THE FOUNDATIONS OF SOCIAL ECONOMY

A Land Policy

The war has brought home to us the importance of developing the natural resources of our own country. At present we labor under many disadvantages. There is no effective recognition of the rights of the people to the land, and our system of taxation facilitates the withholding of land from use and penalizes improvements. The great majority of those who cultivate the land have no secure and continuing interest in it. Titles to land are complicated and sometimes uncertain, the expense of ascertaining them is considerable, and the cost of transferring land is excessive.[1] These conditions check production at its source and are too bad for tinkering. We need a policy of systematic reform.

Principles of Action

At the outset, there must be a clear assertion of the right of public property in the natural elements and the right of private property in the results of private effort. Those who hold the natural elements—which may conveniently be referred to as the land—ought to be taxed according to the value of the land that they hold, whether they use it or not; the continuous payment of this tax, which should be regarded as a State rent-charge, ought to be a condition of their continued possession of the land; and all improvements ought to be tax-free.

Economic Effects

This remodelling of land taxation would have important economic effects.

[1]These observations refer to the United Kingdom and those about title and transfer relate particularly to England.

(1) The taxation of landed property on a true basis would secure to the people the value that attaches to the land owing to their presence and competitive demand.

(2) The pressure of having to pay the tax whether the land were used or not would induce those who are holding land without using it either to use it themselves or to let other people use it.

(3) The untaxing of improvements would give free course to building in all its branches, and to the making of many other improvements that are checked by the present system.

(4) The continuing liability to the tax would incline landlords to let the land on continuous tenancies, which might be made more easy by providing for the revision of rents from time to time.

Land, Labor and Capital

The case for taxing land-values and untaxing improvements becomes stronger when we consider the fundamental relations between land, labor and capital. These expressions and certain others are used here in the following way:

Land includes all the natural elements that exist independently of labor, and Rent means payment for the use of land;

Labor includes all human activities, and Wages means payment for the use of labor;

Wealth includes all the products that labor obtains from the land, both in their natural conditions and as subsequently developed;

Capital means wealth considered as an agent for the production of more wealth, and Interest means payment for the use of capital.

In actual practice Land, Labor and Capital are often combined, and the joint yield is partly rent, partly wages and partly interest, as the case may be. The yield of land and buildings, for instance, is partly rent and partly interest; the hire of a driver and vehicle is partly wages and partly interest; and the return from land, labor and capital together is partly rent, partly wages and partly interest.

Land and Rent

At the root of economics is the land question, and at the root of the land question is the law of rent.

Different portions of land have different productive capacities: to the same amount of cultivation, for instance, different acres will yield different returns, some yielding much, some little and some less. In the use of land for the satisfaction of their needs, people naturally prefer those portions that will yield the largest return to a given effort, and, as occasion arises, they gradually extend their operations to those portions from which the returns are smaller, to those from which the returns are smaller still, and so on. At any given time the least-productive land that offers a sufficient return to attract agricultural effort is the lower limit of agriculture and the datum-line of agricultural rent, from which owing to competitive demand, the rents of the more productive lands are graded upwards in proportion to their extra capacities. The payment of these higher rents tends to reduce the net rate of return obtainable from the more-productive lands to that obtainable from the least-productive land in use, and the extra capacities of these more-productive lands are absorbed by the extra rents that they command.

The law of rent, thus stated in relation to agricultural lands, applies to other lands also. As we approach centers of population, we find that lands yield a better return to building than to agriculture, that what may be called super-agricultural rents increase with the increase of the demand for sites, and that in the heart of a great city even a small portion of bare land may be worth a fortune. Moving in the other direction, we find that lands which are too barren or too remote for agriculture may yet be desired for grazing or for sporting purposes, or even for the pleasure of possession, and that they command what may be called sub-agricultural rents, decreasing with the decrease of the demand. This classification is of course only illustrative. There are no boundary lines. Cultivation is carried on within urban limits, houses are built in country districts, and agriculture is interwoven with grazing. The differences between the various lands are differences of degree, and through all the gradations it will be found that the rents of the various lands are roughly proportional to the returns that they yield to similar efforts, as compared with the return of the least-productive land in use.

The operation of the law of rent is qualified by many circumstances. The yields of different lands cannot be estimated exactly, the actual rent may vary with the other conditions of the tenancy, leases generally include improvements as well as land, and allowance must be made for the effects of custom, local opinion, personal relations and many other factors. But the law of rent is fundamental. It is the key to the position. It was first stated by Dr. James Anderson—a practical agriculturist—in a pamphlet entitled "An Inquiry into the Nature of the Corn Laws, with a view to the Corn Bill proposed for Scotland," published in Edinburgh in 1777, the year after the appearance of Adam Smith's *Wealth of Nations*. Neglected at the time, the law of rent—in the words of John Stuart Mill—"was almost simultaneously rediscovered.....by Sir Edward West, Mr. Malthus and Mr. Ricardo," about forty years later. Mill, who did much to make it clear, called it "one of the cardinal doctrines of political economy," and said that until it was understood no consistent explanation could be given of many of the more complicated industrial phenomena.[1]

Rent is thus the natural and inevitable outcome of the competitive demand for lands that return different yields to similar applications of labor and capital. It represents the surplus-value of the more-productive lands as compared with the least-productive land in use. There can be no question of abolishing it, nor would its abolition reduce the price of the products, because the prices of similar products are the same whether they are produced on land that produces much or on land that produces little, and the cost of production which regulates the

[1]*Principles of Political Economy*, 2, XVI, 3. J. R. McCulloch makes similar observations about it in his annotated (1854) edition of the *Wealth of Nations*, p. 452.

price of the product is the cost of producing it on the least-productive land on which it is commercially produced.[1] But it is important that this surplus value of land should be treated as public revenue, and that those who hold land should be taxed on the basis of its true value, whether they use it or not.

The effects of such a tax will be seen more clearly when it is borne in mind that the lower-limit of agriculture is not fixed but moveable, varying with the ratio between the supply of productive land and the demand for it. An increase in the demand or a decrease in the available supply tends to force agriculture down to land that yields a smaller return, to lower the datum-line of rent, to increase the rents of the more-productive lands which are graded from that, and to leave less of the produce to the producers—while a decrease in the demand or an increase in the available supply operates in the contrary direction. The demand for land is roughly proportional to the population; the natural supply of it is practically a fixed quantity; but the withholding of the land from use and the checking of improvements have the effect of reducing the available supply and hindering production. In order to secure the rights of the people to the land, to increase the available supply of it and promote production, to raise the datum-line of rent, to reduce rents generally, and to leave more of the produce to the producers, we need a land policy of the character already indicated.

Labor and Wages

The law of rent leads to the law of wages, because the natural wage of labor is the amount that the laborer can obtain by working for himself on such land as he can get for nothing, or on any more-productive land subject to the payment of its rent. As he need never work for an employer for less than that amount, that amount fixes the minimum rate of wages for the time being, from which the rates in various occupations are graded upwards,

[1]Thus, as Dr. James Anderson showed in 1777, it is not prices that are regulated by rents, but rents that are regulated by prices, which in their turn are regulated by the cost of production as above stated.

in rough proportion to the strength, skill, training or other qualifications required. Thus also, to repeat and extend what has already been said, it will be seen that an increase in the demand for, or a decrease in the available supply of productive land tends to lower the lower-limit of agriculture which is the datum-line of rent, to increase the rents of the more-productive lands which are graded from that, to leave less of the produce to the producers, and to reduce wages—while a decrease in the demand or an increase in the available supply operates in the contrary direction. Thus the first steps towards improving the condition of labor are to increase the available supply of more-productive land and to remove the hindrances that check production.

Many examples might be given to show how this relation between land and wages has been recognized in practice. The West India Royal Commission[1] found that the owners of sugar estates did not regard with favor the proposed opening of the Crown lands to the people, because "what suited them best was a large supply of laborers, entirely dependent on being able to find work on the estates, and, consequently, subject to their control and willing to work at low rates of wages," and they realized that it would become practically impossible for them to obtain laborers "at the prices which they were prepared, or could perhaps afford to pay," if the people had easy access to the Crown lands. The South African Native Affairs Commission[2] recongized that what made it difficult for the mine owners to obtain native labor for the mines was that the natives "had access to the land on terms which have enabled them to regard work for wages as a mere supplement to their means," and the Minority recommended "to do away with free land to the natives" as the economic strategy for compelling the natives to work in the mines on the mine owner's terms. The natives were saved from that fate by the maintenance of their rights to the land, and these rights are of the first importance to labor everywhere and always.

Adam Smith observed that one of the chief "causes of prosperity in new colonies" was the "plenty and cheapness of land,"

[1]Report, *Blue Book C.* 8658 (1897), paras. 116, 288.
[2]Report, *Blue Book Cd.* 2399 (1905) paras. 392, 413.

which led to the colonists giving "most liberal wages" to attract laborers, and led also to these laborers setting up for themselves and, in their turn, offering liberal wages to others.[1] Patrick Edward Dove showed that far the most important matter that affects the value of labor is the distribution of the land, that "wherever there is free soil, labor maintains its value," and that where laborers "cannot get the land to labor on, they are starved into working for a bare subsistence."[2] But it was left to Henry George, and it was one of his great achievements, to analyze the the relation between land and wages and to correlate the law of wages with the law of rent.[3]

Capital and Interest

Unlike Land and Labor, Capital is not a primary factor in production. It comes into being when the wealth that labor has obtained from the land is used to produce more wealth—when roots and grain that have been collected are used for planting and sowing, when animals that have been captured are used for breeding and milking, and when natural objects are made into weapons and implements.[4] These processes, and many others that are kindred to them, have developed with increasing rapidity, assisted by the discovery of the metals, the progress of invention, and the utilization of water-power, wind-power, and the power latent in wood, coal and other fuels. All wealth that can be used as capital, including mechanical energy, is obtained ultimately from the land. The land is the storehouse of capital, and the consideration of capital ought to

[1] *Wealth of Nations* (1776) IV. 7. II.

[2] *Theory of Human Progression* (1850) p. 406.

[3] *Progress and Poverty* (1880) Bk. III. ch. 6, 7.

[4] The first two of these processes appear to have been suggested by the germination and sprouting of roots and grain that had been stored, and by the breeding and multiplication of animals that had been captured, particularly those that had been captured young; see, for instance, *A History of Politics*, (1900), by Edward Jenks, p. 22, 43. The third appears to have developed from the primitive use of sticks and stones, those of the more covenient forms being gradually preferred, and becoming types to which others were afterwards shaped.

include not only the amount of capital that has already been obtained from it, but also the ever-increasing amount that will be obtained in the future.

Capital is wealth considered as an agent for the production of more wealth, and the mimimum rate of interest for the time being is determined by the amount of the additional increase, over and above the replacement of the capital, that can be obtained by applying the capital to assist production on the least productive land in use, or on more-productive land, subject to the payment of its rent. Thus the datum-line of rent determines the datum-line of interest, from which the higher rates are graded in proportion to the higher risks and other considerations. Thus also the interest on capital, which has been called "stored-up labor," fluctuates in the same direction as wages, rising as the lower-limit of agriculture is raised to lands which are more-productive, and falling as that lower-limit is lowered to lands which are less-productive. Thus also, to repeat and extend further what has already been said, it will be seen that an increase in the demand for, or a decrease in the supply of productive land tends to lower the lower-limit of agirculture which is the datum-line of rent, to increase the rents of the more-productive lands which are graded from that, to leave less of the produce to the producers, to reduce wages and to reduce the rate of interest—while a decrease in the demand or an increase in the available supply operates in the contrary direction.

The earlier writers on interest devoted much more attention to discussing whether interest was morally justifiable than to ascertaining its cause and investigating its character. Some of them recognized in a general way that the reason why capital could command more than would just suffice to replace it, was that land could be made to yield more than a bare subsistence to the laborer, but accurate analysis was not possible until the rediscovery of the law of rent by Ricardo provided the clue that has subsequently been followed. In the article on "Interest and Usury" in the *Dictionary of Political Economy*,"[1] for instance,

[1]W. H. Inglis Palgrave (1896) vol. II, p. 435.

it is said that the rate of interest on capital "is determined, on the analogy of Ricardo's theory of rent, by the competition of borrowers and its least productive employment. Hence, as a community increases in civilization, and capital has to be employed on less fertile lands and less productive investments, the return of capital tends to decline; in other words, interest falls." While recognizing this relation between rent and interest, we ought not readily to assume that progress in civilization necessarily forces industry to less-productive lands, or that the effects of an increasing population cannot be counterbalanced by an increasing efficiency in production, particularly if the general conditions are improved.

Interest, like wages and rent, is a natural and inevitable outcome of the fundamental conditions of life. There can be no question of abolishing it; it is bound to persist in some form or other so long as capital can be used to increase production by more than the amount required to replace it. The weak point in the present system is not that interest attaches to capital, but that capital is distributed inequitably owing to the inequitable distribution of the land from which it is obtained. The treatment of land as private property has led to the treatment of rent as private property, and to the further result that, when the wealth received as rent is used as capital, the interest on it goes to private individuals instead of to the people as a whole. There is also the aggravation that, owing to causes already mentioned, rent absorbs too large a proportion of the products of the land, and leaves too little for the producers, thus depriving the producers of a share that would otherwise belong to them and which they might use as capital, the interest on it being theirs also.

General Considerations

The present economic difficulties are largely due to the penalties on production, the withholding of land from use, and the treatment of the rent of the natural elements as private income instead of as public revenue. There must be a reversal of these conditions. Rent should be treated as public revenue by taxing those who hold the land acccording to the value of the land they hold, the withholding of land from use should be stopped by taxing them on this basis whether they use the land or not, and the penalties on production should be abolished by making improvements tax-free. These are the fundamental reforms, and they will prepare the way for improving the conditions of tenure, for simplifying title and for cheapening transfer. Nor must we limit our view to land reform at home. With a bad land system and an increasing population, the conditions of life in these islands would have become unendurable if we had not been able to exchange our manufactured goods for the produce of other lands, and it is vital that this indirect use of other lands should be continued and extended by letting trade have free course. The policy is a world-policy. In all countries the re-modelling of the land-system on these general lines would increase production, and the treatment of rent as public revenue would prepare the way for the abolition of taxes on trade and for giving free play to the processes that bind together individuals and nations.

The Encouragement of Production

The extent to which production will be developed is governed by the demand for the products and the increase of return that can be obtained by increasing the expenditure of labor and capital on the land—a consideration that brings us to what is known as the law of diminishing return. The operation of this law, as Henry George has shown in his chapter on "The Relation of Space in Production,"[1] is by no means limited to agriculture.

Even if abundance of suitable land could be obtained freely, the most convenient area for a particular piece of work would be that which was neither too contracted on the one hand nor too extensive on the other. In stacking a certain quantity of bricks or other materials, undue extension of area would increase the distances they had to be carried and expose too much of their surface, while undue contraction of it would entail excessive lifting of them and lessen the stability of the pile. In providing

[1] *The Science of Political Economy*, Bk. III, ch. 7.

a certain amount of house accomodation, undue contraction of area would necessitate building to an inconvenient height, while undue extension of it would have other disadvantages. In agricultural work, like growing a certain quantity of potatoes, undue extension of area would involve unnecessary labor in planting, hoeing and digging, while undue contraction of it would cause the plants to interfere with one another's growth. The fact that land has to be paid for and the undesirability of burdening an industry with too much rent are additional reasons against extending the area unduly.

When more labor and capital are expended on production, there is therefore a tendency to continue applying the further expenditure to the same land, so long as the increase of the expenditure can be made to increase the return in the same proportion as before. But, however wisely applied, there will sooner or later be a point beyond which any further expenditure on the same land will not increase the return in the same proportion. At about this point, known as the point of diminishing return, any further expenditure on production will be applied not to the same but to some other land which, in the ordinary course and for reasons already stated, will be land of lower productive capacity.

The taxation of improvements, by absorbing part of the additional return that would otherwise be the reward of the additional expenditure to which it is due, decreases the net return for that expenditure, brings the point of diminishing return nearer, checks the further development of that land,[1] reduces its yield, and has the same general results as a decrease in the available supply of it. Conversely, the untaxing of improvements, by letting the whole of the additional return be the reward for the additional

[1]The taxation of houses, for instance, checks building, the taxation of glass-houses checks intensive cultivation, and the taxation of farm-buildings checks ordinary agriculture. All such taxation is wrong and mischievous. There should be no restrictions on the development of land, beyond what are required for general convenience or public health or to prevent one portion of land being so used as to interfere unduly with the use of another, like regulations designed to prevent nuisances, to control offensive trades, to secure sufficient width for streets, and to limit the height of buildings.

expenditure to which it is due, would increase the return for that expenditure, would move the point of diminishing return further away, would promote the further development of the land, would increase its yield, and would have the same general effects as an increase in the available supply of it.

There is no need to discuss whether the taxation of land-values, by increasing the available supply of productive land, or the untaxing of improvements, by increasing production, would be the more important. The two are bound up together, they both operate in the same direction, and both of them are necessary to improve the conditions of life.—J. D. W.