

WHO MADE THE LAND VALUE?

By Stephen Hoskins / 28 February, 2022

It is the oldest rule in the property investor's playbook: location, location, location. Savvy speculators know that it is far more profitable to direct your dollars to a townhouse in a thriving city than to a mansion in the rust belt. It's also why decaying shacks [like this](#) can sell for ten times what the median worker earns. Property investment is much more about picking desirable locations than it is about the houses above ground.

So this leaves us asking: Where do land rents come from? What factors make land more or less expensive in different locations? Can land owners improve the value of their own land, or only change the buildings? When land rises in value, who gets the credit?

As part of a team who are building an [automated land valuation model](#) in Philadelphia, I have been reviewing the huge volume of economic studies which seek to quantify every imaginable variable which influences property prices. This article answers the above questions by exploring what makes land valuable, considering who creates this value, and identifying ways to allocate it to its rightful owner. Since the vast majority of land value is in [urban areas](#), in this article I'll concentrate on the factors that affect the price of land in cities.

Nature

Let's start with the obvious stuff. Imagine a generic plot of urban land which is for sale. Its physical features will clearly influence the asking price. Larger bits of land will be more expensive, as the seller knows that buyers will be able to build more housing on the site. Likewise, sites with [topography](#) which is amenable to construction will have higher value. Parcels in a [floodplain](#), hurricane tracks or at [risk of wildfires](#) will be less valuable because of these risks of natural disaster. Sites exposed to the coast [sell at a discount](#), but only in areas which believe in climate change. If the

parcel is somewhere with a beautiful view of the [beach](#), [mountains](#), [water or some greenspace](#), the seller will also demand a higher price.

What unites all these factors is that they are all inherent geographical features of the site and its surroundings. These aspects of land value are given to us by god or mother nature. Take your pick, they certainly predate humanity. Either way, we've finally found the one thing that the theists, atheists, and ayahuasca hippies can all agree on: these elements of land value are definitely not created by human effort, and certainly cannot be changed by the land owner on their own. Henry George opens *Progress & Poverty* by emphasizing this crucial distinction "*between things which are the produce of labor and things which are the gratuitous offerings of nature.*"

Government

Okay, so nature has given us this lovely piece of land. What other factors will make it more valuable? Government actions are essential here. [Being invaded is rather bad for house prices](#), so we're going to need a functioning government willing to enforce and protect the owner's property rights. Regulation of land use is intricately related to property prices, which is why decisions over upzoning are debated so fiercely. Individual properties do become much more valuable if given [permission to build](#) as much as the market demands. However, by lobbying for strict zoning on their neighbors' properties, so-called '[homevoters](#)' can create a scarcity of housing which boosts the value of their own land. Heritage designations also have the effect of [protecting land value](#). Planning which protects residential areas from [pollution](#) and improves [air quality](#) is observed to raise property prices. Similarly, policy which reduces [crime](#) also raises [house prices](#). Access to public [parks](#) and [lakes](#) capitalizes directly into land values, and home buyers compete fiercely for properties within the zone of a [high-performing school](#).

[Street design](#) also matters; property values tend to be higher in neighborhoods with good [street connectivity](#), plenty of [trees](#), and

which are [walkable](#) and friendly to [cyclists](#). Areas which are well connected to the rest of the city by public infrastructure like [transit](#) and [highways](#) will be priced at a premium, although this depends on how well the noise from [traffic](#) and [trains](#) is mitigated. Lastly, receiving a connection to [water & wastewater](#) infrastructure can more than double the value of a property.

All of the above factors clearly demonstrate that land values are utterly dependent on a wide range of government functions. Landowners have no more ability to increase the value of their land than a generic tenant does. Yet it is landowners who are the primary beneficiaries whenever government actions successfully produce safe, attractive and productive cities. Indeed, the success or failure of infrastructure projects or place-based policies is often explicitly evaluated by their [impact on local house prices](#). Rising rents are terrific for land owners in the area, but can burden and displace poorer tenants, which is a core mechanism of gentrification.

Society

There is one final factor which has a huge impact on land values: access to people. In countries [throughout the globe](#), you will find the highest land prices in the middle of the biggest cities, because people like to be around other people. Cities provide access to jobs, bars & restaurants, romantic partners & cultural activities, all right at our fingertips. Improved access to all of these social amenities is one reason why urban land is so valuable.

Cities provide economic as well as social benefits. Dense collections of workers and firms make us all more productive, in what economists call ‘agglomeration externalities’. [Thick labor markets](#) help make better matches between employers and employees. They provide workers with the ease of mind in knowing that they will have plenty of [other opportunities](#) if they happen to lose their job. Firms can access inputs more cheaply when their full range of suppliers are available nearby. Workers enjoy ‘knowledge spillovers’ which make them more productive and help them develop their skills [more rapidly](#).

While these benefits are all created by private individuals just going about their daily lives, access to them is capitalized directly into land values, in what is called the '[urban land premium](#)'. George was ahead of his time in emphasizing the capitalization of agglomeration externalities into land values:

Here intellectual activity is gathered into a focus, and here springs that stimulus which is born of the collision of mind with mind. And rent has increased accordingly.

As the modern economy grows increasingly reliant on high-skill innovation in industries like tech & pharmaceuticals, and as consumer tastes increasingly value the buffet of activities available in the city, the advantages of urban locations are growing ever stronger over time. This explains the relentless rise in urban land prices around the world, much to the glee of homeowners in these locations.

Yet again, we see that the value of a given piece of land is not created by the individual who happens to own it. Rather, the collective actions of society allows landowners to extract rents from the land. George again: "*The value of land [...] is not in any case the creation of the individual who owns the land; it is created by the growth of the community*". Indeed, even factors like having [friendly, well-educated neighbors](#) or even being [close to a church](#) can raise property prices. These are yet more ways in which landowners benefit from value at the expense of those whose actions created it.

Land owners do not influence the value of their land

The crucial point is this: land value is entirely created by nature, government, and society. Urban land owners have essentially no ability to influence the value of their own land. They can simply sit back and enjoy the land rents that are created by the efforts of everyone else around them.

Georgists recognise that many landowners do improve the value of their property, by building and maintaining homes and productive

businesses. We see the value as legitimately theirs, and we're not interested in taxing it at all. But buildings are depreciating assets, and most of the [growth in property values](#) actually comes from land, which the landowner does not create. Likewise, many homeowners feel that this isn't 'real' wealth, because they don't intend to sell any time soon. But these homeowners do get to enjoy the daily opportunities provided by living in that location, free of rent. When nearby land rents rise, it is a sign that the advantages of that location are also rising, as is the avoided-rent which the homeowner does not have to pay. Occupying a location excludes others from its advantages, which is a crucial difference between land (a natural resource of limited supply) and financial assets like shares. Homeowners also enjoy the security of being able to borrow against their property or downsize if they need some cash to open a business, pay a medical bill, or fund retirement. These are real advantages which accrue from the ownership of land, over and above the profits made when it is eventually sold.

In a society which prides itself on rewarding those who work hard, it is a glaring contradiction that [most household wealth](#) derives from passive ownership of a natural resource whose value is created by the collective efforts of the rest of society. These contradictions are made all the more offensive when we observe that land owners enjoy the value that land generates largely tax free, while workers' productive efforts are directly punished with income taxes. The average worker in the US pays a tax wedge of [28%](#), while households can accrue \$500,000 in capital gains on their home [without paying a cent in taxes](#). Across the OECD, only 6% of [tax revenues](#) come from property; more than half comes from income and consumption.

What's worse is that the actors who generate this value are not being compensated for their contributions. Mason Gaffney describes how public infrastructure projects, funded by taxes "[wrung from workers](#)," generate value which is privately captured by land owners. This process essentially redistributes wealth upwards, which is why [land rents](#) lie at the [heart of inequality](#). This gives property owners a direct financial interest in maintaining

restrictive zoning across the city, which creates a scarcity of housing, meaning that prospective homeowners must take larger mortgages than they would otherwise need to, and tenants are burdened by punitive rents.

Indeed, tenants have the worst of it under the current system. When they go to work, not only do they pay taxes on their earned income, but they must also pass a [sizable chunk](#) of their wages to a landlord for the mere right to occupy a patch of land near to that job. When their contributions to society make their city more desirable, they are punished with constantly climbing rents, which make it harder to stick around and enjoy what they've helped to make. "*The invariable accompaniment and mark of material progress is the increase of rent*".

The remedy.

To right these daily injustices, we must find ways to return land rents to the public. All humans have a moral right to share in the material wealth that was given to us by nature. Value which is collectively generated by society and through the government should be shared by all members of that society.

We have many mechanisms for capturing land rents available to us. Georgists prefer the land value tax (LVT), which charges landowners a fee in proportion to the value of their land holdings. We have seen that this value is directly attributable to the relative advantages offered by a given location. Because LVT is charged as a fixed proportion of land value, it has the desirable property of being more like a user charge: people who enjoy ownership of large parcels of highly desirable pieces of land will compensate society for generating their land value. Folks who wish to reduce their tax burden can do so by economizing on the amount of land they consume, or by moving to cheaper locations. For these reasons, and many more (watch for my future posts), LVT is widely [considered by economists](#) to be the best, or at least the '[least-bad](#)' tax.

Other mechanisms for land value capture include [betterment taxes](#), which recognise that a specific public investment has raised nearby

land prices and requires those landowners to pass some of their profits back to the municipality. Hong Kong's [Mass Rapid Transit Corporation](#) acquires sites close to planned transit stations and leases them back to developers once the station has been built. This has enabled them to operate entirely free of government subsidy, generating twice as much revenue in land rents as they spend on line construction. Value capture mechanisms can make infrastructure investment much more financially viable, and provide the government with a direct incentive to provide a [socially optimal bundle](#) of public goods.

Revenues from land taxes can be used to cut taxes on income, so that workers will get to see more of the wealth that they personally create. Or the revenues can be paid out as a UBI, so that as we all improve society, we will all get to share in the bounty. Property owners will have less of a motive to [vote for restrictive zoning](#) to generate scarcity rents; instead they will look for ways to use their land as productively as possible.

Land was given to us by nature, and made valuable by the actions of government and society. We must return this value to the rightful hands of the public. It is for this reason that Georgists seek to shift the tax burden off the backs of workers and onto land value, where it belongs.