

Suburban Land Speculation

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Source: *The Journal of Land & Public Utility Economics*, Aug., 1936, Vol. 12, No. 3
(Aug., 1936), pp. 221-227

Published by: University of Wisconsin Press

Stable URL: <https://www.jstor.org/stable/3158462>

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THE JOURNAL OF LAND & PUBLIC UTILITY ECONOMICS

AUGUST
1986



VOLUME XII
NUMBER 3

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By ROBERT WHITTEN*

EDITORIAL FOREWORD

THIS article by the late Dr. Robert Whitten gives us a striking picture of the social wastes of unwise land policies. It might be better, however, to say the losses resulting from the absence of land policies. Throughout our history we have followed "happy-go-lucky" methods in the utilization of our land. We have never had well thought out plans that deserved to be designated as social policies. Happily, we are just now beginning to formulate and put into operation land policies which will, on the one hand, prevent disasters such as have occurred in the past and, on the other hand, promote prosperity.

The present depression is, in my opinion, attributable first of all to the absence of sound plans for the utilization of land in its broadest terms, that is to say, our natural resources. This depression began with the land at least two or three years before the crash in 1929. It was keenly felt in Mon-

tana and elsewhere as early as 1926. The farmers felt it first and then it spread out in wider and wider circles and now the cities, in many cases, are in a worse plight than the farming areas.

A Congressional committee recently has estimated the losses resulting from the absence of proper planning of land uses at \$20,000,000,000. Speculation in land is only one of the bad features and after all, on the whole, perhaps a minor cause for the losses, vast as have been the wastes and suffering caused by speculation. Dr. Whitten's article has the strength of understatement.

I must add a few words about Dr. Whitten, who was my friend and associate. He stands out among the wise and modest men with whom I have been associated during my career. He was so impressed with what had yet to be learned that he was not too proud to go to school after he had already attained distinction in his chosen field as a planner. When I started the School

**Editorial Note.* Robert Whitten, Director of the New York State Planning Board, died on June 6, 1936 at Albany, N. Y. He was born in South Bend, Indiana, and was graduated from the University of Michigan and later took a Ph.D. degree at Columbia University. He first served as legislative reference librarian of the New York State Library, 1898-1907. This was followed by seven years with the New York Public Service Commission, during which time he published *Valuation of Public Service Corporations* (1912) and *Regulation of Public Service Companies in Great Britain* (1914).

In 1914 Mr. Whitten became identified with the city planning movement, serving first as secretary of the Committee on City Plan and Zoning of New York City, then as consultant to city planning commissions in various parts of the country. In 1933 he became consultant to the New York State Planning Board, of which he was Director at the time of his death. In addition to numerous articles and joint publications, he published *Economics of Land Subdivision* (1927) and *Neighborhoods of Small Homes* (1931).

of Land Economics in New York City in the autumn of 1930 he enrolled as a student. Naturally, he made an excellent record. Later our trustees appointed him as full professor in the School of Land Economics. This position he held until he was called to Albany in 1933 as consultant of the New York State Planning Board. He was advanced to the position of Director of the

New York State Planning Board, which position he held at the time of his death.

He was born in 1873 and had before him the prospect of many years of service with growing fame. His friends mourn the loss of a lovable personality, and, like others, feel that his untimely death is unfortunate for the country.

RICHARD T. ELY.

THE social wastes of speculation are well exemplified in the suburban land situation. Acreage that has no prospect of utilization for building purposes in a hundred years rises to absurd heights in boom years and sinks correspondingly with the boom's collapse. Some of it is subdivided into building lots. These lots are not needed. They are bought by people of small means as an "investment." In due course they are (or in all reason should be) abandoned because they are not worth the taxes that are levied upon them.

As shown in the careful study by Messrs. Simpson and Burton, there was excessive speculation during the period 1923 to 1928 in the Chicago region.¹ Farm lands that would not be needed for building purposes within any ascertainable period were bought and sold at values that would scarcely have been justified if they were dead ripe for building operations. Farms were subdivided and the lots retailed to hundreds of thousands of speculators. Most of those subdivisions are still vacant and a large proportion will remain vacant for the next 20 years at least. Many of the lots will doubtless be forfeited for unpaid taxes.

At the start of the boom much of this land was assessed at farm prices. With the progress of the boom, assessments

were gradually increased until in 1928 the assessments, while low as compared with growing speculative values, were several times greater than warranted by sound investment principles.

For Cook County outside the City of Chicago in 1928, 240,000 acres of vacant lands and 335,260 vacant lots were valued at \$593,000,000 or an average of \$1,794 per acre. Messrs. Simpson and Burton have estimated that the true value, speculative inflation excluded, did not in 1928 exceed an average of \$538 per acre, or but 30% of the assessed value. Here is a loss of \$410,000,000; it is some indication of the tremendous wastes incident to present methods of urban expansion. The 335,260 vacant lots were estimated to be more than sufficient to take care of probable growth for a period of 30 years. Most of these lots are a dead loss to the buyers. Doubtless many have been or will be forfeited for non-payment of taxes. The only possible use of the land was agricultural and that possibility has now been destroyed by the many small ownerships.

Value Stages of a Building Lot

Three important value stages may be noted in the development of a building lot: (1) the farm value of the raw acreage; (2) the subdivision value of the raw acreage; and (3) the value or cost of the lot when fully improved and built upon.

By the "farm value" of land is meant

¹ Herbert D. Simpson and John E. Burton, *The Valuation of Vacant Land in Suburban Areas: Chicago Area* (Chicago: Institute for Economic Research, 1931).

its normal or income value for agricultural purposes uninfluenced by possibilities of future urban use.

By "subdivision value" is meant the value of acreage when it is ripe for conversion into building lots.

By the "value or cost of the lot" when fully improved and built upon is meant the difference between the normal cost of the building and the total cost or value of the house and lot. The cost of the lot includes the cost of the raw land in the lot and its proportion of the cost of the land in streets and in neighborhood parks and playgrounds. It includes also the cost of lot improvement and planting and a proportionate share of the cost of street and park improvement or of other community services or amenities.

In a fairly typical case in 1930, near a city of less than 300,000 population, farm value might have been \$50 to \$200 per acre; value of land ripe for subdivision might have been \$1,500 an acre; and the value of a fully improved dwelling lot might have been \$1,200 (total cost of house and lot \$6,000). At six lots to the gross acre this gives a total of \$7,200 an acre for the fully improved land. It is difficult to get at the real farm-use value of suburban acreage. Its selling value, even if located much beyond the range of present subdivision activity, is affected by possible demand for various semi-urban, open-development uses and by a possible future demand for subdivision. These purely speculative future possibilities do increase the present sale value of the land; how much depends on the particular stage in the long-term speculative swing. In 1926 the speculative element was large. At present it is small.

Messrs. Simpson and Burton in their study of vacant land values in the

Chicago area estimate average farmland rentals at \$7.00 to \$8.00 an acre.² This was in 1928. The rich prairie soil of Cook County is unusually valuable for truck gardens. The lands around many cities would average much lower in farm value than those in the Chicago region.

Close-in agricultural land has little additional value, even for truck-raising purposes, because of nearness to the city market. The motor truck brings all land within a 50-mile radius into direct competition with the close-in land. Moreover, the close-in land is usually handicapped for agricultural use by the uncertainty of tenure. The capital invested in buildings, improvements, and soil enrichment may be lost if a subdivider concludes that he can make a profit by cutting the land up into building lots and retailing them to small speculators.

Based solely on a rental income of \$7.00 an acre, a capital value in excess of \$100 or \$150 an acre cannot be assumed. If taxes are 2% and interest on investment is figured at 5%, the capital value will be \$100. We are considering here value for farm uses only, with no consideration whatever of possible future urban use.

The Value of "Ripe" Farm Acreage

Assuming that, in 1930, \$50 to \$200 may have stood for the real capital value of an acre of land for strictly farming purposes in the environs of the typical city, what was the value of the farm acre when it was ripe for conversion into urban building sites?

The value of raw land when ripe for subdivision and development is fundamentally dependent on the same general factor that creates land value for other purposes: that is, a capitalization of

² *Ibid.*, p. 28.

income or satisfaction derivable from the highest use for which the land is suitable. Elements in the value of a tract of suburban land are: (1) value for agricultural purposes; (2) value for country estates; (3) value for various open-development uses, such as golf courses, parks, institutions, airports, heavy industries, etc.; and (4) value for subdivision and sale and use for house sites.

The value of acreage will certainly not be less than its value for open-development purposes. If acreage is to be purchased for subdivision into building lots, the cost of the acreage plus the cost of development and marketing cannot normally exceed the total sale value of the building lots. The sale value of the lots, in turn, though dependent on many factors, is fixed within certain limits by the economic status of the families that will buy the lots and build homes upon them.³

A study made in 1930 of sale values of acreage ripe for large-scale building operations in some 20 cities shows a marked variation in acreage values depending on the size of the city and the value range of the houses for which the tract seemed appropriate. The value range of the houses to be erected and sold was of more importance than the size of the city. It was found that for cities under 300,000 population the acreage values in tracts suitable for high-cost houses were normally about 2.5 times the values in tracts suitable for low-cost houses; and acreage values in tracts suitable for medium-cost houses were 1.5 times the values in tracts suitable for low-cost houses. For cities over 300,000 these multiples were respectively 3 times and 1.75 times.⁴

The value of acreage is, of course,

dependent on the profit that can be made from its subdivision and sale. This must in turn depend on: (1) the cost of grading, drainage, and street and lot improvements; (2) the cost of marketing; (3) the current sale price of lots of the most suitable kind; and (4) the number of such lots per gross acre.⁵

This same study also disclosed a fairly close ratio between the value of the lot and the value of the typical house for which the lot is most appropriate. It was found that the value of the lot averaged about 20% of the total value of the house and lot. There is, however, considerable variation in this relation. The normal range is clearly between 16 and 25%. In the cities of over 500,000 the median is generally above and in cities of under 300,000 below the 20% average.⁶

If the lot bears its full share of the cost of neighborhood or community utilities and services, including small parks, as well as all costs of lot improvement (grading, seeding, walks, and planting), these costs plus the raw land costs are quite likely to be at least 20% of the total cost of the house and lot.

While in a particular city at the height of the boom in 1925, the real investment value of suburban acreage might have ranged from a farm value of \$50 to \$200 an acre to a subdivision or conversion value of \$1,000 to \$3,000 an acre, the actual prices obtained for acreage in that year probably ranged from \$500 to \$6,000 an acre. In many cases these lands were bought at these inflated prices by subdividers who staked off the land into 40-foot lots, erected a few mammoth signboards, advertised an auction sale, and "sold out" in a few months' time at an average price per

³ Robert Whitten and Thomas Adams, *Neighborhoods of Small Homes* (Cambridge: Harvard University Press, 1931), pp. 29-37.

⁴ *Ibid.*

⁵ *Ibid.*, p. 31.

⁶ *Ibid.*, p. 32.

acre of \$10,000 to \$20,000. A large share of this spread between acreage price and subdivided price is made up of merchandising costs — advertising, salesmen, and office overhead. Quick sales at inflated prices require an expensive order of super-power salesmanship.

Under the influence of boom psychology the practically worthless so-called house-lot approaches the sale value of the fully improved lot in an established residential neighborhood and the so-called business frontages along the “main avenues” laid out on a subdivision plat take on really fantastic “values,” induced by a vision of their speedy occupancy by high-rental business buildings.

The Land Lottery

Most vacant lot buying is pure speculation—not investment. The buyer takes a chance at great and, to him, unfair odds. The total losses are much greater than the total gains. But it is the nature of man to be willing to gamble for high stakes. He is ready to risk a little to gain much, even though he knows he is risking more than the real odds against him warrant. This is true of the honest lottery where the total receipts from ticket sales are ordinarily much in excess of the disbursements for prizes. Land speculation, however, is a lottery in which the grand prizes are so enticing that under the influence of boom psychology men are willing to take odds of 5 to 1 when on any logical, actuarial, or probability basis they should be entitled to odds of 100 to 1.

There are certain distinct disadvantages of land speculation as compared with the ordinary lottery. The land speculator discovers that his purchase price is just a first payment. Thereafter he must make burdensome tax

payments and these payments increase as the assessments gradually catch up with the inflated values. Then there may be interest payments on a mortgage. The land speculator gets in and in most cases he cannot get out without sacrificing all he has put in.

The subdivider of unimproved lots is a merchant—not a speculator. He buys acreage at wholesale from farmers or large-scale speculators in order to be able to retail it in small lots to the little speculators. His business involves risk because he may overestimate the “sucker” market and a high-pressure campaign costs a lot of money. This risk must be compensated for by a high margin of profit. Hence the tendency to higher and higher acreage prices is somewhat restricted.

Of course, tax assessments follow, though with considerable lag, the inflation caused by speculation in acreage and vacant lots. The tax revenues derived from these inflated values constitute a large portion of the total tax revenues of many suburban towns. Indeed, it is a considerable item in the revenue of metropolitan counties and cities. These governments do participate very largely in the profits of the great American lottery of land speculation. The subdividers also participate in these lottery profits. The speculators who buy the lottery chances probably pay out at least \$10 for every \$1.00 that is returned in prizes.

But the tax revenue obtained is not all clear gain. Roads are paved and water mains laid at public expense to aid “development.” Scattered homes in scattered subdivisions increase the cost of most municipal services. Standardized street and lot systems, already discarded in good planning practice, will be quite obsolete in 20 or 40 years when the typical boom-period subdivision

will be actually needed for urban expansion.

From the standpoint of municipal economy an honest government lottery would probably be more profitable and dependable than the present tax on the capital value of vacant land. Generally speaking, the evils of gambling in lottery tickets are not as serious and far reaching in their social and economic repercussions as are those attendant on speculation in vacant land.

Taxes and Speculation

As to whether the tax on vacant land tends to diminish or increase speculation is an open question. On the one hand it is argued that a 2% tax on the capital value of the land is a very heavy burden and must tend to discourage the holding of vacant land for speculative purposes. It is doubtful, however, if under boom psychology the thought of the tax burden plays any appreciable part in limiting speculation. It probably is considered most by the speculator in acreage. But in boom times the chances of great gains seem so rosy that taxes appear quite negligible. The subdivider of unimproved lots does not have to consider taxes, because he expects to sell out before taxes are due. The small speculator in vacant lots, to whom taxes based on sale prices will be really confiscatory, apparently never gives the matter a thought.

On the other hand there is some reason to think that the taxation of land at its capital value tends to increase land speculation. Farm land for which there is a possibility of urban use within a period of 20 years does have a partly real and partly speculative capital value considerably above its income value for farm use. As farm land it may rent for \$5 to \$20 an acre. A rental of \$14 an acre will pay 5% interest and allow for a 2% tax on a \$200 valuation. But when

the assessed value becomes \$1,000 an acre and the annual tax \$20 the farm owner has to pay in taxes 43% more than the total rent. Under such conditions sale to some speculator or to a subdivider is the only solution for the farm owner. As land values increase, the tax burden becomes very heavy for the owners of large private estates and also for golf and country clubs. As a result, fine estates and golf courses are cut up into lots many years in advance of any real economic need.

The present spread between farm value and future urban value is so great as to handicap seriously the efficient utilization of a broad belt of suburban land for a period of 30 to 100 years. Even assuming that all land buying is based on a conservative consideration of probable growth and necessary carrying charges, a 30-year period of ripening is quite normal. An investor buying land for \$100 an acre can hold it for 40 years before his investment figured at 5% for interest and 2% for taxes or a total of 7% compounded will amount to \$1,500 an acre. If he buys at \$200 instead of \$100, this period will be 30 instead of 40 years. It is easy to see therefore that most suburban land, even without the stimulus of unreasoning speculation, will necessarily have a capital value substantially in excess of value for farm purposes. The land is partially sterilized so far as effective social utilization is concerned. To this evil must be added the really tremendous social and economic waste and wreckage of the subdivision lottery.

Practically the entire spread between farm value and acreage value when ripe for conversion into building lots is a surplus or residual value. It is not, in general, created by the owner; it has no ascertainable cost of production. It may have cost the owner in interest and

taxes either more or less than the amount for which it can be sold. The amount that the owner has thus invested does not bear any necessary relation to the amount that it is actually worth to the developer who converts it into building lots or to the small home owners who buy the houses.

It is entirely possible to assume conditions under which acreage ripe for conversion into building lots would possess little or no surplus or residual value above that actual income value possessed by the land when used for farming or other "open" uses. If, for example, the development costs are so increased by high standards of community services and the provision of trees, parks, and amenities that these development costs plus building cost and plus a minimum farm value for the land, produce a total cost equal to the price that can be obtained in the market for the completed house and lot, there

is no surplus remaining that can be used to give additional value to the raw land.

The present normal spread between farm value and value for building purposes can be reduced by social controls that will compel whoever undertakes the responsibility of the subdivision of land into building lots to assume also the responsibility of building the completed neighborhood with a full complement of utilities and community services. If this is done, the range of acreage value will be quite definitely limited. The developer cannot pay more than the limited margin between other necessary costs and selling price and the owner will not take less than the value of the land for agricultural or other semi-urban uses. Possibly by these increased development standards the cost of the raw land for low-cost housing could be stabilized at two- or three-fold its value for farm purposes instead of at 10- to 15-fold as it was in 1930.