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# The value of land

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**Developed land is a major but neglected share of property holdings. In a new book, Alain Trannoy and Etienne Wasmer analyze this form of property, identifying its causes in ways that will generate discussion about its distribution—and possible taxation.**

Reviewed*:* Alain Trannoy & Étienne Wasmer, *Le grand retour de la terre dans les patrimoines* (The Great Return of Land in Property Holdings), Odile Jacob, 2022. 256 p., 24 €.

We begin with two caveats. First, this book is not concerned with farmland, but with the land upon which cities are built. Second, unlike housing, land does not play a major role in capital's return, as analyzed by Thomas Piketty. The topic of Alain Trannoy and Étienne Wasmer's book should thus surprise readers who are unfamiliar with urban economics--a fact, I hope, that will lead many to read it.

## The extraordinary value of urban land

Trannoy and Wasmer present a detailed panorama of the use and value of land in France, while also providing international data that allows for useful and informative comparison. For centuries, ownership of farmland was the foundation of Europe's social and political structure. In 1700, its value rose to seven times France's GDP (Piketty & Zucman, 2014). In 2019, the cumulative value of all land represented three times France's current GDP. Yet within these aggregates, things have changed

considerably. As Trannoy and Wasmer note, in 2018, developed areas represent only a small portion of all land--around 1 or 2%. This figure is comparable to what one finds in most of the planet's inhabited regions (Ritchie & Roser, 2013).

Yet the value of developed land comprises more than 80% of land's total value, whereas farmland represents only 9%. In French property holdings, urban land has thus replaced farmland. Unsurprisingly, the wealthiest households own the largest share of all real estate: the 10% with the greatest assets of any kind own 40% of the country's real estate (according to value) (p. 70). Even so, 61% of all households own some real estate.

It is worth remembering that, at the global level, only 3% of inhabitable land is considered urban (Liu et al., 2014). One can thus legitimately ask: if cities and towns occupy such small areas, why is housing so expensive, at least in large cities? It should immediately be noted that this phenomenon is hardly unique to France.

A building consists of two parts: land and structures built on this land. Many believe that a building's value is determined by the building. In fact, the opposite is often true. If housing prices regularly increase, it is not because of construction costs, which have risen little. The reason must be found elsewhere. Because the cost of built-up land can usually not be seen--land and structures being frequently inseparable--it can be easily undervalued.

In 2019, the share of land in the total value of French real estate was 44%, which corresponds to about three times the GDP. The trend is similar in the United States, where the share was 46%, and Switzerland, where it reaches 53%. *Land has returned to property holdings*, Trannoy and Wasmer declare, *but the land in question is urban land*. They note that "these wealth assets are not very visible," which probably explains why they fail to register in debates over wealth distribution.

Furthermore, land value as a share of real estate holdings has continued to increase in most developed countries. For example, Knoll, Schularick and Steger (2017) show that, between 1945 and 2012, more than 80% of the average increase in housing prices in the fourteen OECD member states is due **…** to growth in the price of land. How can this trend be explained?

# Real estate value and its rise

Urbanization happened. The global urban population is over 50% and, in developed countries, it exceeds 80%. Increasing population density in urban metropolises has contributed to a notable improvement in living conditions, allowing access to a wider range of opportunities. It is well established that labor productivity is greater in large cities than small ones, even if one considers the spatial distribution of human capital. Many factors explain these differences in productivity (see Fujita & Thisse, 2013, for a more in-depth discussion of these processes). One strikes me as particularly important. The rapid circulation of information and knowledge in innovation-friendly settings ensures higher productivity for skilled workers (it is too soon to predict telework's impact on productivity gains due to proximity). This results in higher salaries. These exchanges are particularly intense because they occur in dense networks, which explains why a greater share of skilled workers reside in cities. The distribution of human capital accounts, moreover, for half of the spatial disparities in France (Combes, Duranton & Gobillon, 2008, 2015). The pull of higher salaries is strengthened by the availability of consumer amenities that are less accessible in small towns.

The main cause for the rising price of land is competition for real estate in the densest areas. Specifically, land is most expensive in major cities, and, in the latter, it is in urban centers that the most expensive land is found. For example, the cost of a lot in the area delineated by a three-kilometer radius from Notre Dame Cathedral in Paris is, on average, twenty times greater than lots twenty kilometers away (Chapelle, Trannoy & Wasmer, 2022). The same phenomenon can be observed in most large cities. The distinguishing factor, in this instance, is proximity to major urban centers.

When one thinks about it, it is clear that "good" locations are important, for business as well as for living conditions. But what is a "good" location? The criteria that immediately comes to mind are proximity to one's workplace, consumer services and entertainment, public transit, public services like schools and hospitals, and, finally, a neighborhood's architectural quality.

Urban economics posits that the ability of potential landowners to pay depends on their income as well as their preferences. The real estate market works like an auction, in which each lot goes to the highest bidder. In this system, "good" locations often go to the richest and the worst to the poorest. Spatial segregation in cities thus mirrors income disparities (Fujita & Thisse, 2013).

The ability to pay is also highly dependent on where a building is located. Its desirability is thus determined by its position relative to other factors. These can vary considerably and have positive or negative effects on a site's desirability. In short, a location is (under)valued because a large number of economic actors made it (un)desirable, whatever their intentions may have been.

In short, *the price of land accentuates the advantages and inconveniences of the location in question.* This fundamental mechanism is too often overlooked. As an example, consider housing situated near subway stations, whose prices are rising due to better access to the subway. Houses located near airports, however, are declining in value. As we have seen, the capitalization of real estate can be positive or negative.

A corollary is immediately evident: landowners often benefit from decisions made by numerous actors, though the landowners played no role in the rising value of their assets brought about by this array of decisions. Furthermore, these profits **…** escape taxation, even when they are extensive, because they cannot be observed directly.

## Is it time to tax land?

It is for these reasons that Trannoy and Wasmer propose a tax based on the value of land rather than the buildings, whose value is determined by their owners and the decisions they make. Unlike financial assets, landed capital is immobile and cannot be hidden. Trannoy and Wasmer's tax would apply to occupied land as well as vacant lots, and to land connected to rented or empty buildings--thus creating incentives for such land to be used at a time when it is relatively scarce. Trannoy and Wasmer also show that the revenue generated by this annual tax, which they propose setting at 2%, would allow reductions on taxes on work and capital, thus promoting growth. This tax must be independent of buildings and universal. It is a fair tax, as those who benefit from land value gains would pay the most; and it is an efficient tax, because it does not lend itself to fraud.

Due to a lack of data, Trannoy and Wasmer do not address how their tax would be geographically distributed. Land value varies considerably across cities, and even between different sites in the same city. Some sense of how this distribution might work can be seen by considering the case of the United States, where land value in the

five largest cities represents approximately half the total value of real estate. It is easy to imagine the disproportionate place that Paris would occupy were the tax implemented in France, where the contribution of some localities would be negligible. Because the most expensive lands are often located in the most prosperous regions, great disparities in the revenue generated would simply reflect the organization of France's economic space.

The price of developed land is not, however, due to urbanization. In many cities, an artificial scarcity results from Malthusian policies that limit new construction. It is worth recalling that the inhabitants of a community are often uninclined to encourage the establishment of new households, a trend that condemns new arrivals to living in places that are often very distant from their workplaces. It is necessary to densify inhabitable areas by facilitating new construction, allowing young households to choose residences that best correspond to the geographic distribution of jobs. At the same time, one must fight unregulated urban sprawl. It is worth noting that the practices employed at the local level to limit construction are found in different forms in the United States and the United Kingdom, countries deemed far more liberal than France. Furthermore, unwarranted rent control, which is so popular with many French people, has discouraged new housing construction, thus exacerbating the problem of high rents and prices.

Trannoy and Wasmer's book contains a great deal of information that is poorly known, even to economists. It launches a fascinating debate about a question that is important yet neglected at almost every level of society. The French do in fact have a strong preference for real estate. As Trannoy and Wasmer note, the value of real estate holdings in France is six times that of productive capital based in the country itself, compared to ratios of 2.4 in Germany and 3.6 in the United Kingdom. These differences are by no means accidental. They express a system of values rooted in the history of France, which, compared to its neighbors, has been less inclined to commerce and industry.

To conclude, it is worth recalling--as Trannoy and Wasmer point out--that the idea of a 100% tax on land generated income is not new. It goes back at least as far as the American economist Henry George, who, during the second half of the nineteenth century, saw it as an efficient means to finance public services. More recently, in 1990, American economists--including several Nobel laureates--recommended that Mikhael Gorbachev not privatize Russian land, as its value primarily reflected the activity of

the totality of economic actors. The ideas explored by Trannoy and Wasmer are important and are likely to be widely debated.

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