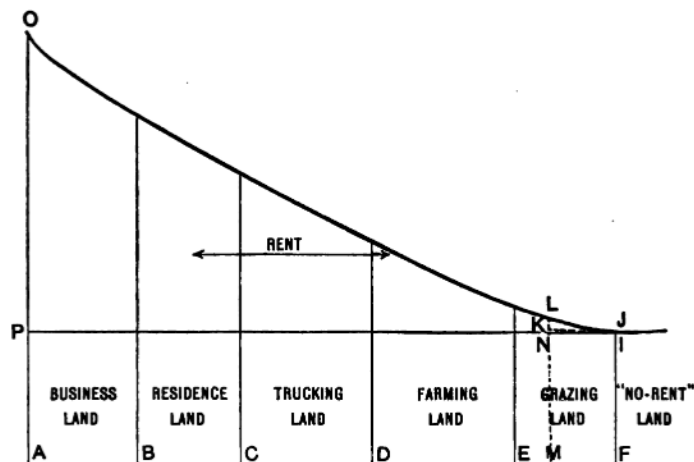
If, now, we go even farther toward the city, we immediately pass into the next belt in our illustration, the residential. The poorest land used for this purpose gives us the new marginal rent for that belt. It is obvious, however, that the amount paid for the poorest or marginal land in this belt must be a little higher than that paid for the best land of the next lower or trucking belt. If this were not so, the land would be put to truck farming again, because it would yield by that method a larger return. As a result, we have this general principle running throughout all rents, the rent of the marginal land of the next higher belt is always a little greater than the rent of the marginal land of the next lower belt plus its greatest differential rent.

This entire theory of rent is usually illustrated by the diagram on page 271.

The horizontal base represents, of course, the lands themselves, while the vertical lines show their varying productivity. From this illustration we are enabled to see, not only the varying values of the different classes of lands, but also the varying values of different lands within the same class. For example, at one end of the horizontal base we have land *A*, the most productive land in the most valuable grade, with a productivity represented by *AO*, of which *PO* is rent. At the other end

The general principle.
Explanation of diagram.

we have land F , the least productive land in the lowest rent-paying belt, with a productivity represented by FJ , of which IJ is rent. This land F is the marginal land of the lowest rent-paying class and its rent (IJ) is marginal rent. A little farther up in this grazing land, however, we find that land M has a productivity of ML and that, consequently it has a differential rent of KL above the marginal rent of F .



Altogether this land M has an economic rent of NL , which represents the sum of both the marginal and differential rent.

So far we have applied the law of rent to only one kind of "land," namely, the fields. It is, however, applicable to other forms of "land," such as mines and water power. For example, marginal water power would be the poorest kind of water power that could be profitably used for a certain purpose, as the running of a sawmill. A larger and stronger stream, capable of being used for the same purpose, would

yield a greater return of sawed lumber. This additional income would represent the differential rent. Were there a source of water power so strong that it would just pay for the machinery used in harnessing it and the labor needed in operating it, it would correspond to "no-rent" land and might well be called "no-rent" water power. Likewise, we can apply the same fundamental principle of economic rent to mines and other gifts of nature.

According to these principles, land takes one great portion of the world's wealth in the form of rent. In any advanced civilization the share of distribution that goes to land in the form of rent is always increasing because the value of land is always rising. In young and newly settled countries, where natural resources are abundant and unappropriated, the amount of wealth that goes to land is correspondingly small. However, as population increases and resources are utilized, the landlord class must develop and appropriate a larger and larger share of wealth. In the United States, should the monopoly of natural resources go on unchecked, a great mass of wealth could not help but be diverted to the land-owning classes.

TOPICS FOR CLASS DISCUSSION

1. With whose name is the theory of rent most closely associated?
2. Give local examples of a general rise of rent; the cause. Of a general fall of rent; the cause.
3. What is meant by the "law of diminishing returns" when applied to land?
4. Do the governments of other countries own land? Would it have been better for the United States to retain the ownership of its land instead of giving it away?