Evolution of a Theory

by HARVEY SEGAL

THE theory of land rent has gone through successive transformations at the hands of successive generations of economists over the past two hundred and fifty years. The formal theory, as nearly as I can determine, had its origins in the writings of the great mercantilist economist and statistician, Sir William Petty (1623-1685). He established the principle that rent, whether paid in money or in kind, represented the net yield of the soil—that which remained after all expenses of production, including the consumption of the farmers, were paid.

This surplus, in Petty's view, varied with soil fertility and with superior locations, although, in his analysis, both factors were of subordinate importance. He and a number of the later mercantile writers believed the surplus farm land determined the rate of return on capital in general. Some of these, notably Nicholas Barbon and Sir Dudley Worth, saw in existence of rent an argument against usury laws. They identified land with what we would call capital assets, and which they called stock. This idea emerged again in a different form in the writings of Frederic Bastiat, Henry C. Cary and John Bates Clark—the last two of whom were americans.

A. R. J. Turgot, the celebrated French economist and government administrator, did much to generalize the theory of land rent in the early 19th century. He made land rent jointly determined by soil fertility, the entrepreneurial demand for farm land, and the proprietor's reservation prices. Land rent, in his opinion, was determined by the demand for and supply of rent.

Adam Smith carried on along the essential lines laid down by Turgot. He did, however, make a notable extension of rent theory to cover what he called ground rent and building rent, asserting that ground rent was a surplus in excess of a competitive return on the investment in buildings. Moreover, he asserted, and here I think he anticipated Henry George by a hundred years, "ground rent should be taxed separately from building rent." He believed that ground rent represented a monopolistic gain and was a most appropriate object of taxation since a tax upon it would not discourage further construction.

The revolution in the theory of land began the year after the appearance of *The Wealth of Nations,* when Dr. James Anderson, a Scottish agriculturist, linked the payment of land with diminished returns which resulted from a differential soil fertility. The theory of differential land rent, in which the existence of rents is attributed solely to soil fertility differential—or differences in the cost of producing agricultural products — was simultaneously developed by Sir Edward West, Robert Malthus and David Ricardo, all of whom published important pamphlets on the subject in 1815.

Rent, according to Ricardo, is "that portion of the produce of the earth which is paid to the landlord for the original and indestructible powers of the soil." He explained that rent was paid on superior land as inferior lands were successively brought under cultivation, and he further pointed out that rising rents were a concomitant of falling profits and wages. He believed in short that the yield of wheat on an acre of land governed the return on capital in general and determined the shares of national income going to wage-earners, capitalists and landowners.

Ricardo viewed rents as pure transfers, arising because of the differences in costs of production on different land. No rents, according to him, were paid on the margins of cultivation.

Rent was an important part of the theories of economic development held by Ricardo and John Stuart Mill, since they would tend to increase relative to all other incomes as population grew and the returns from the land continued to diminish. Henry George accepted the Ricardo-Mill theory of rent in toto—and I think the role he assigned to rent and land speculation in *Progress and Poverty* owes much to the Ricardo-Mill construction.

Actually there was a counter-revolution against Ricardo's theory that rent was an unearned increment. This had reached a high point by 1879 when *Progress and Poverty* was completed, although Henry George could not have been fully cognizant of the fact. With the rise of the neo-classical school in the 1870's, both in Europe and the United States, the attacks on the Ricardian theory of rent took different forms and was motivated by different ends. . . .

The most radical attack came from John Bates Clark, who paradoxically credits Henry George's book for the inspiration that led him to develop his version of the marginal productivity theory. Clark denied the indestructibility of the soil, except for spatial limitations. He held that both fertility and economic location are amenable to human decisions. Land, he believed, could be manufactured, and he denied that land was a unique factor of production.

In 1903 Alvin S. Johnson wrote a brilliant dissertation in which Clark's ideas, which had a powerful influence on American economists, were expounded. F. A. Felten and Herbert Davenport held similar views.

However the first volume of Alfred Marshall's great *Principles of Economics* had appeared in 1890. He synthesized what he thought of as the best ideas in both classical and neo-classical traditions, and one of the classical concepts which he retained and refurbished was the Ricardian theory of rent. He preserved the outer shell, namely the notion of an unearned surplus, and held that land rent was one species of surplus in a "genus" which he called producers' surplus.

Today the theory of rent is far from dead and has "by no means lost its vitality and instructiveness," though it occupies a rather lonely position in the textbooks.

The articles on pages one, three, five and thirteen reflect addresses delivered at the Annual Conference of the Henry George School in New Brunswick, New Jersey. It is unfortunate that they had to be so drastically reduced in length.