

**AN ARISTOTELIAN CONSTRUCTION OF THE
SOCIAL ECONOMY OF LAND**

By

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CERTIFICATE

I certify that this thesis has not already been submitted for any degree and is not being submitted as part of candidature for any other degree.

I also certify that the thesis has been written by me and that any help that I have received in preparing this thesis, and all sources used, have been acknowledged in this thesis

.....

Garrick R. Small

To Bonaventure and Anthony who
considered these things long before I did *ad
majoram Dei gloriam.*

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I would like to thank my good wife for her support, encouragement and tolerance through this project. She appears to have married a professional student but has adapted to her penance quite well.

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Abstract

Aristotle's metaphor for economic relations was the household. Although the household is engaged in the material activities of internal production, consumption and exchange which are economic, its fundamental connections are social. Social dynamics, including care, respect, authority, loyalty, charity and self-restraint are the motivations within the household. These are all virtues in Aristotelian terms and can be grouped under the more general social virtue of solidarity which is the intention to act in support and draw closer to the other in relationship in such a way as to become more perfectly human. An economics based on this family metaphor will be socially grounded, it is social economics. A key identifier of social economics is its capacity to realise the common good. This thesis is an examination of the contribution of property in land to the common good leading to the identification of the location of land within social economics.

An Aristotelian methodology has been adopted for this thesis, following an examination of its component parts and comparison with alternative methodologies. While the defense of the methodology is not exhaustive, it is sufficient to provide reasonable justification of Aristotelian realism and point out some of the shortcomings of competing approaches. Aristotelian realism is accepted as employing an acceptance of essences, the validity of abstraction, and the importance of observation. Contrasted to positivism, Aristotelian realism accepts knowledge that is not simply observation-based, especially the possibility of the knowledge of essences.

Cultural practices in land have been reviewed in order to observe the anthropology of land property. It has been found that the great majority of cultures surveyed have adopted institutional structures with respect to land property that do not privatize income flowing from land assets. The only counter examples, apart from the modern West, were cultures that had flourished but were near the end of their period of cultural dominance. Modern Western land practices have been shown to be no more than about five centuries old, and have been associated with the introduction of unemployment, especially evident in England. The sociological notion of cultural universality has been considered, along with other concepts relevant in the interpretation of the cultural data.

Property theory has been reviewed. This includes ancient positions on property as well as modern. Islamic property theory has been included in the review in order to broaden the cultural base. Ancient Western property theories have been shown to be divided between simple acceptance of the fact of private ownership, especially

evident in Roman law and early modern practice, and a more complex theory of ownership first articulated by Aristotle. Aristotle's theory of ownership was a dual principle of private ownership but common use. The Aristotelian position was developed by St. Thomas Aquinas in the Medieval period. St. Thomas recognised that property in external property was naturally for common use but privately owned by convention. John Locke attempted a labour based theory of absolute private property and Adam Smith returned to the positive fact of possession. The Islamic position straddled the Lockean and Thomistic. Modern property theory is a development of the Smithian identification property as a fact of society.

Apart from the institution of individual private property in land, several other economic institutions mark modern Western economics. The most important of these is the free market. The theoretical foundations of the free market have been examined and have been found to be based on moral foundations. The components of market theory have been reviewed and significant shortcomings have been revealed. The theory of supply has been found to contradict practice and the commonly portrayed market functions that are asserted to depict market behaviour in efficient circumstances have been shown to be in error. Capitalisation has also been reviewed and its dependence on the risk-free real rate of return on money loans has been explored. The moral problem of usury has been introduced and linked to capitalisation, but not taken beyond recognition and defense of the fact that it is a social artifact rather than a product of economic forces.

The critical factor in the operation of the market was shown to be its inclusion of demand in the development of prices. In the absence of theoretical support, the acceptability of the market was tested empirically by surveying attitudes to demand based pricing. Three hundred and forty Sydney home-owners were asked ten questions regarding situations where prices and profits were linked to demand or price. The data was analysed and found to lend support to the hypothesis that demand-based pricing did not have community support.

A general theory of property was constructed from human nature and the nature of land. It was then used to develop an ethical structure for the pricing of wages, land and products. It was argued that property rights in labour were fundamentally different to property rights in land, the former being natural and the latter being conventional. It was also evident that the market was an inappropriate instrument for the determination of wages, but appropriate for the determination of commodity prices. Land was recognised to be the gap between wage price and commodity price.

Ricardo's rent theory was reviewed as a mechanism for pricing land income. Various aspects and implications were considered and it was recognised that in a

closed land market the returns to land competed with the return to labour in a manner that was better explained in political terms than economic. Despite its importance in social economy, the operation of Ricardian rent theory is obscured other mediating factors. It has also been used as the central theory in a protracted political debate over the taxation of land. Both of these issues have contributed to the the marginalisation of interest in rent theory and a degree of suspicion as to its validity.

A behavioural experiment was run to examine the validity of Ricardian rent theory within the confines of its own assumptions, which are basically those of an efficient market and the recognition that land has varying productivity. The results of the experiment lent strong support to the theory but highlighted the conventional nature of the return to labour. One of the shortcomings of Ricardian rent theory is its assertions regarding subsistence wages, and there was evidence in the experiment that did not support this aspect of the theory.

The significance and construction of subsistence wages were specifically reviewed and also other sources of economic rents. An analysis of non-land economic rents revealed that they were either land-like, transient or politically maintained. A theory of supply was developed from a rent base that was argued to be causally accurate and returned a monotonic upward curve consistent with practical observation.

The implications of the political economy of the findings were reviewed. Some major traditions in economics interpreted in terms of the ethical issues revealed. The thesis concluded that many cultural resolutions of the property problem are possible, however they must conform to ethical fundamentals that may be paraphrased in the notion of solidarity. Suggestions for possible corrections or improvements to specific existing practices and policies were developed.

Chapter 1

Introduction To Property in Land

...property is the first and most essential element of justice; justice is the pillar on which society rests; and society, in its turn, is necessitated by the essential features of human nature." (Buckle 1991, p.2)

1.1 BACKGROUND

Property is a very general concept. People have many properties. A property of Socrates was that he was mortal. A property of a thing is a part of its particular being. To remove some property from a thing is to change it. As perfections, properties expand the being of the thing to which they are attached. Humans have long maintained the practice of taking to themselves properties which are not theirs by nature. Of these, property in land is the most significant in terms of its impact on human ability to manage material needs.

Land is not proper to humans personally, because it is not part of the specification of what it is to be human. It is proper to them in common, for all people are born into a material world and without it they cannot live. Life is a property of the human person, and so to deny people a common right to the material world is to risk constraining their life. When a person takes land as a personal possession, the person expands his human capacity to provide for his material needs and the needs of others. This is a good thing, and one which has been argued to be most appropriate to human nature as it is currently found. Humans are social by nature, the convention of taking private property in land is an important and necessary motivator for its responsible utilisation. As a conventional property of individuals, it does not extinguish the natural common entitlement of people to the world in which they find themselves. The resolution of this tension between the conventional rights and the natural responsibilities of property in land underlies the problem of economics. It is the problem that this thesis attempts to enlighten.

Aristotle considered that human nature was such that the most important human pursuits had little to do with material issues. Intellectual, social, artistic, spiritual and philosophical objects have greater interest to the human person because they exercise his most perfect faculties. While Aristotle realised the importance of these higher things, he was also a practical enough person to understand that they were only achievable when people had reached a satisfactory resolution of their material desires.

Aristotle understood that the economy existed to solve the material needs of society and free it to pursue these higher goals. The contribution of economics to human flourishing is therefore something more than the futile attempt to sate the infinite appetites of humanity that its modern construction asserts.

Marx took Aristotle's insight into the lofty possibilities of humanity, but, disillusioned by the corruptions of economics evident in his time, inverted it. For Marx, production was everything, in a world that was only material. Aristotle's higher pursuits were the tricks of a parasitic class of oppressors used to exploit the workers. The working class in his adopted England did not have time for culture, nor reason to trust an established religion whose head was also the political leader of a realm of unparalleled wealth that impoverished its own and sent them to prisons the size of colonies. Regardless of one's agreement with Marx's materialistic reading of humanity, his suggestion communicates the importance of economics in society and its capacity to influence other spheres of human life. A disordered economy stunts both its immediate victims, usually the poor, and society as a whole.

The discipline of economics was initiated by Aristotle within his works on politics and ethics, implying its location within the sciences. Aristotle's understanding of economics was based on the metaphor of a well run household, which subtly conveyed not only the need for material thrift, but also the context of human relationships within which economic understanding lies.

Households are families, bound primarily by relationships of care which is itself derived from love. These relationships are manifest in the allocation of both toil and material rewards. While a sound upbringing dictates that one should learn the virtue of working for one's supper, within a family this principle is commonly put aside for those too young, too old, or otherwise incapable. These earn the right to their supper merely by their membership of the family, or more generally, by merely being human. The material dimension of the household, *qua* family, is the optimum satisfaction of its members' needs through the toil of those members best suited to the work necessary. This optimum satisfaction of the needs of the group is understood today as the material dimension of the common good.

The common good is therefore the motivator behind the toil of those in the group (family or society) whose efforts benefit others, apparently gratuitously. Because it is inconsistent with our native inclinations, it must be consciously willed. The decision to will the common good is itself based on the nature of the family, in particular the bonds that unite it. Contrary to Marx's mythical genesis of family relationships originating as

the result of conflict¹, common experience, especially between parents and children, demonstrates otherwise. Parents love their children in a unique and powerful way and will their good, even if such a willing involves self-sacrifice. For this reason, despite Marx's visible debt to Aristotle, his methodology departed from *The Philosopher*² in favour of an Hegelian anthropology.

Aristotle's understanding of economics is therefore implicitly based on love between economic agents, though in his time there was no reason to explicitly examine the point. In his time, the spontaneous and self-sacrificial care shown by parents for their children, and between adult siblings was an uncontentious characteristic of human nature. This is a difficult suggestion to make in a Western culture that is dominated by economic motivations that render relationships more as contests of exploitation of the other. Both socialism and *laissez faire* capitalism by-pass Aristotle's invitation to understand sound economic relationships as being based on the personal willing of the good of one's neighbour, which is the social expression of economic motivation that is modelled on the family. In contemporary terms, at the level of the community, this notion is best expressed by the term *solidarity*. Solidarity is currently being used to signify that human motivation, based on the intention to move closer to those with whom one has dealings by willing their good, and in so doing drawing persons closer into human community.

Aristotle's economics is therefore social at its core. Its dynamics have been reflected in the economic behaviours of several non-Western and pre-modern cultures. By contrast, much of the economic behaviour and theory of the past several centuries in the West has been motivated by individual self interest, on the basis that a society filled with self-satisfied economic actors would be economically optimised as a whole. Despite the assertions of Smith's *Invisible Hand* and more recent developments along the same lines suggesting that self-interest will produce the common good, history seems to have been rather niggardly in providing concrete examples.

By adopting Aristotle's concept of economics, the common good enters the discipline. Socialist thought pursued roughly this same direction, hence its name, though it did so by adopting two problematic premises. Firstly, it ignored the metaphor of family, with its essential dynamic of charity, replacing it with the dynamic of conflict. Secondly, it invented a notion of property that in practice replaced the property owner with the state. It cemented both of these propositions in place through a combination of speculative theory and fanciful invention. Hence the family was re-framed to have developed from warring between its members that led to an uneasy and

¹Although this view was best expressed by Engels, commentators recognise that Marx was by no means adverse to it (Tong 1992)

²Aristotle

unnatural status quo based on power balances and property rights that were created as a result of the subsequent slavery of the weaker family members (Everling 1997; Marx and Engels 1968). This is not the sense of *social* adopted in this study.

Within economic enquiry, property is an important starting point. Liberal capitalism is based on a theory of property affording unrestricted title, while socialism follows a theory of property, linked through the labour theory of value, that denies private property in productive assets. Title to property can be broken into two parts, that attaching to the fruit of labour, and that over valuable factors of production that have no labour content. There appears to be little debate over the right to property resulting from labour. Both major positions accept it, despite its actual proportion within the final product being in continued dispute.

Title to things that are valuable, though not the result of human agency is more contentious, and constitutes an issue that has been resolved in varied ways by various cultures. These things constitute the factor of production that Adam Smith denoted as *land*. By land in an economic sense, Smith meant all resources that did not contain a human component in their production³.

Hence, the social economy of land appears to be central in the resolution of the economic problem. It concerns the issue of property rights, problem of value and the overarching issue of the contribution of property in land to the common good. It is very possible that more than one practical method of resolving the issue of the social economy of land may be valid. Several different approaches are in evidence, and their successes and failures deserve attention.

For example, there is a current global interest in the land title rights and aspirations of indigenous peoples. These cultures display an extraordinary essential similarity in their fundamental approaches to land, despite their geographical isolation. Likewise, pre-modern practices in those cultures that are the forebears of what is now known as the West, evidence a treatment of land that is very different to today. In many ways these are more closely aligned to contemporary indigenous peoples. The strength of socialist thought must be recognised as a form of rebellion against liberal private titles to productive capital. Although Marx did not pursue the issue, by accepting labour title while rejecting title to capital, he implied a rejection of the unproduced component of capital, i.e. land⁴.

³In this context, actual blocks of land may include a manufactured component, as in the case of farming land obtained by draining swamps. Conversely, moveable things, such as wild sheep, are land also, because they have not been produced by human husbandry.

⁴This perspective needs to be explored cautiously. Marx explicitly denounced what may be interpreted as the failure of the just wage principle in suggesting that the capitalist profited through buying labour at its cost value and selling it (embodied in the product) at its use value. This is arguably true. While this argument does not make explicit reference to the contribution of land in the process, it could be

As well as this major attack on Western liberal economic belief, there have been several others. Several writers have called for a return to small (family based) holdings, usually arguing from what could be termed a political perspective⁵. The best developed critique of modern Western land practice has been developed from the thought of David Ricardo and J.S. Mill by the American political economist Henry George. Known as Georgism, this system of economic thought closely resembles Smith's liberal capitalism, with the exception that George and his followers argued that the total rental value of all land should be taken as tax, thereby effectively nullifying its capital value (George 1879/1992). This position is based on a rejection of the private right to rent from land. It may be correctly described as the socialisation or nationalisation of land rents. While it technically does not reject private land ownership, it implies the conversion of land titles from freehold into perpetual state leasehold title.

State leasehold titles, as exist in many parts of Australia, are often the result of the success of Georgist thought, as is the tendency to fund local government from rates on the unimproved value of land. The Australian Capital Territory, which contains the nation's capital, Canberra, was designed and developed around leasehold title that was intended to make the capital self-funding (Brennan 1971).

Despite certain successes, Georgism has attracted a vast torrent of criticism, ranging from the entire neo-classical movement (Gaffney 1994), to the Pope of his time⁶. The difficulty with George's movement is that in focusing on the taxation of land, it has diverted attention from interest in the underlying validity of the theory it employs. In particular, George's appropriation of Ricardo's Law of Rent has meant that meaningful study of this supposed relationship has been discouraged. In general, Georgists adopt this teaching of Ricardo without question, while his detractors ignore it.

Interesting questions regarding the validity of Ricardo's Law of Rent, its usefulness in developing an understanding of the social economy of land and even what this may suggest regarding the nature of laws in economics have therefore tended to be ignored.

It is suggested that due to the importance of land as a factor of production, the development of a robust theory of social economy should begin with this element. The nature of property in land, its contribution to production and consequently its claim for a return, its just value and its capacity to provide for the common good are all a part of

suggested that one of the main reasons that the capitalist can achieve this revaluation of labour is through the control of the land component within capital.

⁵Wilhelm Roepke, G. K. Chesterton and E. F. Schumacher are amongst these

⁶Most commentators consider that the references to the right of individuals to own land found in the papal encyclical *Rerum Novarum* of Pope Leo XIII was aimed directly at Henry George, and George recognised the attack himself and wrote a book specifically to deal with what he considered to be the Pope's misunderstandings. A supporter of George and Catholic priest, Fr. McGlynn, was subjected to close Vatican scrutiny of his Georgist position and found to hold nothing contrary to Church teaching.

the social economy of land. These rely significantly on the balance of return between land and labour that is the question allegedly answered by Ricardo's Law of Rent.

Moreover, while Ricardo's Law may be empirically evident in behaviour, there remains the underlying issue of the meaning of economic laws. This issue relates to human action, specifically the operation of human will. Ricardo was following in the French Physiocrat tradition, both in method and content, and his understanding of laws was set in the Enlightenment paradigm of human nature. Under this paradigm, human nature was knowable by observation of human behaviour, and human behaviour was the result of rational decisions based on the individual's circumstances and history. The former belief eliminated a formal need for interest in the common good and the latter eliminated human free will.

This conception of human nature has attracted considerable criticism. Most people accept the notion of free will, and much of what is commonly recognised as human nature is beyond the reach of perception. Hume's moral sentiment was itself a strategy for overcoming the glaring inadequacy of Enlightenment strong form empirical epistemology. However, the positing of an inner sense to enable the direct perception of a commonly accepted part of human life, i.e. knowledge, that was not otherwise perceptible (therefore knowable) was transparently begging the question. It is beyond the scope of this study to exhaustively investigate the nature of free will, however, it will be argued that there is a strong enough basis for its acceptance.

On the other hand, it is not clear that the acceptance of free will necessarily eliminates the possibility of economic laws. Perhaps these identifiable tendencies in human behaviour reflect laws of a different type to those anticipated by the Enlightenment thinkers. If this is the case, then conclusions based on the identification of these tendencies would not be ill founded, although their moral foundations would deserve careful investigation. For example, the familiar market functions of supply and demand, with their respective positive and negative gradients, may constitute laws of economic behaviour. However, there may be reasons for these empirical gradients that render them unsuitable for adoption for economic decision making. For example, if the shape of either function was the result of market imperfections, their force as a cause of ethically justifiable prices would be compromised.

These are methodological issues, and neo-classical economics has spawned an entire body of its own methodological critique, the most penetrating of which has welled up from within its own ranks (Boland 1992). If the positivist methodology underlying neo-classical economics is capable of demonstrating its own shortcomings, then the direction forward implies a revised methodology. The socialist alternative is hardly appealing, despite its explicit attempt to address to social failure of liberal capitalism.

Close analysis reveals considerable similarity between the two that diminish the strength of their claim to be the only possibilities. The challenge is therefore to investigate beyond these systems, to identify the methodological issues that can produce a robust social economy that is truly human.

The Austrian school attempted a validation via various degrees of subjectivism. However, it will be seen that this does not address some of the necessary metaphysical requirements of the science. Several other significant attempts have been made including several social/political movements including Distributivism, Georgism and Douglas Social Credit. Many other notable writers, such as Christopher Dawson, Hillare Belloc and G. K. Chesterton have contributed to the debate demonstrating that the economic problem is partially a problem of culture. Most of all, these men appeared optimistic that economics need not be a dismal science. Most of these movements and writers also maintained a special place for land in the order of political economy.

The Aristotelian system is based on ethical and metaphysical propositions and structures that are quite distinct from those fundamental to the major contemporary positions, and although this has been recognised as the reason it has been largely ignored by modern economics (Meikle 1995), it would appear to be a strong contender as a genuine methodological alternative. This is especially evident when it is recognised that the entire Enlightenment position upon which neo-classical economics is built, was developed as an alternative to that development of Aristotelian thought that was Thomistic Scholasticism⁷.

1.2 STATEMENT OF THE PROBLEM

The basic problem that emerges from these considerations is the following:

Are the fundamental ethical principles governing the social economy of land knowable, and, if so, what are they?

Although the problem appears to have two parts, one cannot be approached without the other. To some extent, a reasoned statement of the principles is proof of their existence and acceptance of the possibility of their existence is a pre-condition of enunciation. The problem is methodological, and is in no small way complicated by the modern Western cultural context in which it is being presented. For this reason the problem requires close attention to methodology and will use cultural contrasts where ever possible reach beyond its own cultural limitations.

⁷This aspect of Enlightenment thought is especially evident in the writing of David Hume, *the Father of British Empiricism*, whose object was explicitly the unseating of Scholasticism and its metaphysics.

The problem may be approached by dividing it into three specific sub-problems as follows:

1. *What are the natures of, the relationships between, and the limits to, the various dimensions of private property rights, especially in land?*

Economic theory is based on notions of ownership and property (Nomani and Rahnema 1994). Without ownership, trade is meaningless. Early European economics was based on a dual theory of ownership that validated private ownership but made it a moral duty for use to be in common (Aquinas 1981). This dual nature of productive property can be seen today in productive capital assets. These serve the common good through the provision of employment and products which both benefit far more people than the owners. Post-Renaissance commerce was characterised by private ownership without the necessary obligation for common use and gave rise to the commercial capitalism of the Mercantilists (Fanfani 1939). Theories of ownership were revived by the political economists and took one of three courses: (1) total despotic private ownership (Smith 1778/1910), (2) rejection of ownership of the means of production (Marx 1957), or (3) a separation of property rights between products and land (George 1879/1992; Nomani and Rahnema 1994). In one sense, George came closer to the Aristotelian position, though debt to Aristotle is not explicit in his work.

The current revival of *laissez-faire* capitalism under the title of Economic Rationalism relies on an unrestricted theory of private property, similar to the economic thought of late eighteenth century England. Despite its supporters citing elevated per capita incomes through that period as evidence greater economic welfare, a closer inspection reveals that although gross production was growing, the proportion flowing to the working people was actually shrinking. Harrison has made the striking observation that throughout the industrial revolution the new wealth actually flowed not just away from the the working person, but for the major part past the capitalists as well, to be collected by the landlords (Harrison 1983). Hence the nature of ownership and land ownership in particular, is central to the economic problem.

Property in land cannot be argued from labour, because the factor land has no labour content. Title from inheritance must regress to some other form of claim. Various cultures use religious beliefs to ground their land titles and usually attach to them ethical responsibilities. Pure philosophical enquiry, such as that of Aristotle, has suggested similar conclusions. The problem remains as to how these claims arise and how they can be assessed. If property rights in land can be transferred, how do the responsibilities attaching to title transfer?

Land is an especially useful asset to consider when investigating ownership because it is recognised as a bundle of rights, which may be packaged in a large variety of

legally recognised ways (Hallman 1973). Of these, freehold is the most complete form and the one that is currently preferred in Western free market economies (Lean and Goodall 1966). Aristotelian metaphysics may be used to analyse the nature of ownership and appears to be able to explain some of the recurrent non-western cultural practices regarding land's place in society (Small 1997). It appears that the various property rights can be allocated into three clusters: (1) those totally belonging to the owner, (2) those belonging to the purchaser in the case of assets intended for sale, and (3) those belonging to the community as a whole. Equity is only possible when this natural allocation is balanced.

2. What is the origin of the price of land?

Locke suggested that all value was related to human effort and formalised what came to be known as the labour theory of value (Locke 1924/1962). Adam Smith adopted this basic position when he suggested that value could be gauged by the amount of labour a person would be prepared to sacrifice in order to purchase a thing.

This willingness to exchange labour for a thing could only be the result of it being either (1) capable of satisfying a need or desire, (2) is capable of saving labour in some future production, or (3) is rare and sought after and may appreciate in value in the future. These all relate to the usefulness of the thing to the purchaser. For different purchasers this value may be very different, proportional to their desire or estimation of how they will be able to utilise the thing. Aquinas observed that this was a quality of the purchaser, not the thing, and raised the curious point that if price was set by a quality within the purchaser, then the vendor was selling something that was already the property of the purchaser - a form of theft⁸.

Aristotle suggested that value was based on demand and equality in exchange was therefore utility equality. This position is reflected in the Austrian school of economics, which has developed a subjectivist theory of economics. It may be argued however that Aristotle's position, while holding an essential truth, has been misunderstood in its application. Aristotle also held positions regarding slavery and the status of women that are considered problematic today. In both cases, his position contains some truth, but careful application of his own method reverses his own conclusions⁹

⁸ *Yet if the one man derive a great advantage by becoming possessed of the other man's property, and the seller be not at a loss through being without that thing, the latter ought not to raise the price, because the advantage accruing to the buyer, is not due to the seller, but to a circumstance affecting the buyer. Now no man should sell what is not his, though he may charge for the loss he suffers.* (Aquinas 1981, Pt.II-II, Q77 art. 1, p. 1508)

⁹ Aristotle's position on slavery is often used as a criticism of his entire system, yet his thoughts on slavery are more complex and subtle than his critics usually imply. He considered that some persons did not have the mental resources to be autonomous, and for these slavery was appropriate. He never sanctioned poor treatment of slaves. Today, certain people, such as the mentally handicapped, are denied a degree of autonomy. The care and direction of these people mirrors Aristotle's vision of slavery.

Current pricing theory is largely a response to this observation. Two major positions are available, marginalist pricing, that contributes to the foundations of neo-classical economics, and full cost pricing, which can be shown to be essentially labour based. Neither of these are theoretically applicable to land as both rely in some way on production/supply parameters.

3. How does ownership inform the social economy of land and pricing?

There appears to be a significant level of concern for the level of mal-distribution of wealth in modern societies. Wealth distribution data is not readily available in most states and income distribution data is a poor proxy. Raskall studied probate data to estimate wealth distribution in Australia and there appear to have been a handful of other attempts, though not forming a systematic series (Colebatch 1999; McTeggart 1996; Raskall 1986). Wealth distribution has been correlated to economic cycles with causal inferences, though this work is at yet immature (Das 1993). Several authors have related land tenure to mal-distribution of income, from historical and contemporary studies (Harrison, 1983; George, 1879,1992).

4. What are the implications for land investment practices?

Current western land investment practices have evolved from the enclosure of land that signified the end of the feudal land tenure system. It stands at variance to the land allocation practices of many cultures (Small 1997). Current interest in the resolution of customary title claims by indigenous peoples suggests the need for a general theory of the social economy of land that is more comprehensive than the current western conception. It also has implications for trade and investment in general.

1.3 FORMAL OBJECT

Adopting the definition of economics as the study of appropriate relations between persons with respect to material things, the study of land within economics would appear to be *the study of appropriate relations between persons with respect to property in land*. this is the formal object of this study.

Property in land consists of a set of rights, the most important from an economic perspective is the right to a share of the income that arises from the productive use of land. The nature of property rights is therefore relevant, as is the determination of the magnitude of the share of income that property rights validate. The income that attends

Beyond this it must be recognised that Aristotle did err due to the pressure of his culture in permitting this justification to extend past its natural limits. However, application of his method of thought can be shown to draw conclusions on slavery more in keeping with the dignity of the human person. In the economic area a similar situation exists, the purpose and application of his thought on demand based pricing is not as transparent as may be assumed from a reading of the passages in isolation.

property rights in land is commonly referred to as rent, and it gives land property a value in exchange, making property in land an expression of wealth. Because economic relationships are studied in terms of their appropriateness, they are ultimately moral or social.

The study is therefore directed towards understanding the nature and operation of wealth associated with property in land and its social implications.

1.4 OBJECTIVES

1. To examine the metaphysical, ethical, cultural and behavioural basis for property ownership.
2. To examine the social economy of trade and pricing of land and products.
3. To empirically study social attitudes to market pricing
4. To develop an Aristotelian/Realist theory of the social economy of land.
5. To examine the behaviour of land rent and economic rent in general.
6. To empirically test Ricardo's rent theory using an experimental environment.
7. Use 1-6 above for the development of policy applications

1.5 HYPOTHESES

	Hypothesis	Treatment
1.5.1	The treatment of property in land is highly varied by different cultures.	Ch. 4
1.5.2	The majority of cultural practices in land may be reduced to common underlying principles relating to the social destination of land income.	Ch. 4
1.5.3	The social destination of land income is an ethic that is linked to a constellation of social ethics capable of being summarised within the notion of solidarity.	Ch. 4
1.5.4	Current Western treatment of land is culturally distinct from the majority of distinct cultural resolutions of property in land.	Ch. 4
1.5.5	The Western notion of property is positive and historically recent.	Ch. 5
1.5.6	The construction of modern market theory is evidence of its reliance on morals.	Ch. 6
1.5.7	Popular sentiment does not support pricing from use value.	Ch. 8
1.5.7.1	Modern market theory is based on a positivist methodology, yet fails positivist tests.	Ch. 6&8
1.5.8	Modern market theory is successful as a species of social psychology.	Ch. 6
1.5.9	Trade is initiated by the desire of the consumer, as final cause of production.	Ch. 9
1.5.10	Pricing by the market is not suitable for natural property	Ch. 9
1.5.11	Commodity use value lifts price above normal costs in current market practice.	Ch. 6 & 9
1.5.12	Price naturally derived from cost.	Ch. 9
1.5.13	Conventional property is priced as the difference between demand and the return to natural property	Ch. 9
1.5.14	Supernormal profit results from the fact that sale is made for utility based prices but production is based on costs	Ch. 9
1.5.15	Land rent is the differential between socially accepted subsistence and net site product.	Ch. 10&12
1.5.16	Rents will find equilibrium at levels that absorb marginal productivity.	Ch. 10&12
1.5.17	Rents will find equilibrium at levels that normalise returns to other factors.	Ch. 10&12
1.5.18	Productivity increases will tend to be absorbed by rents	Ch. 10&12
1.5.19	Land prices are a function of capitalised rents.	Ch. 10&12
1.5.20	Land rents are not derived from land values	Ch. 10&12
1.5.21	In practice, the resolution of the actual level of the subsistence wage is social/political.	Ch. 12&13
1.5.22	The behaviour of productivity (and hence use value) differs between land and products	Ch. 13
1.5.23	Rent taking in land is distinct but related to other (economic) rent taking.	Ch. 13
1.5.24	Supernormal profit, interest on debt, and taxation are all naturally paid out of rent.	Ch. 13
1.5.25	Private property in land is licit subject to social destination of super-normal income.	Ch. 9 & 14

These will be reviewed by chapter and summarised in Chapter 14.

1.6 SCOPE

The study is primarily a methodological inquiry into the construction of property rights in land using an Aristotelian social economic framework. Consequently, it examines the human use and administration of land and its economic consequences. It is considered that economics, being part of the practical order, has a moral dimension. The moral foundations of Economics will be examined and used to develop an understanding of the economic significance of land that takes into account both personal and community values. The moral order contains a social dimension and this dimension extends into the moral expectations of economic behaviour. The study will differentiate between behavioural economics and normative, morally grounded economics and relate these perspectives to the location of land within the economy and pricing.

Using this foundation, the study will consider several practical issues that relate to land ownership and explore the suitability of an ethically/metaphysically grounded theory of property in examining these issues. These will include customary title, land tax, betterment taxation, economic and real estate cycles.

Ricardo's Law of Rent will be examined in terms of its practical validity and its social implications. Perry's question of the par, regarding the just balance between returns to land and labour will provide a background to this investigation. The nature of laws in economics will be examined and Ricardo's Rent law will be tested experimentally. The implications of land pricing will also be examined in terms of the tension between utility based pricing and cost based pricing to inform the relational issues pertinent to commerce in land.

1.7 FOCUS

The focus of the study is methodological. Its aim is to examine the appropriateness of current Western practices with respect to land and the methodological implications for economics flowing from a realist metaphysical/ethical theory of property in land.

The conformity of economic/commercial behaviour to classical *laws* pertaining to land will form one of the foundations of the study. In particular, the validity and significance of Ricardo's *Law of Rent* will be examined as a foundation for the social economy of land. This necessitates an investigation into the nature of economic laws and their reliability as a basis of policy.

Building on this, the social dimension of the economic use of land will be considered. Fundamental to this focus is attention to the question of property rights and

their nature. The human utilisation of land extends beyond a particular culture or economic paradigm, however the natural location of land within human society is assumed to be a constant which is intelligible through an investigation into the nature and usefulness of land and its essential position within inter-human relationships. The latter is part of the moral order, which is itself intelligible in terms of human nature. The focus is therefore on the natures of land and humanity and their interaction.

The study will therefore focus on the metaphysical construction of property rights, the application of this conception of property rights to land and the use of these insights for the just organisation of society. The notion of value in land is the economic centre-piece of this study and this will be examined in terms of property rights and social/ethical obligation.

The usefulness of land is partly a function of technology, but its economic meaning is somewhat simpler, land provides the raw materials for all production and land also provides the siting for all human activity. The study is not primarily undertaken within the discipline of Economics as it is currently understood, though it will critique key economic concepts in order to inform the investigation into land. Likewise, other disciplines, such as financial economics, will bear on the study to minor extents insofar as they offer insights into fundamental issues relating to the nature of investment in land.

The study is an investigation into the methodology of Land Economics, not its content. However, the study will test its methodological conclusions using empirical methods .

1.8 DELIMITS

The ethical and metaphysical aspects of property rights provide a foundation for the study. However, the study will not explore or argue either metaphysics or ethics extensively. In both of these areas, argument towards justification of the systems adopted will be presented, but it is recognised that divergent systems and beliefs regarding their merits exist. While these will be recognised, they will not be exhaustively explored. Some moral and metaphysical systems may not be explicitly considered. In this way the study will be limited to a basically Aristotelian/Realist philosophical base.

The nature of modern economic thought will be examined in order to locate it with respect to ethical/social economics. In particular, some implications of its positivist methodology will be explored to develop an understanding of its relationship to ethical and political concepts. Beyond this, modern economics will not be examined. This

delimitation places outside of this study much of the content of economics developed from the foundation of market theory. Market theory itself provides the boundary for this study, and will be examined in terms of ethical expectations, perfect market theory and free market (libertarian) implications. Because much of modern economics stands on the assumptions of free and perfect markets, the locations of these concepts within an ethical structure is held to be sufficient to provide much of the ethical/social dimension of economics generally. The fact that liberal free market economics is successful as positive social science will be explored as a resolution of the apparent dilemma for its critics that it appears to have failed ethically, while having simultaneously succeeded to some extent in predicting future economic behaviour.

Location theory will not be extensively explored. Urban economics is largely interested in the economic management of urban property taking into account social and productive issues that are geographically determined. These will be largely taken as given. The broad mechanisms that give rise to land productivity in a human sense will be surveyed, however their actual origin will not be pursued. Land will generally be assumed to have a knowable highest and best use which may be related to necessary labour and capital costs to infer land rent.

While land is a necessary component in any commodity, the implications for produced commodities will not be extensively explored.

The unit of land that will be considered is that which can be worked productively by a single occupier. The unit adopted to denote occupiers will be the working family following the classical recognition that it is this unity that is both the basis of society and capable of autonomous reproduction. The family unit is also the boundary between two sets of relationships, internally it is motivated by care and typically not managed using monetary transactions, while externally it meets the rest of society on a generally commercial basis for the majority of its material transactions.

By focusing on that unit of land that is capable of supporting a single occupier unit, the study will not investigate those issues that complicate land uses that operate at a level that necessarily employs a large number of persons as employees. It is asserted that once the unit-occupier situation is understood, these larger scale land uses may be fitted into the same economic relationships.

Financial aspects of land value and the interplay of debt and land will not be examined extensively, beyond an exploration of the effect of debt leverage on land prices and the implications of this practice for price stability. The importance of financial perspectives in determining the rate of profit will be explored, especially the Capital Asset Pricing Model (CAPM). The issues regarding the precise application of

the CAPM will not be engaged due to their irrelevance to its use in this particular context.

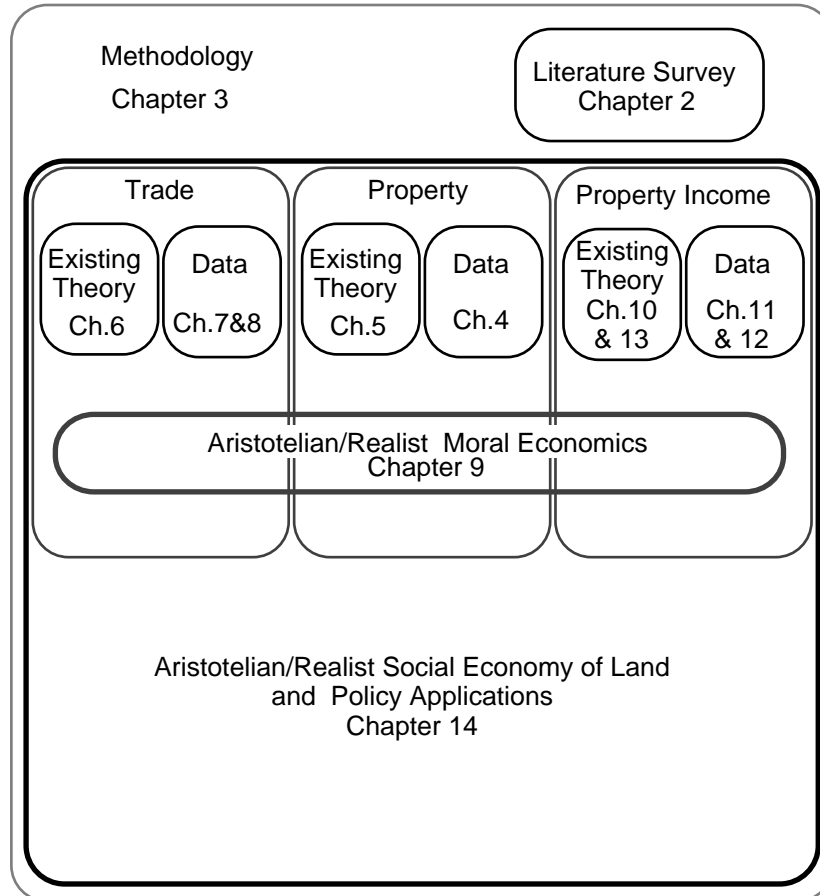
In considering just price, discussion often moves into an almost interminable regression based on the fact that subsistence wages are based on the cost of commodities, which are the product of labour. What this means is that the utility value of subsistence consumption is actually the cost value of labour, hence it would appear that an argument in favour of labour (cost) based commodity pricing cannot be distinguished from the utility values of that same set of commodities. This argument will be noted, but will not be explored beyond the establishment of a reasonable starting point, being a subsistence wage rate. This is not to suggest that the issue will be avoided, but that the extent of its treatment will be limited to what is required to relate labour returns to land.

The study is limited by boundaries set by the literature available. While the task has been to integrate so far as possible the sound elements found in the literature and only reject those that can be clearly shown to be insupportable, there may be evidence or thought in the literature beyond that which I have investigated that would moderate the conclusions drawn in this study. As it is, some of the material that has come to my attention late in the study has proven to be most valuable in confirming, completing and supporting the thrust of the position outlined, which has been encouraging. It is very possible that there remains some degree of rashness that would benefit from exposure from additional perspectives. Likewise, it may be very possible that other authors unknown to me have already explored this aspect of the social economy of land and have presented more polished analyses. I owe to them the responsibility of continuing to try to seek them out and if possible making their contribution more accessible to others.

1.9 RESEARCH FRAMEWORK

The structure of the study is shown in Exhibit 1.1:

Exhibit 1.1: Research framework



1.9.1 Methodology

The conceptual framework will be developed from an examination of the appropriate philosophical foundations and an exploration of the context pertaining to property rights in land. Major themes in metaphysics and moral philosophy will be considered, especially as they pertain to economics, and a philosophical framework adopted.

An Aristotelian/Realist methodology will be adopted that will locate the social economy of land as a species of economics which in turn is a species of practical science, predominantly within moral science.

1.9.2 Literature Survey

The literature pertinent to the various methodological, theoretical and empirical issues treated in the study will be examined.

1.9.3 Topic Treatment

Three major topics will be examined and developed. These are trade, property and property income. Each will include a critique of existing theory and presentation of relevant empirical data.

An Aristotelian construction of the three topics will be made. The exchange event will be analysed in reference to the social dimension of human nature. The Aristotelian concept of justice in exchange will be used to review pricing practices. The debate regarding the source of price will be engaged and the implications of two major positions, utility or cost, will be examined. A metaphysical construction of property, based from Aristotelian causality will be presented and examined. These will be used to formulate the dimensions of property and income from land.

The treatment of land rent will be examined in detail, both its theory and practice. The interplay between land rents, other rents, wages and other disbursements will be examined in order to relate the various components in economic distribution.

The three topics will be integrated into a single construction of the social economy of land which will enable conclusions regarding policy and practice.

1.9.4 Empirical Validation

Trade

An empirical study to examine the degree of acceptance of utility based pricing will be undertaken. Despite utility (as evidenced in demand) being normally accepted as part of the process to leads to market price formation, (Frey and Pommerehne 1993) found that 80% of respondents considered it unfair. If land price is necessarily based on its use value to the purchaser and rents result from the productivity potentially available to the tenant, then this perception of unfairness could well extend to land values.

The empirical methodology of this part of the study is that of an attitude survey. The usefulness and limitations of attempting to resolve ethical questions using this approach will be considered. It will be argued that rather than necessarily resolving the ethical merit of the situation, results are sufficient to infer that the practice has a moral content and further more, that there is a significant balance of opinion on the matter.

This empirical component will contribute to an understanding of hypotheses 2.5.

In addition, the study of property market fluctuations, while being primarily conceptual, includes an empirical analysis using secondary data drawn from published studies of particular property markets.

This section will contribute to an understanding of hypotheses 3.5 and 4.4.

Property

Data on the various practices regarding land property will be assembled from the literature. The recent interest in Australia and elsewhere in customary title rights to land by indigenous people and their integration into the dominant Western system has generated considerable interest in this area. There is also a considerable amount of historical and anthropological data available on various cultural resolutions of the property problem. These will be collated and commonalities and differences analysed.

Property Income

The validity of Ricardo's Law of Rent is central to the social economy of land. Marshall established a methodological watershed by redefining the discipline of economics as a positive science. Part of this change was the assertion that the underlying causal mechanisms would be forever obscured by confounding variables, and therefore their existence could only be inferred inductively using empirical methods. Associated with this belief was the background debate over the nature of human action, between free will and determinism. The existence of necessary causal laws of human action would infer determinism, which is counter to the general acceptance of the existence of human free will.

Taken to an extreme, either of these views could render study of economics pointless. If the causal mechanisms are so obscured by confounding variables that they cannot be known, then there is no point exploring them. Likewise, if human willing is so unique and personal that it makes human action so unpredictable that causes cannot be clearly identified for human responses, then the practical sciences are similarly emptied. Fortunately, there is a middle ground. Human behaviour, especially when observed at a social level, does exhibit a degree of predictability. A careful investigation of human action reveals that without denying free will, identifiable causal patterns are evident, and some of these may be the result of a reasonably well formed moral awareness in most people in a community, leading to uniform responses to moral situations, or it may be the result of intellectual, rather than moral, virtues being exercised. These are not so intimately bound up with moral willing.

The formation of rentals across a property market is an example of such a potentially predictable case of human behaviour. Ricardo's Law of Rent suggests that rents are based on productivity less subsistence wages, which for uniform subsistence wages, reduces to the single variable of land productivity. There has been little apparent attempt to empirically validate this law. Without necessarily denying free will, it will be argued that rental determination may be more in line with the exercise of an intellectual virtue, especially in Western culture. The moral dimension of rentals will also be

considered elsewhere in the study, but the focus of this section of the study is on examining the validity of Ricardo's Law.

In order to eliminate as far as possible the confounding variables commonly present in economics research, an experimental investigation will be used. In this way environmental variables may be controlled more completely. The experiment intends to expose the structure of rents that emerge in a market exhibiting the characteristics of near-perfect competition, and by inference the resulting outcomes for labour (wages).

The experiment will contribute to an understanding of hypotheses 3.1, 3.3, 3.4, and 3.5.

Evaluation of the remaining hypotheses will be developed from the literature. It will include an investigation into varied cultural practices with respect to land, which may be considered positive in an historical or anthropological sense. The majority of this will be attempted within the argument that constitutes the section of the study that develops the conceptual model.

1.20 APPLICATIONS, POLICY RECOMMENDATIONS

Generally, the debate regarding the political economy of land over the last two centuries or so has been focused on taxation. Some aspects of this debate will be treated within the conceptual model, basically arguing against the supposed panacea of community appropriation of land rents as a single tax for the community. A broader survey of the possibilities will be attempted, informed by various cultural precedents and an overall concept of the social dimension of ethics.

Recommendations pertinent to the current debate regarding customary title rights will be explored. Material considered within this section will have significance to the general land taxation issue.

The significance of land in the behaviour of economic cycles (fluctuations) will be considered. Economic fluctuations will be examined in terms of rent-taking and examined against particular market examples.

1.21 DEFINITION OF TERMS

Personal Pronouns: Consistent with the generally accepted definition of the generic *man* as referring to a human person of either gender (equivalent to the latin *homo*), the personal pronouns *he*, *him*, and *his* will be used in this thesis to refer to persons of either gender without any bias intended.

Appraisal: The intellectual virtue pertaining to the accurate assessment of the potential sale price of an asset, usually of a real property asset.

Broker: A person who acts as an agent in the sale of a real property asset.

Capitalisation: A method of appraisal that uses the rental expected on a property and a rate of return (yield rate) to estimate the financial value of an asset which is assumed to signify its rational price. (*Note the etymology of the term: to capital-ise signifies that something is being made into capital, suggesting a recognition that it naturally it begins as something else*)

Domain: For the purposes of this study, domain refers to the sum of land parcels available to a particular society.

Economic rent: the gap between factor costs (including land rent) and normal profit, and sale price of a commodity.

Exchange value: Price.

Factors of Production (factors): These refer to the causal components of production, summarised by Adam Smith as land, labour and capital

Financial investments: For the purposes of this study these will refer to equities, equity derivatives and land. They are distinguished by deriving their value from being a right to a share in future income without impacting on actual productive capacity. Land is included in this group because its financial behaviour is more akin to equities than physical productive assets, such as tools. It will be argued that all financial returns are participations in land rents.

Land taxation: any form of taxation (public revenue) that is levied on the site value (preferably *rental* value) of land. Local government rates are frequently levied in this way, however, when they are levied on the improved value of the property they are no longer strictly speaking a pure land tax.

Marginal Land: Sites with a gross productivity that can only just support the occupier. On this land Ricardian theory suggests that no rent will be paid and hence it would have nil intrinsic sale price.

Modern (society): Denotes that general cultural orientation that is permeated and dominated by modern thought. Modern thought is that ushered in by the so called Enlightenment, especially David Hume in the English tradition and Rousseau in Europe. Modernity takes its name from that representationslist epistemology that sees all knowledge as an internal *model* of perceived reality. Culturally, modernity is often identified as *Western*, though this is confusing, there exist many non-Western modern societies today, just as there have been particularly successful non-modern Western

ones in the past. The advent of post-modernism is evidence that modernity is no more than a passing phase in cultural orientation.

Normal Cost: the cost to produce a thing that includes all factors of production, including normal profit.

Normal Profit: that rate of profit on capital sufficient to maintain stable real equity values. The rate of profit in the absence of economic rents

Occupier: in connection with land, that person who physically works or otherwise utilises a land parcel, either as tenant or owner occupier. The unit adopted for occupiers is the working family, that is, a family that earns its income from the toil involved in utilising the site.

Price (of land): Unless otherwise specified, this refers to the market sale price (of land). Note that in discussion of the intrinsic meaning of value it will be argued that price does not necessarily signify value. Land has both a sale price and a rental value, these two values should not be confused, although they are closely related through the capitalisation relationship. The common conditions of the market are assumed.

Perfect market: That market condition where price is the result of free and fully informed decisions to transact by parties who may enter or leave the market at will. It normally assumes a plurality of vendors and purchasers.

Rent: Pertaining to land, the share of the product from the utilisation of land that returns to the person that holds rights to it. Generally, economic rent is a measure of market failure or imperfection, being the amount by which price exceeds normal cost. Several rents are evident and deserve specific definition:

Market rent: Pertains to land. This is the actual rent paid on a site, it may differ from the underlying true rent.

Economic rent: This is the excess flowing from a market failure (market imperfection), it may be captured by any party, it is enjoyed as super-normal profit by capital, super-subsistence wages by labour, but in Ricardian theory is taken out of true land rent.

True (land) rent: This is the rental determined by Ricardian rental theory. Despite being referred to here as true rent, its private appropriation may not always be ethical

Sites: while this term may be generally be used to refer any specific parcel of land, within this study it refers specifically to land parcels that are capable of being fully utilised by one occupier.

Use value; Utility: The degree to which a thing contributes to some human good. This is distinct from a thing's metaphysical value that relates to its order of being, or other 'values'

Value: The degree to which a thing contributes to some human good. This is distinct from a thing's metaphysical value that relates to its order of being, or other 'values' commonly encountered in economic discourse, especially market value (referred to here as *price*) and perhaps *cost value* (referred to simply as *cost*)

Wages Line: In Ricardian theory, the level line representing wages across various land productivities. Its existence suggests that tenants will enjoy a normalised income independent of site productivity.

Chapter 2 Literature Survey

The purpose of this chapter is to review the relevant literature currently available. Some consideration of existing theories has been included but only so as to distinguish the positions of authors and their relationships.

2.1 METHODOLOGY

Boland (1992) suggested that despite the assertions of recent economists, economic theory necessarily begins with metaphysical assumptions. Boland noted that statements such as "consumers maximise their utility" while being metaphysical in nature are also highly questionable in fact.

There are many approaches to metaphysics. Classically, it is the first philosophy, the only science that is capable of testing its own premises (Wallace, 1977). Two metaphysical principles will be used in this study, causality and the concept of natures, particularly human nature. Aristotle proposed four causes to any existing thing (Aristotle 1956). Coppleston outlined how they were a consistent development of Platonic thought (Coppleston 1993, p.306). The four causes, or principles are (1) the material cause (matter, raw materials), (2) the formal cause (form or design), (3) the source of movement, the efficient cause (the maker), and (4) the final cause (the need or demand). These principles are central to other traditions of realist thought, such as that of St. Thomas Aquinas and the Scholastics.

Modern philosophy and the economics that derives from it follows a very different approach to metaphysics. Hume was suspicious of causality, not believing causes could be known. His strong empiricism led to an abandonment of Aristotelian metaphysics and his conclusion when faced with metaphysical arguments: "*All this is metaphysics... ..That is enough; there needs nothing more to give a strong presumption of falsehood*" (Hume 1777/1975, p.289). Boland's well reasoned conclusions regarding the necessity of metaphysics in the study of economics may be in fact evidence of the failure of a two hundred year experiment aimed at producing a metaphysics-free science of economics. Writers in the natural sciences, especially physics, appear to be reaching similar conclusions, though for different reasons, however their dabbling with metaphysical issues arising from their empirical examinations often betrays their poor understanding of philosophy (Johnson, 1995).

Warnock (1967) argued that by the beginning of the twentieth century moral philosophy had been effectively "*emptied of its content*" making way for that century's innovations in moral thought that he systematically demonstrated to be meaningless in any normal sense of the term moral. Durkheim's endeavour in establishing Sociology

was driven by his intention to provide support for what he saw as the failure of European moral thought. The point that is evident from both of these is that empirically modern moral thought, as derived from its Enlightenment roots, has failed. While this observation is made directly on the basis of Warnock and Durkhiem, there is a vast literature on the failure of morals over the last century or two that is beyond the scope of this study.

2.2 ETHICS AND ECONOMICS

Historically, economics was a branch of moral philosophy known as political economy. Up until the twentieth century, writers in economics were identified as doing philosophy - Adam Smith for example, held the chair of moral philosophy at the University of Glasgow. His work rests on his moral system and his own cultural context as can be seen from his position on liberty for his own countrymen in commerce:

'To prohibit a great people, however, from making all that they can of every part of their own produce, or from employing their stock and industry in the way that they judge most advantageous to themselves, is a manifest violation of the most sacred rights of mankind' (Smith 1778/1910), Vol.II p.79]

His reliance on sacred rights as the base for his conclusion is explicitly moral. His reference to his own countrymen, while patriotic and typical of his age, was partisan. His partiality has been recognised even by his supporters (Fay 1932, p.13). It is not to be found surprising that his economics should validate their behaviour. His famous '*invisible hand*' is no more than a metaphysical metaphor that has served as the premise for the morality of the market ever since his day. Like Hegel's universal spirit, it is no more than a useful phantom that lacks reality beyond the speculative and fades rapidly on closer investigation.

Marxist thought can be better located as part of the philosophy of appropriate relations between humans; moral philosophy rather than economics, with his work heavily influenced by earlier philosophical movements. Although Roll (1942) devoted some space to outlining the elements of Marx's economics, his role is better understood as a sociologist (Robertson, 1987).

The connection between economics and ethics is a necessary one as evidenced in the common treatment in general works on social ethics (Kavanagh, 1954). Economic relationships are necessarily based on concepts of justice which is a moral concept. The connection can be slight, using moral philosophy to provide definitions of the parameters of justice, thus leaving economics to operate within them or it can be more

involved. The trend in the nineteenth century has been to opt for minimisation of the connection.

Marshall adopted the positivist approach to economics, re-focusing the discipline on what could be visibly measured. Although he recognised that '*... the economist, like everyone else, must concern himself with the ultimate aims of man*' (Marshall 1920/1938, p.17), he also asserted that:

'It still however probably be always true that the greater part of those actions, which are due to a feeling of duty and love of one's neighbour, cannot be classed, reduced to law and measured; and it is for this reason, and not because they are not based on self-interest, that the machinery of economics cannot be brought to bear on them.'
(p.24)

Marshall coined the term 'economics' as distinct from the previous 'political economy' as the title of his discipline and in doing so eliminated the *political* element. As a study of data on transactions measured in monetary terms, he made it part of the domain of the statistician. By eliminating a direct connection with considerations of intention and responsibility, he removed its moral, or political, content. Statistics can never reveal causality, only probabilities. Marshall recognises this when he observed '*...there are no laws of economics which can be compared for precision with the law of gravitation.*' (p.31) and more precisely '*The term "law" means then nothing more than a general tendencies, more or less certain, more or less definite.*' (p.33).

Curiously, within all of this all of this positivism and indeterminacy, through the study of economics he asserted that we could aim '*... to obtain guidance in the practical conduct of life, and especially the social life.*' (p.42) thus making economics look very much like a tool of moral philosophy. For this reason Marshall asserted that his discipline '*... is better described by the broad term "Economics" than the narrower term "Political Economy"*' (p.43).

What Marshall did was cut the discipline off from the practical science of moral philosophy and re-establish it as a quasi-natural science, built on no more than inductive probabilities. There is a deep philosophical point here that is illustrated by his objection:

'The less we trouble ourselves with scholastic inquiries as to whether a certain consideration comes within the scope of economics, the better. If the matter is important let us take account of it as far as we can. If it is one as to which there exist divergent opinions, such as cannot be brought to the test of exact and well-ascertained knowledge;

if it is one on which the general machinery of economic analysis and reasoning cannot get any grip, then let us leave it aside in our purely economic studies.’ (Marshall 1920/1938, p.27)

The reference to the Scholastics is a telling pointer to Hume who used the perception that ‘(s)uch confusion reigned on these subjects, that an opposition of the greatest consequence could prevail between one system and another, and even in the parts of almost each individual system; and yet nobody, till very lately, was ever sensible of it.’ (Hume 1777/1975)(n.134, p.171) to dismiss all moral philosophy that went before him and “... attempt a like reformation in all moral disquisitions; and reject every system of ethics, however subtle or ingenious, which is not founded on fact and observation” (n.138 p.175). Marshall is attempting the same thing in political economy which is a discipline located as a subset of moral philosophy. His premise is the existence of disagreement and his revised methodology is empirical induction and his application is the guidance of human action.

Such an enterprise is not itself noteworthy, but it does align economics, in all of its statistical sterility, with the fortunes of modern moral science. Velasquez has described the way in which Bentham’s utilitarianism has informed economic theory from the nineteenth century onwards, including Mill, Jevons, Pigou and current market theory, implying that modern economics still finds its roots amongst moral philosophy (Velasquez 1988). Mirrlees described the successes of this union (Mirrlees 1982), however his argument holds for theoretical economics only; the realities are not so unequivocal and deserve further review.

Knight was critical of the positivist approach to economics, and attempted to maintain the moral foundation of economics as one of its fundamental principles when he observed:

‘And the economic aspect of behaviour itself has its own quality of rightness, beyond mere desire; it is within limits "a matter of principle"; "waste is sin." (Knight 1940, p.25-26)

His analysis of positivist economics concluded with the caution that although it was focused on individual decisions that aggregated to social trends and aimed at controlling or directing those individual decisions, a positivist methodology could “never carry anyone very far toward the prediction or technical control of the corresponding economic behaviour.” (Knight 1940, p.30). Although he defended the necessity for a moral basis for economics, his discussion did not extend to analysing which moral system was appropriate.

Contemporary, or modern, moral theory is inevitably based on Hume and its transition from the pre-Humean theoretical systems can provide insights into the prospects for Marshall's vision of economics. Warnock outlined this transition and the resulting moral positions which have reduced morals to no more than a particular form of statement (Warnock 1967). The power to make the statements becomes an arbitrary competition and justice little more than 'the will of the stronger party' so persistently argued by Thrasymachus in *The Republic* (Plato 1987). In such an environment it is easy for economics to develop an essentially value-free profile.

Marshall's equation of empirical with scientific mirrors the other recent science that has broken away from moral philosophy, sociology. Durkheim, the 'father of sociology,' had an explicit objective of regenerating western morality by using social enquiry (Ritzer 1983). The governors of nations now call on legions of economists and sociologists as policy advisers. There does not appear to be an unequivocal indication that these new moralists are capable of better results than the old, despite considerable general debate.

The success of neoclassical economics, with its emphasis on mathematical rather than moral interpretations of the doings of society with respect to material things, may be inferred from the evidence of an inverted hierarchy that is sometimes evident between economic and social values. Calabresi (1975) noted that altruism tends to be treated as a commodity subject to economic analysis, rather than a value that should guide behaviour. This observation succinctly expresses a more general fact that within economic analysis both moral and immoral behaviours are equally valid as economic variables. Jones used this independence of the economic and the moral to argue that market theory could be employed to discourage criminal behaviour by simply making it very costly (Jones 1976). Others have demonstrated the application of economic theory to a wide variety of social choices from family structure to choice of religion (Becker 1969; Becker 1974; Becker 1976; Becker 1991; Becker 1996; Becker 1997; Jones 1976).

Modern economic theory is based on the moral system of utilitarianism which is itself based on the identification of good and evil with pleasure and pain. To use such a system to review or direct social behaviour using economic means, appears to clear the way for a variety of peculiar outcomes. Where value is no more than an economic concept that may be evaluated and manipulated the absolute anchor of morals could easily be lost. For example, if motorists pay fines for speeding it could be seen as their compensation for dangerous driving, and no more. If the fines pay the police salaries, then speeding becomes the manner of funding law and order, which is a social good. Dangerous drivers are therefore socially responsible because they pay their fines and fund law and order. On the contrary, Phelps has argued that economics is highly

dependent on ethics by demonstrating the impossibility of equilibrium outcomes in the absence of a concept of inter-generational justice (Phelps 1975).

The notion of value suggests goods, both concepts having their roots in Aristotelian economics and his moral philosophy. Flubacher (1950) has explored the connection between ethics and economics and has suggested that Mercantilism marked the beginning of the separation of economics from being subordinate to ethics, citing Tawney, Weber and Fanfani for support. Despite this historical separation, several ethical limits have remained very evident in economic theory, such as the rejection of monopoly and the justice of various forms of taxation.

Pearce (1987) provided a philosophical basis for price within economics. The notions of value, price, and justice are integrated in a manner that offers a foundation for specific policy considerations to be built upon. Others have outlined similar models based upon an attempted synthesis of the classical realist Smithian (Humean) approaches (Young, 1997). These are among a veritable plethora of works supporting various alternative systems of economics.

Common among many of these is a desire to produce a more just world. Consequently, regardless of their method, the social fact emerges that humans desire justice and they see part of its realisation in the working out of economic relationships. Foster (1985) argued for "simplicity" as a necessary ethic in economic life to overcome the negative social outcomes of broadly applied self-interest, effectively arguing against Smith's fundamental of economic motivation. This mirrors the ancient moral warnings against avarice directed towards merchants in the Medieval era (Little 1978).

A strong theme in the present study is to use moral philosophy as the foundation for the work. To do this, an analysis of the history of economics and its divergence from ethics is necessary. Roll (1942) is indicative of the historians of economics who set out the development of economic ideas. A difficulty with these histories is the perspective of the author, which typically locates evaluation of differing views relative to the writer's own position, producing a colouration. While this is neither conscious nor malicious the effect can still cloud a fair understanding of the subject material. This bias has been widely recognised in sociology (Merton 1969), especially within the sociology of knowledge (Popper 1968; Susser 1989) and feminist theory (Grosz 1990). The historical critical method of history is based on testing historical facts against current understandings in a way similar to Hume's classical criteria for the admissibility of evidence from history (Hume 1777/1975). Kant's a priori forms are recognised to exert considerable pressure, giving rise to Kuhn's belief that scientific revolutions follow a random walk with respect to truth (Kuhn 1970), despite the stated purpose of science to draw ever nearer to it.

The notion of ethics in trading has a long history. Little (1978) outlined the way that the Medievals perceived the merchant as living precariously because of the occasion of sin that was daily work. Ruskin described eloquently the way that every profession, except for the merchant, was distinguished by the values that its practitioners would die for (Ruskin 1931). Hence soldiers would die for country, and doctors would die rather than knowingly cause a reduction in a patient's health (the realities of the Hippocratic oath), but the merchant is motivated by greed, not care for others, and hence would die for no one.

Just Price

Three issues are central to the relationship between economics and ethics, these are usury, pricing/value and distribution. Usury is fundamental to the consideration of debt and has been dealt with. Value and pricing is a distinct part of the distribution problem. Aristotle set the parameters of price which were refined as the just price doctrine of the Medievals (Aquinas 1981; Blaug 1991a; Blaug 1991b; Dempsey 1935; Langholm ; Langholm 1992; Roll 1942; Wilson 1975; Worland 1977). It is also implicit as part of Marx's economics within his adoption of the C-M-C vs. M-C-M' models of exchange (Marx 1957).

Distribution is a major issue and underlies almost all economic thought. Justice in distribution is held to be the goal of a just economic system and will be used as a test in analysis. The problem of distribution is classically aligned with the balance of returns to land, labour and capital.

The purpose of competition is to reduce prices to the same level that appears to have been St. Thomas Aquinas's intention in his notion of the just price, that is, to the cost of production including a consideration for normal profit. This can be seen in von Kettler's explanation of competition:

'Competition is at its best, however, if all natural and artificial restraints are removed, and this refers especially to such restraint as would interfere with free trade in the market. Universal free trade, therefore, implies unrestrained competition, and unrestrained competition reduces prices to their lowest limit - the limit set by the costs of production.' (von Kettler 1981 ,p.325)

Bishop von Kettler's position was clearly in favour of the free market, evident not only in this passage, but in the general thrust of his social teachings. This did not prevent him from maintaining a recognition that the market was a tool, a strategy, that could achieve the common good. The Papal encyclical *Rerum Novarum* extended this approach of being open to the emerging structures of commerce but testing them against social criteria. The thought of von Kettler is recognisable within the encyclical

and Pope Leo XIII openly acknowledged his debt to von Kettler¹⁰. The social teaching of the Catholic Church has continued to develop this openness to free market economics, but only when subject to respect for all persons and the more recent encyclicals have especially stressed the virtue of solidarity (Ederer, 1995). Solidarity is the human virtue that is exercised by willing the good of the other in a relationship in a brotherly way. Its fruit is unity between persons; von Kettler and the popes of the social encyclicals recognise that it is possible through the market.

This is not to say that the market is either necessary or sufficient to realise the material dimension of the common good. The current realities of the competitive market suggest somewhat less than this ideal. McKenzie introduced the political economy of the market place in the following terms:

The competitive market can be defined as a process by which buyers and sellers, in an attempt to pursue their own interests, try to outdo, outwit, outdistance, or outmanoeuvre other people. In the process, market rivals are induced to reveal what, at the limit, they are willing to do, not just what they would like to do under the circumstances. (McKenzie and Tullock 1978, p.110)

There appears to be no shortage of evidence of this type of market and while the implied disclosure could suggest the outcomes outlined by von Kettler, the evidence appears otherwise. Imperfect markets, markets that do not achieve the objective of honing actual prices to the cost of production, appear to be common. Blumberg's (1989) survey of markets that have failed to produce competitive prices is illustrative of a more general opinion. Pricing policy as found in conventional finance theory is based on manipulating prices for optimum profit (Wilson and Keers 1990) in a manner that necessarily assumes that the firm is able to adopt prices arbitrarily above the costs of production, at least within a manageable domain. Much of the rationale for marketing expenditure is underpinned by assumption that through specific communications (advertisements) profitability may be increased, i.e. revenues in excess of marginal costs will be received.

2.3 Social Economy

Social economics is best described as the continuation of the tradition of political economy despite the removal of the social dimension of the discipline, especially by Marshall. It tends to operate as a critique of positive economics, pointing out the deficiencies of that discipline in meeting the needs of society, but not beyond adopting, as far as possible, its methodology. Sometimes it operates within a Marxist paradigm,

¹⁰See Rupert Ederer's preface (vonKettler 1981)

such as Everling (1997), although this is a distraction from the core of the enterprise. Marxists may even be uncomfortable with the majority of what is found within social economics. Ederer (1995) has demonstrated that the social dimension of economics is found in the social teaching of the Catholic Church, which is in no way Marxist. Van-Eeghen (1997) used the capitalist aims themselves to critique its operation.

Altman (1999) likewise used an investigation of the assumptions of positive economics in comparison to the behavioural realities to review their appropriateness. This constitutes a positivist critique of positive economics. Prasch (1999) looked simply at social outcomes in his review of minimum wages and adopted positive behaviour to consider a political issue.

Social economics is therefore very broad and appeals to an interest in the common good. It appears to recognise that it is young as a discipline and therefore open to methodological exploration. The common thread is a practical interest in developing an economics that is consciously directed towards the common good.

2.4 Property rights

Economics depends on trade and in order to trade, the parties must own the things traded. The right to property is therefore at the heart of economics. While few people exist that do not accept the right to private property, the nature and extent is less apparent. The modern West views property rights pragmatically as "*... the liberty or permit to enjoy benefits of wealth while assuming the costs which those benefits entail.*"

Aristotle (1976) grounded property rights in the moral order. In order to achieve happiness, the most practical arrangement is the private ownership of goods. The most novel aspect of his theory was the recognition of private property, but only when attached to common use. Aquinas (1981) adopted this position and extended its justification, giving rise to a dual principle of property. More recently, Ederer (1995) reviewed the last century of papal encyclicals devoted to social (economic) issues and found it taught the same basic position that "*While the ownership of property is private, its use must always be social*" (p. 7).

Hugo Grotius, the seventeenth century lawyer and writer, held a position that may have originated from the ideas of Aquinas, but used a different basis for property. Like Aquinas, he believed that in an early "*Golden Age,*" private property was unknown and unnecessary. Whereas Aquinas saw private property as a rational necessity, Grotius believed that it evolved as a result of private appropriation through use (Buckle 1991). Buckle used this supposed natural evolution of private property to argue that Hume's position on property was in fact a natural law theory. The significance here is that

Grotius, and later Hume, believed that the natural law was learned only *a posteriori*, and its contents could evolve.

Locke (1693/1967) took a different view of property, basing it on labour. He accepted that *"tis labour indeed that puts the difference of value on everything"* (p.40). This position leads both to the labour theory of value and a labour theory of property. It is coincidental that this is very close to that adopted in Islamic economics, however the Moslems recognise the residual question of the extent of title to the underlying land (*qua* unimproved natural resource) and resolve it in a way that is more sympathetic to Aristotle by only allowing its owners title condition on their submission to the will of Allah.

Hume (1777/1975) based property on his moral sentiment theory, suggesting, that is, acceptance by people was the whole of its moral validation. Fisher (1923) suggested as much when he accepted that *"... property rights as not physical things or events, but are abstract social relations"*. This position is largely what has been adopted in the modern West though it has been refined to assert that *"property rights are relations among men that arise from the existence of scarce goods and pertain to their use"* (Pejovich 1990, p. 27). Pejovich further asserts that this definition is consistent with Roman Law, common law, Marx and the new institutional (property rights) economics. Using an approach based on Pareto optimality, Pejovich concluded that property rights provide persons in a free economy to maximum benefit with zero losses (p. 37-8).

Socialist property rights appear to run counter to most others in denying the private right of productive property. Marx is normally attributed with the most systematic theory aimed at validating the destruction of private property rights, however, in practice this has meant only the transfer of the economic benefits of property rights to the ruling Politburo (Pejovich 1990, p.18-9 & 97).

2.5 Cost Theory and the Just Price

There has been a long debate between various theories of valuation. The two main classes of theories that have been distilled over time are theories that set price (or exchange value) by use value (utility) and those that set price by cost, especially labour cost. In classical political economics although he began with a labour theory, Adam Smith is associated with use value pricing while Marx held a labour theory of value. The most explicit utility value theorists in recent times compose what is known as the Austrian, mainly associated with the work of von Mises (Shand, 1990).

Pricing by utility value appear to be very closely linked to the modern notion of property. Utility value theorists tend to include as part of their argument a strong form of property argument. Shand (1990) devotes an entire chapter to property under the title

Freedom and including references such as the statement by Lord Acton that "*A people adverse to the institution of private property is without the first elements of freedom.*" Two important points follow from this. Firstly, it will be shown that the critical issue is the matter of who owns the final cause of production. Although being the cause of causes, it is extrinsic to the thing produced and St. Thomas Aquinas recognised that it was the property of the purchaser. Secondly, it points to the critical importance of methodology. The dominant positivist methodology of modern economics makes it almost impossible to distinguish the title to the final cause because it is not observable. Property, positively conceived, can only follow from possession, and this implies the 'despotic' rights of property described by Lord Devlin.

This debate regarding utility versus cost pricing has subsided to some extent in recent times with few non-socialist theorists being willing to openly refute a utility theory of value. This is despite what has emerged from this literature survey as a consistent lack of empirical support for the position. Outstanding in this area are the works by Langholm and Seton that variously demonstrate situations that tend to give support to a cost theory (Langholm 1969; Seton 1985).

Langholm used computer modelling to compare full cost pricing to marginalist pricing and concluded that despite full cost pricing, which derives its theoretical basis from a cost approach, being considered theoretically inferior, it performed better than marginal pricing which has the support of current economic theory. Langholm went further and suggested that while theoretical economists display a disdain for cost based pricing, practitioners consider that marginal theory is impossible to apply in the concrete world of actual goods and markets. The concurrence of a practical system out performing a theoretical one in a simulation that should have allowed the latter to perform at its best is telling.

2.5.1 Eigen Values

Seton is less direct in his comparison of the two approaches, preferring to use his own theory of 'eigen' (equal/equivalent) prices to be used as a synthesis of the two. His treatment of labour theory is characteristic of the current trend; he distances himself from it but fails to give convincing criticism, despite valid observations regarding its over use.

2.5.2 Philosophy and Price

Pearce (1987) and Boland (1994) have both presented philosophical interpretations of the available theories from the same general school of thought. Both couched their economics in Thomistic terms and relied on Aristotelian causality to analyse

production. Pearce more than Boland undertook a more explicitly Georgist analysis of price. Boland's objective was a more general analysis of economics.

Boland observed that it is the purpose of the economy to maximise the use value for the community in broadly utilitarian terms. The productive act results in new use value or utility being produced and this belongs to the producer who then sells it to the user or consumer. Because the product and its use value belongs to the person who produced it, and because it is an increase in the total use value (utility) in the community, the producer deserves to be rewarded in proportion to the contribution to the community utility. Hence, Boland concluded that it is the use value that the producer is entitled to charge in the market. This is consistent with Aristotle's *Ethics*, especially the English translation used in this thesis. Pearce was more apprehensive and warned that, " *it is very easy to slip into a subjectivist economics by over-concentration on the demand side of the exchange*" recognising that the object of price was an *objective reality* (p.8).

Meikle (1995) has devoted himself to a very detailed study of Aristotle's economics and questioned how accurately the English translations reflect Aristotle's intent. He presented as part of his larger treatment of Aristotelian economics an entire chapter to the matter of Aristotle, demand and the ideology of translators. It would appear that demand was not necessarily the measure of natural exchange in Aristotle's thought. This is an area for further study.

2.5.4 Thomistic Just Price

Thomas Aquinas's treatment of price is considered to be a major theoretical foundation to the argument for pricing by use value. However, it does have some curious shortcomings. For example, air and water, which are most useful, are free, while gold and stamp collections, which have little actual use, command high prices. Also, use value is a highly subjective quantity, as marketing experts are keenly aware. Marketers earn their income by generating a greater subjective use value in consumers, causing them to pay more for a brand named product, even if it is identical to another. By increasing desire, which is the final cause of a thing and its use value, advertising companies increase manufacturers profits. While the actual operation of advertising and its effects on sale may be complex and open to debate, it is hard to accept that the companies who invest in advertising are not convinced that in some way it supports profits. Advertising can only operate on the consumer's desire, but the consumer's desire belongs to the consumer. Thomas Aquinas was concerned about what the consumer was actually paying for and concluded:

'... if the one man derive great advantage by becoming possessed of the other man's property, and the seller be not at a loss through being

without that thing, the latter ought not to raise the price, because the advantage accruing to the buyer, is not due to the seller, but to a circumstance affecting the buyer. Now no man should sell what is not his, though he may charge for the loss he suffers.’ (Aquinas 1981, Q77 Art 1 Pt.II-II, p 1508).

This notion of an actual value, or worth, residing in a thing is known as its ‘just price’ (*justum pretum*). This passage is the clearest statement of what is known as St. Thomas's double rule of value (Langholm 1992). It clearly states St. Thomas's recognition that one cannot charge a person for what already belongs to him, and a person's desire is his property.

The notion of a just price is also found in several ancient sources. Goyder (1993) noted that it was first explicit in Roman law for the estimation of price in various legal compensation cases. Talmudic economics had the Ona'a rule against ‘overreaching’ (Kleiman 1987) and it is apparent in Islamic economic thought (Islahi 1988). Thomas Aquinas explicitly based his position on Aristotle, especially *The Politics* as well as biblical sources and their commentaries by earlier Churchmen (Aquinas 1981, Q77 Pt.II-II, p.1507-11). It is likely that he would have been aware also of the other early ancient positions, but less likely to acknowledge them.

Aquinas clearly saw that a thing has three evaluations: its worth to the owner, its worth to the purchaser and its own worth. For Aquinas, a price set by the situation of the purchaser is not just by nature if this price is greater than the just price. Obviously if the just price is greater than the value to the purchaser, however constructed, either the transaction will not proceed, or the vendor will accept the lower figure out of need. In this latter case, one would expect that the vendor would be well advised to move into another line of business.

Langholm discounted Aquinas's arguments here by simply asserting that such a subtle thinker as Aquinas could hardly have meant to have asserted such a simple argument (Langholm 1992). He goes on to use Aquinas's ‘double rule of valuation’ to conclude that because it is the vendor's use value that may be used as the basis for price, price is set by the balance of market forces. Aquinas's text seems so contradictory to Langholm's analysis of it, that one could be excused for thinking that he was referring to a different text. This tendency to interpret the Scholastics selectively is also found in some other writers. Chafuen (1986) traced the thought of the late Scholastics, selectively choosing those that even that author described as liberal, to use them to make a case for the modern author's support of liberal free market capitalism. This would be reasonable if these authors engaged the same methodology that the Scholastics used, but they do not. Chafuen's methodology is the

history of ideas, he presents an evolution of positions, but does not attempt to integrate their foundations. Chafuen adopted late Scholastics whose common justifications reduce to the argument that pricing by anything other than the market was not socially acceptable. This appears to be a revisionist approach unduly influenced by sympathies developed elsewhere in his text for modern capitalism. It implies that social acceptability is the criterion for morals.

A second line is taken by other commentators. Dempsey (1935) is representative of a number of authors who conclude that even in Aquinas's time the market was taken as the best forum for judging the just price. With this proposition accepted, it would appear to follow that the market is the only reference needed for justice in pricing. If the markets were and are the best arbiter for the just price, then nothing has changed. Fanfani, (1939) went to some lengths to show that something has changed.

2.5.5 Just Price and Capitalism

In his well known sociological analysis of the relationship between capitalism and Protestant Christianity, Weber noted that the two are more than coincidentally related in the history of Western Europe (Weber 1974). The reaction to his observations have been curious. His concept of a *Protestant work ethic* has been taken up popularly by opponents to Christianity as a taunt, while more serious critics question the whole issue of causality that is commonly attributed to Weber's thesis (Ray 1987). Ray argued convincingly that the resolution of the main criticisms lay in the fact that Weber did not intend the causal conclusions commonly adopted by his readers.

Fanfani, in dealing with the genesis of capitalism, relates capitalism to the decay of the just price doctrine of the Scholastics (Fanfani 1939). This is consistent with both Weber's analysis of the consistency between the reformation and capitalism.

2.5.6 Economics and Value

There are other variations to the value debate which have led Lambert to conclude, in his comparison of different schools of economics that "... *any theory of economics (is) ... based on an express or implied theory of economic value*" (Lambert 1994).

Smith's theory of value which was later adopted by Henry George. At first both authors argue what appears to be a labour cost theory, however both transform this into a negative labour theory. George summarises the final position as:

"It is not the toil and trouble which a thing has cost that gives it value. ... It is the toil and trouble that others are now willing ... to relieve the owner of, in exchange for the thing, by giving him the advantage of the results of exertion." (George 1981, p.246)

This is a curious approach and one which in a very few words outlines a value theory that is quite complex and one which can illuminate our consideration of the other more common theories. It is still not without serious shortcomings and for all of these reasons it deserves careful attention.

At first it appears to provide a *labour value to the purchaser* theory of value, and as such, virtually completes the possibilities available in the matrix of use and labour to the vendor or purchaser as shown in Exhibit 2.2. On closer examination it is partially an acceptance of the (labour) cost of production of Aquinas.

George was considering normal equivalent exchange where value is considered as a relativity between two goods. This is evident in the fact that the purchaser is willing to surrender “toil and trouble” i.e. labour. This labour can only be packaged either as direct labour, money or goods in exchange. George has not specified direct labour, though it would simplify the text. In most modern exchanges the labour is packaged in the money value of the sale to be later used to buy goods.

If the labour was indicated simply by money, then George has given us a theory of the value of money, and then more by assertion than reason. While a labour theory of the value of money may be reasonable, it does not actually inform the price of goods at all. The only explanatory possibility is that the, *toil and trouble that others are now willing* to surrender, is embodied eventually in goods that the other party is willing exchange. This is consistent because in order to buy the commodity the purchaser would first have had to sell either some other good of labour. This means the Smith/George labour commanded theory of value is best thought of a type of reflexive labour content theory. Its advantage is that the amount of labour commanded depends on the utility of the commodity apparently and immediately for sale. A complete analysis of this theory must however include consideration of how the prior sale by the purchaser was priced.

What is being considered is most evident in barter transactions, but it is also in totality what Aristotle and Aquinas referred to as natural exchange. Natural exchange is an exchange of equivalence and was later formalised by Marx as his “C-M-C” exchange, where a commodity is exchanged for money which is further exchanged for a different, equivalent, commodity. In this form of exchange, money is the medium of exchange and the termini are equal in value. The problem of value is to understand how the termini are equated justly. This in turn gives a means of valuing the medium, money. If Smith's position, as developed by George, is correct, he has given us the solution to not one, but two problems. George's statement of the theory will be reviewed here.

George sees the vendor as receiving in exchange for his product, something that has a value equal to the labour that the purchaser was willing to exert in order to receive the commodity. the purchaser's labour commitment was most probably embodied in another commodity. Where money is used as an intermediary, its value is therefore this same labour content of the goods purchasable for the price of the thing on sale. This is a simple labour cost theory of value and half of Aquinas's double rule and the basis for wages observed by Marx. It makes labour the value unit of money. But if this was all his theory was, he could not put a price on land, which has no labour content, nor could he explain the fact that the central objective in capitalism was to sell your products for more labour than they contained. He wanted to explain the former and justify the latter, and his 'command over labour' theory achieved both.

His formulation is not developed in terms of the other party (the purchaser), although we have shown what this actually entails, but stays with the vendor's commodity, setting its price as the amount of labour another (the purchaser) would sacrifice to have that commodity.

George assumes a transaction, with a price and then works back to explain the source of that price. The more interesting problem, which George does not address, is the question of what the conditions are that provide the necessary and sufficient conditions for the transaction in the first place. Exhibit 2.1 presents an analysis of the Labour commanded theory in terms of the decision parameters of the purchaser, and also the implications of what labour commanded actually entails. It is evident that the price for a commodity will be limited by the use value estimate of the purchaser. The labour that may be commanded by the vendor may be anything less than or equal to the purchaser's utility estimation. If the owner is entitled to the full use value of the product, price will be that price that in the purchaser's mind equates his utility with the labour he is willing to sacrifice to fulfil his desire.

The problem comes when it is recognised that the labour surrendered by the purchaser will most probably be in the form of his own product and this must be treated similarly. The result is the equation of everything which is not particularly useful.

This should not be surprising because the it does not recognise the fact that what is commanded (labour, supposedly) must be valued by the same mechanism. Formally, it also does not sufficiently engage the problem of equating utility and cost implicit in Equation 1. Thomistic thought would also have difficulty with the fact that Equation 1 is totally in terms of properties of the purchaser, yet are being used to price the property of the vendor.

Exhibit 2.1: Analysis of Labour Commanded Theory of Value

Value components	Party A (Vendor)	Party B (Purchaser)
Commodity C1 Commodity for Sale	L1a Labour cost to produce for sale. (Also utility value to producer, U1a.)	U1b Use Value; (also cost to self-produce, L1b)
(Commodity C2) Sold to fund the purchase of C1	(U2a) Use Value; (Also cost to self-produce, L2a)	(L2b) Labour cost to produce for sale, (Also utility value to producer, U2b)

George's *labour commanded* theory of value states that the price of a commodity is the amount of labour that its purchaser is willing to surrender in order to have the commodity. In the situation above, if party B desires Commodity C1, he will have to sell his own product (C2) containing labour L2b to get the money to buy C1.

B will consider purchasing C1 so long as: $U1b \geq L2b$

Smith, George and others considered that since A owns C1, then A is entitled to the whole of the value of C1 which prices C1 as:

$$\text{Price of C1} = U1b = L2b \quad \text{Eqn. 1}$$

This labour theory only works if B sells C2 at its labour cost. This tends to be the case for labour itself, but for all other cases B will sell his product, C2. To be consistent, the labour commanded theory must price C2 by the same means. Assuming A is considering the purchase of C2 it will be priced through:

A will consider purchasing C2 so long as: $U2a \geq L1a$

Hence:

$$\text{Price of C2} = U2a = L1a \quad \text{Eqn. 2}$$

Assuming an efficient market, even if A and B do not directly exchange C1 & C2, they will still be priced by Equations 1 & 2. If C2 is sold to buy C1 then:

$$C1 = C2 \quad \text{Eqn. 3}$$

Combining Equations 1, 2 & 3:

$$C1 = C2 = U1b = L2b = U2a = L1a$$

The Labour commanded theory therefore reduces to a relatively indeterminate theory of value. It certainly equates the purchaser's utility with his willingness to pay in labour, but this does not make it a utility theory or a labour theory. It does not price money. When the reciprocal transaction (C2) is included in the analysis, it could lead to any and all theories.

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Value components	Party A (Vendor)	Party B (Purchaser)
Commodity C1 Commodity for Sale	L1a Labour cost to produce for sale. (Also utility value to producer, U1a.)	U1b Use Value ; (also cost to self-produce , L1b)
(Commodity C2) Sold to fund the purchase of C1	(U2a) Use Value ; (Also cost to self-produce, L2a)	(L2b) Labour cost to produce for sale, Also utility value to producer, U2b)

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Smith, George and others considered that since A owns C1, then A is entitled to the whole of the value of C1 which prices C1 as:

$$\text{Price of C1} = U1b = L2b \quad \text{Eqn. 1}$$

This labour theory only works if B sells C2 at its labour cost. This tends to be the case for labour itself, but for all other cases B will sell his product, C2. To be consistent, the labour commanded theory must price C2 by the same means. Assuming A is considering the purchase of C2 it will be priced through:

A will consider purchasing C2 so long as: $U2a \geq L1a$

Hence:

$$\text{Price of C2} = U2a = L1a \quad \text{Eqn. 2}$$

Assuming an efficient market, even if A and B do not directly exchange C1 & C2, they will still be priced by Equations 1 & 2. If C2 is sold to buy C1 then:

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The rationale for George's value theory is interesting. He wanted a theory that could explain the pricing of land, which was his main focus, he was a part of a free market society and therefore inclined to see price as a fact to be explained rather than the result of moral rational actions. His considerations of price and value led him to adopt Smith's introductory suggestion that, "*The value of any commodity, therefore, to the person who possesses it, and who means not to use or consume it himself, but to exchange it for other commodities, is equal to the quantity of labour which it enables him to purchase or command. Labour, therefore, is the real measure of the exchangeable value of all commodities*" (Smith 1778/1910, p. 26). Book VII of *Progress and Poverty* was his argument for private property to consist wholly in terms of a title to labour, and this necessitated a labour theory of value of some kind. The labour cost of self-production outlined above is the logical conclusion of his position, but one which he specifically wanted to avoid. It would not have allowed him to explain the price of land, which has no labour cost for vendor or purchaser. Cognisant of the fact of land price and the rational necessity for a labour cost explanation, his theory was the only reasonable solution. It is insightful to note that he went on to subdivide values that attach to goods with a labour content, and those without as *value from production* and *value from obligation* respectively. He effectively placed the two on opposite sides of a moral evaluation, at least when the latter is held privately.

To appreciate the relations between these various theories, they need to be compared directly. This is difficult because of the apparent variety of sources used for value, and few authors appear to be willing to compare in detail more than two at a given time. If, as Lambert suggests, economic theories rest on value theories, then their comparison must begin with an analysis of the value theories that underlay them.

Boland appears to come close to providing an adequate method for comparing the fundamentals of varied approaches by noting the distinction between cost, value and price. The objective of "value" theories is usually to explain the appropriate price in the market. Value theory should perhaps be re-focused as "price" theory. This would explain the Thomistic interest in just price, the Austrian and broad current interest in market price, and the Marxist theory of surplus that is really the difference between the market price of labour and the market price of the products of labour.

2.5.7 Marginal Theory of Market Value

Adam Smith saw that, "*Labour ... is the only universal, as well as the only accurate measure of value...*" (Smith 1778/1910, Vol.1 p. 32), his labour commanded theory of price differentiated market (exchange value) from labour cost. This initiated the line of thought that has become known as marginal price theory. This theory of value is based

on use value, where the market optimises the total aggregate use value, or utility, by valuing commodities by the subjective calculus of the user.

"...the marginal theory of exchange, or market values...simply regards value in exchange as the first derived or 'differential' function of value in use; which is as much to say, in ordinary language, that what a man will give for anything sooner than go without it is determined by a comparison of the difference which he conceives its possession will make to him, compared with the difference that anything he gives for it could have had instead of it will or would make." (Wicksteed 1914, p.5)

The prospective purchaser weighs up the subjective benefit that the commodity will have for himself and deducts the subjective cost of the toil and trouble that must be surrendered for its purchase.

Knight presents a curious synthesis of Scholastic morality and use value pricing when he states: *'Value and cost are...axiomatically equal, and as in the exchange system the value of all similar units must be equal, so must their costs. In the writer's opinion this is also socially and morally correct.'* (Knight 1924, p.176). While this appears to conform to the Scholastic position, it must not ignore his understanding of cost which includes *'...the rent element (which) always equalizes them'* (p.175). Although Knight was apparently referring to land rent, his argument would appear to uphold any economic rent.

He has adopted the Scholastic moral necessity for price to equal cost, but by unabashedly including rent he has actually eliminated any need for the essential equation. Simply, if price exceeds cost, then rent should fill the gap. This is the opposite causal direction to true costs, which sum to contribute to price under the operation of just price. There is no intrinsic need in the case of rent, simply an opportunity. Incidentally, it is in fact a validation for the Ricardian law of rent which asserts as much, contrary to the assertions of Wicksteed.

2.5.8 Price Theory

When considering price, two approaches may be followed. One is empirical, which is to analyse price as it occurs in some markets and to provide theory to explain it. The other is rational, seeking to provide guide-lines for the setting of price. The former assumes that value is set by the market, the other assumes that the market should be conformed to value. Free market theorists tend to use price as a given quantity and the indicator of value, hence adopting the empirical approach. Land valuation theory sets actual sales as the ultimate indicator of value, given willing but not eager parties, and is a good illustration of this approach (Rost and Collins 1971).

Normally there is no possibility of a price being at variance to value, unless there is some compulsion. Good and bad prices are therefore determined by the degree of freedom from compulsion. The rational approach seeks to set value according to some notion of good and to use this value to test the goodness or otherwise of a market price. The resistance to monopolistic trading is a good example of this perspective today, although the usual remedy, the introduction of a competitor, while politically popular is by no means unequivocally proven to be a complete solution. The point here is that a price may not be a good price, not because of faults in the market, so much as the market not settling on a price that is conformed to value.

A second dimension that may be considered is objectivity or otherwise of price. Labour contents, either to the vendor or purchaser may be reasonably objective for the majority of products, but use values, the amount of good a person derives from a thing is necessarily subjective. Modern marketing directs considerable resources to enhancing the evaluation of use value to the purchaser. There is a common tendency for rational treatments of price/value to gravitate towards labour theories of value because they provide objective formula for value, thus simplifying the test of price against value. Marx's labour price is an example of this, though Aquinas escapes the trap by admitting either an objective or a subjective element into his value theory. Where Marx straddles use value and labour cost, Aquinas bridges labour cost and opportunity cost of sale. Marx is doubly empirical while Aquinas is doubly rationalist.

Exhibit 2.2: Comparison of Pricing Theories

<u>Price</u>	Price derived from vendor	Price derived from purchaser
Use <i>Subjective</i>	Price as the utility of the thing to the vendor, <i>qua</i> good, not <i>qua</i> commodity Aquinas as part of double rule $(UP \text{ or } LS)UV > LC$	Price as the utility of the thing to the purchaser Adam Smith's use value, Marx's observation of free market capitalist commodity pricing Implicit in modern free market economics $LS > UP > (UV \text{ or } LC)$
Labour Content <i>Objective</i>	Price as the labour content of a thing Aquinas as part of double rule Marx's observation of <i>labour</i> price $(UP \text{ or } LS)LC > UV$	Price as the value of labour the purchaser is willing to surrender for possession Adam Smith's labour theory Henry George $UB > LS > (UV \text{ or } LC)$

LS = Labour saved by purchaser

LC = Labour cost to vendor

UV = Use value to vendor

UP = Use value to purchaser

The various approaches are summarised in Exhibit 2.2. This shows a matrix formed by the party that sets the price and the method (use or labour). It also includes the conditions for a transaction to take place, in the form of an inequality, with the quantity that set the price highlighted.

In the summary form the various price theories may be contrasted fairly easily. In Exhibit 2.2, Aquinas occupies the price from the vendor column, sharing labour cost pricing with Marx. This area is a little more involved than it at first appears. The classical assessment of the cost of labour is in terms of the cost of keeping a unit of labour at a subsistence level. The labour unit was considered in the eighteenth and nineteenth centuries as a labourer, his wife and two children, and the appropriate wage rate, especially in English literature was that level that allowed them to no more than survive and reproduce themselves. This has significance today, mainly with the advent of double income families and falling fertility rates. To sustain a modern Western family, wage rates may be set with the expectation that two incomes will be supporting

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Exhibit 2.2: Comparison of Pricing Theories

<u>Price</u>	Price derived from vendor	Price derived from purchaser
Use Subjective	Price as the utility of the thing to the vendor, qua good, not qua commodity Aquinas as part of double rule (UP or LS)>UV> LC	Price as the utility of the thing to the purchaser Adam Smith's use value, Marx's observation of free market capitalist commodity pricing Implicit in modern free market economics LS>UP> (UV or LC)
Labour Content Objective	Price as the labour content of a thing Aquinas as part of double rule Marx's observation of labour price (UP or LS)>LC> UV	Price as the value of labour the purchaser is willing to surrender for possession Adam Smith's labour theory Henry George UP>LS> (UV or LC)

LS= Labour saved by purchaser
 LC= Labour cost to vendor
 UV= Use value to vendor
 UP= Use value to purchaser

a family of somewhat fewer children than the past. Two centuries ago, the excesses of capitalism that gave Dickens his raw material for reflection on the lot of English working people, Marx the ammunition for the Communist Manifesto and *Das Kapital*, caused families to send both parents and children to work: today it is apparently being freely chosen as a right.

What is often ignored from the estimation of labour cost calculations, is the basis for this cost estimate. It is in fact the costs of the basket of consumables and other costs that constitute a subsistence lifestyle. If these come at an inflated price, as George suggested with rent, then the labour cost theory is not itself an absolute base. The apparent regress is halted if one assumes that the costs under consideration are themselves based on the labour costs of other producers and labourers.

The second column, price derived from the situation of the purchaser would be considered illicit by Aquinas, though not by later Scholastics as evidenced by Langholm and Chafuen. George's contribution falls into a reasonable relation to pure use value when one considers the various situations of the purchaser. If the purchaser identifies a desire for a thing and that need is considered greater than the price set by the vendor's costs or use value, the purchaser will act to acquire the thing. If the labour required by the purchaser to produce the thing is less than the use value to the purchaser, the purchaser will be prepared to pay up to the price of that labour.

2.5.9 Social Perception of Demand Based Pricing

The current dominant paradigm for price is based on the marginal theory of exchange which has been shown to be based on a balance of use values (Wicksteed 1914). This approach all but removes the significance of the objective nature of the object itself - if a thing is regarded as having a high use value, this will be transformed through the strong demand that such a high use value infers into a high price.

Conlisk has demonstrated the lengths that pricing by demand can be manipulated to maximise profits in the case of periodic discounting of prices to temporarily access a different part of the demand curve and exploit demand that would not enter the market at the regular price (Conlisk, Gerstner, and Sobel 1983). More generally, the financial techniques involved in the practices of pricing and profit planning, and accounts receivable management (Wilson and Keers 1990, pp.165-8 & 326-9), are commonplace examples of procedures that maximise profit by the arbitrary manipulation of price. They all rely on the analysis of sales increases resulting from lowered prices, that is, a shift in the point of the demand curve that is used.

The only limit is perhaps the possibility of a potential purchaser choosing to produce the item for himself, but beyond this, the actual material content of the thing is

apparently according to the theory. Sassone recognised this as a non-contentious truism when he observed that OPEC was careful to keep oil prices as high as possible, but always limited by the price level that would make shale oil viable (Sassone 1994, p.34).

Frey has analysed the sociology of price perception, and found that the conventional economic notion of rationing by price increase is perceived by most people as repugnant (Frey and Pommerehne 1993). This is consistent with common experience, where there is dissatisfaction when a product is found to objectively contain less than its price would suggest.

If demand as a basis for price is on shaky ground, then market theory is doubly problematic if Wicksteed's conception of the supply is adopted (Wicksteed 1914). The supply curve to Wicksteed is no more than a reflected demand curve belonging to the possessors of the commodity in question. It could be considered as the demand curve for money by the owners of a commodity being taken to market. In his own terms:

'But what about the "supply curve" that usually figure as a determinant of price, co-ordinate with the demand curve? I say it boldly and baldly: There is no such thing. When we are speaking of a marketable commodity, what is usually called the supply curve is in reality the demand curve for those who possess the commodity; for it shows the exact place which every successive unit of the commodity holds in their relative scale of estimates' (Wicksteed 1914).

This should not be surprising because the marginal theory of pricing is set purely in terms of equating the pleasures of ownership between the various players in the economy. These are the very stuff of demand. If demand is under suspicion as a component of just price, all theory based on utility theory is flawed, because utility is the technical term for the pleasure of ownership.

This is an issue that appears to receive relatively little attention in the more recent literature. Boland's treatment is sensitive to a most important philosophical point in this regard (Boland 1994). The very fundamentals of economics are related to the optimised provision of society's material needs. These may be proxied by material objects or commodities, but, as Fisher reminds us, the fundamental interest for humans is the experience of living (Fisher 1930/1977). If the very reason for the science relates to the optimal balance of material things, then it is in this arena that value should be assessed.

2.5.9 Practicalities of Demand Based Pricing

Regardless of the philosophical merits of demand based pricing, there are some practical issues.

Uzair pointed out the gap between economic assumptions and western realities when developing an argument for Islamic economics (Uzair 1976). Working went further by exploring the shortcomings of actually observing demand and found four reasons for any empirically derived demand curve being highly suspect. These range from the impossibility of separating them from supply considerations to the difficulty of constancy over time and in the face of other changes in the economy (Working 1927).

Working's discussion is never far away from Wicksteed's difficulties with the reality of supply, and his conclusion suggests that in demand theory, economists have a likeable academic notion that will forever be totally quarantined from the real world of commerce. In this he is joined by others who are likewise puzzled by the gap between economic theory and the concrete realities in the commercial world (Clapham 1922a; Clapham 1922b).

2.5.10 Demand as Basis for Price

The just price theory cuts at the heart of market theory because it rejects demand as a just component in price setting. Demand relates to the behaviour and the experience of the purchaser, things that do not belong to the vendor, and for which a charge by the vendor is tantamount to selling what is another person's property to that person.

2.6 ECONOMIC DISTRIBUTION AND THE RATE OF PROFIT AND PRICE

One of the fundamental issues in economics is the problem of economic distribution, relating to the sharing of the benefits of production between the various economic parties. As land, labour and capital are the factors of production, distribution is primarily between them. Since most products are produced for sale to others, persons as consumers may be distinguished from persons as controllers of various factors of production. The state will also take a share as taxes. It is also useful to consider money as a *de facto* factor of production and to separate its share in the distribution process as a sub-group of capital.

Kaldor identified three approaches to the understanding of distribution (Kaldor 1955). Firstly, Ricardo and Marx began with the payment to labour as set by their subsistence needs, leaving land and capital to compete for the remaining *surplus*. Secondly, he described distribution as a function of implicit monopolies following Kalecki. Finally he considered a neo-Keynsian theory based on the capitalist's propensity to consume, which tended to make wages the residual.

Sraffa believed that the rate of profit was '*... susceptible of being determined from outside the system of production, in particular by the level of the money rates of interest*' (Sraffa 1960/1975, p.33), which would suggest also that wages are a residual. Panico analysed Marx and Keynes, concluding that their theories both included aspects that supported Sraffa's theory (Panico 1988).

Nuti (1971) concluded his survey of theoretical explanations of the distribution problem recognising the potential usefulness of Sraffa in moving towards the convincing theory that, he admitted, was still apparently some way off.

An enduring problem in Political Economy is the relation between price and the rate of return on a particular asset. Wilson is typical of current financial theory which sets the value of a capital asset as the *present value of its future returns* (Wilson and Keers 1990). The financial realities here involve discounting and summing the future returns, or dividends, flowing from the possession and use of an asset. These could well be infinite, but the use of a discount factor, usually expressed as the required rate of profit adjusted for risk, provides a practical asymptote. The more classical method, referred to in the real estate industry as the '*capitalisation method,*' is mathematically simpler, being the division of the annual dividend by the expected rate of return, or capitalisation rate. The capitalisation rate and the discount factor are reflections of the anticipated (often expressed as the *required*) rate of return or yield.

In this way the valuation of a capital asset is wholly on the basis of its financial utility. In terms of Thomistic just price, this evaluation could perhaps be justified as the value to the vendor, or the application of the second part of the double rule.

The more problematic part of asset valuation concerns the rate of profit, or capitalisation rate used in the discounting process.

Perry adopted the rate of interest applicable to money to capitalise land rents to set a price for land (Roll 1942). This infers that money interest is a causal influence in the determination of land yields. Conversely, Ricardo considered that rates of profit regulated the interest rate, inferring an acceptance of the reverse causality, this is the view that has been dominant since the nineteenth century (Panico 1988).

Marx used a more complex analysis. Despite recognising the dependence of interest as a share taken from the capitalists total profits, he ultimately recognises the virtual independence of interest rates from the rate of profit. Following Hegelian conflict theory, he interprets money interest as largely set by the outcome of the conflict relationship between bankers and capitalists. Panico summarised Marx's position in this regard in the following terms:

'The direction of this influence he (Marx) said, depends upon the role and position of power of borrowers and lenders in the process of reproduction and in the social structure.' (Panico 1988, p.100)

Marx did not ignore that bankers generally had the upper hand in the relationship because of the ability to create credit rested with them. The limits to the outcomes for long term money interest rates appears to be zero as a minimum and the rate of profit as a maximum. This ignores the possibility of dynamic effects flowing back into profits and asset prices that will adjust asset prices downwards in periods of high interest rates, thereby lifting profit yields. Although modern financial modelling includes capital valuation movements as an additional component of profit or loss, this is sometimes ignored in theory. It does reinforce the possibility that the causality does move as Perry suggested from money interest to profit rates.

More recently Keynes has contributed to the issue by adding a psychological dimension to the determination of average rates of interest when he stated:

'Any level of interest which is accepted with sufficient conviction as likely to be durable, will be durable; subject, of course, in a changing society, to fluctuations for all kinds of reasons round the expected norm.' (Keynes 1973, p.203)

Clearly, this is a psychological process, not bound in any ordered way to particular relationships with other parts of the economy. While the psychological determinants are not explored, and some psychological calculus involving interests rates, perceptions of demand or other factors in the economy are not excluded, it does put an end to the question of causality between profits and money interest.

Keynes extended this psychological basis into other key economic factors. If perception is the basis for interest rates, there may be an influence by these on decisions regarding acceptable rates of profit, which would in turn affect capitalised prices. In addition, Keynes recognised that the evaluation of price as the present value of future returns also revolves on an evaluation of these future returns, which, being future events cannot, by nature, be known. Keynes is surprised to admit that this too is a

'...psychological phenomenon ... The value of a company's shares, or even its bonds, will be found to be sensitive to a degree, which a rational observer from outside might consider quite absurd, to short - period fluctuations in its known or past profits.' (Keynes 1971, p.322)

Apparently Keynes did not consider the recent past to be a very sensible way to predict the long term future, despite recognising that it was the most popular technique in use. Despite the impressive mass of his theory, he left no superior concrete methodology to deal with this problem. The current literature and debate relating to the applicability of discounted cash flow analysis to asset valuation, especially in real estate, may profit from a review of Keynes's observations in this respect.

Panico recognised that both Marx and Keynes rejected the possibility of rates of profit or money interest being set by any natural or material laws, making it virtually independent of production and profit:

'For Marx and Keynes, the rejection of natural or material laws, which are in opposition to an historical conventional analysis of the interest rate, corresponds to their view of the role of the banking sector in the economic system. This sector can have the power to determine the conditions of liquidity of the economic system. It can, therefore, regulate the interest rate and can make smooth or difficult the working of the production process, which requires the provision of financial means.' (Panico 1988)

Moreover, he concludes that by merging the psychological acceptance theory of Keynes with the conflict theory of Marx and the political realities, the only limits to the interest rate are:

"The existence of intense competition among bankers, the adherence to some international agreement, or the introduction of legal arrangements which increase the control of the government over the banking sector, may reduce the power of this sector and allow other groups or decision centres to influence the conditions prevailing in the money markets. The determination of the average interest rate, therefore, does not depend on the rate of profit. It is rather, as Marx's analysis in particular suggests, the outcome of the conflictual relations between different groups of lenders and borrowers, like bankers, industrialists and the government, trying to affect through policy decisions, the liquidity conditions of the money markets.' (Panico 1988)

This makes money interest rates a social outcome which will in turn influence rates of profit and hence the valuation of capital assets. The 'required' rate of return used in financial analysis such as the currently popular 'discounted cash flow' (DCF) analysis' is therefore derived psychologically. A significant factor in its determination is the

interest rate on money, which Marx saw as a social outcome of conflict relations between economic players.

Dobb surveyed the dominant distribution theories and concluded that, while he found no convincing theory of distribution, *'another plausible hypothesis is the minimum rate of profit is somehow fixed by some kind of quasi-political or institutional decision-mechanism'* (Dobb 1973,p.270-1) which he recognised as Sraffa's theme. While he is critical of the earlier theories, he seems to miss the opportunity to recognise the possibility of their partial compatibility. As Panico recognises the fact that Keynes and Kalecki both see wages as the dependent variable, and Sraffa is certainly continuing this theme, Panico has shown that even Marx believed that money interest rates were an independent variable and therefore a determinant of profit rates.

Kalecki has perhaps come closest to uncovering the core issue, although slightly more subtle than his interest in monopoly. Dobb's criticism of him is telling in this regard. Dobb notes that an implication of Kalecki's theory that distribution problems arise from imperfect competition that enables virtual monopoly situations is that *'...the markup would be zero under conditions of perfect competition'* (Dobb 1973,p.269). While Kalecki may not have been clear in his expression, what he undoubtedly meant was not zero markup, but that markup that would result in normal profit. Samuelson recognised this fact when he described the demand curve as perfectly horizontal (price fixed regardless of quantity), at the level of normal price when the conventional condition of perfect knowledge is applied (Samuelson 1975).

Accepting that this was Kalecki's intention, he is simply observing that the problem of distribution exists because of super-normal profits, otherwise known as economic rent. Economic rent is the difference between the cost of production, including reasonable rewards for capital and management, and the price. Where price is set by the market and includes demand, the price will be somewhere between the cost value and the use value. The market therefore will include economic rents in all cases except where so many enter as suppliers that price reflects only supply costs, i.e. perfect competition. This is Kalecki's point, apparently, that Dobb finds troublesome. The appropriation of economic rent by the vendor is the core of the rejection of just price that was the genesis of capitalism (Fanfani 1939).

2.6.1 The Nature of Supply and Demand

Aristotle initiated the belief that price was demand-based when he proposed:

"There must therefore, be one standard by which all commodities are measured. This standard is in fact demand, which holds everything together (for if people had no needs, or needs on a different scale, there could be no exchange, or else it

must be on different lines); but by a convention demand has come to be represented by money. (Aristotle 1976, p.184)

This belief is consistent with his 'final cause,' (desire, need, demand) often referred to as the 'cause of causes' because without it a thing would not be brought into existence. He is recognising that production would not proceed if there was no demand, for products, which is true. However, that price should equal demand is not so clear. Even in pure market theory, it is set somewhere between utility value and cost.

With the rate of money interest and the rate of profit recognised to be social products and not strictly determined from within the bounds of the economy, other related key economic variables deserve similar review.

In harmony with Aristotle's demand pricing, the Austrian School, beginning with Menger has championed the subjective theory of value, asserting that price is set by a psychological evaluation of utility (Dobb 1973, p.189-195). This concept has been developed by later members of the Austrian School, such as Weiser, Böhm-Bawerk and Ludwig Von Mises (Chafuen 1986; Dobb 1973).

Böhm-Bawerk especially gave a psychological account of price and interest rate. Koslowski explored the extent to which this leaves economics determined from without. He adopted Schmoller's belief that "*Supply or demand as summations of psychic forces, but not as real monetary or credit quantities, influence the value.*" (Koslowski 1992, p.26), but also Schmoller's belief that the '*... economy is not only the sphere in which exchange and production occur, but also the ethical order of that part of social life that is economic.*' (ibid. p.26). In this way Koslowski argues for a *psychological-moral* dimension to be included within the discipline. He is reversing Marshall's treatment of the discipline from seventy years earlier.

Gallimore's application of psychological methodology to the behaviour of valuers reflects the doubly subjective nature of property valuation (Gallimore 1996). Not only is value *qua* price a subjective evaluation dependent on the persons in the market at the time of sale, but valuers may be shown to display curious psychological characteristics in reaching their forecast of this future behaviour.

2.7 THE CONCEPT OF SOCIAL ECONOMY

Market economics matured in the eighteenth century causing the massive impoverishment of the working people at the end of that century and into the next. This eventually gave rise to the opposing socialist trend of the nineteenth century that eventually matured into Marx's *Des Kapital*. Hence, by the end of the nineteenth century there were two opposing economic theories, free market theory, with its unlimited private property and socialist theory with its rejection of private property.

The nineteenth century was ablaze with the failures of free market economics, just as the twentieth century was dominated by the failure of socialism. It appears that the closing decades of the twentieth century were marked by a rekindling of faith in the free market. This century has also been visited by various attempts to establish an economics that avoided the errors of both theoretical poles. These have often been heralded under the collective banner of the economics of *"the third way."* These tend to be motivated by a belief, not so much on the theoretical faults of the dominant economic poles, but more on a perception that positivist theories of behaviour alone are insufficient to meet the economic needs of society. Marx is perhaps himself indicative of this motivation, though his methodology tends to avoid overt moral method in favour of quasi-metaphysical derivations of Hegel.

Major Douglas, a Canadian Engineer, manager and politician, recognised the deficiencies in Western economies and developed his *"Social Credit"* theory as a method of correcting perennial mal-distribution. His theory developed a strong following and was applied in Canada for a time. It was primarily focused on money supply and a novel 'social dividend' designed as a form of negative tax to reward productivity. Douglas recognised that the fundamental problem that gave rise to economic instability was the denial of sufficient money to the working person to purchase the products generated.

More recently, Schumacher focused on the gap between persons as producers and persons as consumers (Schumacher 1974, p.87). The gap is the same one that Douglas recognised, though Schumacher develops it in a slightly different direction. He is concerned with the way that the gap is really a drain on the ordinary economy that flows to the unproductive members of society. Schumacher sees this as a broader social problem when he observes:

"The prestige carried by people in modern industrial society varies in inverse proportion to their closeness to actual production." (p.125)

His prescription is for a return to smaller scale productive units, and therefore less non-productive overheads through an attitudinal change.

Wilhelm Roepke, writing between the wars, offered a similar prescription. He was aware that economics, as part of a civilised society, demanded an ethic that went further than self-interest (Roepke 1948/1996). His solution was also based on decentralisation and greater economic autonomy to working people. He described his vision of economics as *"This 'third road' of economic policy (which) is, above all, a road of moderation and proportion."* (p.271)

These approaches all share the intention to maintain private property without allowing it to continue to disadvantage the agents of production. In reviewing the

social encyclicals, Ederer noted: *"While the ownership of property is private, its use must always be social"* (Ederer 1995, p. 7), suggesting a social responsibility attaching to private property.

A common theme that underlies these promptings towards smaller organisations, and greater worker participation in the fruits of production, is a critique of the now dominant corporate form. Simon outlined this position when he suggested: *"Having perhaps benefited briefly by corporate organisation, America might now be better off if the corporate form had never been invented or never made available to private enterprise."* (Simons 1948, p. 34). More recently van Eeghen outlined in detail the capitalist case against the corporation, demonstrating how it eroded the genuine free market and consequently other aspects of modern democratic society (van Eeghen 1997). Macken came to a similar conclusion through a review of the legal and historical debate regarding the corporate form, reviving concerns that were apparently rife in the nineteenth century (Maken 1992).

2.8 THE NATURE OF OWNERSHIP

Ownership, especially ownership in land, is a critically important issue for any society. Today the major economic ideologies, socialism and capitalism, differ as a result of their understanding of ownership.

Private ownership is a part of every society, even though the ownership of the means of production are considered a State right in most socialist societies.

The question of the rights and duties that attach to ownership is basically a philosophical one, located in ethics. Langholm observed the scholastic twin rule of ownership, private ownership and use in common (Langholm 1992). This view upholds private ownership, but also insists on the application of one's possessions for the common good. In this way it is a combination of the tenets of socialism and capitalism, however unlike either, the criterion for just behaviour was deontological, not political or utilitarian.

The meaning of ownership is best illustrated in the ownership of land where ownership is seen as "a bundle of rights" where a certain minimum set is considered ownership, though the possession by others of particular rights to land may concurrently exist. To other possessions, chattels, a similar notion can be used, where ownership does not necessarily entitle all possible uses of a thing.

A second fundamental question is the source of ownership title, that which gives one the right of ownership. Several possibilities have been considered. The most liberal view is that anything may be owned. This would even include other people, a practice

generally rejected today. A more limited perspective is any non-human material thing. This is the current general belief.

Marx suggested that the means of production should not be privately owned as a way of returning to workers title to their products. Veblen had a notion of “collective social wealth” where the achievements of the past formed a reserve that should be the heritage of all people, not simply those who control the material tools that embody this past technological treasury (O'Hara 1995). Almost complementary to this is Henry George's theory of ownership that suggests that ownership is title to the labour contained in a thing. This approach both validates the ownership of material and intellectual products and renders problematic the ownership of land, which has no labour content.

One would expect that if title is based on the labour embodied in a thing, then the limit of title would be the limit of labour. This would immediately imply Aquinas's cost theory of value, but as we have seen, George prefers to make the labour content the basis to full title and at least the validation of any amount of labour in return. He does at least go part way to limiting this title by expanding his ‘value from obligation’ as a parasitic title that is the result of political, rather than natural mechanisms. His theory of ownership and his theory of value are closely related, as indeed are most of the other theorists.

2.9 LAND OWNERSHIP

Land is a special case of ownership. In countries such as Australia, land ownership is derived from feudal tenure, the crown (state) holding ultimate title and even the most complete title to land, freehold, is subject to various restrictions. Legally, the laws of a state extend over its lands, inferring that the ownership of land, and human activities on the land are under the influence of the state.

2.10 LAND AND SOCIETY

Culturally, private land tenure is a peculiarity of the modern West, shared with few cultures beyond the late Greek and Roman Empires (Small 1997b). Aristotle taught that private land ownership should not be permitted beyond need and be conditioned on expectations of civic and military service (Aristotle 1992). Observers of indigenous people repeatedly note that customary treatment of land is communal (Bannerman 1996; Booth 1990; Boyd 1995; Caraman 1975; Hall 1958; Hornby 1996; Savae 1994; Teggart 1969; Terblanche 1996; Toms 1996).

Western capitalism developed in no small part as a result of the transformation of an ethic of public responsibility attached to land ownership and a sense of proportion in terms of holding to one of acquisitiveness (Halterman 1988).

One of the earliest references to land ownership and administration is found in the Holy Bible:

In the year of jubilee the field shall return to the one from whom it was bought, whose holding the land is. (Lev. 27:24)

The jubilee occurred every fifty years, and it was Moses' decree that the land should be returned to its owners at that time. This clearly indicates an intention to respect private property and in addition ownership rules particular to land. Apparently, Moses did not want his people to be dispossessed of their land and even though they were permitted to sell it, it reverted to the original owners in the jubilee year. This is a prototype for leasehold.

This early example is also reflected in the attitudes of many native peoples who see the land as the inalienable possession of the people or tribe. Ezigbalike summarises the cultural background to current interest in native title reflecting this common attitude (Ezigbalike 1994), and this attitude is also found in other authors dealing with a variety of native peoples (Bannerman 1996; Boyd 1995; Hornby 1996; Rakai 1995; Savae 1994; Terblanche 1996; Toms 1996; Williamson 1996; Williamson and Enemark 1996). The historian Belloc observed that the social works of the Medieval period, such as the establishment of hospitals and care of the poor were funded from "excess rents" referring to the fact that in the feudal system, land was owned by either the state or Church, and hence ground rent was public revenue, and hence directed towards public activities such as defence, law and order, welfare or the support of the clergy (Belloc 1937/1973).

Several economists and historians indicate that the relative standard of living of working people in England before 1500 AD was superior to its level in the mid-nineteenth century (Cobbett 1824/1988; Green 1874; Lingard 1883). This disparity continued well into the twentieth century (Charles 1991; Peace 1933; Rogers 1884/1949), though a systematic comparison between current relativities and those of the late fourteenth century was not found.

In each of these societies, ownership of land is treated as a special case, where the wealth of the land is the property of the community, either as family, tribe or community.

Barlowe outlined the origin of rent theory with the Ricardian law of rent (Barlowe 1958). This relationship posits a relativity between land and the other factors of production solving Perry's problem with the par (Roll 1942). Barlowe notes that Ricardo, the French Physiocrats, Adam Smith, J.S. Mill and others all held the belief

that land rent was the appropriate source of community revenue. This view was limited by Ricardo's reliance on agricultural fertility as the determinant of land value, a view inappropriate in urban situations and hence limited. George extended Ricardo's model by relating land values in urban areas to access to social benefits accruing to position with respect to population (George 1879/1992; George 1981). This development locates land value as a social product.

If land value in urban situations is supported by the quality of the society that surrounds a particular site, then it is produced by the development of that society. George connected this observation with the moral point that the value of a product should be shared in proportion to the various agents' causal involvement in its production. The economic evil of slavery is premised on the observation that slave workers do not enjoy a just share in their product. George's conclusion that if it were society that caused urban land values, then it was to society that such values should accrue. Small (1997a) demonstrated the widespread support for this moral connection in the beliefs that underlie what is currently referred to as customary title as well as the land systems of many ancient cultures.

The significance of the types of land tenure on society may be argued to be a social, a moral and, most of all, an economic issue. The rising issue of customary tenure is a social/cultural issue that is expressed largely in economic terms (Bannerman 1996; Ezigbalike 1994). The treatment of land in comparison to other assets is an economic issue that appears to be largely fought on moral and metaphysical grounds. George's remedy hinged on the metaphysical distinction between land and other material goods, just as the neoclassical rejection of it begins with the assertion '*... that as there is no theoretical difference between the part played by other factors of production ... so there can be no general assertion about rent and land which is at once true and distinctive*' (Wicksteed 1914, p.20) or similar.

In his encyclical letter *Rerum Novarum*, viewed by some as an attempt by certain vested interests to discourage Catholic interest in the distinction between land and other forms of savings, Pope Leo VIII asserted, '*Therefore if he saves something by restricting expenditure and invests his savings in a piece of land in order to keep the fruit of his thrift more safe, a holding of this kind is certainly nothing else than his wage under a different form*' (Leo XIII 1891, n.9 p.8). This statement is quite complex. It has been taken as part of a censure against Henry George, and in context this appears reasonable. It is a definite acceptance of property in land, however it has an important provision in terms of use rights. The pope specifies land property as a valid form of saving, he does not make any comment as to what type of return may be had from land

investment. Considering the pope's theme elsewhere in the encyclical regarding private property with common use, the pope's intention may not be so wide as to validate all property investment.

Many cultures perceive land as the possession of the whole society (Small 1997a). Islamic legal theory is illustrative of this view from nature where the Qur'an asserts:

'The nationalisation of all natural resources (land) may be argued on the basis of two verses of the Qur'an: 'The first states that God has left His natural resources for all men {1:29}. The second states that God emphasises the entitlement of all men equally to the necessities of life {107:7}.' (Nomani and Rahnema 1994 p.68)

Using this general metaphysic for the origin of land and its conveyance to society by God, many other cultures have various communal tenures. Islam is perhaps representative of the more advanced of these, where it allows land to be privatised by the application of labour, limited by one's own needs, and by the prohibition of such privatisation disadvantaging others (Nomani and Rahnema 1994 p. 66).

2.10.1 Land Tax

In modern times the major impact of Georgist theory has been in terms of the taxation of land (Becker 1969; Break 1978; Brown 1979 1924; Chandler 1982 1980; Dunkley 1990; Ekelund 1990; George 1881/1982; Harris 1983; Lindholm 1967; Lynn 1976). This ignores George's position on many other areas of political economy such as tariff barriers [George, 1980, 1886 #108] and population (George 1879/1992, Book II).

Most of the literature on Georgist theory appears to be theoretical, which is a difficulty in the present empirically oriented economic world. This is largely due to the difficulty in conducting large scale experiments with land tenure and the absence of data where the treatment of land is the only independent variable. The positive effects of land reforms such as Japan appear to present some empirical validation of Georgist theory (Manchester 1979). MacArthur believed that the inequality of land tenure in Japan was a social problem that needed correction by the redistribution of land. His land reforms enabled him to announce '*... that 98% of the country's farm land belonged to the people who tilled it*' (Manchester 1979, p.509), and resulted in reduced peasant discontent and increased agricultural production.

Das has shown an empirical relationship between the polarisation of wealth in a society and the economic cycle (Das 1993); Raskall has shown that in Australia in 1986 over half the real estate in Australia was owned by 10% of the population, the top

1% owning 13% alone (Raskall 1986, p.76). Geisler has made a strong case for the inclusion of land in considerations of social policy, especially welfare and taxation and points to the heavy polarisation of land ownership in the USA, where only 25% of Americans own land and of those, the top 1% own 40% of the country and the top 5% own a total of 75% (Geisler 1995).

Singapore appeared to be cognisant of the mechanics of land value at the time of drafting its constitution, with its only marked variation from the Malaysian constitution from which it was derived being with respect to compensation for land values (Small et al. 1996). The government at the time recognised that land value could proceed from off-site community investment and for the community to resume land at values that were caused by the community's own investment would be immoral.

His insistence that the best way to deal with the distribution problem was through the adoption of a taxation system based on land tax and is found debated in most texts on urban economic theory (Barlowe 1958; Harvey 1987; Kieve 1977). Gaffney illustrated the appropriateness of the concept for royalties on extractive industries. Land tax as the prime source of public revenue is not a popular notion for those who hold interests in land.

2.10.2 Economic Theory and Vested Interests

Roll noted that the history of economics is dominated by the thinking of those who held economic power at the various times (Roll 1942). It is reasonable to assume that an economic theory that challenged powerful vested interests would not find easy acceptance. George was not without powerful critics in his own time (Andelson 1979b). Even the Pope included references to the treatment of land that have been broadly recognised as being specifically directed against George in his well known encyclical *On The Condition Of The Working Class* (Leo XIII 1891). Gaffney has outlined the history of the attempts to sway the study of economics into a position antagonistic to George (Gaffney 1967). It appears to have been successful. This is especially true when the general public also believes that they are the beneficiary of a particular economic situation.

The history of George's success in promoting his economics is colourful (Barker 1991 1955); although he is an American his theories have found at least two applications in Australia as well as other countries. The leasehold tenure in the ACT successfully utilised Georgist principles for many years, effectively eliminating the cost of land in that territory (Brennan 1971). Also, the NSW reliance on tax from the unimproved capital value of land for local government funding follows his theory. Many other writers support the position (Andelson 1979a; Busey 1992; Dowe ; Gaffney 1994; Harrison 1983; Kavanagh 1995; Pearce 1987; Rushdoony 1982).

2.11 Land as a Factor of Production

Land was conceived by the classical economists as one of the three fundamental factors of production along with capital and labour. The trend in economics over the last century has been to combine land within capital, effectively condensing the factors of production into two. Wicksteed goes one step further in asserting, “...*that there is no theoretical difference between the part played by land and that played by other factors of production...*” (Wicksteed 1914, p.20). If one accepts this assertion then there seems to be no point in distinguishing the factors in the first place.

Unfortunately, his defense is not convincing. While he makes the valid observation that other factors may be analysed in ways that produce curves apparently similar to Ricardo's law of rent, he ignores the fact that the similarities are superficial and analogous only. This may be seen by reference to Barlowe's analysis of machine productivity that produces a curve analogous to the rent curve (Barlowe 1958). Barlowe observes that as new machines come into production, they are able to return larger profits due to their more efficient technology. He also correctly observes that the price for the goods so produced is set by the least productive machine in use, which mirrors the marginal land site. However, it is there that almost all similarity ends. Land use begins with the most productive sites and users are only forced reluctantly onto the progressively less desirable sites. The progressive extension of the margin implies that as successively less productive sites are forced into use, rents on prime sites will grow.

In the case of machines, additional production is normally done by bringing more new machines on line, not delving into museums for old and less productive ones. In any case, the return during the life of a machine is the the opposite of that for land. When a machine is new it will typically be made to utilise the latest technology and will enjoy the greatest profitability due to the increment between its productivity and that of the least productive in use. Through time, the least productive machines tend to fall out of use, and so the base level of efficiency rises, the opposite of the land case.

A curve similar to Barlowe's could perhaps be drawn for labour, illustrating the way that productivity falls off with the diminishing quality of labour. Labour quality is determined by both the nature of the labourers and, more importantly, their skill. A little reflection reveals that the interplay between wages and skills will normally entice higher skills into the the work force through training, thereby making the behaviour of that factor resemble that of tools and not land.

This debate can be illuminated by another classical debate in political economy, that of the *par*. The *par* was the name given by William Perry to the question of the relationship between the return to labour and the return to land, or rent. Roll outlines

Perry's solution and notes that while it was ingenious, it was partly circular (Roll 1942).

Perry reasoned that the return to land should equate to the return to other capital assets of equal value. This means that if a rate of return is set and value is set, then rent can be computed as the quotient of value divided by rate of return. Ignoring the question of risk as a partial determinant of rate of return, the problem that remains is still one of value which, even in Perry's time, was a function of rents.

A deeper significance may be seen in the par, the fact that labour and land were recognised as fundamentally different and hence also their part in both the productive process and distribution. Tools and labour both represent labour, the former as *embodied labour*. to borrow a term from Marx. The fact that the curves for both of these factors behave similarly, but in the opposite way to land may in fact be a result of them both representing labour and both being capable of the improvements over time that are characteristic of the human element in technology.

This underlines the issue of valuation and pricing. Other capital assets could be priced objectively by cost, although this practice was largely discouraged by the mercantile capitalists.

2.12 COMPETITION & SELF-INTEREST

The Market has its own moral justification that traces back to Adam Smith's metaphor of the invisible hand. However, Rothschild questioned Smith's actual attachment to the metaphor, suggesting, "*Smith did not particularly esteem the invisible hand and thought of it as an ironic but useful joke*" (Rothschild 1994). The relationship that Smith recognised was the antithesis of that implied in his text, "*Smith thought the interests of merchants and manufacturers were fundamentally opposed to those of society in general, and that they had an inherent tendency to deceive and oppress society while pursuing their own interests*" (Bishop 1995).

This is not totally surprising because Smith is not noted for his originality. In his introduction to Smith, Seligman notes how little of the Wealth of Nations is original Smith (Smith 1778/1910, Introduction p.xii). Rashid (1992) demonstrated the way that Smith's ideas, "*not only existed, but had been explained better by his predecessors.*" Pack (1999) is more to the point suggesting that "*what is true ...*" in the Wealth of Nations, "*... is not original and what is original is not true.*" It is therefore not such a surprise that Smith's exposition of what was held by others may not depart in places from his own beliefs.

The assertion of the validity of competition is reflected in the confidence in the eventual settling of markets towards equilibrium. While the confidence in stable market

equilibria has become an important theme in economics, and Bryant (1997) has shown that there is no mathematical foundation for equilibrium at all building on Saari who earlier demonstrated that there is no mathematical justification for expecting that markets will find stable equilibrium.

2.13 WEALTH DISTRIBUTION & THE MARKET

Advocates of the free market assert that it is the economic system that returns the greatest material benefits to the communities that adopt it. Freeman asserted, "Wherever the free market has been permitted to operate ... the ordinary man has been able to attain levels of living never dreamed of before" (Friedman 1980, p.179). Easton and Walker (1997) compared Hong Kong with a selection of east European countries to demonstrate the effectiveness of capitalism to warn of the folly of China's intention to introduce market socialism. Novak observed the success of the US economy when he observed, "Today, seeing the incredible vitality of free economies - by which, for example, the United States doubled its gross national product in real terms between 1960 and 1983 - we see full well that the elimination of grinding poverty is within reach" (Novak 1984, p.47)

Despite this Wiener and Monto (1998) concluded that for many of those in the lower income levels, free market industrial capitalism has failed to deliver comparable improvements. Grubel (1998) presented data from 115 countries reaching a similar conclusion, resonating with the observations of the Economist suggesting that income inequality in Britain and USA is the highest in fifty years (Economist 1994). Briggs supplied data on the USA to conclude that despite the economic indicators showing the economic health of American capitalism, social indicators, such as income disparity, show the reverse (Briggs and Jnr. 1998). Briggs appears to have observed a fault in the causal connection between national wealth and poverty elimination assumed by Novak.

Gilder painted the heroic virtues of entrepreneurs such as J.R. Simplot fighting against a government who believed, "that profits were a form of theft" as the source of progress in the free world (Gilder 1984). He made no secret of Simplot's accounting gymnastics performed in order to minimise his tax liabilities and fund expansion. The inference is that entrepreneurs should be free to enjoy their successes as a stimulant for the whole economy. By contrast, Stilwell noted that the more recent Australian tendency to impose controls on wages, but release non-wage incomes was producing greater income inequality (Stilwell 1994).

2.14 MONEY, DEBT AND INFLATION

The return to money, interest, is a vital component of the pricing problem. If economic rent, which can be traced to land pricing, is properly social property, then the return to money may be entirely the proper property of the community. The problem of money tends to be ignored today, despite Galbraith's warning at the beginning of his investigation into money:

"It has long been fashionable for historians, except in the secret recesses of their belief, to be modest about the lessons of history. Perhaps it teaches only that it teaches little. Where money is concerned, this restraint is unwarranted" (Galbraith 1995, p 1).

2.15 MONEY SUPPLY

Several writers relate inflation to money supply, some considering that the generation of money represents a form of unfair revenue for the government (Lockman 1991; Rushdoony 1982). Inflation is recognised as a form of tax (Beare 1978).

The ethics of money supply is variously represented as a useful economic tool and an evil used by the state to steal from citizens. Economists are not renowned for consensus. More fundamental is the question of whether economics does involve ethics. This question will be dealt with separately.

Three theories of money appear to have survived. These are not an exhaustive set of monetary theories, but indicate those currently supported. The metalist theorists believe that all money should be in the form of precious metal, usually gold, or at least be backed by gold (Davis 1990; Lockman 1991; Rushdoony 1982). This position has survived many centuries, but has several difficulties. It is based on the necessity for money to be backed by real value i.e. a product that has concrete value. This position is weakened by the variability in the supply of precious metal but essentially would constrain inflation. It is less clear if it could control money creation due to the multiplier of the banking system and possibly revaluation due to velocity changes.

Social Credit theorists assert that money should balance the value of production. Social creditors would control both money creation through the sale and conversion of government bonds and through the banking system. Money would be printed to back goods produced, as they are produced and would be distributed in a socially equitable way. This complex arrangement also requires price control. While it may prove cumbersome and politically unattractive, as a theory it does have the merit of relating money supply to production which has a reasonable basis. Analysis under this theory would possibly view the current arbitrary money creation as justified to the point where

it was backed by production. The fact that the state currently is the prime beneficiary of money production would be viewed in this theory as equating as an implicit tax.

The dominant monetary theory is free from any correlation to objective wealth, viewing the supply of money as an inflationary influence that is managed by the state for the maximisation of economic goals (Beare 1978, p.223-36). Several problems are recognised by the implicit taxation resulting from inflation largely related to the uncertain distribution of the burden.

2.15.1 Inflation as Tax

Beare describes the government's income from money creation as analogous to an excise tax, a wealth tax on money (Beare 1978, p.286). It is possibly this that causes governments' reluctance to make deductible inflation losses on invested money even though such a loss is analogous to depreciation on other assets. Beare also suggests the real impact of inflation and strategies for their minimisation. It appears to be a far bigger issue than can be adequately dealt with using only an economic framework. Where these are taxed on the gross (non-real) money amount they constitute a second way that the state earns income purely from inflation (Small 1989).

2.16 DEBT

The place of debt in economics and society has been varied. Today it is widely used and accepted in most societies enabling Barlowe to refer to it as the 'life blood' of the real estate business (Barlowe 1958 p.438). However, Uzair outlined the theoretical flaws in the modern justifications of interest (Uzair 1976).

Islamic law prohibits the charge of interest and historically, in Christian countries, half of the Christian era was marked by a similar moral prohibition that was only broken by the Protestant Revolt (Langholm 1984). Scholastic thought discouraged the use of debt, though there was a gradation of severity from strict imposition of moral sanctions (Broderick 1939), to more cautious and limited prohibitions (Aquinas 1981; Little 1978; Lowry 1987; Noonan 1957; Roll 1942). Langholm outlined the way that the position on debt straddled both Christian and Aristotelian moral philosophy (Langholm 1992).

Analysis of this prohibition, its removal, its relationship to capitalism and its impact through the economy, is necessary in order to locate its ethical significance. The mechanisms of debt when applied to land acquisition will follow from this analysis.

The concern over the moral basis for the charge of interest extends as far back as Aristotle (Langholm 1984). It is based on an understanding of what money and its use are. Aristotle introduced the idea that money, *qua* money, was not in any way

productive, and so a charge for its use is unwarranted. He is known for his notion that money was sterile, it produced no goods useful to human society. Calvin is known to have rejected the sterility argument and saw money as just as productive as any other asset.

Aquinas recognised the immorality of interest on money, and developed the understanding of the arguments in support of the position. In particular, he stressed that in many cases durable assets have a use that is distinct from themselves. Hence these assets have two components that contribute to their value, the first being themselves, especially as artifacts, the second is the value of goods that are produced through their use. A house has a value as a building, and this may be owned regardless of its use or vacancy. It also produces a good, i.e. shelter, through occupancy. The occupancy of a house may be sold separate to the ownership of the house itself. This is seen commonly in leases where the lease is essentially the sale of the occupation of the dwelling for some period. The house, at least conceptually, is not consumed or otherwise affected by the act of occupancy. Where some negative change is affected on the house as a result of occupancy by persons under a lease agreement, they are usually expected to make good the change as a separate charge, thereby leaving the house in the same condition after the lease as before.

For money, like other valuable items, such as food, their use necessarily involves their consumption. To use food is to eat it, so at the end of use the item is consumed. Where food is borrowed, it is the use of the food that is borrowed and no one expects that it will be the same food that will be returned, but an equal quantity of similar food, having an equivalent ability to be used as food. Likewise the return of a money loan involves only the return of an equal use value of money, not the original pieces of money.

The immorality of interest on money, usury, was a source of difficulty for the Medievals. Little has shown the growing tension between the Church and the bankers during the period (Little 1978) Broderick (1939). chronicled the life of St. Peter Canisius who stood against the German bankers on usury Chafuen cites De Roover's summary of the difficulties of the medieval usury doctrine:

'The usury doctrine was the Achilles heel of scholastic economics. It involved the schoolmen and their sixteenth-century and seventeenth century successors in insuperable difficulties that contributed greatly to bringing their whole doctrine into disrepute' (Chafuen , p.145)

Chafuen chronicled the development of Scholastic thought after Aquinas's progressive attempts to bring Church teaching into line with the practices in the street (Chafuen). In doing so it became increasingly irrelevant (de Solenni 1971).

2.17 Interest Theory

The Medieval theory of interest is fairly well documented (Langholm 1984; Noonan 1957). The concept relies on the distinction between two components that may be present in a given interest rate charge: usury and licit extrinsic titles. Usury was held to be immoral and unjust, however it has always been accepted that there may be grounds for insisting on more being repaid on a loan than simply the principal. These grounds were known as 'extrinsic titles' on the basis that they were not a return on the money itself, but for reasons external, or extrinsic, to the money loan.

The twentieth century has seen several theories put forward such as expectations, risk and inflation premium and market segmentation (Wilson and Keers 1990), but these are more descriptive than explanatory. Fisher perhaps provided the best theoretical basis for interest as an "impatience premium" (Fisher 1930/1977), although this is also problematic. Fisher's perspective is useful however, because in the course of his investigation he returned to the very issues that are currently being investigated, the relationship between land and price and its impact on the wider economy.

Fisher noted that, *"Income is derived from capital goods. But the value of the income is not derived from the value of the capital goods. On the contrary, the value of the capital is derived from the value of the income"* (p.14), and consequently, *"It is true that the wheat crop depends on the land which yields it. But the value of the crop does not depend on the value of the land. On the contrary, the value of the land depends on the expected value of its crops."* The valuation he is referring to is the capitalisation of returns into price which is dependent on the rate of profit.

Fisher has implicitly recognised the pre-eminence of the rate of profit in setting price, and in the absence of a theory for the rate of profit, appears to be agreeing with Panico. The price of land therefore ultimately depends on the rate of money interest.

2.18 PROPERTY AND BUSINESS CYCLES

The existence of marked irregularities in the patterns of economic activity is generally accepted. What is less accepted is the possibility that these irregularities may be correctly termed cycles. Cycles are recurring phenomena that may be predicted with some certainty. While several theorists have observed cyclic patterns in historical records, the reasonable prediction of future economic events has been less successful. What is clear is that the cycles within the economy, if they exist, are the composite of many economic forces and perhaps sub-cycles. They may also be influenced by exogenous factors such as political trends and changes and social psychology.

2.18.1 Kondratieff

Study of this area of economics appears to have begun systematically in the nineteenth century (Hall 1990). The existence of cycles in economic behaviour appears to be evident back into the eighteenth century. More recently, several cycles have been identified by duration. Kondratieff identified long waves, or cycles, early in the century and successfully predicted the Great Depression (Freeman 1996; Solomou 1987). It earned him heavy penalties in his homeland, as his Russian keepers were more intent on using the depression as a proof of the final failure of capitalism rather than a natural, recurring event (Mager 1987). Had they looked more deeply into his observations they may have realised that his waves were only found in capitalist economies and its European history is tied to the emergence of capitalism itself (Mandel 1995). Using the British economy, Aldcroft demonstrated that not only the Great Depression, but previous major depressions of the modern era have been related to cyclic fluctuations (Aldcroft and Fearon 1972). Some have suggested that they are the recurring symptoms of a malignant economic malady that cries out for explanation. Many writer perceive long waves as more of a general sociological phenomenon than one limited only to the field of economics (Goldstein 1988). This more general interpretation of long cycles in human affairs would appear to suggest a more fatalistic response, except that they do not appear to be apparent before the emergence of capitalism.

Kondratieff waves, with a period of about forty-eight years, have been explored with renewed interest since 1970 due to the suggestion that the next wave is about to break. Galletly (1988) was illustrative of the growing expectation that the next depression is near. Considering the events of the five years following the publication of his work, he should have been pleased with his predictions. However, the severity of that recession/depression was not been so great as predicted, leading many, such as (Kavanagh 1995) to suggest that the real crash is yet to occur. For these, a long cycle of about half a century does exist and the recent global recession is only a precursor of the next downward adjustment.

A variety of causal explanations exist for trade cycles, summarised in many texts (Davis 1990; Dokko et al. 1995; Gaffney 1994; Harrison 1983; Rushdoony 1982; Samuelson 1975). To introduce the issues that form a back drop to cycle theory, the circumstances surrounding the rise and fall in popularity of one of the earlier theories is useful. The Jevons causal theory for business cycles will be used.

2.18.2 Jevons

Jevons noted an apparent correlation between trade and sun-spot activity (Beare 1978). This unlikely correlation is useful in considering some of the issues that surround the recognition of possible causal influences. The Jevons sun-spot theory initially enjoyed substantial popularity, however it is currently used as a caricature in

cycle literature, not given any credence whatsoever in the majority of the literature. The question remains however, as to whether it does have any influence on the behaviour of business.

It is more credible when one considers that solar activity appears to strongly influence global temperatures and hence climate. Because rural production has until recently dominated the economy, climatic changes will influence agricultural productivity and hence the economy in general. The point here is that some aspects of the economy will be at the mercy of nature and these may be able to bring others into synchronisation with natural forces. The current interest in market shocks is a more general theory that recognises that external factors may stimulate the cycles in the economy.

Sun-spot activity has a short term period of about ten years and this is close to the observed trade cycle period in Jevon's time. The slight difference between the two periods has been sufficient to discredit the correlation in recent times, but it should not be totally ignored. Given that natural, external, events that may influence trade, human factors will also be an influence that may intensify or negate the natural. The observed difference in period may have been the result of the influence of other, additional, influences. Hence, to cast aside a theory, merely because it is not a total explanation, is rash. Perhaps the tendency towards industrialisation as the core of modern production has been such an influence. The discrepancy in period may be not so much an indication of the theory's fallacy, but merely recognition of the existence of other factors.

There are some contemporary economists who continue to adopt the Jevons solar interpretation (Davis 1990). While the influence is no doubt changing with the changing agricultural technology and the relative importance of the sector, it may still be one of many causal influences. This both highlights the shortcomings of purely statistical analysis and exposes the theory-driven behaviour of those who assert a purely scientific, empirical, approach. The rejection of a valid, though tenuous causal connection, is scientifically invalid if done on the basis of a failed correlation, however it is the view commonly taken.

Harrison asserts a basic eighteen year property cycle compounded with other cycles (Harrison 1983). Several authors recognise a long wave of about fifty years and this seems to have enjoyed considerable popularity over the last fifteen years. Curiously, Samuelson optimistically asserted the end of trade cycles in 1975 (Samuelson 1975) only to find history apparently outwitting the economists a few years later. Kavanagh suggests that the low point in the current long wave has not yet hit, while Davis holds that society should learn to ride the long wave rather than try to dam it (Davis 1990).

The optimism of the seventies, believing that trade cycles, especially deep long cycles, tended to bury interest in trade cycles, and they were seen as the manifestations of economic ignorance that would be removed with developing economic understanding and fine tuning. Conversely, the past ten years has generated enormous interest with over thirteen hundred published academic items on economic cycles in the last decade.

Key et al. succeeded in developing effective predictive models for the property cycle using UK data, however there is a distinction between predictive and causal results. Many of the significant variables in Key's study are not causal but correlational (Key et al. 1994). Key adopts the Cobb-Webb theory that posits cyclic instability resulting from decision making that uses current situations as a basis for decisions that will affect future (delayed) outcomes.

The result is essentially similar to chaos theory along the lines of Lorenz's strange attractors. There is no difficulty with the outcomes, which recognise cyclic behaviour in many real estate parameters, however the reduction of all cyclic behaviour to the lag in the effects of development decisions is not totally convincing. There is considerably more variation in the market than development itself can account for, and even development decisions are subject to external variables.

Dokko similarly produced a useful predictive model based on US data linking the property cycle to broader economic indicators, and was able to replicate observed real results (Dokko et al. 1995). Again the outcome locates several variables as influencing real estate, including interest and inflation. The issue is the mechanics of the interest/inflation/price relationship which is identified in this study though not specifically pursued.

The current study is focused on the impact of debt finance on instability in land prices. It acknowledges the instability produced by the Cobb-Webb hypothesis and the mechanism involving development decisions and the delays in commissioning new stock. It seeks to explore the operation of debt funding as an underlying factor that stimulates instability.

Several authors recognise that historically trade cycles developed in Europe concurrently with the use of money. Either money is fundamental to trade cycles or it is only when an economy uses money that it can quantify the economic variables that indicate cyclic behaviour. It is asserted that the former is the case.

Cycles can only be the result of natural or human factors. Most recent explanations stress the human factors, usually in terms of production, consumption and other economic tendencies. Hall gives a history of the early theories of trade cycles (Hall 1990). He distilled cycle theory into Keynesian and monetarist theories and used these

to analyse the economic events of this century. His interpretation of the cycles since the World War II placed the trade cycle at the mercy of movements in aggregate demand (Hall 1990, p.168). (Zarnowitz 1992) developed more of the modern theory of equilibrium and disequilibrium as a temporary anomaly caused by external shocks. Curiously, sun-spots have also re-entered theory as a metaphorical term to describe external shocks, although they more often refer to events of a more human nature.

The study of shocks appears to be a current area of interest in the literature. It relies on the assumption that there does exist an equilibrium to which the economy will return, but which it is often deflected by special and usually external factors. Shocks may include technological developments, natural occurrences and political events.

Das has noted a correlation between economic activity and the polarisation of wealth in the economy (Das 1993). His analysis has exposed a relationship between the gap between rich and poor and the health of the economy. It is an observation that is worthy of greater attention.

The majority of the literature on trade cycles uses gross economic indicators, such as GNP, and fails to specify models that differentiate the various parts of the economy and the interrelationships between them. Some more specialist works deal with specific parts of the economy, such as building construction, but these appear to reflect more specialist interest in these areas than an attempt to infer causal theory that includes the dynamics between the various parts of the economy. It appears to be well recognised that the phasing of various parts of the economy differs. Hence some sectors, such as building construction, lead the economy, while other sectors lag. The existence of this complex pattern of leads and lags appears to have been empirically recognised, but relatively little attempt has been made to use this pattern to explain the operation of the cycle itself.

2.18.3 The (Real) Property Cycle

The property cycle is a recognised concept in land economics and is generally treated as a semi-autonomous cycle to the general business cycle. Phyrre gave a descriptive account of the property cycle (Phyrre et al. 1989) that is a comprehensive indication of the scope of the concept within land economics. Hargreaves used a quantitative methods approach his methodology sought a predictive outcome, less interested in causal issues (Hargreaves 1996). With Phyrre, he is representative of a large amount of the literature on property cycles is not so much involved in the development of causal theory, but prediction and policy aids.

Phyrre notes the fact that the property cycle is actually a compound of several cycles reflecting different aspects of the property market. This introduces its own problems

because of the peculiarities of the market itself. Hendershott has noted cyclic property valuation errors which suggest that the actual shape of the cycle in value may be different to that reflected in valuations (Hendershott and Kane 1992).

Mayer has observed the complexity of the real estate market itself and has been able to take several useful conclusions from the fact that the market is composed of a wide range of differently priced units (Mayer 1993). In particular, average price and volume statistics have less usefulness for those actually participating in the market because the sub-markets may be operating in ways very different to the aggregated data.

Despite the observation that the property cycle is related to some extent to interest rates, the relationship between property and the rest of the economy is often not explored. Case offers a curious and perhaps important exception to this tendency in his analysis of the economy of Massachusetts (Case 1992). He suggests that the property cycle is a causal influence on the economy as a whole, resulting in property booms leading to economic down-turns. This is an important observation because it runs counter to the classical cycle theories which tend to diminish the significance of real property as a distinct asset group. This position is supported by others. George suggested about a century ago that land booms were the result of speculative over-investment in land that both drew investment funds away from productive assets and pushed up rents (George 1879/1992). Harrison found evidence of land based cycles in his analysis of UK markets (Harrison 1983). Kavanagh has applied George's cycle theory to long wave evidence to suggest that land is indeed causal in economic fluctuations (Kavanagh 1995).

2.19 FINANCE AS BEHAVIOUR

Commons' institutional economics has been shown to have a social psychology foundation consistent with the thought of John Dewey (Albert 1997). Commons developed Dewey in economic behaviour to posit negotiational psychology, suggesting further the psychological basis for economic theory.

Shiller (1998) used the behavioural principles found in psychology, sociology and anthropology to review recent literature in empirical finance. The stock market was interpreted in terms of cultural, rather than rational, motivators and included the curious prospect of 'magical thinking' suggested as explaining investor behaviour. While at first sight this appears absurd, the tendency in boom-times for the investing community to believe that the boom will never end, does have a touch of magic thinking about it - somehow the rules that have always held in the past, have been magically suspended this time. Shiller (1995) interpreted investment behaviour specifically in terms of herd behaviour - investors quick to jump in where others have shown that there is money to make, even if the opportunity has evaporated.

Clark and Oswald (1996) examined the tendency for conformity behaviour to link to personality measures in economic decisions, placing a value on conformity/deviant decisions wholly beyond rational financial optimization's computations.

O'Donoghue and Rabin (1996) examined behaviours such as human propensities to save in terms of perceived short and long term costs and benefits. They observed the effect of personality differences on decision outcomes. This line of research indicates both the behavioural dimension of investment and the developing interest in this study.

Organisation theory can be interpreted as the management of the psychological context of the organisation in order to maximise financial objectives (Ansari 1988). In this case labour provision is seen to respond to psychological variables rather than economic ones. Behavioural economics, as the background to marketing is transparently the same technique applied to the other side of the organisation's profit equation - the use of psychologically determined interventions to maximise revenue.

2.20 LITERATURE GAPS

Several major gaps appear to exist in the literature that have relevance to the problem as follows:

2.20.1 In the western tradition, this gap is evident in the transition through John Locke to the Enlightenment thought of Adam Smith and especially in the development of theory in the last century. Modern property theory has contracted into legal positivism. The customary title literature appears incapable of bridging the gap between the Western positivist construction of property and the essentially Realist methodology implicit in the explanations of property by customary peoples.

2.20.1 The notions of price and value seem to have been developed on one of two methodologies, the Aristotelian or the Smithian. The notion of justice in exchange appears to have been abandoned to the market, despite evident flaws in market theory.

2.20.3 Little application of Aristotelian metaphysics has been applied to key economic concepts.

2.20.4 The literature on indigenous title reveals a tendency to ground title to land on theological assertions regarding the creation of the world and the relationship between the earth's creator(s) and the community. Of the non-Christian literature, the Islamic contributions appear to be the best developed. The theology of land property appears to be inadequately treated in Western Christian scholarly circles and the attempts do not engage non-Christian positions. Newman's proof for the existence of God through the commonality across mankind of a religious sense

would appear to find a parallel in land. If many cultures exhibit an essentially common moral theology of land property, it would appear to provide evidence that such a position should be taken seriously following St. Paul's assertion that, the truth of God is written on the hearts of men.

2.20.5 The elimination of Land as a distinct factor of production. Recent literature in economics, finance and land economics reveal the absorption of land into capital. This trend has certain positivist support, but has made the study of the "components of capital" more difficult. Little critique of this collapsing of the factors of production and money into wage and non-wage factors has been attempted.

2.20.6 The absence of interest in rent theory beyond its application for arguing towards Georgist single tax conclusions.

2.20.6 An absence of discussion of the significance for political economy of the change in the meaning of human nature that resulted from the Enlightenment. This issue is especially evident in writing that adopts Adam Smith's notion of human nature and attempts to merge it with the Aristotelian notion of human nature.

2.20.7 Most critiques of the economic system that attempt to engage a moral perspective tend to deal at a political or cultural level which leaves a methodological gulf between criticisms of the social failure of market economics and an analysis of economic theory as employed by economists

2.21 PROBLEMS ARISING FROM THE LITERATURE:

The need for modern economic thought to review its need for a systematic ethical and metaphysical base.

2.21.1 The need to develop a metaphysically based practical science of the social economy of land.

2.21.2 The potential for constructive critique of dominant economic theory based on a metaphysically based notion of land in economics

2.21.3 the application of 2.21.2 to major contemporary economic problems, especially those focused on land.

Chapter 3: Methodology

The overall purpose of the thesis is methodological. It will argue towards an appropriate methodology for the social economics of land. In order to do this, its own methodology must be explicitly articulated. The purpose of this chapter is to consider the major issues surrounding the science of economics and to defend a suitable methodology for its investigation. The location of empirical methods within this methodology is discussed and its application in this thesis outlined.

The exploration of methodology in this chapter is not intended to provide a complete treatment or defence of the issues raised. Its purpose is to consider major competing approaches and to provide sufficient reason for the approach adopted. It is not intended to be a rejection of other methodologies, or a denial of the possibility of them having some value. It will however consider some of the major limitations that have become apparent in some of the more popular approaches of recent centuries.

The organisation of this chapter is as follows:

The object of economics: defining and locating the science of economics.

Metaphysics: A review of the significance of metaphysics for economics and selection of an appropriate system

The interrelationships between the sciences: a discussion of the various sciences and their connections

Moral Philosophy: A review of the relationship of morals and economics and selection of an appropriate system

3.1 THE OBJECT OF ECONOMICS

Aristotle recognised that humans were social animals. Humans are by nature "...dependent on others at every stage of life, for existence and for the fulfilment of physical, emotional, intellectual, social, and even spiritual needs." (Wallace 1977, n.75.1 p.231). Society is therefore necessary for the human person to provide the environment for the flourishing of the various dimensions of human nature. Hence, "(t)he function of society is to actualize its inherent end, the common good, viz, the conditions that make a fully human existence possible for all of its members" (Wallace 1977, n.76.4, p. 235].

The material dimension of human needs involves two major aspects in a social environment, production and allocation. Production is a human activity that is distinct from natural production, in that although nature is productive (trees grow fruit without human intervention), human agency is also productive in its own right as well as instrumental in managing natural production for greater efficiency. Part of production involves those activities that makes the fruits of production available for human use, hence the fruit must be picked from the trees and transported to those who will eat it. Most production is social, in that the producers are not the consumers.

Allocation is the process of distribution of product amongst consumers. The problem of distribution is the ethical question of the proportioning of the benefits of production amongst the various members of society. While economics may appear to be concerned with production, the arts of production are not connected with economics directly. Their objects are their respective productive activities, and not allocation.

Allocation, and the problem of distribution is the core of economics. Economics must resolve the question of how to manage distribution so as to realise the common good. Elements within this enquiry include issues of justice between various parties, sufficient rewards and incentives to producers, the rights of persons who are not able to contribute productively to the economy, and the material support of other social institutions, such as governmental and charitable functions that are necessary for the common good.

The problem of distribution is manifest in many places between the first act of collecting raw materials to ultimate consumption involving various returns to labour, the owners of raw materials, capital, money and the state, as well as final prices to the consumer. Economics is therefore "*... concerned with social interaction from the point of view of production, distribution, and consumption of goods and services*" (Wallace 1977, n.75.4, p.345).

As such economics is a branch of social science, which in turn is a branch of practical science. Practical sciences may be divided into two main branches being "*... the arts of making and the arts of directing human conduct*" (Wallace 1977, n.1.6, p.5). The former refer to what will be discussed as intellectual virtues while the latter falls under the umbrella of ethics¹¹.

¹¹*Ethics is the philosophical study of voluntary human action, with the purpose of determining what types of activity are good, right and to be done, or bad, wrong, and not to be done, so that man may live well. As a philosophical study, ethics is a science or intellectual habit that treats information derived from man's natural experience of the problems of human living, from the point of view of natural reasoning* (Wallace 1977), n.49.1 p.149]

3.2 METAPHYSICAL FOUNDATIONS.

All sciences apply logical development to a specific set of premises. Generally, premises must be adopted *a priori*, which suggests a fundamental dependence of science on untested premises. Metaphysics, however, is the science of being, and has the distinction of being the only science able to prove its own premises. Although metaphysics is concerned with very fundamental and background issues, it is a necessary starting point for any science. (Boland 1992, pp. 14-9) argued that this necessity is no less important in economics.

Boland reviewed Marshall's framing of economics as a positive science¹² and explored the implications of the latter's conclusion that the presence of exogenous variables would always make definite knowledge in economics impossible (p. 42). Boland's contribution was to re-open the question of the validity of Marshall's metaphysical assumptions that have compromised economics' status as a true science¹³.

Marshall's position was a continuation of the empirical tradition set in place by the Enlightenment thinkers, notably David Hume, *the Father of British Empiricism*. Hume's position on metaphysics was quite explicit: "*All this is metaphysics...That is enough; there needs nothing more to give a strong presumption of falsehood*" (Hume 1777/1975, n.239 p.289). Hume set in place a methodology that ignored its metaphysics, and which has been widely adopted over the intervening two centuries. Hume's aim was to replace metaphysics with direct observation as the grounding for knowledge, making epistemology the starting point for philosophical enquiry¹⁴.

Hume's methodology is based on experience, and has led to positivism and the dominance of the experimental method in most sciences. In several instances this has implicitly proved to be self-refuting. In Physics, scientists are recognising that observation has its limits and an increasing number of physicists are working more on metaphysical questions than observational (Johnson 1995, Ch. 3). Boland's analysis demonstrated that empirical economics has failed methodologically. These observations could be interpreted as empirical evidence that the empirical method

¹²Positivism is the position that accepts only what can be observed. It does not accept the existence of essential natures and aims to draw no conclusions past what may be linked through observation. Hume's empiricism may be viewed as the beginnings of positivist science.

¹³The unfortunate title of Economics as *The Dismal Science* is perhaps a reflection of the fact that economics no longer reflects the optimism that should be natural to a practical science. Rather than a science that is popularly perceived as a contribution to human good, or flourishing, it is more often associated with theories and policy that spell uncertainty and practical outcomes that are popularly perceived as unpleasant compromises that often militating against the weak.

¹⁴Hume's position was not without its own metaphysics - Hume asserted a universal negative in positing the absolute absence of metaphysics, in the realist sense. Such an assertion is itself a strong metaphysical statement, hence, it is either self-refuting or meaningless. This is not to mention the necessary impossibility of a finite creature originating a universal negative synthetic truth (Kreeft 1984, pp. 53-63).

cannot stand alone, that is, the last two centuries of empiricism may be viewed as an experiment that has disproved the independence of empiricism, *modus tollens*.

Recognising this failure of pure empiricism, Boland's suggestion that economics must begin with an explicit set of metaphysical premises will be adopted in this thesis. Hume's outright rejection of metaphysics will itself therefore be rejected.

A realist methodology, following the classical approaches of Aristotle and the late realist thinkers, will be adopted for the thesis in general. The realist tradition recognises the necessity for an explicit metaphysics as the foundation of any science. Metaphysics, as the study of what is fit to be, provides a foundation for knowledge about what exists by first supplying an understanding of what can exist, that is, what constitutes being.

Closely related to metaphysics is epistemology, which is the branch of philosophy that is the study of the nature, limits and criteria of knowledge. While Hume's rejection of metaphysics necessitated the modern trend towards adopting epistemology as the first science, this approach has always been highly problematic. The fundamental premise of realism is acceptance that reality exists. This simplifies epistemology to the extent that the major modern questions in epistemology tend to resolve themselves.

The realist metaphysical position makes the following assumptions and epistemological inferences that will be adopted in this work:

- The world is real and exists independently of human perception of it.
- The world changes as a result of consistent processes that are knowable; i.e. it is rational.
- Because the processes by which the world changes are consistent and operate regardless of human perception of them, they form a set of laws, which are beyond human control. These laws that depend only on the natures of their subjects are correctly referred to as natural laws.
- Human understanding begins with observation of particulars; knowledge of particulars is then generalised, or abstracted, into knowledge of the essences or forms that make the particulars what they are.
- Similarly, human understanding begins by positing of possible laws as hypotheses or theories; these are then examined and tested. Such hypotheses may be provisionally adopted as theory, until such time as they are either refined into laws or proven false.
- Human understanding is expressed using terms and concepts that derive their value from the degree of conformity they enjoy with the reality to which they relate.

- Concepts that conform accurately to the reality they signify are considered true in proportion to the accuracy of that conformity.
- Knowledge is justified true belief (Plato)
- Humans, through their intellect, are able to know natures.
- Truth is a measure of the conformity between real things and the terms or concepts that are used to denote them. Truth is found not constructed.
- Accuracy is differentiated from precision, in that the former signifies a conformity that is true but not closely determined, whereas the latter signifies fine determination without necessary accuracy¹⁵.
- Concepts that are accurate though imprecise are considered true, despite being amenable to a further refinement.
- It is the purpose of scientific inquiry to increase the accuracy of knowledge with respect to the processes that govern the behaviour of the world, and secondly to refine accurate understandings towards greater precision. It is possible to have precise theory, such as Ptolemy's astronomy, that is not accurate. The latter are essentially false, even despite the possibility of them having moderate predictive accuracy.
- Through *modus tollens* a single definitive counter example is sufficient to render a theory unacceptable.
- Empirical investigation strengthens the reliability of theories inductively, but are insufficient to render confidence in the theory strong enough to assert true knowledge of the underlying law.
- The status of a theory can be elevated to a law only when there is sufficient support available to render the possibility of a *modus tollens* rebuttal impossible.
- There are different kinds of laws that operate in different spheres, for example, laws governing moral action do not have the compulsion that is evident in non-willed action.

3.2.1 Rationale for selection

Currently there are many systems of metaphysics, many of which would find difficulty with one or more of the above propositions. It is not the intention of this thesis to exhaustively prove each of the above, despite asserting that the following evidence is available in their support:

¹⁵Target shooting illustrates this distinction. A worn rifle with well-adjusted sights will produce a broad group of bullet holes in a target that will be equally distributed about the bull. Such a weapon would be accurate, but not precise. A high quality target rifle with mal-adjusted sights will produce a tight group of bullet holes, but will always miss the bull. It would be precise, but not accurate. A shooter using the latter weapon, who relied on its sights as they appeared, would always miss the target.

- (1) they generally fulfil the conditions of Occam's Razor (not to multiply entities without reason)¹⁶,
- (2) they are held, (at least in practice) by almost every human, except for modern philosophers and then only while they are doing philosophy¹⁷,
- (3) they are developed from common sense (especially with respect to being)¹⁸, and
- (4) they are implicitly evident in the world view of even the youngest persons capable of speech.

Even so, they are not without criticism. Part of Hume's rejection of metaphysics involved a rejection of most of the above. (Hume 1777/1975) is foundational to the line of criticism that initiated that general body of philosophy, beginning in the Enlightenment, which rejected key parts of the realist metaphysical position. As such, a defence of realist metaphysics may be made by addressing the criticisms developed by Hume and others.

Hume's critique began with the assertion that it is not possible to know what cannot be sensed (perceived). Hume continued this line of thought to conclude that causal relations cannot be known because they are not perceived. All that is perceived are "common conjunctions" of events, and it is up to the observers to infer causality, which can only be inferred inductively. For this reason science is always hypothetical, dealing in theories that cannot be known sufficiently well to resolve into laws. This highly sceptical view remains as a dominant theme behind empirical science. Fundamentally, it rejects the Aristotelian principle of abstraction, that is the rational ability of intelligent persons to abstract accurately from particular perceptions to universal natures.

Hume made the further observation that because philosophers¹⁹ frequently disagreed, the Aristotelian process could not be reliable. Undoubtedly, to some extent this observation is true, philosophers do disagree, however Hume's application of this truth over-stepped its validity and force. The fact that an enterprise is difficult and often

¹⁶Unless the rationality of the universe is rejected, any alternative theory of existence would require some external entity to maintain the consistency of existence. This was Descartes' only option after recognising the certainty of his own being, and his achievement despite the limitations of his strong sceptical methodology.

¹⁷ Hume recognised that his methodology was not valid the moment his maid entered his study (Hume 1777/1975)

¹⁸ Beginning with the notion that things exist independently of our perception of them, which is pure common sense, and progressing through the confidence that common sense places in the consistency and rationality of existence, even the less apparent propositions can be seen to be deductive conclusions derived from propositions adopted as common sense.

¹⁹By which he targeted the realist scholastic philosophers that had dominated his era and whose philosophy was fundamentally Aristotelian.

done poorly does not necessarily mean that it is impossible²⁰. The acceptance of reality, logic and our human ability to abstract accurately, not only provides a route to true understanding, but also a methodology for testing it. This does not mean that the methodology is consistently employed, or that certain knowledge is easily won concerning the more important human questions.

The actual balance of true versus false realist conclusions is difficult to quantify. While Hume may take issue with contentious philosophical and moral conclusions, the facts are that there are an incalculable number of realist conclusions correctly abstracted by almost every human being, most days of their lives. When a toddler recognises that a creature in a pond, a picture in a book and a few lines drawn on a page all are fish, that young person has correctly abstracted from particular perceptions the essence of fish. Furthermore, when that person is presented with other particular cases, whether they may be real fish, or other representations, even when they may bear little resemblance to the first encounter, the recognition of the essence will most probably be accurate. Adults perform this process of identifying things in their daily lives constantly, with negligible error. Whenever one comes into a new situation, a new room, or an encounter with a new thing, it is not necessary to test every aspect of every part of it, or to explore the possibility that its nature has changed.

While it is true that we are occasionally fooled and a thing is not what it appears, this is numerically rare. If it were not, we could literally not take a single step without empirical testing that the spot on which we were about to place our foot was not of a different nature to the one before²¹. Hume would suggest that we can develop a certain confidence of such things inductively, but in doing so has inverted the common balance between certainty and the unexpected. The empiricist expects uncertainty and treats consistency as unreliable through the application of undue scepticism. The realist trusts the accuracy of previous abstractions, despite the fact that occasionally they are not precise enough for a new situation, or eventually may even be found to be inaccurate²².

²⁰This situation is a specific case of the assertion of a universal negative, though it is even more seriously flawed as a logical device. By analogy, the fact that many people had tried and failed to produce a heavier-than-air flying machine before the Wright Brothers, did not prove that such a machine could not be built. So it is with philosophy. Disagreement between philosophers does not prove that they are *all* wrong. Hume employed similar fallacious logic in other places. For example, he concluded that no miracles could be true because competing religions each had their own miracle stories (Hume 1777/1975, sec., Pt. II, 95). Logically, this evidence can at best prove the fallacy of all but one of the claims.

²¹ Even empirical testing could not help our confidence in taking that next step because we could not be sure that our testing instruments are of a reliably known form. Empiricists must accept some certain knowledge of the essences of their world, they merely push back their acceptance of certainty from the object of enquiry to the instrument of perception. Only very few empiricists have attempted to live strictly according to the implications of their belief which involves ultimately a rejection of trust in both one's material surroundings and all communication.

²²Even Ptolemy's astronomy, though formally erroneous, contained a degree of mathematical accuracy. If the error between elliptical and circular orbits can be accepted as negligible given the instruments in use at the time, the notion of celestial spheres rotating on invisible axes may have been ontologically

The empiricist belief that all that can be known is what comes through the senses has other serious shortcomings, in particular those related to the assumption that only perceptions are knowable. If it is perceptions that are knowable, then it is not the things perceived at all. Our knowledge ceases to be knowledge of the world, but only knowledge of perceptions. This is the representationalist position. If we only know perceptions then it is impossible to know what is behind them. This was Descartes' problem when he applied radical doubt to the mundane question of the reliability of his senses. His recourse to a benevolent deity has been scorned both by those who adopt his conclusions and those who recognise its folly. Descartes first piece of true knowledge, *cogito ergo sum*, "I think, therefore I am" remains the one certainty that withstands the Humean scepticism. Hume himself stated that when he was doing philosophy he could not be sure of the existence of anything, such as the study in which he was working, or even his pen. However, he also accepted that when he was not doing philosophy, the existence of these things was automatically accepted. This cognitive duality should have been recognised by Hume as highly problematic, but such a recognition would not have led to his desired conclusions, so it lives on as the Achilles' heel of the traditions of representationalism and phenomenalism that have followed from it.

Likewise, the fact that certain knowledge is never possible under empiricism appears to make it a less attractive methodology than realism. At the very least, within realism the prospect of certain knowledge is possible, though difficult. At best, it offers a methodology that is capable of self-assessment. For example, some of Aristotle's beliefs regarding the status of certain people within his community, notably slaves, were arrived at using his method, but their shortcomings could be recognised using the same method. Likewise, the Humean method, in asserting the unknowability of certain knowledge, is positing a certain truth, thereby creating a contradiction.

On this basis, the empirical approach to science has dubious foundations. While it is not debated that observation and experiment are useful in the gaining of knowledge, Hume's position that they form the totality of knowledge must be rejected through. Observation and experiment are useful at the beginning of the scientific process to provide material for the formation of hypotheses, and also to aid in the testing of hypotheses. However other logical techniques, such as deductive support or elimination of hypotheses, are also admitted, enabling the possibility of certain the knowledge of natural laws. In particular, knowledge relates to universal essences, not particulars. The realist accepts that essences (that are never directly perceived) can be known. The empiricist does not.

inaccurate, but it never the less provided a kind of mathematical metaphor of the actual workings of gravity that was moderately accurate.

While Hume's position may not be representative of all lines of thought that have pursued the empiricist tradition, its basic failing tends to permeate many systems of thought that reject realism. Kant for example, accepted the existence of the world, but insisted that awareness of it was necessarily mediated by perception. While perceptions were necessary for knowledge of the world, they were necessarily systematically distorted. Kant concluded that it was therefore difficult if not impossible to know the external world as it really is. His insistence that all perceptions are moderated through what he called *a priori* forms (perceptual distortions) effectively made objective definitive knowledge unattainable.

Kant's observation of the *a priori* forms is reasonable to a degree. In many cases, persons do apply personal biases to their observations. However, this is not to say that no perception is uncoloured.

Kant's position falls into the same logical trap that beset Hume²³. The fact that most people apply a coloration to their moral thought does not mean that such coloration is necessarily present in all cases. It only means that true moral thought is not as straightforward as it may appear. The fact that a pursuit is difficult does not make it impossible; it makes it all the more valuable.

If it were agreed that there was no knowledge that was not coloured by the observer, then one would have to conclude that there could be no discourse that carried any obligation of acceptance by virtue of its truth. I am not compelled by the argument of a madman because it does not conform reliably to the way the world is. This has been interpreted as evidence that truth is unknowable and, more recently, that truth does not exist²⁴.

The attack on truth (the foundation of knowledge) has been developed from these roots to the point that Feyerabend could suggest that:

'A truth that reigns without checks and balances is a tyrant who must be overthrown and any falsehood that can aid us in the overthrow of this tyrant is to be welcomed'.

(Feyerabend 1989, p. 157)

This reformulates truth itself into an oppressive political weapon and is the line taken in the sub-discipline of sociology known as the sociology of knowledge. Sociology of knowledge developed from the Humean rejection of certain knowledge by focusing on the tendency for social forces to encourage belief structures for ideological

²³See n.8, above. If one were to ask for George Washington to raise his hand in a crowded room and five men raised their hands, this is not proof that one of them is not George Washington. It does make the task of identifying Mr. Washington more challenging.

²⁴The statement that *there is no objective truth* has been criticised systematically since Socrates, Plato and Aristotle; however, it has formed a recurrent theme in philosophy and currently enjoys a popularity so great that it is one of the foundations of the *post-modern* movement. Apart from being very difficult to prove without violating logic, the statement itself is a well-recognised paradox.

ends and has moved towards a position that basically rejects the objective reality of the external world (Susser, 1989). By recreating truth as a social construct, something that is made and managed, especially by those in power²⁵, it relegates reality to the status of a dependant variable that is constructed rather than found. If it were taken as true, not only would it be its own rejection, but its own application would necessitate questioning the ideological agenda of its proponents. The ideology of an enterprise directed towards the destruction of truth would appear to be self-evident. Despite the popularity that this position currently attracts, it is not adopted in this thesis and will not be discussed further.

3.2.2 Natures

Fundamental to Aristotelian metaphysics is the notion that specific things have their own nature (essence or form), and that a change of nature constitutes a change of thing, or being. This also implies that natures are constant.

O'Neill paraphrased the Aristotelian position in his analysis of its importance for understanding the market when he observed that the nature of a thing is "*that set of essential properties of an entity of a particular kind ... that it must have if it is to be an object of that kind*" (O'Neill 1998). O'Neill also considered the recent attacks on what he termed *essentialism*, the belief that essences exist and are useful in scientific understanding. His treatment is basically a defence of the Aristotelian doctrine of essences and he made the important point that its detractors typically created a straw man of the doctrine in order to demolish it.

Natures are not restrictive. Noting that an entity happens to be a particular kind of thing does not restrict that entity, but merely asserts a truth-value to a statement of being. Also, membership of a class of being does not fully restrict the member of that class and prevent any individual variation. For example, if an entity is identified as a wolf, then this does not specify its colour or its size, apart from the bounds of variety found within that class of object known as wolf. The wolf is constrained in as much as it cannot be a cat, but can fully express itself in terms of its nature. Hence, if it eats a sheep it is doing what wolves do, it is a normal wolf, even if humans may prefer that it didn't act so.

²⁵(Foucault 1976) has developed the theme of power as the foundation of human relationship and uses Sociology of Knowledge methods. This is generally in harmony with current readings of Hegel (Grosz 1990, ch.1) but points back to Thrasymachus's definition of justice in Plato's Republic that Plato had Socrates reject so strenuously in the *Republic*.

Moral philosophy is interested in a particular aspect of human nature; hence a sound understanding of what is meant by nature is important. Other natures are important in this thesis, especially the natures of land, value and economics.

Following the Aristotelian system of classification, natures occur in hierarchies. At each level is a set of necessary (essential) properties that constitute the nature of that class, or *genus*. Each genus has its own name, or term. Within each genus there may be identified specific subsets of entities that share properties accidental to membership in the genus. Where a specific set of such properties are identified with a specific sub-set of the genus, that sub-set is referred to as a *species* and its defining properties as well as its membership in the overarching genus define its nature, or essence. The species has its own title and, when separated from its parent genus, forms a genus in itself, within which also may be found species, and the classification process is reproduced²⁶.

At each successive classification level the membership is more tightly defined, hence the natures are more precise. At the higher levels of classification there are fewer and fewer necessary properties, though they become more fundamental. At the most general level is the set of things that share only *being* in common, which is simultaneously the least informative characteristic, but the also most necessary.

3.2.3 Aristotelian causality,

An important part of Aristotle's metaphysics was his doctrine of the four causes. His identification of four necessary causes to all things that exist will be adopted in be analysis of economic goods. The four causes of all things that exist are as follows:

Material cause: The matter that the thing is composed of. In the case of material things, especially products, this could be taken as the raw materials. In economic goods, the ultimate material cause is the classical factor of production, land.

Formal cause: The design of the thing, its blueprint. There is no matter in form, in human terms it may be approximated to the design that may be represented in drawings, mathematical expressions or other media for communication.

Efficient cause: The mover, that which puts the form into the thing, combines the material and formal causes. In the case of products, this is the manufacturer and

²⁶ The process is replicated with progressively greater specification. At each level there is some variety possible, down the final level of a specific individual. For example, gemstones are a species of geological material, and have an identifiable set of characteristics. Gemstones may be classified by type into various species, such as sapphires and diamonds, which themselves each form a genus within which species exist differentiated by such things as colour and quality.

includes as instrumental efficient causes those tools used in the production process.

Final cause: The need or desire for a thing, the motivation for its production by the efficient cause. In the case of human economic products this is demand.

This system of causality will be adopted throughout the thesis.

There has been some critique of these four causes in recent times, especially the formal cause. Johnson (1995) located the motivation for this attack in a particular theological position and defended its retention as a foundation for all scientific investigation. The application in economics generally does not need to take the causes past the human final cause and production is generally located wholly within the material realm. For these reasons economics is not engaged in the application of causality in contentious areas and does not need to explore the matter further.

3.3 THE INTERRELATIONSHIP BETWEEN THE SCIENCES

Science is accepted as being the pursuit of *certain knowledge through cause*, a definition that provides definite boundaries, and within which the social sciences have a place. This does not automatically mean that any study can become a science because the aim of a science is *certain knowledge*. Scientific enquiry, especially that done following the Enlightenment tradition, has shown how difficult certain knowledge can be to obtain. Obviously, the possibility of *some* certain knowledge is sufficient to establish a line of enquiry as a science, even if the preliminary work does not reach this goal.

This definition explains why there has been debate for some time regarding the social sciences as true sciences. When their methodology precludes certain knowledge, they would appear to fail in the scientific endeavour, even if they do yield some practical results. Developments in the Sociology of Knowledge suggest that true knowledge is impossible. Although this is a self-refuting universal negative, it signals a popular belief that has infiltrated scholarly circles, especially in the social sciences. It is not accepted in this thesis.

Economics, as a species of social science, is considered to offer the possibility of certain knowledge, hence it has the capacity to be a true science, although it is also accepted that economic certainties may not be as plentiful as many would like to expect. In particular, certain knowledge does not imply certain predictability, and the laws underlying the social sciences are not deterministic. There are two reasons for this. Firstly, practical judgements are the result of freely willed decisions often made as the result of balances between competing goods, such as is found in the workings of

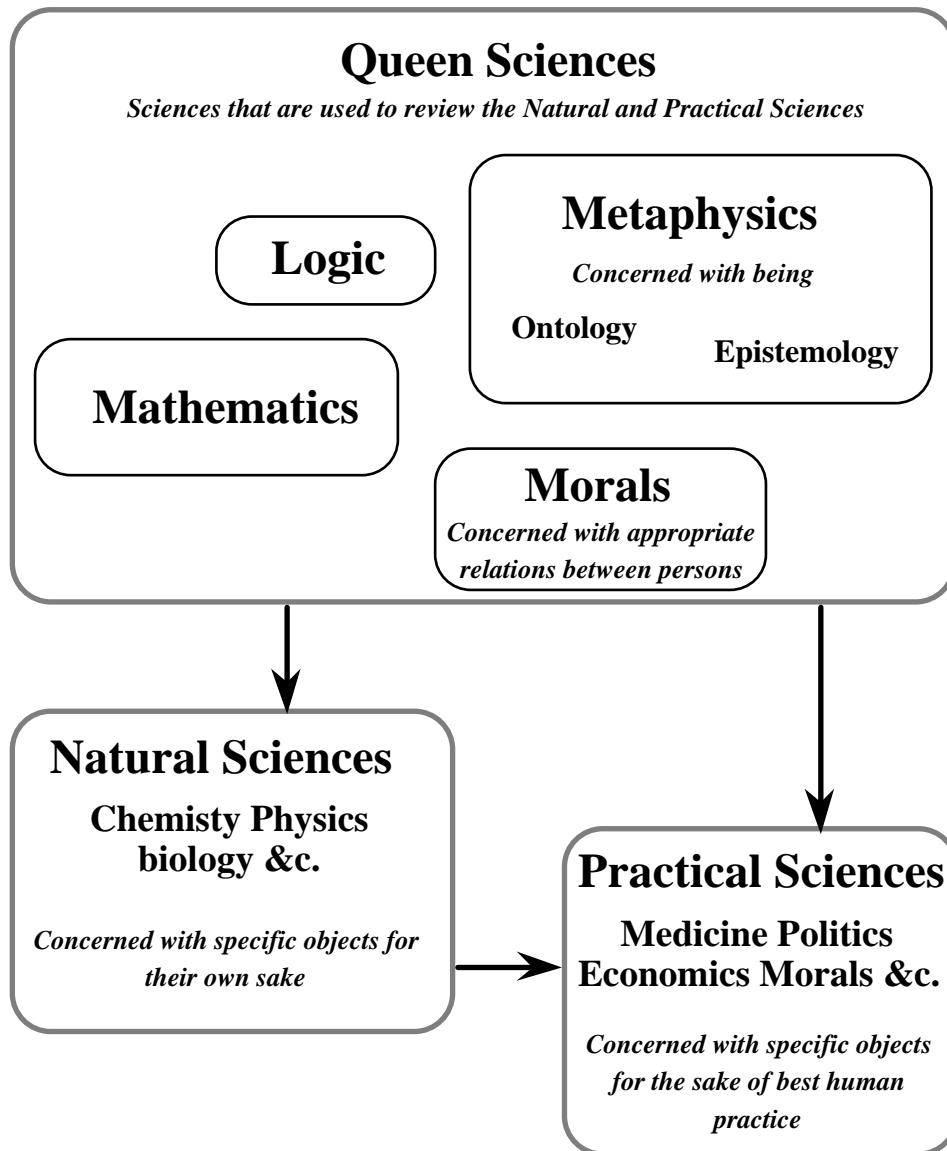
common law. Secondly, practical judgements are often highly sensitive to previous practical judgements of the same kind.

An example of the latter in the economic realm is the practical decision to purchase an investment, which would result in an increase in its demand and hence (adopting the common understanding of the operation of markets), its price. Such a decision is strongly influenced by the recent decisions of others regarding the purchase (or sale) of that kind of asset. In this respect, an analogy may exist between practical economic decisions and those physical systems, such as weather, that are currently being studied using chaos theory²⁷. Chaos theory suggests that certain physical systems follow rule bound behaviour but even though the rules may be knowable, the behaviour of the system may not be capable of determination in any practical sense (Gleick 1987).

The classical relationship between the sciences will be adopted as shown in Exhibit 4.1. Logic, metaphysics and mathematics form the Queen sciences, under which the natural and practical sciences fall. Economics falls within the practical Sciences.

²⁷Chaotic systems are usually characterised by relationships where the current values of a set of variables are the result of previous values of the same set of variables. Climate behaves in this way; climatic parameters are a function of previous values of themselves and other climatic parameters. Financial parameters are often complex results of decisions based on perceptions of the existing financial environment. In this way they fulfil the basic requirement of a chaotic system, although this is not sufficient to conclude chaotic behaviour.

Exhibit 4.1: The Relationship between the Sciences



Some relevant points that follow from the above are as follows:

- All sciences have a metaphysics which consists at least of statements regarding the existence of the objects of that science.
- All sciences follow the rules of logic.
- Moral Philosophy necessarily follows logic and has its own metaphysics. Sound moral thought may be analysed in terms of its logic and the validity of its metaphysics.
- Mathematics is logical and has its own metaphysics²⁸.

²⁸The type of existence enjoyed by mathematical entities is a particularly interesting and instructive metaphysical issue being capable of actual observation.

- Natural Sciences are pursued for their own sake, to better understand their respective objects²⁹
- Natural Sciences are logical and have their own metaphysics which consists at least of statements regarding the nature of the objects of the respective science.
- Natural Sciences do not study willed events and are therefore deterministic, making them amenable to mathematical interpretation.
- Natural Sciences are influenced to a limited degree by moral thought, in that some natural questions are considered immoral to pursue.
- Practical Sciences are all logical and have their own metaphysics which consists at least of statements regarding the nature of the objects of the respective science.
- The Practical Sciences are all directed to various human goods. They are all heavily influenced by moral science, to the extent that some are purely subsets of morals³⁰.
- Practical Sciences often apply knowledge found in the natural science for human good³¹.

3.4 MORAL PHILOSOPHY

Moral philosophy has been described as *the study of appropriate relations between intelligent beings* and this definition will be adopted in this thesis. Its purpose is to discover those actions that are most appropriate between beings that are endowed with reason and will. Most practical sciences are either wholly or partly within the general parameters of morals. For example, political science is concerned with the organisation and governance of society with the aim of optimising the life of its citizens, and quite visibly falls within morals as defined. Engineering on the other hand, is a practical science that aims at utilising various natural sciences (physics, chemistry, geology, etc.) for the benefit of humanity. It also borrows heavily from the highly mathematical methodology usually associated with these sciences. Its exercise is predominantly an intellectual virtue. However, the fact that its object is ultimately human action directed towards human goods, means that it too has a moral dimension. To this extent, engineering directed towards an end other than human betterment could be rightly considered to be poor engineering practice, even if it achieved that other end. Economics will be argued to fall somewhere between political science and the engineering of production, hence it is subject to morals and part of the methodology of

²⁹The biologist studies living things to understand them better, not to benefit the human condition directly, even though applied biology, as used in medicine, may use biological knowledge to aid in the achievement of the good of human health.

³⁰Professional ethics is an example of this.

³¹ For example, medicine has the good of human health as its object and it pursues this object by using knowledge from various natural sciences, most apparently biology and anatomy.

the thesis must therefore include the selection of an appropriate moral system under which to examine economics.

There have been many attempts developing robust moral systems, these largely vary on the basis of the meaning of *appropriate* within the definition, more recently they have even gone so far as to ask if moral philosophy actually has any content. A selection of moral systems will be briefly reviewed and contrasted with the Aristotelian system. Although built on the moral thought of Plato and Socrates, Aristotelian morals have been widely accepted as constituting the foundational moral system, against which others are either developed or contrasted.

3.4.1 Sophist Morality

The Aristotelian realist morality was not the first systematically recognisable moral system. That distinction is held by the Sophists. Sophist moral thought may be paraphrased by the maxim: "*Seek pleasure, harm no one.*" The shortcoming of this system is in its identification of pleasure as the ultimate moral goal or greatest good (*summum bonum*). It also fails to recognise occasions when harming others or avoiding pleasure may be valid behaviour.

The Sophist's success in spreading their morality, especially amongst Greek youth, was largely what stimulated Socrates and his followers to look deeper. Sociologically, Greece at the time of Socrates was suffering cultural demise. This was evident especially in the poor behaviour of Greek youth. The fact that Plato and Aristotle were critical of the youth of their day has been taken by some, especially in recent times, to suggest that poor behaviour amongst youth is a part of human nature. Unfortunately, this position ignores most of human history. What is evident is that the sophist maxim tends to be popular in periods of affluence as it is ultimately highly self-indulgent and not conducive to the self-discipline required by members of a community in order to develop, either materially or culturally.

Aristotle recognised the value of some choices that were not pleasurable, such as choosing to defend one's country, or studying, or truth telling when such would cause personal harm. In general, civilisation is reinforced by self-restraint, expressed in a wide spectrum of situations from personal development to willing not to take advantage of others in situations in which they may not be aware of the exploitation.

3.4.2 Aristotelian Morality

The Aristotelian moral system has several planks, one of which is the maxim to "*do good and avoid evil*" which parallels the Sophists, though it uses different criteria. Good was understood by Aristotle to be anything that was conducive to supporting humans in fulfilling and perfecting their lives. As such, it has many dimensions, hence

a good meal supports material life while a good friend supports a higher aspect of human existence. The social nature of humans suggests an area of the good that relates to inter-personal relationships, expectations and trust.

Aristotle recognised that the highest human goal is happiness. It is the end (final cause) that is desired for its own sake and not for the sake of anything else. He recognised that happiness was intimately related with perfecting the expression of one's nature. For the human, as a social creature having a nature that includes intellect and will, this infers that the good will include these higher dimensions, expressed partly within a social context.

Unlike bees and other creatures that live in communities by *instinct*, humans *will* their social interactions. The social dimension infers that the good human must will the best realisation of human nature for those others in the community. This produces a reciprocity of goodness; the person achieves the best realisation of human nature in self-fulfilment that depends in no small degree in willing those things that promote the best realisation of human nature in others in society. The realisation of good in the society is known as the *common good*, and it is evident that it is part of the intended willing of the good person.

Habits of action that achieve good outcomes (as defined) are termed virtuous. A habit is an inclination towards a particular course of action. Aristotle identified two classes of virtues, which are referred to as moral virtues and intellectual virtues. A moral virtue is a habit that inclines the holder towards moral actions. It is a part of the person in the sense that to have it is to exercise it. Moral virtues include truthfulness, respect for property and respect for persons. One cannot act contrary to a genuinely held moral virtue without losing that virtue. Hence a person who lies does not have the virtue of truthfulness, even if that person tells the truth on the majority of occasions. The importance of respect for property and truthfulness has obvious importance for economics.

Intellectual virtues relate to skills that a person may have that enable that person to do useful things. Engineering and accounting are both intellectual virtues. The engineer and the accountant both have particular abilities that can be used to bring about good for themselves and others. Unlike the moral virtues, it is not necessary to exercise intellectual virtues in order to hold them. Hence, I may have the intellectual virtue of being able to fix automobile engines, but choose not to practice it. Financial skills, such as being able to select the most profitable investment, or accurately assess market value, are intellectual virtues at the heart of economics.

Aristotelian morals are based on natures, especially human nature. If people achieve happiness when they most fully realise their human nature, in all of its facets, then an

understanding of human nature is a necessary starting point in the science of action directed at that nature's flourishing. As natures do not change, morals do not change. This is not to say that our understanding of morals will not change, or that differences will not exist between various persons or groups. It does mean that there is a spectrum of quality that may be identified in moral thought, depending upon how effectively a given moral system achieves maximum human happiness³².

Aristotelian moral thought combines both pure and practical moral determinations. Respect for the human person may be considered as an absolute moral principle. It derives directly from the moral aim of willing human good. It would be impossible to will the human good of a person without respecting their person, their humanity. To treat a man like a dog would not contribute to his flourishing. In addition to these absolute and intrinsic moral values, there are many moral determinations that derive their moral status either indirectly, or through some practical judgement. Indirect moral values typically follow when an intrinsically amoral act acquires its moral status from its end. While this is a very important principle, it must be remembered that a good end cannot justify an intrinsically evil act³³.

In practice, virtuous acts are usually the outcome of a balance between competing moral principles. This will be discussed under the heading of *virtus stat in media*.

The Aristotelian system combines both morals as the result of a consideration of ends and purpose (teleology) and morals as duty (deontological morality). Aristotle employed teleology in determining morals, but it is equally relevant that humans conform to their human nature in choosing their actions. This obligation of the good person towards the free willing of good signifies duty. Here duty is really no more than the choice to conform to one's own human nature. The good person is more completely human than the evil person is. This theme is embodied in the common evaluation of an evil act as *inhuman*, or sometimes *bestial* (though evil is below the action of animals, which always conform to their natures). The duty of humans is therefore to act according to their nature, which requires acting so as to facilitate the flourishing of all that is human (i.e. human nature), both in themselves and others.

³²This notion of happiness maximisation should not be confused with the Utilitarian calculus of *The Greatest Good for the Greatest Number*

³³ An important apparent counter-example to this principle was Aquinas's conclusion that market commerce was *of the nature of evil*, but that *its exercise was not always evil*. What Aquinas appears to have been saying here was that market commerce, if allowed to follow the patterns that were normally in evidence in its exercise by fallen men (all mankind) followed rules that were intrinsically directed against the flourishing of human nature. This would be evident through the exercise of vices such as greed. However, Aquinas recognised that a self-restrained man could engage in commerce in the market that was not motivated towards exploiting his neighbour. This would infer engaging in what Aristotle understood as natural exchange. While natural exchange may be practised in market commerce, the market does not necessitate it and is usually characterised by maximised self-interest.

3.4.3 Modern Moral Systems

David Hume sought to eliminate the metaphysical dimension from philosophy in general, and developed a system of moral thought based purely on perception. His aim was to “... attempt a like reformation in all moral disquisitions; and reject every system of ethics, however subtle or ingenious, which is not founded on fact and observation” (Hume 1777/1975, n.138 p.175). To do this he had to posit the existence of an inner moral sense, his *moral sentiment*, which reacted to perceived series of events and responded with sentiments of approval or disapprobation. His argument in support of the moral sentiment was based on the observation that “*This final [moral judgement] depends on some internal sense or feeling, which nature has made universal in the whole species*” (n.137 p 173). That is, all peoples in all times have shared a common set of responses to events that are recognised as carrying moral significance, and hence they are able to virtually see the morality of situations without deep reflection or philosophical education.

His basic position that persons are latently aware of the morality of situations is a very strong theme in popular thought today, especially in the tendency to allow all persons the right to make their own moral determinations and the popularity of attitude surveys in studying moral values.

The shortcomings of his moral sentiments become apparent when one contrasts them to the metaphysical moral essences that he sought to usurp. The moral sense is supposedly universal, somehow available to all. As a universal it is similar to a metaphysical essence. Unlike its metaphysical counterpart, that can be explored, discovered and refined, a sense faculty cannot be consciously changed at all. People cannot change their sense of smell.

It therefore makes no sense discoursing on morals, though many humans, not the least those most fond of Humean thought, tend to behave otherwise. More problematically, some people do not seem to have been granted the same moral sense as others have, some entire societies behave in ways that most others find morally repugnant. If moral behaviour follows on moral perception, how can a murderer be guilty, if *the cold-blooded killing of an innocent* appeared at the time to be morally acceptable to the moral sensibilities of the murderer? If the Humean concludes that the murderer has a faulty moral sense, then against what standard is it faulty, if not some essential form for the moral sense? Hence, essence reappears.

Likewise, entire nations engage in moral dialogue, and somehow universals, such as peace, seem to be promoted by global fraternities such as the United Nations. Again the

conclusion must be that there exist essential moral values that are available to the intellect.

The greatest difficulty for the moral sentiment is differentiating it from a metaphysical construction of morals, which is also universal, intangible and accessible through means other than external perception. The latter has the advantage that it is a most suitable subject for human discourse, and also admits of variation in personal determination, though the latter usually is the result of some sort of human mistake.

3.4.4 Kant's Categorical Imperative

It is not difficult to demolish the strong Humean position, despite its persistent popularity, evidenced by recent slogans such as *"Do what you think is right"* or *"If it feels good, do it"*. Kant (1993) sought to strengthen the Empiricist moral system with his suggestion that one should only act on maxims that could be reasonably adopted as universal laws. Kant was trying to marry the obvious necessity for moral universals with an ultimate personal onus as to their determination.

In Kant's system, the person decides what passes muster as a suitable moral value. The lofty prospect of individually recognising contenders for universality makes man the measure of morality and subtly derides the knowable existence of universals. His system validates moral discourse and punishment of those that the majority, or at least those in power, consider to have acted in a morally deficient way.

Curiously, he also argued strongly against lying in any circumstances. Such an argument could only be taken as recognition that at least one moral universal did exist that was not open for personal evaluation.

Kant does not necessarily disagree with Aristotle, in terms of a procedure for testing the quality or content of morals, only on his denial of universals. On this basis, he may be interpreted as offering a vaguely consistent system, and the application of Aristotelian method may even aid the seeker in identifying suitable maxims. Aristotle does considerable more than this, but the point is that an Aristotelian moral enquiry does not necessarily evoke objection from a Kantian on the basis of method. The Kantian's discomfort develops only when the Realist Aristotelian asserts that universal essences can be used in understanding morals or that moral conclusions may themselves form universals.

Kant's moral system was strongly deontological. He argued that only when action was undertaken out of duty, and not out of any other inclination, did it have moral merit. While it is true that coerced action has no moral value, Kant appears to have excluded the possibility of the merit of freely willed actions chosen because the moral agent recognised the value of the ends of such action, both in terms of personal

fulfilment and the good of others. While duty is a convenient shortcut for moral choice, it is contingent on the virtue of the system that originated the duties and hence the moral merit of the person accepting duties derives its value partly from the reasonable moral enquiry of that agent into the reliability of the duty system.

Consequently, duty cannot be a true foundation for moral action, as it must be tested using some more fundamental moral criteria. Kant's moral system is therefore a useful practical guide, but points ultimately to the necessity for a more fundamental moral system that is able to provide reliable moral determinations. The notion of personally selecting contenders for the status of moral universals gives curious support to the necessity of the latter, while ultimately subverting its importance.

3.4.5 Utilitarianism

The basic Sophist moral system was revived and refined in the nineteenth century as a quantifiable empirical moral system that has found favour up to the present. Jeremy Bentham and later John Stuart Mill adopted the basic Sophist identification of pleasure with goodness and provided a maxim for moral action that was simply "*the greatest good for the greatest number.*" Using the basic materialism and empiricism of the Enlightenment, these men concluded that good cannot extend beyond the material order and hence must be co-extensive with pleasure. Although including intellectual pleasures, these fell far short of Aristotle's notion of the whole man. Utilitarianism has difficulty with self-sacrifice where there is no apparent beneficiary. However, it does suggest a potentially objective system by which moral action can be evaluated with mathematical precision by the simple addition of the total pleasures less the total pains for all affected by a particular course of action. These could be notionally compared to competing courses of action with the moral choice falling in favour of the greater positive net outcome.

The attraction of this calculus for maximising goodness across an affected group, i.e. utility maximisation, was that it could be objective and definitive and therefore a most suitable basis for both private and public policy. Utilitarianism has found considerable application in political science and is foundational at the heart of modern economic theory which depends on the consumer being a person who maximises utility.

The shortcoming of utilitarian morality is that, like Kant, it leaves the moral actor to compute the utility maximisation of each contentious moral decision, without any need for recourse to fixed guide-lines. While the latter may provide a convenient shorthand, the former presents a serious practical problem. Psychologically, people tend to value the here and now more heavily than the remote. This tendency applies both for

evaluating the relative costs and benefits across those others who may be affected and also for the moral actor alone through time.

It is commonly recognised that news reporting weighs human disasters in proportion to their proximity. A single local murder receives the same media interest as the genocide of thousands in a remote part of the world. Humanly, utilitarians are likely to prefer cheap imported shoes even if they put many out of work in a distant part of their own country. Because utilitarianism relies on effects as they are perceived, incremental harm, such as the increase in insurance premiums as a result of fraud, may slip from the calculus altogether. This is the backdrop to some popular stories, often expressed on film, where "good" thieves use their takings for philanthropy, while their victims escape actual harm because their losses were insured.

Likewise, the difficulties many people have managing credit card debt illustrates the extent to which immediate pleasure outweighs future distress. In addition, utilitarianism has two other major and crippling problems.

Firstly, it assumes that the utility calculus can be accurately achieved. The reality is that utility is notoriously slippery, in practice it often appears to be an individual subjective evaluation that changes with time. Economics is probably the area where its evaluation is most advanced, but even there is only vaguely effective and its apparent successes may be an illusion. Fisher (1930/1977) described the way that the real reason a person engaged in the economy could not be observed or measured. Fisher suggested that people seek an enjoyable life, and this is their real income. However, an enjoyable life cannot be directly measured, but may be only proxied by the material things that fill a person's life. Unfortunately, these diverse things cannot be directly compared, but their value may be proxied by their prices. Consequently, utility is observed at best only through two successive proxies, neither of which is particularly accurate. Hence, the suggestion that economics can equate utilities is poorly defended.

In particular, price would only be a reasonable proxy if it did accurately reflect utility values. But this can only be a coarse assumption at best. People may continue to buy milk for given price, even though their fondness for it may vary daily. Further, market theory would appear to suggest that even in a relatively mature and near-perfect market, Demand theory suggests utility is a function of quantity which means that price is only one possible utility on a quantity-dependent continuum.

The second weakness with utilitarianism is that it includes negative utilities indiscriminately in its calculus. It is true that sometimes persons choose personally unpleasant courses of action in order to help a larger number of others. However, that is very different to inflicting hardship on others because it will be outweighed by the

pleasure one receives personally. Mugging and burglary could easily become virtuous in utilitarian morality.

Most people recoil from the prospect of willing harm on innocent others, even if the outcome is a great good for the community. Unlike accepting the risk of harm oneself for the greater good of others (courage), the willing of the same on others is the greatest cowardice. Kant was clear in his denunciation of using other humans as objects, rather than respecting them as persons. Realist thought would view this a violation of Aristotle's imperative to 'avoid evil'. Even the Sophists were explicit in their insistence to "harm no one" and Hume's moral sentiment would appear to reject such a possibility, given the response of the average person. The moral sentiment has been seen to be the least reliable indicator of moral direction, and in this instance it must be noted that in the case of *mixed goods*, situations where a moral choice involves a mixture of good and evil, moral sentiment can be swayed by the attraction of great apparent benefit³⁴.

The utilitarian could be expected to retaliate from this broad consensus of rejection from virtually all other major schools of moral thought by pointing to the fact that most societies do also harm others for a greater good. Their example would be punishment for crime.

However, punishment and public order are poorly justified in utilitarian morals. Bentham is also remembered for designing prisons and although his moral system inferred that the individual might validly choose bank robbery³⁵, he suggested that punishment had the effect of swaying the individual's moral calculus away from acts that were not in the public interest. There are many problems with this position, mainly orbiting around the tension between the utilitarian calculus of the individual and the community. How is the community able to know the best outcome? Why is it not simply the oppression of a minority? If the community is able to apply a more universal perspective, why is it that this perspective is not a genuine universal and on what basis is it justified? What is the individual to do when the community enacts peculiar and apparently immoral sanctions? Does this not then mean that punishment no longer

³⁴ Abortion is a good example of this. The harm involved is generally poorly understood by the average person in most Western countries, while the convenience and facility it affords for a licentious lifestyle is a great apparent good. Hence the moral sensibilities of many people are swayed to the point that the reality of the murder is ignored. The point here is that the moral sentiment that may validly recognise the evil of the act is deadened by the overarching attendant benefits. This may be an argument in support of the correlation between moral sentiment theory and utilitarianism. Hume used the notion of utility in his construction of morals that would support such a connection. However, his recourse to utility was actually evidence of the failure of a natural and innate moral sense in the terms Hume described it.

³⁵ An individual may decide that the benefit from such an act would outweigh the harm to depositors, especially if they were convinced of the credit creation powers of banks.

needs to be proportioned to the crime, in that it should be severe enough to ensure the desired outcome³⁶?

Part of the appeal of utilitarianism is its underlying anthropology which, like much from the nineteenth century, assumed that human action was no more than a deterministic result based on "laws" of behaviour. This position often referred to as voluntarism still dominates Western social science. It is opposed to the view of the person as an intelligent being who acts on intellect and will, according to human nature. This latter view is known as naturalism. While voluntarism has an elegant simplicity expressed in Skinner's behaviourism, it has proven problematic in yielding useful predictions of human behaviour. Positive social science is content with levels of statistical significance that an engineer or physicist would discard as far too vague to be reliable. On one hand this would appear to be empirical proof that voluntarism has failed to disprove its own null hypothesis³⁷ Like the multiplication of Ptolemy's spheres, the voluntarist can construct any number of extra levels of deterministic calculus into the decision framework of the person.

However, three lines of evidence appear available that make such a construction appear unrealistic. Firstly, common experience and popular belief weigh in heavily on the side of naturalism. While this is not a definitive argument, its broad occurrence must be considered seriously before being dismissed. Second, Aristotle and other realists have shown that human action can be understood more simply in terms of intellect and will rather than a complex moral calculus. Occam's razor would cut in favour of the simple rather than the complex theory. Thirdly, positivist social science has been unable to identify the supposed laws of action nearly as precisely as the voluntarist position would suggest. Positivism itself upholds that what cannot find expression in observable terms does not exist, hence it would appear to be a positive conclusion that voluntarism is deficient.

3.4.6 Twentieth Century Moral Thought

The current development of what is known as post-modernism is largely built on an poorly understood realisation that modernism is a failure, not only in popular common sense terms, but even in its own terms. It is a failed experiment. Unfortunately, rather

³⁶ Ancient Babylon had basically two punishments, minor fines, or death. This had the advantage that there was no need for prisons and the deterrent of the death penalty powerfully controlled inclinations towards crimes such as burglary. It is hard to justify this today, despite its formal utilitarian attractions. Conversely, transportation was a rather severe penalty for petty theft in Enlightenment England, yet it failed to curb theft amongst the common people.

³⁷ Empirical science is done by experiments designed to disprove the negation of a particular causality, the null hypothesis. The null hypothesis to the proposition (hypothesis) that positive social science is valid is the proposition that empirical social science is incapable of explaining human behaviour sufficient to assert the voluntarist position.

than reviving interest in the system of thought that modernity sought to replace, it has taken the dysfunctional aspects of modernity and moved further from reason. This is especially evident in moral thought, where the ascendant moral system is Propositionalism, the belief that a moral is no more than a particular literary form distinguished by the intent of its author to cause a particular behavioural outcome in its recipient.

Propositionalism contains an element of truth. Moral discourse is intended to affect behaviour. The current debate on the effects of media on society's moral direction, regardless of which position is concerned, concerns the way that these communications are recognised as affecting behaviour. However, to refuse that moral philosophy has any further depth is to empty its content, which is exactly what (Warnock 1967) concluded was sum of twentieth century moral development.

Propositionalism is barren and unsatisfying. While it is true that given a modern philosophical foundation, and the recognition that modern moral thought leads to subjective relativism, it must be concluded that there can be no firm basis for morals, this is blatantly contrary to human experience. Torture and theft are repugnant, and a statement directed against them is more than an exercise in behavioural modification.

More problematic, is the difficulty in using propositionalism in any meaningful analysis of moral value. Propositionalism perhaps may be used to identify the existence of a moral statement, though even that is possibly unreliable, but it is certainly useless in delving into the reasoned development of moral understanding or the application of moral evaluation to novel situations.

3.4.7 Selection of a Moral System

Similar to the argument in favour of rejection of the hard form of modern empiricism, Warnock's assessment of the plight of recent moral thought may be taken as sufficient evidence that the fundamental direction of modern moral thought is deficient. This does not mean that these systems contain nothing of use, only that they are insufficient to provide a robust test of moral worth. The shortcomings of the Sophist system has already been considered and in light of its similarity to utilitarianism, the latter may also be rejected.

While this survey of moral systems is by no means complete, it is sufficient to demonstrate the potential superiority of the Aristotelian system, or at least its validity as an alternative. In addition, the Aristotelian system has a unique advantage for the present enquiry. Because it encompasses both moral and intellectual virtues and considers both objective and practical dimensions of moral values, it is singularly

suitable for use in evaluating the practical science of economics, since the latter appears to contain all of these elements.

In addition, Aristotelian moral thought provides a methodology that may be used to review even Aristotle's own moral conclusions. This is especially useful, because it is often noted that some of his conclusions are considered unsatisfactory today, which is sometimes used to validate the rejection of his entire system of thought. Because Aristotelian method may be used to review these controversial conclusions, such as his acceptance of slavery³⁸, it provides a dynamic tool that is not limited to his position in totality. This will be very useful, as there are some Aristotelian economic ideas that this thesis will seek to revise.

Finally, like some other moral theorists (including David Hume, Adam Smith, & J.S. Mill) his thought includes treatment of economic issues. Like these, he has integrated his economic thought into his moral thought using one to inform and illustrate the other. It is no surprise that various recent economists have referred either positively or negatively to Aristotle³⁹.

3.4.8 Virtus Stat in Media

Aristotelian moral thought does not merely consist of a set of moral absolutes, even though it is filled with universals. Aristotle recognised that while there were undeniably components and processes in morals that were unchanging, moral action was not so cut and dried. In particular, practical moral decisions were the result of complex prudential judgements both between competing moral goods and the degrees of application of specific courses of action.

Common law is a good example of a public attempt to determine practical judgements between competing moral principles (Dworkin 1977). For example, if I am short of time before a meeting and have the choice of either shaving or arriving late, I must make a prudential judgement between two competing goods. Being on time for a meeting is one way of respecting the person whom I am to meet, just as much as being well groomed is. Neither is necessarily absolutely better, both are good, but one must be sacrificed.

Aristotle in his *Ethics* (bk. II) recognised that the degree of action in various spheres of action must be proportioned, with both excess and deficiency being morally deficient. For example when a response is required in the face of danger a person can

³⁸Even here caution should be applied because what is often criticised is a straw man compared his actual position

³⁹Marx adopted much of Aristotle, most visibly his notion of natural and unnatural exchange while (Hayek 1976) used his notion of household.

either respond as a coward and avoid action or foolhardily by taking unnecessary risk. Even in the domain of telling the truth, excess and deficiency both exist - a deficiency in truth telling is lying, while an excess in truth telling is gossiping. This principle of virtue standing in the middle (*virtus stat in media*) has become known as Aristotle's Golden Mean and is an important component in practical moral judgement.

3.4.9 Justice

An important dimension of moral action is justice. Aristotle devoted considerable attention to justice in his *Ethics* (bk. V) and subdivided it into several parts. At the least, it denotes fair play and Aristotle considered that legal justice focused on this aspect, though his idea of law is not always clearly distinguished between particular civil law and the underlying natural law (he does explicitly treat this distinction (1134b8-1135a8)).

Of interest in economic enquiry is his treatment of justice with respect to material things. Aristotle identified distributive and commutative justice as important elements in economic relationships, as well as having significance for other human relationships. Distributive justice relates to fair distribution across the community and is evident in the economic problem of distribution that is perhaps the core issue in economics. Economic distribution explores the appropriate distribution of goods and services across the community and considers questions such as the just returns to the owners of capital versus workers or the community in general. The modern welfare state is partly in place on the basis of a set of beliefs regarding just distributions to those who, while not contributing to production directly, have some claim of the community's product merely on the basis of their humanity.

Commutative justice relates to fairness between individuals who interact in some way. The Old Testament "*tooth for a tooth*" doctrine is an expression of commutative justice. In the economic sphere it relates to fairness in trading exchanges.

Justice is linked closely to property, because without some understanding of property rights, commutative justice in trade could not be resolved.

3.4.10 Economics and Morals

Economics as a science is aimed at the efficient allocation of material goods within the community. Efficient allocation is an application of distributive justice - that each person should receive a just share of the goods of the economy - but also on charity: that those who are unable to provide for themselves deserve a reasonable share in the goods of the community merely by virtue of their humanity.

Economics is also concerned with market behaviour, which assumes private property rights and justice in exchange, that is an application of commutative justice.

Although positive economics has developed as an experimental and quantitative science, its prescriptions are fundamentally directed towards the good of the economic players and the good of the community as a whole, the common good. In proposing the name "Economics" for the discipline, Marshall (1920/1938) suggested that its moral purpose would be best realised through a positivist methodology. Largely this is the current form of the discipline. As such, it is evident that it is a sub-set of moral thought.

Economics has been defined as the study "*of appropriate relations between people with respect to material goods*" clearly drawing out its compatibility with the earlier definition of morals. This definition will be adopted in this thesis.

The methodology of economics, being predominantly positivist, is open for discussion, and this is largely the focus of this thesis. The question of how far economics should adopt the methodology of moral philosophy, and in what ways this methodology can inform economics is central to this thesis. It will be argued that purely positivist economics is not only incomplete, but also contains contradictions within the positivist methodology itself.

3.4.11 Laws in Moral Thought

Moral laws are of a different order to physical or mathematical laws. Hume's endeavour to produce a moral science modelled on Newton's physics reflects an expectation that laws could be found that would always find deterministic expression. This is clearly evident in the Physiocrat's economic enterprise that set out to identify the laws underlying economic behaviour. Some authors suggest that the market works under the *laws* of supply and demand, however this appears to be a somewhat looser conception of a *law* than Newton's isomorphisms between physics and mathematical equations.

What is probably more reasonable is the identification of principles of action, rather than deterministic laws. In this way laws may be identified that contribute to the content available for reasoned moral deliberation, without necessarily resulting in definite behavioural outcomes.

Examples of this type of law include the following:

- 1) Lying is morally abhorrent
- 2) Do good and avoid evil

- 3) When deciding between competing goods for purchase, if quality is comparable, choose the less expensive

While each of these is recognisable as a principle for action, it should be evident that they do not result in deterministic behaviour. It is also important to recognise that while the first two determine behaviour morally the third does not. The third case will be considered separately under consideration of intellectual virtues because of their special relevance to the study.

Overall, most practical moral decisions are the result of the practical weighing of a set of moral principles that are often in competition⁴⁰. While there are some moral principles that are fixed, that is, objective, such as the admonition to do good and avoid evil, the application of this moral law may be the result of a highly personal and partially subjective calculus. This means that moral truths/laws may not be simply positively evident as behavioural cause/effect events.

This does not mean that they do not exist, only that they exist at an intellectual level, not a behavioural one. Also, it may be possible for different persons to follow them yet give them very different expression. For example, with respect to real property rights, various cultures have very different cultural practices ranging from feudalism to the jubilee practices of the ancient Hebrew tribes that are all various expressions of the one underlying moral theme of common use.

Property rights in land and their expression in prices will be major part of the focus of this thesis. It is asserted that property rights may be constructed using Aristotelian metaphysics, which can be further developed to draw certain objective moral conclusions. Consequently, these moral conclusions could be validly labelled natural moral laws, despite them not prescribing specific models for economic behaviour.

A relationship between property rights, productivity and price will be explored developing Ricardo's rent theory, often referred to as his *law of rent*. This economic law will be examined as a behavioural law based on intellectual, rather than moral, virtues. This necessitates consideration of the distinction between moral and intellectual virtues.

⁴⁰This point is most evident in the operation of common law, which may be best understood as a particular application of the moral law, in that is commonly understood as the best determination that a community can make of what is generally understood to be appropriate behaviour between persons (Devlin 1965). (Dworkin 1977) explored the way that the court must weigh competing principles to arrive at a just determination, where the principles in themselves often led to conflicting conclusions.

3.4.12 Laws and Intellectual Virtues

While moral laws are evidently of a different nature to laws governing the natural world, they are not the only exceptions. Aristotle's distinction between moral and intellectual virtues recognises a third realm that has its own principles of operation. A theory of action in the area of intellectual virtue may differ from that appropriate to the action of morals, and both are distinct from the sub-human movement that is commonly referred to as the behaviour of nature.

Intellectual virtues are those that a person may have that enable the person to act in a way that results in a good that is not moral. For example, a pastry cook is able to produce a more effective enjoyment of human life for those who benefit from the fruit of his art, than somebody who does not know their way about in a kitchen. There is no moral, or even necessarily material, difference between dry bread and exotic pastry, but most would prefer the latter. Most occupational skills are intellectual virtues, as are sporting abilities. They all allow the holder to either achieve a higher level of human perfection, or provide goods or services that enhance the quality of life for themselves or others.

Intellectual virtues are found in most parts of the economy. They can be recognised as the skills of producers (efficient causes of material goods), designers (producers of the formal causes of material goods) and service providers. The reason many commodities are referred to as '*goods*' is precisely because they enhance human life, or flourishing, and the causal factors of their production indirectly contribute to this good. Because acts powers and habits take their value from their ends, they are good by consequence, though they are not necessarily morally good.

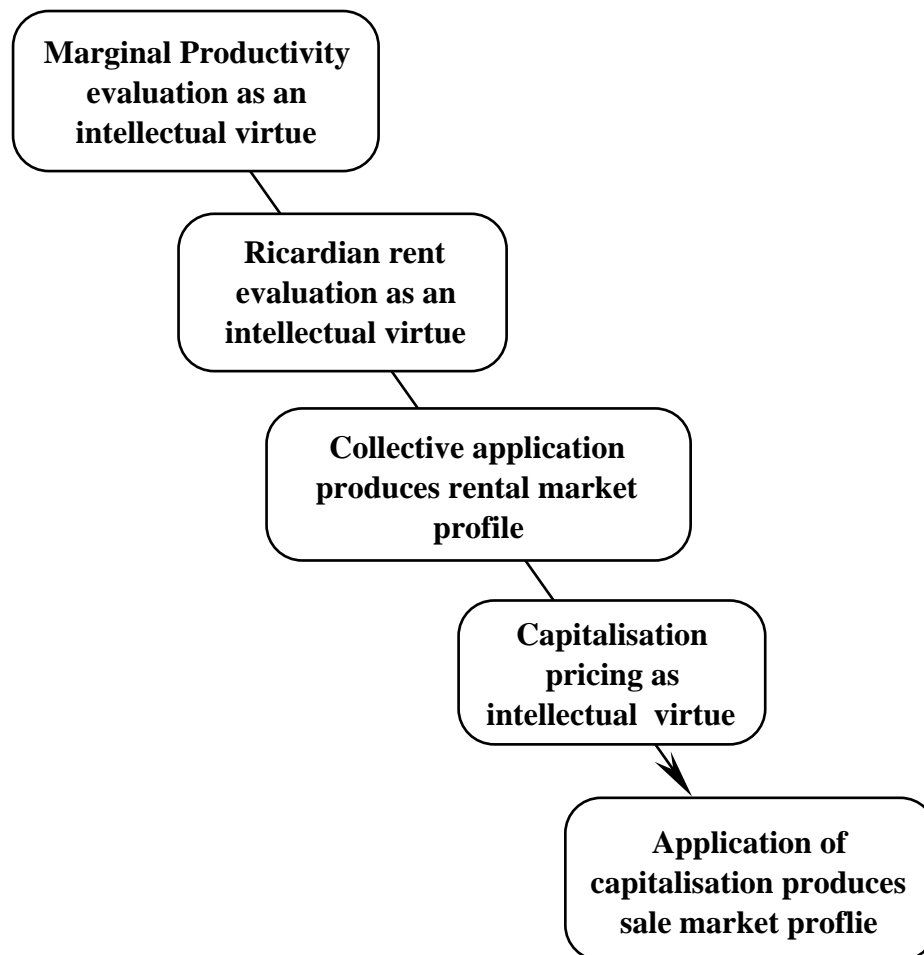
Significantly, the holder of an intellectual virtue, say the pastry cook, may choose whether or not to exercise that virtue, and indeed such a restraint may serve a higher, moral, good. For example, the pastry cook may choose not to practice his craft at home out of prudent concern that such may prove too strong a temptation for his family towards gluttony. The fact that the cook sometimes chooses to cook plain things does not in any way diminish the reality of his intellectual virtue. This is in contrast to the moral virtues. A person who occasionally chooses to lie does not possess the moral virtue of honesty, even if that person speaks the truth on the majority of occasions.

If the market place is filled with intellectual virtues, then it is appropriate that a science of the market place should explore the way that these virtues are exercised. If there are constant fundamental principles governing their operation or consistent objective results evident from their application, then these are reasonable to explore, especially if they have apparent implications for the individual or the community. Exhibit 4.2 illustrates the way that the recognition of Ricardian rental law and

capitalisation valuation as intellectual virtues places intellectual virtues as the cause of the market profiles of both the rental and sale markets for real estate. In particular, if the operation of intellectual virtues follows constant knowable principles, then it would appear reasonable to consider these principles as laws of a similar, though distinct, type to the moral laws.

They are similar in that they are both fundamental, almost background, principles governing behaviour decisions and also instances of their particular violation is not sufficient reason to discard them. They are distinct because essentially they are not moral and they may be expected to be more evident in behaviour than moral laws⁴¹. They tend to operate within a moral umbrella.

Exhibit 4.2: Intellectual Virtues as a Theory of Action



⁴¹ When the pastry cook or the engineer are practicing their arts, their behaviour is highly stylised, whereas the operations of moral intent may be masked by the complexities of a particular situation. This is not to say that moral laws are not evident in behaviour, but rather that intellectual virtues reside more in the practical order than the pure.

The Enlightenment thinkers definitely thought that these principles were in the form of laws. Hume and others following his tradition was explicit in setting about to study the laws of human action, hoping to reduce them to a Newtonian model. This tradition underlies methodology behind the modern sciences of sociology, psychology, and positive economics, however these are young sciences and their positive dimension has been rather niggardly in yielding clear and useful conclusions. While these are in many cases explicable in moral terms, much of their attention relates to the practical operation of intellectual virtues as well.

The failures of these sciences in exposing Newtonian like laws is often due to their failure to take into account key aspect of the human condition, especially the operation of will, but they also appear to have little place for charity and other human moral virtues. These are moral issues, and it has been argued that the exercise of intellectual virtues operates under a more encompassing moral umbrella.

However, given a suitable moral situation, it may be said that persons exercising intellectual virtues do display consistent and predictable behaviour that may be interpreted sociologically as sufficiently causal to warrant the label *law*, even though plentiful exceptions exist. If it is assumed that overarching moderators, such as morally based decisions not to exercise one's intellectual virtue, do not impede one's choice of action, then the exercise of intellectual virtues may produce apparently law bound behaviour. For example, consider the following:

- *Small's law of tennis*: given a reasonable approach trajectory, a tennis player will propel the ball over the net, to bounce in the opposing players court at a location inconvenient to that other player.
- *Small's law of plumbing*: after plumbers have finished their work pipes do not leak.

These are both amenable to sociological observation, but:

- They do not infer that the subjects observed have no will (only that they have been observed at times when they have willed to exercise their intellectual virtue).
- The subjects have the freedom not to exercise their intellectual virtue.
- The exercise of their intellectual virtue, as observed and embodied in their respective laws, is not moral.

In addition, the existence of laws such as these provides a basis for evaluating the quality of the intellectual virtues being exercised. This is exactly what is being tested in sporting events or evaluated by the market when a price is linked to a perception of quality.

In the instance of the market place, two sets of intellectual virtues may be identified. The first have already been described and relate to skills as either material cause of production, or the contribution to its formal cause as a human designer. The second set of intellectual virtues found in the market place relates to the ability to assess value. It is this latter species of intellectual virtue that is distinctly economic and is found at almost all levels of the production/trading process.

It will be argued that in practice the allocation of value has a moral dimension, but it should be evident that the moral aspect is a determination based partly upon inputs derived from more fundamental intellectual virtues pertaining to commercial value estimates. For example, consider a person who retains a broker to sell some real estate. The broker will apply the intellectual virtue of appraisal to assess the worth of the property and make certain suggestions to the owner regarding a marketing strategy. The suggestions may carry moral overhead; they may be purposely biased to gain a quick commission, or to benefit a developer with whom the broker is in collusion. The stated appraisal may be a compound of an accurate appraisal in the mind of the broker that is deliberately misrepresented to the client. The positive fact is a poor appraisal, but the reality may be a sound appraisal combined with a lie committed for some personal gain.

Applying this to the issues under immediate consideration relates to the issue of whether economic laws actually do exist or not. The market is supposed to be a major reference point for value (price), but the market is the aggregated result of the individual appraisals of many people and those appraisals are the result of skill. Hence the pricing outcome of the market is the result of the action of the intellectual virtue of appraisal of a large number of people.

If the market is the result of the interplay of a large number of free and willing participants, each applying their intellectual virtue of appraisal, and appraisal follows identifiable principles, then the market will exhibit some degree of order. That order will depend on the degree to which appraisal is rational.

The rationality that underlies appraisal does not necessarily infer moral reason, ordered towards good as morally understood, but may be ordered towards goods materially considered consistent with the limitations of the intellectual virtue of appraisal. For example, a person may recognise the (use) value in an item offered for sale that is considerably above its asking price and be prepared to buy it, expecting to

be able to later sell it at a profit. The price offered will be no reflection of the purchaser's estimate of worth. The recognition of value may be accurate, and its exercise will benefit the material situation of that person, though the moral issues surrounding the transaction (possible exploitation) are not considered.

Because it may be expected that competent appraisal will result in consistent estimates of price, it must be accepted that the various principles of appraisal relate to objective economic relationships. These relationships, if they exist as consistent determinants, may be considered as laws, even though they will not always be evident to similar extents. Both the degree of skill held by the appraiser and additional moral considerations may moderate the operation of the law just as a safety net moderates the effect of the law of gravity as applied to falling bodies.

Of particular interest in this thesis is Ricardo's law of rent. This classical economic law was believed by Ricardo and his contemporaries to be a binding Newtonian determinant of value or price. The Enlightenment approach to natural laws was fundamentally problematic because of the contradiction between a notion of an unchanging form underlying a thing's nature that comes from the term itself (*law*), and the empiricist belief that such an unchanging form could not be known beyond an inductive inkling developed from particular observations. This meant that Enlightenment thought denied the possibility of abstracting to the level of essence and thereby lost any connection to essence. On the other hand Enlightenment thinkers sought deterministic laws of behaviour, hoping to use them to frame a science of human action and provide the foundation for social policy.

Care needs to be taken in assessing this endeavour. If there are concrete and identifiable principles of action that may be identified, especially in the practical exercise of intellectual virtues, then these could be profitably employed as considerations within larger moral debates. This is the methodology employed in this thesis. In exploring Ricardo's law of rent, it does not assert that such a law always has the power to effect a particular outcome, but merely that it represents a rational inter-relationship within commercial practice that may be used in further exploring moral implications. It implies neither a moral dimension to the law, nor Newtonian determinism.

3.5 REALIST EPISTEMOLOGY

Plato defined knowledge as *justified true belief*. Knowledge is a belief that must be true and certain. Many beliefs are short of this standard, however they may act as useful guides. Ptolemaic astronomy is a good example of a belief that was untrue, yet was still capable of yielding useful predictions. Sound scientific method does not rest with conclusions that merely yield useful predictions of future phenomena. This is

because scientific method recognises that mere predictive success may not be reliable and more importantly it does not accurately reflect the causal processes that give rise to the phenomena.

Aristotle recognised that abstraction proceeded from observation. Knowledge of the world begins with experience which is rendered intelligible. However, scientific knowledge is distinct from common knowledge in that "*...it is acquired and evolved systematically, although it must take its beginnings from ordinary experience*" (Wallace 1977), n.1.1 p.3]. In addition to experience, abstraction towards conceptual knowledge needs certain self-evident truths. Self-evident truths are those that may be known without observation and which may be proven to be true without need for external reference. The fundamentals of metaphysics and logic supply self-evident truths, metaphysics being the only science capable of proving its own premises and logic is fundamental for any ordered understanding.

While this claim of realist metaphysics has been criticised by many modern theorists, there does not seem to be a way of refuting it without leading to absurdity⁴². Despite this many have chosen this latter option, it would appear to be its own refutation. Support for the notion of self-evident truth is also appearing from within modern science. The linguist Noam Chomski has concluded that language is not wholly learned, as was the modern belief. He found it necessary to accept that an understanding of basic grammatical forms must precede experience. Given the close relationship between language and logic it would appear reasonable to extend this conclusion to basic logical relations as well.

Chomski's conclusion is insightful further because it recognises that even without formal understanding of grammar, people are able to use it. Their use is unconscious, though reasonably accurate. It would seem to be so with logic also. Without formal training in logic, most people, even the very young order their understandings quite rigorously by its rules. Likewise with metaphysics, people recognise that it is form that distinguishes a ball of wool from a woollen scarf even though they may not have learned what form means in philosophy; they also know that forms are constant and that balls of wool need knitters to add form to them in order to turn into scarfs. If pressed, few people would doubt that scarfs would be knitted if nobody wanted them. They do this even though they do not know what form is, or the other causes.

⁴²(Wittgenstein 1922) is one of the better respected modern philosophers who illustrated this inevitability when he ended his famous text with the conclusion: "*My propositions are elucidatory in this way: he who understands me finally recognises them as senseless, when he has climbed out through them, on them, over them. (He must so to speak throw away the ladder, after he has climbed upon it.) He must surmount these propositions; then he sees the world rightly. Whereof one cannot speak, thereof one must be silent*" , p. 189]

The self-evident truths that a person knows before observation are neither the whole set of self-evident truths nor are they necessarily consciously recognised as knowledge at all. For this reason they are often overlooked or played down. While this may have many practical advantages (it saves time not to dwell on self-evident knowledge), because these truths are fundamental to further understanding their omission from a detailed theory of knowledge is erroneous. This is one of the features that distinguishes a scientific approach from a common approach to knowledge.

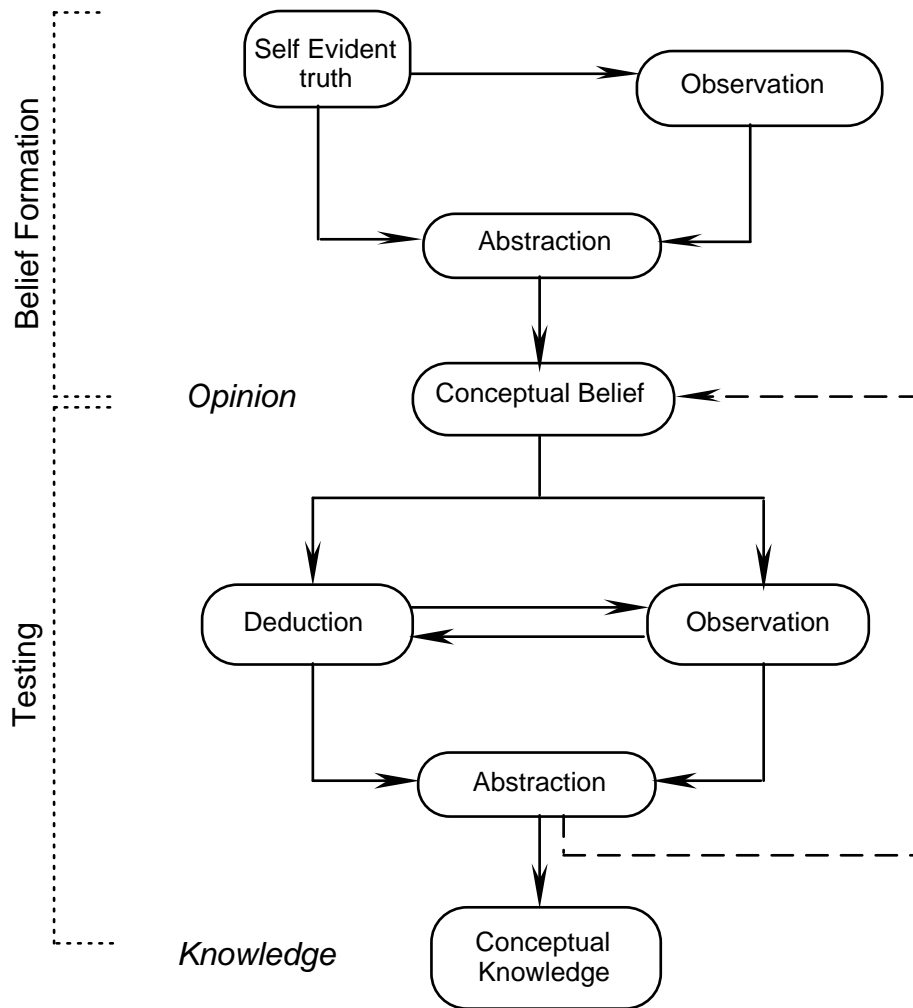
While some self-evident truth and some observation is sufficient as a starting point for knowledge, it is not necessarily reliable. The initial product, obtained by abstracting from the particulars of the observational experience to the formal level, is a belief about the world. Normally it is composed of terms and concepts that express the nature of the things under consideration and usually includes causal relations between things. The abstractions relate to natures, which, being unmoved by material circumstance, can be used to predict future events.

The initial abstractions should fit the initial observations, but through various limitations may be essentially inaccurate or imprecise. This does not mean that they will have no capacity to predict future events, because they have been built on a set of observations which proves limited predictive accuracy. However, their reliability will be limited. Despite being useful beliefs, they cannot be knowledge, because they are not true.

It may also be suggested that they are also not justified, on the basis of justification meaning testing. This is probably not strictly valid, as the initial observation may have provided some level of justification. It does however suggest the need for further testing or justification. Justification of beliefs involves logical analysis involving investigation of the way that the belief may involve inconsistencies, either with other knowledge, internally or against further observation. Observation alone will seldom provide definitive justification of a belief, unless it is of a type that makes it logically impossible for the belief not to be possible.

It is only when a belief can be shown to be incapable of not being true that it is genuinely knowledge. Knowledge does not warrant further testing, though it is wise to retain a lively understanding of the reasoning that led from opinion to knowledge. The process is outlined in Exhibit 4.3.

This model for gaining knowledge has the advantage that it discriminates between opinion and knowledge and locates observation within the process of gaining knowledge. A major distinction between empiricist and realist epistemology is the place of observation.

Exhibit 4.3 Realist Scientific Method**3.6 EMPIRICAL INVESTIGATION**

The initial observations pertaining to the issues in this thesis have been made already by many other observers and systematically recounted centuries ago. This thesis will review these observations and other information that either supports or contradicts the early interpretations in an effort to construct an explanation of the issues involved that integrates the data consistently.

This thesis will use as its data the previous arguments and conclusions pertaining to the topic, existing studies of cultural practices with respect to the social economy of land and two sets of primary observations. The first set of primary observations will be in the form of a survey of attitudes regarding demand and price and the second will be a behavioural experiment conducted in order to examine rental formation behaviour. It is considered that there is sufficient controversy regarding these two issues that

empirical testing is appropriate in order to clear the way for the construction of a consistent theory of the social economy of land.

3.6.1 Survey of Attitudes to Demand

One of the key issues in market theory is the benign belief that pricing by demand is socially acceptable and efficient. Land pricing is necessarily based on demand, as it has no cost of supply, hence the social economy of land is heavily influenced by the suitability of demand as a basis for price. It will be argued that its theoretical support is doubtful, its contribution to the common good is not reflected in much of the evidence and that its popularity is illusory.

It will be argued that the fact that the market dominates Western economics is not equivalent to saying it is embraced by the people who must use it. Moreover, the market may be moral under certain conditions. The acceptability of the market when it results in pricing by demand and not cost is the critical issue.

In order to test the actual acceptability of demand based pricing, an attitude survey will be undertaken and analysed. This is considered to be an effective way to study social attitudes to demand-based pricing. The thesis is modelled on an earlier study by Frey (1993).

While the thesis will not contribute directly to the moral argument, but will remove the positivist argument that market pricing is socially acceptable.

3.6.2 Experimental testing of Ricardo's theory of rent

An experimental observation of Ricardo's theory of rent will be attempted on the basis that this is the most appropriate way to examine its validity. While Ricardo's rent theory follows deductively from relatively uncontentious propositions regarding land and the economic process, its operation is often masked by a combination of practical issues including:

- Market imperfections, especially imperfect knowledge and restricted mobility.
- Decisions based on extra-market forces, such as personal location preferences.
- Competing non-land investment and production opportunities.
- Other rent-takers who are able to divert land rents directly or indirectly.
- Timing complications, such as pre-emptive speculative rent-taking distorting sales markets.

Normally experiments in economics are not possible due to the scale, time-frame, complexity and social impacts of the experimental manipulations necessary for meaningful study. However, the advances in the use of game theory and simulation in

economic research have suggested the use of game-like simulations that involve the same intellectual virtues appropriate real estate investment.

This thesis will use an educational game environment that has as its presenting purpose the observation of the dynamics of rental markets. The game will simulate the dynamics of a rental market in order to facilitate an experimental study of rental formation behaviour. The game environment naturally produces a laboratory in which the integrity of the game supports several goals of sound experimental design including:

- The game creates a simplified economy wherein extraneous variables may be contained.
- As an educational game, sanctions may be imposed paralleling those encountered in the real world.
- Interest and involvement are ensured by grading incentives.
- Experimental manipulation is encountered as part of the game
- Experimenter effects may be reduced through the perception that the exercise is a game, not an experiment, with a focus on winning, not impressing the experimenter.

3.7 CONCLUSION

The philosophical issues regarding methodology have been considered and have revealed the importance of an explicit metaphysical foundation for the thesis which is primarily within the umbrella of ethics.

Of the major available possibilities for a metaphysical system, Aristotelian Realism, sometimes referred to as *Classical Realism* has been selected after comparison with some competing approaches. The implications of realism, the position based on acceptance that objective reality pre-exists human perception and is knowable, have been considered and found reasonable, at least in comparison to the alternate systems investigated.

The relationship between the sciences has been examined, and land economics located as a practical science that is composed of both intellectual and moral virtues. The nature of laws for human action have been considered, and it has been found that they are different to laws governing other aspects of nature. The laws applicable to the workings of intellectual virtues have been differentiated from moral laws. Neither of these are considered to act as binding deterministic laws governing human behaviour. The existence of human will has been accepted.

A survey of several moral systems has been attempted and the Aristotelian realist moral position accepted. This is based on Aristotelian Realist metaphysics and admits rational formal as well as practical moral determination.

Observation has been located within the methodology and the use made of empirical components for this thesis have been discussed.

Chapter 4: An Economic Analysis of Cultural Variations in Land Tenure

The purpose of this chapter is to review and integrate various cultural practices in land. It is necessary to broaden the cultural perspective beyond that of the modern West in order to facilitate an unbiased consideration of the formal foundations of appropriate social relations with respect to land property. It will do this by focusing first on customary land title systems and then using these as a foundation for the review of historical cultures. Within this broad cultural perspective, modern Western practice in land property can be evaluated.

Organised political and legal actions have forced debate on the recognition and integration of customary title rights into the public discourse in several young countries in the last three decades. Indigenous people have confronted Westerners with an opposition that is growing in strength but expressed in terms that are now foreign to the Western commercial mind. The initial First World reaction was dismissive, however the confrontation has not diminished and Western land administrators are now trying to come to grips with the cultural and social significance of land to indigenous peoples.

This chapter explores the cultural fundamental of property in land via a dimension of the problem that is not commonly recognised, that of the practical significance of the land to the survival of indigenous people and the similarity between this relationship and that of the forebears of Western culture. Ancient Roman, Greek, Hebrew and German cultures are considered. The Islamic basis for private property is also reviewed. Medieval European feudalism is considered as a form of land administration and socio-economic structure and related to contemporary native attitudes. Several commonalities are observed, when the traditions of these cultures regarding land is reduced to modern economic terms.

The strength of the commonality evident in most non-modern cultures studied leads to the conclusion that these aspects of the social attitudes to land may constitute a cultural universal. The study concludes with discussion of the sociological implications of cultural universality, progress and socialism are considered as they apply to cultural practices in land property.

4.1 BACKGROUND

The current interest in customary title and the understanding of land by indigenous peoples suggests that these peoples have an understanding of land that is fundamentally different to Western culture and more primitive to it. Many indigenous groups share essentially similar understandings of the place of land in society, despite geographical isolation and widely varied mythological and social structures.

This commonality concerns the communal ownership of land, sometimes referred to by various terms, such as customary title or native title. It is expressed in varied ways by different peoples, but can be seen in virtually all indigenous cultures (Boyd 1995; Hall 1958).

Beyond this apparent similarity in customary title, there lies a broader cultural parallel that becomes apparent when the various types of customary title system are analysed using Western economic methods. In particular, analysis of the distribution of the material benefits derived from the land reveals a near universal sense of distributive justice that is foreign to the West.

By using a similar approach, a surprising similarity becomes evident between current customary title systems and historical European land systems, especially as both contrast to the modern Western system of land. This study seeks to consider the theoretical dynamics of the various systems to provide a comparison of the political economy of these three land systems, focusing on the broader social and economic outcomes in each.

Many Western people assume that native title is a regressive move occasioned by the successful political tactics of indigenous minorities, to the detriment of economic development and the population as a whole. Not only do these attitudes reflect an ignorance of the current facts, they also betray an ignorance of the history of the Western political economy of land.

4.2 THE ESSENTIALS OF INDIGENOUS TENURE

A survey of the relationships between various indigenous peoples and their land reveals that the relationship has typically two dimensions as shown in Exhibit 4.1. The first dimension is spiritual, or metaphysical, and the second is material, relating to the political economy of land.

The metaphysical understanding forms the rational basis for the material, but is not the focus of this investigation. Despite a great diversity of metaphysical interpretations of land and people, the political economy of land in native cultures displays a surprising convergence.

To understand the extent of this convergence, the notion of the material benefit accruing to the owner of land will be used as an analytic tool in the interpretation of the various systems. It is uncontentious that land is a factor of production, the quantity and quality of land affects the total production possible. Given a fixed amount of land for a given community, and assuming that significant portions are neither held out of use nor constrained to inappropriate uses, production will be a constant. Given a fixed product, the political economy of land concerns its impact on economic distribution, the allocation of portions of the generated wealth across the community. This is an old problem that has interested such classical theorists as William Petty, David Ricardo and others since the beginning of the modern era. It appears to have a peculiar resolution in the case of indigenous people.

For some indigenous peoples, such as those of Australia, North America and some African states, the tribe is considered to be the owner of the tract of land that it controls. The value of the land for producing the material needs of the tribe is freely available for any member who wishes to apply the labour necessary for the production required (Donigi 1994). For that person the land is free, there is no rent to pay for its use.

For these peoples the land is used by the tribe as a group, so there is negligible distinction between the quality of access available to various members of the group. Because the land is the common legacy of all members of the tribe, no individual may draw income purely from its use without personal labour, nor economically control land beyond that which is personally used. This arrangement combined with a simple set of material desires has enabled these peoples to be "... among the most leisured people on earth" (Robertson 1987, p102).

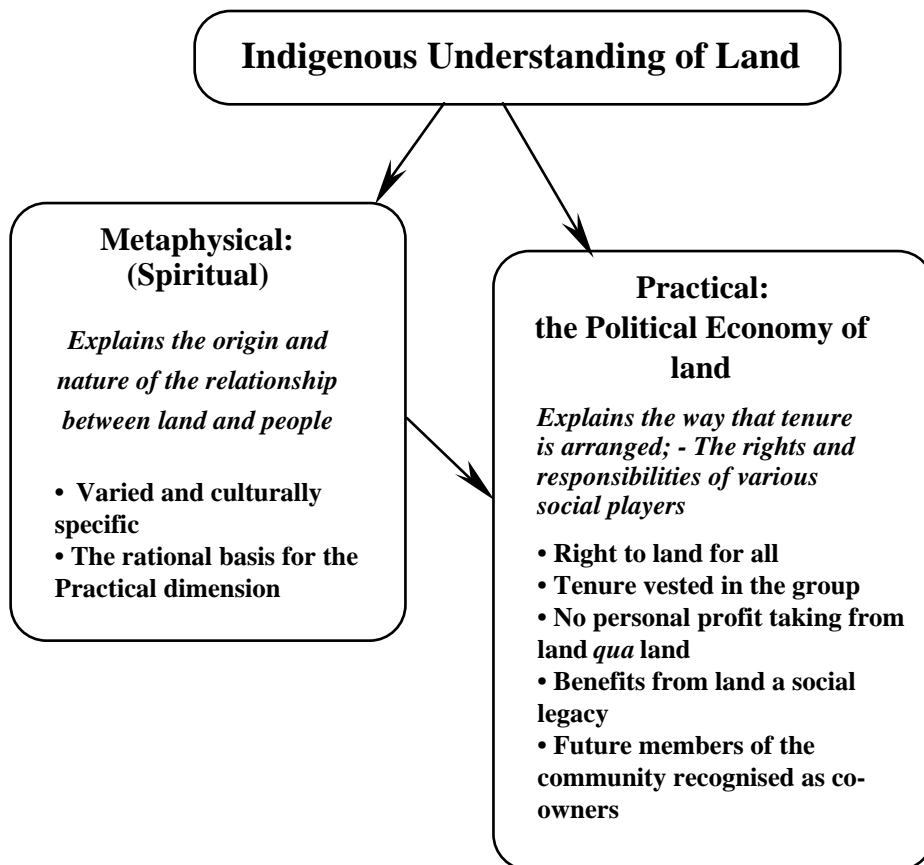
In some simple customary title situations, land is privately owned but it is more akin to a loan from the clan. In the eastern parts of the Torres Islands where population is dense and food is cultivated, there is some private ownership (Paterson 1889). Likewise, in the Cook Islands, land is privately allocated, however, it is recognised that despite the ability of some people to be able to assert that a piece of land is theirs, such title exists only as a particular participation in the tribe's land and with the tribe having the permanent reversionary interest (Crocombe 1964).

In the long term, a strong ethic of conservation insists that the land be preserved for future members of the tribe. These are regarded as having the same rights of access to the land as those tribe members currently alive. Children cannot be charged for access to the land of their parents for the same reasons. The land is free for the use of current tribe members, on condition that it be passed on without degradation to future members. This strong understanding of the totality of the tribe and the corporate

ownership by it of land is difficult for Westerners to appreciate, being undergirded by an alien metaphysical mythology.

To interpret this in modern terms, we could consider the implicit rental value of the land and its capital gain over time. These quantities are seldom realised in monetary terms, but rather in the more direct physical quantities derived from the goods gleaned from actual use the land. There is no reason why they cannot also extend into commercial monetary land uses, and such a prospect may offer a way forward in consideration of the integration of customary and Western land use.

Exhibit 4.1 Land Property in Customary Culture



The benefit from using land on a day by day basis, is its rent. An owner-occupier implicitly enjoys rent in terms of direct utility, while the tenant buys that utility by paying rent to the owner. In the case of customary use, the rent that comes from the use of the land is implicitly shared amongst the tribe. To the extent that the benefit is greater for those who exert themselves more, it is proportional to labour. To the extent that some in the tribe labour for rewards that are shared by members of the tribe who are not capable or suited to active land use, the rent is shared even amongst the non-

labouring members of the tribe. It is the basis for social distribution beyond direct labour.

Analysed in this way, the tribal situation can be further interpreted as drawing income from a combination of wages and rent, profit can be ignored. The tribes people who actively labour on the land produce the goods that the tribe needs. These can be divided into wages, as a fair and necessary return to those who labour, and rent, the excess that they may either enjoy themselves or share with their fellows. The classical notion of wages as subsistence income aids this division. While few tribes people would consider such a dissection, it is useful in considering tribal economic distribution.

In addition, the notion of the changing value of land, its capital gain, has an essential parallel in tribal societies that deserves reflection on exactly what capital gain is and between whom it is paid. To apply the concept of capital gain, it can be best considered in this situation as the inter-generational charge that one generation can make on the next for access to land. This definition has applications in Western analysis also, although our time-frames are not usually expressed in generational terms.

Any capital gain, say as a result of greater competition for land from increasing numbers, is vested in the tribe the following generation already has tenure by virtue of its status as apart of the tribe, in this case in the future members themselves. In this way the prohibition on charging future generations for access to land is totally consistent.

To put tribal collective ownership of land into Western terms, one could consider the land as the joint property of all the members of the tribe, past, present and future, with present members having only a leasehold interest, with their rental obligation equal to their income as joint owners and a commitment not to diminish the reversionary value during their tenancy. This interpretation requires only a relaxation of the Western understanding of owner as a person who is currently alive, but otherwise reduces customary title to a form that could be otherwise totally integrated into the Western system.

Obviously, in the case of joint tenants, no action can be legal that follows from the decision of a minority of the joint owners for their benefit at the expense of the others. So too with tribal collective tenure - a currently living member of the tribe cannot sell the tribe's land, even if the rewards are shared amongst the whole (living) tribe. Perhaps a leasehold interest could be sold, with rent shared by living tribe members, but this has the distinction of not alienating the land itself.

This joint-tenant/leasehold interpretation works well for hunter/gatherer peoples, but is not applicable to more complex societies, especially when there is a complex division of labour and land use. In Fiji, Tonga and Hawaii, for example, differential

access to land is necessary, due to the complex and developed land uses, and the allowance for foreigners to use the land. In these societies private tenancy is possible on what is effectively a leasehold basis. Often, title to the land is formally vested in the leader of the tribe or society on behalf of the collective, in structures that are recognisably feudal, even though they have little apparent connection with historical European feudalism.

This form is still essentially because the land is not owned by individuals, but rather by the society as a whole. Even though the leader may have nominal ownership, this ownership comes with obligations to the community that are so extensive that it is in fact a form of collective tenure. These are the most explicit examples of private ownership with common use that exist. They have been regarded as similar to the simpler system found in hunter/gathering cultures. An analysis of the distribution of the income derived from the land strengthens this similarity.

There can be no inter-generational capital gain because land is not owned individually. The future users of the land will have the same terms of access as present and past users. Population growth may limit the proportions of area available to each succeeding generation, but this is balanced by increasing productivity from technology and the increased value per unit area resulting from relative scarcity.

The question of rent is more complex. Rent is charged because land utilisation is not homogeneous across the society and may even be available to foreigners. At least theoretically, the charge of rent has the effect of removing that component of production that accrues to the land, leaving the land users a reasonable income for their contribution to the process (wages). This is not contentious.

The pool of rent in a feudal society flows to the public purse, in the person of the leader, chief or king. The rent amassed justly belongs to society and because the leader holds title on behalf of the society as a whole the attendant responsibilities mean that it flows back to the community. This mirrors the implicit processes found in the simpler societies that makes the benefit of the tribe's land available to all. Its distribution varies between societies; in Hawaii it funds education primarily and other public services for native Hawaiians, while in Fiji it is in the form of a direct dividend to native Fijians. The distribution of this common income is often through traditional social hierarchies that originated in leadership structures.

Within these two groups several variations exist, however the core issues remain. This is most significant. Despite various systems, ranging from simple tribal ownership (eg. Australia) to elaborate and identifiably feudal systems (eg. Tonga) several economic consequences recur, in places as varied as Fiji, Tonga, New Zealand,

Nigeria, North America and Paraguay (Boyd 1995; Caraman 1975; Crocombe 1964; Ezigbalike 1994; Hall 1958; Rakai 1995; Savae 1994).

These include the following:

- 1) Individuals may not control more land than they have immediate need for.
- 2) Individuals may not sell or alienate land to foreigners.
- 3) The land is considered to be a resource whose exploitation must serve equally present and future members of the community (tribe).
- 4) Individual profit taking from the control of land (ground rent) is unknown in any form, the surplus represented by ground rent is returned to the community, sometimes through the person of the chief.

These restrictions have secondary consequences, especially the reluctance to use land as security for debt and a perception that native land is not available for development. The first has attracted considerable attention because it challenges contemporary beliefs regarding finance and aid, the second is a fallacy that exposes some of the underlying characteristics of the development process.

Native people recognise that the use of land as debt security (collateral) exposes the people to the real possibility of loss through foreclosure (Ezigbalike 1994). Native people understand the land to be the possession of the tribe, including its future members, so to alienate the land is an injustice against some (most) of its owners and a betrayal of fundamental tribal beliefs (Poynton 1994). In modern terms, present owners may be looked on as holding a type of leasehold, where reversion is to the tribe's future members. Formalisation of leasehold relations is a strategy that is currently being explored to solve the collateral problem.

Development is not proscribed on native land. What is frustrating for developers is that the ground rent cannot be appropriated privately, and often it is the capital gain on the land, and not the net return of the development *qua* development that is the source of the super-normal profits so attractive to developers. The ground rent belongs to the community under native tenure systems, and there is ample evidence that indigenous people are not adverse to development, so long as the developer takes only the profit due to the development itself. Examples of this include the tourist facilities within Kakadoo in the Australian Northern Territory, and the vast tracts of developed land in Hawaii, both of which return ground rents that are distributed to the community, often in the form of community services, such as education.

The return accruing purely to the land, sometimes referred to tellingly as "the unearned increment" is a component of property profit that has become very important in Western property dealings over the past five centuries. Its private appropriation was

validated along with economic rent in general by Smith's "invisible hand" metaphor, a metaphysical assertion that is no less immaterial and suspect than the most primitive of native mythologies. Although it has now been in place for centuries, it is still only a historical novelty compared to the whole of Western history, secure neither theoretically, ethically nor historically. The event of native tenure agitation is forcing us to re-examine our own history.

4.3 SOCIAL AND ECONOMIC INEQUALITY

One of the criticisms of native societies is the level of inequality, even in small groups, and the apparent rigidity of social location. This inequality is often bolstered by preferential control of land. Native peoples typically accept the reality of inequality within a social group. Such an acceptance is also fundamental in modern societies, where thinkers such as Friedman assert "*Equality of outcome (economic status) is in clear conflict with liberty*" (Friedman 1980, P160). The difference is that the chiefs who command greater land in native cultures have clear and definite social responsibilities (Ezizbalike 1994) unlike those with wealth in modern societies, who are merely revered as more successful.

The importance of a nexus between social responsibility and income is lost to the modern liberal mind. The irony in the West is that despite the democratic election of representative leaders, there is apparently widespread suspicion of politicians. Political scientists often relate politicians' perceived poor quality and susceptibility to corruption to the fact that they are not adequately remunerated. Without losing sight of the historical instances of corrupt monarches, one can wonder whether the elimination of monarches has effected any real improvement in leadership quality, or the respect of leadership by the people.

To understand the native position, a sensitivity to the role of the chief and the structure of native societies is necessary. Native societies are typically smaller than modern states, resulting in simpler social structures. This brings the chief closer to the people and reduces the number of social strata. Within a simplified social hierarchy, less economic stratification is necessary.

The difference in labour and remuneration between the chief and others in the tribe is therefore more apparent, but this inequality should be placed in context. In Australia, the contrast between rich and poor is a statistic that is relatively hidden, despite its obvious social importance. Raskall analysed probate data to generate a wealth distribution for Australia (Raskall 1986). He found that the most wealthy one percent of the country owned 138 times more than the average wealth of the entire lower 50%. It seems doubtful that tribal chiefs typically maintain this level of wealth disparity, or if they do, its significance is somewhat less objectionable.

Whereas wealthy Australians have no specific civic responsibility, the purpose of economic privilege for leaders in native societies has three functions. It releases the leaders from the burden of labour to concentrate on the task of governance, it provides funds for certain activities of government and it rewards the director of the community for the importance of the task. This is analogous to the West, where taxation funds a specialist public service and the activities of government, while higher remuneration of senior management for directors in all sectors is recognised as a necessary element in achieving optimum organisational performance.

Oliveira has argued that a social hierarchy is a social necessity, which has not been eliminated in modern liberal times, but transformed into an alternate set of social leaders who do not necessarily share the same long term interest in the direction of society found in '*primitive*' leaders (Oliveira 1993). The Western elite are no longer the visible social and political leaders, but an increasingly invisible social strata who rely on commercial power for their position. Several commentators on the history of economics have noted that this trend has dominated the modern era, with commercial success being used to secure political and even theoretical support for itself, starting with the English mercantilists who succeeded in swaying English foreign policy and protection in their favour (Roll, 1942).

A native person could well ask a modern why their political leaders are not rewarded adequately, and why they choose such poor quality law makers. The modern could hardly reply that it represented progress. A nexus between wealth and civic responsibility would appear to be a worthwhile social goal that native cultures are more likely to maintain than their modern critics.

4.4 ACCESS TO LAND IN VARIOUS SOCIETIES

The common, tribal, or feudal systems found in customary tenure systems do not necessarily mean that all members of a native social group will use the land, or use it equally. The common ownership does mean that future members of the group will have equal access with their fellows at any given time and that the tribal lands will not diminish. They correctly recognise that the land is the basis for all human activity and that its alienation creates a vulnerability for the entire group.

Modern systems provide the opportunity for access to land to those who have the economic resources at any given time to afford it. However, the realities are that often younger generations are not able to afford land adjacent their parents. This is illustrated in both urban markets such as Sydney, where younger land buyers are continually forced further and further from the city centre, and rural markets, such as Ballina, on the NSW north coast where superannuees are raising land prices and forcing younger local people out of their own town.

In each case, the probability of family groups being able to remain in physical proximity has been compromised. Indigenous people recognise that the quality of a tribe's land is an asset that belongs to the children as much as the parents. This has been lost to the West, though it appears implicit within of Marx's concept of alienation. While his alienation is usually considered in terms of the separation of the product from the producer, his earlier writings stressed also the separation of the producer, as a family, from a connection with the land. His examples in *Kapital* included farmers who accepted high sale prices for their farms, only to be later impoverished as tenant labourers (Marx).

4.5 ANCIENT WESTERN LAND TENURE SYSTEMS

4.5.1 Greeks

Both the Roman and Greek cultures rose to prominence while utilising communal land tenure based on family title to land. In this way they were similar to many current tribal peoples. The Greeks were the first to move towards concentration of land ownership resulting in the emergence of a wealthy landed class who used their land wealth to enable them to exercise political rule. Between about 800 - 650 BC this group, the aristocrats, from the Greek *aristoi*, (best people) dominated the rule of the Greek states under oligarchy (Peach and Millard 1997).

The early Greek culture was organised around families. Membership was by blood relations and meant both the expectation to conscientiously contribute to the labour of the family and a share in the family's material wealth. Within this system, labour was not differentiated and material resources, land, were owned by the family, not by the individuals within it (Glotz, 1926).

Private ownership in Greece followed the formation of the cities and was at first a strategy for enabling individuals to serve the commune that was the city (Kamenka and Neale 1975). By allowing individuals to privately own property and slaves, it was believed that they would be able to contribute to civic life. The introduction of private land produced a dual system of land tenure, with traditional family owned properties and private individual tenures as well.

Young Greeks were especially attracted to personal property in land as a means of avoiding the responsibility to support their families out of their work, and despite originally being introduced for the purpose of civic involvement, it soon become a vehicle for personal wealth concentration. Trade in land and the use of slaves on a larger scale developed. The transition from a family centred use of land income, coupled with expectations of using land based income for civic and sometimes military

purposes paralleled a shift in the general Greek ethic from the community to the individual. The result was the progressive delineation of land and its subdivision. Over time considerable disparities developed in the amount of land held by individuals (Glottz 1926).

Despite the privatisation of land property, it was never treated as capital, in the modern sense, and the only references to increasing value related to the investment of labour. Athens did not keep any formal records of land and it was not used as security for debt (Finley 1973).

4.5.2 Romans

A similar pattern was evident in the development of Roman land tenure. During the early republic land was owned by families or tribes. Land ownership carried with it social responsibilities, the most onerous of these was military service. As Romans, property owning families understood that they were obligated to supply men and equipment for military service. In the early part of the empire, this would often entail only short intermittent periods of military service. The army at that stage neither equipped its men or paid wages, these came entirely from the soldier's resources, which was related to their land property (Marks and Tingay 1996).

As the empire matured a series of changes which dismantled this connection between Roman loyalty, land property and military service. Wages were introduced around 340 BC to expand the size of the army and make it possible for soldiers to be away from their homes for longer. Due to the long absences during distant campaigns, soldiers' farms fell into disuse and were progressively absorbed into the estates of a rising upper class. Returning soldiers would often find that their land holdings had evaporated in their absence (Toutain 1938). Although the government granted soldiers small farming plots after 20-25 years service, this was nowhere near equivalent to the losses many small land-owning Romans suffered that forced them into either unemployment or permanent full-time military service.

Towards the end of the empire, the size of the large estates continued to expand along with the influence of their owners. The Roman army became a professional class and eventually largely composed of mercenaries. The Roman Emperor was the largest landowner and out of his land resources it was expected that he would finance the military, however this responsibility was progressively shifted onto his subjects (Finley 1973). Whereas in the early empire the Romans left land titles relatively untouched, towards the end of the empire they were more active in exploiting provincial land, largely for private profit. In the provinces, as far as Britain, there is evidence of large estates that were worked by tenants (Coulanges 1890/1927). The Romans transported

slaves to work on distant estates as a way of controlling them and providing cheap labour.

Both the Romans and the Greeks made the transition to private land holding later in their rise to prominence and while it may be asserted that this represented a form of progress, such a conclusion is premature. In both cases. Private property in land developed out of earlier collective, family-centred titles that carried considerable socially orientated responsibilities and ended in self-interested relationships using property not unlike modern capitalist freehold. This transition was the conversion of the notion of property from a vehicle for social service to a tool for self-interest.

While it is true that both of these great powers evolved freehold private property in land, it is also true that each faded as a great power, so a correlation could even be made between the transition to private freehold and cultural demise. It would seem unlikely that freehold could have such a devastating causal impact on these ancient cultures, but perhaps there could exist a third social factor that exercised a causal effect on both. Such an argument is not unrealistic, especially when a possible common cause, such as the transition from a community centred ethic to one of self-interest, is considered. The rise of a culture is partly a function of its cohesion: a community that operates as an integrated unit will be more successful than one that is disparate. This is illustrated in team sports today, just as it was the key to the military superiority of the cultures under consideration.

Communal ownership of land, and the communal distribution of “the unearned increment” is a reflection of an integrated and cohesive society. The transition to self-interest and individualism cannot but result in a reduction in community integration. The ethic of individualism and immediacy that most probably preceded the transition to individual freehold, is also seen in the later lack of cultural vigour that spelt the end of the Roman Empire.

4.5.3 Ancient Germans

At about the time of the Roman empire and later, the Germanic tribes in the north of Europe also operated under forms of communal land tenure where the tribe was considered to be the owner of the land. While these tribes had elaborate social systems, private land ownership was unknown. Since private ownership of land was unknown, land was instead held by the family, which eventually grew into clans of fifty to one hundred families. Blood relations defined membership and the head of the family had considerable responsibility and authority. Property was understood to be the result of toil and was built up as families progressively cleared and developed the land available

to them. Land was basically available in abundance, but it had to be cleared. When numbers in a particular settlement grew beyond what could be supported from the available land, the family would be divided and part would move into new territory (Ross, 1883).

One of the confusions in the literature on the origin of property, regards the question of whether the ancients enjoyed communistic or individualistic title to land. Coulanges (1890/1927) was animated by the desire to demonstrate that communistic title never existed. However, he cited the ancient Germans as examples of individual title. Given the influence of the family head and the identification of individuals with their families, this may have been understandable, but despite explicitly recognising that these titles were family based, Coulanges counted them as individual. Ross (1883) covered the same material and noted that there were numerous references to the rights of individuals in land, but correctly recognised that these rights were always held in common. Ross always noted that the Germans did not have community rights to land. This is a very important distinction, because although it upholds Coulanges' contention against communism, it does not at all indicate private property in land of the modern sort⁴³.

The Germanic tribes used land in much the same way as the simple tribal ownership practiced by many contemporary indigenous peoples.

With the atrophy of Rome, the Germanic tribes increased in importance. Clans grew and become larger political groupings. Status became associated with the control of land, but in order to hold land it was necessary to be able to defend it. The result was the genesis of European feudalism (Reinhardt 1962).

3.4.5.4 Hebrews

One of the cultures that has influenced Western legal thinking originated not in Europe itself, but in the Middle East. The Hebrews held elaborate beliefs regarding the treatment of land on the basis of communications between their prophets and God, recorded in the book of Leviticus and elsewhere. Their system is summed up in the following passage:

"The land shall not be sold in perpetuity, for the land is mine (God's); with me you are but aliens and tenants." (Lev. 25:23)

This establishes the notion of tenancy, based on a metaphysical understanding of the origin of the land and suggests what we would understand as leasehold. Although it is

⁴³The debate regarding land tenure and property in general around the end of the nineteenth century was no doubt animated by the challenge from Marx and Proudon and has provided some valuable insights into culture and land.

considered as leasehold for individuals, it is the permanent possession of the families or tribes as suggested in Genesis 48:4 “... I (God) will make of you a company of peoples, and will give this land to your offspring after you for a perpetual holding.” More over, land could not be alienated for more than fifty years under Mosaic law, under the notion of the Fifty Year Jubilee wherein:

In this year of jubilee you shall return, every one of you, to your property. When you make a sale to your neighbour or buy from your neighbour, you shall not cheat one another. When you buy from your neighbour, you shall pay only for the number of years since the jubilee; the seller shall charge you only for the remaining crop years. If the years are more, you shall increase the price, and if the years are fewer, you shall diminish the price; for it is a certain number of harvests that are being sold to you. (Lev. 25:13-16)

This is possibly the first reference to leasehold and reversion in history. It clearly indicates the intention for the land to remain the property of the family or tribe. It is a curious bridge between individual and communal land tenure because it allows for private use and even a form of alienation, without disinheriting future members of the tribe.

In terms of the ‘unearned increment’, clearly in the long term this would remain with the traditional owners in the Mosaic system. This example illustrates the subtle and complex understanding of land evident in ancient peoples. Despite its apparent allowance for individual ownership, it has in fact more in common with current customary tenure. Although the actual enactment of the jubilee system is not recorded, neither is any rebuttal of the system and the text has remained as part of the central lore of that ancient people.

4.5.6 Islam

The Qur’an outlines a simpler approach to land tenure based on a similar understanding of the relation between God and humanity. Nomani explained that “Islam’s concept of property is based on God’s absolute, natural and divine right of possession in relation to all that is on earth” who has “...made man His viceregent and entrusted him with his possessions on earth” (Nomani and Rahnema 1994).

Limits exist on the extent of private property. Islam recognises private property as a type of loan from God, and consequently limited by a person’s allegiance to the Shari`a, being an expression of God’s will. Some things are to be held in common and never to be privatised, these include water, fire and pastures (Nomani and Rahnema 1994, p.67). This apparent reversal of the rights of private property in land is resolved

by “Islamic jurists and economists (who) agree that property gained has to be the fruit of one’s labour” (Nomani and Rahnema 1994, p.71)

While there appears to be some debate as to the actual mechanism to allow common ownership of ‘pastures’ to co-exist with a private title to the products of labour (development) on that land, the essence is now familiar. In modern Western terms it would appear that the intention is for the ground rent to be communal, while the income from improvements remains private. This suggests a leasehold relationship between user of the land and the community, though other models are possible.

There is current debate within Islamic scholarly circles as to the balance of these rights with some arguing that labour applied to land gives one absolute title, resulting in a land title that is effectively totally private, similar to the modern West. The result is a traditional theological base, that leads to fairly clear implications, being overtaken by an interpretation that would clearly have benefits for those in control of land. This tension is also evident in the Western experience.

4.6 EUROPEAN MEDIEVAL FEUDAL TENURE

The private land holdings of the Romans eventually gave way to the early Feudal system, as individual land owners traded freehold tenure for military security. The lords accepted title to land in return for the promise to maintain an army to repel invaders. Land owners became tenants who paid rent to the lords who maintained an army. Rent was paid in various forms, seldom as money, but more often as produce, labour and in time of need, military service. This can be interpreted in modern terms as ground rent being used to fund security and defence.

As feudalism matured, the lords provided domestic law and order, and a degree of public infrastructure, still funded primarily from rent. The popular image of feudalism, with despotic lords exploiting semi-slave tenants is largely the product of political disinformation during the sixteenth century. Richard Green (1837-1883) in speaking of the reign of Elizabeth I as, “*It was an age of political lying; but in the profusion and recklessness of her lies Elizabeth stood without peer in Christendom*” (Stenhouse 1996).

Both Elizabeth and her father had much to gain from denigrating the integrity of the political economy that was in place at the beginning of Henry’s reign and they were schooled in the statesmanship which Machiavelli both observed and counselled “*...experience in our time shows that those princes have done great things who have valued their promises little, and who have understood how to addle the brains of men with trickery*” (Machiavelli 1989, p.64). The misrepresentation of the time was cemented by the coloured but popular English history of David Hume. That history has

greatly influenced the common beliefs about that period right down to the present time, despite the factual discrepancies revealed by such historians as Lingard, Cobbett, Chesterton and Belloc among others (Belloc 1937/1973; Chesterton 1917; Cobbett 1824/1988; Green 1874; Lingard 1883).

A second occurrence came with the maturation of feudalism - exceptions were granted that consisted of land without obligation, something closer to freehold. These were granted to the Church and to individuals, with significant but very different outcomes.

Monasteries became significant land owners as the result of three processes. The first was the irony that when men retired to the wilderness to devote themselves to their spirituality, their material needs necessitated the clearing of the wilderness. This resulted in remote and unwanted land eventually becoming productive farm land. This was especially the case when human settlement was relatively sparse, as it was in those times.

The second source of land was by gift from lords and kings in gratitude or in order to promote the work of the monastics. The third, which developed later, was a strategy for retaining family control over land, a form of tax evasion. Whatever the source, the outcome meant that religious communities eventually controlled significant amounts of land, from which they obtained rents.

While the popular understanding of land-rich monasteries is one of corrupt and worldly abbots, the realities were not so clear cut. Like all institutions populated by humans, there was no doubt some degree of corruption, but in general the monasteries used a significant part of their income to provide services such as hospitals, help for the poor and education. The charge of self-indulgence on the part of the monks, could only be made by persons totally unaware of the facts and ignorant of the whole ethic of monastic life. It remains as a popular myth, first invented by Henry VIII as justification for the plunder of monastic lands.

To illustrate its departure from fact, one of the less publicised outcomes of Henry VIII's sacking of the monasteries in the mid-sixteenth century was the near collapse of the universities, as a result of the destruction of the educational infrastructure that had previously provided them with students. The fall of the monasteries meant the fall of the national educational infrastructure, all funded out of land rent. Cobbett notes other community costs resulting from the destruction of the monasteries (Cobbett 1824/1988).

There was one other characteristic of Medieval feudalism that is critical in understanding the political economy of land in that system, this is the provision of the Commons. The Commons were tracts of land available to all and which were capable

of providing a livelihood for those who did not have other income sources. They ensured that no one was alienated from the land and provided a form of natural unemployment relief.

This worked reasonably well, however it was undermined by the granting of freehold tenure to vassals in what were known as 'immunities'. These were usually large land holdings, and the beneficiaries gained private control of entire communities. Because the flow of rent no longer went to the public purse, alternate funding was required and a variety of taxes were introduced. This privatisation included the privatisation of the Commons. The expansion of arbitrary taxes in turn produced the pressure for the English Magna Charta, which had the curious quality of being intended primarily to protect the land barons from the taxes that their privileged land holdings had themselves produced. It was a spiralling process that eventually resulted in the dismantling of feudalism.

This process, though started in the thirteenth century and accelerated in the sixteenth, continued in England up until the last century. The beneficiaries of the Enclosures came to hold power in the English parliament and dominated political economy for the centuries following, writing theory to suit their privileged position (Roll 1942). This has further compromised modern understanding of the economic system that preceded it in the English tradition.

The significance for the present study is that in essence, medieval feudalism provided government functions, defence, law and order, infrastructure, education, health and welfare predominantly out of land rent. In this way the land was a source of funds for the community, not for individuals. The perception of lords as privately benefiting from oppression through land ignores the responsibilities that they also took *qua* lords in a manner analogous to the role of chiefs in current native tenure situations. Individuals could not profit from land which behaved as a perpetual community resource.

Medieval Feudalism illustrates another way that even given apparent personal control of land, the benefits of the land *qua* land were distributed across the community.

4.7 OTHER FEUDAL STYLE SYSTEMS

The Qur'an strongly holds that all land belongs to God and it is made available only for private use through toil. This found various application within the Ottoman Empire. In Iraq, the land was tribally owned, which ensured that tribesmen earned the full benefit of their labours. More recently the practice was replaced with the transfer of legal title to the sheikhs which has left the tribesman as a share-cropping fellahin with

no land rights (Warriner 1962). Elsewhere there developed a feudal system almost identical to Europe, though based on Islamic principles (McGrew 1985). The early Ottoman empire located title to all land with the sultan, who granted it on life tenure to individuals for specific purposes.

Fiefs known as *timars* were granted to cavalymen on very similar conditions to Western vassals. Peasants (*rayahs*) had rights to occupation, and also obligations to pay taxes, that were land based. Similar to the West, land was also dedicated to religious purposes through *wakf* that supported mosques, schools and other works related to religious duty. Amongst these titles, there was also private title, *mira*, though this was sanctioned neither by law or the Qur'an. Despite its persistence, it was not secure and in the sixteenth century was formally dissolved, although even this did not wipe it out.

In Japan, variations on feudalism have existed from the earliest Japanese history when the Japanese kings adopted the Chinese doctrine, "*Under the heavens there is no land which is not the king's land; among the holders of land there is none who is not the king's vassal*" (Hewes 1955, p.21). The distribution of power changed through time between the king/emperor and the major landholders, the *shoguns*, who were military lords who in theory were subject to the king, but in practice often held the greater power. In 645AD the Taikwa Reform attempted to centralise power and administration with the Imperial clan. This established the systems of taxation and land tenure. Over time gave way to what was known as the Estate system which paralleled English history leading up to the Magna Charta.

By the fourteenth century feudal lords had consolidated much of the fragmented older structure into new concentrations of wealth and power. The Meiji Restoration of 1868 attempted a redistribution of land title in favour of tenants and in order to come to grips with the Western practices, however it tended to continue the power of the land-owning group (Dore 1959; Sansom 1962; Waswo 1977). This attempted to redistribute title to the peasants and establish a uniform system of land tax. Less than a century later land ownership had once again concentrated necessitating the post war redistribution by MacArthur (Manchester 1979). Despite MacArthur achieving a 98% return of title to the occupiers of land, it appears to have been again re-concentrated to a large extent, at least in the valuable urban markets.

Other examples of feudalism are widespread. European feudalism is believed to have originated from the Germanic tribes, however disparate Asian and Pacific countries have been found to have identifiably feudal tenure systems, such as India (Campbell 1881; Coulanges 1890/1927), China and Tonga. The ancient Egyptians had a tenure system similar in some key respects to feudalism. The control of land and the right to

rent for public funding vested in the Pharaoh even though land title was family based and more like individual title.

Exhibit 4.2 Summary of Cultures

Summary of cultures studied	
<i>Freehold title</i>	<i>Collective title</i>
Modern western Late Greek Late Roman	Australia New Zealand North America Nigeria Paraguay Early Greeks Early Romans Ancient Germans Ancient Hebrews Ancient Egyptians Hawaii Tonga Fiji Medieval Feudalism Pre-industrial Japan
	Explicit Tribal ownership Ownership by leader on behalf of collective
Land income privately taken Land changes hands, may be aggregated beyond individual needs Future citizens must pay for land at market rates	Land income remains with collective Title resides with the collective perpetually Private title leasehold, related to use needs Future members ensured access to land
<i>Emphasis on the individual</i>	<i>Emphasis on the community</i>

4.8 FREEHOLD VERSUS COLLECTIVE TENURES

The various approaches to land tenure are summarised in Exhibit 4.2. With the exception of modern Western and late Greek and Roman cultures, in every case considered, both contemporary and historic, the relationship between society and land has contained key commonalities. These include:

- 1) The retention of ownership by the collective, sometimes personified by the feudal lord or tribal chief.

- 2) The distribution, in some way, of the profits from land, the rent, as a public benefit, often as a funding source for community services.
- 3) The common provision for personal allocation of title as a function of labour input and resembling a leasehold with reversion to the community.
- 4) The absence of personal profit from land *qua* land either as rent or as capital gain.

These characteristics reduce to the following fundamental issues which are often evident regarding property:

- Land property is recognised as not the natural property of individuals.
- Where land is owned by a person (feudal lord) that person owns the property under the obligation of the benefits from the use of the land remaining common through the application of rents, in whatever form, to various social ends.
- Personal property in one's labour is respected as licit and often generates title to land that is limited to the fruits of a person's labour.
- Title and use of land tends to follow from a causal explanation of its origin, often as the work of a deity.
- Membership of the tribe or clan is sufficient for the right to a sufficient share in the group's material resources and product.

4.9 SOCIALISM?

A possible observation at this point is to note a superficial similarity with socialism, however this is erroneous. The study to this point has been empirical/historical and not theoretical; socialist theory is usually the reverse. Those acquainted with the work of Marx and Engels would be aware that they used a theoretical framework to influence future action. Most curious in this respect is their only attempt at locating their theory in history, Engels' *'The Origin of the Family, Private Property, and the State'* (1845) which consisted of no more than a speculative myth masquerading as an historical description of the first pre-historic communities (Tong 1992). Observations can be no more than observations, working them into a theoretical framework is a separate project.

Had any of the tenure systems discussed so far contained support for socialist theory, the major socialist theorists would have appropriated them long ago. As it is, the avoidance by socialist theorists of an analysis of collective land tenure systems is itself a telling indication that they do not support socialist theory.

In repelling land socialism (Coulanges 1890/1927), a contemporary of Marx, argued against the Rousellian belief in an original state of communism in land, however, his attack failed to discriminate between clan title and private title. While his point can be

accepted that there was never a historical point where developed societies failed to recognise systems of land property, this does not infer private title. Coulanges' examples very evidently combine family title with private title and this would include collective tribal property rights. The fact that tribes recognised boundaries to their lands and were prepared to fight for them certainly indicates something other than communism, but it does not deal with the vast difference between a tribal notion of property and a modern Western individual one.

There is also a technical difference between socialism and the collective land tenure systems considered. This is the distinction between land ownership and the ownership of other non-labour factors of production. Socialist theory sees no distinction between non-labour assets, which include land, tools, buildings and money, and seeks to socialise them all.

This would necessarily include socialising the labour content of produced capital assets (tools, buildings, machines, etc.), that has been repeatedly observed to have been the basis for, and limit to, private property in the tenure systems considered. A native person, or an ancient Roman, Greek, German, Hebrew, Moslem or Medieval European would find the community appropriation of a person's labour repugnant and unjust, but the non-land tools of production are precisely this, the fruit of labour.

Capitalism can work quite unaffectedly within the non-Western tenure systems described, and some have even suggested that the privatisation of land income has worked powerfully against pure capitalism, especially in the nineteenth century (Harrison 1983).

Within the capitalist tradition there has been an attempt to revert to a system of public funding using land rents. The Physiocrat economists recognised the suitability of land rent as a taxation base that could be publicly appropriated without affecting production and commerce. Adam Smith, in his treatment of taxation and rent, falls just short of a similar conclusion in the *Wealth of Nations*. David Ricardo gave further theoretical support to the notion with his *Law of Rent* (referred to in this thesis as Ricardo's rent theory) and John Stuart Mill suggested an elaborate strategy for the eventual resumption of land, which would leave private rights to the exclusive use and control of land intact, but the return of ground rent to the state.

This strand of political economy perhaps reached its climax in the single tax movement of Henry George. George developed his theory largely from the observation of trends in the USA (George 1879/1987). The single tax referred to land tax and was the conclusion of his entire theory of political economy. George used the political sphere to promote his position, but encountered massive, and understandable, opposition from landowners which eventually undermined his political aspirations.

George visited Australia at the height of his fame leaving the local government rating system of NSW and the leasehold system of tenure in the Australian Capital Territory as an implementation of his theories (Brennan 1971).

His theoretical structure also came under widespread attack, including an apparent, though unnamed, condemnation by the pope (Leo XIII 1891). Gaffney outlined the way that American economics has developed in this century partly as a systematic demolition of George's political economy (Gaffney and Harrison 1994). Although this opinion appears to be rather paranoid on the part of the single tax movement, especially as Georgist theory is now relatively insignificant and unknown, it does correspond to some developments in economic theory. A century ago land was recognised as a distinct factor of production, today it is lost amongst capital, leaving only two factors. More fundamentally, George argued on the basis of justice which Marshall excised from the science when he successfully created economics as a moral-free derivative of political economy (Marshall 1920/1938).

More recently Day has illustrated the benefits of a Georgist approach, drawn largely from his experience as a senior town planner (Day 1995). When this is combined with the various instances where land tax and state leasehold have been successful, it must be admitted that despite its unpopularity, there does exist a line of thought in the modern West that is sympathetic to the community appropriation of ground rent. Hence, this line of theory is fundamentally aligned with the economic fundamentals of customary title.

Also within the context of Western economic culture, Tollemache (1913) argued for what he called the "*occupying ownership of land*" suggesting that property in land be limited to owner-occupiers. Without exploring the rationale for his suggestion, it can be easily seen that it was partially motivated by a suspicion of the merits of allowing absentee landlords, which is a key component of capital accumulation in land. Land would hardly be socialised if it was only permitted to be held on the basis of occupation, but it would prevent the concentration of wealth that is a common outcome of Western capitalist practice.

4.10 SOCIOLOGICAL INTERPRETATION

A more fruitful direction for explanation is to subject the political economy of the tenure systems to sociological theory. Two sociological theoretical constructs suggest themselves, the notions of *progress* and of *the cultural universal*. (Robertson 1987)

4.10.1 Progress

It is tempting to lump the tenure systems considered together as *primitive*, and in contrast to the *advanced* tenure of the modern West. This is especially attractive when

one can also correlate the modern Western system with the latter Greek and Roman practices to form two dichotomous sets, one primitive and the other advanced. This practice of interpreting current non-Western anthropological data as indicative of, and aligned with, ancient social practice belonging to an inferior level of social evolution, is the sociological principal of *progress*.

The principle of progress is a sociological developmental theory that flourished in the nineteenth century as a way of validating much of the intellectual arrogance of the Enlightenment. By positing human culture as a progression from ignorance to Enlightenment, thinkers were able to assert that the most recent thought was necessarily superior to anything antecedent.

To an extent the notion of progress can be validly seen in certain human domains, especially the natural sciences and mathematics. Each generation has the scientific learning of those before as the foundation for further research and development. However, its sociological application, being primarily to the moral sciences, is unreliable and theoretically dubious.

The nineteenth century saw the notion of progress used to produce Herbert Spencer's notion of social evolution, from which biologists borrowed key concepts (Newby 1983, p.70). It was to validate social evolution that the work of Darwin was first embraced, as the former was recognised to have serious conceptual, philosophical and scientific flaws and needed empirical support. Social evolution was used to stitch together observations of living nineteenth century peoples into a suggested historical progression.

Among other things, it validated the oppression of indigenous peoples that had been practiced by European colonists for centuries. The thin veneer of charity by European occupation of foreign cultures, supposedly in order to bring them up to Western Enlightenment, hid the massive exploitation that was the real dynamic of colonisation. This practice validated black slavery, the oppression of India and extended into the second half of the twentieth century with the exploitation of Middle Eastern oil.

The nineteenth century theorists found that nature had apparently been so courteous as to have left examples of every age of man culturally frozen in time for the moderns to interpret as history (Block 1978). The belief in progress afforded considerable stimulus to the study of anthropology that began at that time. To some extent we are still heavily influenced by these novelties of the nineteenth century.

Unfortunately, the sociological principle of progress does not sit well with the activities of Stalin and Hitler, nor does it find support in the fall of the Roman, Chinese or Indian cultures. Many would argue that modern Western culture is not an example of social/moral progress but at the edge of decay. At the other end of history, the assertion

that human thought has followed a monotonic ascent over the course of history does not explain the intellect of Aristotle, the poetry of Homer, or the subtlety of ancient Hebrew legal thought. This led Teggart to observe:

“The difficulties which the humanist must meet at the present time arise from his acceptance of the idea of progress as the directive concept in the study of man” (Teggart 1941/1977, p.214)

For these reasons and others, it is no longer uncritically accepted in the social domain - progress being described by Bierstedt as *‘hardly even an idea and belief in progress is a matter of optimism rather than fact’* (Block 1978) Despite this, it is still often used implicitly in the evaluation of issues such as indigenous people’s relationship to land. The concept of progress is more correctly identified as an ideological tool for the subversion of earlier, or alien, thought. For this reason, it is not appropriate to consider customary land holding systems as primitive, but rather as only different.

This does not infer equality - comparison between the modern and native systems may be found to differ qualitatively - but it does remove a pejorative which would otherwise impede an unbiased comparison. With the pejorative inequality removed, the merits or otherwise, of customary land systems can be more reasonably assessed and the comparable virtues of the modern system better understood.

4.10.2 Cultural Universals

Modern philosophy generally has excluded the notion of universals from its metaphysics. This has proven to be a massive difficulty, because universals must logically exist. Sociology, largely built on the modern Western philosophical tradition, has empirically observed certain human behaviours and beliefs that are not culturally relative.

Every culture has an understanding of music for example. Even though one culture’s music may be another’s cacophony, the fact that *‘music’* is a comprehensible human artefact in every culture means that it is culturally universal.

Sociologists take interest in testing other aspects of social behaviour for universality. Honesty is an example in the ethical realm. While most cultures practice some level of dishonesty, they all have an understanding of what honesty means, and a preference to be told the truth, even if they do not often tell it themselves or have cultural practices that make ritual dishonesty, say between certain groups or to strangers, the norm.

With an understanding of the notion of cultural universals, it is reasonable to ask whether collective title, or some of its fundamental characteristics, may constitute a cultural universal.

On one hand the widespread occurrence of the commonalities noted suggest some core elements that could be cultural universals. On the other, the fact that late Greek, Roman and modern Western tenure systems are marked departures suggests otherwise. In addition, the collective titles considered display a wide variety of particular details, in some there is no notion of ownership at all, in others there is some, or even the recognition of a leader as the land owner. To be considered as a cultural universal these objections must be overcome.

In terms of the variety of actual systems, from pure communal to feudal, the central issue is not the operational details, but the core concepts of land title and distributive justice that appear to be resolved in essentially the same way in every case. The facts at this level support the cultural universal status.

The exceptions to collective title, predominantly modern Western tenure, but also the late Romans and Greeks, are a more serious problem. This is because the acceptance of private rent taking is high and expanding, supported in part by theorists trained in its application and who often hold a vested interest in its operation.

To assert that something akin to native tenure is in fact a cultural universal infers that the current tenure system is an aberration. This is a serious charge and one that cannot be made lightly.

One line of evidence is the relative success of the two systems. Superficially, this would be a blinding victory for the modern West - indigenous peoples are all economically backward compared to the West and by contrast, those cultures, such as Japan, who embraced Western commercial and land practices are amongst the most developed in the world. Moreover, the ancient Western collective titles, including feudalism, have all been overtaken by the modern system.

This analysis however is not entirely satisfactory. Its shortcoming is analogous to the problems with casual inference encountered with the Romans and Greeks. The implicit and problematic premise is that private freehold is causal of the wealth production of the West. To buttress this common premise, defenders typically look to history and cross-cultural comparisons, but this is to beg the question. The problem is that the assertion relates to productivity, whereas the issue is more obviously one of distribution. There is no denying that modern Western economies are more productive, but this may be the result of other coincidental factors, such as, and more likely, capitalism, especially adopting the uncontentious Smithian notion that the market facilitates productivity.

Land tenure is not centrally a production, but a distribution issue. Its success cannot be correctly measured in terms of production, or total wealth, but rather in the distribution of that wealth. In these terms the performance of the West has not been so convincing. Rogers observed that the highest relative wages of the six centuries preceding his study occurred at the end of the fifteenth century and first quarter of the sixteenth in England (Rogers 1884/1949). This coincided with the effective end of English Medieval Feudalism. Charles observes that real wages were three and a half times greater in 1495 than in 1770 (Charles 1991, p.1). The First Poor Laws in England were passed in 1598 signifying impoverishment of the common people on a national scale at the end of the century that began with record wages but was punctuated only by the dismantling of a key part of the feudal system.

Add to this the fact that improvements in distribution to the common family since the time of Dickens have been the result of the rise in the strength and organisation of labour - not Friedman's free market - and the social success of modern land tenure is even more questionable.

Finally, even a casual study of the Enclosure Movement, reveals the commonly accepted view that despite its asserted benefit in prompting more efficient land use, it resulted in widespread impoverishment and the funnelling of wealth to a tiny landed class to the detriment of the remainder of the nation.

If modern Western land tenure does represent an impediment to effective and optimum economic distribution, then it actually becomes a fact supportive of the cultural universality of collective title. This is an area that deserves closer attention and may contain important policy implications. The conclusion would mean that what is currently referred to as customary tenure is not properly described by the pejorative *primitive*, but is more accurately understood as a system of tenure closer to what is universal to society and historically more effective.

The notion of cultural universals is the closest that the modern methodology of sociology can come to recognition of an apparent essential characteristic of human nature. This survey of cultural practices could be considered to form a set of observations that suggest aspects of human nature in the Aristotelian/Realist sense that follow as a result of formal abstraction.

4.11 CONCLUSION

The fundamental elements of the indigenous practices regarding the political economy of land, share essential commonalities with prominent ancient Western cultures and Medieval feudalism. Feudalism itself is curious in its wide distribution and although far more elaborate than simple collective land ownership, feudalism

incorporates the same fundamental elements in a manner suitable for more complex communities.

Society's relationship with land may be interpreted as possibly conforming to the requirements of a cultural universal. All of the examples considered here, even including exceptions, such as modern Western freehold tenure, support this view.

If property practice in land has essential elements that are culturally universal, these provide strong evidence for the appropriate treatment for property in land. The evidence surveyed in this chapter would suggest that the application of the surplus product from land to the common good is believed to be the appropriate way to treat land property. This does not prescribe a unique economic system, but rather a criterion that any sound economic system must embody. Hence, many societies have been successful using feudal systems, many have adopted simple tribal or clan based land ownership and there has been a vocal political movement in favour of land rent as the tax base for modern Western economies. These represent vastly differing resolutions of the land problem, but united by the same core belief.

This chapter has also reviewed land property practices in terms of progress. Apart from the fact that the sociological concept of progress has lost favour within the social sciences, there appears to be ample evidence, from Greece, Rome and even the English Enclosures that the transition to individual private property does not constitute a positive progression in social functioning.

4.12 CONTRIBUTION TO THE SUPPORT OF THE THESIS HYPOTHESES

	Hypothesis	Conclusion
1.5.1	The treatment of property in land is highly varied by different cultures.	Supported
1.5.2	The majority of cultural practices in land may be reduced to common underlying principles relating to the social destination of land income.	Supported
1.5.3	The social destination of land income is an ethic that is linked to a constellation of social ethics capable of being summarised within the notion of solidarity.	Supported
1.5.4	Current Western treatment of land is culturally distinct from the majority of distinct cultural resolutions of property in land.	Supported

Chapter 5: The Concept of Property

The purpose of this chapter is to review the theory of property as it has been expressed by various theorists and economic systems.

5.1 PLATO

The earliest treatment of property would appear to be Plato's consideration of it in his *Republic* (Plato 1987). In it he suggested that his Guardians, the peace keepers of his republic, should not hold property. His argument was a political one, his goal was the formulation of a strategy that would ensure that those whose task in society was supervisory, would discharge that role without corruption. Property was considered amongst discussion of several issues that Plato believed had bearing on a person's ability to impartially and vigorously act for the good of the community.

Fundamental to Plato's Guardians was education, implying the significance of what he developed into the desirability of his Philosopher Kings, an expression that has evoked passionate discussion ever since. Plato's notion implied an optimism that a disinterested, well educated ruler would rule wisely, philosophy here being understood to lead to good deliberations. Much of the later concern regarding the term appears to have been centred on the fact that much that passes today as philosophy is not good in the common understanding. Without exploring these issues further, it is evident that Plato held the desirable behaviour of his rulers in moral terms, and that moral dimension was assisted by sound education.

Property was seen by Plato as a threat to the moral purity of his Guardians. He insisted that they should "*have no private property above the barest essentials*" (Plato 1987, p.184). They should have no money, no land or houses and should be forbidden "*to touch or handle silver or gold*". Plato's admonitions were in the strongest terms believing that it was "*(u)pon this their safety and the that of the state depends.*" Plato's concern obviously was that when those in authority developed a taste for gold, or any possessions, they would shortly abandon the ethical discharge of their duties in favour of using their position for comfort and personal gain.

This position is not identical with a rejection of property, or a rejection of material comfort, though Aristotle would later criticise Plato for precisely this, that the Guardians had a hapless existence. Plato held that although they did not have the opulence that marked many rulers, they would never the less be happy, due to the intrinsic pleasure that came from philosophy and discharging their duties well. Plato obviously believed that property was not a necessity for happiness.

Plato believed that their material needs should be provided by the other citizens “... *as an agreed wage for the duties they perform as guardians ...*” It would be incumbent on other citizens to hold and use property. Indeed, Plato held that “... *(i)f they they acquire private property in land houses, or money, they will become farmers and men of business instead of Guardians, and harsh tyrants instead of partners in their dealings with their fellow citizens ...*” Property was therefore licit in Plato’s political thought, but only for those whose occupation it was to use it productively. From property the civic function would be financed.

It must be remembered that Plato is setting out what is arguably the first systematic attempt at an investigation into political order available in Western thought. Hence his system may be excused for its apparent failure to respond to the subtle complexities of his subject. However, too much should not be made through this excuse. While his beliefs may appear simplistic and Utopian, they generally contain substantial truths regarding human nature. The tendency for rulers to grow too fond of the material privileges that can easily come their ways has been evident in every century, and no less in every form of government. Plato’s attempt to limit its exercise through an official sanction against rulers holding property is therefore praiseworthy, even if naive. His observation that the opportunity of holding private property constitutes a grave distraction for those in public office reflects a truth. Property can move a person to act in a way that deserts other social responsibilities.

Roepke seemed to recognise this danger when he quoted Bacon’s view on property that, “*Wealth is like muck. It is not good but if it be spread.*” He was reflecting not only the attractiveness of distributed wealth, but also indirectly observing its offensive quality when overly concentrated (Roepke 1948/1996). This is clearly what Plato wanted to avoid, especially through the misuse of civil authority.

Plato considered private property appropriate to the industrial and agricultural classes in his society. These worked their property and earned it through their toil. Their success was material and so was their reward. Further, Plato expected that the propertied citizens would provide material support for their guardians as a sort of wage. The guardians were apparently aloof from the partisan approaches of citizens, though Plato does not seem to have considered lobbying by citizens in his political construction. Rather, the propertied class was believed to be intellectually inferior to the Guardians and there even appears to be a subtle snobbery in Plato’s inference that a well educated person would be above distraction by material pleasures.

Within his culture, Plato’s interest in questioning the private ownership of land and other property was topical. While private ownership of chattels and slaves was not contentious, ownership of land was an issue. The Greeks early in their history vested

land ownership with the family, or tribe. This practice would have been still common in Plato's time, however it was giving way to private, or individual, ownership. Family ownership of land meant the sharing of the product with the family. It was not uncommon for that sharing to mean that while fit members may toil to work and manage the family estate, even with the assistance of slaves, the product was distributed amongst many who were not actively supporting the work. Young Greeks recognised that their standard of living could be enhanced by buying land privately and working it. The product from this enterprise did not have to be shared with relatives.

Plato's concern with private property in land may well have been born from his familiarity with this developing practice. In modern terms he was witnessing the transition to the nuclear family and the economics of the individual. From his perspective he appears to have seen private property as a distraction from social responsibilities, and his denial of it from the Guardians a reasonable, though perhaps impractical, response.

5.2 ARISTOTLE AND REAL PROPERTY

Aristotle's solution to the issue of property was almost the complete reverse. He argued that private property was a practical necessity, using arguments that seem familiar to Western thought. Through private property, persons are encouraged to be more productive and also motivated to care for their property in a manner that is not generally evident when possessions are shared. The political use of property in Aristotle's understanding was also the reverse of Plato's Republic. Aristotle was not convinced that Guardians could be happy in their property free life, exacerbated by Plato's further denial of family to them. Moreover, he considered that it was more appropriate that those who function as Plato's Guardians be the land owners.

For Aristotle, the warriors in a society should be the land owners, but not the workers of the land. Further, he suggested that they should all have holdings both near the borders of their state as well as close about its central city. In this way they would be equally motivated by security threats and not leave the border lands poorly defended. In this way Aristotle recognised a particularly pragmatic aspect of real property rights in the political order. There is much in Aristotle's model that appears to have found expression in the European feudal system that crystalised out of the dark ages almost a thousand years later and feudal structures that existed in his time as distant as China and Japan.

Surprisingly, European feudalism developed with little debt to Aristotle's political thought, growing instead out of German practices. The tendency to conclude that European feudalism somehow was a development of Aristotelian thought points up a curious fact about feudalism. By the time Aristotle was using deductive logic to arrive

at the most appropriate allocation of real property, his conclusions had already found realisation in the political economy of real property in a number of disparate peoples around the globe. When Aristotelian thought returned to Europe in the thirteenth century, via the Arabs and manifest in the work of St. Thomas Aquinas, his political thought could be seen as philosophical validation of the European feudal system and several Islamic states as well (Small 1997).

The development of this aspect of Aristotelian property thought will be examined further under discussion of St. Thomas Aquinas.

5.3 ARISTOTLE AND PRIVATE PROPERTY

In general, Aristotle accepted the right of private property, but only when connected with an obligation for common use. He did not differentiate between real property and products, though it becomes evident on closer examination that such a distinction is appropriate. The dual principle of property was later adopted in Medieval thought and continues within Catholic thought to the present, although its precise application is not always defined in practice (Ederer 1995).

The fundamental aspect of Aristotle's position is that property rights exist but are limited. In this way, it stands between the dominant ideologies of the present day, capitalism and Marxist socialism. Capitalism accepts private property, but not common use, while socialism accepts common use but not private property. Aristotle's construction of private property was ordered towards the moral end of the common good. He recognised the necessity for the conscious inclusion of a social role for property.

5.4 MEDIEVAL SCHOLASTIC PROPERTY THEORY

Medieval thought as found in the Scholastic tradition, especially the thought of St. Thomas Aquinas (Thomism), went some distance in exploring the nature of property, however the project appears to have never been taken to its conclusion. This may be either because the issues of that era did not necessitate the endeavour, or that it was not clearly recorded. St. Thomas Aquinas grounded his economic thought on a theory of property, locating property as a conventional institution that was necessitated as a defence against certain human weaknesses, *"the ownership of possessions is not contrary to the natural law, but an addition thereto devised by human reason."* (Aquinas 1981, II-II, Q. 66).

St. Thomas recognised that private property had two aspects, ownership and use. Ownership in this context relates to authority over the property and use relates to enjoyment of the thing or the benefits that flow from it. Ownership was considered by St. Thomas to be necessary to human life because a personal owner could be expected

to be more discerning in procuring and caring for a thing, and because personal ownership led to greater order and peace as opposed to the possible quarrels that could arise over commonly held property. Although he recognised that God had given all things to man, he also recognised that in order to achieve the above ends, private property "...arose from human agreement which belongs to positive law." It would seem apparent that the exercise of discernment, care and peaceful disposition towards one's neighbour are all within human capacity, but in practice often violated. For this reason, private property can be associated with the necessity of man's fallen nature.

St. Thomas's position is usually seen as a continuation of Aristotle, but its formulation was present within the Scholastic tradition before Aristotle arrived. The Franciscans Alexander of Hales and John of Rochelle⁴⁴ had written on property in a *Summa Theologica* compiled and largely written by Alexander. They concluded that property was naturally common but that private ownership was a necessity of man's sinful nature. St. Bonaventure, again without the help of Aristotle and before St. Thomas's *Summa* had written repeatedly on both the nature of licit private property and especially on the notion of the concurrent obligation for common use (Langholm, 1992, pp.117-160). St. Thomas's treatment may be viewed as an integration of the understanding of property expressed by his close friend St. Bonaventure within the philosophical methodology of Aristotle.

Use is a broader concept than direct use and can include the indirect enjoyment of goods resulting from a thing. St. Thomas recognised that human dominion could not extend into control of the natures of things, these are reserved for God alone, but the material world had been given to man for his profit by God. This means that by nature material things useful to man and given to him for his use. This does not infer personal use, but only use on account of the individual's membership of the human race. This is common. Because this conclusion is based on the nature of material things and Divine positive action (Divine positive law), it cannot be changed by man.

Common use in advanced Western societies can be very indirect, for example, property in an oil well finds use in transport (a family trip into the country) or even as a plastic toy by persons totally unknown to the owner of the well. Between the well and the plastic toys are a large number of people who rely for their livelihood on processing the various intermediate partially finished commodities. The use of the productive wealth, resources and land exists as utilities and employment for many and is distributed through the various exchanges and prices between the well and the final user (Kavanagh, 1954).

⁴⁴These two men successively occupied the Franciscan chair of theology at the University of Paris ending in 1238 and 1245 respectively. Alexander's *Summa* was the first of that form of compilation.

Common use represents a kind of mean in the distribution to various parties. When this distribution is distorted, such as by through the disbursements being drawn to one party or another, the virtuous use of property becomes a vice. At one extreme, if the well owner also used slave labour for the entire manufacture and sale, selling the final product close to its utility value, he would appropriate the full use value to himself. On the other hand, if he and the intermediate labourers supplied the product at no cost, then the use value of the well would effectively be located with the end user. Neither would seem to represent the community of use that St. Thomas intended. Any party is capable of unjustly benefiting from an imbalance.

For this reason holding wealth is not improper for St. Thomas, however using wealth to exploit others is. Hence, "... *a rich man does not act unlawfully if he anticipates someone in taking possession of something which at first was common property, and gives other a share: but he sins if he excludes others indiscriminately from using it.*" , [Pt II-II Q66 art.2, 1471]. This would appear to mean property in land, because property in goods arising entirely from one's toil (e.g. services) does not seem to have an existence prior to its private realization through toil. The source of property was not differentiated by St. Thomas, however it would appear that even here the worker must accept the origin of his productive capacities as contingent and Divinely willed, and hence its use also not exclusively personally owned. This thesis will not pursue the origin of human nature, hence its contingent nature will not be further considered.

5.5 ISLAMIC PROPERTY THEORY

Ibn Taimiyah (1263-1328) is representative of early Islamic thought, though he was a contemporary of St. Thomas Aquinas. Islam had adopted Aristotle before the West, and it had been used by Islamic scholars in a similar way to that of St. Thomas. Moslem scholars used Aristotelian methodology to systematise and extend notions that they found in the Koran. Private property was accepted, usury prohibited and just pricing promoted (Islahi 1988).

Modern Islamic scholarship brings Western economic analytic tools to the Koran with results that are not dissimilar to that of Ibn Taimiyah. This may be partially because of the common methodology that is based on the Koran, but this masks the pervading Aristotelian aspect of its methodology that is still realist. For this reason modern Islamic economics has the advantage of being better developed in terms of its analysis of economic issues from the perspective of the natural law, informed by modern economic analytic tools. While some Western people are repelled by some aspects of Islamic culture, its economic scholarship should not be passed over lightly. This is not to advocate an indiscriminate adoption of the Koran, rather a considered

review of the value of the premises that Moslem economists draw from it and the conclusions that can be derived from them.

Modern Islamic economic thought begins with a theory of property that is separable into two components. Some property originates with human effort, and is in a sense absolute, whereas other property originates from the appropriation of natural resources, a gift from God. The Koran carries a more explicit statement of the origin and purpose of the material world, God made the world, it is His and it is given to humanity as a loan. The latter comes with particular obligations. *"As long as he (the property owner) remains worthy of God's trust by following the Shari'a, he has the right to enjoy the use and advantages of God's property"* (Nomani and Rahnema 1994). These obligations are simply the responsibility to live according to God's will, which from an Islamic point of view is to live as a good Moslem.

The notion of common use features indirectly through the implications of Islamic practice and also explicitly in the case of several things that are reserved as common or public property. These include several forms of primary resource, following from the saying *"People are partners in three things; water, fire and pastures."* The extent of common property appears to be a matter that is still being debated in Islamic economic thought.

Islamic thought on private property recognises that most property is a compound of personal labour and God's gift of natural resource. Through labour, the Moslem attaches himself to a particular piece of natural resource, making it his. Debate in Islamic circles still surrounds issues such as whether the work of a servant is the property of the master and how far the title gained through labour extends over the natural resource. It is evident that at least in theory title dissolves on land left abandoned, though this precept suited a simpler culture and taken to its conclusion would prohibit rent taking. The private taking of rent is immoral in Islamic theory, but exists so widely in Islamic society that it has been accepted legally.

5.6 MODERN PROPERTY THEORY

John Locke is usually cited as providing the original theory of property, at least in the modern era. This is not to say that his account of property was unique in the period, or that the notion of property had not been considered before then. His position in the modern theory of property may say more about modern thought than about his theory. His aim was to establish the legitimacy of property within natural law and he used labour as the key in this endeavour. Whereas Aquinas went directly to private property in things once common, Locke apparently sought a natural law account that avoided the common use responsibility. Labour appeared to Locke as the key to property leading him to conclude:

"Though the Earth and all inferior Creatures be common to all Men, yet every Man has a Property in his own Person. This no Body has any Right to but himself. The Labour of his Body, and the Work of his Hands, we may say, are properly his. Whatsoever then he removes out of the State that Nature hath provided, and left it in, he hath mixed his Labour with, and joyned to it something that is his own, and thereby makes it his Property." Bk.2 Ch.V, 27]

As well as property arising from personal effort, Locke also appropriated as licit private property the labour of those under his control:

"Thus the Grass my Horse has bit; the Turfs my servant has cut; and the Ore I have digg'd in any place where I have a right to them in common with others, become my Property, without the assignation or consent of any body" (Locke 1693/1967), II, n.28]

It can be seen that this is not so very different to what Moslems had been aware of for some centuries, and leaves unanswered the same issues. However, in Western thought it was significant because it is in the natural law tradition, but does not leave private property as *conventional*. This is the force of the assertion that it exists without the assignment of anybody. If it is natural and defined by labour, then it is absolute and does not come with any responsibilities of the type implied by St. Thomas's common use. This was important to Locke who reflected the dominant British sentiment of his time that had been moving towards individualism in private property in land especially since the sixteenth century and especially evident in the Enclosures.

Locke also appropriated as his own the property obtained through the labour of his household which considerably extended his reach and made the possibilities for ownership almost unlimited. The notion of household echos Aristotle and suggests the way that within the household property is common under the management of its head. (Prasch 1999) noted that the apparent identification of the household with the economic individual has caused some confusion as it has subsequently been used to refer to the individual person. This transition from a collective focus to the individual appears between Locke and Smith.

Locke's labour theory of property extends into a labour theory of value leading him to assert *"tis labour indeed that puts the difference of value on everything"* and establishing a labour theory that would remain dominant for about two centuries. The labour theory of value can be seen to be consistent if the natural resource component, land, has no substantial economic significance. This is implied in Locke's theory of property and is perhaps its most significant departure from both the Islamic theory that it resembles and the Thomistic that it sought to replace. The failure of the labour theory

of value may be evidence of the relative merits of Locke's property theory with respect to its predecessors.

Before Locke, the Dutch Lawyer Hugo Grotius (1583-1648) had attempted a natural law theory of property. Grotius noted that when a person made use of a resource within what was otherwise common, it prevented others from using it. On the basis of exclusion, Grotius interpreted private property to follow. If people were to be permitted to use resources, even if they were common, the result was private enjoyment, which generalised into private property. While this approach differs to Locke, it also locates property in human action but also as natural and frees it from the ethical bounds of the Scholastics. Grotius is significant in that this methodology for understanding the natural law is also what Locke used and was later developed by Hume (Buckle 1991).

Hume also attempted to relate his thought to the natural law as Buckle has shown. His methodology was consistent with Grotius, deriving its force from the assumption that nature could be known only through observation. By observing human action human nature could be inductively known. Hume observed the dominant commercial practices of his time and inferred human nature from them. Smith and Hume were very close as is evident both in their writings and their actual friendship (Fay, 1932). Smith's economic writing has proven more popular than Hume's, but is built on the same methodological base. This is evident from a comparison of their moral writing. Hume's methodology which has become the foundation of modern economics (Meikle 1995) is based on what can be perceived and rights of property cannot be perceived, only possession. This is evident in Smith's restricted scope for natural title to property which, in the example of the hunter "... according to Smith, the idea of property was absent, and possession was all" (Reeve 1986). Smith accepted the right of a person to his own body but adopted a strong conventional view on other property believing:

Property and civil government very much depend on one another. The preservation of property and the inequality of possession first formed it, and the state of property must always vary with the form of government. (Smith 1978, p. 410)

Although within his economics Smith recognised the connection between labour and property, the thrust of his theory is positive. While this could return to the Scholastic notion which is conventional it does not contain the depth of the Scholastic/Aristotelian understanding of the whole of the convention. For Smith, if government establishes private property, it exists, end of question. The positive institution of private property extends not further than its definition by the state. In Smith's case, that was private property of the type conducive to capitalism that contained no expectation of social

responsibility. It is the conception of property that currently reigns in modern Western thought.

This is not to say that it has escaped criticism. A century after Smith, Marx was refuting property totally, although his approach may have been included within Smith's understanding of the state setting the parameters of property. Marx simply advocated a government that set a different positive definition of property. Proudhon proclaimed before Marx that *property was theft*, alluding to some objective moral foundation to his view, despite being otherwise critical of objective morals. Henry George thought a minor readjustment of land property rights would set the economy straight⁴⁵.

Macpherson (1978) identified the Enlightenment as a watershed in the understanding of property. Property had ceased to be private or common, because common property was meaningless. Moreover, the replacement "*of old limited rights in land and other valuable things by virtually unlimited rights*" (p.7) was recognised by Macpherson to have validated a regressive transition in property. It was encapsulated in the oft quoted description of Blackstone:

(Property)"... that sole and despotic dominion which one man claims and exercises over the things of the world, in total exclusion of the right of any individual in the universe." (Blackstone 1979, p. 2)

Contemporary with Smith, Blackstone's description indicates the positive construction of property as it existed at the time. His choice of words is revealing, a despot exercises power as a tyrant, a usurper whose rule carries connotations of harshness. A recent analysis of the institution of property using a basically Humean methodology concluded:

Yet the price that has been paid for the compulsive power of the absolute dominion trope has been a heavy one, a maddenly persistent tendency to suppress and to deny the collective and collaborative elements, the necessity of mutual dependence, inherent in social endeavour, and the consequently enormous distortion in our common capacities to understand and regulate our social life. (Gordon 1995), p. 108]

The current defense of property is usually found within arguments leading to liberal free market economic conclusions. Pejovich (1990) considered that "*property rights are relations among men that arise from the existence of scarce goods and pertain to their use*" (p. 27). He went on to argue that private property was Pareto optimal, and implicitly therefore morally superior. The liberal approach identifies property with

⁴⁵George's economics accepted private ownership in land but provided common use by taking its rental value for public revenue.

freedom, a position that is reasonable except that it adopts the Enlightenment construction of property uncritically. Its basis is usually the assertion that the modern liberal institution has been responsible for the greatest material success, such as in terms of GDP per capita. It tends to lead to respect for property in land but not for property in one's life and has no place for the notion a social dimension to private property. It is a necessary foundation to current pressures towards economic rationalism and globalization.

5.7 MARX AND PROPERTY

Marx believed that property was not natural to humans, but that it developed along with other institutions. Property for Marx was a tool for oppression and grew as part of the development of patriarchal dominance. According to Marx "*(t)he first form of property is tribal property.*" (Marx and Engels 1968). This form of property occurs when tribal people have large amounts of unused land and internal relations modelled on the family.

Everling (1997) explained Marx's belief that "*Patriarchy, as embodied in the slavery already implicit in family relations, become the management also, of social slavery*" exposing the peculiar disdain for the family that pervades the thought Marx and Engels. Given that the family exists under the domination of the father who controls his family as slaves, the product of the family becomes the property of the father through the implicit internal conflict. This confirms and informs the Marxist understanding of the development of property as, "*The slavery latent in the family only develops gradually with the increase of population, the growth of wants, and with the extension of external intercourse, both of war and of barter*" (Marx and Engels 1968, p. 21-2). As the tribe expands its dominance through the dominance of others via the institution of slavery, the patriarch appropriates the product of others as his property and his title is held through political domination.

Implicit in Marx's understanding of property is its social product, an aspect that Everling goes to some length to explore. Things only have significance as products and products only come into existence through the exercise of labour. In this world land has only social importance that is manifested only through production and its ownership is meaningless if not as a tool for oppression of the working class.

The historical/anthropological basis is highly doubtful, though the conclusion of land ownership as a tool for inter-class extortion has substantial empirical support, especially in Marx's century. However, his observation of the abuse of real property do not validate his genesis fantasy, nor his rather dismal view of family slavery and hence the origin of property. Marx's eventual rejection of private productive property is well known, though its foundation is more based on political reaction than reason.

Marx's belief that property was a positive institution and his preoccupation with labour as the only owner of products echoes parts of the major theorists, at least back to St. Thomas. Like Blackstone, property confers despotic authority, like Smith it is purely conventional, like Locke it is keyed to labour and labour is the only natural title. But much is missing from Marx. Although Marx owes an evident debt to Aristotle with regards his construction of natural and unnatural exchange, he ignored his acceptance of private property linked with common use. No doubt this was connected to some degree with the post-Enlightenment experience with property owners who had proven incapable of even conceptualising the possibility that their property could be used to benefit others.

Whatever the shortcomings of the Enlightenment theory of property may be, Marx's response has little to offer. His theory evidently grew from sentiments found in the earlier socialists who, like Proudhon, considered property to be theft, but as a serious theory of property it makes no contribution.

5.8 CONCLUSION

Plato recognised a connection between politics and property in his construction of his Republic. He recognised the necessity for rulers to be supported, but to be above the corrupting influence of property. Aristotle was critical of many aspects of Plato's Republic and recommended an outline for the political use of property that could easily be seen in feudalism.

More importantly, Aristotle argued that private property was licit, but only when use remained common. This theme of private property incorporating common use recurs in various cultures and has come down to this present century, not only in the cultural values of many non-Western peoples, but also in the social teaching of the Catholic Church. The Catholic tradition refined Aristotle's understanding of property in the thought of St. Thomas Aquinas, and established property as natural to man as regards ownership but this does not infer despotic private ownership. Private ownership was argued by St. Thomas to be a practical advantage, given the condition of human nature, and instituted as a positive institution which necessarily had no authority to privatise use, which was the natural property of humanity in common.

Property was therefore natural in common, but positive with respect to private title. No interest was taken in one's ownership of one's self, however a person's natural right to their own life does not appear to have been challenged.

Islamic economic theory is based on a theory of property and develops this duality between what is natural property and what is acquired. Natural property are those things that are proper to the human person by nature, these include physical attributes,

life itself and consequently one's labour. All else is the work of God for the Moslem, therefore properly His, His property. A moral theology follows on the Islamic metaphysics of external things, in that human property in external things is conditional on serving God. Part of this is a theory of private property that sees property rights as following from the application of labour to a common resource.

John Locke reached a similar basis for private property based on the natural private property of one's own life and labour. Labour appropriated what was previously common in Locke's view, paving the way for the despotic dominion noted by Blackstone. Smith replaced the theoretical construction of property by the simple positive connection of property with the reigning legislation defining the institution. This understanding remains as the dominant modern position, despite some recognition of its shortcomings.

The socialist reaction to Smith's modern liberal property may be viewed as a return to a strong form of Locke's labour theory of property. Unlike Locke, Marx located property title in the hands of the worker, who for Locke was only a servant and instrument and of no separate consequence. In practice, property rights in socialist communities are held by the state and not by the workers which leads to a similar outcome for labour.

5.9 CONTRIBUTION TO THE SUPPORT OF THE THESIS HYPOTHESES

	Hypothesis	Treatment
1.5.5	The Western notion of property is positive and historically recent.	Supported

Chapter 6 A review of contemporary market theory and its moral and positive reference points

The purpose of this chapter is to review the modern theory of exchange as found in neoclassical market and marginalist theories. These theories are constructed within a modern world view and tend to be currently maintained within a positivist methodology. The positive existence of trade and what appears to be a free market are undeniable. More interesting is the way that market theory is not content to rest on its reliable positive foundations, but asserts theoretical explanation that is only explicable as a strategy for moral justification. The limits and validity of the positive basis of market theory will be reviewed as well as the moral issues that are evident within the theoretical construction of neoclassical market and marginal theories.

The predominant development of economic science in this century has followed Marshall's (1920/1938) prescription for the discipline to be a positive science of behaviour. His outline of the science made economic phenomena the object of the science and led Friedman (1953) to describe its methodology totally in terms empirical behaviour. As such it is quantifiable and capable of interpreting the likely outcomes of policy initiatives. Currently it exists as a discipline dominated by observation and interpreted using the tools of mathematics.

Despite this, economic science has never completely shaken free of its earlier roots in philosophy, particularly metaphysics and morals. Economics grew out of Political Economy, a moral science that is "*the study of appropriate relations between intelligent persons with respect to material things.*" Before Marshall, most contributors to economic thought were primarily philosophers. Adam Smith, *the father of modern Economics*, studied economics as part of his activities as professor of moral philosophy. St. Thomas Aquinas, whose economic thought summarised the medieval position, was writing economics as part of moral theology. Other writers in political economy, such as David Hume and J. S. Mill are also known as least as well for their philosophical writings as for their economics. Aristotle, *The Philosopher*, identified the key elements of political economy that have been debated down to the present day, although his economics is predominantly found as parts of his investigations into Ethics and Politics.

Today, positive economics claims the success of being able to interpret and predict human economic behaviour, yet its critics object on two grounds. Firstly, that as a positive science its objective successes are not commensurate with expectations, and secondly, that its prescriptions are often bereft of adequate moral content.

The purpose of this thesis is to evaluate the claims of positive economics with a view to locating its value to the community by evaluating its characteristics as a behavioural, not a moral, science. In this way it is proposed to demonstrate that both the claims of its supporters and the criticisms of its detractors may be simultaneously upheld.

6.1 MARKET BEHAVIOUR

Economics is focused on the market. Without trade there is no content for economics. Controlled economies are no more than markets where critical processes have been suppressed. The aberrations in behaviour that result from socialist controlled economies are well documented and do more to support the essential theory of market behaviour than to detract from it.

When persons freely meet in the marketplace to exchange goods and services, certain behavioural realities are evident. Suppliers are attracted by higher prices and they tend to multiply as prices improve, giving the characteristically upward sloping supply curve. Similarly, purchasers are prepared to pay higher prices when quantities are limited, but reluctant to pay high prices when the market is flooded with goods.

Despite the market being the prime focus for observation, both supply and demand are not fundamental but understood to be themselves the outcomes of causal explanations. The theory of the firm is used to generate the supply curve, while demand is the outcome of a utility maximisation calculus that is somehow carried out by purchasers.

Jones (1976) outlined several examples of the successes of market theory and similar examples abound in most standard texts on economics. In particular cases, such as urban economics, the impacts of market controls have been well examined, often as the result of observations of the outcomes of state interventions (Barlowe 1958; Harvey 1987). Generally, these have been unanimous in finding that artificial controls result in distortions that manifest as various disincentives, the encouragement of black market activities and over-compensations when restrictions are removed.

Consequently, market theory can be considered to have been empirically validated by the evidence of economic behaviour. However, despite a degree of empirical support, several areas of economics still resist the positivist approach. Macro policy

appears to be an area where theory follows behaviour, rather than predicting it. About two decades ago stagnation and inflation were found to co-exist despite the theoretical impossibility of such a union and today the move towards deregulation appears to be creating as many problems as it solves. Blumberg (1989) chronicled some of the outstanding examples of market failure and outlined some reasons why they should be expected to be the norm, despite the difficulties of study. The shortcomings of positive economics are also evident in the continuing existence of economic recessions and the failure of mechanisms such as government and central bank policy to control them. Grieder's (1987) study of the US Federal Reserve's decisions during some of the most critical years of the post war period illustrates the gulf between the major theories, practice and effectiveness.

6.2 ECONOMIC THEORY AND CAUSAL EXPLANATION

Various lines of empirical evidence exist supporting the demand curve. A major part of the success of advertising can be attributed to the fact that by enhancing the consumer's perception of a product's utility, its demand function will be elevated. Since advertising and marketing expenditure are justified on the basis that it produces a net increase in revenue, its continued use must indicate its success.

Some aspects of evaluating demand are less straightforward. Some time ago Wickstead (1914) noted that statistical studies of demand for specific goods were usually flawed by violations of their assumptions. For example, the generation of demand curves derived from observations of prices and volumes as traded relied on several impractical assumptions. These studies assumed a fixed demand function over time and virtually removed supply behaviour. Wickstead even asked why the data acquired was not evidence of the supply curve and concluded that some of the anomalies reported were more due to methodology than to genuine aberrations, such as giffen goods. His critique does not appear to have been answered.

Boland (1992) considered in some depth the assumption in economic theory that the consumer is a *utility maximiser*. At the very least, this axiomatic assumption of neoclassical economics that consumers maximise utility is a metaphysical assertion concerning the nature of consumers. Perhaps consumers are not very effective at performing this maximisation. Except for the market itself, there appears to be no definitive evidence of how consumers evaluate their maximum utility; this makes utility maximization as a justification of the market a tautology. You cannot explain market price using utility if the only evidence of utility maximisation is the market or experimental models of it. The existence of giffen goods suggests that consumers are significantly influenced by additional factors, of which ignorance would certainly

figure prominently. The question of objectivity must be also considered. Obviously, the objective merits of a product are not changed through advertising, yet it influences demand. It seems hard to justify this expanded demand through the pleasure experienced subjectively as a result of advertising imagery. The practical lack of substitution opportunities further limits consumer utilisation calculus, as does whim.

Economic utility maximisation must also consider the difficulties experienced in moral utilitarian theory, as it is no more than a specific application of it. One of the well-recognised shortcomings of utilitarianism generally is the impracticality of the computation of maximum utility. While utilitarianism is a powerful rhetorical tool, its outcome in ethics has been moral anarchy. It can be used by the individual actor to estimate apparent personal optimal outcomes, but this is not the same as the common good, and even for the individual it is highly questionable whether its determinations constitute genuine optimums. Most troubling are instances where ignorance, or disordered self-interest, have resulted in utilitarian determinations that are objectively deficient. These problems appeared to be well recognised in the nineteenth century. One of Durkheim's motivations to establish the discipline of sociology came from his perception that moral philosophy had failed to deliver adequate guidance for Western culture (Ritzer 1983). Warnock (1967) analysis of the developments in twentieth century moral thought revealed that it was founded on the fact that moral theory had lost its usefulness by the end of the nineteenth century. If utilitarianism generally cannot provide robust determinations of the greatest good for the greatest number, how much more difficult must it be for consumers to reliably determine their utilitarian optimum in the economic order. The positive performance of utilitarian calculus will be discussed in Chapter 8 as part of the analysis of attitudes towards demand as a basis for price.

On the supply side, the problems of causal explanation are even more pronounced. Jones recognised that the supply function rested on the theory of the firm, which explains the upward sloping supply curve in terms of the rational optimization behaviour of the firm. The theory, also known as *marginalist theory*, suggests that firms set their operating points at the intersection of their marginal cost and the marginal revenue curves. It yields a rational *marginalist* price through the interaction of these two functions.

Marginalist pricing has the advantage that it takes market behaviour into account. The marginal revenue curve is derived from the demand function and the marginal cost curve relates to the production constraints encountered on the supply side. In this way it provides a superior pricing theory to the older labour theory of value that is the implicit foundation of *full cost* pricing. Full cost pricing is the practice of applying a

mark up to factor costs in order to set sale price. Most observers recognise that it is the most common in practice (Jones, 1976, Langholm, 1969, Seton, 1985) Because full cost pricing does not have any explicit connection with market conditions, especially demand, it is not useful for explaining supply behaviour.

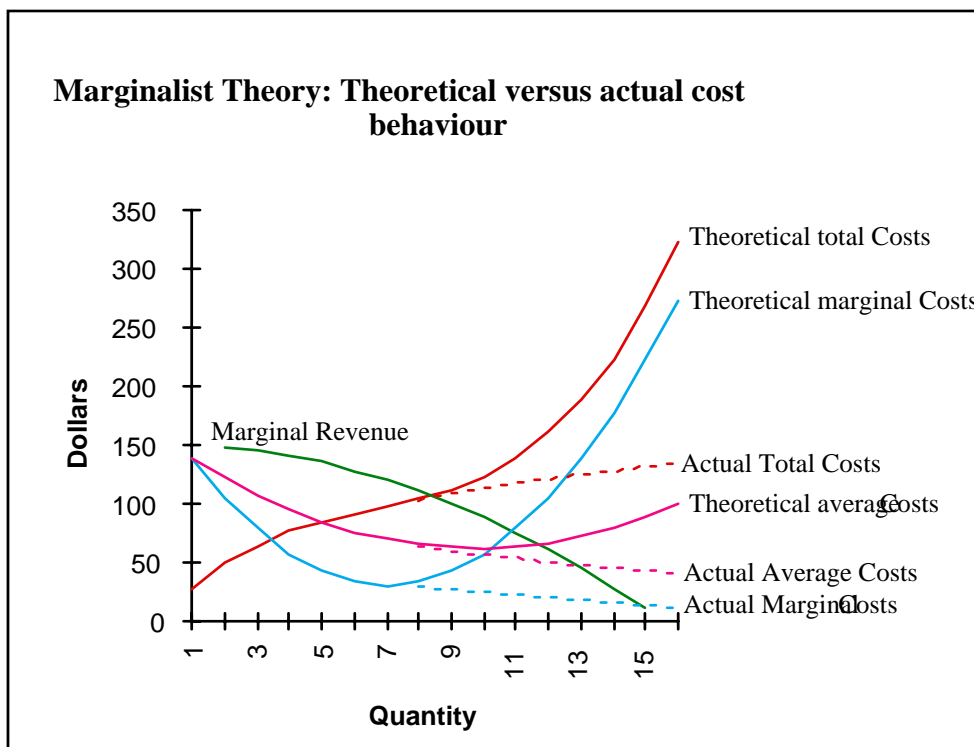
Unfortunately, Jones failed to find a single case of marginalist pricing in practice. Further, the literature on the absence of the practical application of marginalist theory now reaches back about two thirds of a century. Other recent studies have encountered related problems. Langholm (1969) compared the two pricing theories, using a simulation approach, and found marginalist pricing less efficient. Seton (1985) rejected both pricing theories for reasons similar to the above and attempted to formulate yet a third pricing theory. Friedman (1953) proposed positive methodology as sufficient to justify this gap between theory and practice. Friedman suggested that as long as the positive behaviour of firms (viewed externally as prices) matched the predictions of an economic theory, then it made no difference if the theory did not relate to the actual causal processes. Some economists therefore have suggested that prices can sometimes be shown to behave *as though* firms were performing marginalist analysis, even though it is known that they do not. Hence marginalist analysis is valid only so far as it is accurate in predicting price. Apart from looking a lot like Ptolemaic astronomy, actual prices cannot be shown to be capable of being reliably predicted by marginalist methods because of the practical impossibility of generating the mathematical relationships with anything like the precision necessary to yield a specific price⁴⁶.

In addition, Boland (1992) explored the related matter of the assumption of the upward sloping marginal cost function. The explanation of this function is usually done using examples where limited short-term productive capacity means that an increase in production can only be achieved at significant cost. He noted that in the real world this condition only applies in the very short term, hence both the marginal cost curve, and the supply function that is derived from it, are only applicable in cases of rapid changes in the market. This is contradictory to the temporal (dynamic) assumptions of equilibrium, which normally needs some time for the market to settle. If equilibrium needs time, but marginal pricing only works instantaneously, they cannot both operate, yet both are needed to support market theory.

⁴⁶To be practically applied, a precise demand function would have to be known. This is not possible directly, or indirectly with sufficient precision. It is also likely that it is temporally unstable. The derivation of marginal revenues from the demand curve is highly sensitive to small errors, making this function practically impossible to derive from noisy demand data. Marginal cost data is highly stylized in theoretical presentations, and as will be shown, the theory is contradicted by the cost behaviour in real firms. Even if it was corrected, the intersection between the marginal cost and marginal revenue curves would be so far from orthogonal that the resultant price would be hopelessly affected by noise in both functions.

Moreover, the upward sloping supply curve suggests dis-economies of scale that would provide no incentives towards larger organisations. Yet, the real world reveals an almost universal trend towards massive productive capacities and is filled with examples of corporate aggregation. There is an obvious contradiction between the supply function as found in economic theory and the complaints of ever growing corporations that in order to be profitable they apparently need to operate at immense scales of production, necessitating access to global markets. This is shown in Exhibit 6.1 that plots theoretical versus actual cost behaviour.

Exhibit 6.1: Marginal Price Theory



Apart from inferring a supply function that is the inverse of that adopted for market theory, the reality of widespread economies of scale is upsetting for marginalist pricing. Marginalist pricing assumes that marginal revenue (MR) is a diminishing function that follows the diminishing demand function, while the marginal cost (MC) function is an increasing function⁴⁷, at least in the vicinity of its intersection with MR. If MC is also a decreasing function, as is the case with economies of scale, then its intersection with MR will be considerably less determinate and would most probably

⁴⁷Marginal costs are believed to initially fall as the firm approaches its most efficient operating point, but then rise as the physical productive limitations of the firm are reached and exceeded using management strategies such as overtime shifts. Actual firms faced with growing sustainable orders will quickly expand into a larger scale and more efficient productive capacity.

produce a decreasing supply function. It is therefore no surprise that it is rare in practice.

Marginalist theory is said to be necessary for the survival of the firm, thereby inductively validating marginalism, however (Altman 1999) demonstrated that firms may survive that violate the assumptions that make up this assertion. The widespread positive existence of firms that do not operate at the efficiency frontiers that are necessary means that the real world is nowhere near as finely tuned as the theory would need to be valid.

The evidence is therefore not favourable to marginalist theory. The retention of marginalist theory, despite its absence from the real world, is contrary to positivist methodology, at least as it is applied to the natural sciences that its application in economics is supposed to replicate⁴⁸. Its only merit is its implicit validation of actual supply behaviour in a moral sense. The upward gradient of the behavioural supply function is evident, yet it would be no more than a *greed function* if it was not for the theory of the firm asserting that suppliers have *no other commercial choice*. Its retention is therefore an indication of the importance of moral validation as foundational in economic theory. The positive science of economics therefore has very sensitive moral roots.

6.3 PERFECT COMPETITION AND ITS MORAL ASSUMPTIONS

Market theory can be morally validated directly however, under conditions of perfect competition. Von Kettler (1811-1877), amongst others, has described the way that a perfectly competitive market achieves a moral goal when price is honed down to normal levels when he observed:

'Competition is at its best, however, if all natural and artificial restraints are removed, and this refers especially to such restraint as would interfere with free trade in the market. Universal free trade, therefore, implies unrestrained competition, and unrestrained competition reduces prices to their lowest limit - the limit set by the costs of production.' (von Kettler 1981, p.325)

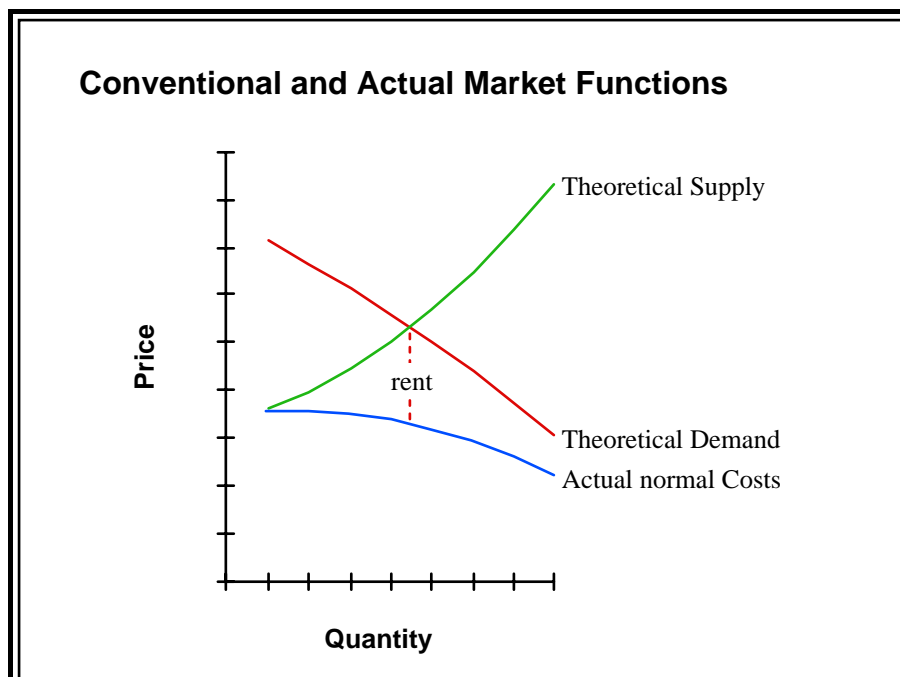
An immature or imperfect market does not pass this moral criterion and its moral failure, also termed market failure, can be related directly to the amount of economic

⁴⁸Positivism is supposed to test theories against evidence and discard theories that do not accord with observation. If marginalism only produces appropriate results when the data is false, then it should not be adopted. Even Friedman's methodology cannot help marginalist construction of the supply function because data on actual cost behaviour (including realistic modelling of economies of scale) will not predict a supply function anything like the behavioural phenomena

rent that is left in the price. Economic rent is the gap between normal price and market price and leads to super-normal profit. Monopolies, and other examples of market failure, are all characterised by perennial economic rents.

Samuelson (1975) noted the way that the characteristic negative gradient of the demand curve was purely an artefact of market failure. He argued that since perfect competition assumes full knowledge, mobility, freedom to participate in the market (or abstain), a plurality of suppliers, and defines normal profit as sufficient to provide suppliers with a sound income, suppliers would always be found who would be willing to supply under terms that would return normal profit. Prospective purchasers, knowing both the costs of production and the fact that numerous potential suppliers existed who could frictionlessly enter the market, would therefore be reluctant to offer super-normal prices for goods, regardless of quantity traded. Under perfect market conditions demand should therefore have a zero gradient (or, more precisely, should follow the normal cost of supply).

Exhibit 6.2: Market Functions



A similar argument could be mounted for supply. The monotonic positive gradient has been shown to be a practical phenomenon, not a theoretically supported one, given the problems with marginalist pricing⁴⁹. Under perfect competition, new suppliers

⁴⁹This issue will be further developed later in chapter 8.

would enter the market as soon as normal pricing was exceeded thereby capping supply. Therefore supply in a perfectly competitive market would also follow normal costs. This is shown in exhibit 6.2. The gap between the normal supply cost and market price is economic rent.

Along this vein also lies the problem of perennially imperfect competitive situations due to other causes. Under perfect competition, revenue to the producers is sufficient to cover costs, risk and provide a normal level of profit. Insufficient profit will cause share prices to fall, while super-normal profits cause growth in real share prices.

A perfectly competitive market should therefore be characterised by stable share prices. Moreover, if revenues are stable and super-normal, finance theory, especially capital asset pricing theory, suggests that share prices should rapidly adjust upwards to absorb the excess profitability in a one time adjustment⁵⁰. Hence, stable super-normal profits capitalise into higher stock prices that effectively normalise returns for subsequent stock purchasers. However, the realities of the equities markets are that stock prices tend to appreciate in real terms over the long term. Hence, not only are the markets imperfect, but the degree of imperfection cannot be adjusted out at any single point in time. Discussion and social attitudes regarding the behaviour of returns from corporate investment is relatively immature in a historical sense. (Goyder 1993) noted the fact that acceptance of permanent returns on capital were only permitted from about the middle of last century in England, and the notion of earning a return that did not amortize over time was recognised as an aspect of usury. This issue will be discussed separately.

The conventional explanation of growth in stock prices is that it is the result of the necessary reinvestment of a part of profits as retained earnings in order to maintain relative productive capacity within an inflationary, and rapidly changing economic environment. While this is a significant part of the mechanism of stock growth, the real component of growth (above inflation) is not accounted for, and even when supplied through retained earnings indicates that the latter are derived from super-normal earnings. Moreover, new capital investment often results directly in a form of economic rent. Barlowe (1958) demonstrated how new technology earns a rent governed by its marginal productivity over the least productive machinery in use. As old technology is taken out of service the rent dissolves. The rent is supposed to cover research and commissioning costs, further complicating the justification of the super-normal profits that are pre-emptively held to initially fund them. Resolution of this

⁵⁰The value of a financial asset is capitalised by dividing the expected future returns by the normal rate of return for the asset's risk class. Hence, an elevated but stable pattern of future returns will capitalise into a higher current value that will then return only a normal rate of return.

question of returns from capital investment carries considerable cultural overhead. To the modern Western mind, the thought of permanent profits from capital investment is normal. This makes an objective review of its foundations all the more difficult and will be pursued in a later section⁵¹, the point here is that perennial super-normal profit is evident in modern Western economies, despite indicating market failure and hence moral failure.

When viewed from this perspective, the entire discipline of finance appears to stand in opposition to the notion of perfect competition. The object of finance has been defined as being "*...to maximise the shareholders wealth*" (Wilson and Keers 1990), yet the only tool that is conspicuously absent in the technology of finance is attention to increasing productivity.

Necessarily, if profitability is improved, especially when not attended by greater productivity, it can only be the result of the generation of super-normal profit. The ongoing success of the finance function is testament to the absence of any real trend towards perfect competition at that level. Some tools of financial management, for example pricing and credit policy, can be interpreted as techniques to manipulate the market to maximise revenue to a point just short of the onset of market adjustments. Tackling the moral issue headlong Gilder (1984) depicted economic rent taking as the dynamo of development and Wilken (1979) sought to validate entrepreneurial rent-taking by noting that without the entrepreneur the other factors would not be productive. What these authors recognise is that market imperfection is the source of disproportionate income and hence is a powerful enticement. The moral argument goes well past these pragmatic factors.

Belief in the market could be maintained if it could be shown that markets tended towards equilibrium. Equilibrium infers the removal of economic rents and fulfils the moral criterion. Unfortunately, Saari demonstrated that there is no mathematical justification for expecting that markets will find stable equilibrium which Bryant developed to show that there is in fact no mathematical foundation for equilibrium at all, building on (Bryant, 1997).

Hence, the positive realities appear to be that supply and demand do constitute actual and quantifiable tendencies in the behaviour of parties engaging in trade. That is, they are positively evident. However, the causal explanations for both supply and demand are highly problematic and the accepted theories are demonstrably lacking. By contrast, once it is recognised that our usual rendering of the market functions relate to simply to

⁵¹Technology rents and other economic rents are further explored in Chapter 13.

positive behaviour within imperfect markets, then all that follows in economic theory is consistent.

Positive economics is therefore in a curious position. While it can justly claim substantial empirical success, its causal underpinnings are less than satisfactory. This can be resolved most effectively by recognising that market behaviour is simply *behaviour* and dropping the morally inspired (but problematic) causal justifications. The gap between the market supply curve and the medium/long-term cost of production curve is simply economic rent and firms act to maximise their collection of economic rent.

The demand curve is also a simple behavioural reality. In the practical order, purchasers lack adequate market knowledge, they cannot easily substitute alternate goods and suppliers are not sufficiently mobile. As purchasers evaluate the cost/benefit performance of goods, it should come as no surprise that as net utility is eroded by increased price, purchasers on limited budgets will progressively choose to go without.

The market is therefore a behavioural reality and positive economics stands up very well as a sub-set of the study of group behaviour, i.e. social psychology. Scan through the methodology and methods of social psychology and much is familiar for the economist. Experiments in social psychology involve setting up situations and observing behaviour. Demand studies do the same. Listen to commentary on any finance market and you find that it bristles with psychological overtones, such as market confidence or uncertainty. Marketing uses an explicitly psychological methodology to achieve financial objectives and the sub-discipline of Behavioural Economics appears to be well developed. Hedonic analysis in econometrics and real estate appraisal research are no more than specialised and well-developed branches of social psychology.

The identification of economics with psychology is not novel. Commons (1934) associated the traditional economic theory of his time with an individualistic psychology, and in arguing for his institutional economics proposed social psychology as the appropriate explanation for the behaviour of the economic actor. He proposed a special branch of psychology, "*...the psychology of transactions, which we may properly name transactional or negotiational psychology*" (p.90-1) as the appropriate foundation for institutional economics. Even the notion of institutional economics suggests the conventional nature of economic interaction, hinting at the fact that it is essentially a positive social artefact. This is consistent with the positive nature of property derived from land. Writing somewhat later Albert (1997) was critical of the

institutionalists whom he considered had "...failed to make clear that social psychology provides them with their core image of the human agent" (p. 909).

Social psychology and modern economics are methodologically compatible, both are positivist and amoral. Psychologists are just as likely to study the tendency of people to avoid giving help when others are in great need, as the dynamics of friendship. This frees the discipline to study any culture and to simply describe its behaviour, regardless of its ethical merit. Its goal, like economics, is simply to model and predict human behaviour, especially in the short run. Having found that nine out of ten people will walk past an automobile break-in in progress, one can anticipate future behaviour and make informed decisions regarding security. The fact that the major part of economic theory is built on the foundation of actual (imperfect) market behaviour explains its successes as a well-developed branch of this type of study.

The construction of human nature that follows is not the morally inclined notion of nature that gives rise to the natural law and the consequent normative behaviour directed towards the good, but rather the positive, *Enlightenment*, notion of human nature constructed empirically and inductively from observed behaviour. The former leads towards human perfection, while the latter, containing as it does all the imperfections of particular persons, leads only to short run behavioural predictions. It is possible that the social fluctuations that have been evident in Western cultures over the past five centuries as economic cycles are no more than evidence of necessary corrections to the excesses of the short run tendencies⁵².

Although positive economics is generally divorced from morals, it does retain certain significant vestiges of moral thought. The utilitarian assumptions at the very roots of economics are derived explicitly from the moral thought of Bentham and Mill and some of the shortcomings that carry over from moral utilitarianism have been discussed. In addition, other moral issues are normally accepted as part of modern economic thought, despite not being a necessary part of the positive science. For example, there appears to be a generally held belief that monopoly situations are to be discouraged and that economic distribution should evidence some level of distributive justice.

Concepts of distributive justice have a long history in Western thought, beginning with Aristotle, evident to some extent in scripture, expounded by great Christian thinkers such as St. Augustine, St. Thomas Aquinas and St. Bonaventure and most recently championed in the last century of social encyclicals. Even Islamic economic

⁵²See (Shuman 1972)

thought is founded on moral principles that closely parallel Christendom (Nomani and Rahnema 1994). The movements that have given rise to modern positive economics also have a strong moral strand. The ordinary person still relies on economics to provide morally sound prescriptions for the appropriate relations between persons with respect to material goods and this was exactly what Marshall argued would come from a positive science of economics. In no small degree is the popular criticism of economics a criticism of its failure as a moral science, and hence the empirical failure of Marshall's assertion⁵³.

For this reason, economic inquiry is still popularly expected to provide the best outcome for society and a level of justice for all participants. These are moral goals. Even Pareto's optimality hypothesis is a moral optimum, though it is less evident if real markets can achieve it⁵⁴.

History appears to be studded with examples of failures in the economic endeavour. Almost a century ago Rogers used sound historical methods to study six centuries of work and wages in England. His conclusion was that over the period of his study, the highest level of real wages occurred at the close of the fifteenth century and up to the first quarter of the sixteenth. Although Rogers was no friend of the Catholic Church, his observations placed the high point of wages at the very close of the Catholic era in England (Rogers 1884/1949) and also the end of the period dominated by non-market price fixing using the principle of the just price.

His observations also challenge the relevance of GDP per capita as a measure of the success of an economy. If GDP per capita is increasing while wages are falling in real terms, it must be the result of a significant polarisation in the distribution of wealth. The seventeenth and eighteenth centuries saw England a world economic leader. However, the establishment of New South Wales, Australia's first white settlement in 1788, was not stimulated by economic opportunity. It was rather necessitated as a sink for destitute Englishmen, Scots and Irish who were forced into lawlessness through lack of participation in the massive wealth generated in their own economy. At the close of black slavery in North America, Negro slaves enjoyed a significantly better

⁵³Marshall believed that economics would be more reliable in realising the common good by being based on data drawn from observations of men's actions which could be seen rather than considering what was in men's hearts, which could not be observed. As well as establishing positivism, it made intention in economics irrelevant.

⁵⁴Pareto optimality suggests that the optimum level of material welfare occurs when the market is so frictionless that at any given point there are no opportunities for trade such that the sum utility of the trading parties could be improved. That is, the best distribution of utilities across the community comes through the operation of a frictionless (totally unfettered) market. Because Pareto optimality is grounded on belief in prices as utility indicators, markets that price otherwise could not reliably achieve his optimality. There are considerable difficulties linking prices to utilities in any precise way.

standard of living than did free working people in Britain. Despite the current tendency to ignore the reality of Dickens's portrayal of English life for the common person, it stands as one tiny, though highly visible, indication of the moral failure of the economics that Adam Smith championed half a century earlier.

Adam Smith's economic theory was self consciously moral, but its moral system was based on Enlightenment foundations. His biographers proudly point to the well known fact that he wrote little in his *Wealth of Nations* that was not first discussed with his friend David Hume. Although Smith wrote on morality, his philosophical position is essentially a reflection of Hume's. Hume was very clear in asserting that human nature was knowable by observing what humans did. Hume's moral system was premised on the assumption that humans are guided by an internal moral sense that interprets events as experienced, that "*crime or immorality ... arises entirely from the sentiment of disapprobation*" (Hume 1777/1975, pp291-2)⁵⁵. This was essentially adopted by Smith when he asserted that it was "*the sentiment or affection of the heart, from which all action proceeds and upon which its whole virtue or vice depends*" (Smith 1759). Smith observed self-interest as the mainspring of commerce and concluded that it was not only a part of human nature, but that it mysteriously guided commerce towards the optimum outcome in his metaphor of the *invisible hand*. Smith provided a moral validation of positive market behaviour that was grounded in a conception of human nature⁵⁶.

That Smith could have made such a statement in the face of a massive rupture in distributive justice is not nearly as extraordinary as the way that it has been repeated down to the present day. Promoting an economic position that is in practice indistinguishable from Smith, Novak (1984) was content to assert that "(t)oday, seeing the incredible vitality of free economies - by which, for example, the United State doubled its gross national product in real terms between 1960 and 1983 - we see full well that the elimination of grinding poverty is within reach" (p.47). Despite this encouraging news being true, it failed to recognise that the income gap between top and bottom 20% also doubled over roughly the same period (Douthwaite, 1992) and that the real income of US high school graduates as a class has been falling (Gottshalk, 1997). It is hard to recognise solidarity or the common good in this data.

⁵⁵ Hume's *Enquiry Concerning the Principles of Morals* was first printed 1748 and was a tempering of a similar position expressed in his *Treatise of Human Nature*, 1739-40. The quote taken here is from the posthumous edition.

⁵⁶(Buckle 1991) expanded the Humean notion of human nature, asserting the continuation of the Realist tradition science being based on the understanding of natures. The difference was that human nature was observed empirically rather than developed through reason.

The common good was best served by the pursuit of self-interest by each individual in asserted Smith. The criterion of the common good makes this a moral assertion, though many have found its validation of self-interest quite extraordinary. Self-interest, or more plainly *greed*, is normally considered to be a vice. At best, there may be an argument based on Aristotle's Golden Mean that would suggest that excessive self-interest is vicious, but moderate self-interest is virtuous. Virtue here relates more to the strict moral definition that links virtue to those actions that benefit humanity. Indeed, a deficiency of self interest, say as a lack of a sense of self-preservation, can be hazardous, making both deficiency and excess vicious and completing the familiar pattern *virtus stat in media*.

Virtuous self-interest relies on its ability to achieve the common good. Smith left the economic actor free to subjectively assess this moderate position through direct perception of personal moral sentiment. The failure of Hume's moral sentiments as a moral system are extensively recognised, effectively freeing persons to pursue any desire - the bank robber and the rapist both consider their acts to be most attractive, hence their moral sentiments are aligned to what are generally held to be objectively immoral behaviours. Moderation with self-interest is therefore unlikely if the test is sentiment and even the notion of moderation is not prominent in Smith's text itself. Rather, by stressing the virtuous aspects of self-interest, Smith tended to portray it as an absolute good and paved the way for the eventual popular adoption only a decade or so ago of the notion that *greed is good*.

Smith's metaphor of the invisible hand asserted that the common good followed from individual self-interest. Given the evidence of his era alone, even the empiricist should have been wary. However, the decision makers and theorists tended in large measure also to be the beneficiaries of the resultant mal-distribution and their perception in this area was deadened somewhat (Roll, 1942). If self-interest is virtuous and is the foundation of the market, then the market becomes the natural moral floor for economics, and no further enquiry in this direction is necessary, thereby freeing economic theory to develop in other areas. This is the position that is generally held today.

Smith's invisible hand can be interpreted more successfully as a behavioural reality, rather than a moral or metaphysical one. Self-interest does provide a stimulus for movement between market positions. The best market positions are those affording the greatest economic rents. Fortunately, this tends to result in a distribution of suppliers roughly according to a community's needs⁵⁷. However, this distribution of supply does

⁵⁷A concentration of suppliers defuses the opportunities for economic rents, whereas an absence of competition facilitates it.

not necessarily mean the elimination of economic rents, neither theoretically nor in practice, and it has been shown that market failure indicates moral failure and is indicated by the existence of economic rent. Likewise, Pareto optimality, while stressing optimised utility, is silent on economic rent, as is the utility maximizing consumer at the end of the economic process.

The split between economics and morals is one that is now well accepted. The neoconservative position is largely based on asserting that economics provides tools that inform the moral decision-maker, implying that the former has negligible native moral content. This is entirely consistent with economics as behavioural science. To some extent, the lack of moral structure within the discipline of economics creates the necessity for external review. Michael Novak is perceived by the community more as an economist than a moral theorist, but although his audience is usually from the commercial sector, his work is primarily not economics but morals.

The subjection of behavioural economics to review from without has evoked strong objection from within. The neoconservatives have constructed a subtle and credible moral support to overcome this external criticism through a "*...synthesis of free-market economic science and the science of moral theology ...*" while striving "*...to maintain the rightful autonomy of both...*" (Gronbacher 1998, p. 3). This would seem to be an explicit expression of the latent tension. Economics has always been understood to be ordered towards a moral purpose. Rourke (1997) has provided a useful review of this reality in his comparison between the essential elements of the neoconservative position and the more conventional philosophical understanding of the key issues as explained by Yves Simon. Behavioural economics may minimise its moral element, but it has been shown that this is still its most sensitive fundamental component.

In practice, ignoring the weighty theoretical defense of liberalism generally, the neoconservative position rests on the recurring theme that the free market has been responsible for the greatest economic successes in history. This is a simple positive validation based on evidence. Objective economic data apparently proves that *laissez-faire* markets result in the most successful provision of the material dimension of the common good. Much rests on this assertion, but it is essentially a moral, or possibly political, observation and it explains the appropriateness for review by these sciences. It provides the fundamental credibility for the behavioural science of economics. Without it economics could be the science of robbery and have every bit as much behavioural validity.

If economics relies on its moral effectiveness for its validity, then the more interesting investigation would be the exploration of how deeply economic behaviour

is penetrated by moral issues. Like other practical sciences, economics must contain objective moral reference points, though it would appear that most of the accepted theory of this century has tried to depreciate this possibility. The fact that the endeavour has failed to produce a coherent body of theory should be taken as evidence of the shortcomings of this approach.

6.4 CAPITALISATION AND THE RATE OF PROFIT

While the market provides a social estimate of exchange value, there are several additional methods of price setting, of which marginalist theory and cost-based pricing are but two. This is important because they provide the people in the market with rational reference points that are more concrete than subjective notions of utility. Capitalisation is one of the most important of these, especially as it is very important in the valuation of land. This section will review capitalisation, especially with respect to its theoretical implications.

If an item of capital that costs P returns an income R , an important factor in considering its relative investment worth, and hence its attractiveness for purchase, is its rate of return i . These variables are related through equation 6.1 as follows:

$$i = R \div P \qquad \text{Eqn. 6.1}$$

In a mature market, the rate of return is well known and the potential income from the asset will also be known. Hence the unknown is the price P . Equation 5.1 may be re-arranged to make P the subject as follows:

$$P = R \div i \qquad \text{Eqn. 6.2}$$

A long standing question in economics regards which of these relationships is prior, which is to say, is it price or rate of return which is the independent variable. This is a very difficult question for positive economics because both rates of return and prices exist in established markets and appear interrelated. Knowledge of the return R appears less contentious, though it raises a separate set of issues that will be considered elsewhere.

If the rates of return are the dependent variable, then price must originate elsewhere and capitalisation is not relevant as a valuation tool. This may be reasonable, but it does not inform the market determination of price, and is therefore only useful as a relationship for computing rates of return. Conversely, if price is the dependent variable, then some method must be available for establishing the rate of return.

This problem is better understood when put in concrete terms, consider an item of capital, say a printing press. A printer may know how much work a particular machine may be able to do, and its worth. From that data the printer can estimate the revenue that the machine will generate. Normally the printer would be expected to compare this to the price that the press can be purchased for and decide on whether the machine will be adequately profitable.

Since the printer cannot alter the output of the machine or the value of its product, the revenue is fixed. The price is also taken to be a given, in that it would be unusual to go into a machinery merchant and find price tags of 13% or 18%, being the rates of return available from investing in particular machines. So long as capital assets, such as printing presses, come with price tags in money units, then the rate of return would seem to be the dependent variable.

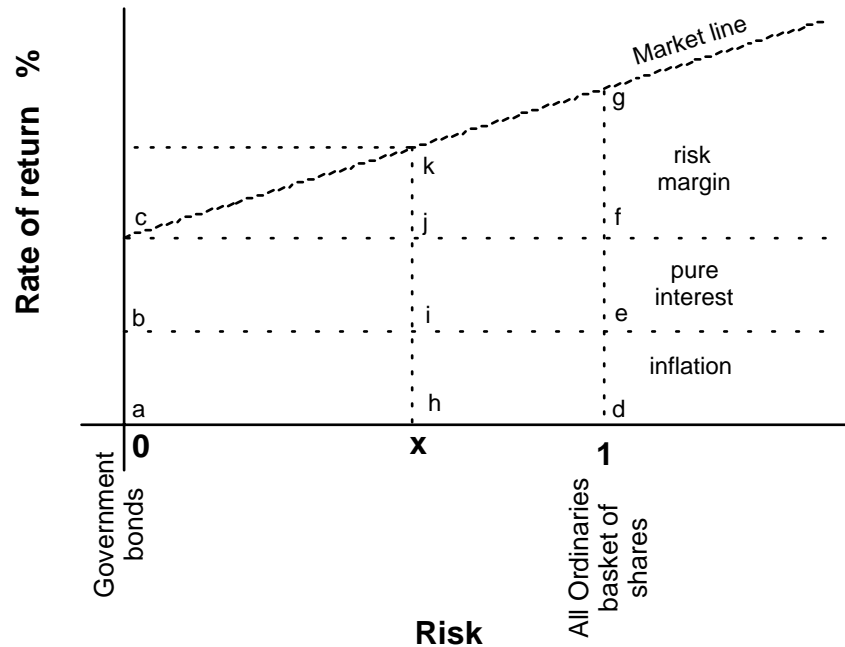
Conversely, the manufacturer of the printing press, in deciding on undertaking its production, will need to assess whether or not it will be profitable to build. This means that the sale price will need to be estimated and compared to the cost to build to decide if the manufacture of the machine is worthwhile. To estimate the machine's sale price the manufacturer may estimate the value of the printing the machine can produce and use this with an estimate of the least rate of return that the printer will accept and use this data to set an asking price for the machine.

Despite Western expectation of explicit prices for most manufactured goods, the rate of return does appear to be the prior parameter. This is apparent in finance theory where the financial value of a capital asset is defined as the present value of its future return (Wilson, 1990). It is also apparent in real estate where there is no way of setting land price through cost, forcing land price to be composed of a participation in its use value. The origin of rent and land price will be examined empirically in chapters 11 and 12.

The priority of the rate of profit as the independent variable appears to be strongly supported. In its absence, the market would only have costs to base prices on, which does not suit land and other financial assets. It is congruent with the practical applications of finance theory. Several major theorists supported this perspective. Sraffa (1960/1975) recognised that the rate of profits was an independent variable '*... susceptible of being determined from outside the system of production, in particular by the level of the money rates of interest*' (p.33). Panico (1988) cited several major theorists, including Keynes and Marx who thought likewise. This is both useful and problematic.

The capital asset pricing model (CAPM) is a useful theory for understanding Sraffa's assertion. The CAPM locates the values of all financial assets along a single function that links rate of return to risk, as shown in Exhibit 6.3.

Exhibit 6.3: Capital Asset Pricing Model



The CAPM model suggests that all financial assets exist on a continuum of returns that begins with the risk free rate of return on money loans and increases with increasing risk. Government bonds are the most secure fixed interest (debt) security in the market and are used as the closest practical approximation to the risk free rate of return available. The gradient of the market line is set by the differential in return between government bonds and the average return on the stock market, the all ordinaries return. The all ordinaries return is given a risk value of 1.0 and all other securities are rated against this reference point. The CAPM links fixed interest securities with equities and other income producing assets. It sets the rate of return that underlies normal profit. It is assumed that if a financial asset out performs expectations derived from the CAPM, then it will experience capital growth. The capital growth will increase its price to the point where the rate of return is once more normalised.

Normal profits are therefore based on expectations of a reasonable rate of profit for a particular level of risk. Fixed interest securities have low risk and hence a lower return, whereas equities are more risky and warrant higher returns. Land would appear to be

located on the CAPM somewhere between the two fixed points, however that is highly dependent on the particular situation⁵⁸.

The CAPM construction of rates of return is useful for understanding rates of return, for quantifying normal profits and for grounding capitalisation, but it introduces an additional problem. This is the question of what explains interest rates. While this may appear to be an issue quite remote from the social economy of land, it is surprisingly relevant. If the price of land is best understood as the market determination of its appropriate capitalisation, which is well accepted for productive land (commercial, industrial and retailing land) and capitalisation is a function of the rate of return, which in turn is based on interest rates on money, then land value is a function of money interest rates.

The rate of return (rate of profit) for a particular asset, say with a riskiness of X in Exhibit 6.3, will be h-k. Several theories have been proposed to explain the rate of return and these will be briefly reviewed. The CAPM itself suggests that part of the return is a margin for risk, a type of insurance, this is represented in the exhibit as j-k. While its value could be expected to average zero as a result of unsuccessful assets absorbing the premium returns from successful ones, the difficulties in concrete evaluation make this assertion impossible in practice. It is sufficient to accept that the risk gradient is necessary to attract investment in useful, but risky investments. Keynes was suspicious of the degree of rationality applied in determining these margins, believing *"The value of a company's shares, or even its bonds, will be found to be sensitive to a degree, which a rational observer from outside might consider quite absurd, to short -period fluctuations in its known or past profits."* (Keynes, 1971, 322)

Similarly, the inflation premium theory, suggests that apparent rates of return include a component that merely compensates for the loss of value from inflation. This is represented in the exhibit by h-i. It would appear that it is reasonable for an investor to be compensated from losses emerging from the investment, which is what inflation represents⁵⁹.

The remaining component, i-j, is pure interest. It is best interpreted as the expectation of the investor of a return. It is also explained in terms of *time preference*. and may be refined using tools such as the yield curve to explain the way that time preference is related to liquidity. The difficulty with all of these is that they all reduce to an explanation based on no more than the desire of the owner of money wanting

⁵⁸Investment performance of land is heavily related to its social context, especially technology, population and economic growth. Some land-related investments such as debt leveraged property development and resource exploration are very risky.

⁵⁹This would be an example of the Medieval allowance for the extrinsic title to a return on a money loan due to *Damnum emergens* (losses emerging).

more in return for a loan than the value of the loan and the willingness of the lender to oblige.

The modern Western mind has no difficulty with this practice as it has been a part of its commercial life for centuries, but other cultures and times recognise it as contrary to the purpose of economics. A little reflection shows that a theory of interest, based on no more than the inclination of the owners of money to want a profit being supported by those needing money to supply it, suffers from the same susceptibility to a charge of exploitation as the upward sloping supply function in the absence of the marginalist theory of price.

The arguments supporting the return of more money than was loaned are complex. The most convincing argue that money is a productive form of capital and therefore warrant a return. The issue is complicated by the fact that actual interest rates include risk and inflation components that would appear to be quite reasonable⁶⁰. If the pure interest component of apparent interest rates was actually productive, then its productivity could be measured, and interest rates could be shown to be tied to this productivity. The difficulty here is partly the circularity that tends to emerge from the capitalisation process, but mainly the empirical fact that interest rates are not set in this way.

Despite extensively developing the economics of using debt, Keynes saw that the determination of its price was actually a *"psychological phenomenon"*⁶¹ outside of the actual bounds of the economy. He recognised that *'Any level of interest which is accepted with sufficient conviction as likely to be durable, will be durable; subject, of course, in a changing society, to fluctuations for all kinds of reasons round the expected norm.'* (Keynes, 1973, p.203). The acceptance by a society of a particular regime of interest rates is all Keynes saw as necessary for their adoption. Social acceptance between lenders and debtors reflects back to market processes, especially Schmolter's notion of market value as the result of summations of psychic balances between the parties.

The explanation of interest rates, especially the pure interest component, has only been satisfactorily attempted in this century and then only within modern methodological parameters⁶². Interest rate determination constitutes a rule bound aspect

⁶⁰The currently popular view on interest is that it is licit up to a point. Unfortunately the threshold point is the critical issue. If the market rate covers only inflation, risk and other possible licit grounds the market interest rate is not pure interest, or usury at all and there is no argument.

⁶¹His expression for the determination of interest rates (Keynes, 1971, p.322)

⁶²The neoconservative movement would appear to be an exception, asserting a theological and sometimes Thomistic base. Chafuen (1986) gave a 'Christian' history of the dissolution of the moral prohibition of usury by the late-Scholastics, but close study reveals that his argument is based largely on common practice. Like the neoconservatives, his methodology is based more on Smith and Grotius than Aquinas.

of the behaviour of the players within the economy that is amenable to positive theories that display moderate predictive success⁶³. The notion of time-preference may describe a positive phenomenon that is amenable to observation, but remains difficult to justify. Western history has been divided over the ethical validity of pure interest, with the practice of taking interest on loans (usury) being considered immoral and often illegal for about half of the two thousand years of Christendom. Aristotle was likewise critical of money lending and his reservations found a ready home in Medieval thought that had a tradition rejecting the practice well before St. Albert the Great re-introduced Aristotle to the West. It took Calvin to break the theological prohibition on usury and slowly the late Scholastics tempered their position to bring it more into line with common practice (Chafuen, 1986).

The difficulty with usury is its evident lack of connection with the productive process. While Aristotle focused on this aspect of money (as sterile) its real problem concerns equality of values, especially through the transactions that make up a loan and its repayment. The practical issue is the way that interest rates cannot be grounded on an objective base, but are always resolved by extra-economic forces, even if these use the market as a forum.

Without exploring the arguments surrounding usury, it is sufficient to recognise that capitalisation is grounded partly on this difficult foundation. If pure interest, as usury, were to be removed from Exhibit 6.3, the rate of return on investments anywhere on the CAPM line would only just cover risk in real terms (i.e. inflation adjusted). This would appear to explain why it was only in the middle of last century that permanent returns on equity capital gained legal acceptance (Goyder, 1993). The point here is that culturally capitalisation is relatively immature. This is not to say that it has not been understood and employed for some time⁶⁴, but that the issues surrounding it still carry some controversy.

Money interest may therefore represent a form of super-normal income. If it does, then all returns that may be located within the CAPM share in this species of income. It will be seen in chapter 13 that these appear to exist as a participation in land rents.

Consideration of Ricardo's rent theory in chapter 10 relies heavily on the inclusion of normal profits as a licit return to capital and hence comprises part of necessary subsistence income to non-land factors. For the purposes of this study it will be

⁶³See Grieder (1987) for an account of the effectiveness of theory in the Federal Reserve's direction of the US economy.

⁶⁴Petty's resolution of the problem of the Par regarding the value of land was solved using the principle of capitalisation. However, it was significant that his explanation explicitly made the performance of land parallel the performance of money loans. Consequently, his explanation was dependent on the social acceptance of money interest.

accepted that normal profits are recognisable and quantify, which would appear to be a reasonable positive fact.

Finally, land sale price will be seen in chapter 12 to follow from productivity via rents, but this is dependent on the capitalisation rate. For these reasons it can be seen that capitalisation and the rate of profit play an important role in the economics of land. Because of the ethical and social issues surrounding the setting of the rate of interest, it would appear that these issues will also impact on the social economy of land.

6.5 CONCLUSION

The market is still held as the moral floor for economics, largely on the basis of Smith's invisible hand and to a lesser degree on concepts such as Pareto optimality and utilitarianism. Each of these has been shown to be problematic. Modern economics passes lightly over its moral foundations in order to focus its primary attention on its positive behavioural aspects. In terms of this latter focus, i.e. as behavioural science, it must be recognised that it is moderately successful.

The moral failure of market economics is positively evident in its failure to achieve reliable guide-lines for action leading to distributive justice and the common good. This failure can also be traced further into the assumptions underlying the very construction of the primary market functions of supply and demand.

The market may be interpreted as a social phenomenon where the balance of personal or political power determines the outcomes. Market price may therefore be positively interpreted as a social artefact, the result of social forces. This places it outside of what is strictly considered economic, as is evident in the failure of economics to adequately explain market functions. Price by capitalisation appears to the intelligible as a function of economic variables, but these break down on close examination into a similar origin. While revenues have not been reviewed, the rate of return which is critical for capitalisation of land and other capital assets, is understood by major theorists to originate from a similar constellation of social and psychological workings.

6.6 Contribution to the Support of the Thesis Hypotheses

	Hypothesis	Conclusion
1.5.6	The construction of modern market theory is evidence of its reliance on morals.	Supported
1.5.7.1	Modern market theory is based on a positivist methodology, yet fails positivist tests.	Supported
1.5.8	Modern market theory is successful as a species of social psychology.	Supported
1.5.11	Commodity use value lifts price above normal costs in current market practice.	Supported

Chapter 7 Survey Design and Procedure for a study of community attitudes regarding price setting practices

7.1 INTRODUCTION

This chapter outlines the design and procedure adopted to study social attitudes towards price setting.

It has been seen that there are considerable problems associated with adopting the market as the mechanism for determining price. The theory of supply is deficient because of the unrealistic assumptions associated with the marginalist theory of the firm, and even the gradients of the supply and demand functions are only valid under conditions of market failure.

The positivist response is to assert that this is of no consequence, so long as the theories produce reasonable predictions of future market behaviour. While this may be sound social psychology, it fails to meet the ethical criteria that appear to be widely understood as composing at least part of set of criteria for a sound economics.

Discussion of ethics in the context of economic behaviour often invokes charges that one is asserting unreasonable normative beliefs. The implication is that ethical restraint is abhorrent and dysfunctional. Langholm (1969) has presented a strong case to suggest that cost-based pricing is more efficient and several authors, including supporters of the free market have recognised that the market is not rational⁶⁵. It would appear that it is market pricing that is dysfunctional, even in terms of its own theoretical structure. This leaves the objection that ethical restraints of free market behaviour are abhorrent.

The proposition that ethical restraint of market pricing is abhorrent infers that the absence of restraint is not abhorrent, i.e. that liberal market determination of price is socially acceptable. The key ethical aspect of market determination of price has been shown to be the fact that the market often settles on prices that are significantly above the normal costs, which afford economic rents to the vendor. It is principally the strength of demand that determines how far above the normal production costs the market price can be set. The issue is therefore related to the matter of whether economic rents are commonly considered to be acceptable by the community.

There are three questions that this issue raises:

⁶⁵For example: Samuelson (1975) noted that the the shapes of the market functions contradict the assumption of efficiency, Jones (1976) explained why the marginalist theory of the firm was necessarily flawed, Working (1927) explored the problems with observing demand, and Wicksteed (1914) redefined the supply function as no more than the demand function of those who own the commodity offered for sale.

- 1) Should prices be related to costs? Say, if costs fall, should prices follow?
- 2) Should demand be allowed to draw prices higher?
- 3) Do purchasers have adequate negotiating power in the market?

The most direct way to study whether ethical restraint in the market is in fact considered negatively by the community would appear to be to ask the community. This is the sociological approach to the determination of ethical issues. While it is incapable of determining the nature of the issues in an absolute sense, it is capable of providing a form of jury decision that conveys the moral judgements of society⁶⁶.

A number of difficulties immediately appear. It is not possible to ask the entirety of the human race, and in any case the choice of questions may produce response aberrations that may cloud the underlying attitudes. The following attitude study has been developed with the aim of minimising these problems.

7.2 AIM

The study aims at observing community attitudes to pricing issues through the use of a simple questionnaire administered to a sample group.

7.3 HYPOTHESIS

Popular sentiment does not support pricing from use value (Thesis hypothesis 1.5.7).

7.4 METHODOLOGY

An empirical methodology has been adopted in order to survey community sentiment as found in modern social science research. This means that the attitude survey will be constructed with the goal of observing as accurately as possible community sentiment with a minimum of reliance on understandings of human nature. The realities of human behaviour, in terms of dishonesty, various biases and other limitations will be accommodated as far as possible in a way that does not distort the results. Discussion and interpretation will include consideration of broader issues.

Interpretation of the data will rely on statistical analysis, especially the use of non-parametric evaluation using the Chi squared (X^2) statistic. Statistical inference will use standard acceptance levels between 0.1 (10%) and 0.001 (0.1%) with discussion of

⁶⁶A discussion of the appropriateness of this approach and its significance for the meaning of society is found in Devlin (1965). An important difference between sociological survey and jury determination is that in the latter a unanimous result is expected, whereas in the former a majority suffices. The difference may be valid to the extent that a criminal case, because of its gravity, requires a higher level of agreement and it may be expected that the jury is in no way connected with the criminal inclinations under scrutiny. In the case of more contentious social issues it is more difficult to find a totally disinterested jury who have a sound understanding of the issue. Self-interest may therefore be more difficult to exclude compared to a criminal jury panel.

significance of the acceptance levels in the context of their particular application. By using a substantial sample size and standard statistical theory, the results of the empirical survey may be generalised to the wider community. It is recognised that because the sample is drawn from the Australian, community it represents a Western cultural position.

The statistical analysis assumes that reliable inferences can be made from observations of samples of the population regarding the population as a whole. The normal acceptance level adopted in this study will be 0.001, which is understood to mean that the trends exposed in the sample data have a probability of 1/1000 of being untrue. While this may appear impressive, two reservations must be kept in mind. Firstly, even nine hundred and ninety nine chances in one thousand of being true is still not a certainty, and it may be that the sample does not accurately represent the entire community. Secondly, the analysis only proves significant biases in the data, in this case that means that it indicates majority attitudes agreeing or disagreeing with a set of statements. This does not mean unanimity.

Discussion will locate the results within the broader theoretical methodology appropriate to the understanding of human nature. In particular, the connections between the empirical findings and broader methodological conclusions will be explored.

7.5 METHOD

Research assistants administered a questionnaire involving ten questions relating to three hypothetical, but realistic, situations related to pricing. The assistants were not briefed on the purpose of the study in order to minimise experimenter bias. A total of thirty four research assistants were used to further reduce the possibility of bias derived from the questioners.

The questions were all in the form of statements that were answered using five point attitude intervals labelled *strongly disagree*, *disagree*, *neutral*, *agree* and *strongly agree*. There were no open ended questions. Responses were coded with the numerals 1 - 5, though it was recognised that they remained nominal only. Collation was by frequency counts by question. The question sheet is shown in Exhibit 7.1

The research assistants administered the survey personally and recorded results on to result sheets as shown in Exhibit 7.2. For brevity in handling the data, each result sheet could record data from several respondents which may have introduced the possibility of experimenter effects towards the end of the sheet. Since each assistant was only required to survey ten respondents and they were instructed not to communicate

previous responses, this was not considered to be a major problem. Analysis of the data for possible serial correlation within sets has not been attempted at this stage.

Confidentiality and survey quality control constitute factors in survey management that are often in opposition. It is necessary to afford respondents confidentiality when supplying their personal beliefs, but this compromises supervision of the survey assistants who may avoid the toil of performing the interviews and simply invent responses. This survey overcame this problem by asking that respondents voluntarily supply contact telephone numbers on the response sheet in random order. They were asked to do this on the understanding that they may be contacted to check that they did in fact participate in the the survey only. Since the response sheets contained space for ten respondents and the space for contact numbers was a 3x5 matrix of spaces, it was considered that they would be sufficiently randomised. A sufficient number of contact numbers were gathered to indicate reliability. Contact numbers were not entered into the computer spreadsheet.

The data gathered was entered into a computer spreadsheet and responses collated. The data was also simplified for analysis into a dichotomous set of responses by eliminating the neutral responses and summing the pairs of disagree and agree responses into single categories. By considering the data in dichotomy form, the possibility of neutral responses producing phantom significance levels was removed. Analysis considered both the five point and dichotomous data sets.

Exhibit 7.1 Question Sheet

1999 Consumer Preference Study

In each of the following, try to imagine your responses to each of the hypothetical situations and answer the questions using a number from 1 (strongly disagree) to 5 (strongly agree):

SITUATION 1

The financial press reports that, despite the costs of building materials remaining stable, due to strong demand building prices have risen strongly over the last six months and building companies are currently making record profits. It happens that you are taking quotes for the construction of a new home on land you previously acquired and have noticed that the quotes are substantially greater than you had expected.

In your opinion:

- 1) You would be pleased to hear that Australian industry was thriving.
- 2) You would take a more determined negotiating position before accepting any quote.
- 3) You would feel powerless and wish you had locked in the project while profit levels were modest.
- 4) You would be critical of whether there was any real need for the higher price.

SITUATION 2

Imagine that both major telecommunications companies completed independent studies of demand for telephone services and have found that it has increased significantly. Over the same period technology improvements have increased call capacity and reduced costs. Because call capacity is considerably above current usage, the system could carry significantly more calls at a negligible increase in total running costs.

On the basis of these findings they both independently choose to leave pricing unchanged.

In your opinion:

- 5) They have failed to meet their responsibility to their shareholders by not increasing prices given the opportunity afforded by the strong demand.
- 6) They should pass lower costs on to consumers as lower prices.
- 7) More suppliers of telecommunications would force the prices down to reasonable levels.

SITUATION 3

While on holidays you recognise your local fruit and vegetable grocer as he steps from his new Mercedes. He tells you that although he only has interests in his one shop, because of the neighbourhood it is in, he has no trouble setting prices at a very profitable level and has done so for some years. He confides that although he started with very little, he is now a very wealthy man, though he still maintains a humble appearance whilst at work.

- 8) You would feel proud to be dealing with such a successful supplier.
- 9) You would be inclined to ask for better prices.
- 10) You would be inclined to change suppliers, even if it meant some inconvenience.

Thank you for your participation.

Note: Situations referred to in the above are hypothetical and do not reflect actual situations or the behaviour of any industries or organisations.

The basic statistical analysis used X^2 analysis. This non-parametric statistical method is most suitable for categorical frequency data, such as found in this survey. It tests the inferential strength of the imbalances found in the data and gives a simple acceptance

test based on the level of reliability sought. The acceptance level is fundamentally an arbitrary probability of accepting an incorrect inference. Common acceptance levels in social science research are 0.05 and 0.01 (5% & 1%) meaning an expected level of error of one part in twenty and one part in one hundred respectively. Acceptance levels of 0.1 (10% chance of erroneous inference) are sometimes accepted. This study found either negligible biases or biases significant at the 0.001 (0.1%) level which are very strong for this type of study and indicate either very strong or very reliable sample biases, leading to good confidence in the results.

The results were prepared in table form. Discussion included integration of the findings with other aspects of economic and behavioural theory.

7.6 SUBJECTS

Three hundred and forty subjects were surveyed. The only selection criterion that was adopted was home ownership. Data on employment, occupation, salary, or other personal characteristics were not gathered. Subjects were drawn from the Sydney metropolitan area.

The subjects could therefore be expected to be stable adults within a Western cultural context. This was considered to be a reasonable sample profile because Western attitudes were being sought and a mature but diverse set of attitudes. The focus of the survey was the acceptability of demand as a basis for price, which is a key aspect of market theory. For this reason, subjects drawn from a Western culture were considered most appropriate because of their familiarity with free market economics in practice.

The three situations covered a broad range of pricing situations and it may have been possible that some respondents were involved in occupations associated with the situations. No attempt was made to identify such possible associations or to screen respondents with respect to possible identification with specific situations. While it may have been useful to have been able to perform analysis on the basis of respondent association with the situations, this has not been attempted. It has rather been assumed that the random sample will have caught a representative component of associated respondents.

7.7 THE QUESTIONNAIRE

The questionnaire is reproduced in Exhibit 7.1. It consisted of three situations as follows:

Situation 1 (real estate building pricing): This pricing situation was chosen because it is a common area for negotiation and the gathering of competing quotes. It is also known to be an area where contractors do increase their prices in periods of elevated demand. The situation explicitly avoided the land cost component.

Respondents were asked to comment attitudes associated with their general view of business success coming from demand, inclination to negotiate harder when aware that prices contain economic rents, perceptions of negotiation power, and the validity of demand driven price.

Situation 2 (corporate consumer goods/services pricing): This situation was chosen because it has evoked widespread debate in recent times and pricing is commonly believed to be demand based. In Australia, the two major telecommunications carriers are both very profitable.

Attitudes concerning corporate responsibility were explored, to shareholders and customers. The issue of technology based profits flowing from cost reductions was surveyed. The notion of competition as a strategy to ensure fair play was surveyed.

Situation 3 (local consumer goods pricing): When the commercial relationship is more personal a different set of factors dominate. This situation tests similar issues to the earlier ones, but in the context of a local exhibit who is evidently profiting at the local community's expense. Contrast between results from this situation and the previous ones exposes the significance of inter-personal issues and suggests cultural expectations that exist at a less formal level.

Response Sheet and data collation

The responses were recorded on a separate sheet by the research assistants as shown in Exhibit 7.2. The response sheets allowed for compact collation of the data and independent recording of respondent contact numbers. The data was entered into a computer spreadsheet (using Microsoft Excel).

The research assistants were briefed with an outline of how to perform their task, including experimental design issues. They were not briefed on the purpose of the survey or the anticipated results. Debriefing included canvassing for difficulties and the promise that the results would be circulated.

Feedback on data collection suggested that there were no significant difficulties encountered in obtaining the data.

Exhibit 7.2 Data Sheet

16553		Data gathering exercise									
		<i>Respondent</i>					Record a number 1-5				
		1	2	3	4	5	6	7	8	9	10
Q U E S T I O N	1										
	2										
	3										
	4										
	5										
	6										
	7										
	8										
	9										
	10										
Respondent contact numbers, do not record in order											
Contact numbers for verification that survey has been conducted only											

7.8 TIMING

The survey was administered over April and May 1999.

7.9 SUMMARY OF SURVEY PROCEDURE

This chapter has described an attitude study consisting of ten questions regarding three situations involving pricing issues. The aim of the survey is to observe community attitudes regarding price, to test the hypothesis that popular sentiment does not support pricing from use value.

The questionnaire will be administered to 340 subjects who are home owners in Sydney. The results will be collated using a computer spreadsheet and analysed using the Chi squared statistical test.

Chapter 8: Results and Discussion for a study of community attitudes regarding price setting practices

This chapter lists and discusses the results of the survey of community attitudes described in the previous chapter. In analysing the survey it draws conclusions regarding the degree of community acceptance of demand based pricing.

8.1 RESULTS

A total of 340 responses were obtained. No particular difficulties appear to have been encountered by the research assistants, suggesting that respondents generally understood the questions and were comfortable participating in the study. The data were entered into a spreadsheet and the frequencies of each response computed as shown in table 8.1. Chi squared (X^2) statistics were computed for the results and the significant results tabulated.

The X^2 statistical analysis tested the hypothesis that there was a systematic bias in the results. The null hypothesis in each case was that there was no bias in the results. In the five point test, the null hypothesis would have been that there were equal responses in each response category. In the dichotomous test, the null hypothesis would be that there are equal agree and disagree responses. The alternate hypothesis in each case did not specify which response was sought, hence it is necessary to review the results by checking first that the results show a significant bias, and then which direction the bias runs. The ratio of agree to disagree responses has been computed for the dichotomous results to indicate the strength of the bias.

Various acceptance levels have been given for each test, usually ranging from 0.05 to 0.001 (5% to 0.1%). Acceptance of the null hypothesis was taken from the 5% acceptance level, while its rejection was generally at the 0.001 level. Question 1 and some of the secondary tests for independence used the 0.1 (10%) and .01 (1%) acceptance levels and these are noted appropriately. The 0.001 acceptance conveyed strong confidence for those results which supported the alternate hypothesis, while the softer criterion for accepting the null demonstrated that those results that failed to reach significance in fact displayed very little attitude bias. The acceptance results are tabulated below the respective X^2 computations and are coded as follows:

- A:** Significant bias found for the agree response
- D:** Significant bias found for the disagree response
- N:** Significant bias found for the neutral response
- X:** Failure to find attitude bias

Exhibit 8.1 Demand Survey Results by Question

Analysis by five point attitude scale

	1	2	3	4	5	6	7	8	9	10
strongly disagree	57	21	60	23	76	30	39	48	45	79
disagree	72	26	63	40	86	41	49	67	52	70
neutral	94	67	96	78	99	57	67	109	89	69
agree	65	80	75	113	47	89	100	64	100	70
strongly agree	52	146	46	86	32	123	85	52	54	52
X^2_{obs}	15.9	150.0	20.7	77.3	45.4	84.7	37.0	34.6	36.0	5.7
df=	4		N= 340			E= 68				

NUL	X^2_{crit}									X
5%	9.49									
1%	13.28	N								
0.10%	18.47	A	N	A	D	A	A	N	A	

Dichotomous analysis

total disagree	129	47	123	63	162	71	88	115	97	149
total agree	117	226	121	199	79	212	185	116	154	122
sum	246	273	244	262	241	283	273	231	251	271
ratio: A/D	0.9	4.8	1.0	3.2	0.5	3.0	2.1	1.0	1.6	0.8
X^2_{obs}	0.585	117.4	0.016	70.6	28.59	70.25	34.47	0.004	12.94	2.69
df=	1									

NUL	X^2_{crit}	X	X		X			X
5%	3.84							
1%	6.63							
0.10%	10.83	A	A	D	A	A	A	

In addition to analysis by individual response, the totals for both the agree and disagree responses were aggregated and analysed separately. This eliminated the neutral response from contributing to the X^2 statistic. While it reduced the sensitivity of the analysis to the intensity of attitude, it removed the possibility of a high neutral frequency contributing to the X^2 statistic leading to the erroneous appearance of a marked attitude result. The significance of this analysis will be discussed within discussion of the specific questions.

8.2 DISCUSSION

The results will be first reviewed in terms of the individual situations and questions, and then the global implications will be summarised.

SITUATION 1

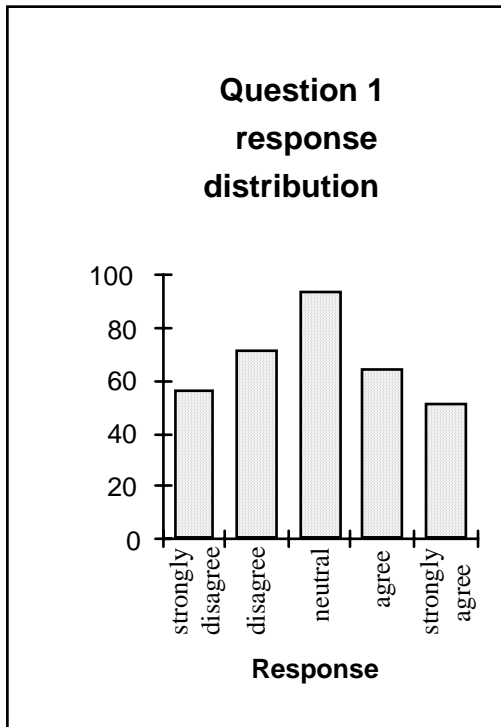
The financial press reports that, despite the costs of building materials remaining stable, due to strong demand building prices have risen strongly over the last six months and building companies are currently making record profits. It happens

that you are taking quotes for the construction of a new home on land you previously acquired and have noticed that the quotes are substantially greater than you had expected.

In your opinion:

1) You would be pleased to hear that Australian industry was thriving.

Exhibit 8.2 Question 1



Question	1
strongly disagree	57
disagree	72
neutral	94
agree	65
strongly agree	52
N=	340
Expected=	68
χ^2_{obs}	15.9
df=	4
$\chi^2_{crit,0.01}$	13.28

Dichotomous analysis

total disagree	129
total agree	117
ratio: A/D	0.9
χ^2_{obs}	0.59
df=	1
$\chi^2_{crit,0.05}$	3.84

The neutral response was significant at the 1% level and the dichotomous χ^2 analysis did not reject the null hypothesis that there was no significant attitude.

Respondents were therefore divided as to whether they considered that the profitable state of the building industry was a good thing, at least for them. Obviously, a personal stake in the performance of the industry that is compromised by buoyant prices is a strong motivator against recognising the macro-economic benefits suggested by the higher profits. To the extent that there are substantially more people using buildings than erecting them, the apparent bias is not unreasonable. It would have been interesting, and perhaps a useful consideration is pursuing this line of study, to have gathered data on the industrial interests of the respondents. Most probably the sample does contain a representative number of persons within this industry, and the industries related to the other situations.

The fact that there was such a wide dispersion of responses and a high degree of neutrality suggests that even when there is a personal cost involved, people are not inclined to view buoyant profits negatively. This may infer that in the absence of the personal stake, attitudes may have been significantly more supportive.

This problem in question design raises an important methodological issue that can be explored by recognising that it brings to the fore two of the difficulties of utilitarianism⁶⁷. The utilitarian would be expected to be pleased with news of a situation that returned *the greatest good to the greatest number*. On that basis, the utilitarian should be indifferent to whether the situation happened to be personally advantageous or not. If this were the case, then the existence of a personal stake would not be an issue. However a likely criticism of the construction of this question is the inclusion of a personal cost resulting from the economic rents being reported as the *record profits* in the building industry.

If self-interest bias at the local and apparent level is accepted, then not only is utilitarianism rendered unreliable, but more remote self-interest bias may also be influencing respondent attitude. For example, consider a car salesman answering this question. If he recognises that this question implies support for the profits from demand sourced economic rents (which it does), he may also recognise, at least sub-consciously, that this is the source of his own commercial success. The self-interested car salesman may detest seeing the building industry profit at his personal expense, but may recognise that his income is supported by exactly the same mechanism. Consequently, his self-interested reply would be biased towards the agree response.

The second shortcoming of utilitarianism that is exposed in the response to this question is the difficulty in quantifying the utilities. There was a wide range of responses, with the neutral response significant. The neutral response indicates that the respondents either believed that it was impossible to resolve the issue, or that the level and source of the building industry's profit held no significance to them. When this is combined with the fact that almost as many respondents agreed as disagreed, with a similar balance of intensities, despite the same information, the result suggests that the greatest good for the greatest number is not the same for different people. This criticism also holds for the concept of moral sentiments, or its twentieth century equivalent, intuitionism. Too much should not be made of this weakness in modern moral systems, at least from this piece of data. Rather, it may be recognised that these systems place too much emphasis on the ability of the observer to remain disinterested and too little on the importance of the underlying objective elements in any moral debate. The former flaw inclines subjectivism while the latter discourages reason and

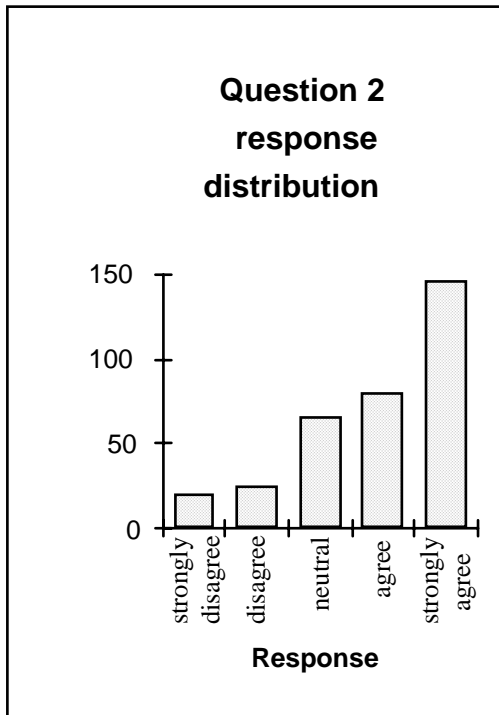
⁶⁷Utilitarianism is used here as the focus for attention because it is closely linked to modern economic theory, however the methodological issue relates equally to most other modern systems of ethics.

these twin fundamental shortcomings comprise the major difficulty in developing social economic theory.

Conversely, it may be the case that the wide spectrum of response was an indication the question was in fact too difficult to resolve, in which case the comments above may be out of place. The strength of the biases revealed in the subsequent questions go some distance to supporting this more moderate interpretation. The issue of community support for strong profits of this kind would therefore appear to be a worthy topic for further study.

2) *You would take a more determined negotiating position before accepting any quote.*

Exhibit 8.3 Question 2



Question	2
strongly disagree	21
disagree	26
neutral	67
agree	80
strongly agree	146
N=	340
Expected=	68
X^2_{obs}	150.0
df=	4
$X^2_{crit,0.001}$	18.47

Dichotomous analysis

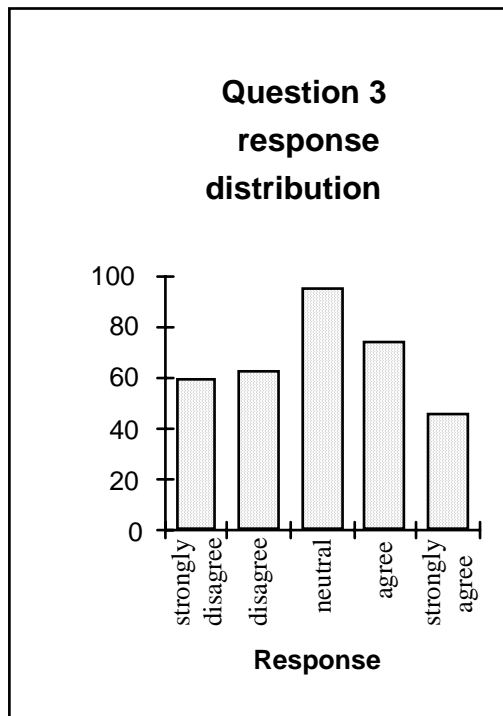
total disagree	47
total agree	226
ratio: A/D	4.81
X^2_{obs}	58.68
df=	1
$X^2_{crit,0.001}$	10.83

With almost five times as many responses in agreement, mostly strongly agreeing, the sentiment is very clearly in favour of taking a more determined bargaining position. This is confirmed by the X^2 test that is significant at the 0.001 (0.1%) level for both the five point and dichotomous cases.

A more determined bargaining position implies a lowering of the effective demand line. The response is consistent with market theory and suggests that the excess profit described in the situation was actually a market failure. The strong inclination of respondents to push to achieve prices more in line with underlying costs suggests a belief that these would be reasonable, hence it indicates a rejection of prices set by excess demand.

3) *You would feel powerless and wish you had locked in the project while profit levels were modest.*

Exhibit 8.4 Question 3



Question	3
strongly disagree	60
disagree	63
neutral	96
agree	75
strongly agree	46
N=	340
Expected=	68
X^2_{obs}	20.7
df=	4
$X^2_{crit,0.001}$	18.47

Dichotomous analysis

total disagree	123
total agree	121
ratio: A/D	0.98
X^2_{obs}	0.008
df=	1
$X^2_{crit,0.05}$	3.84

The five point X^2 test was significant at the 0.001 level suggesting that the null hypothesis (there is no systematic trend in the responses) may be rejected, but the dominant response was the neutral response. This was confirmed in the dichotomous test that failed to find a significant bias of attitude between *agree* and *disagree*. By contrast with the previous question where 66% of respondents believed that they would take a more determined bargaining position, only 36% of respondents believed that they were not powerless in the relationship. The actual count of those agreeing in both Questions was 82, or 36% of those agreeing in Question 2 (see exhibit 8.5) This means that about one third of those who were inclined to bargain harder believed that they would not affect the outcome. This appears to be a rather dismal stance.

The respondents were clearly uncertain of their ability to meaningfully improve their position, despite their strong intention expressed in the previous question. This is important because it suggests that despite a motivation towards lowering the demand curve, there is ambivalence in the respondents' confidence. This suggests a political impotence in the face of what are normally accepted as market forces. Questions 2 and 3 were tested for independence as shown in Exhibit 8.5, using a three option split,

disagree, neutral and agree. This resulted in 4 degrees of freedom and proved significant at the 0.1 level only.

Exhibit 8.5 Independence test between Q2 & 3.

		Q.3			
Count		D	N	A	RT
Q.2	D	25	9	13	47
	N	18	23	26	67
	A	80	64	82	226
CT		123	96	121	340

Expected		D	N	A
D		17.0	13.3	16.7
N		24.2	18.9	23.8
A		81.8	63.8	80.4

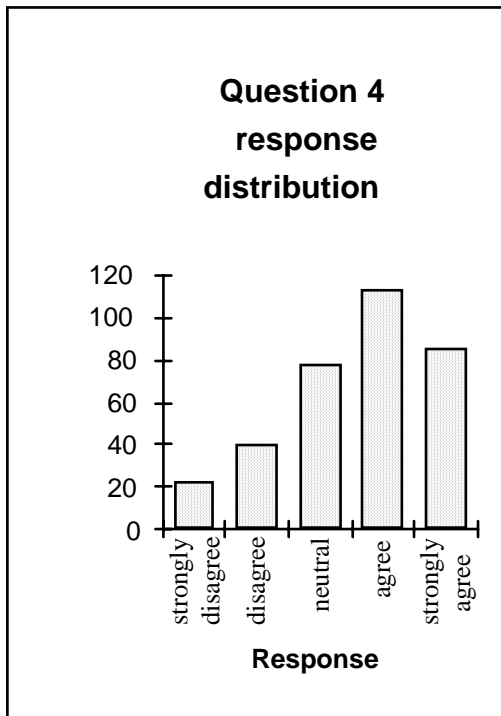
Trend		D	N	A
D		+	-	-
N		-	+	+
A		-	+	+

χ^2_{obs}	8.72
df	4
$\chi^2_{0.1}$	7.78
$\chi^2_{0.05}$	9.49
$\chi^2_{0.01}$	13.3

Xobs		D	N	A
D		3.76	1.37	0.83
N		1.61	0.88	0.19
A		0.04	0.00	0.03
				$\chi^2_{obs=}$ 8.72

4) *You would be critical of whether there was any real need for the higher price.*

Exhibit 8.6 Question 4



Question 4

strongly disagree	23
disagree	40
neutral	78
agree	113
strongly agree	86
N=	340
Expected=	68
X^2_{obs}	77.3
df=	4
$X^2_{crit,0.001}$	18.47

Dichotomous analysis

total disagree	63
total agree	199
ratio: A/D	3.16
X^2_{obs}	35.3
df=	1
$X^2_{crit,0.001}$	10.83

Both X^2 tests indicate significance at the 0.001 level indicating that the *agree* response dominates. Respondents clearly believe that pricing as a result of increased demand is unnecessary. Although the question was not set in ethical terms (the ethical form of the question would have been something like "Was the price rise justified?"), the response signifies the belief that the prices are not considered rational (causally necessary). This is despite market-derived prices normally being considered to be the *natural*⁶⁸ result of economic forces. In this response, the sample surveyed is rejecting the usually accepted behaviour of market mechanics.

By believing that increases in demand have no necessary pull on prices, the respondents in 3 out of 4 cases, rejected the rationality of market forces as the determinant of prices.

It may be argued that the question was complicated by including in the situation a notional personal stake in the prices for the respondents. Obviously, persons likely to personally lose as a result of some situation may be expected to reject it. The next

⁶⁸The term is used here in the loose common sense meaning "common," or "ordinarily found".

situation removes this apparent personal stake, but it will be seen that the results are similar.

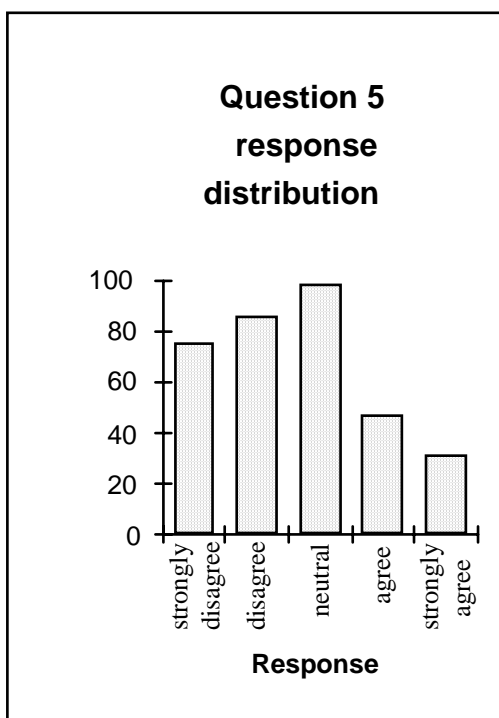
SITUATION 2

Imagine that both major telecommunications companies⁶⁹ completed independent studies of demand for telephone services and have found that it has increased significantly. Over the same period technology improvements have increased call capacity and reduced costs. Because call capacity is considerably above current usage, the system could carry significantly more calls at a negligible increase in total running costs.

On the basis of these findings they both independently choose to leave pricing unchanged.

In your opinion:

5) They have failed to meet their responsibility to their shareholders by not increasing process given the opportunity afforded by the strong demand.



Question 5	
strongly disagree	76
disagree	86
neutral	99
agree	47
strongly agree	32
N=	340
Expected=	68
χ^2_{obs}	45.4
df=	4
$\chi^2_{crit,0.001}$	18.47

Dichotomous analysis

total disagree	162
total agree	79
ratio: A/D	0.49
χ^2_{obs}	14.29
df=	1
$\chi^2_{crit,0.001}$	10.83

⁶⁹Australia has only two major telecommunications companies.

Both X^2 tests indicate significance at the 0.001 level indicating that the *disagree* response is statistically dominant. The importance of the neutral response should be acknowledged as it represented the modal response, and the agree response was more popular than strongly agree.

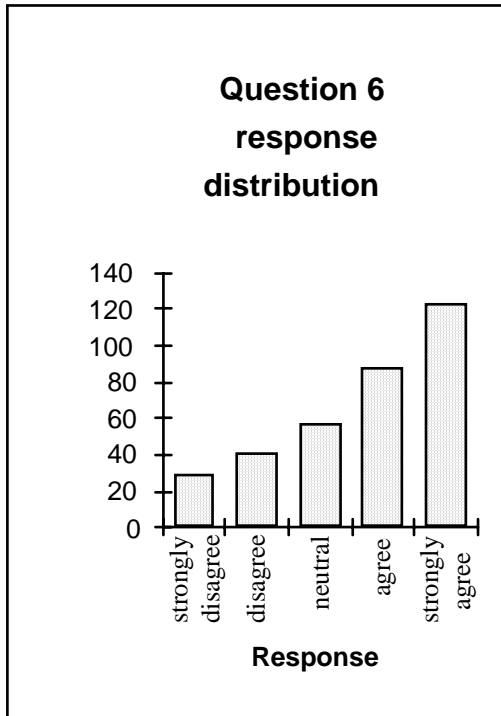
This suggests that there is an element of ambivalence in the sample. The neutral response implies that the respondents believe that they cannot resolve the question of the companies' responsibilities to their shareholders. On one hand, there is the understanding that the company exists only to maximise profits to its shareholders, in which case its very existence is premised on exploiting every opportunity for profit. This would suggest that the reason for the existence of the company supplies an overriding obligation on its management. On the other hand, there is the possibility, not spelt out in the situation description, that depending on the elasticity of demand, lower prices may enhance usage levels to the extent that profits may be maximised more effectively using this strategy than the apparent opportunity afforded by demand. This would suggest that meeting the corporation's responsibility to its shareholders may lie coincident with lower prices for consumers. While this possibility appears to provide a resolution that benefits all parties, it may still include substantial economic rents flowing to the shareholders.

Beyond the complications inherent in the neutral option, 48% of respondents selected the *agree* response producing a ratio of about 2:1 against the disagree position. This suggests a definite rejection of the notion that shareholders should benefit from demand-based opportunities for price rises. This is despite the fact that the shareholders are the owners of the company and its technology.

Future refinement in the study of this type of question may improve the clarity of the data it provides by disaggregating the issues further. As it stands, it still provides significant evidence of popular rejection of the notion that the corporation has a mandate to absorb profit opportunities afforded by demand.

6) *They should pass lower costs on to consumers as lower prices.*

Exhibit 8.8 Question 6



Question 6

strongly disagree	30
disagree	41
neutral	57
agree	89
strongly agree	123
N=	340
Expected=	68
χ^2_{obs}	84.7
df=	4
$\chi^2_{crit,0.001}$	18.47

Dichotomous analysis

total disagree	71
total agree	212
ratio: A/D	2.99
χ^2_{obs}	35.13
df=	1
$\chi^2_{crit,0.001}$	10.83

Both χ^2 tests indicate significance at the 0.001 level indicating that the *agree* response is statistically dominant. The ratio of agree to disagree responses is almost 3:1.

This question is set in moral terms, using the word *should*. It would appear that the dominant sentiment is that the customers should benefit from the technology based cost savings, despite their higher demand. This suggests a belief in cost based pricing as morally superior to market based pricing.

The question also goes some distance towards resolving some of the uncertainties left from Question 5. This question goes past the issue of merely choosing between responsibilities to shareholders and the community (lower prices), which has been shown to include the possibility of higher profits from lower prices, but focuses more directly on economic rents. It does this by questioning the ethics (via *should*) of retaining economic rents, which are the gaps between *costs and prices*.

Care should be taken in interpreting this result, because it is also found within market theory. Market theory suggests that as a market matures towards equilibrium,

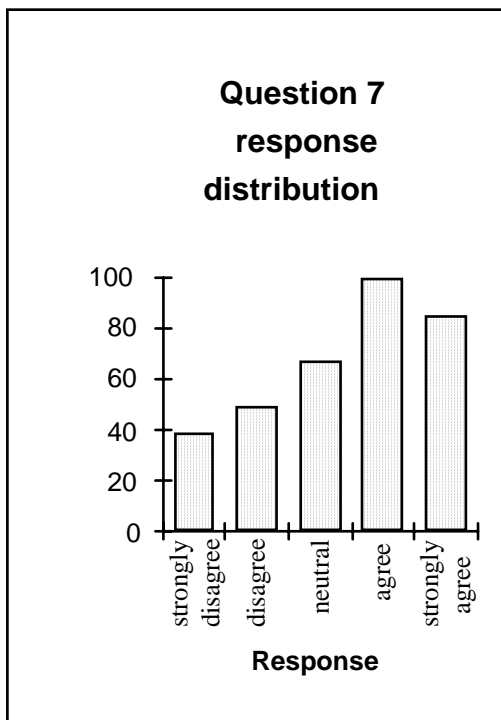
prices will tend towards normal costs. This would be consistent with the responses in the study.

However, there is no indication in market theory as to how long it should take before equilibrium is reached nor how accurately prices should be based on normal costs. The sentiment revealed in the study would suggest that the prices should follow costs from the outset, rather than follow a protracted tug-of-war in the marketplace. If the attitudes exposed in the sample are a reasonable indicator of sentiment, it would appear that the popularly held belief is that the moral nexus between costs and prices precedes market theory. This means that it is more likely that market theory may derive its common acceptance *because* it achieves a more fundamental moral goal; this is counter to the liberal assertion that equilibrium prices gain moral rectitude primarily on the basis that they came from the free market.

The question is one of causal primacy and the data suggests that economic rent is the primary issue, not liberty in the marketplace. The free market may result in prices that coincide with the popularly held belief of fair play, but this is not a necessary connection. The final situation explores this possibility further.

7) *More suppliers of telecommunications would force the prices down to reasonable levels.*

Exhibit 8.9 Question 7



Question	7
strongly disagree	39
disagree	49
neutral	67
agree	100
strongly agree	85
N=	340
Expected=	68
χ^2_{obs}	37.0
df=	4
$\chi^2_{crit,0.001}$	18.47

Dichotomous analysis

total disagree	88
total agree	185
ratio: A/D	2.10
χ^2_{obs}	17.23
df=	1
$\chi^2_{crit,0.001}$	10.83

Both χ^2 tests indicate significance at the 0.001 level indicating that the *agree* response is statistically dominant with about twice as many respondents taking this view compared to its opposite.

Promoting the introduction of additional suppliers is the usual strategy for mitigating an imbalance of power in the market. It would be interesting to study the views of those who did not believe that this strategy would be effective. Perhaps this would be an area for further study.

As a strategy for the control of the market it must be recognised that it is not necessarily an economic strategy. In practice, the introduction of new suppliers to control market imbalances is often done as a result of government intervention, sometimes at considerable cost. At various times different levels of Australian government have entered essentially private and entrepreneurial sectors with the express purpose of controlling market imperfections, such as airlines, banking and even

property development. It would appear that it is better described as a political strategy, because its object is a redistribution of power in the face of some real, or feared, market failure.

Competition is culturally more acceptable in Western society as a strategy to constrain perceived power imbalances in the market although other strategies are also possible. For example, centralised price fixing has been attempted at various times and is a dominant feature of statist economies. These are generally fraught with problems. Discussion of their shortcomings is beyond the scope of this study.

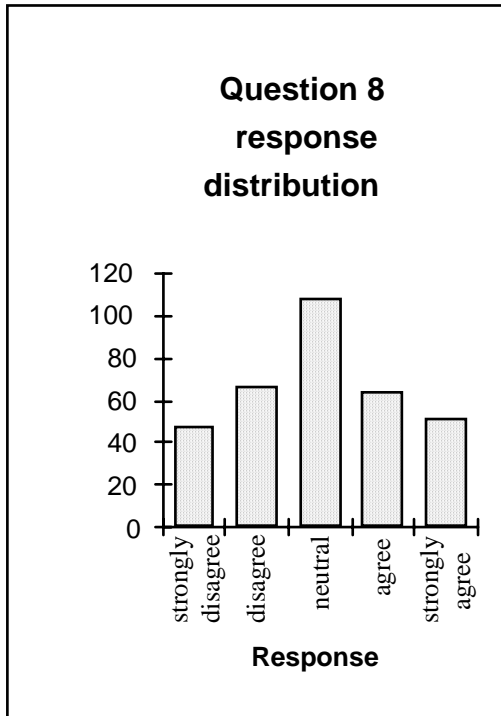
The validity of any market intervention aimed at controlling prices must derive its moral force from moral principles outside of the free market, because it is the free practical operation of the market that produces the anomalies in the first place and the inability of the free market to correct itself that maintains the problem. The very fact that it is possible to speak of market imperfections as problems is strong evidence that there is a higher criterion for performance. It would appear that the respondents in this study identify that higher criterion as relating to the importance of price to be a reflection of costs.

SITUATION 3

While on holidays you recognise your local fruit and vegetable grocer as he steps from his new Mercedes. He tells you that although he only has interests in his one shop, because of the neighbourhood it is in he has no trouble setting prices at a very profitable level and has done so for some years. He confides that although he started with very little, he is now a very wealthy man, though he still maintains a humble appearance whilst at work.

8) *You would feel proud to be dealing with such a successful supplier.*

Exhibit 8.10 Question 8



Question	8
strongly disagree	48
disagree	67
neutral	109
agree	64
strongly agree	52
N=	340
Expected=	68
X^2_{obs}	34.6
df=	4
$X^2_{crit,0.001}$	18.47

Dichotomous analysis

total disagree	115
total agree	116
ratio: A/D	1.01
X^2_{obs}	0.002
df=	1
$X^2_{crit,0.001}$	3.84

The five point X^2 test was significant at the 0.001 level suggesting that the null hypothesis (there is no systematic trend in the responses) may be rejected, but the dominant response was the neutral response. This was confirmed in the dichotomous test that failed to find a significant bias of attitude between agree and disagree. This question attracted the largest number of neutral responses in the study and the remaining responses were evenly distributed about the neutral position with relatively few extreme responses at either pole.

The respondents were apparently undecided as to whether or not their association with a merchant who had grown rich as a result of the willingness of their neighbourhood to pay high prices was a good thing. If the free market was the moral floor in economics, one would expect that an association with a successful person would elicit pride as it would in connection with an outstanding person in some other pursuit, say an athlete or scientist. Only about a third of the respondents were convinced that this was the case with respect to a local merchant.

There was no indication in this question that the basic conditions for an efficient market were not being met, although question 10 will probe this at a practical level. In practice, many local shopping centres can only support one merchant in each of the

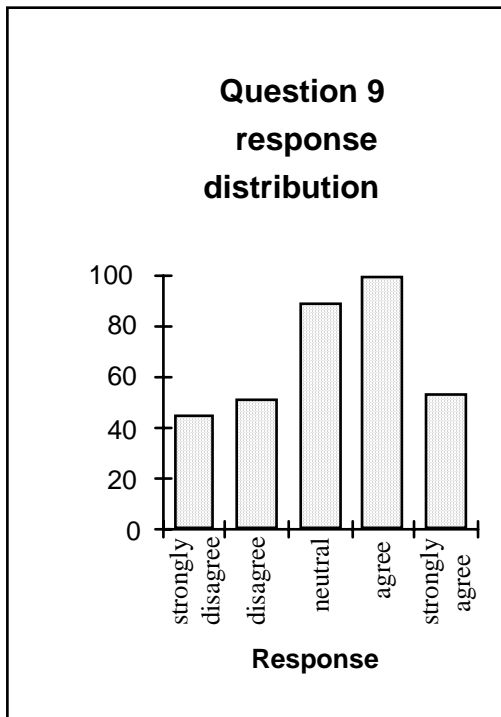
various regular consumer needs, but shoppers are not prevented from opting to shop at other centres. The lumpy nature of supply and the other elements that constitute special nature of local traders may suggest other issues that can never be resolved by efficient market theory. These include the implicit monopoly possibilities due to lumpy entry into a market as a supplier and also community expectations of fair play from its members.

The element of a personal stake was once again present in this situation, as it was in situation 1, only here there is no necessity for personal loss as there was in the former case. There are other suppliers available and there is nothing in the situation to suggest that fruit and vegetable merchants as a group were super-normally profitable, as was the case in situation 1. The personal stake is therefore attenuated and controllable, but it does have the advantage of making the respondent aware that the situation does have a community impact.

The question is further complicated by the various possible sources of pride. It may be that a person could experience pride in knowing that he has achieved a level of material success sufficient to be able to live in a locality that can support high prices. It may also be connected to personal aspirations of material success of a similar type to the fruitier. The decade beginning 1980 was popularly regarded as the period in which the sentiment *greed is good* took hold, such an ethic could be seen to be consistent with this possibility. The positivist methodology which is being adopted in this part of the study is not competent in dealing with the moral overheads of these possibilities, but this should not preclude their observation as possible explanations for the data.

9) *You would be inclined to ask for better prices.*

Exhibit 8.11 Question 9



Question 9

strongly disagree	45
disagree	52
neutral	89
agree	100
strongly agree	54
N=	340
Expected=	68
χ^2_{obs}	36.0
df=	4
$\chi^2_{crit,0.001}$	18.47

Dichotomous analysis

total disagree	97
total agree	154
ratio: A/D	1.59
χ^2_{obs}	6.472
df=	1
$\chi^2_{crit,0.001}$	10.83

Both χ^2 tests indicate significance at the 0.001, level indicating that the *agree* response is statistically dominant and the null hypothesis can be rejected. Despite this, the distribution of responses included a large number neutral responses and the dominant reply was not the extreme. This would imply a relatively weak sentiment which is further confirmed by the ratio of agree/disagree which was only 1.6:1.

To contrast this result to Question 2 is interesting from a social perspective. The same sample expressed a very strong inclination to push for better prices in the case of building prices, compared to the weaker inclination in the case of a local food merchant. Numerically, 66% of respondents would push for keener building prices while only 45% would do the same for food. This is a one third reduction in willingness to act to reduce demand-induced prices. A χ^2 test for independence returns a χ^2_{obs} statistic of 30.1, which with 1 degree of freedom is significant at the 0.001 level. This confirms that the difference in the responses is not random.

Several factors may have influenced this outcome. Fruit and vegetables are only a minor purchase and it could be expected that they do not warrant careful scrutiny. If this is the case then it would appear that there may be systematic market imperfections in particular classes of consumer goods that fall into this blind spot in market interest. However, in total over a period of years, say the life of a building, a family may be expected to spend a comparable amount in total on food compared to the cost of buildings⁷⁰. This would make care in pricing food just as important as major purchases.

A second factor that may influence a person's willingness to bargain for regular purchases is the personal dimension of the relationship. It is not a part of Western culture for shoppers to argue over prices when listed in a shop context. Hence, even if prices are known to be high, it could be expected that shoppers will be reluctant to ask for discounts. On one hand this presents an opportunity that may be capitalised by a merchant who has no scruples about charging what the market will bear.

Also related to the personal dimension of the relationship at a local level are three additional factors. Bargaining is wearying, and the prospect of engaging in it regularly may not be judged as worth the trouble, even if prices are perceived to be high. Secondly, it may be considered demeaning to haggle for minor purchases. Thirdly, to question prices may be perceived as questioning the integrity of the merchant. This last issue is peculiar because it implies that there is an issue of integrity involved in pricing which is above the determinations of the market, that is, even though the market may freely settle on one price, the integrity of the merchant would prevent accepting such a price. To some degree this relates to the previous question.

Finally, it may be considered that negotiation is reasonable in the case of building quotes, but not so in the case of food. This is strongly influenced by Western culture. Builders may be perceived as profit-seeking, not to be trusted to give a fair price and in any case are usually not personally known. By contrast the proprietor of the local fruit shop is perceived as none of these things.

The data from this question is therefore useful in understanding extra-market issues that appear to be significant when compared to the responses to question 2. Two issues crystallise out of these possibilities. The first is that there are cultural issues that prevent efficient market behaviour. The second is that there may be an expectation on merchants not to exploit market opportunities, at least in particular markets.

Anyone who has spend time in cultures where bargaining is the custom for minor purchases knows that the practice is quite inefficient. One of the achievements of the West has been the development of set prices for the majority of goods. It tends to be

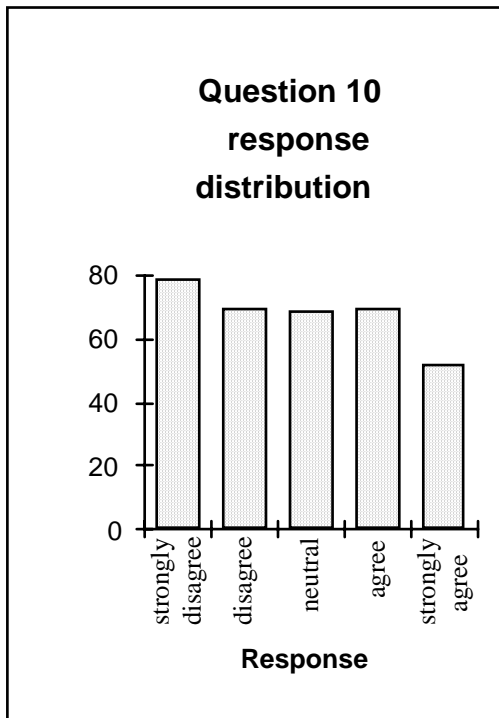
⁷⁰In thirty years a family spending \$150 per week on food will spend over \$230,000. This is well in excess of the building cost of the average Sydney residence.

ignored that the majority of purchases in Western cultures, at least by number, are made using prices that are set by the merchant and trusted by the community to be reasonable. While it is true that these merchants may take demand into account to some degree in setting price, and that customers do exercise a degree of discretion in choosing their purchases, the extent of these behaviours appears to be considerably less than the theory of market behaviour asserts. Market theory assumes full knowledge, which would require all parties researching all commodities constantly. Not only would purchasers have to know the production parameters of every item in their shopping cart, but suppliers would have to understand demand and cost dynamics, including elasticities. Friedman (1953) admitted that this was impossible in practice and Jones (1976) showed that it was impossible in theory, despite both authors being staunch supporters of the market.

In practice, consumers assume a sense of fair play and believe that the threat of competition in supply will constrain economic rent-taking. This eliminates the need for personal analysis beyond comparison of some competitors. This practical compromise leaves considerable latitude for market inefficiencies. For purchasers, the element of trust that underlies these commercial encounters returns considerable savings. Purchasers tend to trust that suppliers are not unreasonable in their pricing which means that they can eliminate the need for a considerable amount of market knowledge which means a considerable saving in effort. The attitudes revealed in this question, especially in combination with question 2 support this view of pricing.

10) *You would be inclined to change suppliers, even if it meant some inconvenience.*

Exhibit 8.12 Question 10



Question 10

strongly disagree	79
disagree	70
<i>neutral</i>	69
agree	70
strongly agree	52
N=	340
Expected=	68
χ^2_{obs}	5.7
df=	4
$\chi^2_{crit,0.001}$	9.49

Dichotomous analysis

total disagree	149
total agree	122
ratio: A/D	0.82
χ^2_{obs}	1.345
df=	1
$\chi^2_{crit,0.001}$	3.84

Both X^2 tests failed to reach significance, even at the 0.05 level indicating that the respondents were widely varied in their opinions regarding the option of changing supplier. Unlike the other questions that failed to find a significant attitude bias, this question did not return a dominant neutral response. This means that respondents were widely varied in their attitudes, not uncertain.

The question was complicated by the fact that the alternate behaviour carried a cost and did not specify a reward.

This is fairly realistic in practice. There is a search cost which puts a premium on choosing alternate suppliers, both as a result of the resources that are consumed in researching the options and the possibility that the alternatives may achieve monetary objectives only at the expense of other factors, such as increased travel, lost time, or disruption of convenient shopping patterns. This buyer inertia is a second economic anomaly that may be capitalised by a profit-oriented merchant.

The mechanics of the efficient market hypothesis may also impact on behaviour. If it is believed that the merchant's ability to charge high prices is partly due to the fact that (1), there has not been a mass exodus of his customers, and that (2), this must be because many of his customers have evaluated the alternate options and found that there are no better opportunities, then it would be reasonable not to bother with a personal examination. The risks here are obvious. If everyone adopted this attitude, there would be negligible transfer of customers, and a high apparent validation of the merchant's pricing. Also, consumer purchases are not like financial instruments and the efficient market hypothesis may very well suit the latter far more than the former.

It may be observed that about a third of the respondents expressed an inclination to change supplier, and if this inclination were acted upon it would damage the merchant's sales so much that he would have to adopt a more competitive stance in order to attract them back. In practice, even if a third were so inclined, they would only be motivated to act in that way if they become aware of the merchant's inordinate profitability. If only a few customers became aware that the merchant was charging liberally, only a third of those may be motivated to move their trade, which may not be significant to his business.

Linking questions 9 and 10 may provide some insights into respondent strategies. Exhibit 8.13 summarises the data regarding the various response combinations concerning agree attitudes in the two questions. A dichotomy has been established for the purposes of analysis between the two agree responses and the other responses. This is on the basis that action attitudes in both questions follow only from the agree

responses. Consistency in responses were found in a total of 200 responses, while 140 respondents agreed to one question and not the other.

It can be seen from the X^2 test for independence that there was a significant correlation in the responses at the 0.01 level. The apparently inconsistent results may also signify reasonable and active response strategies. Particular customers when aware of unnecessarily high prices may see the two questions as providing two possible retaliatory strategies. Personal preference may incline the adoption on one and not the other - some people may choose to stand and bargain, while others will make a statement *with their feet*, avoiding the discomfort of confrontation by shopping elsewhere. Viewed in this way, a total of 208 respondents have expressed the attitude of intending to retaliate in some way, some by bargaining and some by patronising the competition.

Independence was also tested using a three option split of the attitudes (disagree, neutral & agree). The data also revealed significant correlation between the responses to the two questions and the same comments would also appear to hold.

Exhibit 8.13 Analysis of Independence between Questions 9 & 10

Count		Q.10		
		not agree	Agree	RT
Q.9	not agree	132	54	186
	Agree	86	68	154
CT		218	122	340

Expected		not agree	Agree
not agree	119	67	
Agree	99	55	

Trend		not agree	Agree
Disagree	+	-	
Agree	-	+	

χ^2_{obs}		not agree	Agree
not agree	1.4	2.4	
Agree	1.6	2.9	
		total= 8.4	

df=	1
$\chi^2_{0.01}$	6.63

Independence between Questions 9 & 10, three option split

Count		Q.10		
		Disagree	Neutral	Agree
Q.9	Disagree	56	14	27
	Neutral	43	19	27
	Agree	50	36	68

χ^2_{obs}	17.09
df	4
$\chi^2_{0.005}$	14.9

8.3 FACTOR ANALYSIS

The possibility that responses to the three situations were influenced by a common factor was considered. It may be the case that respondents were inclined to either a liberal market or a socialist cluster of attitudes. If this were the case then clusters of responses to the questions 1, 5 & 8 could be expected to be affirmative for liberal market enthusiasts and negative for socialists and the reverse questions 4, 6, & 10. Other clusters of responses may also be expected.

Covariance analysis was undertaken for correlations between the results for the different questions. The results are shown in exhibit 8.14. There were only three cases where the correlations reached the 0.5 level, which is still not a strong correlation.

Exhibit 8.14 Covariance Table

	Q1	Q2	Q3	Q4	Q5	Q6	Q7	Q8	Q9	Q10
Q1	1.69									
Q2	-0.12	1.48								
Q3	-0.08	0.06	1.66							
Q4	-0.13	0.51	0.17	1.39						
Q5	0.13	-0.11	0.11	0.08	1.53					
Q6	0.24	0.29	0.06	0.31	-0.32	1.71				
Q7	0.01	0.58	0.15	0.32	-0.24	0.51	1.73			
Q8	0.39	-0.05	-0.05	-0.03	0.11	0.01	-0.15	1.57		
Q9	0.08	-0.02	0.11	0.16	0.03	0.05	0.07	-0.34	1.58	
Q10	-0.04	0.13	0.13	0.20	0.15	0.14	0.06	-0.48	0.41	1.93

Question 7 was regressed against questions 2 and 6 but returned considerably worse results than either variable separately. It was evident that there was no indication of a common 'ideological' factor in the data and statistical analysis was not pursued further.

8.4 CONCLUSION

Responses to questions regarding Situation 1 (real estate building pricing) reveal a general criticism of profits derived from elevated demand. Respondents were ambivalent as to whether such profits were a welcome indicator of the state of Australian industry, were critical of whether the attendant prices were necessary and showed a strong inclination to fight harder to negotiate them down. Despite an overwhelming inclination to push for lower prices only a third of respondents believed that they had the power to meaningfully improve their position.

Situation 2 (corporate consumer goods/services pricing) revealed that the dominant belief in corporate pricing is that shareholders should not benefit from the capitalisation of strong demand through elevated pricing. Furthermore, it is believed that lower costs should be passed on to consumers as lower prices, despite demand levels. The notion of increased competition as a strategy to prevent corporate rent-taking was supported.

Situation 3 (local consumer goods pricing) revealed a weaker rejection of excessive pricing by local suppliers. There appears to be a high degree of ambivalence towards the attractiveness of merchants who profit from the local willingness to pay and a reluctance to explore the competition if it meant some inconvenience. There was a significant inclination expressed to ask for better prices, although it was quite attenuated compared to the similar issue in Situation 1.

In total, the study has revealed a pervasive rejection of demand based pricing and support for pricing related to costs. These attitudes appear to straddle both notions of reasonableness and ethical values. Implications from the data suggest cultural views that are more dominant than market theory alone can explain. The study has confirmed Frey's (1993) findings on beliefs regarding the fairness of pricing and provides social support for Langholm's (1969) conclusion that cost based pricing is the more successful strategy in practice.

8.5 CONTRIBUTION TO THE SUPPORT OF THE THESIS HYPOTHESES

	Hypothesis	Treatment
1.5.7	Popular sentiment does not support pricing from use value.	Supported
1.5.7.1	Modern market theory is based on a positivist methodology, yet fails positivist tests.	Supported

Chapter 9 An Aristotelian Construction of Exchange and Property.

The purpose of this chapter is to construct a causal theory of material goods and to use this to construct a metaphysically consistent theory of property. Most of the components of what will be described appear to be widely accepted on an individual basis but apparently not taken to the conclusions asserted in this discussion.

The chapter will conclude with a conceptual theory of property rights that locates the appropriate use and limitations of the market and an argument for the exclusion of some transactions from market determination.

Humans need a variety of goods in order to sustain their life. Aristotle reasoned that the ultimate end of human existence was happiness and happiness may be understood as the complete realisation of human nature. This means that to be happy is coincident with being fully human. Human nature is a complex thing and its full expression, or flourishing, is the result of the balanced expression of its many component parts. It may be argued that the essential human freedom is the freedom to be human. This is not necessarily freedom from restraint, but the opportunity to flourish as a human person.

Anything that genuinely contributes to human flourishing is good. The goodness of these things is taken from the excellence of their end, the human person. Aristotle recognised a natural hierarchy in existence that was adopted and completed by the Scholastics. Living things are more perfect than non-living, sentient life is more perfect than non-sentient, and intellectual beings are more perfect than brutes. A thing that supports a more perfect thing is itself ennobled by the perfection of what it supports. Hence food is more perfect than dust and wine more perfect than straw. Things that support the flourishing of more perfect things are good in proportion to the degree of support they provide and the perfection of the thing supported.

Part of human complexity is the way that humans have material, intellectual, social and spiritual dimensions. While these may be seen to lie within a natural hierarchy, this is not to say that any one can exclude or replace any of the others. Anything that supports an aspect of human nature is good, and these things are referred to as *goods*. Goods may be found that support the different dimensions of human nature. Economics is about the provision of human material goods. Because it has the capacity itself to

satisfy to satisfy a human need, it is itself a good. Economics is not a material good but an intellectual and moral good.

Material goods are goods that support the material dimension of human nature. While this is not the most perfect aspect of human nature, it is the necessary foundation for mortal human life and therefore of fundamental importance to the possibility of human flourishing. Wright (1998) quoted Aristotle as saying "*happiness seems to require a modicum of external prosperity...*" to be "*adequately furnished with external goods*" (p. 292) leading to his conclusion that Aristotle understood that while happiness consisted also of higher pursuits, it had to be supported by an appropriate material situation. This also raises questions regarding the notion of human subsistence which will be dealt with later.

Human material needs have been summarised as food, clothing and shelter and these seem adequate for the present discussion. Each may be found directly in the natural environment, however human societies have long recognised the advantages of obtaining one's material needs indirectly through exchange. Three apparent advantages arise from meeting human material needs indirectly as follows:

- It allows specialisation of labour which reduces the total effort required for a given quantum of goods.
- It facilitates greater processing of raw resources that greatly improve a good's effectiveness.
- It can be managed to enable some individuals live at the expense of the toil of others.

Of these, the first two genuinely improve the provision of material goods and can be seen in the productivity and improved living standard of developed countries. The third affords individual advantage, but not necessarily the good of the society. The first two relate to improvements in production and physical distribution, they mostly relate to the intellectual virtues associated with production. The third relates to the good of providing for those who do not materially contribute to production, it is a moral question. Some persons are provided for out of charity, such as the elderly or the sick. Some persons are provided for because of their non-material contribution to the society, such as administrators. These have a just call on a share of the society's material goods, that may not be economic, but is never the less real due to the value of the non-material goods their toils provide. Lastly, some persons appropriate goods from the efforts of others as thieves. These often justify their position along the lines of

Thrashymarchus, the Sophist who asserted that *justice was the will of the stronger party*.⁷¹

Economics assumes a productive society that operates using exchange of goods and seeks to inform the question of how to identify and reduce the incidence of persons inappropriately receiving the goods produced by others. Exchange is the core event in economics and it usually occurs in the marketplace. Market can denote at least two things, the first is the physical or social institution comprising of opportunities for persons to exchange things. The second is an intellectual or conceptual institution where supply and demand interact to resolve the transaction decision and its attendant price. Despite the dominance of the identification of the two meanings of market in the modern Western mind, there have been many successful cultures in which exchange largely occurred outside of the Western conceptual market institution. These are often covered by the description *gift economies*. There appears to be considerable evidence that pre-modern Western economies were substantially gift economies (Little 1978).

This is not to suggest that the market institution is necessarily deficient, but only to recognise that market exchange is not the only possibility. Also, it is very possible that even within gift economies injustices occur. Economics also assumes that the exchanges take place using money and the nature of money was something that Aristotle used as a tool in understanding the ethics of economic behaviour.

If economics is to explore appropriate relations between persons with respect to material things, it must examine the appropriate circumstances for exchange and be able to suggest methods of resolving the major uncertainties. While Aristotle did not set out to be an economist, his general scientific method is most suitable for economic enquiry and his moral and political thought provides a valuable starting point for the science. Indeed, although Adam Smith commonly holds the title of being the *Father of Economics*, Langholm (1984) noted that his core topics were a restatement of Aquinas, who in turn was restating Aristotle. Themes such as value and price, property, profit and monopoly that are evident in both of the earlier writers and their treatment was sufficiently developed to influence public policy.

Aristotle used the analogy of a thrifty household as the basis for his considerations of economics in the early parts of his *Politics*, which led to the name of the discipline (economics: from Gk. *oikos*, a house; *nomos*, a law). The analogy suggested that economic success at any level of human society may be directed by the same principles that make for a well run household. This was recognised by Hayek when he stated:

⁷¹Thrashymarchus may be encountered directly as a historical Sophist or indirectly as Socrates' principle protagonist interlocutor in the first section of Plato's *Republic*

"An economy in the strict sense of the word in which a household, a farm or and enterprise can be called economies, consists of a complex of activities by which a given set of means is allocated in accordance with a unitary plan among the competing ends according to their relative importance. " (Hayek 1976, p. 107)

Various aspects of Aristotle's economics will be explicitly considered as they inform the social economy of land. Initially, the importance of the household as a metaphor for economics should be considered. Today, the family's front door is the interface between two very different sets of inter-personal relationships. Within the family solidarity is the most dominant characteristic, even in modern nuclear families that have shed most of the richness of the extended family. Solidarity, the fundamental social virtue that is exercised in intending to stand with the other, to support them and bring out their best, is often diagnosed as charity. While this is a reasonable approximation and carries considerable truth, solidarity also encourages justice and whereas charity connotes compassion and perhaps some paternalism (as appropriate in measured degree) solidarity connotes brotherhood. Solidarity does not require democracy to achieve equality, but dignity and ordered relations.

These are the relationships that are found in a functioning family. Modern Western may profit from close contacts with other cultures where these family relations are evident, they have been largely leached out of Western social thought by the Enlightenment. Review the fathers of sociology, Durkhiem, Compte and Marx and what is found is an existentialism that has no place for charity and puzzles over the remnants of solidarity in Western culture. Anomie and alienation are the social costs of individualism. Aristotle lived in similar times. The Sophists placed more weight on winning a debate that telling the truth and promoted an ethic that was every bit as self-centred as Hume's moral sentiment. Aristotle's solution for appropriate relations between persons in the market was to remind them that the *other* in the market was to be understood like the *other* in the family, a brother. On that basis, justice, charity and solidarity would appear to supply the reference points for action.

Unlike classical and neoclassical economics with their focus on the individual and a belief that the common good would be realised by a collective of self-interest, the family metaphor of Aristotle's economics is social. It is not socialist - that reaction to Smith's economics took economic thought from one imperfect extreme to the other. It rejects the assertion of self-interest as a moral floor to economics, but does not reject the institutions of freedom and property. It places limits of those institutions.

Aristotle was very fond of proportion, and used that geometrical metaphor repeatedly through his *Ethics*. Proportion includes principles, but does not necessarily

make them absolutes, it can balance charity against justice. It allows for differences without inequalities. Aristotle recognised the opportunity for proportion in economics and used it to inform his understanding of exchange. His work responded to the needs of his time, answering the questions that were being asked then. He has left some puzzles. The intention of this thesis is not to critique his economic thought⁷², but rather to use it to understand one economic question, and that is the appropriate economic treatment of land.

Land is a unique form of wealth. Although being the source of all material goods, it is totally free. For many cultures it is a wealth that is not personal but a common heritage for a family group. It is necessary to understand its relationship with the other fundamental component of all material goods, labour, in order to understand its social economy.

9.1 FACTORS OF PRODUCTION

Three factors of production were accepted in classical political economy, land, labour and capital. These will be adopted in this study. Some attempt has been made in recent times to add a fourth factor, *enterprise*, though this will be discovered to be no more than an attempt to validate perennial super-normal profits.

The three factors are reasonably apparent, as they were to Smith in his early discussion of them. Land includes all resources before they are affected by human effort and includes the locations used for production and commerce, labour is human effort and capital is specifically that set of products used for production, tools. Under this set of definitions capital is limited compared to current understanding. Capital refers to products that assist the human efficient cause and are therefore properly instrumental efficient causes of production. They are analogous to labour in that they are also efficient causes, but quite different in that no production can proceed without labour as ultimate efficient cause⁷³.

Because capital is produced, it does not include land. This is evident both from the natures of each and also from common usage. Land derives a value through the *capitalisation* of its rental value. The suffix *-ise* is usually attached to denote a change of nature, bones are *fossilised* to change from bones into fossils. Capitalisation changes land into a form of financial capital.

Also absent from capital is money, although this is a more subtle omission. Aristotle believed that money was not productive, hence it could not be a species of capital. St.

⁷²That has been done by others such as Langholm (1992) and Meikle (1995).

⁷³This study is limited to the natural realm and the scope of production is limited to human agency and ends. Hence, even though humans may not be strictly speaking the ultimate efficient cause of production, within the bounds of human mortal experience such a description is reasonable.

Thomas tended to agree with Aristotle, but St. Bernadino of Sienna did not. It is not necessary at this point to pursue this issue beyond noting two things:

- Money derives its financial value as the present value of its future returns. Land derives its value likewise. By contrast, material products, including capital, find equilibrium prices according to their costs of production.
- The only way that money contributes to material production is through being consumed. A productive loan is worthwhile to the borrower only because it allows him to purchase some real capital that has a higher rate of return than the interest cost of the loan.

Ignoring the complications of money, within the definitions of land, labour and capital, there is often a distinction between the apparent forms and their essential components. For example, a vacant block of land may be considered in most cases to be a product, it may be cleared, irrigated and will be served by adjacent roads, electricity and water supply. Likewise, in addition to being the fruit of human willingness to toil for others, labour is an amalgam of a unique set of natural human abilities, and intellectual virtues (training and education) that are capital-like in that they are the result of previous human effort. The relationship between the apparent and essential factors of production are summarised in the table in exhibit 9.1

Exhibit 9.1 Factors of Production

Apparent Factors	Essential (Component) Factors		
	Land	Labour	Capital
Land	Undeveloped resources; degree of natural endowment of resource potential	Evident in apparent land as implicit capital; for example, cleared land contains embodied labour evident as the enhanced productive ability of a cleared site.	fertiliser as placed, irrigation systems, clearing, fencing; off site infrastructure: roads, social amenity, water supply, drainage
Labour	Undeveloped capacities and abilities; degree of natural endowment of human abilities	Activity of a normal human person, especially when directed for the good of others.	Education and training; exceptional physical development; artificial enhancement; embodies previous labour by the subject or others.
Capital	Raw materials from which capital items are constructed	Labour used to produce capital items	Capital items used in the production of the subject capital item
Comment	Includes all non-labour resources; necessary for material production; material cause of production.	Unenhanced activities of the human person; ultimate efficient cause of production. Basic unit is a healthy unskilled worker.	Instrumental efficient cause of production; regresses into land and labour components.

9.1.1 Land

To understand Land the appropriate returns to the factors it is necessary to consider the essential factors and use this understanding to interpret practical situations. If the vacant block of land is able to satisfy human needs more effectively as a result of the utilities that have been made available to it, part of the price or value of the land is actually payment for the utility, a product. The vacant lot itself may have been cleared, which means that it contains some labour. In a sense the apparent land itself is actually a product, however it usually more appropriate to be aware that there is a labour component, when this is only a small part of the whole. Likewise the land may have been fertilised or fenced and these improvements represent capital which has been added to the land. Recognising that the land is a compound of the land factor and some capital will improve appropriate pricing and policy.

9.1.2 Labour

Land is fairly clear from this summary, though labour and capital deserve further comment. Labour is enhanced by superior natural abilities that a person may be born with and training and education that the person may have previously toiled for. Unusual personal abilities are like an unexpected bounty. Training and education is now being interpreted as analogous to capital - it is the result of previous labour and enhances the person's abilities. The pricing of labour is better informed by being able to dissect this compound, and is found in practice in the habit of many states in setting minimum wage levels. Minimum wage levels assume no special physical abilities or training.

Essential economic labour becomes a little more difficult to define as a result. It may be defined as doing something of value for others, or more accurately, the willingness to toil for the good of others. An activity is a hobby if it is pursued for one's own benefit. To be meaningful, labour must be directed at some good. In many cases labour has value merely through the intention of doing something of value, such as in the case of a shop assistant who will be paid regardless of whether there are customers in the shop or not at any particular time. Labour must also be human to deserve inclusion in economic thought; an animal may be driven to do good for a man, but it does not deserve the same consideration as regards wages.

9.1.3 Capital

Capital is found within apparent land and apparent labour and can be seen to warrant particular returns in these cases. In itself capital is only contingent. Both land and labour have an essential element when the other two factors are distilled away, however nothing remains when labour and land are removed from capital. All capital is the

result of land labour and usually some previous capital. The return to capital will therefore be a return that can be formally regressed into land and labour. While this is conceptually possible, it presents practical difficulties due to the historical regression into previous capital tools.

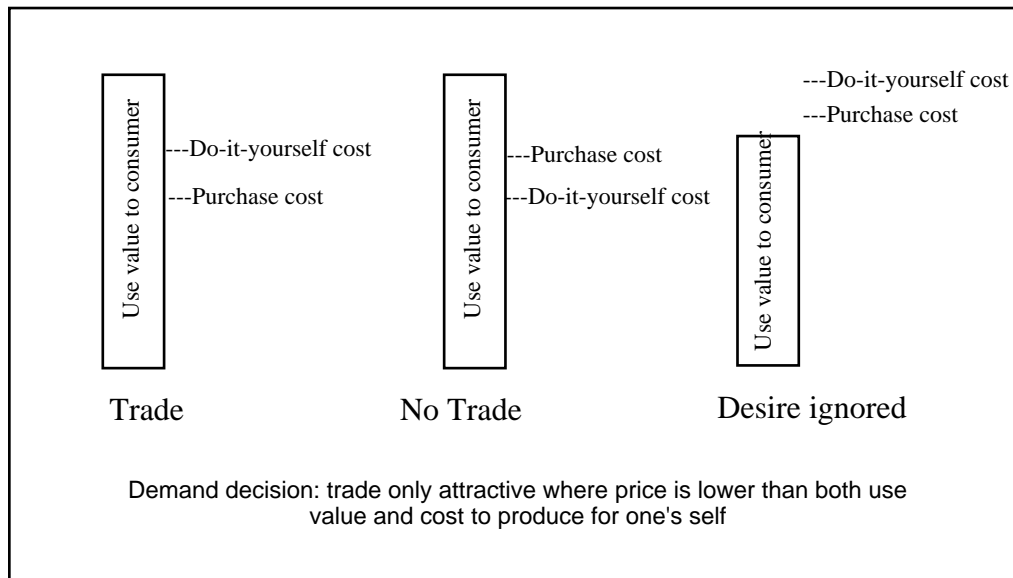
9.2 THE BASIS OF EXCHANGE

Economic exchange only takes place when it is in the best interests of the parties concerned. Modern Western markets have developed to the point where some important fundamental aspects tend to be overlooked. To reclaim a sensitivity to these issues it is first useful to review the conditions under which economic exchange takes place.

A person with a desire for some material thing has three options, to make it himself, to obtain it from someone else, or simply to ignore the desire. The desire is the final cause of the good but is offset by its cost, which is either directly personal or via a third party. Many desires are not deemed worth their cost and left unsatisfied. I may like to have my shoes shined regularly, I may shine them myself, have someone else do it, or conclude that the pleasure of shiny shoes is not worth the time or money. Many human goods are found in each category. It is the inclination to act on a desire that describes essential demand, though economic theory tends to use the proxy of willingness to spend money as the economic demand function. The latter will be referred to as effective demand in this study following the usual terminology, although it should be noted that effective demand is not social demand, i.e. actual need in a society.

The decision to acquire a good follows the personal judgement that the desire is greater than either the trouble to make a thing or the cost to buy it. A person will not buy a thing if it is estimated that the cost to buy it exceeds the trouble of doing it one's self. The decision to obtain a good from the market is therefore the result of the estimation that the price in the market is lower than both the desire for the thing and the cost to produce it one's self. This is shown in exhibit 9.2

Exhibit 9.2 Demand Decision Thresholds

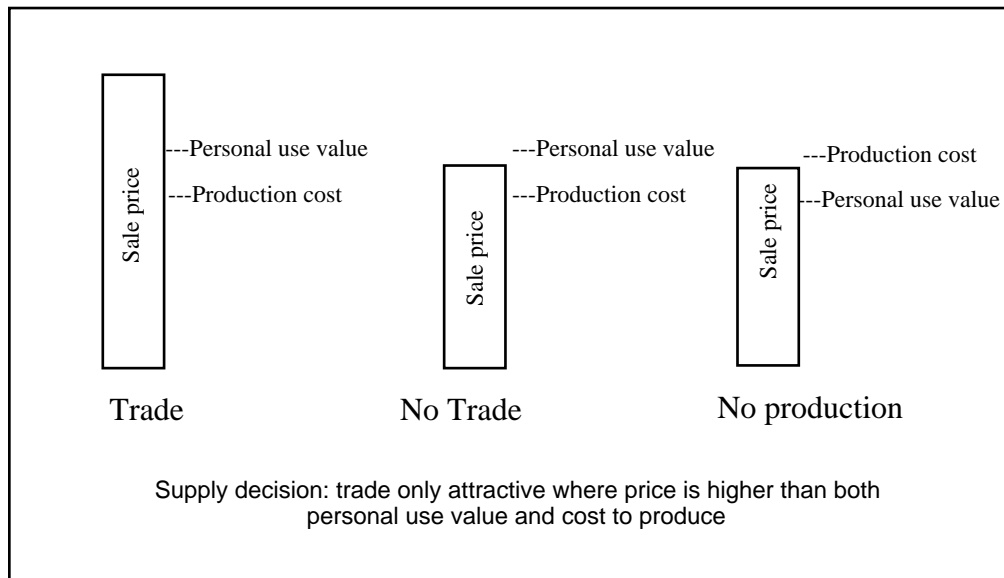


Supply comes from a person, or economic entity, that has the capacity to produce goods that are desired by others. As persons, producers also have some personal need or desire for their own goods; the cobbler wears shoes. In a moderately developed society some producers will be found who are more efficient than others in particular productive arts and hence they will be able to produce specific goods with a minimum of toil. They may be expected to be able to produce things at a lower cost than unskilled individuals producing for themselves on a one-off basis.

To the extent that producers may also have a desire for their own goods, their inclination to sell them may be tempered by their own needs. That is, a producer could be expected to only want to exchange a good when the price offered exceeds both the producer's costs to produce the thing and the producer's own desire for the good. Aristotle alluded to this when he described the two uses of a shoe, one is to wear, and the other is to trade⁷⁴. This observation has several implications. In a commercial exchange there are three uses, or final causes, to be considered, wearing by the buyer wearing by the seller, as well as the seller's use of the shoes in order to trade for other needs. In general the producer will have his own use needs met and his product may even have negative personal use value. - the cobbler is inconvenienced by excess shoes clogging up his shop. The producer's decision possibilities are shown in Exhibit 9.3

⁷⁴Aristotle was considering only wearing by the buyer in his example, though St. Thomas added the importance of use by the producer to the analysis of trade.

Exhibit 9.3 Supply Decision Thresholds



In both cases it should be obvious that the parties should be free to make the decision. This implies that they have the right to set the thresholds discussed. All of this would appear to lead to the simple conclusion that trade will occur when the price is higher than the two supply thresholds (cost to produce and producer's use value) and lower than the demand thresholds (use value and cost to personally produce), however, it does somewhat more. The problem is that the discussion to this point do not resolve the question of exactly where the price should lie. There are four thresholds, two use values and two costs to produce and it would appear that any one of them can act as a limit to price. There is also no indication as to how much latitude may exist between the limits set by demand and supply, suggesting that the uncertainty may be quite sizeable in some cases.

In discussing this problem the terms *demand threshold* and *supply threshold* will be used to refer to which ever cost or utility threshold is critical for the purchaser or producer respectively, unless otherwise noted. The resolution of this question has been most successfully attempted within the general topic of the just price.

9.3 JUST PRICE

Just price refers to pricing that is moral, recognising that market transactions may not result in just outcomes for the participants, despite being apparently free. Just price was one of the key components in Medieval economics, closely associated with usury. Historically the notion of just price appears to have been based on the recognition in Roman law that sometimes fair prices had to be assessed, such as in the case of compensation (Goyder, 1993). Violations of these principles were considered theft in a

culture that understood that unrepentant thieves earned eternal damnation. The Roman law adopted the principle that, "...a willing party cannot be harmed" meaning that in a free market transaction neither party can claim that they were unfairly affected by the price struck (Langholm, 1992). It is now commonly held that the Scholastics adopted this principle, meaning that the market was the best final arbiter of just price (Chafuen, 1986; Dempsey, 1935)

As economic and moral thought progressed through the late Scholastics, both usury and the just price tended to be submerged in a belief that the prices for both were found as a result of common practice, as was found in the operation of the free market and common estimation (Chafuen 1986). Although they have considerable commonalities, usury was more explicitly sanctioned with legal as well as moral prohibitions, which makes its transition from moral determination to common practice more conspicuous. Once the free market emerged as the arbiter of justice in pricing, usury could then also find a validation in common practice and in the sixteenth century Henry VIII legislated that an interest rate of up to 5% was licit (Goyder 1993). The transition to market determination was also evident in changes in the behaviour of the guilds where standards of quality and responsibility gave way to self-interested commercial success around the end of the fifteenth century (Welshman, 1964).

While markets were a part of commerce in Medieval Europe, it would appear that there was something additional that marked just price. The market itself is an enigma because it has been shown to gravitate towards equilibrium prices that are cost based, though its practical resolution draws heavily on use-value as utility motivates demand. The purpose of this section is to review the fundamental issues involved in the construction of just price, especially the possible sources of licit price and use these to examine the capacity of the market to arrive at just prices. This examination will be used to construct a theory of property and price, and use it to demonstrate the pivotal importance of land in its resolution.

Aristotle distinguished between two types of exchange which has provided the foundation for some of the most important debates through the history of economic thought (Aristotle 1992, 1256b40-1258a18). His two exchanges are referred to as *natural* and *unnatural* exchange. Marx borrowed and expanded the distinction, demonstrating that unnatural exchange was the centre-piece of capitalist activity.

9.3.1 Natural Exchange

Natural exchange is the exchange of one good for another. Barter is the simplest example of this and in a free exchange it is evident that the values of the goods involved will be equal. Money is known as the medium of exchange, a store of value and an indication of worth. Aristotle recognised that it allowed a person to liquidate a

surplus good into its (equivalent) value and use this store of value in a second exchange for a desired good. The use of money was more convenient and flexible than barter, but depended no less on equality in exchange. In this way, persons were able to obtain those things necessary for life.

There are several dimensions of naturalness in this form of exchange. Persons were able to satisfy the needs natural to their human condition; money was used according to its nature; natural equalities between goods were respected. This type of exchange was also deemed *economic* by Aristotle because its end was the material needs of the household and consistent with sound household management. The extent of natural exchange was limited, because the goods acquired were directed towards material needs and as the needs were met the motivation for exchange to satisfy was amortised. This is essentially what is known today as the law of diminishing marginal utility: there would come a point where persons would no longer need exchange because they would have enough to satisfy their needs. This tendency is seen today in some indigenous cultures where work stops when the immediate needs are satisfied. The limitedness of human material needs is natural.

Marx summarised this type of exchange using the symbols:

$$C-M-C$$

where the "C's" refer to commodities and the "M" refers to money as the medium.

9.3.2 Unnatural Exchange

The second type of exchange that Aristotle identified was termed *unnatural*, or *chremastistike* (for the market). While both natural and unnatural exchange occurs in the market, unnatural exchange does not have the final end of household use. Unnatural exchange begins with money, which is exchanged for a good (*commodity*, for Marx), which is later exchanged for money again. This is the behaviour of the merchant who uses money to buy goods for resale, the point of the exchange is to sell the commodity for more than it was purchased for, that is its end is money. The usual expression of unnatural exchange is:

$$M-C-M'$$

where "M'" is a greater amount of money than M. Note that the commodity must have two prices (M and M') which is difficult to explain for the one good.

This form of exchange is unnatural because it does not use money as the medium of exchange, but the termini and also because the exchange is not based on equality because one amount of money (value) is transformed into a greater amount of money, yet money is supposed to be an indicator of value. Desire for money cannot be satiated in

the way that desire for food has a natural limit because it does not satisfy any desire (except avarice). Aristotle was concerned because unnatural exchange appeared to usher in inequality and hence injustice. If it is an injustice it could be expected that it should violate the goals of social economy and lead away from *appropriate relations*.

Because financial assets satisfy no desire apart from the desire for more money, it should come as no surprise that Aristotle considered that they must be aligned with unnatural exchange. Hence money changing and interest on loans were also considered unnatural or worse in Aristotelian thought (Langholm, 1984).

Aristotle's preference for equality, proportion and balance was violated by unnatural exchange because it implied a duality of price. This cannot be explained by factors such as transport, etc. because these would contribute to the commodity's price in natural exchange. The transformation of one amount of money into a greater amount was interpreted as a form of injustice.

The immorality of the practice was tempered by at least two factors. Firstly, price was recognised as a value that could not be known precisely. Hence, there would be some opportunities arising from the imprecision in pricing, even though prices generally were accurate. Taking advantage of these anomalies was considered reasonable and may even be necessary in order to avoid local social imbalances.

Secondly, if the merchant applied himself diligently to his work and only took sufficient income from his unnatural exchange to provide for his own needs, his income was not considered immoral. Diligence and self-restraint still provided moral limits in this case. The application of excess income to charitable works was considered also to be a licit use of unnatural exchange (Meikle, 1995).

Apart from these instances unnatural exchange was considered immoral as a form of theft.

9.3.3 Basis for Price

A key issue in consideration of exchange is exchange value, or price. To distinguish natural from unnatural exchange it is necessary to be able to specify what the price of a good should be. Price is usually quantified by money. What does money quantify as an indicator of value/price and what does it represent as a store of value? Adam Smith identified the possibilities when he teased out the notion of value into use value (utility), exchange value (price) and cost (ultimately labour). Most pre-twentieth century political economists, including Smith, held varying forms of labour theories of value which have been replaced in the last century by a utility theory of value. The first issue in identifying justice in pricing is therefore to resolve the question of which value theory is capable of returning prices suitable for natural exchange.

Aristotle appears simple and clear on what is equated in natural exchange, "...*this standard is in fact demand*" (Aristotle 1976, 1133a13-31)⁷⁵. Demand relates to desire, or in Aristotelian terms, final cause. It is not surprising that Aristotle would chose demand, or the final cause of production, as the dynamo for the market because the final cause is also known as the *cause of causes*. Without it there would be no trade and no production. The other causes can be varied, but the final cause cannot be changed without changing the thing. Demand suggests that prices that are determined by use value or utility and this has been accepted by many economic theorists, not the least being the Austrians.

Both Aristotle and St. Thomas have been quoted suggesting that an exchange that equates utilities will be just. This may be reasonable for goods that are exchanged in some way remotely from the event of their production. For example in the case of well used goods being traded. It may be noted that finance theory values investment assets on this basis, as the present value of future returns. That is, a stock or bond is valued entirely in terms of its expected future money benefits, its financial usefulness. Land appears to be treated likewise through capitalisation of its future rents.

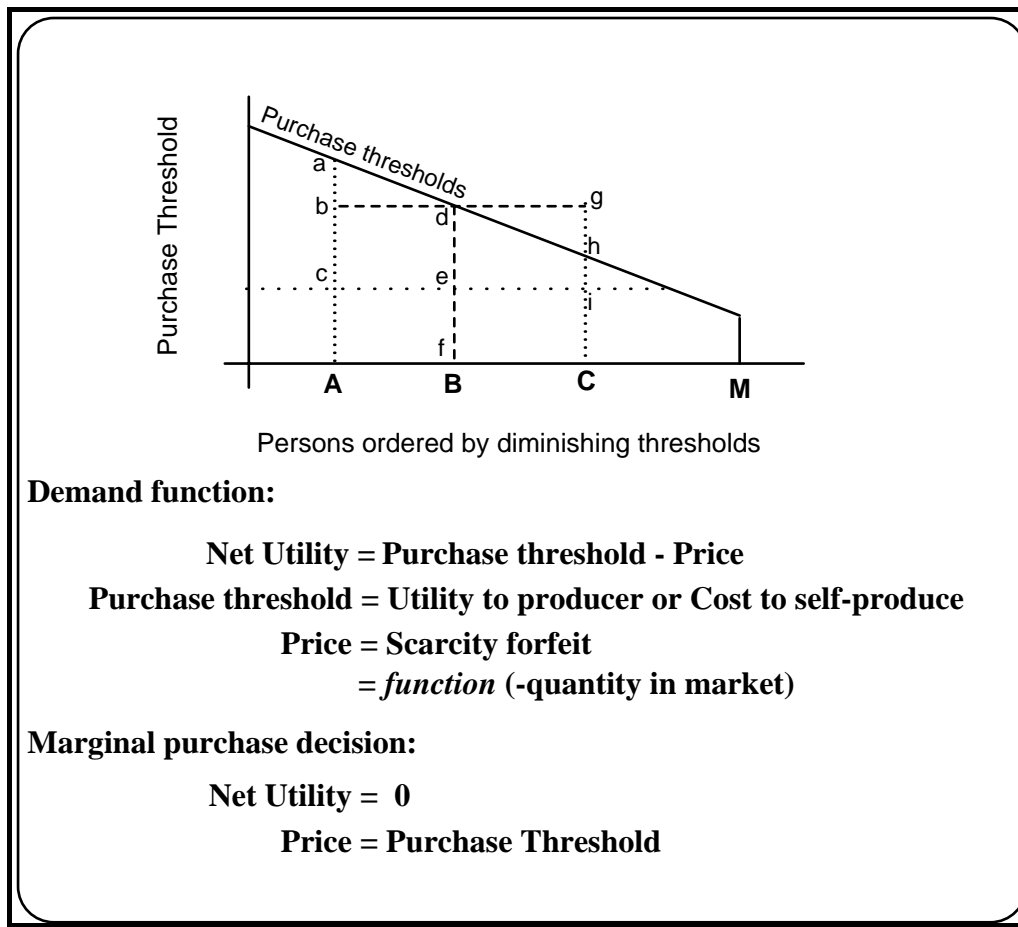
In the case of material goods, especially close to either their source as raw materials, or the productive event, utility pricing breaks down. Consider water, it has a very high utility value, life cannot exist without it, yet it is provided at a very low price. A man dying of thirst may be prepared to pay a fortune for a little water, and there may even be several potential suppliers, but the price would not be considered just. More generally, if the owner of any resource or productive capacity priced his product at its utility value, then he would be retaining the full use of that property. If private ownership with common use is upheld, this would be immoral.

In the case of produced goods sold immediately after production, market pricing by utility value (use value) can be shown to be problematic as an expression of natural exchange. If the market achieves natural exchange by equating utilities, it must result in prices from balancing two utility functions. The demand function is said to be a utility function to the extent that it represents the utility to consumers at different quantity levels, expressed as price. Supply is also a utility function, being likened to demand by Wicksteed (1914) who observed that. "...*what is usually called the supply curve is in reality the demand curve for those who possess the commodity*" (p.15). The utility that the producer seeks is profit. When Aristotle observed the two uses of a shoe, he noted that one was the utility of the wearer (consumer) and the other was its use for

⁷⁵Meikle (1995, pp.28-42) studied the use of the word demand in English translation of Aristotle's Greek in the this section of his work. He suggested that Aristotle's text was far less definite. In some cases recent trends in translation reflect preconceived expectations consistent with modern thought rather than Aristotle's actual words.

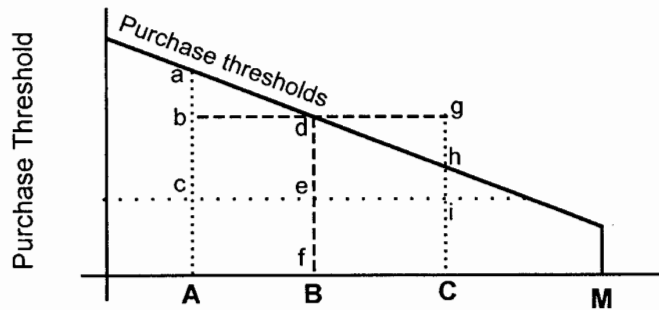
sale. Clearly a good that sells for more is more perfect in its use for sale, it affords greater utility to its maker. The market functions represent the net utilities to the consumer (demand) and producer (supplier). As one increases, the other decreases, until a compromise is found which becomes the price. This appears to balance the consumer and producer completing the earlier discussion of thresholds. In a balanced market it may be attractive to conclude that a fair price would be one that is midway between the supply and consumption thresholds. However, what are being balanced are not utilities at all in any natural sense.

Exhibit 9.4 Demand Function



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Exhibit 9.4 Demand Function



Persons ordered by diminishing thresholds

Demand function:

$$\begin{aligned} \text{Net Utility} &= \text{Purchase threshold} - \text{Price} \\ \text{Purchase threshold} &= \text{Utility to producer or Cost to self-produce} \\ \text{Price} &= \text{Scarcity forfeit} \\ &= \text{function} (-\text{quantity in market}) \end{aligned}$$

Marginal purchase decision:

$$\begin{aligned} \text{Net Utility} &= 0 \\ \text{Price} &= \text{Purchase Threshold} \end{aligned}$$

9.3.4 The Demand Function

The demand function is best considered as a sociological decision function. Utility is the capacity of a thing to satisfy a human need or desire. The ability of the good to satisfy the purchaser's desire is not altered by its cost. From the perspective of the purchasers' utility, purchase price may be best thought of as a *scarcity forfeit*. It simply negates the utility derived from owning the thing, and may be pushed higher when supply is more limited.

Different people have different demand thresholds. If individuals were ordered by diminishing purchase thresholds, for any given price there would be a person for whom the *scarcity forfeit* (price) equals their purchase threshold. This person will be indifferent to purchase. If the person purchased the good at that price, they would have no net utility. This is shown in Exhibit 9.4. For a price of f-d, purchaser B will be indifferent to the purchase and the volume traded will depend on where in the queue of diminishing thresholds person B stands. Taken cumulatively, this is the demand function. Purchasers with higher purchase thresholds, say at level A, will experience a net utility of a-b, while potential purchaser C will not purchase because of a dis-utility of g-h. It is not a true utility function, because it does not reflect the utility of any but the marginal purchasers (level B). It will have a monotonic negative gradient because it is a cumulative function.

The decision threshold itself is not necessarily an expression of utility at all, as it may be the purchaser's cost to self-produce. While the utilitarian may object to this observation as hair-splitting, and respond that cost is actually negative utility, it should not be passed over. If the enquiry is aimed at arguing towards either cost or utility as the basis for just price, the fact that they cannot be differentiated out of the demand function would appear to suggest that the question is more difficult than it first appears.

To be strictly accurate, the independent axis should be unit-purchase thresholds to accommodate the fact that *some* persons will choose to purchase multiple units of the product following the principle of diminishing marginal utility. The fact that the majority of purchases in any given market for economic goods⁷⁶ are not multiple purchases, points up a major difference between this construction of the demand function and its common explanation. A restaurant may have difficulty selling multiple meals to patrons, regardless of price, because of their diminishing marginal desire for additional lunches, but this is not where the restaurant needs to direct its pricing strategy. It must price its product to attract sufficient passers by to fill its tables at each

⁷⁶Economic goods are goods, including tools and productive equipment that satisfy an actual material desire. They exclude financial assets, which Aristotle would have difficulty accepting as capable of being used in natural exchange.

sitting, each of whom will have a different purchase threshold. The markets for lawn mowers and steel mills are no different. By contrast, the markets for financial assets tend to be the exception to this tendency, and it may be that modern economic theory is modelled unduly on these cases.

For every purchaser except the marginal one, the price represents a positive net utility, and all purchasers would prefer a lower scarcity forfeit. For absolute necessities, such as air, the scarcity forfeit must be low enough to allow for the lowest purchaser threshold. This explains the pricing of water, but it does not explain why many potential purchasers are effectively excluded from having their desires met for other goods.

Modern economics usually responds by explaining that the market finds equilibrium at the cost of production, and this is the minimum price that can support stable production. Unfortunately, this would imply that the market cannot operate on utility based pricing because its stable end-point and only reference is a cost. It may mean that the market is a hybrid that balances utility based demands against cost based supply. At best, perhaps what is referred to as the cost of production may actually be a utility. Examination of the supply function informs this question.

9.3.5 The Supply Function

Like the demand function, the supply function is not a utility function in a natural sense. Modern thought would disagree, suggesting that a high sale price means the power to obtain more goods that the producer desires for less productive effort. Both contribute to the producer's utility, therefore the supply function is a utility function. However, these are largely contingent utilities, and even the cost to produce is only a negative utility at best. Similar to demand, supply can be thought of as based on the supply thresholds, but with a market bonus added, as shown in Exhibit 9.5. Supply would appear to offer zero net utility if price merely equalled the supply threshold, either of normal cost to produce, or utility to the producer. The suggestion that the supply function is a utility implies what is encountered in practice, that it is an excess over the supply threshold. The net utility can be thought of as a market bonus, derived from the market price and is a margin above normal costs, consistent with the discussion of supply introduced in Chapter 5.

The merit of marginalist pricing theory is that by locating production at the intersection of marginal cost and marginal revenue in order to set price and maximise profit, it recognises two significant practical aspects of actual markets. The first is that marginal revenue is a given in the determination of the supply function. If the revenue function is a given, it must come from the market and that must mean the demand function. This means that the supply function is constructed from demand. The second

is that it is marginal costs and revenues that are equated, not the average quantities. If price was based on normal costs, then the operating point would be at the intersection of average cost and average revenue and profits would be normal. The fact that it is recognised that price is based on the intersection of the marginal quantities is recognition of some bonus income above that needed for normal profits is a normal part of the commercial environment. These two observations hold despite the criticisms made of this theory in Chapter 5, because they relate only to the general conditions that marginalist seeks to explain that are well accepted. A careful review of the criticisms of the theory show that they relate to systematic errors in the presentation and evaluation of the critical cost and demand functions. There are other ways of supporting these two observations, however, their emergence from commonly held views used as premises for the marginalist theory will be considered sufficient for this thesis as it demonstrates that they are not contentious.

Exhibit 9.5 Supply Function

Supply function:

$$\begin{aligned} \text{Net utility} &= \text{Market price} - \text{Supply threshold} \\ &= \text{Market bonus} \end{aligned}$$

$$\text{Supply threshold} = \text{Utility to producer or Cost to produce}$$

$$\text{Market price} = \textit{function} \text{ (demand willingness)}$$

Marginal supply decision:

$$\text{Net Utility} = 0$$

$$\text{Price} = \text{Supply threshold}$$

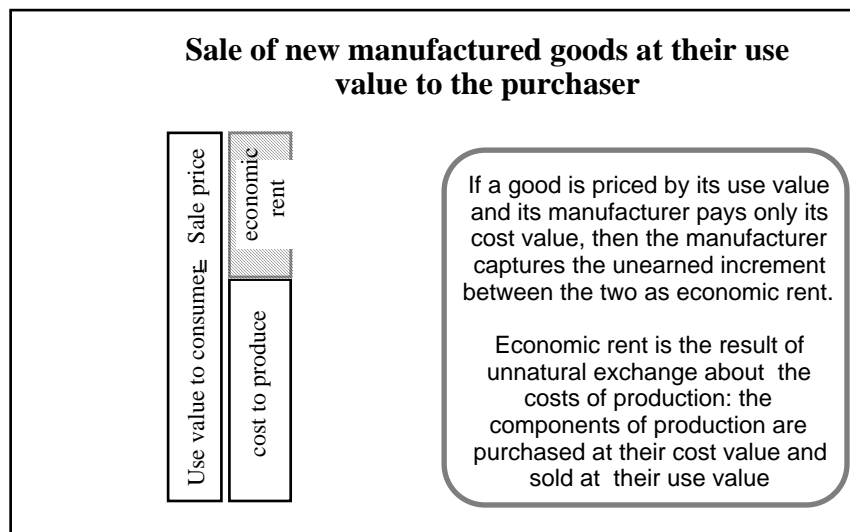
Interpreting the supply function as a utility function therefore leads to the recognition that although it is a utility function, in that it reflects possible patterns of *chremastistike* utility, it must be a function of demand, that is, the purchasers' willingness to pay. It sets price at a level that clears the market and maximises the supplier's utility. The ultimate source of price is the pattern of forfeits that consumers are willing to pay for a given quantity available in the market.

The market bonus taken by the producer is a utility subtracted from the utility enjoyed by the purchasers. It actually appropriates all of the utility of the marginal purchaser. Furthermore, it excludes some purchasers all together. Returning to Exhibit 9.4, if the supply threshold was e-f, but the price in the market was d-f, then purchaser

C would not purchase. The utilitarian argument is complicated by this fact, in that the apparent zero-sum trade off between purchasers and suppliers ignores purchasers who are excluded from participation and therefore their utility is negated. The consequence of this is that the net utility is actually the sum of that enjoyed by both producers and consumers, and this is actually maximised as price is lowered⁷⁷. Overall, it is difficult to see how utilities are in fact *equalised* between demand and supply. Even utility maximisation, which is the utilitarian goal, would prescribe prices set at the normal cost of production, which destroys any argument for utility based pricing. Investigation of supply in terms of utility leads back to cost based prices.

Even ignoring the complications of utilitarian investigation, the existence of what has been referred to as the market bonus can be shown to introduce what appears to be inequality and injustice. The quantity, market bonus, is better known by the expression *economic rent*. Exhibit 9.6 presents the construction of economic rent and will be used to examine the way that prices that balance demand and supply thresholds somewhere about their mid-point, necessarily result in inequality.

Exhibit 9.6 Economic Rent from Mixed Thresholds



For a manufacturer who buys raw materials, pays various expenses including wages and sells finished product, the many transactions that make up the operation of the firm reduce to the purchase of the product in component form, and its sale as a whole. This would not be problematic, except that the costs of production, especially labour, tends to have their cost value as their supply threshold. Consumer goods are priced by the

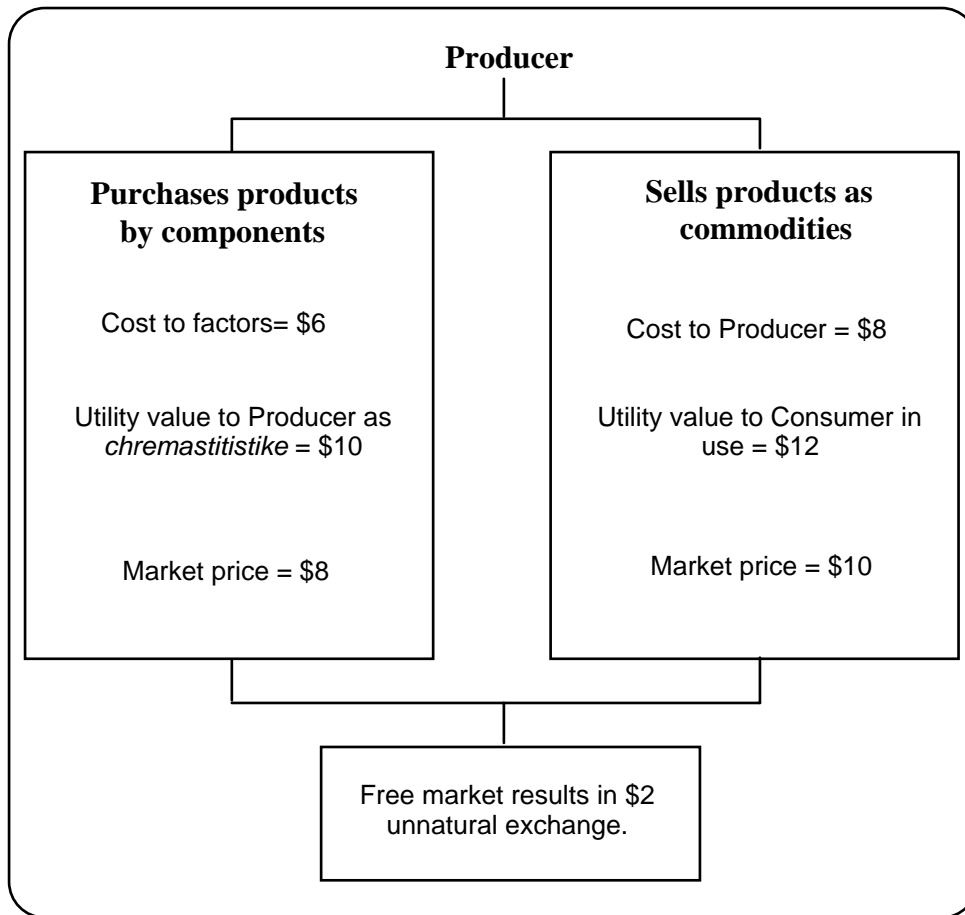
⁷⁷This is because the suppliers' utility is the rectangle below and to the left of the price point (point "d" in the figure if consumer B is the marginal purchaser), which is taken out of the consumers' utility which is the entire area under the curve to the left of the price. As price falls the price point moves to the right expanding the total utility.

market forces as described, which makes the consumer purchase threshold either the utility value or the cost to self-produce. This leaves a significant gap that is pure profit, or economic rent. Even if market forces located price at midway between vendor cost and purchaser utility in the two transactions that make up the process described, unnatural exchange will still result.

For example, consider a product with normal costs of \$6 and a utility value of \$12 to the consumer. In free markets that place price at the mid-point between supply and demand thresholds, an entrepreneur could buy the product (including normal return to himself) at \$8 and sell it at \$10 as shown in Exhibit 9.7. Both transactions are mid point prices between the respective costs and utilities, but result in an economic rent of \$2. This illustrates that mid-threshold prices will tend to result in unnatural exchanges in the common processes that make up current free market commerce.

Marx focused on this aspect of capitalist production and his criticism of it made up a significant part of the theoretical base of his *Kapital*. He illustrated what he interpreted as theft against workers with many examples of the low wages paid to English workers in contrast to the high sale price of the finished goods. The practice appears to have been resurrected in recent times in the form of low wages paid to Third World labour for products sold in the first world (Korten 1995).

Exhibit 9.7 Unnatural Exchange Through Mediated Thresholds



It may be concluded that utility based pricing cannot be found in the operation of the free market because any attempt at natural exchange based on utility through the production process will lead to contradiction or to arguments for cost based pricing.

It may be argued that if labour and land were priced at their utility values this may not be the result. Unfortunately, the sum of the utility values of the factor inputs is equal to the utility of the the product. Such a practice would normalise returns to the intermediaries. It has been seen that because utility value is subjective and at best only evident in the behaviour of the marginal purchaser, it is difficult to see how the factors could price themselves at their final utility⁷⁸. In any case, an attempt by factors to actually price themselves at the utility value of their product would exclude some purchasers (such as consumer C in the example) and lead to a deficient total utility for the whole system. If it were possible for the factors to price themselves at the utility

⁷⁸An average utility could be suggested, but this is really what is presented as person B in Figure 9.4. Anyone below the average, say person C would not purchase and person A continues to enjoy a net utility that perhaps could be argued is the property of the factors. The situation of person A also points up one of the problems of a labour based theory of property and value.

value of their product, they would retain the full use of their property which has been shown to be immoral. Utility pricing does not stand up to close scrutiny.

In practice, utility pricing is closely associated with arguments aimed at justifying liberal free market pricing. Neither utility pricing or market determination of price appear to be capable of yielding natural exchange, at least for economic goods.

9.3.6 Cost Based Pricing

The question of which thresholds set price can be seen to lead into discussion of a major issue in social economics. While Aristotle and modern finance are comfortable with use-value, it leads to injustice when production is considered. The alternative to setting prices by utility value is to base them on costs. Because most costs reduce to labour cost, this approach is usually associated with what is known as the labour theory of value. This is the value theory used by Marx, and most pre-twentieth century political economists.

Barrera is one of the several scholars who have considered the curious fact that St. Thomas appears to have held both a labour theory of value and a utility theory of value. Aristotle is guilty of the same apparent equivocation. In view of the importance that both placed on the final cause as the *cause of causes* it is no surprise that they gave some support to the notion of licit trade as being a market outcome where utilities were balanced. It is possible however, that utility can be retained as the motivator for trade, without it being the source of price.

It has been usual to dismiss the possibility that they supported a labour theory of value because of its adverse implications for free market economics. However, St. Thomas did state in very definite terms that utility value to the purchaser could not be licitly used as a basis for setting price when he stated:

Yet if the one man derive great advantage by becoming the possessed of the other man's property, and the seller be not at a loss through being without that thing, the latter ought not to raise the price, because the advantage accruing to the buyer, is not due to the seller, but to a circumstance affecting the buyer. Now no man should sell what is not his, though he may charge for the loss he suffers. (Summa Theologica Q. 77 Art.1 Pt. II-II)

The final cause of the product is the desire of its end owner for it. It is a part of the final purchaser, composed of his situation, abilities and outlook. It cannot be the property of the producer, even though the producer possesses the product. If I was to chance upon the inexpensive secret recipe for a tonic that would add fifty virile years to your life, you could be expected to have a strong desire for it, however your desire

would be more for your life than for my tonic. I do not own your life and therefore St. Thomas would prevent me from setting my price according to your desire for something that is already yours. You cannot sell people what they already own, that would be theft. The Medieval aversion to theft was only one aspect of the overall community understanding of the importance of justice in exchange in that era as was evident in the significance of the guilds and their relationship to their society (Kurth 1943/87; Small 1999).

The final cause is extrinsic to the product and strictly speaking the vendor's title cannot extend over it. The temptation here is to conclude that the final cause cannot be used as a basis for pricing. This is consistent with several lines of argument. The example of the elixir of life above suggests that I would be taking something of yours if I priced my tonic close to the value that you place on your life. To price by costs, say using a labour theory of value, appears to suggest two major policy directions.

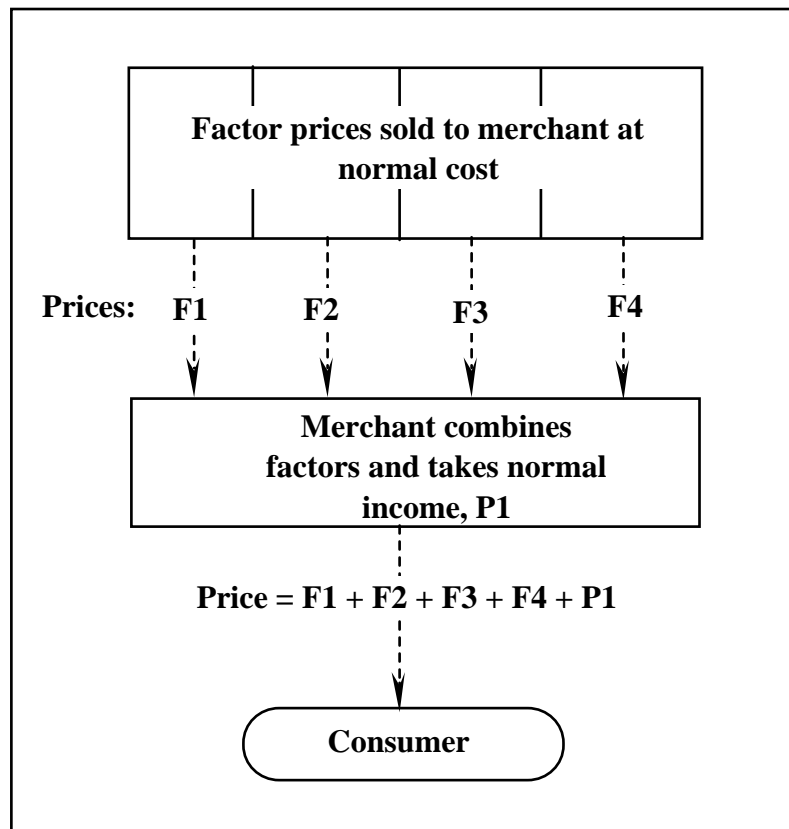
The first cost-based pricing policy is the one that was experimented with by several nations during the twentieth century as various forms of socialism. By and large these have proven problematic in theory and practice. Essentially, they adopt the notion of labour as the origin of production and nationalise what has been referred to in this thesis as conventional property. Pricing may attempt to follow labour costs in an effort keep prices close the cost of production, but the strategy has been through the state as the custodian of productive property. The adjective *statist* has been often applied to the economic decision making in these regimes. It points to fact that as the only property owners, these states exercise the same type of control over they criticise in capitalism. the difficulty appears to be centralised decision making over what remains apparently self-interested societies.

The second approach to cost-based pricing contrasts to this in that it relies on individual persons within the community choosing to price their product by its factor content. This means that suppliers of the factors of production sell them at their cost of production to merchants who sell them as products priced using the factor costs plus a normal income. A normal income to such a merchant would be sufficient to provide for the needs of a diligent merchant at a reasonable standard of living. Diligence and limiting one's self to a reasonable standards of living, suggests decisions that are ultimately motivated by self-restraint. Self-interest aims at an easy working environment delivering a royal quality of life. This is necessarily an ethical position. It will be characterised by:

- The market place will be dominated by prices set *a priori* by vendors but trusted to be reasonable.

- Self-restraint infers as an intention to refrain from benefiting at another's expense, hence, it would be reasonable to trust practitioners in other areas of social responsibility.
- The final cause, demand, remains as the initial motivator.
- A mature market place will be able to recognise true prices through experience rather than demand/supply bargaining.
- Prices that begin at levels that carry negligible economic rent do not admit undercutting up by competitors, so the relationship between similar producers will not be characterised by competition as it is usually understood
- In the absence of economic rents, there is little incentive for the growth in the size of productive organisations that around a year
- Social utility will be maximised along with the other benefits of pricing by normal cost of production.

Exhibit 9.8 Price by Normal Costs



The existence of a market place that trusts vendor's to set keen prices is foreign to Western minds but the existence of price tags on the majority of goods sold in

European countries and their cultural satellites may be evidence of a remnant of such a way of doing business. The self-restrained pricing of factors at their cost price is obviously an instance of natural exchange as shown in Exhibit 9.8. The factors that contribute to production may include such things as transport retailing expenses. Their price attaches to the factors themselves and sum, together with the merchant's income to form the final price.

A culture that practices pricing of this sort may be expected to experience a greater level of equity between its various members as well as several other benefits. Purchasers could trust price to be a good indication of the content of a product so the current requirement for buyers to be able to evaluate all the goods they buy becomes less onerous. This is a social saving. The market place is not dissolved, in the sense that socialist societies tend to operate, but neither is it a battle between self-interested parties bargaining for a bigger share of a fixed total benefit. While the suggestion that cost based pricing solves the problem of the just price and cuts through the problems of the market functions, appears almost too simple to be novel. Voluntary pricing by cost still leaves several issues to be resolved including:

- The problem of non-conformists who prefer pricing by demand.
- The quantification of cost is not resolved because it appears tied to the price of consumer needs.
- How are the contributions of the various factors balanced within the final product?
- The role and price of conventional property is not explained.

The first item relates to the Enlightenment tendency to view human nature as what humans are seen to do. This notion of nature infiltrates Smith's economics despite his occasional exhortations towards higher ideals. In the market place humans have a tendency to want more than their share and Smith was subtle enough to be able to see how this tendency could still be used as the foundation for the flourishing of society. The problem of humanity is the tendency for people to act in anti-social ways, despite reason being able to demonstrate a more effective choice.

In most cases, the mark of civilisation is self-restraint and one of its fruits is trust. Humans appear to need to learn to will self-restraint for the good of others and it appears to be one of the principle challenges of human personal development. All human ethics consist of self-restraint of some kind, though for most the habit ceases to be the duty that Kant saw as the totality of ethics. The various aspects of civilisation are learned and socially reinforced. There is evidence historically that they can both rise or fall over time. Self-restraint in the market would appear to be no more than another instance of an ethical principle that may be adopted or omitted by an individual or a society. It would appear that the costs and benefits of these choices could make an

interesting study in themselves, but that would be beyond the scope of this thesis. Suffice for the present is the recognition that self-restraint is a possible and practical virtue.

The choice to charge on a normal cost basis with acceptable accuracy would also appear to be practical, given the previous discussion of accuracy and precision, and the information available to most participants in the economy.

The remaining items point to the need for a more complete theory of property and the place of land in pricing. The metaphysical construction of property goes some distance towards providing a basis for this theory and a review of Ricardo's rent theory can be used to place land.

9.4 CAUSAL ORIGIN OF PROPERTY

Aristotelian causality can be used to resolve this problem by examining the limits of property using a metaphysical approach. Aristotle recognised what have become known as the four causes of being. A thing exists as a result of four separate causal factors as follows:

Material cause: the raw materials that compose the thing.

Formal cause: the design, (blueprint, shape) of the thing.

Efficient cause: the maker, including the tools employed

Final cause: the desire for the thing, need or demand

These are as much practical observations about actual things as they are deep philosophical concepts. For example, shoes exist as a result of a shoemaker forming leather into a particular pattern (the efficient, material and formal causes, respectively) as shown in Exhibit 9.8. In addition to these, the shoemaker would not be motivated to produce the shoes unless there was some need or desire for them, this is the final cause.

Exhibit 9.8 Consumer Product Title Through Causal Composition

Material Cause	The owner of the raw materials has title to that part of the product that comes from its raw materials. Raw material are often partially manufactured products
Formal Cause	The designer: the design of the product is the result of the work of a human designer who devotes part of his life to the production of the design
Efficient cause	The maker: expends part of his time and effort, his life, in causing the thing. He uses tools as instrumental efficient causes and these share in the title due to efficient cause

To apply this to economic production and property, the four causes can be related to their owners. The shoemaker devotes time and effort to the production of the shoes. The time spent is a part of the shoemaker's life and therefore naturally belongs to him. Likewise the shoemaker's effort is naturally the property of the shoemaker. This suggests that the shoemaker has some title to the shoes in proportion to his contribution as efficient cause.

The shoemaker may licitly trade his interest in the shoes, either by selling the shoes, or by accepting wages. In his way title to that part of the shoes is transferred to others. Where the shoemaker employs tools in acting as the efficient cause, he must share his title to part of the shoes through his action as efficient cause with the owner of the tools. While the split between labour and capital appears to be the fundamental problem of distribution in capitalism, it may also be resolved using the same method, as shown in Exhibit 9.9.

The designer of the shoes supplies the formal cause of the product. Title to the formal cause can also be grounded in the fact that design is the result of human effort of some sort. The designer must learn how to design and must devote time and effort to the work of producing a particular design. Like the shoemaker, the designer invests part of his life in producing the design that eventually differentiates shoes from a mere piece of leather. Because the designer devotes a part of his own life, to which he has natural title, to the formal cause, he justly holds title to that part of the product that is due to design.

Exhibit 9.9 Property Title to Tools Through Causal Composition

Material Cause	The owner of the raw materials has title to that part of the tool that comes from its raw materials. Raw material are often partially manufactured products
Formal Cause	The designer: the design of the tool is the result of the work of a human designer who devotes part of his life to the production of the design
Efficient cause	The maker: expends part of his time and effort, his life, in causing the tool. He uses other tools as instrumental efficient causes and these share in the title due to efficient cause. The process may be regressed (at least historically) to a purely human efficient cause.

The owner of the material cause contributes a necessary component to the product, and thus holds title in a manner similar to the efficient and formal causes. Title in this case is not due to investment of part of one's own life, but only due to a conventional right to particular raw materials. Raw materials here include the sites used for production. By adopting Adam Smith's factors of production, land, labour and capital, the material cause can be understood as Smith's land factor. As previously discussed, the leather in the example is actually a product that has embodied within it human title holders through its formal and efficient causes. These hold titles to part of the leather similar to the shoemaker and designer. However, assuming the leather came from a wild beast, title to its material cause cannot be located in human time and effort. All intermediate raw materials can be regressed to human and natural (gifts of nature) causes as shown in Exhibit 9.10.

Exhibit 9.9 Intermediate raw material title through causal composition.

Material Cause	The raw materials used to produce the partially manufactured intermediate raw materials are licitly owned. Just title to them commutes to just title to that part of the partially manufactured intermediate raw materials that are the result of their own raw material component. this train of ownership regresses to raw material components that are not manufactured, but are owned.
Formal Cause	The designer: the design of the partially manufactured intermediate raw materials is the result of the work of a human designer who devotes part of his life to the production of the design
Efficient cause	The maker: expends part of his time and effort, his life, in producing the partially manufactured intermediate raw materials. He uses other tools as instrumental efficient causes and these share in the title due to efficient cause.

Aquinas considered that it was licit to claim title to things found ownerless, so long as such an acquisition was not used oppressively. Hence the material cause is the property of the person who somehow appropriates the right to it, but only if it is not used oppressively.

The shoes in the example therefore consist of at least three joint owners, the makers (efficient cause) the designers (formal causes) and the owners of the raw materials (material causes). Each of these causes may be themselves compounds of prior causes, but all reduce to property rights originating from either title to human life or appropriated title to the gifts of nature.

A criticism that is sometimes levelled against labour theories of value and may appear appropriate also in this case is the impracticality of the suggested dissection of titles. To subdivide each of the three causes considered into their components and continue the subdivision until only purely human effort and gifts of nature are the causes is impractical for any one product. However, much of this subdivision is already done within the day to day workings of productive economies. Each productive organisation in a modern economy divides its revenue amongst the causal components of that level of production. Accountants routinely perform this task in preparing the *Profit and Loss statement*, and the dispersions to causes are labelled *expenses*.

If each producer already divides returns between the various causes then the need for a global dissection disappears. The question is not so much a matter of computing a global set of partial title holders to a given consumer good in order to compute a price, but only that there is a reasonable attempt made at each level to ensure that the set of title rights is adequately balanced at any particular level.

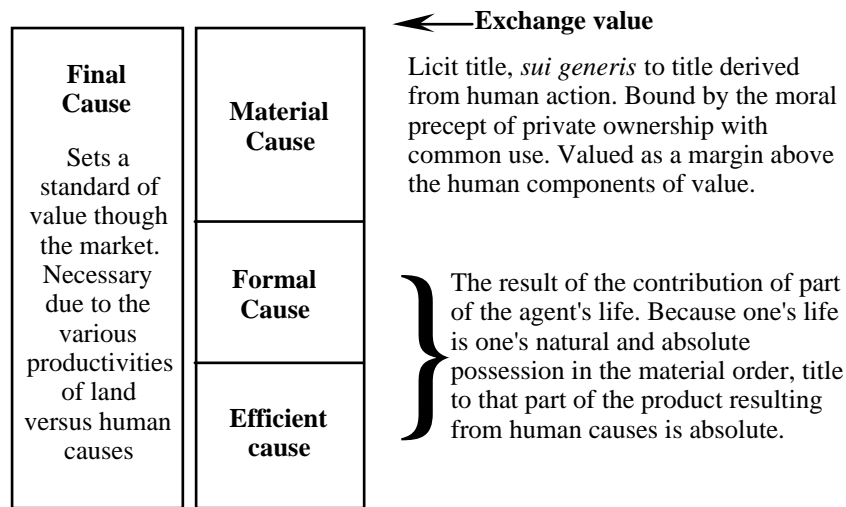
More generally, this causal theory of property rights may appear to be moving towards a labour theory of value, but it is not. A labour theory of value would not attribute a value to the material cause, as this is not the result of human labour, however just title is accepted over raw materials (Smith's land factor). What has been omitted to this point is the contribution of demand, the final cause. To this extent, this causal construction of private property does appear similar to a labour-based theory, but it will be shown that prices necessarily depend also on demand via the market.

The problem with a construction of value that ignores the final cause becomes evident when one attempts to value the material cause, gifts of nature that are the material base of any product. These may be referred to as the land component and include both the raw materials consumed in the production of a thing, those consumed in producing the tools used and also the ground rent of the land whereupon the manufacturing and commerce takes place.

It has been seen that the three causes may be separated and regressed into two classes of title, each of which is composed of various elements that combine into the three immediate causes of the final product. These two classes of title are titles that come from the investment of one's life (labour), and title that comes from the investment of gifts of nature (land).

It is not intended to challenge the right of the landowner to ownership of land, although this has been the conclusion of some theorists who have approached this problem. Title to land is ownership. It is ownership validated by the arguments of Aristotle and St. Thomas Aquinas. It is property resulting from the causal participation of matter in the existence of the product. But St. Thomas recognised that "*because the division of possessions is not according to the natural law, but rather arose from human agreement, which belongs to positive law,...*" (Aquinas 1981), Pt II-II Q66 art.2, 1471]. Property in things found that were once common (land and other gifts of nature) is therefore a conventional property, not natural property. It is property in the product analogous to the labour property. Property in land is property *sui generis* to natural property.

Exhibit 9.10 Product Price by Property Cause & Title Components



Fundamentally, the material cause has no cost of production and therefore would appear to have no defensible market price using the strategy of perfect market competition. Its only value comes from its necessary participation in the final product that in turn has a utility value as final cause. If land was in unlimited supply and all equally productive, it could carry no price. Land ownership would not confer special economic power and the question of the moral validity of ownership would not occur. However, land is neither of these things. Hence these two essential qualities of land (*qua* material cause) make it possible for landowners to expect a return for its use.⁷⁹ The morality of ownership is not intrinsically connected to ownership *per se*, but rather to the economic power that it affords. The economic power relates to use and the appropriation of the material benefits flowing from use. This is not a power that is naturally the property of a human owner, despite the fact that in the practical order private ownership is the most effective way to ensure the best care and use of a thing.

9.4.1 Material and Formal Causes: Natural Property

The contributor of labour to a product has a natural title to part of the product in proportion to the amount of the person's life that is contributed to the product. The person's dignity as a human being suggests that the person has a just claim to sufficient of the value of the product to support that person's life in proportion to the person's material needs. These latter are a function of the amount of productive work that has been contributed to the product compared to the total for a given period and the relative standard of living that is appropriate for the person. Obviously, a person's contribution

⁷⁹If land was available in unlimited supply, but with varying productivity, the situation is effectively a free frontier; if land were uniformly productive but in limited supply, landowners could extract a rent from the landless because land is a necessity.

to production may vary with skill, responsibility and risk, and these variations justify varying levels of reward expressed in varying standards of living. The Medievals appear to have been very conscious of this variation, expressing it in their understanding of just price as sufficient income to maintain the producer *according to his station* in the society.

The notion of station in society is alien to Western thought but may be explained by the fact that Aristotle had no place in his economics for many occupations that modern life remunerate most comfortably. Medicine and education were not considered economic because they did not provide material goods. Likewise, the degree of responsibility attached to occupations was not developed beyond a general recognition, going back to Plato, that they would need sufficient remuneration to attract practitioners. The problem of the non-economic occupations can be partly resolved by a review of the limited scope of production in Aristotle's thought. Part of the problem, as well as the problem of responsibility can only be resolved outside of economic analysis by admitting social values beyond the material.

Beyond skill, some occupations involve particular responsibilities and therefore are allocated a status that is reflected in a higher personal income than would appear proportionate to the toil involved in the work. A good example is a tribal chief, who may toil less than his fellows but be cared for better. The rationale for his higher income is based on the importance of his role in directing the tribe. It is understood that the tribe is better off when the chief has the material resources sufficient free him from having to waste his time on material issues when his role necessitates his whole attention to more weighty issues. The same is true for the surgeon and a range of modern occupations. These issues will be considered further in Chapter 13 in dealing with subsistence wages and also economic rents accruing to labour.

The basic claim by those who contribute their labour is therefore related to their life. At a minimum, this would infer pricing of the life contribution within products based on an objective estimate of the cost of maintaining a labour unit. This is partially social because it requires a community determination of how much life should be supported. Adopting a basic family as the unit of labour, how many hours per week should the labour unit contribute to external work to generate the income necessary for a week's subsistence? How old should children be before they are considered separate labour units? What health risks may be tolerated by workers? What standard of living is considered basic? In the West this may include a car, a colour television and a telephone, while many in the Third World would find clean water and reliable food sufficient. These are representative of non-economic issues that surround the question of a basic wage rate. Once these are resolved, it is possible to set an objective basic

income level, and there are several examples of this calculus having been successfully completed for various purposes (Ederer 1995)⁸⁰.

In addition to the basic call on sufficient income for the survival of the labour unit, there is also a relative dimension to the claim for income by labour. Human nature is social, and if it is assumed that society is engaged conscientiously in production, then each labour unit has title to an appropriate proportion of the society's product. This may not be the case for persons who consciously avoid participating in society's productive activity, although even those people deserve some degree of maintenance. It does mean that if society's level of production is generally rising, all members of that society have a right as conscientious participants in the society to some share in the benefit. This is implicit in the notion of needing to set subsistence wages in accordance with the society's norms, Bangladesh and Germany have different understandings of what is a subsistence wage. Since humans are the same in both countries, the difference can only be justified on the basis that Germans have a greater entitlement because they are Germans.

This notion of participation is alien to Western economic thought. Despite considerable national economic growth incomes for US high school graduates fell by 20% between 1979 and 1994 (Davis 1999) and the British experience is little different (Douthwaite 1992). Regardless of particular opinions regarding the degree of participation by ordinary people in the economic progress of society, it may be concluded that the claim of labour for income follows from their natural title to products following from their natural right to their life. The balance between objective and social quantifications may be still in need of clarification, but a socially determined basic standard of living as the due of conscientious working people must be acknowledged.

In this way conscientious working people have natural property in products due to their contribution to them as material or formal causes. Title to those contributions is derived from human properties. Properties of things are necessary and absolute parts of them. This suggests the nature and extent of personal natural property through the material and formal causal factors of products. The natures and values of those properties absolute but limited. Their valuation is connected with the value of life, or at least sustaining it. To misappropriate this property, which could be done by incorrect pricing of it in sale would be theft. The market has been described as driven by relative negotiational strengths and not by an acceptance of absolute prices. It would appear that the market is an inappropriate pricing mechanism for natural property.

⁸⁰In addition, estimations of poverty levels, for which there is a considerable literature imply knowledge of the threshold income (Prasch 1999).

9.4.2 The Material Cause: Conventional Property

The owner of the material cause has no natural claim for the support of his life, as none was surrendered in the act of production. It may be that supervision of his estate may occupy all of his time, in which case an argument may be made for the landowner, but this is a distraction from the essential issue. Such supervision, if necessary for reasonable and efficient management of the material resources, is actually labour, and not strictly speaking a true return to land⁸¹.

Given that land has varying productivity and is in limited supply, the owner of a particular parcel can demand a return based on one of two grounds. Firstly, through the labour saved on more productive land and secondly, through monopoly⁸². The value of these interests cannot be assessed intrinsically in the same way that the labour interest can be. Even the return due to higher productivity (the labour saved), while appearing to be quantifiable in terms of the labour saved, cannot be evaluated without reference to the market price of the product. This is because the value of the labour saving is a function of the value (as selling price) of the product⁸³. Likewise, the return as monopoly follows from the gap between the market price of the product and the cost to produce and is appropriated by land because the land is necessary for the productive endeavour. This is especially the case when planning limitations place an artificial limit on appropriately zoned land.

Products are therefore constructed from two types of interest, labour which can be objectively priced on the basis of the cost of supporting the labour unit, and land, which has no cost but does contribute to the utility value of the product in various ways. Determining wages by supply and demand for labour risks violating the labourer's property. Even allowing the labour market to pay unnecessarily high wages could be seen as violating property rights, because it would be paying labourers more than their due, which would be theft from some other⁸⁴. Labour does not suit market determination. The price of land, or more accurately its rental value, is a derived quantity being the gap between sale price and costs to produce. It cannot be determined unless some price (exchange value) is placed on the product.

Product prices must be determined by common estimation because products do not have determinant costs (land cost cannot be resolved before product price), and the most effective form of common estimation appears to be the free market. If products

⁸¹The landowner could retain a property manager on wages and avoid the personal toil, in which case the net return after paying the manager would be the land rent.

⁸²Adam Smith described land as a form of monopoly, though *oligopoly* may be more accurate.

⁸³For example, if the more productive land produced only sufficient to support the occupier, it would have negligible land value and the less productive parcel would probably be deserted.

⁸⁴It is not intended to make too much of this possibility as it deserves specific treatment under the heading of just wages which is beyond the scope to this study.

were priced by their full utility (use) value, the consumer would enjoy no net use value from their use, which would flow back to the factors of production. This would violate Aristotle's condition of common use on property⁸⁵. The market operating in this capacity would still perform its allocative and informative functions.

The discussion to this point assumes that the various quantities can be known with accuracy and precision. In practice this is not so, however it does not provide a substantial difficulty. St. Thomas recognised that the just price could not be precise and this will be explored further in discussion of economic rents. At this point it is sufficient to note that one cannot hide behind imprecision when one is benefiting from an underlying systematic inaccuracy. Accurate pricing would result in negative errors and positive errors balancing out over the longer term, whereas erroneous pricing may still lie within a commonly accepted band of uncertainty but result in a long term bias in the outcome⁸⁶.

Overall, the pricing for products is seen to be well served by the free market, especially when the market place is inhabited by self-restrained participants. This is satisfying because utility value is validated as a necessary practical component in the construction of prices and the market is seen to be a way of distributing the use value of the various property rights that contribute to the product.

This does not totally overcome St. Thomas's prohibition on pricing by demand, but it does have the capacity to explain the special place of land in the social dimension of man's material welfare. It may be noted that market pricing of products does not take all of the utility value of the product from the consumer. Some of the utility value is absorbed by labour, but this has been shown to be the labourer's natural property, hence it is just. The remaining utility value becomes the return to land, its rent or the royalties for extraction of raw materials.

If the two types of property title found within products is understood, it leads closer to validating the economic return to land, its price. The landowner holds property rights of a different nature to the labourer. The labourer's title demands a price governed by social determination of just wages, which is objective within social parameters. The landowner appears to be taking a share in the utility of the product without any justification beyond the fact that they have a conventional right to it. It will be seen that to some extent the return to land and the return to labour compete with each other and

⁸⁵Any factor could appropriate this margin. For example, a psychiatrist may use few resources in his work but extract the utility value of sanity from his patients which could be expected to be unreasonably high.

⁸⁶Imagine a merchant selling gift wrapping ribbon where the typical measuring error for each metre length sold was one centimetre. If the merchant regularly sold 101 metre lengths off 100m rolls, one could conclude that even though each sale may have been within tolerable limits, the merchant is abusing his customers.

it would seem that a positive right (land title) could not violate a natural right (the consumer's ownership of their desire).

The key here would appear to be *common use* and also a review of those necessary activities that are found within a society that Aristotle chose to exclude from the economic realm. For Aristotle, the economy consisted of those activities involved in the production and distribution of the things needed for material welfare. These could be summarised as food, clothing and shelter. Civil order, education, religion, arts, care of those who are unable to care for themselves medicine and even Aristotle's own philosophy are all omitted, yet they provide some of the most important contributions to society. Generally they contribute substantially to the common good. Funding for these has no place in the economy. The owners of conventional property have the right to an income sufficient to maintain them at a suitable standard, but the application of the remainder of their income in order to provide for common use would appear to naturally suggest its application on these non-economic contributors to the common good.

Like the self-restrained merchant introduced at the conclusion of discussion on cost based pricing, the self-restrained property holder must take the responsibility upon himself to place the limits on his own income and chose to devote his excess income to applications that pursue the common good⁸⁷. The element of responsibility in willing marks the distinctions between capitalism, socialism and the ethical model being considered. The capitalist considers that the whole of his income from conventional property is for his own enjoyment, the socialist removes the right of the individual to make the choice and appropriates the authority to the state. This model suggests that ownership of conventional property involves concurrent responsibilities which would include:

- The immorality of setting prices at levels that absorb all of the utility value of products by the sellers.
- The obligation to use excess earnings originating from ownership of lands (raw materials and ground rent) for community and charitable purposes.
- The respect for the part title to products due to human effort as an absolute and value, placing it, strictly considered, outside of market determination.

The Medieval just price principle can be seen to follow from the first consideration. The Western practice of objective pricing, that is today evident in the existence of price tags in Western shops, is a remnant of the just price mentality and is conspicuous in its

⁸⁷The right to determine the allocations in this area is partly in justice and include other prudential judgements. For example, a wealthy person must decide how much income to re-invest in order to maintain his wealth.

absence from the commercial of culture of non-Christian societies. The immorality of monopoly trading also follows from this moral precept.

The construction of the feudal system is an example of the second moral obligation attaching to land ownership. The use of various forms of land tax that have historically been the dominant source of public revenue up until the present century are a modern expression of this same tendency. The difference in the nature of ownership between labour based and land based title may be included in the consideration of such issues as income taxation. It is a widely held belief in political economy that all taxation is ultimately paid out of land rent, though this belief should be carefully considered before being adopted in a particular application. Even in the most capitalistic societies there tends to remain an inclination for wealthy people to voluntarily devote some of their income to what they perceive as charitable and social purposes. St. Thomas in his treatment of private ownership implies this common or public use when he quotes from St. Paul's letter to Timothy (6:17-18) "*Warn those who are rich in the present world... Let them do good enrich their lives with charitable deeds, always ready to give and to share in the common burden...*"

The theme of a just wage follows from the third precept. The tendency to put wages at the mercy of the market in the eighteenth century is possibly the single major cause of the impoverishment working people in Britain that led to the penal colony of NSW. It is also the injustice that stimulated the rebellion of the working people in the nineteenth century that led to both the beginning of the social encyclicals and the over-reaction that is socialism. The current trend to treat wages as but another market commodity, apart from reproducing the dysfunctional economic thought of two centuries ago, may be usefully informed by a close consideration of these differences in title to property.

In most areas of life we accept limitations on our sovereignty over the things that we possess. If I own a box of matches, I accept that I still may not use them to burn down the town hall. Similarly, while respecting the right of private ownership, it seems reasonable to accept that that right has limitations. For the capitalist this implies the seed of an objective theory of moral obligation with respect to property, while to the socialist it denies the right of the state to appropriate what is licitly private. For the economic personalist it places the economic actor central in responsibility for his moral acts, but simultaneously insists on an objective moral base that is an inseparable part of economic theory.

9.5 CONCLUSION

The ultimate mortal end of humans is happiness which is realised through the perfection of human nature. Human nature includes material and social aspects and economics is seen to relate to both of these aspects of human nature. Satisfying human material needs provides the foundation for higher human pursuits, it is necessary but not necessarily comparable. Production is the result of labour acting on land using capital to produce commodities that fulfil human desires. These factors can be meaningfully isolated in their contribution to the final product through regression from their apparent manifestations. Interpreting their contribution through Aristotelian causality identifies the natures of the various titles to property.

Trade, or other exchange, facilitates specialisation leading to the most effective production. Despite this, trade raises one of the most important fundamental problems in economics, the resolution of price. Price can be based on cost, utility or the market. Cost has been shown to be limited in scope, being incapable of pricing land and financial assets. Utility has been shown to inevitably lead to either unnatural exchange or the violation of the common use provision in private property. The market also appears to lead to unnatural exchange and violation of the property rights of labour when it is used indiscriminately.

It has been shown that the property rights of labour are natural and absolute, but proportioned quantitatively to that share of the the society's product sufficient to live at an appropriate standard. Studies have been cited that demonstrate the practicality of such a determination.

Property rights to land and consequently the land components embedded in other apparent factors, especially capital, have been shown to be *sui generis* to natural property rights. They are valid conventional rights, though conditioned by the expectation of common use. Some cultural resolution of the common use expectation have been cited.

The exploration of price has shown the limited appropriateness of the market as a method of determining price. It has not explored the dynamics of the price of land which will be attempted using David Ricardo's rent theory.

9.6 CONTRIBUTION TO THE SUPPORT OF THE THESIS HYPOTHESES

	Hypothesis	Conclusion
1.5.9	Trade is initiated by the desire of the consumer, as final cause of production.	Supported
1.5.10	Pricing by the market is not suitable for natural property	Supported
1.5.11	Commodity use value lifts price above normal costs in current market practice.	Supported
1.5.12	Price is naturally derived from cost.	Supported
1.5.13	Conventional property is priced as the difference between demand and the return to natural property	Supported
1.5.14	Supernormal profit results from the fact that sale is made for utility based prices but production is based on costs	Supported

Chapter 10 Ricardo's Theory of Rent

The purpose of this chapter is to review Ricardo's rental theory, often referred to as Ricardo's law of rent. While it may be premature to refer to this relationship as a law, it has become its traditional title. It will be argued that the relationship follows deductively from the nature of land and the behaviour of commerce, however, its operation is partly obscured by imperfections in the behaviour of actual markets. The implications for land taxation will be briefly considered in this chapter, but the shortcomings of land rent as a sole source of public revenue will be considered separately in a later chapter.

10.1 HISTORY

Ricardo's theory of rent is central to understanding pricing of both land and products, although attention to it appears to have been distracted by taxation issues over most of the last century. To understand its importance, both its history and implications need to be considered.

Ricardo's theory of rent has been accepted as a truism in real estate theory. Like other theories of value and location, it is usually taught using general observations, while simultaneously recognising that other practical factors obscure its operation in the real world. Ricardo asserted that rents were derived differentially from varying productivities⁸⁸ between land parcels (Ricardo 1817/1973). His law assumed perfect competition, with its own set of assumptions, including perfect knowledge and mobility. Perfect knowledge and mobility in the context of land use infers an understanding of the highest and best use of each land parcel and the ability to achieve it.

Critics of Ricardo correctly note that the efficient operation of his rent law is unlikely due to market imperfections and the pluralistic use potential of land. Two adjacent sites can command different rents because of different patterns of use and one land use can affect the rental potential of adjacent sites. For example, in shopping centres, anchor tenants improve the rental potential of adjacent sites, whilst themselves often returning only a diminished direct rental cash flow to their landlords. Theme parks can have similar impacts on surrounding values.

The agricultural focus of Ricardo's observations may be responsible for this apparent disparity. Because he was preoccupied with rural lands where optimum land use was

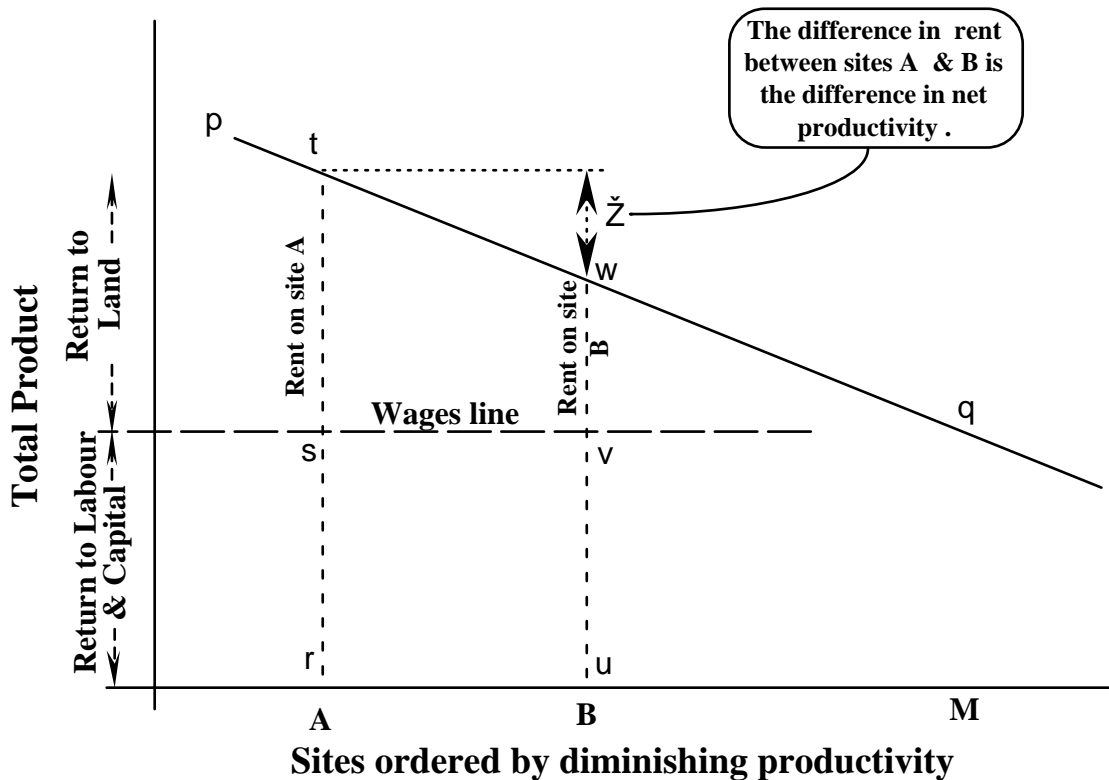
⁸⁸Productivity is total income from the utilisation of a land parcel and is the product of the volume of product and its price. Rent therefore derives its value from the gap between product price and the non-land factor costs to produce it.

fairly evident and stable, these objections were irrelevant. They were probably a partial stimulus for the development of the location theories of urban economics, and it is not uncommon to identify Ricardo's law of rent with locational factors. Alonso's theory of bid rent curves can be viewed as a development of Ricardian ideas as tied to location.

Theorists such as John Stuart Mill and Henry George were shy of the locational aspects implied by Ricardo and moved his rental theory into the urban context by consciously rejecting a simple locational dependence and replacing it by economic productivity. This approach is more flexible and recognises the contribution to rental value of human externalities, though its supporters tended towards a preoccupation with its potential for taxation. The notion of land taxation as a desirable form of public revenue goes back at least as far as Smith, who devoted some considerable attention to its benefits (Smith 1778/1910). Ricardo, and the French Physiocrats both saw the suitability of taxing land and Mill suggested that land values should be frozen and any incremental value should be taken through a rising rate of land tax (Mill 1848/1965). George added his own observations and developed an economics focused on land but otherwise consistent with Smith (George 1879/1992). He then took these sentiments to heart in what became an international political crusade for a single tax on land. This preoccupation with taxation implications has proven highly problematic and has distracted attention away from the essential issue of the validity of the relationship between land productivity, rental value and market value. Despite being the last major theorist to develop Ricardian rent theory, most references to him in general texts are almost entirely devoted to the land tax issue and its practical shortcomings⁸⁹.

Ricardo's law of rent begins with the simple observation that rent will absorb the marginal productivity of land, as shown in Exhibit 10.1

⁸⁹See for example Barlowe (1958), Harvey (1987) or Samuelson (1975)

Exhibit 10.1 Ricardo's Rent Theory

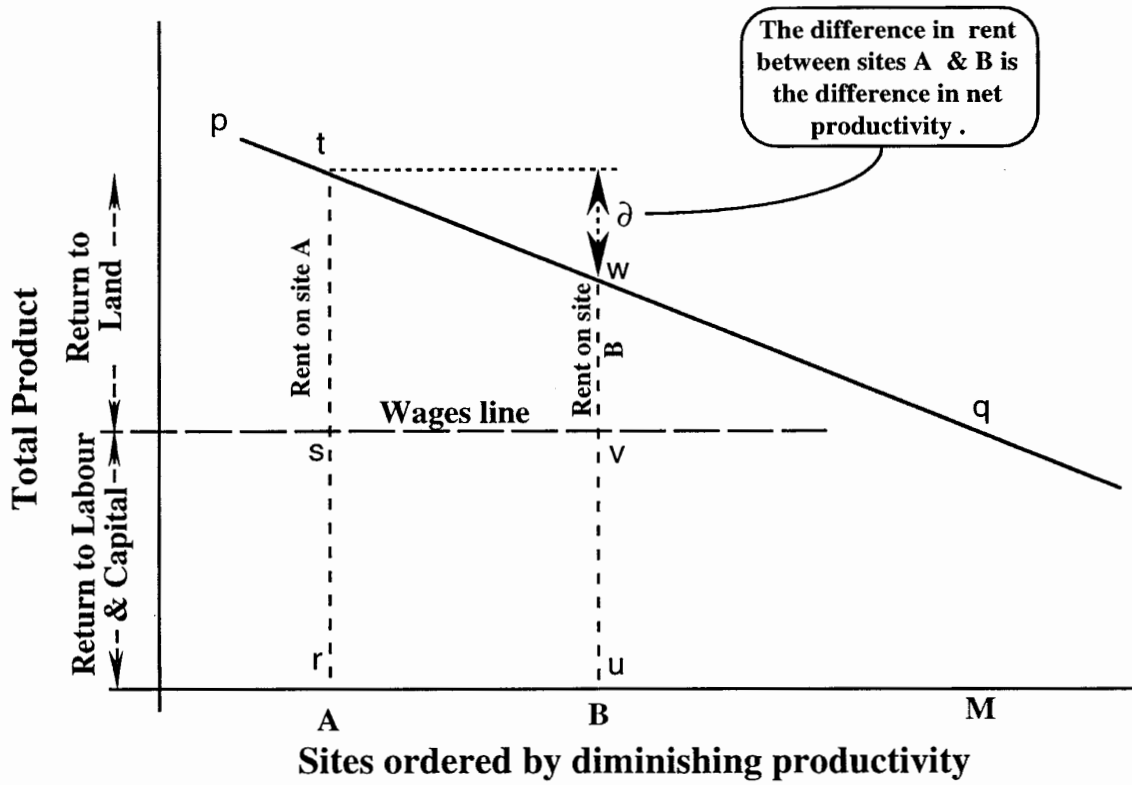
Ricardo's Law of Rent suggests that in the exhibit above, the difference in rent between sites A and B will equal the marginal productivity (difference in productivity) between the sites. Likewise, if one knows one of the rents and the difference in productivity between the sites, then the rent of the other site can be accurately computed. The comparison of sites to assess value is a central technique in property valuation (appraisal), known as *valuation by comparables*. In this method of valuation, a subject site is valued by assessing its relative merit against several other sites whose values are known. In practice, the sites used for comparison are chosen to be as similar as possible to the subject site and the valuer (appraiser) applies skilled judgement to assess the differentials. This overcomes the problem of imperfect knowledge by using comparisons where the differential value is slight and the residual error is controlled by the use of multiple observations.

While appraisal is more often made in order to assess sale price not rent⁹⁰, because of the connection between the two it is consistent to conclude that valuation by comparables is evidence of the underlying law of rent. The incremental connection of

⁹⁰Residential land valuation relies on comparables for valuing sale price. Commercial valuation uses comparables to assess rents and yields that are then used to deduce sale price.

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Exhibit 10.1 Ricardo's Rent Theory



individual comparable valuations across an entire market results in a wholly coordinated set of values⁹¹.

Although Ricardo was considering agricultural land in formulating his Law of Rent, George demonstrated that it easily translated into the urban context. Valuers base their appraisals on the highest and best use of the land that they assess, which is assumed to be known. While urban land has a more complex pattern of productivity, in the medium term it may be assumed to be stable and knowable.

If rents absorb the differential productivity of land, then the return to non-land factors (labour and capital) should be constant across all grades of land. Georgists have adopted the term "wages line" to identify the horizontal boundary between rent and non-rent returns from productive land uses across a market, as shown in Exhibit 10.1. A tenant pays either the rent S-T on site A, or V-W on site B. Because the sites have a differing productivity of δ and this is imbedded in the rental relationship as:

$$S-T = V-W + \delta,$$

Hence, the tenant would enjoy the same net income from either site. Conceptually, this is not surprising as the failure of rents to absorb the productivity differential would make one site more attractive to tenants and the resultant demand for that site would push its rent up until the advantage for tenants was absorbed.

Obviously, such a mechanism only works in an environment of good market knowledge and mobility, that is, in perfect or near-perfect markets. In practice, productivity knowledge is relatively poor and mobility limited. The advent of precisely managed retailing centres has gone some distance to reducing the knowledge limitation. Retail leases in these centres now commonly insist that tenants inform landlords of their turnover and rents are being linked to tenants' sales levels (Hendershott 1999). The mobility problem diffuses with a longer term perspective.

10.2 FUNDAMENTALS OF RICARDO'S THEORY OF RENT

The operation of Ricardo's law follows from three premises:

- (1) Land is necessary for production
- (2) Land has varying productivities
- (3) Demand is rational, informed, mobile and driven by financial evaluations of value.

In practice, proposition (1) is generally true. Exceptions, such as the fishing industry, where land is not used for production, are rare. However, even these prove the rule, in

⁹¹Individual valuations by comparables are rather like individual links in a suit of chain mail. While the individual elements contribute only a tiny amount to the whole, their combined effect is a smoothly coordinated whole.

that the oceans, and even the radio bandwidth for the electronic media, are all contained within the definition of land adopted in the economic factor sense which is used here. The ocean could be interpreted as a form of common. The internet, computer software and other services that use negligible resources or office/industrial space may be closer to genuine counter examples. It may be argued that because these are relatively rare, and because wages are linked to tenant income (in Ricardian rent theory at least), they do not escape the general operation of the theory⁹²

Proposition (2) appears to be evidently true in the world.

Proposition (3) is no more than the assumption of a perfect market. If actual markets are near perfect, then this proposition will be true. Hence, the operation of Ricardo's rental relationship will be an indication of how closely an economy is to the perfect market ideal.

If these propositions are adopted, then Ricardo's rent theory follows deductively. This does not mean that market rents will always conform precisely to the differential products between sites, but it does supply a rational principle that may be used by persons when determining actual rentals. Often violations of the third premise and political factors (e.g. a retail centre may be able to charge as rent the whole of the difference in productivity a tenant enjoys, but this is never done in practice, despite it being generally recognised that the productivity increment is due to the centre management).

In addition, Ricardo's rental theory provides a terminology that is useful in the analysis of social economy issues. Land rent, in terms of the theory, is not the market rent at a particular time, but an amount that may be deduced if productivity and other rents are known. It is in fact the equilibrium rent. In practice, often the Ricardian rent will be shared between the landowner and tenant, with the market rent being a discount to the true (Ricardian) rent. Likewise, wages are set universally by the theory. This is not to say that wages are all equalised, but rather normalised. Particular wages will be moderated by the usual factors, especially skill⁹³.

One further complication that will not be explored here is the way that apparent wages will often contain a component to cover the residential requirements of the labourer. The implications from this include the possibility that one land market will

⁹²Wages are tied to tenants' incomes because the latter signify all of those in the economy who toil for their income. In a near perfect market, a land-free service provider could not over-charge or there would be the risk of the entry of competition. Likewise, if service income were too low, a service provider could abandon that occupation and take up frontier land.

⁹³Skill has been considered a form of human capital, and as an investment that returns dividend in the form of higher wages the analogy appears to carry considerable weight.

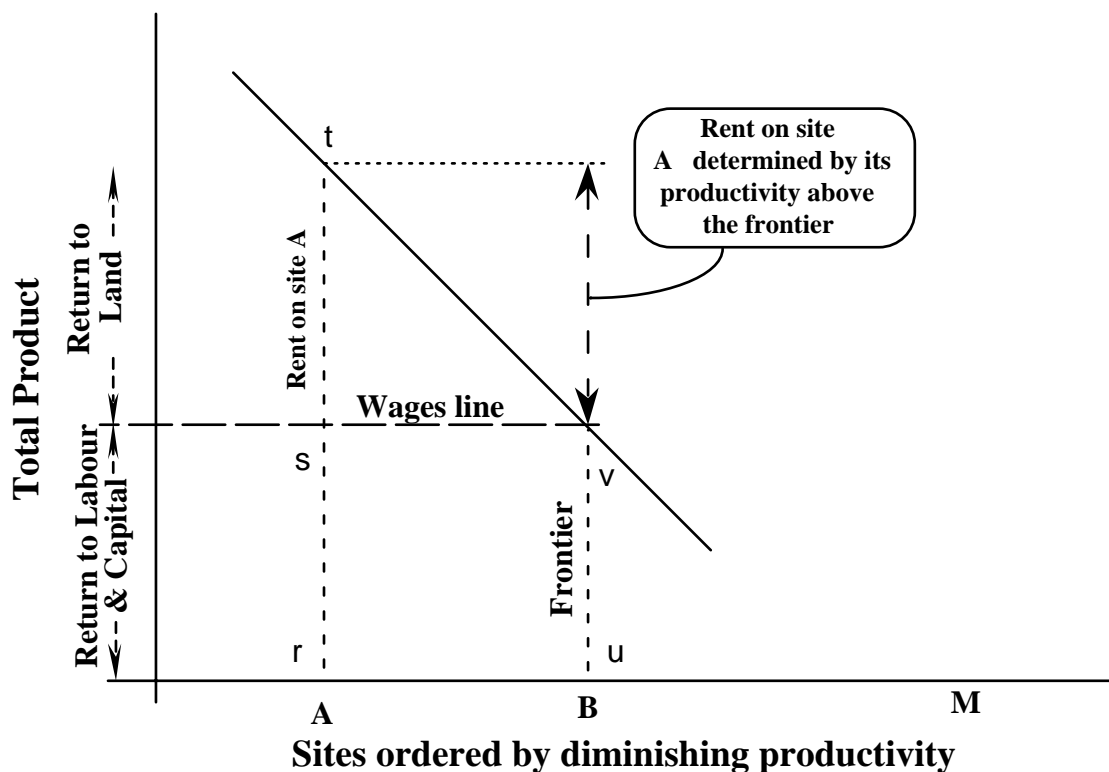
balance the other. For example, if commercial rents are too low and wages become high, then residential rents may expand to absorb at least part of the excess.

This simple theory therefore appears to offer some very powerful results. It appears to follow deductively from premises that are generally not contentious and offers a mechanism for understanding not only land rents, but also wages across the entire economy. Despite this, it is limited one very important shortcoming - the rentals are only relative, hence it is necessary to know at least one rental value before the market can be determined. This starting point will determine rents for one productivity, hence wages universally and therefore all other rents, assuming productivities are known. Ricardo, and those who expanded his law, suggested two ways that his starting point could occur, depending upon the presence of a frontier.

10.3 RENTS IN THE PRESENCE OF A FRONTIER

If a frontier exists, not all land is allocated and some land is freely available for the taking. It may be assumed that the most productive land will be utilised first, hence the unoccupied frontier land will be at a grade lower than that in use. Hence the frontier provides an alternative for existing tenants across the entire economy. If existing rents are too high, tenants will take up free frontier land, thus the frontier provides a floor for the return to non-land factors across the entire market as shown in Exhibit 10.2.

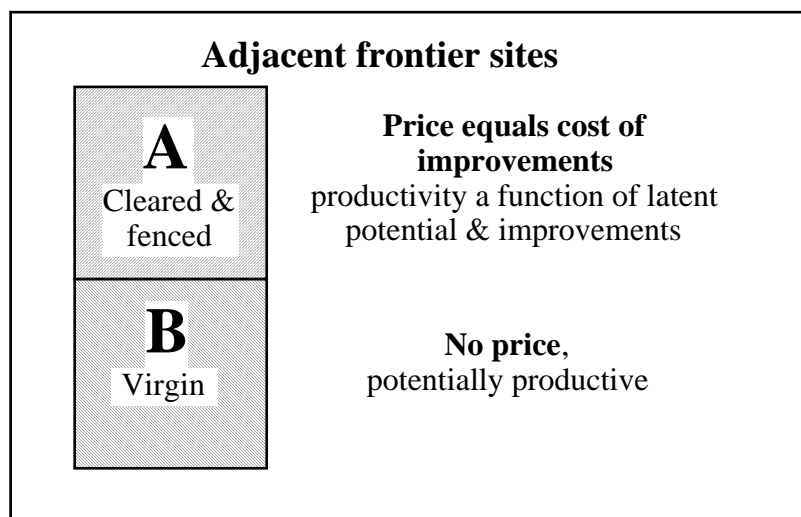
Exhibit 10.2 Rents with a Frontier



Because frontier land is essentially free, tenants have the option of either renting available productive land, say site A, or appropriating a site at the frontier B at no cost. In practice, this may appear to involve costs such as clearing and fencing, however these are actually capital improvements, and raise the value of the land. A person clearing and fencing frontier land may see these activities as necessary in order to render the property productive, but has actually transformed the site from the untouched raw material designated in political economy as *land* into a capital product. Clearly, another settler coming to the frontier area would have the choice to either apply these improvements to an adjacent (free) site or purchase the cleared site. The choice is shown in Exhibit 10.3. The price could be no more than the labour value of the improvements, even though the cleared site may be highly productive, while the adjacent uncleared site may have nil immediate usefulness.

The price of land at the frontier, where similar land is free but uncleared, will be based on the value of capital improvements, not productivity. Likewise, it should be evident that the ultimate productivity is more a function of the land than improvements, as the latter will have similar costs on sites of vastly varying ultimate productivity⁹⁴.

Exhibit 10.3 Valuation of Frontier Land



A practical side effect of a frontier is that it renders unemployment unnecessary. Any fit person desiring an income may take up free frontier land. The only barrier to

⁹⁴The improvements relate to appropriate investments on similar lands, which both would require in order to become productive. There also exists potential for vastly inferior land grades to become equally productive through intensive improvement, such as irrigation, but this is a different case.

employment is mobility and even this is unlikely to be a problem for at least two reasons. Firstly, perfect market theory assumes mobility and implies that a mobility problem would be the result of some political factor, and not an economic one. Secondly, there is the likelihood of some persons leaving situations in settled areas for the independence of life at the frontier. This suggests that jobs would be available in settled areas for those who were either unwilling or unable to take up the opportunity of free frontier land, these could be expected to occur randomly through the settled areas.

Not only does the frontier set the floor for working incomes across the entire labour market, but it sets it at a level that may be considerably above the living needs of the workers, because land productivity, not the cost of living, sets working incomes. This has been suggested by George and others as an explanation for the high relative standard of living experienced by working people in nations such as the USA at the time when frontiers existed and even as a cause of economic strength for some considerable time following⁹⁵. Implicitly it was recognised in Wakefield's plan for settlement of the Australian colonies⁹⁶.

10.3.1 Spatial rental gradients with improved infrastructure

For agricultural land uses it is well accepted that productivity is partially a function of distance from urban centres. This is the result of the extra costs involved in both bring product to market and providing the necessary supports for remote properties necessary for occupation. The latter includes the transport and communication costs associated with providing fuel, equipment, service and support services such as education and medical care. Although the spatial distribution of land productivity is not strictly speaking Ricardo's law of rent, it is derived from it and has the capacity to inform some aspects of its operation. In particular, it may be used to demonstrate the effects of human developments that change the level or distribution of productivity across a land domain.

In actual frontier situations, such as the USA or Australia in the nineteenth century, the spatial gradient across productivities for the set of sites between the most productive (typically near cities) and the frontier sites was quite steep. This was the

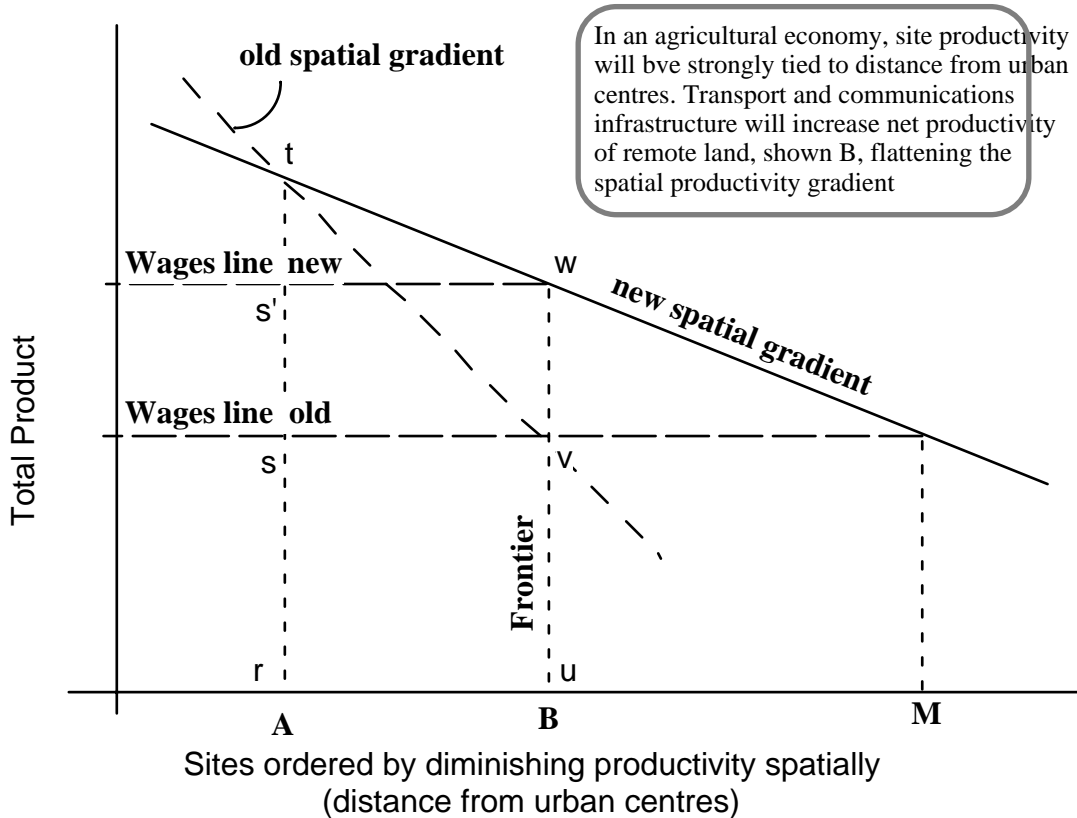
⁹⁵This suggestion works for nineteenth century USA and the Australian squatters, however, many parts of the Middle East have an apparent frontier for which the assertion is not true. The difference is that in the former cases, the productivity of the frontier land was high, whereas in the latter frontier land is near desert.

⁹⁶Wakefield recognised that access to land in colonies such as Australia should be controlled by the state charging a substantial price for land grants (Wakefield 1829/1929). Wakefield's plan was to use the funds acquired to develop the colonies, especially to finance new immigration. Because the sale price of land is financially equivalent to the future rental stream, a high price for frontier land has the effect of depressing wages by raising the rental profile across the entire market.

result primarily of poor transport and communications. Location theory can be applied to examine the effect on the productivity gradient as a result of improved transport, such as the introduction of rail transport (Harvey 1987). The point here is that the spatial gradient in productivity and value is influenced by human infrastructure external to the sites themselves.

For a given set of sites, where the productivity gradient is set by the negating effect of transport costs on productivity, an improvement in transport will reduce the gradient as shown in Exhibit 10.4.

Exhibit 10.4 Spatial Gradients Resulting from Transport Infrastructure



In the case of the USA, and to a lesser extent Australia, improved transport, especially the railways in the nineteenth century, had the effect of improving the productivity of remote land, thereby raising the wages level. It may even reduce the rental value of the most central sites. This was the case following the widespread introduction of the automobile and improved public transport following the Second World War in many cities. In Sydney, transport developments facilitated the residential development of fringe suburban areas and significantly depressed the values of many inner residential suburbs. This effect was at its worst at about 1970 and also affected other land uses. While urban redevelopment has since reversed the trend, its success is the result of a different set of forces and does not negate the initial negative impact of transport on the inner areas.

Recent discussion on the effect of the widespread use of internet based commerce on retailing rents can be interpreted as the result of the severing of the previously necessary spatial connection between retailers and their customers. The internet enables retail customers to travel virtually to any retailer on the internet. In this case,

the improved rental at the sites that the retailers actually occupy may be negligible, however, the flattening of the virtual spatial gradient facilitated by the internet is predicted to topple the high rents currently enjoyed by premium retail sites (Baen 1999; Borsuk 1999; Miller 1999). The concerns are that retail rents will fall as a result of elimination of geographic factors in retailing.

A little reflection exposes the provincialism of concerns over losses arising from transport improvements. Transport is an inefficiency and a cost in human exchange and any reduction in this cost should result in a net gain for society. More important issue is how to provide the goods and services society needs most efficient, followed by the development of institutions that neither concentrate inappropriately or cause some persons to be unjustly disadvantaged.

Generally, transport infrastructure it improves the situation of those at both ends of the transport link. Not only does it improve the spatial gradient, benefiting the remote lands, but also the urban real estate at transport nodes. In the examples cited above, although the automobile may have caused inner city residential values to fall, the efficiency of central employers and retailers increased through better connections to large markets. The internet promises similar benefits to the parties at both ends of the electronically connected trade link, partly because the retail centre landlord has been omitted.

This effect was quite evident in Sydney and Melbourne in the nineteenth century as a result of the squatters. Squatters were essentially illegal land occupiers who took up inland tracts in a manner that could not be practically contained by the government. Even though they were officially frowned on by the urban community, because squatters generated considerable commerce in the cities, they developed unlikely political allies there. This was illustrated in the way that initiatives to control them met with substantial urban opposition (Brennan 1971). Given the volume of trade that they produced, it is easy to link part of the urban land values to the success of these remote settlers.

Hoyt (1970) concluded that the single most important factor in pushing Chicago land values ahead dramatically in the mid nineteenth century was its strategic decision to become a railroad centre. While economic theory might suggest that this could have been the result of economic activity associated with the construction of the railroads, the fact that construction in the last decade of that century did not have a similar effect points away from this conclusion. The benefit to land values come from the productivity gain, not the construction stimulus. The benefit may be negated by the cost of using the infrastructure. If fees are applied, such as road tolls or high ticket prices, the effect on land values will be diminished, leading to some studies not

observing an impact on values (Karantonis 1998). Once tolls are removed, the benefits will gravitate first into a net utility, and then into property prices "*..by the complex function of the property market*" (Bajic 1983), p.156]. This is consistent with (Harris 1973) who recognised that tenants faced higher rents as a result of government transport investment.

The fact that public expenditure finds itself in the pockets of landowners has been recognised since at least the middle of last century to be a sound reason to pursue funding methods that target this group. Infrastructure funding through charges levied on land values have also been shown to return greater overall efficiency as well as other benefits in developing areas (Small, 1997).

If site rent is a function, not only of distance, but also of transport, communications, other infrastructure, habitation patterns and land use, simple locational theories of rental distribution will be insufficient to provide an understanding the social economy of land. The Georgist model that adopts the basic theory of Ricardo, but strips it of its single (agricultural) land use restraint and locational dependence, appears sound.

Several points can be concluded from the effect of infrastructure on frontier lands as follows:

- Transport and communications infrastructure will increase the productivity of distant land, and by flattening the spatial gradient and may depress rents of prime sites
- Infrastructure and other amenities may increase rentals in urban lands.
- Land productivity incorporates monetary and non-monetary components that become evident as higher rents and hence sale prices.
- Emerging technologies have the capacity to rearrange the patterns of site productivity.
- Simple distance based theories of rental distribution are important in establishing initial relationships, however they are limited in their practical ability to explain the complex distribution and behaviour of rental values.

Similar effects are evident as a result of urban transport infrastructure and also other urban facilities (Asabere and Huffman 1997; Benjamin and Sirmans 1997; Bible and Hsieh 1997; Burrimer, Rutherford, and Witton 1997; Carroll, Claurette, and Jensen 1996; Cornell and Inoue 1995; Kim and Nelson 1997; Rosiers and Thériault 1997; Tse, Lee, and Ganesan 1997). The fact that proximity to other facilities, such as places of worship, improve land values implies that they are positively valued by the community as contributing to one's quality of life. George suggested that urban rents were a dynamic result of urban society itself as well as its hinterland. Hence, the security

premium that may have attached to established areas was partly the result of the development that had been completed but also the result of the social surroundings themselves. Generally, land is more valuable in those areas where people are. George's major contribution was the observation that it was *people* who gave land its value⁹⁷.

Commercial activities reflect this. Shops locate where customers are likely to be found and all commerce is best located at the intersections of human activity. This is standard urban economics, but urban economics tends to be used to explain settlement patterns and the efficiency of urban forms. While this is generally valid, its reflection in land values appears to receive relatively less attention. In the case of land at the margin, or frontier, its productivity also enhances the value of the distant cities through which its product travels to market and from which suppliers of equipment work to provision the remote land users.

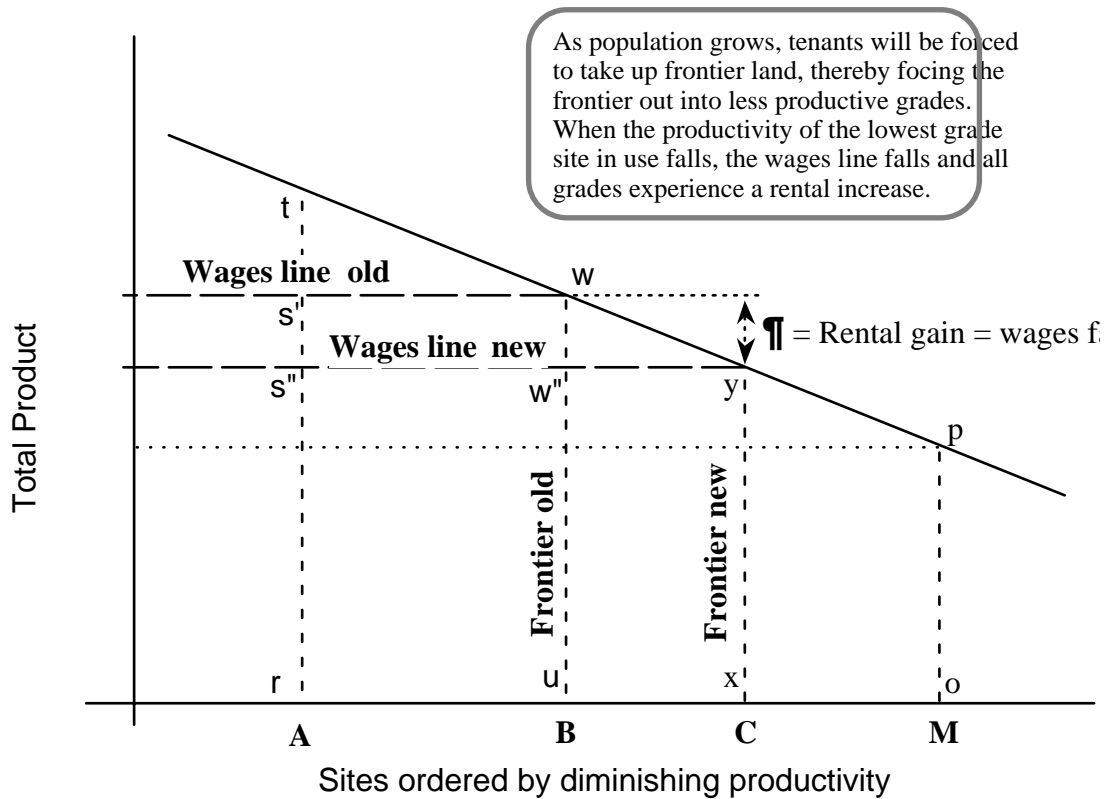
10.3.2 Effects of population increase

Contrary to George's optimism regarding the effects of people on land values, Ricardo adopted a generally Malthusian theory of the effect of population on land and economics. This can be seen in the application of his Law of Rent to a population increase. If a frontier exists and land is taken up in order of diminishing productivity, in the wider understanding of productivity adopted above, then population increase can have only one effect as shown in exhibit 10.5.

If at a point in time land is taken up down to grade B in the set of grades shown above, individuals can take up land of grade B at no cost, thereby earning wages of $u-w$. Land of grade A, being more productive will yield a rent of $s'-t$ which leaves tenants with an income of $r-s'$ which is equal to income at the frontier.

⁹⁷George saw population as a major cause of land value, observing that rent were highest where populations were densest. In this way society is both a material cause of land value and, almost reciprocally, is its final cause also (Dempsey (Dempsey 1935) referred to the way that lower creatures took their value from man in his general discussion of just wage). George saw this dual relationship between society and land as the solution to Malthus's population pessimism, a position that he argued convincingly, but that has been largely lost today, except in the work of economists such as (The Economist who saw human ingenuity as the source of Ec. growth - Becker??, Economics against the grain??)

Exhibit 10.5 Population and Rent with a Frontier

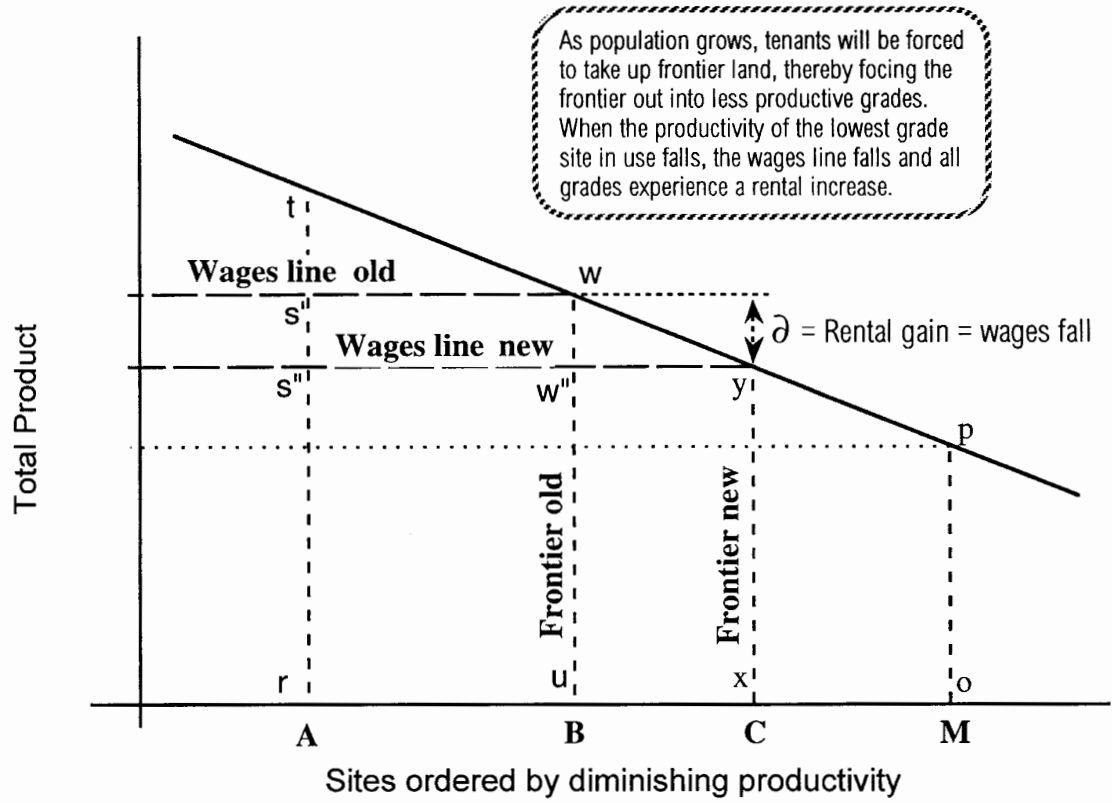


If the working population increases, occupiers of land will be forced onto less productive land, such as grade C in Exhibit 10.5. Because this land is less productive, it will return a lower income to its occupier of $x-y$. This new frontier will cause the old frontier at grade B to acquire a rental value of $w-w''$ which may be capitalised into a sale value. Owners of grade B land will continue to earn a total income of $u-w$, but this will now be composed of a wages component and a rental. On selling the property such an owner will receive a price that is the sum of the depreciated value of improvements plus the capitalised rental. Alternatively, the owner may be in a position to lease out the property and to live off the rental income. The rental value of Grade A will similarly increase from $s'-t$ to $s''-t$. Wages for tenants on Grade A land will still equal to those at the frontier, however that level will have fallen.

Ricardo recognised that given stable productivity, population increases would naturally lead to falling wages and rising rents. There appears to be reasonable grounds for his pessimism regarding the lot of the worker, though it must be recognised that the effect represents a redistribution of total income from the productive members of the community in favour of those controlling property. The erosion of wages resulting

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Exhibit 10.5 Population and Rent with a Frontier



As population grows, tenants will be forced to take up frontier land, thereby forcing the frontier out into less productive grades. When the productivity of the lowest grade site in use falls, the wages line falls and all grades experience a rental increase.

from the drying up of available land is evident in the association of unemployment and falling wages with the English enclosures⁹⁸.

10.3.3 Marginal Land

Under these assumptions, wages would continue to fall under population pressure, however there would come a point when wages would fall to a level below which the occupier could no longer earn sufficient income to subsist. It is shown in Exhibit 10.5 as grade M, producing o-p, which would necessarily all be taken as wages by the occupier in order to subsist. Ricardo referred to this grade of land as marginal and believed that it would attract no rent and consequently would be incapable of realising a sale price. Furthermore, because land below this level of productivity is not capable of supporting even the occupier that works it, sub-marginal land would not be occupied at all.

There are several examples of essentially marginal land in non-modern societies. There are several societies that exist today where land is freely available to its members that is capable of producing a subsistence income and where the notion of paying rent, or capitalising land value into a sale price, is unknown⁹⁹. Also historically, the English commons were freely available and provided the opportunity for earning an income below which no fit person needed to stoop. The commons therefore provided a floor to wages.

In most modern societies, there is no frontier and the complexity of land uses means that highest and best use is not as simple or apparent as in simple agricultural situations. Alonso's bid rent curves went some distance towards explaining the way that the margin for a particular land use tends to be overtaken by other land uses that offer a higher productivity at a given spatial position within the urban fabric.

In practice, in any situation where one person holds title to a site that they do not need to work personally and another needs to occupy it, the owner will almost always be able to extract some amount of rent, and the tenant will try to survive on the remainder. The reality of the failure of some tenants is possibly in part the result of sub-marginal net (after rent) site income resulting from a rental market where at least the tenant was not adequately informed - market failure. If this is the case for super-

⁹⁸ The English Poor Laws were introduced at the end of the first major period of enclosures initiated by Henry VIII and continued by his daughter. While some enclosure had been executed before that time, The Funk and Wagnal's Encyclopaedia is representative of the accepted view that it was the extensive phases of enclosure from the sixteenth century forwards that have been most clearly linked with falling worker incomes. Incomes have definitely fallen during that period (Rogers 1884/1949), however there have been other influences, such as the dissolution of both the just price principle and the moral prohibition against usury. These three changes in economic practice all contributed pressures on the ordinary person by various wealth holders and mark the transition from Medieval to modern commerce.

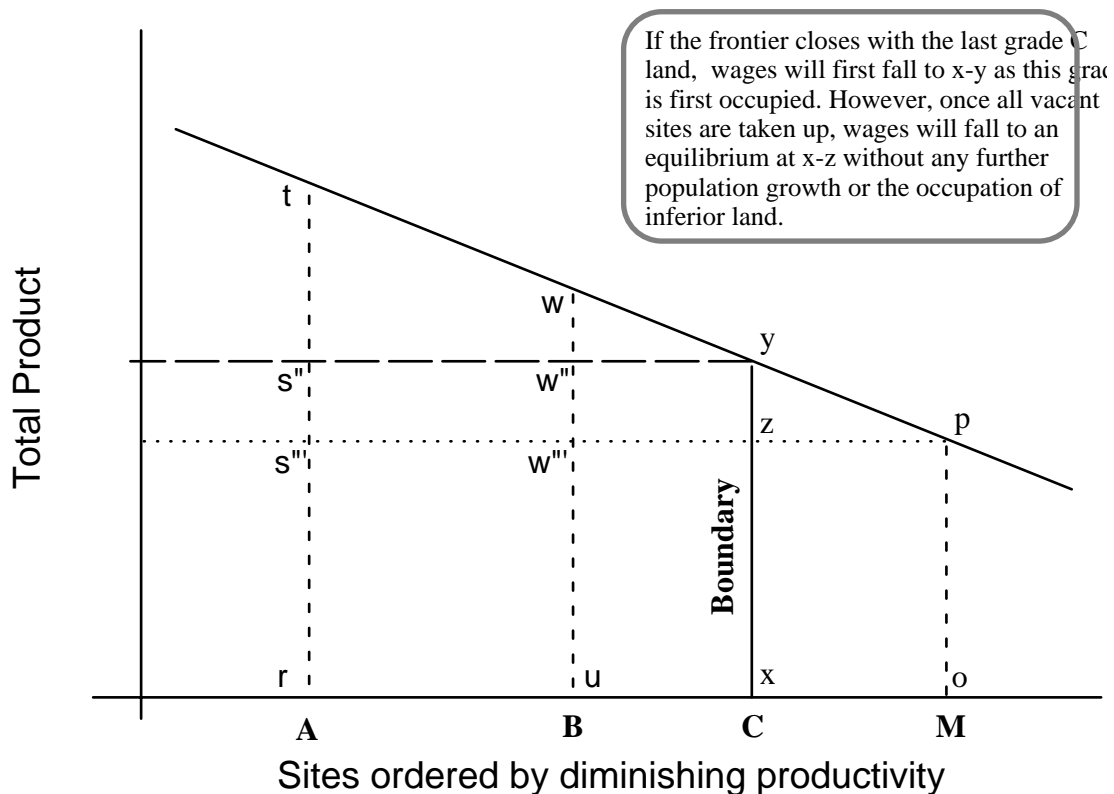
⁹⁹This is not uncommon outside of societies that are Western or Westernised, such as area of the Middle East, Africa, and many regions where customary title is recognised.

marginal sites, then it could easily operate to hide the true margin as well. The absence of marginal land is also closely tied to the absence of a frontier which will be discussed separately.

10.4 RENTS IN THE ABSENCE OF A FRONTIER

If no frontier exists, Ricardo's theory suggests that wages necessarily equal the occupier's subsistence needs, as shown in Exhibit 10.6.

Exhibit 10.6 Rents as the Frontier Closes

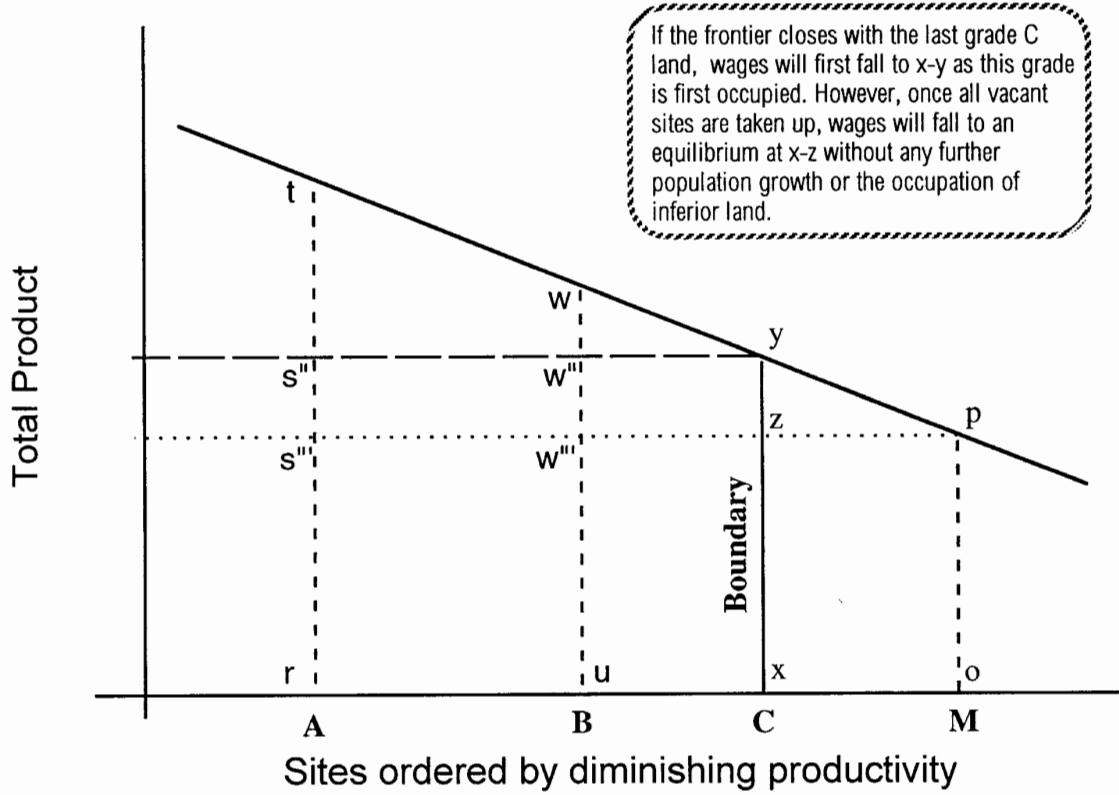


The case considered in Exhibit 10.5 explained how a population pressure that pushes new settlers onto the less productive grade C land, also causes wages across the economy to fall to x-y. However, if the settlers find that grade C is the last land available, that is the frontier closes with the last grade C land, a considerably greater fall in wages may result without the need for any further population change.

If subsistence is the cost of labour, as Marx and others have observed, then a free and perfect market would operate to whittle its price (i.e. wages) down to that level, which is x-z (also o-p) in Exhibit 10.6. While the frontier is open, wages will be able to

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Exhibit 10.6 Rents as the Frontier Closes



maintain the margin $z-y$ above subsistence by virtue of labour's access to rent free land. As soon as the frontier is closed, labour will no longer have any means of maintaining the super-subsistence margin $z-y$ and wages may be expected to begin to fall towards the subsistence level of $x-z$, independent of population pressure. Hence, the occupation of grade **C** due to population growth would not lower wages to $x-y$, but to $x-z$, once the frontier closes.

Despite the boundary at grade **C**, a virtual margin may be considered at grade **M**, even though such land may not physically exist. The notion of a virtual margin is useful in considering the implications of land and other rents, though it is of no material significance.

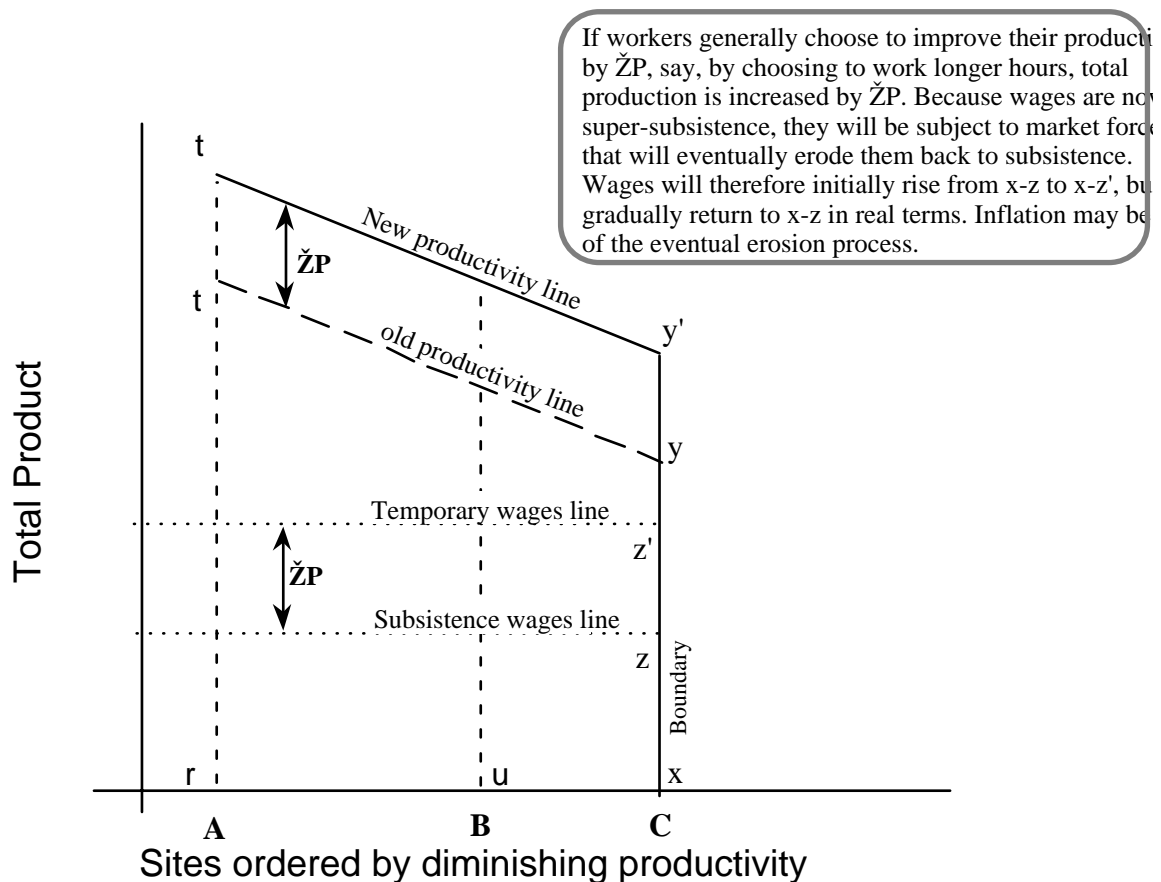
The essential resilience of subsistence wage levels is illustrated by the behaviour of wages as the result of labour-sourced productivity increases.

10.5 PRODUCTIVITY INCREASES WITHIN A CLOSED FRONTIER

Productivity increases within an open frontier have been dealt with, especially with respect to transport infrastructure. The effects of productivity increases within a closed frontier have significant differences, especially with respect to the condition of labour.

There are several sources for productivity increases, technology may advance, labour may contribute more effort, or new resources may be found. If the extra product comes directly from new raw materials the result will directly benefit landowners through increased resource royalties. If the extra productivity comes through increased labour input, then wages may expect to appropriate the benefit. In Australia there has been a recent trend in industrial relations negotiations towards wage increases on the basis of productivity increases.

Exhibit 10.7 The Distribution of Productivity Increases



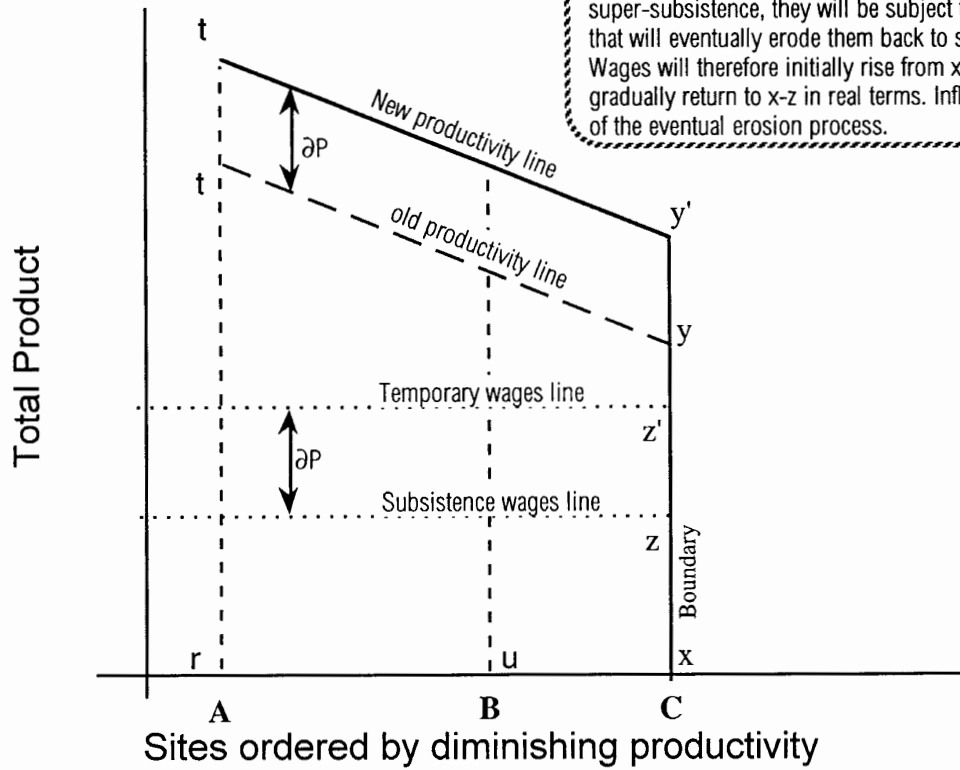
The long term effects are less apparent and may be complicated by the effects of inflation. Human history has been marked by enormous increases in productivity, the greatest of which has occurred over the past century. While this period has also been marked by a considerable increase in living standards, especially in those societies utilising the best technology, many would argue that the increases in living standards have not been commensurate with increases. The increase in living standards since about 1975 in Australia is generally believed to have been relatively stagnant, especially in comparison to productivity increases. It would appear to be similar in other developed countries (Bishop, 1999; Prash, 1999; Davis, 1999). Generally it is difficult to dissect productivity effects on wages and land. However, one significant source of national productivity increase can be examined against its long term effects on wages. This was the transition from single to double family incomes that developed its momentum no more than a few years before 1970. This case will be considered in detail in order to understand the effect of productivity increases on wages and rents.

Assuming a uniform increase in labour input to the economy, say by the willingness of the labour unit to commit more hours to paid work, then the income to labour will rise. Using the family as the labour unit, this was evident in the decade or so following

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Exhibit 10.7 The Distribution of Productivity Increases

If workers generally choose to improve their productivity by ∂P , say, by choosing to work longer hours, total production is increased by ∂P . Because wages are now super-subsistence, they will be subject to market forces that will eventually erode them back to subsistence. Wages will therefore initially rise from $x-z$ to $x-z'$, but then gradually return to $x-z$ in real terms. Inflation may be part of the eventual erosion process.



the introduction of effective contraception methods and their widespread acceptance in countries such as Australia (Small 1995; Small 1997a; Small 1997b).

During the decade or so beginning at about 1968, families began to control of their fertility by postponing or avoiding childbearing on a large scale, which led to several immediate economic benefits. Of these, the most significant was the possibility of families sustaining double incomes for considerably longer than had previously been possible. Effectively, this meant that the labour unit (the family) voluntarily adopted the practice of contributing more hours to external paid work. The effect was an immediate increase in disposable income and an elevated capacity to sustain debt.

For those families that chose this option, the period was characterised by a better standard of living. However, the fact that there was at that time more consumer dollars competing for the pool of available goods and services, meant that the situation was ripe for inflation. In addition, higher family disposable income meant expanded debt servicing capacity which stimulated borrowing, with the dual effects of increasing money supply, through the bank credit multiplier, and also producing an upward pressure on interest rates. While there were other financial changes that occurred at the time, the fundamental capacity of the community to sustain higher interest rates coupled with increased demand for debt funds must have been linked to a basic increase in family income.

The extra productivity of the additional contribution to the labour force is uncontentious. It was of course mixed with other productivity increases, notably due to the introduction of new technology. The owners of new technology would also have shared in increased incomes. However, the important point is that the inflation that was stimulated by strong consumer demand and partially realised through the predominantly debt sourced expansion of monetary supply, has tended to normalise the real gross income of the labour unit (the family) to the extent that dual incomes are now a necessity for many.

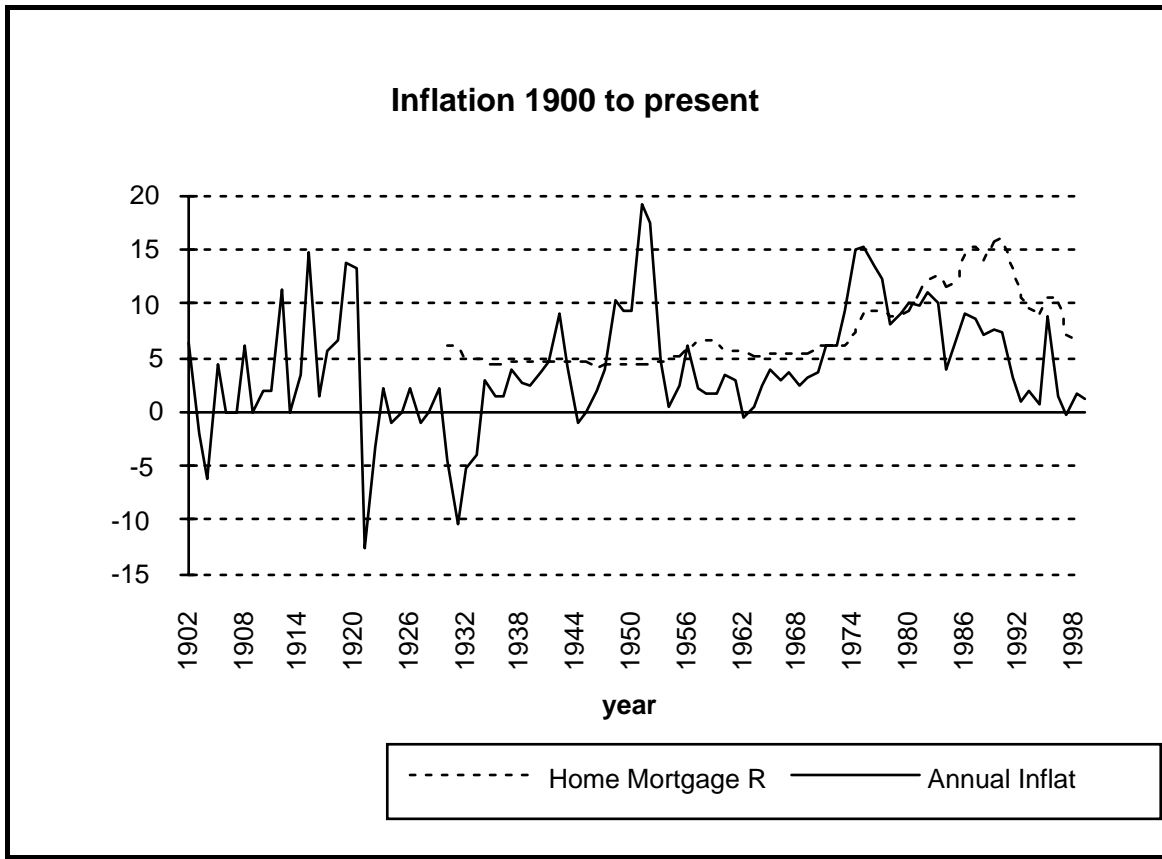
This historical process was not instantaneous, nor uniform or universal. It progressed gradually and included many changes in the relative balances. The transition to widespread dual income families was gradual; as inflation was locked in place, many families considered themselves forced into dual income situations. However, the more families that took on the practice of limiting their family size in order to subsist at what they considered to be a reasonable level, the more that the higher prices were reinforced. Real estate prices during that time also appreciated, absorbing consumer funds and inviting heavy borrowing. Auction prices are set by the party with the most funds, not necessarily the greatest desire. So long as there are two motivated bidders with access to similar funds, price will be pushed to the capacity of those funds in any

particular market. Commercial and industrial real estate also experienced capital gain due to participation in the super-normal profits flowing from increased consumer demand.

The combination of high interest rates and high inflation does not fit into economic theory well. High interest rates are supposed to discourage borrowing, hence constrain money supply leading to low inflation. High inflation is supposed to motivate lenders to expect higher interest rates following the inflation premium theory of interest rates (Wilson and Keers 1990). Historically, inflation has not exceeded five percent for more than a few years at a time any time during this century, up until 1970, as shown in fig 10.8, below¹⁰⁰. (Eichholtz, Theebe, and Mei 1999) studied inflation over several centuries in the Netherlands and concluded that the decades of high inflation beginning at about 1970 are truly peculiar. In addition, the same period supported continued high interest rates at levels that are unique in the century.

¹⁰⁰Previous periods of sustained high inflation both followed the World Wars, suggesting that they were also linked to social changes that were beyond purely economic factors.

Exhibit 10.8 Australian Twentieth Century Inflation



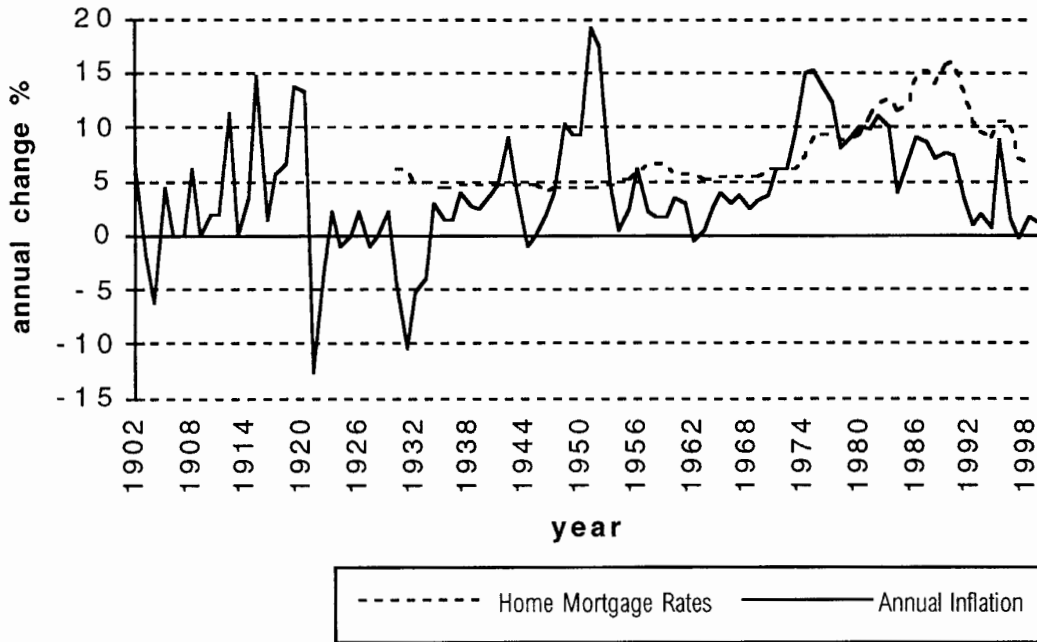
Source: Commonwealth Bank of Australia and the Australian Bureau of Statistics

The economic peculiarity of the period 1970-90 suggests either political or social factors and the dramatic fall in Western fertility does supply such a factor. The impact of this event on land and labour provides support for the thesis that productivity increases eventually flow to land. The fact that most families now accept that double incomes are no longer a luxury but a necessity indicates that the benefits from the longer working hours of families no longer flows to wages. Ricardian theory suggests that it must have gone to land rents¹⁰¹. While it may be argued that living standards are now higher than they were three decades ago, the improvement is not proportional to the extra labour, nor does it match the enormous increase in productivity that has resulted from the revolution in manufacturing technology that has greatly reduced the labour cost within most manufactured goods.

¹⁰¹While direct absorption by land costs accounts for only part of this effect, it will be argued that other long term beneficiaries, such as capital gain in equities, experience growth due to their participation in what is essentially land rent rent at a macro level.

Exhibit 10.8 Australian Twentieth Century Inflation

Inflation 1900 to present



Source: Commonwealth Bank of Australia and the Australian Bureau of Statistics

The evidence from the West following the introduction of fertility restraint is not novel, it follows deductively from the elements under consideration and it was recognised by Smith himself when he concluded his treatment of land rents noting:

"I shall conclude this very long chapter with observing that every improvement in the circumstances of the society tends either directly or indirectly to raise the real rent of land, to increase the real wealth of the landlord, his power of purchasing the labour, or the produce of the labour of other people." (Smith 1778/1910), p. 228]

If labour has some title to its product, and it would be hard to argue that it does not have title at least to the additional increment that it voluntarily contributes above some accepted norm, it would appear that the behaviour of land rent violates it. (Prasch 1999) explored John Locke's understanding of economic freedom and concluded that along with contemporary libertarian economists *"..freedom primarily refers to an individual's property ..one's freedom is largely constituted by owning one's property."* While these same exponents of freedom usually conclude that the market is the pinnacle of freedom, the market for labour is the exact opposite if it operates according to Ricardo's rent theory. Following from this *"..the state's responsibility to the individual consists generally of protecting the individual from any person who might deprive him of his rightful property"* (Prasch 1999), p. 477]

Prasch also discussed the way that this ethical argument found expression in the U.S. constitution, although he recognised that the issue is still hotly debated and ethical defenses of minimum wages are relatively rare. It would seem that his overall observations make study of Ricardian rent theory all the more relevant to the current discourse.

10.6 PRACTICAL CRITICISMS OF RICARDO'S RENT THEORY

The absence of marginal land

Critics of Ricardo, and subsequent Law of Rent theorists, often focus on the absence of genuine examples of marginal land in current actual markets. However, there is land that is unproductive in most countries, such as desert land, and many cultures include substantial proportions of their population who live in frontier-like situations at the margins. However, Western practice does not seem to include opportunities to occupy land at no cost that is capable of supporting a basic income.

In practice, this is often because low productivity land is parcelled in vary large areas that become viable through the use of specialised farming management, and

therefore take on some value¹⁰². Also, town planning restrictions often restrict access and occupation, creating artificial boundaries which maintain rents and values.

The fact that marginal land is only evident when frontiers exist makes the absence of marginal land plausible in Western countries. Also the Western preference for property is such that even if land were freely available it would be quickly taken up and enclosed, for no other reason than Western acquisitiveness. Once enclosed, it would appropriate a value as discussed in the event of a closing frontier.

The existence of a rental structure across a land market means that a virtual margin can be considered that would represent the productivity grade of marginal land if it were available. It could be used to estimate real sites in countries such as Australia or the USA that would be marginal, if the state was to allow its private acquisition.

The absence of free marginal land has been shown to be historically recent, not only in young countries such as Australia and the USA, but, relatively speaking, in England and Europe also. If the English Enclosures are correlated with unemployment and falling wages, then it would appear that labour needs some alternative to the private rental market in order to be able to fix a reasonable minimum wage. In the West this may take the form of minimum wages rates, but is also implicit in unemployment relief.

Historically, these have not been a very reliable floor and their failure has been responsible for the necessity for the organisation of labour over the last two centuries. This has used political action to redeem the worker from the plight of market wages and ineffective public welfare support. Whatever institution is adopted, commons, social security, legislation, or other social control, it will have the effect of providing a floor to wages. The objective minimum, wage rates of the magnitude common in Dickens's England, point to the necessity for some positive institution. Conversely, this amounts to no more than the containment the positive institution of private property in such a way that it respects the natural property of all persons. This is consistent with the Thomistic/Aristotelian principle of common use.

Absence of visibly normalised returns to non-land factors

A second criticism is the difficulty of finding actual examples of a visibly levelled return to the non-land factors. This is a more significant apparent shortcoming, and one that the present study seeks to examine.

At least five significant complications are evident in actual markets that appear to obscure the apparent operation of Ricardian rent theory.

¹⁰²Alonso's theory of bid rent curves uses a locational axis to integrate various rental curves by differing land use

The first is the practical absence of perfectly competitive equilibria. Under the assumptions of Ricardian rent theory, no other economic rents exist in the economy. This assumption is central because of the subsistence requirement in the setting of the wages line. Economic rent is super-subsistence. Chapter 13 will include an analysis of this issue.

The second difficulty relates to practical problems in precisely assessing the highest and best use for a land parcel. While the valuation profession is skilled in this assessment for the purpose of sale, this is not sufficient for the efficient operation of the Ricardian rent theory. The reason for this is the complex and individual nature of the highest and best use of any specific parcel. The precise utility of a land parcel is a dynamic function of instantaneous surrounding land use, infrastructure and social factors as they impact on the specific site and intended use. In most cases the specific outcome will provide some economic rent to the user, though distinguishing this from normal income, especially allowing for risk and long term effects, is impossible. The poor real knowledge behind real estate decisions is also a real complication. These decisions rely heavily on forecasts of the future that are ultimately impossible with any certainty. St. Thomas Aquinas suggested that prices could not be known with certainty and the difficulty with ascribing precise productivities to land would appear to be one aspect of this difficulty. This would appear to be an issue that will resolve itself in the longer term.

The third practical difficulty is the impossibility of regressing the returns to capital into returns to labour and returns to land. Ricardian rent theory implies that the return to capital is a compound, and that its components belong on either side of the wages line. While this is not contentious conceptually, in practice it would appear to introduce time variables that would be impossible to meaningfully analyse. In practice this problem resolves itself through the pricing of capital. The appropriate pricing in an ethical issue for the supplier of capital goods. Once purchased they will provide a normal return. The issue of the appropriate rate of return is not resolved in this process, but that topic has been shown to lie beyond the scope of this thesis.

The fourth difficulty is the fact that even wage earners use land in several different ways. Land provides the raw materials, sites for production, and also a site for the worker's home. If wages are depressed, residential land prices may also be depressed, and if wages are allowed to increase, residential land will increase in value. This would appear to set some land markets against each other, and complicate the meanings of the terms. Apparent wages will contain a portion that will be siphoned off as residential

rent, hence the normative (real, subsistence) wages are net of residential land costs¹⁰³. The theory does not appear to be capable of differentiating between these and they will compete between themselves. The main point is that they are by nature land property and follow the patterns outlined applicable to land, not wages. While they compete internally, they are common in that they are all derived from land, are conventional property and oppose wages, or natural property.

A final difficulty is the apparent simplification of the parameters of the law. Real communities do not have neatly separated classes of land owners and producers. Most people use real estate for both production and residential occupation and are likely to own some non-real estate assets. Similarly, consumer products often pass through several levels of production and exchange between their raw state and final destination. The theoretical treatment of Ricardian rent theory aggregates these into one process and hence ignores a multiplicity of transfer effects between them. Ricardian rent theory is therefore a macro principle in economics and its study necessarily requires simplifications that are not apparent in practical communities, despite being conceptually possible. Marx overcame this problem by seeking to socialise all property while Smith ignored any essential difference between natural and conventional property. It would seem that the appropriate response would be to recognise the common use obligation that attach to that part of one's income that is super-subsistence.

It would appear therefore that Ricardian rent theory may be a useful conceptual tool, but its positive validity may be impossible to verify empirically. If Ricardian rent theory is an operative component of the overall behaviour of real estate, then its omission from consideration is a shortcoming for the discipline of Land Economics.

10.7 CONCLUSION

Ricardo's rent theory provides a simple theoretical mechanism that has far reaching implications for economics. Although it begins almost as a tautology, it has the capacity to tie together various apparently disparate components of economic distribution. It is a vital link in the theory of perfect market operation, and one that has the capacity to inform several contemporary problems in economic thought and policy.

The major part of Ricardo's rent theory follows deductively from a finite set of premises regarding land and human nature. It leads to a simple division of returns between land and labour as wages and rent. Much of the theory has been validated by previous observations and studies. In particular, Ricardian rent theory highlights the nature of the problem of just wages in society. It demonstrates that wage justice is not

¹⁰³The definitions of wages and rent are critical here. Pure wages in the absence of a frontier will be no more than subsistence, even though the apparent wages may be higher. Land rent is the difference between productivity and essential wages and in many cases may be higher than market rents.

possible by relying only on free market behaviour, and in fact that the markets will militate against reasonable wages.

Three problems exist in taking Ricardo's theory of rent further. Firstly, the returns identified are normative returns to land and labour. They do not equate to the apparent positive quantities that are positively identifiable in actual markets. Secondly, the question of the determination of the wages line is lost in the transition in the theory across the closure of the frontier. Thirdly, the practical validity of the theory is not sufficiently evident in practice to be convincing.

The purpose of the next two chapters is to empirically demonstrate the positive validity of Ricardo's rent theory through an experiment that aims to expose the mechanism of rental formation in a perfectly competitive environment.

CONTRIBUTION TO THE SUPPORT OF THE THESIS HYPOTHESES

	Hypothesis	Treatment
1.5.15	Land rent is the differential between socially accepted subsistence and net site product.	Supported
1.5.16	Rents will find equilibrium at levels that absorb marginal productivity.	Supported
1.5.17	Rents will find equilibrium at levels that normalise returns to other factors.	Supported
1.5.18	Productivity increases will tend to be absorbed by rents	Supported
1.5.19	Land prices are a function of capitalised rents.	Supported
1.5.20	Land rents are not derived from land values	Supported

Chapter 11 Design and Procedure for an experimental study of price and rental formation in an efficient land market

11.1 INTRODUCTION

This chapter outlines a behavioural experiment designed to test the practical operation of Ricardo's theory of rent. The origin, operation and some implications of Ricardo's rent theory has been outlined, however its actual operation and the more difficult question of whether it may be referred to as a law, have not been dealt with.

The critical issue in Ricardo's rent theory is the level wages line. This suggests that under perfect conditions the return to non-land factors of production should be uniform across the entire land market. Two questions present themselves regarding the wages line as follows:

Is the wages line level, normalising wages across the entire market?

At what level is it located, especially with respect to overall productivity?

Although there is some support for Ricardo's rent theory, and many theorists appear to accept it, at least in a general way, its precise operation is not simply apparent in actual economies.

Five complications were identified in chapter 10 as being evident in actual markets that appear to obscure the operation of Ricardo's rent theory. These are:

- 1) The absence of perfectly competitive equilibria
- 2) The difficulty of assessing highest and best use
- 3) The impossibility of regressing capital into land and labour
- 4) The multiple use of land and the interaction between land markets
- 5) The multiple income classes accruing to most persons

It would appear therefore that Ricardo's rent theory may be a useful conceptual tool, but its positive validity may be impossible to verify empirically. Conversely, if Ricardo's rent theory is an operative component of the overall behaviour of the economy, then its omission from consideration is a serious shortcoming.

Fundamentally, Ricardo's theory of rent is a behavioural theory - it describes rental formation behaviour in an efficient market. In order to empirically observe its operation, an appropriate strategy would appear to be through simulation within a simplified economy. This approach suggests a behavioural experiment within a laboratory setting where the parameters of a simplified economy can be controlled.

This chapter describes the design of such a behavioural experiment, and the next chapter tables and discusses the results.

The present study is an attempt to examine the validity of Ricardo's rent theory experimentally by creating a simulated land market in which the assumptions of perfect competition are allowed to hold.

11.2 AIM:

To experimentally examine the processes that generate land rents and values in order to explore the validity of Ricardo's rent theory using the behavioural assumptions of general economic theory.

11.3 OBJECTIVES:

- 1) To examine the generation of land rents in a market of varied land productivities under perfect market conditions.
- 2) To examine the efficiency with which rentals are capitalised into land values.
- 3) To examine the distribution of increases in productivity between landlords and tenants.
- 4) To evaluate whether rents follow from land value, or if values follow from rents.

11.4 HYPOTHESES:

Hypotheses are numbered according to their presentation in Chapter 1:

- 3.5 Land rent is the differential between socially accepted subsistence and net site product.
 - 3.51) Rents will find equilibrium at levels that absorb marginal productivity.
 - 3.52) Rents will find equilibrium at levels that normalise returns to other factors.
 - 3.53) Productivity increases will tend to be absorbed by rents.
 - 3.54) Land prices are a function of capitalised rents.
 - 3.55) Land rents are not derived from land values.

11.5 METHODOLOGY

An experimental methodology, consistent with social psychology research, has been employed, using a laboratory situation to simulate a simplified rental market. The experiment involved the observation of the behaviour of groups of subjects in a

situation that required decision and action similar to a life situation. Observations were analysed using appropriate standard statistical methods.

If Ricardo's law of rent is indeed a law, then it must operate in all cases, even though its action may be obscured by the overarching operation of other factors that may obscure it. By simplifying the economic environment, these latter factors may be controlled so that the behaviour of the relationship can be studied. In this case, the simplifications include:

- (1) the removal of land use choices to a single, unspecified, highest and best use that is expressed in terms of financial gross productivity;
- (2) perfect knowledge;
- (3) perfect tenant mobility;
- (4) a single universal capitalisation rate; and
- (5) a general environment of perfect free market ethos.

Implicit in any experiment is the assumption that the relationships explored in one situation will validly hold in other related situations. That is, that they relate to the operation of the constant natures under consideration. This Aristotelian perspective is fundamental to science and recognises that our understanding of future particular situations is intellectually possible as a result of examining available particulars and abstracting accurately to certain knowledge of the appropriate essences. While it has always been recognised that such accurate abstraction is difficult in practice, it has generally been accepted that errors in abstraction will be reduced over time with the application of more human effort. This is the essence of confidence in scientific progress.

The experiment centred on a game. There has been considerable interest in games in recent years both as a most suitable analogy for commercial behaviour and also as an educational tool through simulation. This experiment uses aspects of both of these qualities of games. Through the suitable selection of tasks and rules the game recreates in miniature the same dynamics as is found in the actual market, though with the advantage of considerably more control. The accuracy with which this game parallels the essential operations of rental formation is an important methodological issue that will be discussed in the next chapter.

The methodology adopted is Aristotelian and the object is to study land and the human use of it. The natures under consideration are therefore:

Land: As a necessary factor in production, fixed in supply and capable of varying productivities.

Human nature: As both the tendency towards behaviour and, through free will, the most appropriate directions for action. The latter may be used as a foundation for directing future behaviour through moral, ethical and policy prescriptions.

11.6 PROCEDURE

11.6.1 General description of the experimental activity

The experiment involved two groups of subjects playing a two hour rental market simulation game. The game involved subjects bidding to purchase a limited number of multi-tenant parcels of land that they would lease to the remaining subjects. The productivity of the lots for lease and the terms of purchase which involved repayment out of rental earnings were given and known by all subjects.

The data collected included the prices paid, rents negotiated and the behaviour of the market following a change in productivity.

11.6.2 General Procedure

The experiment was run several times with different groups of subjects. Five runs of the experiment have been selected for analysis. The first three runs were pilot runs and included minor variations in procedure. The final two runs were identical, except for a difference in net productivity to enable the observation of the behaviour of the market as a result of a productivity change using an experimental and control group.

For each run of the experiment the facilitator followed the instructions shown in Appendix 1. The experiment was broken into five phases for each group as follows:

- 1) **Market learning:** Subjects were given information sheets (see Appendix 2) that described a notional real estate market and the general dynamics and rules of the game. The information included both the parameters and the critical values that existed in the market, sufficient to equip subjects with a complete knowledge of the market. The information also included a questionnaire to ensure that the subjects developed an active working knowledge of the market.
- 2) **Land allocation:** Subjects bid for several five lot parcels by tender or auction, such that about 15% of subjects became landlords. Subjects could only purchase one parcel and parcels were sold in order of diminishing productivity. While auction was used in most of the pilot studies, the final runs used tender bidding. Successful bids carried the condition that they must be paid for out of excess earnings from the first four years or suffer foreclosure, establishing a net capitalisation rate of 25%.

- 3) Four years of production and rent:** The remaining subjects became tenants who could negotiate single year leases with landlords. Tenants notionally worked the land at its highest and best use and paid rent. Landlords earned only rental income while tenants retained the difference between their total production and their costs which were rental and a fixed cost. During this period the market was expected to find equilibrium and at its close landlords were brought to account. Low productivity public land (commons) was also made available with number balanced to ensure that some tenants would be forced onto it. Common land returned subsistence incomes to tenants.
- 4) Productivity change and continuing operation:** At the end of year four, productivity, available common land and production fixed costs were changed and the game continued to establish new equilibria. In one group, the productivity increases were negated by increased fixed costs, in the other they were not. In both groups the maximum productivity of available common land was held constant.
- 5) Debriefing:** A week following the game, subjects were invited to complete a debriefing questionnaire and the results of the game were discussed.

Attention to the game was stimulated through rewards and penalties.

The experiment was run several times on separate groups as preliminary pilot runs to refine the procedure. The final two runs contain particular minor developments in procedure and have been executed in such a way as to test for the effect on rents of a productivity increase. Final Run 1 (16553, 1999) is the experimental group and Final Run 2 (16150 1999) is the control for examining the efficiency of productivity increases into rents. Data from the pilot runs have been included in parts of the analysis to a limited extent. This has only been done where it can be shown that the data is methodologically consistent with the final runs or where it informs analysis of the impacts of procedural variations, such as tender versus auction behaviour.

The major procedural variations between the pilot runs and the finals were a tightening of the rewards and sanctions and the various use of tendering and auctioning in establishing the land market. The latter is clearly noted in the results listings for each run.

11.6.3 Specific details of the experimental situation

A detailed description of the rules of the game and its administration are given in Appendices 1 (facilitator's notes) & 2 (preliminary information for subjects). Record

forms are shown in Appendix 3. The critical features of the simulated market are as follows:

- Currency was bags of gold (**B**) and all quantities, except for land purchase price, were annual cash amounts.
- Each player had to earn an income from *either* land rent or productive utilisation of land as a tenant.
- Landlords derived their incomes entirely from rent.
- Each player had to satisfy subsistence needs of **B**30 p.a.
- Each tenant had to pay annual fixed costs of **B**20 p.a., referred to in the game as "*capital costs*" to identify them as a return to capital as distinct from land and wages.
- Five lots of each of thirteen grades of land were potentially available, each grade having a different annual productivity as shown in Exhibit 11.1.
- Grades one to ten provided excess products over fixed costs and tenant subsistence of between ten and one hundred bags (**B**10 - **B**100) p.a.. These were available in five lot parcels. Players could bid for the purchase of a parcel and sufficient parcels were sold to occupy all but up to five subjects. That is, some tenants were forced onto common land.
- Land purchase had to be paid out of excess rental earnings amassed in the first four years, net of landlord personal subsistence expenses. This implicitly set a capitalisation rate based on a four year purchase. The maximum bids (rational prices), assuming nil vacancy and optimal rents are shown in Exhibit 11.2.
- Three levels of commons land were available (grades eleven to thirteen), five each at productivity levels sufficient to provide subsistence, **B**5 & **B**10 below subsistence respectively. These were owned by the state, however tenants could occupy them at no charge.

Exhibit 11.1 Land Market

Grade	Parcels	Lots	Product	Notional Rent	
1	1	5	150	100	
2	1	5	140	90	
3	1	5	130	80	
4	1	5	120	70	
5	1	5	110	60	
6	1	5	100	50	
7	1	5	90	40	
8	1	5	80	30	
9	1	5	70	20	
10	1	5	60	10	
11	<i>state</i>	5	50	0	<i>commons</i>
12	<i>state</i>	5	45	-5	<i>commons</i>
13	<i>state</i>	5	40	-10	<i>commons</i>

11.6.4 SUBJECTS:

Subjects were first and second year UTS undergraduate real estate students. They were considered an appropriate sample because of the following:

- 1) Their interest in real estate could be expected to be greater than the average and representative of lay investors/tenants.
- 2) Their knowledge of real estate could be expected to be reasonably uniform, though not well developed. In this they could be expected to reasonably mirror the profile of the majority of small real estate investors and tenants. Their behaviour could be expected to follow rational economic utility optimization.
- 3) By incorporating performance in the exercise into subject assessment, meaningful rewards and punishments could be incorporated into the game.
- 4) Their attention and continuous availability was reasonably assured.
- 5) Their motivation could be confidently expected on the basis of the game's learning potential and the competitive spirit encouraged within the programme.

In the final run of the exercise, the two groups were as follows:

- 1) A group of 58 first year students was used as the control group by varying parameters at the end of year four without a net productivity increase.
- 2) A group of 33 second year students that experienced a productivity increase of ten units (bags of gold) at the end of year four. Most members of this group had experienced the exercise in 1998 as Pilot Group 2 (16150, 1998).

The effects of the differential familiarity will be examined in the discussion.

11.7 TIMING

The final runs of the experiment were run in March 1999.

11.8 SUMMARY

This chapter has described an experiment designed to examine the behaviour of rental markets in order to test key parts of the operation of Ricardo's rent theory. The experiment is in the form of a game played by groups of subjects, some of whom competitively acquire land parcels and negotiate rents with the remainder who are forced to be tenants.

The game creates a near-perfect market environment with limited variables. By running the game and manipulating the variables, controlled observation of rental market behaviour is possible.

The next chapter will display and discuss the results of five runs of the game. It will use the results to draw conclusions regarding Ricardo's theory of rent.

Chapter 12. Results and discussion for an experimental study of price and rental formation in an efficient land market

12.1 INTRODUCTION

This chapter sets out the results from the behavioural experiment described in the last chapter. It discusses their significance and draws conclusions regarding the operation of Ricardo's rent theory in an efficient market.

12.2 RESULTS

Complete data for the two test runs and three pilot runs are contained in Appendix 4. The prices paid for the parcels sold in both the pilot and final runs are shown in Exhibit 12.1.

Exhibit 12.1 Parcel Sale Prices

Grade	Rational Value	Group One		Group Two		Pilot 1	Pilot 2	Pilot 3
		Bid Price	4 year Earnings	Bid Price	4 year Earnings	Auction Price	Auction Price	Tender Price
1	1880	1880	1866	1880	1559.5	1950	1920	2800
2	1680	1680	1680	1680	1559	1815	1790	
3	1480	1480	1480	1480	1092.5	1700	1720	2080
4	1280	1280	1273			1626	1655	
5	1080							1900
6	880	880	864	880	880	1420	1586	
7	680	680	623			1323	1215	1080
8	480	460	464			1040	855	
9	280	220	264.5	280	153	610	510	780
10	80	60	60	80	40.5	290	370	

The average rentals for the two groups are shown in Exhibits 12.2 & 12.3.

Exhibit 12.2 Group One Average Annual Rentals

Parcel	Rational	Average Annual Rentals					
Grade	Rent	1	2	3	4	5	
1	100	100	98.4	98.1	98.5	111	
2	90	87	88.8	89	88.8	104	
3	80	80	81.1	82	81	95	
4							not released
5							not released
6	50	50	50	50	50	50	evidence of collusion
7							not released
8							not released
9	20	16.6	15	10.9	17.9	30	
10	10	9	9	8.9	8.8	10.2	

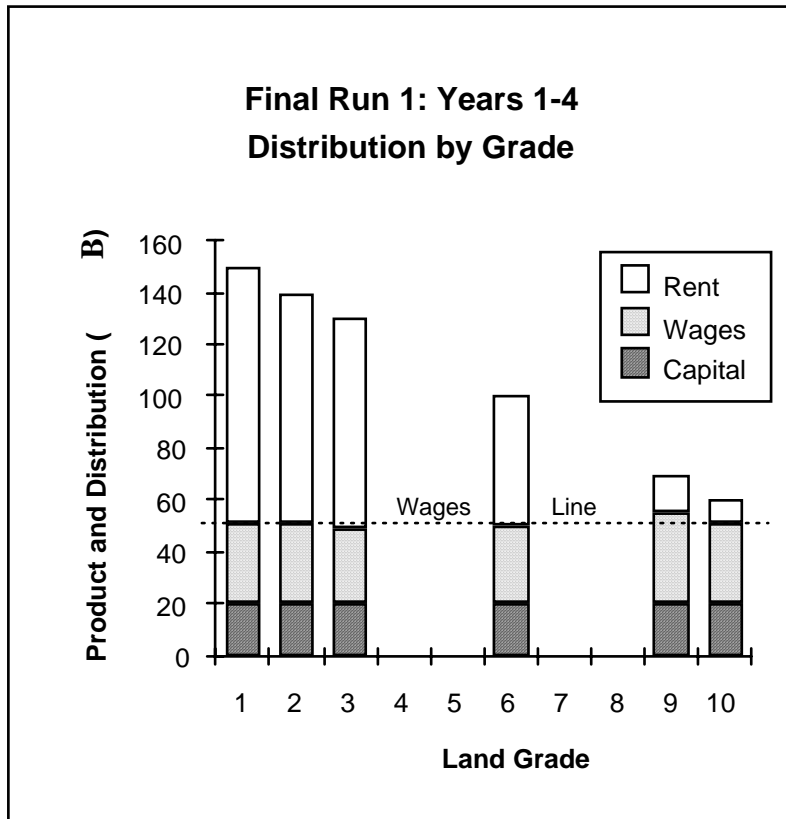
Exhibit 12.3 Group Two Average Annual Rentals

Parcel	Rational	Average Annual Rentals					
Grade	Rent	1	2	3	4	5	
1	100	98.4	99.6	99.6	99.6	99.4	
2	90	90	90	90	90	50	evidence of collusion
3	80	79.6	79.6	80.4	80.4	74.6	evidence of collusion
4	70	69.5	69	69.5	70.6	69.8	
5							not released
6	50	49.6	49.2	48.6	49.4	50	
7	40	39.3	37.2	39	41	46	
8	30	28.8	29	29.6	29.4	29.3	
9	20	19	19.9	19	19	19	
10	10	9.2	9	8.9	8.9	10.2	

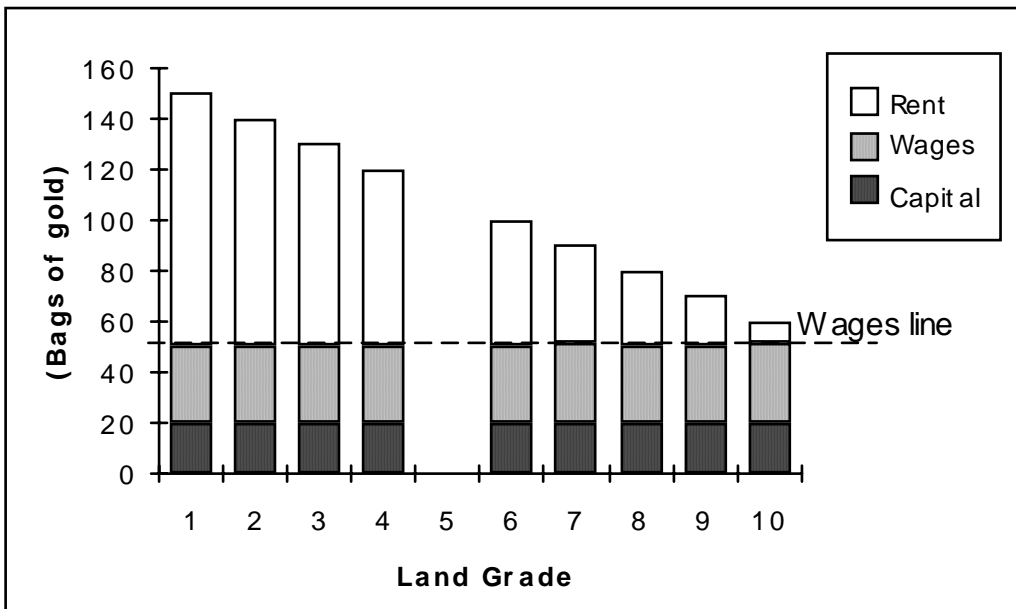
12.3 DISCUSSION

Adopting Ricardo's theory of rent infers that rents will have a rational level based on productivities and normal costs. Rational rents would therefore equal annual productivity less capital costs (return to capital) and labour (subsistence wages). In this way rents should absorb all marginal productivity (Hypothesis 1.5.16) and normalise returns to the non-land factors (Hypothesis 1.5.17). The resultant level wages line dividing returns to land and non-land factors is evident in the results as shown in Exhibits 12.4 & 12.5.

Exhibit 12.4 Final Run Distribution



Exhibits 12.5 Final Run 2 Distribution by Grade Years 1-4



12.3.1 Rental Market, Years One to Four

The first step in analysing the wages line is to compare the available data from the various runs. The exhibit 12.6 below shows the obtained average rents for each grade and year expressed as a difference from the rational rent for the five runs in Appendix Four. The years selected from each run are those before any changes in the market parameters, hence Pilot Run 3, which had a productivity increase at the end of year two, only contributes two years of data.

Exhibit 12.6 Normalised Rental Deviations

	Final Run 1				Final Run 2					Pilot 1				Pilot 2				Pilot 3	
	1	2	3	4	1	2	3	4	5	1	2	3	4	1	2	3	4	1	2
1	0.0	-1.6	-1.9	-1.5	-1.6	-0.4	-0.4	-0.4	-0.6	5.0	0.0	-1.6	-3.0	0.0	-3.8	-4.6	-6.4	-1.0	-1.0
2	-3.0	-1.3	-1.0	-1.2	0.0	0.0	0.0	0.0	-40.0	3.8	-0.8	-0.4	-10.0	-4.0	-2.0	-3.2	-2.4		
3	0.0	1.1	2.0	1.0	-0.4	-0.4	0.4	0.4	-5.4	-2.4	-2.6	0.4	-3.0	-5.0	-0.4	-3.4	0.0	0.5	-0.3
4					-0.5	-1.0	-0.5	0.6	-0.2	0.0	0.0	-3.6	-5.0	-7.0	-3.6	1.6	5.0		
5																		0.0	0.0
6	0.0	0.0	0.0	0.0	-0.4	-0.8	-1.4	-0.6	0.0		-0.3	-6.8	-3.4	5.0	-2.0	-2.0	-1.8		
7					-0.8	-2.8	-1.0	1.0	6.0	25.0		-1.6	-3.4	-10.3	-3.5	-6.3	-6.8		-0.6
8					-1.2	-1.0	-0.4	-0.6	-0.7	0.0	-1.0	-0.5	-1.0	-8.6	-8.2	-6.0	-6.0		
9	-3.4	-5.0	-9.1	-2.1	-1.0	-0.1	-1.0	-1.0	-1.0	0.2	0.0	-15.0	-15.0	10.0	7.0	-4.0	-1.3	-1.8	-2.2
10	-1.0	-1.0	-1.1	-1.2	-0.8	-1.0	-1.1	-1.1	0.2		-0.1	1.0	-2.0	20.8	-5.0	-0.5	20.0		

Using this data to estimate the population parameters of rental deviations suggests a population mean of **£**-1.12 and a standard deviation of **£**4.742. For sample of 139 observations, the departure of the mean from the expected value (**£** 0) has an observed Z^{104} value of 2.79 which is significant at the 0.05 level. The gradient of the wages line can be tested against the expected value by testing the significance of the deviations from the mean. These are listed with their Z values in Exhibit 12.7 and only Grade 10 is significant at the 0.05 level.

¹⁰⁴The z test was used in this analysis in preference to the t test because the total number of observations (139) was great enough to yield a sufficiently precise estimate for the population parameters. Adopting an estimate of the population parameters based on the totality of the data provided a superior estimate that what would have been available from estimates done individually following the standard t test procedure. Analysis using standard t test methods was performed, however, since the critical values were dependent on the individual sample sample sizes per question, these varied significantly. Since the variations come from a single population, this was considered unacceptable. Note that each of the observations itself represents the mean of 5 rental decisions.

Exhibit 12.7 Normalised Deviation Statistics

	Rental Deviation Statistics					
	n	m	Z_{obs}	Z_{crit}		
1	18	-1.3	2.352	-0.20	1.96	
2	16	-1.6	2.872	0.40	1.96	
3	18	-0.7	1.84	0.40	1.96	
4	12	-1.2	3.205	-0.03	1.96	
5	2	0.0	0	0.33	1.96	
6	15	-1.0	2.441	0.13	1.96	
7	13	-0.9	8.379	0.15	1.96	
8	12	-2.9	3.292	1.28	1.96	
9	18	-2.5	6.137	1.23	1.96	
10	15	1.7	7.676	2.32	1.96	Significant
Total	139	-1.12	4.742	2.79	1.96	Significant

The pilot runs contained minor procedural differences to the final runs. Therefore it is necessary to examine if the final runs significantly depart from these results. The mean rental deviation of the two Final runs was **B**-0.876 over 60 observations with a standard deviation estimated from the sample of **B**1.54 for any one observation in the population.

Adopting the standard deviation from all five runs suggests a standard deviation of **B**0.61 for the population of means, leading to an observed Z statistic of 0.4, well within the critical value of 1.65 for significance at the 0.05 level. Hence, the final runs are not significantly different to the complete set of observations.

Hence, null hypothesis to hypothesis (1.5.16), that *rents will not find equilibrium at levels that absorb marginal productivity*, may be rejected. The experiment appears to support the adoption of a zero gradient wages line.

Hypothesis (1.5.17) is not so easily dealt with. Its null hypothesis is that *rents will find equilibrium at levels that normalise returns to other factors*. Normal incomes suggest wages that cover the cost of living, or subsistence, only, yet the experiment has indicated a wages level about **B** 1 above this level.

Tenants were therefore able to retain what is in effect an economic rent of about **B** 1, or super-normal incomes. It would appear that the null hypothesis cannot be rejected in this case, hypothesis (1.5.17) must be rejected.

Most rent theorists in the Georgist or Ricardian traditions would interpret this as a part of the natural land rent that has been retained by the tenants¹⁰⁵. This is problematic

¹⁰⁵Georgist theorists usually believe that the wages line defines subsistence. This is especially the case where other imperfections such as taxation and supernormal profits do not exist, which is the case in this experiment.

in a positivist methodology where the absence of evidence of these economic rents being regularly taken by land rent makes it impossible to make such an assertion. The terms of the game preclude other economic rents which would appear to leave little latitude for retaining the notion of essential foundations for the quantities of rent and wages in the face of the evidence, at least as far as they are linked to subsistence.

The resolution of this tension may be attempted from two directions. Firstly by suggesting moderating causes within the experimental design that may have had the effect of biasing the simple operation of the relation under consideration.

The fact that the experiment has returned rents that are slightly, though significantly, below the predicted levels, but follow its gradient, may be the result of several additional factors within the experimental design which have left slight imperfections in the market. These include the following:

- i) Tenants, knowing that the purchase price of the land represents the total appropriation of rent, could be expected to strongly resist any attempt at charging rents in excess of that level. This places a *ceiling* on rents, meaning that any negotiation must be below that level.
- ii) The existence of common land means that tenants have an alternative to the private market and one that they could be reasonably certain of supplying a subsistence income. Even if sufficient tenants chose this option and so have some forced into occupation of sub-marginal commons, at the time of negotiating rents this possibility would be of diminished perceived importance to tenants.
- iii) Landlords cannot afford vacancy in the first four years when their pricing has assumed full tenancy, and hence could be expected to offer discounts rather than suffer certain major loss.
- iv) The small actual size of the market, the coarse monetary unit, and the relatively small time frame all may combine to introduce a "graininess" into the results which aggravates the apparent shortfall.

It should be mentioned that in both groups certain collusion was evident. In Group One, the landlord for the Grade 5 land and five tenants resolved to adopt marginal rents from years one to four and in the fifth year maintained the same rent. In Group Two there was evidence of similar practices in both Grades Two and Three. Although the collusion was less overt in the Grade Three parcel, it did result in this being one of the few landowners to remain solvent for the four year pay back that may not otherwise have happened. In the case of Grade Two the correction in year five was by way of a massive rent reduction as a reward for loyal tenants. Close examination of the Grade Two landlord's sheet for the exercise revealed that the numbers had been altered late in the exercise in collaboration with at least one tenant. The collaboration underlined the

importance of the rewards and sanctions being well correlated to the total performance. The strategy undertaken by the Grade Two group was designed to return optimum grades to the players while creating market outcomes that were themselves irrational.

The collusion violated some aspects of perfect market behaviour, but also added a certain "real world" flavour to the experiment. Overall, although it objectively distorted the results, it was not sufficient to invalidate the overall significance of the results. The fact that collusion strategies were apparent in both final runs may be related to the stronger sanctions themselves.

The second issue that is relevant in explaining the resultant level of the wages line, is the fact that its level is recognised to behave in a very different way, depending on whether a frontier exists or not. Wages (returns to non-land factors) are notionally set by the least productive land in service. Where there is an abundance of highly productive land compared to producers, the wages line will be well above the cost of living. Conversely, when only poor land is available and population pressure is great, wages may be forced below reasonable subsistence.

Where no frontier exists, all land attracts some rent. Since all production is tied in some way to land and no land is freely available, the wages line may still operate as a leveller to the returns to non-land factors, but demand is no longer arbitrary. So long as there are more tenants than available sites, rents will be the outcome of pure negotiation. The threshold between this condition and one where rents are reined back through real competitive alternatives is relatively soft and dependent on such things as planning controls, levels of technology and political balances between the parties.

The confidence with which Georgist theorists suggest that the wages line defines subsistence ignores this possible real variance. Ricardo recognised the impact of population pressure in pushing the wages line down, though he also suggested that the cost of living is also a function of commodity price levels, themselves the result of the production of others. There is merit in his approach, though it tends to lose its focus in a circularity. Henry George was more optimistic, and while adopting the basic rent theory of Ricardo, brought it into the urban context with the observation that population was largely the source of land values. Side stepping Ricardo's regress, George believed that as the population of a city increases, so does the productivity of its land¹⁰⁶. Urban rentals certainly do outstrip rural ones. This was supposed to negate the downward wage pressure on the wages line by increasing the total product, however as George also recognised, in these situations, greater disparities between rich

¹⁰⁶Julien Simon has shown George to be correct in this respect, though arguing more generally from a premise regarding the innovative capacities of people.

and poor tend to exist, leading to his maxim that in cities *Progress & Poverty* advance together.

Subsistence is therefore a problematic assumption. The wages line appears to have no necessary connection with subsistence, as the latter is normally understood. As a leveller for non-land factors in a competitive market it does appear validated, but as something tied to the cost of living it is more difficult to relate to the theory. Ricardo's recognition that the cost of living is determined by the price levels of consumer necessities has merit, though following these prices back to their source becomes a red herring. The common level of wages is better understood by considering community expectations. Hence, when a community is in the habit of receiving a certain level of material welfare, that level tends to become identified with subsistence. In Western countries, prisons often have televisions and hot and cold running water for the inmates on the belief that it would be unnecessarily cruel to deprive prisoners of these basic human requirements. Subsistence is very dependent on culture and time.

Hence, subsistence may be considered either objectively as that level of material welfare required to enable a working unit (family) to maintain a stable, human, standard of living, or relatively, as that level of material welfare that is common to the working class. While there is considerable overlap in the practical resolution of these two approaches, there is a considerable ethical distinction. The first, if it was at the base of the Law of Rent, would prevent rents rising.

In supplying free, objectively subsistence-level common land, the experiment implicitly connected these two notions of subsistence in its design. This may be reasonable on the basis that any actual market will be settled at a relativistic subsistence, merely because such a definition of subsistence is almost a tautology. The priming notes that subjects worked through before the simulation also contained examples that suggested conventional economic rents to tenants above objective subsistence of **£10**, which may have inclined an expectation of super-subsistence incomes for tenants. Conversely, the exercises that concluded the preliminary notes included questions that explored marginal decision behaviour in a way that explored the conditions under which tenants would rationally choose between the commons and the private market.

Perhaps further work is warranted in this area to experimentally examine market behaviour when either the frontier exists at productivities markedly different to objective subsistence, or in a closed market, possibly with some vacancy.

12.3.2 Rental Market Following Year Four

The average difference between the year five rents for the experimental group (Final Run 1) and the average for that group in years one to four was **£9.5**. For samples of 6

observations in the population examined for years one to four, this mean belongs to a population of means having an estimated standard deviation of **B0.625**.

The observed t statistic is therefore 15.2, compared to a critical t value of 3.14 for significance at the 0.01 level. The observed mean **B8.3** may also be compared to the theoretical zero base and still return an observed t of 13.3, also significant. This result would lead us to reject the null hypothesis to hypothesis (3), that productivity will not be absorbed by rental increases.

In particular, the question is whether the entire productivity increase has been absorbed by rents in year five. Given average rentals of **B-0.88** in years 1-4, the expected new rentals should be **B9.12**, or **B0.78** above the average for year five. The rents for year five suggests a population standard deviation of **B6.63** for a single observation, or a standard deviation of **B2.70** for the means of samples of 6 observations. This results in an observed t statistic of 0.288, against a critical t of 2.015 for rejection at the 0.10 two-tailed level. This means that the results cannot be rejected as members of the population of samples where the productivity increase is fully absorbed by rental increases.

By contrast the control group (Final Run 2) had a mean rental difference from the rational level of **B-4.6**. While this may at first appear to suggest a significant fall in rentals for this group in year five, closer examination shows that this is largely the result of the landlord and tenant collusion in Grade 2 of that group.

The average rental for land in the grade two parcel in year five was **B50**, or **B40** below the marginal rental. The year five standard deviation was **B13.6**, giving the Grade 2 result a Z statistic of 2.94, or an 0.0016 probability of occurrence within the population suggested by the sample as a whole. Combined with the discussion above on the evidence of dysfunctional collusion within Grade 2, there is strong justification for leaving it out of the data for year five. With this done, the mean rental difference from the expected is **B-0.2**. For a sample of eight observations, this result returns an observed t statistic of 1.11, compared to critical t values of either 1.833 or 2.821 for the 0.05 or 0.01 levels of significance respectively. Therefore, there is no basis for rejecting the year five results of the control group from the population of rents that are formed from the results of years 1-4.

The rents for the control group (Final Run 2) in year five appear to belong to the same population as those for both groups for years one to four, whereas the behaviour of the experimental group is statistically consistent with the full appropriation of productivity increases by rents. Hypothesis (1.5.18), that productivity increased will tend to be absorbed by rents, is therefore supported.

12.3.3 Pricing

The first two pilot studies used auctions to sell parcels and the results indicated a systematic over-pricing. The third pilot run used a tender process, though its results were complicated by the initial assertion that productivities would be increased somewhere after year one. The final runs used a tender process with the promise that productivities would be constant over the first four years and returned more sober bids. The premiums paid above the rational capitalised price are shown in Exhibit 12.8¹⁰⁷.

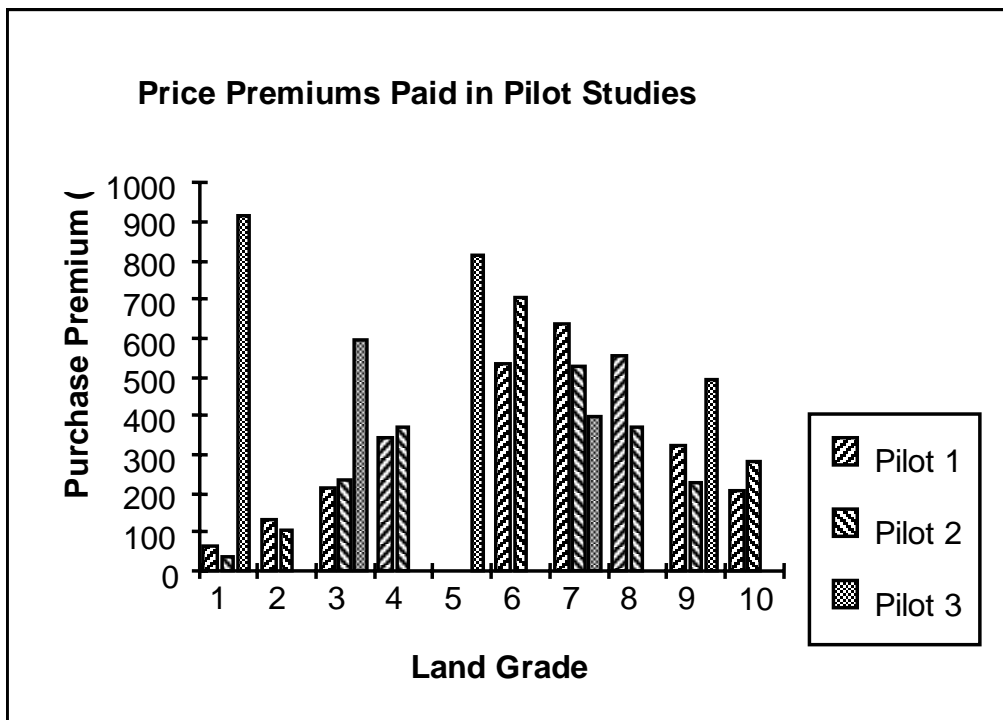
Exhibit 12.8 Purchase price above rational maximum bid

<i>Grade</i>	Group 1	Group 2	Pilot 1	Pilot 2	Pilot 3
<i>1</i>	0	0	70	40	920
<i>2</i>	0	0	135	110	
<i>3</i>	0	0	220	240	600
<i>4</i>	0		346	375	
<i>5</i>					820
<i>6</i>	0	0	540	706	
<i>7</i>	0		643	535	400
<i>8</i>	-20		560	375	
<i>9</i>	-60	0	330	230	500
<i>10</i>	-20	0	210	290	

Exhibit 12.9 graphs the patterns of purchase price premiums for the pilot runs revealing a tendency for an increase in bid premiums from grade one to the middle grades. The fact that parcels were sold in order of their grade, may have accounted for this trend, combined with the bidders' perception of market willingness to pay premiums above the rational maximum. Initially strong bidding may have been stimulated by competitive sentiments that used the market more than the fundamental as a queue for behaviour. The tendency for premiums to diminish from the mid-grades to the least productive grade (grade 10) may have been influenced by growing realisation that the poorer parcels could not support repayments from rentals sufficient for successful purchase over four years. What is clear is that prices were well in excess of the rational bids, reflecting an over-optimism that resulted in uniform landlord failure in these pilot runs.

¹⁰⁷Rational capitalised price is that price that expects zero vacancy, appropriation of the entire marginal product as rent and its entire capitalisation, after removing landlord subsistence, into repayments over four years.

Exhibit 12.9 Price Premiums in Pilot Runs



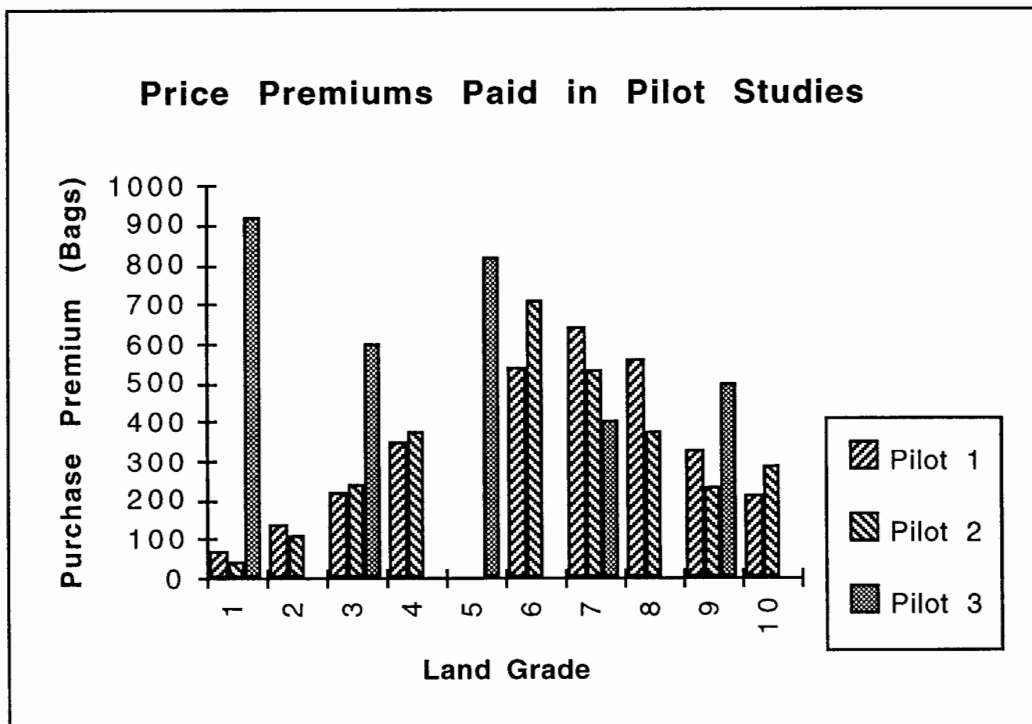
The auction situation itself may encourage irrational premiums. Pilot run 3 was executed using tender, but subjects were told that there would be a productivity increase sometime after year one. The prices bid reflect an inability to price this risky prospect of future benefit. There is no evidence of the hump favouring the middle grades, which suggests that the latter was an artifact of the auction situation.

The data may be slightly misleading due to the fact that only winning bids are listed and parcels were sold beginning with Grade 1. Lusht has suggested in describing the Bidder's Curse that the bidder who errs most optimistically will win the property, but face ruin (Lusht 1994). In the case of Pilot run 3, the winner of the Grade 1 parcel may have submitted similarly over-stated bids for the other parcels, but having won a parcel had the remaining bids dropped from consideration. The pricing behaviour of bidders under uncertainty may be explored in a separate study, for the present purposes uncertainty of this type was removed.

In addition to using auctions, the pilot studies also carried milder sanctions. The final runs carried a nominal 4% grading towards the subjects' final subject grade with possible bonuses well beyond that amount for the most successful players. Penalties meant that poor players, especially landlords, could end the exercise with zero, or even negative, grades. In the pilot runs, few participants who took reasonable interest in the exercise earned grades outside the band of 2-4 marks, which meant that there was little real stimulus for prudent involvement.

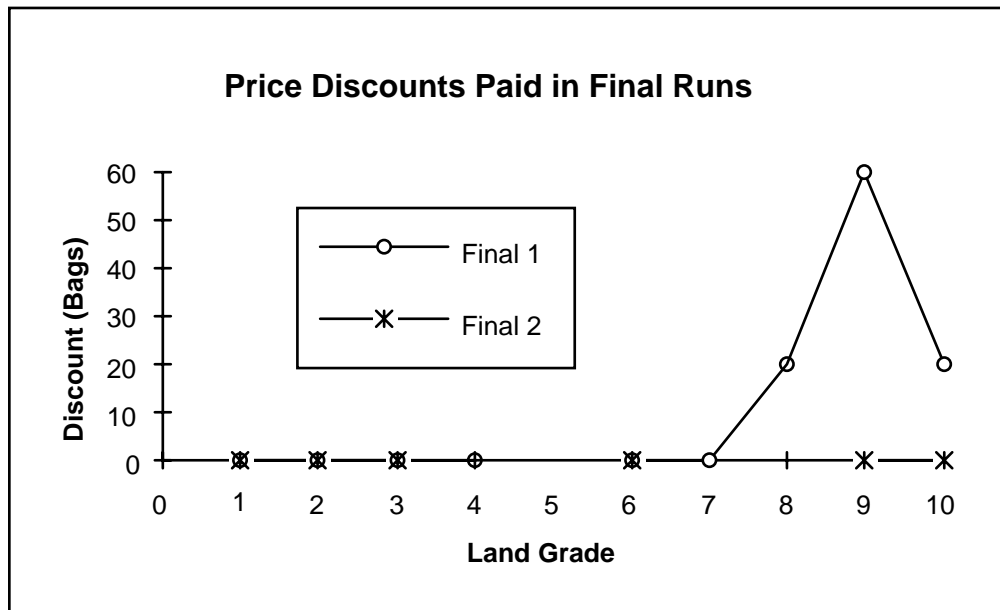
V@Ác@ãÄ æÁ&ç)^áÁ{ Á@Á@ãÁÁ] ^Á-Á@Á@•ãÁÁ
@Áæ^ÁÁ@Á^&d[]æÁ] ^Á æÁ[óã]æç*Á[!^&d^É

Exhibit 12.9 Price Premiums in Pilot Runs



In the absence of effective sanctions, participation could be expected to be more reckless. By contrast, real world real estate decisions carry considerable commercial sanctions, hence the stronger rewards and penalties of the final runs were considered justified.

Exhibit 12.10 Price Discounts on Final Runs



The final runs used a tender process which appears to have encouraged moderation, which is quite evident in the way that bids generally followed the rational values very closely. Exhibit 12.10 shows that no bids were received above the rational value, and in some cases parcels sold for under it (a discount). The parcels that sold for discounts below the rational value were at the end of the sale and may have been the result of coming after the more aggressive bidders had won parcels. Close inspection of the tenders confirm this.

Further study of the contrast between auction and tender behaviour appears warranted, however, it appears reasonable to conclude that behavioural factors in addition to rational financial evaluation was evident in the auction results. It is peculiar that pilot runs 1 & 2 returned patterns of premiums that appear visually correlated, however this will not be explored further in this study. The precision with which the tender bids of the final runs followed the rational expectations suggests behavioural factors in addition to rational expectations applying in the pilot runs.

In terms of Hypothesis 1.5.19, the null hypothesis would be that *land values are not capitalised rents*. The final runs appear to supply sufficient evidence to reject the null

hypothesis. Taken together, they form a sample of 15 observations having a mean of **B**6.7 and a standard deviation of **B**4.2. This results in an observed t statistic of 1.5811. For an acceptance level of 0.10 with a two-tailed test¹⁰⁸ probability the critical t value is 1.76, therefore the null hypothesis may be rejected since the observed mean is probably part of the population formed from the rational value computation.

The rational value assumes that all the excess from production will be taken as rent and landlords will be willing to pay all of this excess in the first four years to secure a parcel. The notes that the subjects worked through in phase one of the exercise did not make this assumption, and the worked examples were based on tenants being left with **B**10 excess. While some reference to marginal choice behaviour was explored in the notes, it was consistent with that found in general economic theory.

What can be concluded from this part of the experiment is that when site productivity is known, investors will expect to be able to appropriate as rent all of the product in excess of subsistence expenses and necessary costs, consistent with the Ricardian rent theory. Contrasting Pilot run 3 with the final runs, it appears that risky growth prospects will be disproportionately represented in evaluating bids, though this behaviour warrants further specific study and may be influenced by other factors, such as market confidence.

The question may still remain as to whether tender or auction behaviour is more consistent with rational evaluation. The discussion so far may appear to be theory dependent, in that the results of the auctions in the pilot runs has been dismissed as irrational. This issue deserves further investigation. However, inspection of the results of the pilot runs shown in Appendix 4 show that the landlords failed to meet their repayment commitments roughly in proportion to the excess of their bids. This would appear to support the charge that the bids were not rational in the normal meaning of the term. In addition, but not tabled in the data, were the results of the briefing (homework) questions, which included the computation of rational bids. Very few subjects failed to accurately compute the rational bids from the briefing questions. This means that subjects entered the auction having accurately computed the rational bids, but proceeded to bid considerably higher. This would appear to be explicable only in terms of the psychological effect of the auction situation.

The Pilot runs provide the clearest information suitable for investigating Hypothesis (1.5.20), that rents are not derived from land values. The final runs returned values consistent with rational values, and hence suggest that values follow from rents. If the converse were the case, and rents followed from values, one may expect that where

¹⁰⁸With a two tailed test, each tail represents an acceptance level of 0.05. Hence the rigour of the acceptance criterion is consistent with the other tests in this experiment.

values are outside of predicted capitalisation expectations, then rents may be expected to follow them. That is, the rents in the pilot runs should be significantly higher because they were negotiated in a market where land purchase prices were higher. The hump in land values in the middle grade should also be expected to find some expression in rents.

The data here is very clear. Despite each of the pilot runs returning purchase prices substantially above rational values, the rentals in each run averaged ~~B~~(1.34) *slightly below* rational expectations, consistent with, but lower than, the final runs that averaged ~~B~~(1.37). There is no evidence to support the null hypothesis to Hypothesis (1.5.20), i.e. that *rents are derived from land values* in perfectly competitive markets where knowledge of productive potential is broadly available. In practical situations, this level of knowledge is rare and its validity is often transient. Hence, through ignorance, it may be the case that values (real estate purchase prices) are used as a proxy basis for estimating rentals, however, this would be the direct result of the failure of the necessary conditions for a perfect market. The finding in the experiment is also consistent with the capitalisation method of valuation which implicitly locates rents prior to values.

Fisher (1930/1977) had asserted the primacy of actual returns when he noted that, "*Income is derived from capital goods. But the value of the income is not derived from the value of the capital goods. On the contrary, the value of the capital is derived from the value of the income*" (p.14), and consequently, "*It is true that the wheat crop depends on the land which yields it. But the value of the crop does not depend on the value of the land. On the contrary, the value of the land depends on the expected value of its crops.*" His observation is also consistent with the view that money interest rates are primary in determining modern capital asset values.

CONCLUSION

The experiment has found support for the critical aspect of Ricardo's rent theory, that rents will absorb marginal productivities in perfectly competitive markets. A zero gradient 'wages line' did result from the free operation of a simulated rental market, consistent with theory.

The level at which the wages line found equilibrium was significantly above the expected level, given normal economic marginal choice behaviour. This meant that economic rents were retained by the non-land factors of production at an approximately even level across the market. This finding has brought into question the notion of subsistence as it is commonly used in connection with Rent Law theory. This will be discussed in the next chapter. While an objectively super-subsistence income was obtained by tenants, this may be consistent with a relative notion of subsistence based

on some form of social/cultural expectations. It may also be explained in terms of the political balance between landlords and tenants.

Ricardo's rent theory has been verified by the simulation, although it has found equilibrium at a wages line slightly above the anticipated marginal level. An alternative way of viewing this outcome is to conclude that the market has actually behaved as though there was an operative frontier and the wages line has settled at a level that is a little above the productivity of the Grade 11 commons. This is despite the fact that the Grade 11 commons were occupied.

Land values within the simulation found differing levels partly as a function of the strength of sanctions (actual rewards and penalties given to the subjects), the type of sales process and partly due to perceived risky opportunities. The final runs used significant sanctions and tender bidding and produced prices very close to expectations. The directionality between rents and prices could be examined because the simulation began with neither rents nor prices known. The indications were that although there was considerable evidence of values being set through bidder expectations of future rents, rents showed no movement as a result of land prices.

The experiment has shed light on the behaviour of markets and has lent support to the basic operation of Ricardo's Rent Law, however, it has also exposed several areas for further research, such as the dynamics of the wages line level. The return to wages was shown in Chapter 9 to be critical in the understanding of just economic relations and will be explored further in the remaining chapters.

CONTRIBUTION TO THE SUPPORT OF THE THESIS HYPOTHESES

	Hypothesis	Conclusion
1.5.15	Land rent is the differential between socially accepted subsistence and net site product.	Appears to support a political, not objective, notion of subsistence/wages
1.5.16	Rents will find equilibrium at levels that absorb marginal productivity.	Supported
1.5.17	Rents will find equilibrium at levels that normalise returns to other factors.	Not supported
1.5.18	Productivity increases will tend to be absorbed by rents	Supported
1.5.19	Land prices are a function of capitalised rents.	Supported
1.5.20	Land rents are not derived from land values	Supported
1.5.21	In practice, the resolution of the actual level of the subsistence wage is social/political.	Supported

Chapter 13 Subsistence wages, economic rents, savings and taxation

The purpose of this chapter is to review some of the issues associated with Ricardo's rental theory. It will deal with the returns to other factors of production, especially wages. It will examine the behaviour of other economic rents, the whole issue of super-normal profits and introduce the relationship between land rents and taxation. The significance of rental incomes for savings and investment will be reviewed and its importance for understanding economic fluctuations. Several of these topics will be explored separately in greater depth.

13.1 SUBSISTENCE AND NATURAL WAGES

The transition of wages from marginal frontier productivity to subsistence with the close of the frontier introduces a considerable problem. The notion that the price of wages in a liberal perfect market finds an equilibrium at its cost is not contentious, nor could it be given the terms of the proposition. After all, liberal free markets assume no more than the positive results of unhampered price determination between agents who are free to enter or leave the market and are motivated by a rational intention towards self-interest. Therefore, in an economic sense, the determination of wages is straightforward and deserves no further consideration. The market will force wages down to subsistence. The problem arises when there is an attempt to actually quantify what constitutes subsistence. This is best understood as a social issue, not an economic one, and therefore forces the resolution of this key term in economics out of market economics.

The determination of subsistence is highly imprecise and introduces a major weakness into Ricardo's theory that appears to have been adopted uncritically by later rent theorists. For any given level of income that may be considered as bare subsistence, the flexibility of humans will enable them to exist on one that is slightly lower. Humans always seem to be able to break their own records - an athlete's endurance is not very different to economic endurance; athletes perform set tasks in less and less time, and persons on limited means will almost always find ways to make do on slightly lower incomes. The problem is that this means that there is no hard and fast base level of subsistence as Ricardo supposed. Historically, Ricardo and Dickens were contemporaries, yet it would be difficult to reconcile Ricardo's optimism regarding the ability of land markets to return subsistence incomes in the light of Dickens' portrayal of the realities.

The danger with Ricardo's theory of rent is that there is the risk of complacently adopting the reality of low wages as a natural result of population pressure alone. This falls into the Malthusian trap and commits three major errors. Firstly, it ignores population as a resource. People are the source of innovation and technology and it is their ingenuity and problem solving ability that drives productivity forward¹⁰⁹. Secondly, it obscures the fact that the depression of wages is not the result of reduced productivity, but results from increased rents across the market. Thirdly, by taking the Enlightenment strong form notion of natural laws that implied that they were inescapable, it frees the beneficiaries of its operation from any moral scruples.

Of these, the third is most troubling, because it is precisely what happened in England between the eighteenth and nineteenth centuries, as the result of not only Ricardian theory, but also Smith's success in establishing the market as a *natural* process and the moral floor to economics. It may be an issue that is re-emerging as deserving special consideration at the present time.

If it was population alone that was the natural cause of depressed wages in Ricardo's day, and wages at that time were at a six hundred year low¹¹⁰, then population control would become a reasonable solution. The considerable support that this conclusion currently enjoys ignores the fact that population, *qua* people, is a massive resource and the origin of all the technological development of recorded history. There is a growing awareness that people are capable of improving their productivity through the application of their intellect at a rate that outstrips the subsistence consumption demands of the world's population¹¹¹

The significance of subsistence as the basis of the wages line is a common theme that runs back through classical theory. Marx was perhaps the last in that tradition who recognised that wages were the price of labour and because price finds its natural equilibrium at its cost of production, wages would be naturally priced at the cost of subsistence (Roll 1942). This was no more than an echo of ideas that were first systematically presented by Smith, however Marx had the distinction of observing that wages determined by the liberal free market were inhuman.

¹⁰⁹Economist Julien Simon has done considerable work on the proposition that human ingenuity is the proven solution to the expanding needs of the growing population (Simon 1995). (Samuelson 1975) featured graphs in the inside cover of his book that showed the correlation between population growth and economic progress. In 1975 such a proposition did not appear as contentious as it has become in later decades, despite an absence of evidence in support of the more recent belief.

¹¹⁰see (Charles 1991; Rogers 1884/1949)

¹¹¹Paul Ehrlich predicted that the world would be subject to widespread global famines about twenty years ago, based on his comparison between the behaviour of butterfly populations and post war demographic trends of human. The spectacular failure of his predictions, despite continued population rises can only be accounted for in terms of improved human productivity, a uniquely human capacity that butterflies are incapable of mimicking.

However, there is a major difference between the prospective subsistence wages of Ricardo's rent theory and that of Smith, or even Marx. Perfect market theory suggests that wages and profits will both find equilibrium at subsistence and normal levels respectively, with the implication that neither wages nor capital will necessarily have the upper hand. Liberal market theorists tend to believe that this will result in a natural balance between labour and capital that is impeded by imperfections such as oligopolies and labour unions. It should be noted that in this view land, labour and capital are not differentiated, so long as each is priced by an efficient market.

Liberal market theory does not differentiate between land and capital, both are capital assets¹¹². This implies that somehow perfect competition will normalise the returns to land as well¹¹³. This is the exact opposite of the conclusions of Ricardo's rent theory, which would normalise wages (and supposedly also the return to capital) by directing all super-normal productivity to land as rent. Ball and Wood (1995) studied long term asset prices and found that real estate prices have appreciated, while his category *equipment* (produced assets, tools) have depreciated. This finding is consistent with Ricardian rent theory and demonstrates that it is capital in land, not capital *per se* that opposes the condition of the working class¹¹⁴.

The English liberal economists of the Enlightenment and following were not fond of affording workers excess wages for fear of permitting them to grow lazy, which produced a patronising self-justification for the exploitation of labour through depressed wage levels. The suggestion that market forces will provide workers with some sort of justifiable/natural wage is still strong today and is typically behind movements against worker association or collective bargaining.

The more developed form of this argument is current liberal market theory which relies on the market to be the moral arbiter. Apart from neglecting the possibility that the market for labour may be far from perfect, or that human solidarity may require allowing working people more than a scant material survival, by omitting any specific

¹¹²Finance and real estate literature makes no distinction between any assets that can return a profit. Hence, land, physical capital, equities and money are all considered to be indistinguishable species of capital assets. This is especially evident in the literature on economic cycles that appears to have great difficulty conceptualising the impacts of the dynamic interplay between these very different assets (Small, 1995; Small, 2000).

¹¹³In the short time frame of actual property investment, this may appear to be the case, as the price of land will approximate the present value of its future returns, thereby normalising the investor's subsequent rental income. This is a distraction from the real issue, which is how the purchase price of the land investment came to be at that level in the first place. Like other financial assets, land is valued at the present value of its future returns, which does not necessarily imply any notion of normal returns.

¹¹⁴Strictly speaking of land is not capital as the latter denotes produced productive assets though current usage tends to blur this distinction.

consideration of the behaviour of land, such a belief is dangerously deficient if anything like Ricardo's theory of rent is in operation¹¹⁵.

Watson (1995) found that rentals were best explained by "*...the balance of negotiating power between landlord and the tenant*" suggesting that rents are ultimately political. This would appear consistent with history and regrettably also with Marx's interpretation of class struggle. However, this is not to say that Marx's interpretation is not flawed in other respects, especially with respect to the necessity of conflict within social relationships. There may also be an inherent instability due to the fact that actual working wages may oscillate either side of a conceptual equilibrium due to the fact that over-exploitation of wages by land and other rent-takers may take time to translate into some sort of political opposition. The over-exploitation of labour will be evident as polarization in wealth and income distributions. These have been observed to correlate with economic recessions and a separate set of fluctuations (Das 1993).

This view was the conclusion of (Raffalovich 1999) who studied patterns on property incomes in OECD countries from 1960-1990 and found two opposing trends. Firstly, property incomes in the short term tended to increase with respect to wages incomes, but secondly, over long term they tended to return to wages. This led Raffalovich to conclude "*This suggests that in advanced industrial capitalism the power of property is rooted in political, not market relations*" (p.14). The short term effect can be seen in Ricardo, and the long term in the political opposition that is mustered when wages are depressed so far that labour militancy is roused to the point of challenging the political power normally held by the propertied. Although Raffalovich's data is limited, his findings accord with broader patterns of economic history.

The examination of population and wages in Chapter 10 only considered population pressure with an open frontier. Population pressure with a closed frontier is the more relevant question for most Western economies. Notionally, the Ricardian rent theory was limited by its implicit assumptions of fixed productive technology and fixed demand. These assumptions are reasonable for consideration of situations involving a frontier, but they must be reviewed when considering the situation when the frontier is closed. If these conditions held with a closed frontier and population rose, there would simply be more workers than jobs. Labour has been likened in the discussion so far to a product, in that it has a cost of production and a price. At best this comparison is no

¹¹⁵There are at least three moral arguments supporting the use of the market to determine wages: (1) Ricardian/Malthusian conclusion that low wages are the result of population pressure, (2) that the market naturally returns economically optimum pricing and (3) that wages should not be allowed to rise for fear of encouraging sloth. If (1) holds it will contradict (2). (3) may be empirically valid but introduces complex ethical questions.

more than analogous. Unlike products, the cost of labour does not abate when the labour 'product' is not being realised. The working family must still find food, clothing and shelter, even when no employment is available. This fact is not recognised in a market determination of wages. Socially, it leads to questions regarding the community's responsibilities to its unemployed members. Within the market, it means subsistence becomes the highest price that employers need to pay once there are more people seeking work than places available.

This can be understood using an example. Consider a village with one hundred working families, a cost of subsistence of \$5 per hour and ninety available jobs, eighty five of which are occupied. The unemployment rate is similar to current Australian levels, but for every job there will be three applicants. Each applicant may ask for \$5 per hour, knowing that to ask any more would certainly be under-bid by other applicants. Ignoring the possibility of leaving the market, which is the case if neighbouring opportunities offer similar prospects, to lose the opportunity for work means no income, or certain starvation. In bidding for work, each worker will consider the one in three chance of being successful and the two in three prospect of starvation. The winning applicant will be the one who bids less than \$5. and the amount by which the winning bid falls short of a reasonable level would appear to have no limit, as any particular bid will leave two others in an incomparably worse position.

Each worker who accepts employment at a wage of less than \$5 contributes data to positive knowledge of the market price of wages. If the five available jobs are filled at \$4-50, the market will recognise this as the market price and the other eighty five jobs will adjust down to that level *as a maximum*. The downward spiral actually returns increasing profits to employers. Apart from the efficient operation of the market, there is no reason for wages to plummet. Within economic theory no reason for wages to be sustained at any level given suppliers willing (free but desperate) to undercut each other. Wages therefore do not find equilibrium at their cost in a free market. Perhaps equilibrium would reach subsistence once sufficient workers had left the market. Ehrlich (1968) suggested that widespread starvation would provide such correction to the world before the end of the twentieth century, following the Malthusian model. The rising desperation of workers in the face of rising profits to employers and landlords would appear to be fertile grounds for political reaction.

The rise of the labour movement through the nineteenth century is an example of this type of political reaction against property power. Likewise, the relative demise of incomes for employed persons that has become apparent in the last two decades may be the result of the consolidation of the political power of the non-labour sectors of society. The erosion in this part of the century of an opposing credible theoretical

positions would appear linked to this power shift and supports Raffalovich's conclusions.

Because of these difficulties, confidence that a subsistence wage would naturally result from the *laissez-faire* operation of Ricardo's rent theory was probably naive, and its failure should have been obvious to Ricardo. His rejoinder to this observation would most probably have been that the misery of the working classes was a result of over-population, a belief that has continued to the present day.

While this may be a practical behavioural observation, it is not without curious ethical complications. If a community, through population increase and hence competition for jobs, found that wages were falling, then it would be reasonable to conclude that there existed an over-population problem. However, Ricardian theory recognises that the greater competition for land resources and jobs actually means that returns to land would have increased, while returns to labour fell. Hence, material welfare per capita could easily be rising while wages are falling due to the increased proportion of the total product flowing to land¹¹⁶. The plight of labour would not necessarily improve with greater labour productivity as the past thirty years has demonstrated, and in fact could easily find workers toiling more for wages that would ultimately be the result of the political power imbalance between them and property.

In the absence of a frontier therefore, the wages line is set as a result of a political/economic balance between land and non-land factors. In practice this hinges on some alternative to reliance on the private rental market, or even the private labour market. Public welfare, such as the Poor Laws, the ancient commons and even criminal behaviour, such as those actions in Ricardo's time that earned transportation to the colonies, are all examples of these alternatives. (Esping-Anderson 1996) studied the necessity for societies to provide an extra-market reference for wages and used the notion of de-commodification by which they meant "*when a service is rendered as a matter of right, and a person can maintain a livelihood without reliance on the market*" (p.22). While their analysis focused on the behaviour of public welfare, it recognised that wage levels are necessarily grounded on factors that are outside of the market.

The success of the colonies and new nations (especially George's own USA) is in no small part related to the fact that small populations operating within extensive rich

¹¹⁶Schumacher took this notion further when he dwelt on *man as producer and man as consumer* (Schumacher 1974). His observation was that in much of our economic theory it is generally ignored that it is the same people collectively who consume goods as produce them. Applying this to the effects of population, not only do the producers in a rising population have to pay more rent, but as consumers they are more numerous, and will generate greater aggregate demand, thereby forcing prices up. This means that the working person, regardless of levels of productivity, will earn less and pay more as a result of population pressure - not as a result of a necessary scarcity of goods and services, but simply because of the wedge of increased rents that separate man as producer from man as consumer.

lands enjoy incomes for the occupier considerably above subsistence and the resulting wealth has been in no small part responsible for their economic success. Conversely, the enclosure of the commons enabled working wages to be pushed down to objectively sub-subsistence levels around the end of the eighteenth century in England, despite otherwise robust national economic conditions¹¹⁷. Charles presented data on the nexus between private rent taking, taxation and wages over the period from the fourteenth century to the present to illustrate this point that has been made in many other places (Charles 1991). Harrison has also related recent major events in economics to the significance of land, leading him to a similar conclusion (Harrison 1983).

Today, the notion of subsistence is implicit in the notion of normal profit, which is at the foundation of perfect market theory. At equilibrium, prices in a perfect market are sufficient to cover the costs of production plus normal profit. The costs of production includes normal labour costs, which will lead back to some notion of a culturally relative level of adequate material welfare. Likewise, normal profits to shareholders are those that result in stable real equity values, again analogous to the notion of subsistence, where that term implies capital maintenance. It is therefore apparent why Ricardo's rent theory is closely associated with perfect competition.

Ricardo's rent theory is therefore of great importance in understanding the mechanisms that set wages levels. It would appear that the transition from a frontier situation to an enclosed one signals a subtle yet profound political/economic transformation. A free frontier maximises wages levels, whereas a closed frontier immediately establishes land property as the key economic power base. Economic power tends to translate into political power (Lenski 1966). It has been met historically by the organisation of labour, at least since the eighteenth century. The extent of political democracy has been empirically connected with the behaviour of property-income share, along with the degree of industrialisation (Raffalovich, Cooper, and Akard 1995). Assuming that industrialisation may run parallel to the formation of labour associations, the political significance of organised labour would appear implicitly connected as an explanation of variations in property income share.

13.2 OTHER SOURCES OF ECONOMIC RENTS

The discussion to this point may appear to suggest that land rents are the only systematic form for economic rents in the economy, however, this is not the case. While market theory may appear to eliminate all other types of rent in the long term, this is not the case in either theory or practice. This next section attempts to enumerate some of the other major mechanisms that generate economic rents, to demonstrate how

¹¹⁷see (Rogers 1884/1949)

they may be related to Ricardian land rent theory and locate the subsequent rent-centred approach within economics. The non-land sources of economic rents that will be considered are the following:

- Differing labour productivities (better workers)
- Differing technology (better machines)
- Economies of scale
- Random market opportunities
- Systematic market opportunities (monopolies)
- Spatial market anomalies
- Variations in local wage rates
- Financial (debt leverage and financial management) efficiency
- Temporal anomalies

It will be argued that the great majority of these are naturally transient, though they tend to become perennial in practice. This transition will be seen to be the result of a change from natural to what will be called political economic rents.

13.2.1 Economic Rents Accruing to Labour Productivity

In the same way that various grades of land attract economic rents, different individuals are capable of widely varied productivities. This can be inserted into a relationship similar to Ricardo's rent theory. Although an apparent cause of these disparities could be education and training, the most spectacular wage rents do not appear to be related to learned skill. Actors, musicians, inventors and entrepreneurial stars often use common skills to achieve uncommon outcomes. Since education and training can be interpreted as a form of capital investment, that part of labour productivity that is due to an educational investment is better recognised as a return on that investment and not strictly speaking an economic rent at all. There is some evidence that education can be used to produce inordinate income gaps between skill levels¹¹⁸, but this may be better interpreted as a form of monopolistic trend¹¹⁹ and will not be further investigated in this study.

Likewise, what is being considered here is not income differences due to different levels of responsibility. An architect and a carpenter are both engaged in same building, in the way that a general and a foot soldier are both fighting the same battle, but the architect and the general undertake considerably more responsibility and

¹¹⁸(Davis 1999) noted the fact that that between 1979 and 1994 college graduate incomes rose by 5 percent but high school graduate income fell by 20 percent

¹¹⁹Industrial relations theory emphasises the restriction of education and training opportunities as a strategy for maintaining higher wages (Dabscheck, 1981).

warrant greater reward. The differential distribution of rewards as a function of responsibility does not appear to have ever been seriously challenged. While the Medievals tended to use it as a given, it appears to have a higher gradient in capitalist societies and, at least theoretically, a lower gradient in socialist societies. In this thesis it will be accepted as a given, however even within different occupations and levels of responsibilities, different personal abilities will be apparent. Some architects are better than others.

Despite the amount of attention that seems to have been devoted to understanding and replicating outstanding personal success, it is not evident that outstanding success is capable of being learned. This is not to say that education is not useful, only that a significant economic rent is not available from it. Both the Beatles and Bing Crosby probably studied music, but their incomes were disproportionate to the value of the training that they received, or its return to many of their equally musical contemporaries.

The additional earnings of highly productive individuals is often referred to as monopolistic; Elvis Presley had a monopoly on his voice, but he did not have a monopoly on singing training, or the human singing voice. This parallels the way that land is monopolistic¹²⁰, while it is available in abundance, its productivity is particular.

It is difficult to categorise the sources of these human rents as they often overlap various characteristics, and their existence is highly individual and sometimes transient, however the following general observations appear to be reasonable:

- 1) They are usually serendipities
- 2) They often relate to monopolistic rights to sought after products (e.g. artistic excellence)
- 3) They are sometimes necessary in order to maintain wage stability for others

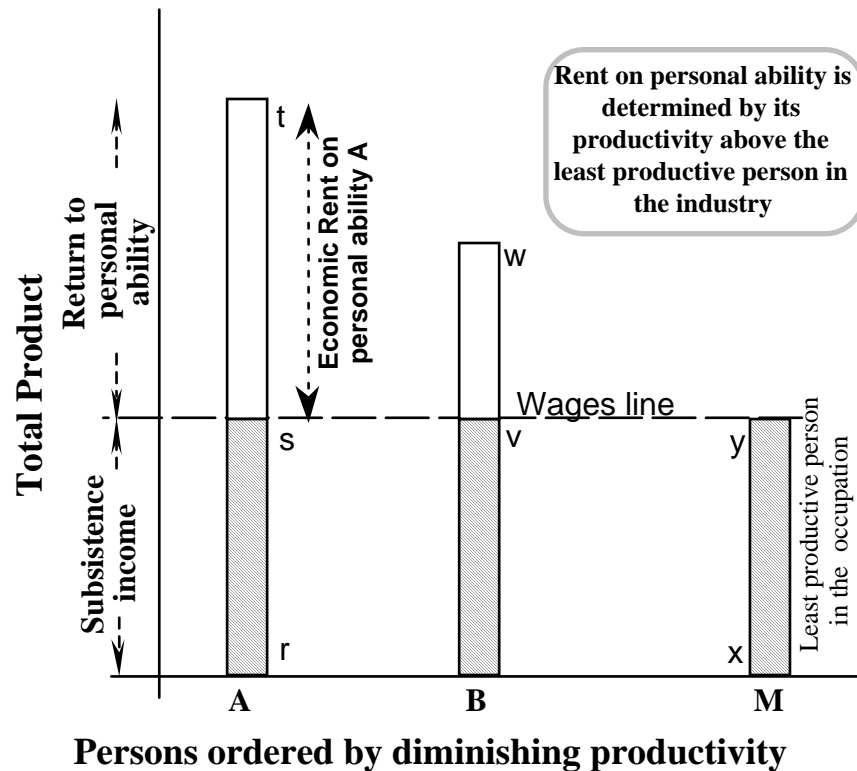
The first quality is uncontentious, and not particularly significant, apart from making them random benign occurrences and therefore beyond the need for general attention. When qualities (1) and (2) are combined however, what emerges is something that resembles land. Extraordinary personal ability is like title to a unique and unproduced productive resource. The major difference is the obvious connection between the resource and the person; unlike land, personal ability is naturally owned. The question of how this personal property is priced is not necessarily resolved, however its determination would appear to follow similar considerations to land property.

Where a personal ability means that a person is capable of out-producing his fellows, even though he may be able to charge less per unit of his produce in order to earn a

¹²⁰This notion was first explicitly stated by Adam Smith

reasonable income, to do so would mean that others in the same occupation may be priced out of being able to provide for themselves. This is illustrated in the Exhibit 13.1, that extends Ricardian rent theory from land into personal ability.

Exhibit 13.1 Rents of Personal Abilities



The marginal situation (m) refers to the base income to the least productive person considered viable in a particular occupation and must be a social decision. It may change with changing circumstances. It will also be influenced by technology and other factors.

All else equal, personal abilities are relatively stable, even if not exploited due to the limitations of an individual's circumstances or personal choices. They are socially determined through demand. They may be developed by training, realised through appropriate work choices, and affected by accidental events, but in all these things, they resemble the economic qualities of the land factor.

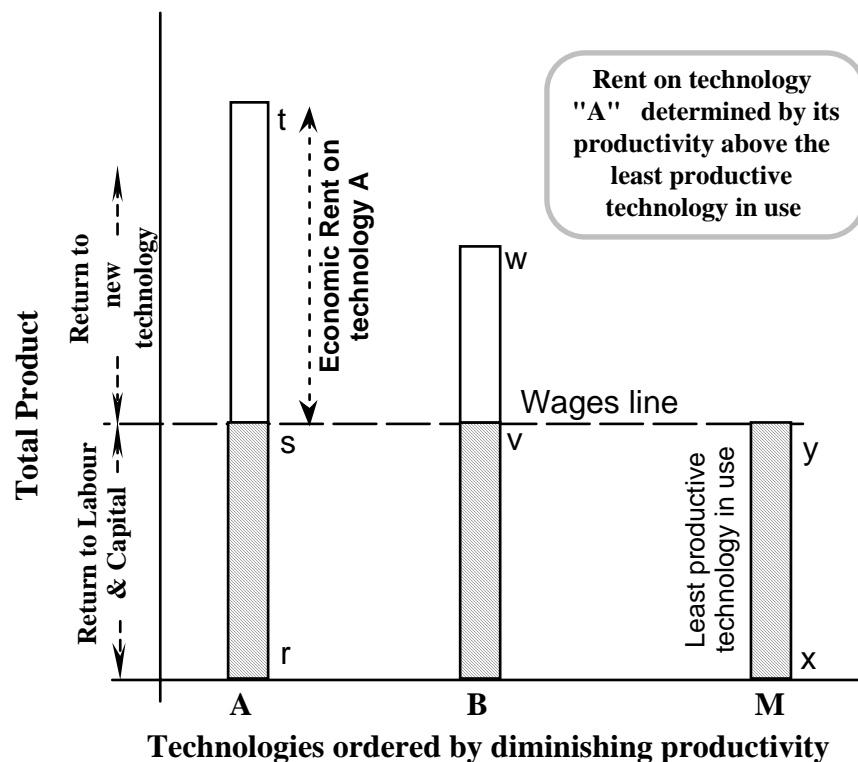
For those who would advocate the socialization of land through a comprehensive land tax, the socialization of super-marginal personal ability would appear to be a consistent policy. This is despite the offensiveness of such a policy due to its similarity to a partial enslavement of the talented to the state. On the other hand, Hercules

achieved his mythical fame precisely through applying his extraordinary abilities to the good of his fellows. The difference of course is between statist control and personal willing, and even here there is a parallel between personal ability and land¹²¹.

13.2.2 Economic rents from technology (Technology-related economic rents)

(Barlowe 1958) demonstrated the application of Ricardian rent theory to technology. He asserted that in a perfect market at equilibrium the least productive technology in use would return only a normal profit. This is illustrated in Exhibit 13.2, below. Newer technology would produce an economic rent on the basis of its higher productivity, and this would capitalise into a value for the technology that would be super-normal.

Exhibit 13.2 Rents on Technology Differentials



In an industry in which several technologies co-exist, the least productive technology in use sets the rent for the rest. Hence, in Exhibit 13.2, technologies A and

¹²¹This is evident to some degree in many customary peoples. Members of a tribe who have exceptional ability are expected to use it for the tribe. The appreciation of the tribe may appear to be a form of remuneration, but it is more correctly understood as a reciprocation of gifts. Customary tenure is intelligible as a community ethic regarding land that makes common use virtuous. Islamic theory is even more explicit. The Moslem is required to personally serve his God, which includes alms giving and other social acts. Islamic property rights are contingent on using land assets in like service. Hence, the theological ethic is the same for both natural and conventional property.

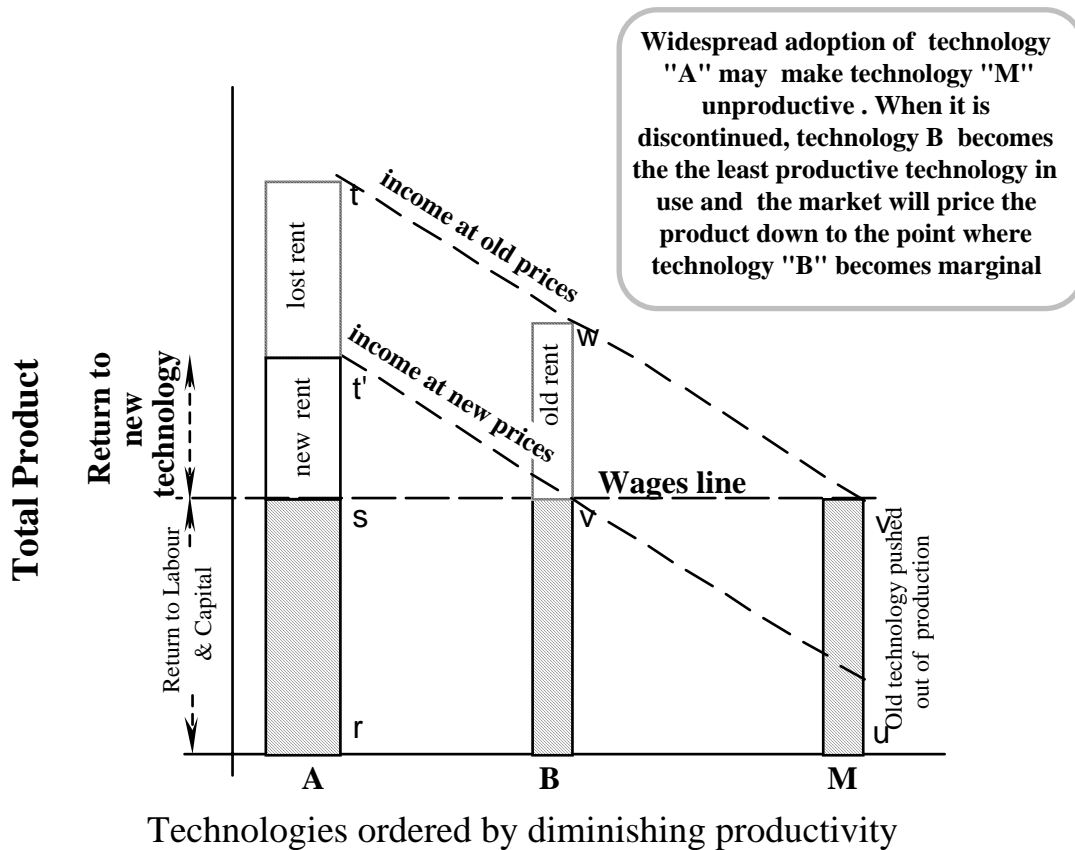
B return economic rents of s-t and v-w respectively. One advantage of this rent process is that it tends to provide a temporary, natural fund for financing new technology and its research.

The parallel between this process and land is obvious, though its similarity should not be overstated. It is probably more correct to consider economic rents in land and economic rents from technology as analogous¹²². Land tends to be occupied starting from the most productive, so the most recent occupation is the least productive. Technology tends to be taken up in reverse order, the most recent innovation is the most productive. This means that at least initially, new technology does not affect returns to the existing technologies. When it does, it is the result of the new technology being employed so widely and producing such efficiencies that the sale price of the product falls, pushing the least productive technology out of production.

New technology is assumed to be more productive, hence it will be capable of producing more product for the same or lower cost. An incentive will exist in the industry to adopt the more profitable technology and it will eventually displace the older methods. The usual presentation of the effect of new technology is a downward shift in the supply function, however in a well informed market, the demand function will also shift downwards as a result of two factors. Firstly, the community will not necessarily expand its physical demand for commodities in an unbounded fashion. Regardless of how low the price of ice cream falls, there will be a point beyond which physical demand cannot be pushed. Secondly, market theory assumes complete knowledge. As the market learns that production costs have fallen, it will be less willing to pay as much as when production costs were high.

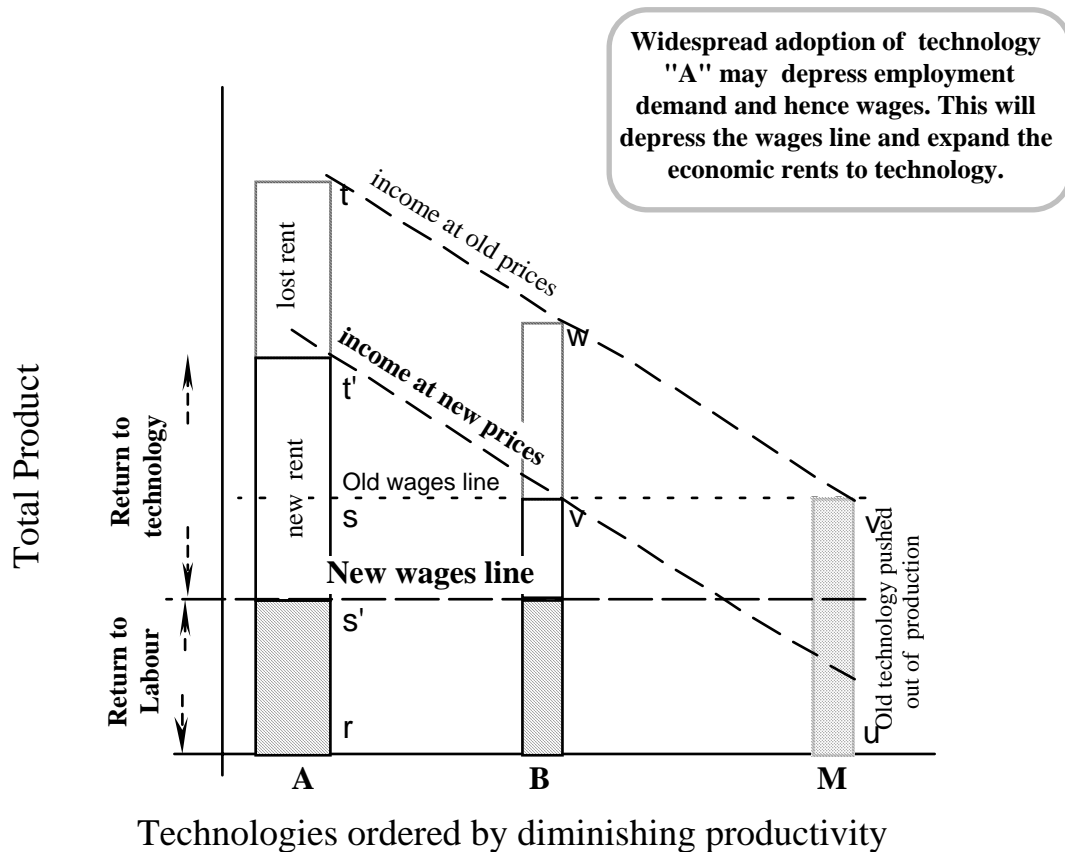
The result will be that the new methods will further displace the old and prices will fall making old methods unprofitable. Once the old methods have been eliminated, the rent will also be eliminated. Hence, although technology appears to produce a similar pattern of rents to land, its long term behaviour is the exact opposite of land rents, the former diminishes in the long term whereas the latter appreciates. This is shown in the Exhibit 13.3.

¹²²In philosophy an analogy refers two things *that are like, but more unlike than like*.

Exhibit 13.3. Rents as Old Technology is Retired

This diagram assumes a near perfect market where the new technology does not introduce monopoly opportunities. The realities are somewhat more complicated. New technology usually involves a reduction in the labour to produce a given output volume. Assuming an inelastic physical demand, this translates into lower employment. If productivity improvement is widespread, employment will fall, and if wages are subject to market forces, they will fall. The result will be a fall in the wages line and a maintenance of the economic rents to technology. This is what has been popularly associated with the industrial revolution. It is illustrated in Exhibit 13.4.

Exhibit 13.4 Technology Rents and Unemployment



Technologies ordered by diminishing productivity

Exhibit 13.4 shows that as a result of reduced demand for labour, wages have fallen from s to s' which increases the economic rent attracted by technology "A" to $s'-t'$. This process is analogous to Ricardian rent theory on land in the case of an expanding population. The similarity is that over time the return to labour diminishes. The difference is that population does not need to change and the effect is the result of more productivity in the case of technology, rather than less in the case of land.

Similar to behaviour of land, the result is connected with the politics of the relationship between labour and the owners of technology. Wages are not pushed down as a result of a lower cost of labour (in the sense of the cost of maintaining the labour unit), but as the result of labour's diminished negotiating power.

New technology has the capacity to provide for the physical requirements of society with a reduced labour input. If labour's inferior bargaining power maintains the low level of wages, the return to technology may be maintained indefinitely. This goes some distance to explaining why the owners of technology, or productive assets in general, can reliably expect a return that does not depreciate in line with the value of the productive assets. The explanation is in terms of the power relationship between labour and the owners of capital.

In Exhibit 13.4, it may cease to be necessary for an inferior technology to be in operation to sustain economic rents for the most productive technology. There is an economic incentive to retire the inefficient technology and the community as a whole must be better off with the widespread adoption of the best technology available, however, in the absence of other social balances it may result in dysfunctional outcomes. If it results in widespread unemployment and rent-taking it will be socially inappropriate and lead to polarization in wealth and incomes between labour and the owners of technology. This is partially behind Schumacher's (1974) rationale for medium technology for emerging societies.

Title to technology-related economic rents is not a major economic concern because it is normally assumed that the optimum technology is available to all producers in a perfect market. In the short term, the rent can be validated in terms of the necessity of funding technology research and commissioning. However there is no necessary connection between the magnitude and persistence of the rents and a normal return on the venture capital required for development, even adjusting for risk. Western thought generally is comfortable with the notion of these technology-related rents being freely and totally available as an incentive for invention. While this position is behaviourally effective, there are many cases where the inventors of key technologies have not enjoyed the rents they have produced. In addition, Veblen argued that innovation was in fact a social function, with the innovator drawing on the accumulated knowledge of society (O'Hara 1995). Veblen's notion of social capital does not have to be wholly embraced in order to recognise that it is an instrumental material cause of innovation, giving the latter a social dimension. In this light, title to innovation is distributed, though the final balance of interests is beyond the scope of this study.

13.2.3 Economic Rents from scale of operation (Volume-related economic rents)

Economies of scale are not contentious. The fact of continual corporate growth, merger and acquisition and the apparent economic benefits of these strategies can only be explained in terms of the expectation that increased corporate size is more economically efficient. At the level of the firm, conventional analysis of costs by dissection into fixed and variable for such purposes as break even analysis¹²³ implicitly recognises the additional profits that come from larger volumes. This means that super-normal profits result from sales above a specific level.

The fact of economies of scale has been dealt with earlier in terms of the problem that it creates for the marginalist foundations to supply theory. Economies of scale mean that the actual supply curve is downward sloping, the reverse gradient to its popular presentation. The significance for economic rent theory is that for any one

¹²³See (Wilson and Keers 1990)

organisation, it is actually impossible to set a unique labour-based objective price on its inventory because the cost of supply is a function of the volume of sales. Volume-related economic rent is a complex function of the behaviour of costs at various sales volumes, however it will be illustrated using the simplified situation shown in Exhibit 13.5.

Exhibit 13.5 shows profits for a notional product line under the assumptions for costs and sale price that are adopted in break even analysis. Costs are assumed to be capable of being separated into costs that vary in proportion to sales and those that are fixed regardless of turnover. For large variations in scale fixed costs will also move upwards, while variable costs may even decrease. Hence this dissection of costs is practical for only a small range of actual sales volumes, often referred to as the relevant range. More accurate models are possible if the behaviour of specific costs can be formulated as a function of sales volume, however they lead to the same general conclusion and may be ignored for the purposes of this illustration,.

Exhibit 13.5 Rents from Economies of Scale

Sale Price	\$11.00 each
Variable Costs	\$6.00 each
Fixed Costs	\$100,000
Normal Profit	\$150,000

Scale-Productivity Grading	Sales	Profit	Normal Price
10	10,000	(\$50,000)	\$31.00
9	20,000	\$0	\$18.50
8	30,000	\$50,000	\$14.33
7	40,000	\$100,000	\$12.25
6	50,000	\$150,000	\$11.00
5	60,000	\$200,000	\$10.17
4	70,000	\$250,000	\$9.57
3	80,000	\$300,000	\$9.13
2	90,000	\$350,000	\$8.78
1	100,000	\$400,000	\$8.50

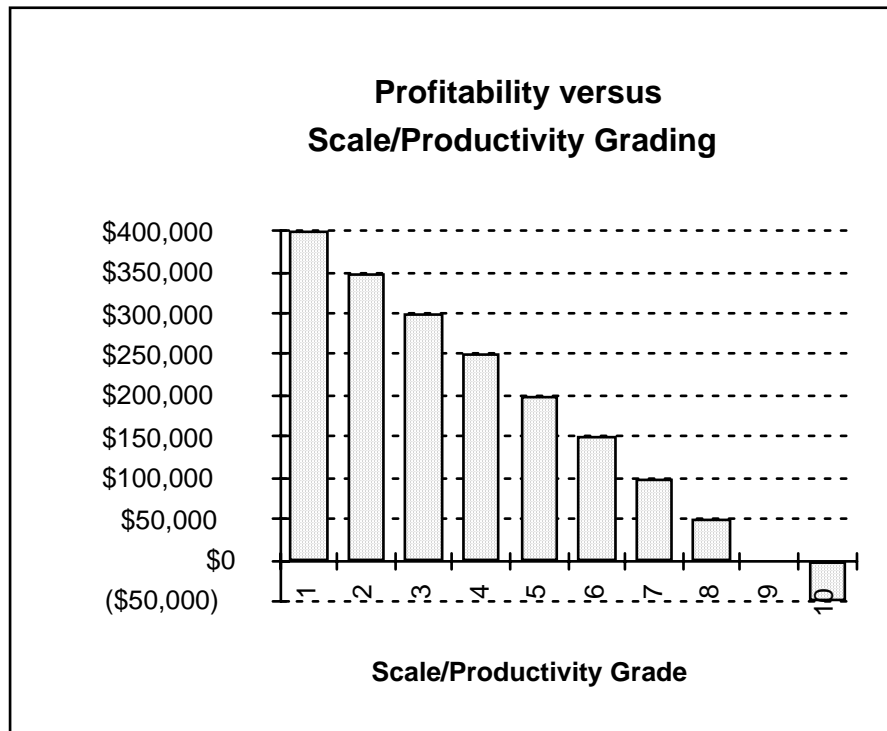
The conventional application of cost management analysis would consider the impacts of varied sales volumes on profit. If it is assumed that normal profit for the assets devoted to that product line was \$150,000, then a cost based price could also be

computed for various volumes as shown in the third column. If the line was currently moving a volume of 50,000 units, the price would contain no economic rent. If volume increased to 70,000 units, the average cost would fall to \$9.57, i.e. the line would generate an economic rent of \$1.43 per unit. On the other hand if sales fell to 30,000 units it would rise to \$14.33. Prices are assumed to find equilibrium at the average cost, though this would be impossible to resolve if volumes varied. If there are several producers supplying to the market with similar production parameters but differing volumes, the price could not be resolved in this way.

For otherwise similar organisations supplying to a single market, the price would be set by the organisation that moved the smallest volume and the larger more efficient organisations will enjoy economic rents due to their scale. While too much should not be made of the simple mathematics of break even analysis, the overall fact of increased profitability due to scale is well accepted. Continuing the example. if the eight levels of profitability are ranked by scale-efficiency, rather than simply sales, the limitations of the fixed/variable cost dissection may be by-passed.

In the example, as shown also in Exhibit 13.6, scale/productivity grade 6 would return marginal profit (at a sales volume of 50,000 units in the numerical example). Because this is the least profitable, there will be a tendency for these smaller operators to eventually discontinue operation, either by closing up or selling out to the larger operators. Similar to the technology case, when this happens competition should cause the prices to be driven down so that the least productive again becomes only marginally profitable.

Exhibit 13.6 Profitability by Scale of Operation



The likelihood of prices responding to the disappearance of the least profitable operator may be reasonable in the case of perfect market knowledge, but the absence of this ambitious assumption must also be recognised. If the least profitable producer disappears, then it may be assumed that their volume will be distributed amongst the remaining producers, further improving their profitability. Obviously, taking over the failing producer may be expected to return the greatest benefits, making a take-over by one of the surviving firms a likely strategy¹²⁴. This may produce a rational take-over price that is above the apparent value of the firm, however this issue is not further explored here.

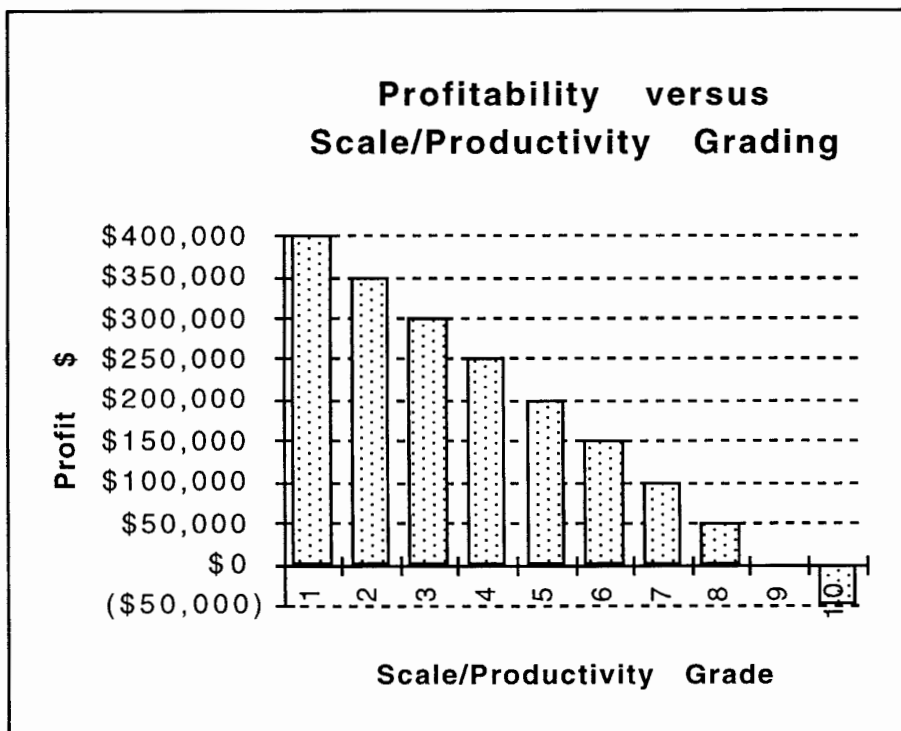
13.2.4 Economic Rents from random market opportunities

The reality of imperfect markets means that there will be opportunities for gain arising from non-systematic variations in prices. Some persons may be more willing or able to act on these situations and turn them into income. This is an example of Aristotle's unnatural exchange, though often a benign one. For on a small scale it will have negligible negative impact on the society and will have the effect of improving

¹²⁴In the example, the purchase of one company turning over 50,000 units by another of the same size would increase the latter's profit by \$250,000, or 167%, assuming the sales volume was transferred. This may easily make the company more valuable to the purchaser than to its shareholders as a going concern even if it had no other reason for winding up.

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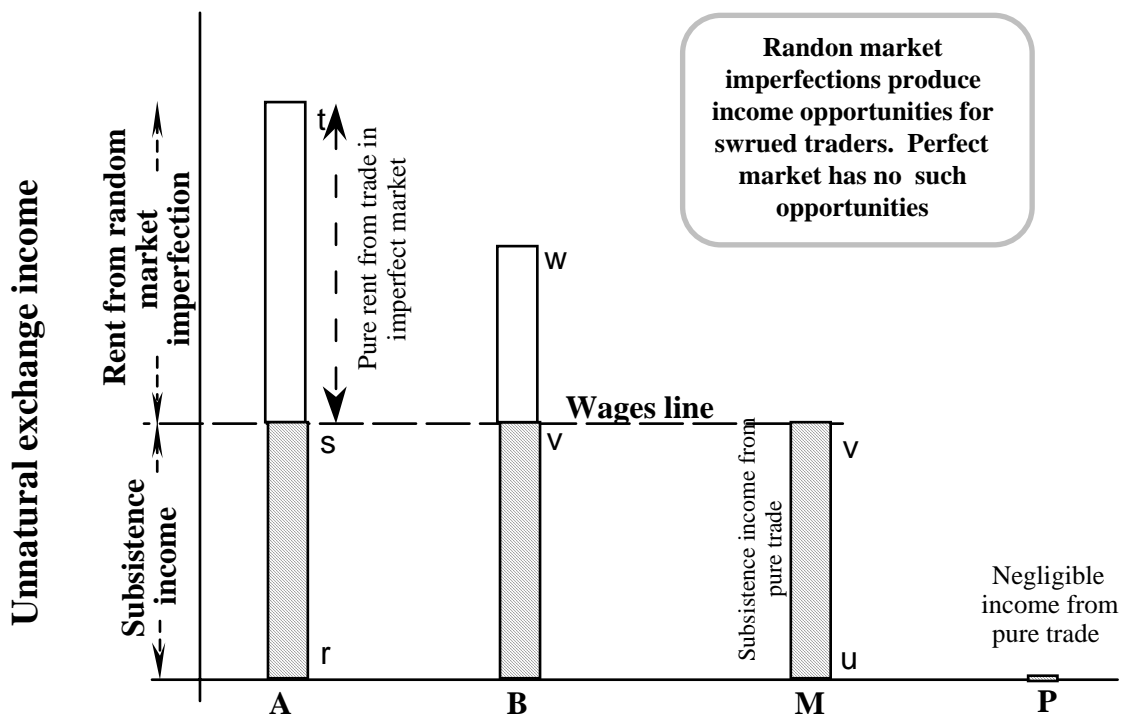
Exhibit 13.6 Profitability by Scale of Operation



market efficiency through the information and balancing aspects of economic agents acting on the anomalies. A perfect market would have no random opportunities.

The effort expended by economic actors who seek to exploit these opportunities may be recognised as valid labour and their effort as contributing to the common good through its improvement of the overall market. This is shown in Exhibit 13.7, which shows the possibilities of incomes at various intensities of pricing anomalies¹²⁵. In a perfect market, **P**, there are negligible opportunities for income through unnatural exchange because the market is mobile, free and fully informed. At point **M** there are sufficient anomalies to provide an income for someone engaged in trade full time. This would be in addition to trade expenses such as transport, wastage, advertising and risk¹²⁶.

Exhibit 13.7 Random Market Anomaly Rents



Random Pricing Anomalies ordered by diminishing frequency

¹²⁵By intensity of pricing anomalies is meant the frequency and size of available opportunities in given societies.

¹²⁶The Franciscan Schoolman Alexander of Hales, writing before St. Thomas Aquinas, was perhaps the first to distinguish the licit occupation of the merchant, which this discussion adopts. When a merchant acts to realise his own material needs, or those of the poor, his use of what in Aristotelian terms is strictly unnatural exchange is licit. Alexander also listed a number of heads for compensation that the merchant may justly charge for similar to the items listed here (Langholm, 1992, pp.130-131).

At levels of pricing anomalies **A** and **B**, there are opportunities for economic rent in addition to true wages. It should be noted that the vertical axis is no longer productivity, but income possibility. The income is not the result of the supply of a good or service which throws into doubt the contribution of pure trade to the common good. The usual arguments in support of the contribution of trade to the common good are as follows:

- 1) By linking supply and demand, trade provides a necessary social function
- 2) Trade reduces market anomalies.
- 3) Because all the transactions are free and Pareto improving, the outcome is beneficial

The first reason is valid for that set of merchant activities that can be classified under labour and risk heads. These include transport, advertising (of the informative variety), storage wastage coverage and risk compensation¹²⁷. None of these are strictly speaking the pure income that flows from the pricing anomalies found in a randomly imperfect market. While trade employing unnatural exchange may achieve the end referred in (1) it is not necessary in order to achieve that end. In a fully informed market there will be spatial differences in price, discounts for volume purchase and other apparent anomalies, but these will only be great enough to pay the costs of transport, retailing labour and risk.

The second reason may cover more than one process. Merchants may succeed in transferring sufficient goods to reduce or eliminate the market anomalies through an increase in the number of merchants employed in trade. The marginal point would actually occur when the income from trade only just covered the labour costs and risk involved in the trade. The question is whether the anomalies would actually be eliminated or merely reduced to the point where they only just covered the transport costs involved. This would again appear to suggest that the limiting case is the elimination of market anomalies. Perhaps in practice there is a social need to support some merchants in pure trade income. This would be the case in order to support 'scouting' for opportunities by merchants. Resolution of this uncertainty is not pursued in this study.

The third reason is illusory. The transactions are made in partial ignorance which the merchant exploits. It can be argued that ignorance limits freedom; if the consumer and supplier knew of each other's situation they would be unlikely bother with the merchant as an intermediary, beyond the latter's valid role in transport etc. As it is, neither the

¹²⁷Meikle (1995) noted that Aristotle recognised that vicious unnatural exchange always rode on some form of licit economic activity. Hence it comes as no surprise that much of a merchant's activity is licit. The illicit component manifests when incomes are taken beyond the limits set by these activities. They may attach to any licit occupation, e.g. the professions.

producer nor the eventual owner have the real opportunity to decide on whom to trade with and for what price. If the market were perfect, the producer may enjoy a slightly higher price and the consumer a lower one, which would appear to be the superior outcome leaving the merchant to find employment in a genuinely productive activity.

The occurrence of random market anomalies may also be due to the difficulty of costing produced goods. Because of the range of technologies, scales, personal abilities and raw materials involved in production it is attractive to conclude that it is impossible to know with precision the marginal price that an efficient market should allocate.

In one sense this may be a valid conclusion, but for any specific producer it cannot be convincing. Contemporary financial management and accounting provides producers with a high level of intelligence regarding their costs of production. This is evident in the fine margins that many producers can maintain and remain profitable. At the simplest level, the profit and loss statement is a precise summary of production costs. With this level of precision it is impossible to assert that a producer cannot know the marginal price of his goods.

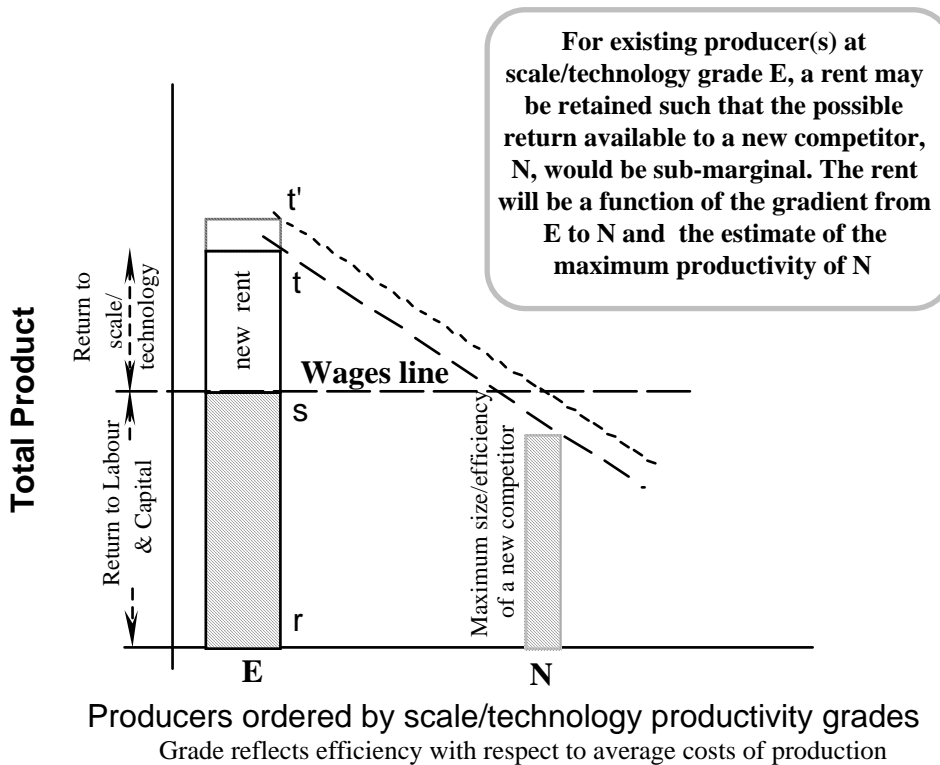
As markets mature, market imperfections will diminish and the opportunities and their economic rents will contract. At best, random market opportunities can be agglomerated to include both productive aspects, such as transport and non-productive aspects which are pure rents. In this way some productivity increment may be honoured, while recognising that the activity includes a component of pure rent.

13.2.5 Economic Rents from Systematic Market Opportunities (Monopoly)

Random Pricing anomalies constitute a common domain of opportunity for income from unnatural exchange that will also respond to economies of scale. Several mechanisms may operate to crystallise these anomalies into permanent economic rents for specific agents. These will be explored in connection with scale and technology rents.

As the economic size of producers increases, it can produce a barrier to competition. A similar barrier can be produced when new technology is expensive and protected by design rights. Because the expense involved in the development of new technology may be expected to be more easily afforded by larger producers, the two effects may be found operating in concert. If an industry is only viable when operated using expensive high technology on a large scale, entry will be limited to competitors who can enter at that level of operation. This is shown in Exhibit 13.8.

Exhibit 13.8 Stable Rents from Competition Exclusion Thresholds



In Exhibit 13.8 existing producers can afford to retain economic rent $s-t$ so long as it does not exceed the level necessary to exclude new competition that is expected to have a productive efficiency of N . If a price rise raised the rent to $s-t'$ a competitor would be marginally viable at N . The fact that new competition will impact on the distribution of volume efficiencies further complicates this strategy. The most likely new competitors will be well funded innovators who can introduce a significant technology efficiency and resist being bought out by the existing operators. The strategies will not be further explored, beyond recognising that they comprise part of a mechanism for maintaining perennial economic rents even in the absence of an intentional strategy aimed at producing a monopoly situation. More than one producer can co-exist at efficiency grade E , so long as they are not motivated to increase their market share, which also results in moderately stable economic rents. This situation appears to better describe the corporate landscape as it exists in practice.

A successful exploiter of random market opportunities may achieve a similar outcome by developing a similar scale of operation, though it would be difficult to maintain in a reasonable efficient market. In addition to practical barriers of productive scale and technology, political barriers may be also erected and these can be funded from part of the subsequent economic rent. This latter process was described by (Bhagwati 1982) and may include several legally supported Western institutions, such

as political lobbying. Despite this, perennial retention of economic rents is popularly perceived as anti-social¹²⁸ and the object of anti-trust and trade practice legislation aimed at its control.

Regardless of the intention, the economic rents are the result of what is in fact a stable market imperfection and produces a monopoly, even in the absence of additional political interventions. Despite possibly originating in productive efficiencies, the economic rent is no longer the result of a productivity increment but chronic market failure.

Given that organisations maintaining optimum scale/technology productivities may retain an economic rent even in the absence of inferior technology, its relationship to land rents can be further explored. If the owners of productive technology are earning robust economic rents as a result of their ability to provide for the physical needs of society with only a small labour input, they will be earning super-normal profits. If the owners of technology rent their factory site, then a *widespread* productivity increase will facilitate land rental increases to the point where profits on productive capital are normalised.

Land is able to extract this rental increment because of its necessity in the production process. The capture of the productivity increment may be shared between the various places land exhibits in the production process, such as mining royalties for raw materials or as rentals on locations for production and sale. Although also necessary for production, labour does not have the bargaining power because the labourer must earn an income to survive, whereas land can be held out of production without cost¹²⁹.

This means that industrial and commercial rents will expand to absorb general productivity increases. Hence, even if capital is able to maintain its superiority over labour, it will not be able to fend off the erosion of its economic position by land. This provides a more complete interpretation of the plight of labour and capital through industrial revolution. (Harrison 1983) quipped that *"if one were to assemble the 100 richest men in nineteenth century England, it would be reasonable to conclude that the industrial revolution had never happened."* The landowners were not displaced by the capitalists, though the latter group had the unfortunate fate of becoming the former's economic henchmen against labour.

¹²⁸Economic rents are fundamentally supported by two pillars. The first is strong effective demand and the second is a market placement that enables the supplier to arbitrarily chose which part of the demand function to operated on. Economic rents are therefore tied intimately to demand based pricing that has been shown to be negatively viewed.

¹²⁹ Apparent costs to hold land out of production include land tax and finance costs. The former is a rental share and the latter is not strictly speaking a part of the land asset, but pertains to the purchase decision. One of the reasons put in favour of land tax is that it puts a cost on holding land out of production.

This is not to say that returns to capital are not significant, or that they have not been allowed to retain some amount of economic rent; the real growth in equities is proof of that. Productive corporations also rely in part on land assets to support their profitability, which makes simple observations of equity returns impossible as a genuine contrast against land rents. Various studies have suggested that equities contain widely varied proportions of corporate land and the actual amount may vary with time and location. The proportion not important, it may be as high as 40%, but the important conclusion is that land remains a dominant ultimate destination of economic rents derived from technology improvements.

Economic rents from systematic market imperfections should be eroded by competition, especially from new technologies resulting in falling prices. The speed of the erosion of economic rents is a function of various political and efficiency factors and also the fact that land rents will rise to absorb global productivity increases. Systematic market opportunities are situations where the marginal producers have been eliminated, but the prices have not fallen to eliminate the economic rents.

13.2.6 Economic Rents Accruing from Spatial Anomalies

Random market opportunities are most evident as spatial anomalies in price. An observant merchant will note locations where prices differ and buy where prices are low and sell where they are high. These are not the only random market opportunities, but they are the most easily recognised. Their operation is similar to random market opportunities and does not bear repeating. They may also become systematic, especially in the case of international trade where licences and other positive restrictions may grant effective monopolies to particular merchants.

13.2.7 Economic Rents from Spatial/Political Wage Anomalies

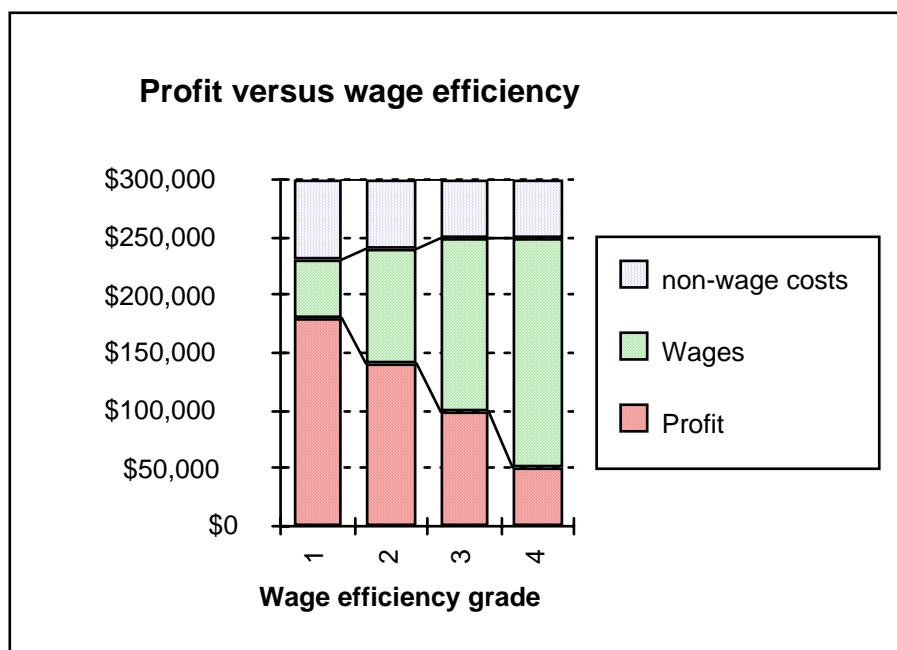
Prices find equilibrium partially in terms of local wage rates. In the absence of developed capacities to utilize low cost foreign labour, the feasibility of potential competing supply will be conditioned on local technology and industrial relations parameters (including wage rate). Amongst other things, effective demand may be expected to be a function of the level of disposable income (wages related), and the perceptions of the labour content of the good.

Goods produced outside the local economy present difficulties for market evaluation. Purchasers may be more critical of quality, but once this differential is assessed, they will have great difficulty assessing the cost content. This is because local purchasers do not have sufficient knowledge of foreign wages rates (beyond perhaps being '*cheap*'), or the complex set of differences in industrial relations, foreign exchange and taxation variables and logical costs. Access to foreign labour is also

limited by cultural, political and economic barriers that produces a significant entry hurdle for potential competing suppliers.

Globalization is partially made possible by the existence of corporate entities that are capable of relocating advanced productive technology so as to maximize the rents from wage anomalies. This does not increase the productive output, beyond possibly enabling production to more effectively exploit the higher quantity end of the demand function. Assuming similar technology is employed in communities with different industrial relations structures (wages, working hours, conditions etc.), the producer paying the highest wage rates will be marginally profitable, while the producer paying the lowest wages rates will earn an economic rent. The actual rent will depend on the proportion of low wages and will be offset by additional costs such as transport.

Exhibit 13.9 Rents from Wage Cost Anomalies



The example shown in Exhibit 13.9 shows a notional product value of \$300,000 that may be produced in one of four different locations with differing wage costs. Non-wage costs have been allowed to vary to reflect possible additional transport and logistical costs involved in production in distant locations. Assuming the location with wages efficiency of grade 3 is the most expensive wage regime used in production (possibly the community into which the products are sold), profits from production in this location would be normal (marginal) at about \$100,000. Wage efficiency grade 4 could not compete in the market but a similar producer in the same market but

producing in a foreign location with wage efficiency grade 1 would enjoy an economic rent of about \$80,000 despite higher transport and logistical costs.

A firm producing in a wages efficiency grade 3 area could increase profitability by moving the production facility to a more wage efficient location. Once production ceased in grade 3 locations prices could be expected to fall to the point where producers using grade 2 locations become marginal. As foreign production became the norm, it may be expected that local markets would have greater difficulty accurately pricing the goods leading to the possibility of permanent systematic market rents.

13.2.8 Economic Rents from Political Inter-occupational Wage Anomalies

Within an economy there can be inappropriate wages gradients between occupations and through organisational hierarchies. These can be thought of as political, in that they are maintained by differences in power between the respective groups.

The relationships between occupations may be conceived of as differing in skill and responsibility, both of which deserve different wages rewards. Dabscheck (1981) discussed the way that the remuneration to different occupations may be distorted through the use of various industrial strategies. Education and training opportunities, especially the control of apprenticeship opportunities have been used to produce artificial limitations in the supply of certain trades. Other controls such as compulsory unionism and control of union membership have a similar effect. These strategies are used as political levers between occupations that distort a just distribution of wages.

Wage anomalies between distinct occupations may be thought of as horizontal anomalies. Vertical anomalies are produced by inappropriate wage gradients between organisational levels within occupational groups. Senior management often has some control over the remuneration of the lower organisational levels, and therefore over the profile of the gradient of wages down an organisational hierarchy. This is a natural source of economic power that may be used to economise on the wage cost of an organisational unit by constraining remuneration to lower levels. The savings are then available as bonus income for upper management. The result is a vertical polarisation of incomes. The lowest levels within organisations are often controlled by industrial relations measures, controlling vertical anomalies to some extent, however lower management usually does not enjoy this sort of protection.

Horizontal wage anomalies may be viewed as a dysfunctional result of specific occupations attempting to obtain reasonable incomes, but unintentionally gaining at the expense of other occupational groups. Vertical anomalies are the result of the inappropriate use of power naturally found in the upper parts of organisational hierarchies. Both are ultimately political.

13.2.9 Economic Rents Accruing from Financial Efficiency

Financial management on the level of the firm involves strategies designed at more efficiently translating sales into profit. There are many topics within this general area but they have the common trait of being independent of actual production efficiency. They include issues such as capital funding, capital rationing, current account management and the strategic use of debt. It is not intended to review all of them, beyond observing that the strategic use of debt is probably the most important single issue. It may be asserted that profitability may be expanded through financial efficiency, the most commonly cited is the effect of positive debt leverage (Wilson and Keers 1990).

If a number of similar competing firms use different levels of debt leverage, and assuming positive leverage ¹³⁰, the more highly leveraged firms will earn an economic rent simply due to their use of debt. This could be shown graphically to produce a spectrum of rents similar to the other rents considered and the firm that uses the least debt may be expected to achieve only normal (marginal) profits. Also like other rents, it produces an incentive for firms to abandon the marginal position, which in this case means adopting a more leveraged position. The evidence appear to be that corporate use of debt has increased over recent years, however this may also be cyclic. Highly leveraged firms suffer most in recessions because of both the mechanisms of leverage and the fact that recessions are often periods of elevated interest rates This has the effect of periodically removing the most aggressive borrowers and spreading a sentiment of caution through the economy.

13.2.10 Economic Rents Accruing from Temporal Anomalies

Temporal anomalies exist as a result of price differences through time. The futures market operates on estimates of future price levels and incomes from futures trading depend on the alignment between the investor's estimate of price movements and the way the market actually runs. For the purposes of this discussion, it is sufficient to recognise that it is a form of unnatural exchange and operates identically to random market opportunities, except that the final outcome cannot be known in advance. Rents from temporal anomalies are also random and risky; futures markets are zero sum, i.e. the net result for the futures market is always necessarily zero net profit or loss.

Futures traders who use the market purely for hedging purposes may be more tolerant to loss outcomes because their goal is price certainty. Speculative trading does afford this comfort, but perhaps this may create a slight rent as a result of the differing

¹³⁰Positive leverage is the situation where debt interest rate is less than the unleveraged return on assets. (Rowland 1993) presented standard arguments why positive leverage may be reasonably expected.

psychologies found operating in the same market. This would be consistent with Commons' negotiational psychology and suggest rents arising purely from the differing psychologies within a market. It would validate the usefulness of brokers and agents, but otherwise resembles a special case of random market opportunity.

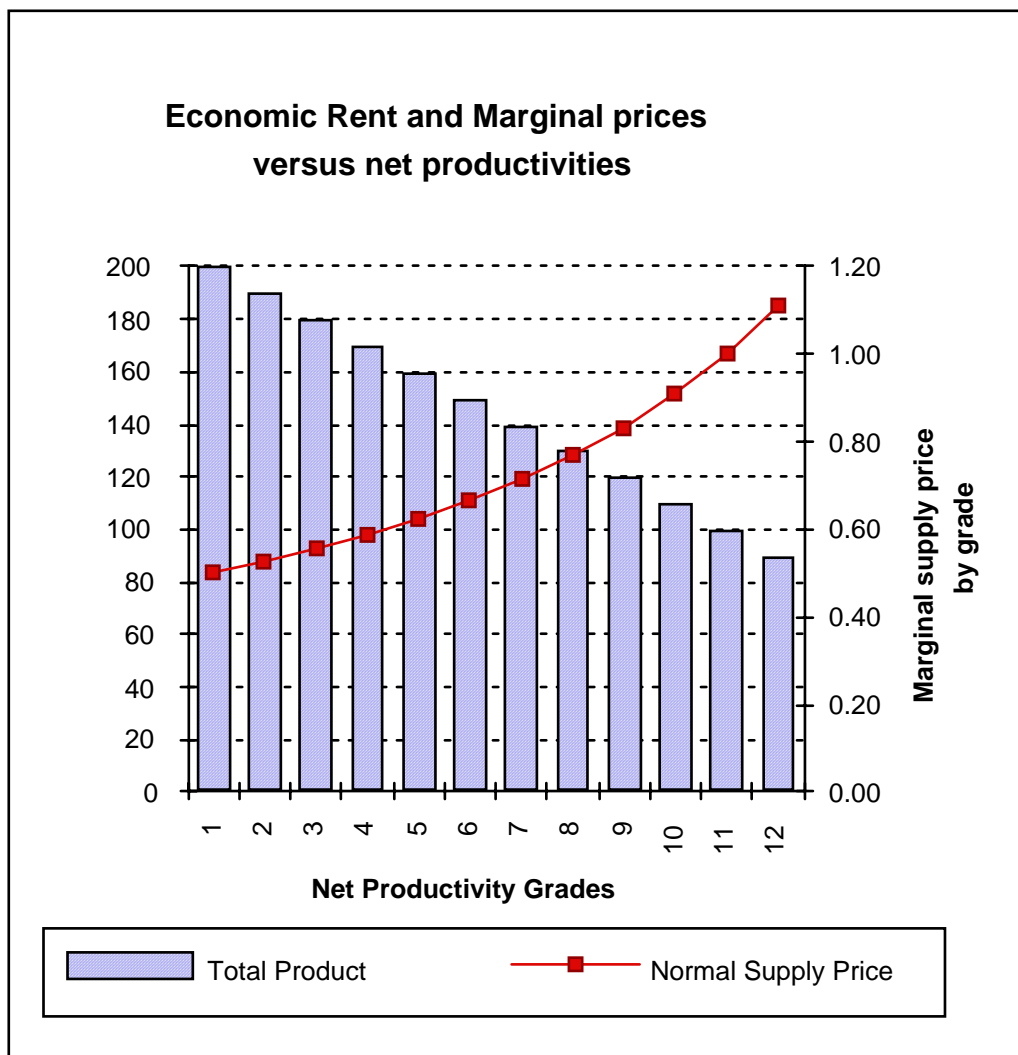
Exhibit 13.11 Summary of Economic Rents

Source	Nature	Marginal case	Comment	Long term	Relation to production/ demand
Land	Varied productivity due to site-specific physical & social factors	Free frontier; Otherwise rents set politically	Widespread & stable; includes all non-produced resources, e.g. radio bandwidth	Existence stable. Distribution volatile.	Rises with production and population
Labour	Serendipitous personal ability, eg: artists, inventors and entrepreneurs	Least productive worker in an industry	Undoubtedly private property but land-like; rights may be sold; surplus to basic needs	Random, stable for specific persons	Productive; highly individual demand
Technology	Superior technology is more efficient hence more productive	Price set by least productive technology in use	Promotes optimum technology; Is eroded as old technology falls out of use	Disappears as old technology discontinued	Rent will rise with demand if high demand holds old technology in production.
Economies of scale	Larger operating scale is usually more efficient.	Smallest operation in an industry	Promotes larger scales of operation; rents disappear as smaller players disappear;	Disappears as smaller producers discontinue production	Rent will rise with demand if high demand holds small producers in production.
Random Market opportunities	Random variations in prices;	Perfect market with full knowledge and mobility	Derived from unnatural exchange, not productive; income from exploiting market anomalies; encourages, but eroded by, market efficiency	Should disappear with better developed markets; Random	Does not contribute to production; random; may rise with demand
Systematic Market opportunities (monopoly)	Market opportunities that are maintained by the beneficiary;	Perfect market	Exploitive. May result from exogenous political factors or natural barriers produced by technology cost or the scale of the dominant organisations;	Politically determined and maintained	Does not contribute to production; will rise with demand
Spatial Market opportunities	Form of Random (or sometimes systematic) opportunity originating from spatial variance in price	Perfect market. (Oppressive when applied to wages)	Often dependent on local wage, technology, resource scale and taste variations; analysis requires attention to specific cause	Should disappear with better developed free markets	Does not contribute to production; dependent on spatial variations in demand versus production
Wage Anomalies	Form of spatial market opportunity; profit opportunities from lowered wage costs from physical production in low wages locality	Producer with highest wage rate, this is often the wage rate in the country of final sale	Exploits international wage rate anomalies; major economic rent driving globalization; supported by spatial anomalies in the political power of labour	Will diminish as wages tend to lowest level tolerable without political retaliation	Does not contribute to production; relies on sustained effective demand, usually in a high wage rate country
Political Inter-occupational wage disparities	Income gradient between occupations higher than warranted by skill & responsibility	Wage gradient matches skill & responsibility gradients	Evident both between occupations and between management levels	Dependent on stability of inter-occupational power balances	Slightly dependent on demand for specific skills
Financial Efficiency	Improved profitability from greater financial efficiency; many strategies, especially debt.s.	least financially efficient firm (lowest debt leveraged)	Does not affect productivity; many strategies produce exposures to various risks	Encourages high levels of debt; cyclically corrected	Independent of production and demand
Temporal Market opportunities	Pricing variations through time; e.g. hoarding, futures, bull and bear opportunities	Stable and predictable price levels	Risky; sometimes capable of exploitive manipulation	Random	Dependent on temporal balances between demand & production

13.3 COMBINED OPERATION OF ECONOMIC RENTS

In general, each source of economic rent has a marginal case, even land in a closed market. In practice if land is purchased for use or rented, the payment to the other party normalises its return to the user. This produces a conventional marginal situation for the user, who may be able to use the land at a more productive level that the market generally expects. In this way, the tenant/owner-occupier is able to realise a rent on his land as the productivity gap above the rent paid.

Exhibit 13.10 Supply Function from Composite Rents



Conceptually, the economic rent available for any particular producer could be computed by evaluating the functions outlined above and summing the various economic rents that a particular producer can exploit. This would yield a single net economic rent for each producer or merchant. While this may be impossible to

construct in practice, production feasibility studies achieve the same result by examining the profitabilities of particular strategies.

Each producer should be aware of the dynamics of the production parameters in getting a product to market. Taken collectively it will be clear that some producers will be more efficient than others and, at least in the medium term, their production capacities will be limited.

The more efficient producers will enjoy strong economic rents, while the least efficient will earn only a normal profit. Obviously, these can be graded in terms of total production efficiency, and the total potential supply charted as shown in Exhibit 13.10.

The example shown in Exhibit 13.10 makes the following assumptions:

- Each productivity grade is expressed in terms of productivity per employee, or labour efficiency, though it includes non-labour rents, such as debt leverage rents.
- Capital assets (including employee training) earns normal profit (return) consistent with their costs where the latter is in labour units.
- The numeric assumptions further assume:
 - labour cost of 100 applicable to each grade (i.e. the total product is the product per 100 units of labour input)
 - marginal pricing refers to possible supply price if subject grade was the productive margin.

The number of producers that will be active depends on the demand in the market. It can be assumed that the first producers to enter the market will be the most efficient, or grade 1 in the example. They will be followed by the lower grades in order until a point is reached when demand is satisfied.

Prices will be pushed down in an efficient market until the least productive producer earns only normal profit, i.e. that grade of production will be marginal. The example computes normal supply prices for each grade, assuming that grade to be the marginal producer. For example, if demand is such that producers down to grade 7 are employed, that grade will become the marginal producer and prices will find equilibrium at \$0-71 (right hand scale). If demand is strong enough to cause producers down to grade 11 to be employed, prices will find equilibrium at \$1-00 and grade 7 producers will enjoy an economic rent of \$0-29 per item.

The important aspect of this analysis is that it produces a supply function that is consistent with the popular configuration of the supply function, but drawn from economic rents rather than the theory of the firm. This derivation of the supply function does not need further specification of the nature of the economic rents involved, nor does it need to make unrealistic assumptions about the behaviour of costs. It is also

able to be modified to accommodate various forms of market imperfection, especially as these are significant sources of random and systematic economic rent.

13.4 COMPARISON OF VARIOUS ECONOMIC RENTS

The table in Exhibit 13.11 summarises the major categories of economic rents that have been considered. It may be seen that economic rents fall into four main groups as follows:

- 1) Stable rents that are randomly distributed gifts of nature. These are primarily composed of land, raw materials, and also natural personal ability.
- 2) Transient rents arising from differing efficiencies in the utilisation of labour that will dissolve with market maturity. These include technology and scale opportunities.
- 3) Transient rents that affect profitability without changing labour efficiency. These include random market opportunities, spatial and temporal market anomalies, spatial wage anomalies and financial efficiency (especially debt leverage) rents.
- 4) Stable rents distributed through the economy that result from market imperfections or the misuse of various forms of power. They are not related to productivity *per se* despite sometimes originating from productivity increments.

The first group may be classed as land, even though when manifested as human ability it may appear personal. It is not intended to imply that these resources cannot be private property, as they are traditionally accepted as such, especially in the case of personal ability. The important characteristic of this group for the present study is the way that its rents are stable and they increase with productive efficiency, market efficiency and population.

The second group may be transiently important, often contributing to superior productivity but eventually dissipating as the superior productivity becomes the norm. It may even be a distraction to make too much of the importance of these significant sources of economic rent at the firm level because "*... it is now generally thought that all firms rapidly adjust to a profit-maximizing choice of technology and level of output that is optimum given the unique circumstances faced by each and every firm.*" (Prasch 1999, p.471) Although market theory suggests that these rents are transient, they have the capacity to produce hurdles to effective competition that lead to rents of the fourth type.

The third and fourth groups are distinct because they do not improve the production of goods and services, only the efficiency with which sales of these are translated into profits. They are the groups that are more usually associated with super-normal profit.

The third group includes non-productive rents that by nature tend to be either self-extinguishing or random. Debt leverage is unusual in this group as it is visibly influenced to some degree by cyclic attitudes towards debt.

The final group represents economic rents that are perennial, like land, but not derived from productivity. They are maintained by political or other structural factors that are exogenous to purely economic actions. They are highly individual and although they may have been initiated through one or more of the other rents, especially from the second or third groups, they are distinct in being maintained well after efficient market forces should have dissolved them. The fourth group is more commonly known by the title monopoly, which is a trading position that is the result of a permanent market failure¹³¹.

The spectrum of economic rents therefore contracts to two perennial types, those that result from natural factors that influence productivity (land) and those chronic market imperfections that concentrate profit despite having no influence on productivity. The only perennial non-land economic rents are the result of factors that are beyond the scope of economics, such as political privilege or scale efficiencies that cannot be matched. Even these can be shown to have an important relationship with land rents, which may be understood by recognising that they are artificial retentions of distributions that would otherwise flow to either land or labour

13.5 PARTICIPANTS IN LAND RENT

If the wages line represents a subsistence return to the non-land factors, then labour will not be able to tolerate any additional economic burdens. This means that all other distributions must be participations in land rent. The most significant of these are super-normal profits and taxation.

Care must be taken with definition. Subsistence wages have been defined as that level of income to those who toil for their living that will enable that social group to maintain itself. If this is a necessary payment, then publicly funded welfare redistributions through the taxation system will be a contribution to essential wages. While this may appear necessary at the theoretical ethical level, at the practical level, there is no actual compelling obligation. The state could simply allow the working people to starve. Sen (1981) described examples of this very outcome in describing the major famines of the last two centuries. His research suggested that in every case he studied famine stricken areas were actually exporting food while ordinary people were starving to death. The Irish famine in the nineteenth century is perhaps the best known

¹³¹Note that the existence of a single supplier does not necessarily signal monopolistic exploitation. It is possible for a lone supplier to charge prices that do not exploit the power of the market position. Market manipulation is the issue and is actually independent of the number of suppliers.

example in the English speaking world, and was visibly connected with the linkage between property rights and political power. These examples also illustrate the problem with a naive trust in wages *naturally* finding reasonable subsistence.

If it is assumed that subsistence wages are naturally the right of working people to a reasonable standard of living that provides them the minimum portion of the society's product sufficient to allow them to materially maintain their social position, then three conclusions must follow:

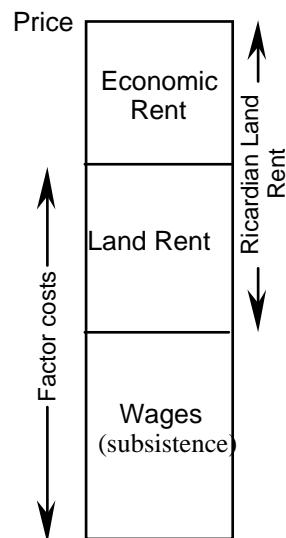
- 1) If wages are below this level, it is a form of theft against working people and will prevent them from enjoying a reasonable quality of life.
- 2) If wages are above this level, working people are sharing in a gratuitous benefit that others may have a call on. They are receiving a portion of the land rent and this may be affected by the operation of Ricardo's rental theory
- 3) If wages are at the subsistence level, then no additional charges may be made against working families or they will be forced below subsistence level existence.

Super-normal profits and taxation will now be considered in detail.

13.5.1 Super-normal Profits

Super-normal profit is the increment of profit above normal profit that is the result of capturing some *economic rent*. In a perfect market at equilibrium these profits should not exist, but in practice they do. Super-normal profits may be identified by real growth in equity values. Some apparent economic rents may in fact be necessary normal returns, as in the case of technology rents. Economic rent denotes the excess by which a commodity's price exceeds its factor costs. Land rent has been shown as deriving its value essentially from the gap between product price and non-land factor costs. If the return to the non-land factors covers subsistence alone, and this could be expected to include normal profits, then any super-normal profit must be the result of participation in part of the return to land as shown in Exhibit 13.12.

Exhibit 13.12 Factor Costs and Economic Rent



If price is determined by a market and wages are at subsistence, then Ricardian rent theory would suggest the the gap between wages an price will become the value of land rent. the that actual land rent leaves a shortfall that is enjoyed as economic rent means that econo rent is a participation in that return that is naturally land rent.

The perennial existence of super-normal profits and their importance for market theory have been discussed, however the fact that they are necessarily a participation in land rents has important implications for the application Ricardo's theory of rent for the following reasons:

- If they exist and are participations in what is naturally land rent, then any arguments concerning the use of land rents should necessarily include super-normal profits, or other occurrences of economic rents¹³².
- Their perennial existence is evidence of imperfections, not only in the markets, but also in the practical operation of Ricardo's rent theory, thereby weakening the validity of policy that assumes its perfect operation.
- Policy arguments that are levelled against private profit appropriation, such as the current concern in many countries regarding foreign investment and the presence of foreign corporations, should be viewed as special cases of a more fundamental issue regarding the private use land rents.

Various aspects of super-normal profit are often targeted for popular criticism, for example the recently popularised trend towards globalization and the huge size of key corporations must be the result of the concentration of super-normal profits. This criticism reduces to popular objection to the visible concentration of a species of rent in the stock market. Despite sometimes supplying impressive critiques of corporate

¹³²This would exclude apparent economic rents such as those that are normal returns for technology innovations or the licit returns to a merchant.

power, they often focus on these concentrations as the primary flaw in market economics¹³³.

If these trends are somehow offensive, then the criticism must either relate to the nature of the profits taken by these corporations, or their extent. The fact that small corporations are often viewed positively suggests that popular sentiment is triggered by the extent of the economic power that is being concentrated, or perhaps its exploitive use. Small business is often perceived as having a more human face, providing employment and, because of its inability to manipulate its market, more responsible in its pricing. This is despite the fact that many small business owners earn comfortable incomes. This suggests that the indignation is not directed towards the nature of economic rents, but rather their use. This is consistent with the ancient notion of common use and the fact that economic rents are participations in land rent implies that they are similarly participants in the essential dynamics of private property in land.

Despite being the metaphysical source of super-normal profit, land is seldom recognised as such in economic thought. Therefore, if Ricardo's rent theory is valid, super-normal profit should be linked through economic rents to land rent, and be considered as a special case of the latter. This is not to say that non-land economic rents do not have a valid place in economic systems; private reward for technology and scale seems valid as it encourages more efficient production. Rather, it recognises limits to these rents.

Economic rents signal market imperfection making their persistence evidence of the inappropriateness of economic theory based on the assumption of perfect markets. The whole discipline of finance is devoted to the maximisation of economic rents and its success is evident. (Bhagwatti 1982) has formalised the study of occupations that are wholly devoted to the maintenance of super-normal profits and concluded that in the long term they are all counter-productive. Despite this, occupations such as political lobbying attract handsome incomes because they leverage considerably greater advantage to their clients than their fees cost, despite being directly unproductive in themselves. In Britain, the thirty three years from 1954 saw a doubling of their per capita income, but a polarization of income benefiting the economic rent-takers at the upper end of the income spectrum at the expense of the labouring lower end. During the same time, despite the marked increase in general unemployment, employment in banking, insurance, stock broking, tax-collecting and accountancy employment expanded from 493,000 to 2,475,000 supporting Bhagwatti's thesis (Douthwaite 1992).

¹³³See for example (Korten 1995).

13.5.2 Taxation

There is considerable historical evidence of land rents being redirected without causing an adverse affect on economic activity. An example illustrates this possibility. Consider for example the impact on production that would follow from a foreign power seizing title to all the land in a society, but otherwise leaving rental levels and the economy intact. Users of land would continue to net the same incomes from their work, no additional costs would be incurred or added to commodity prices and no productive capacity would be in any way compromised. The rents could be completely removed from an economy without producing any change in the motivation to produce or the distribution of goods and services. This would appear to suggest that the beneficiaries of rents in a community could be changed without affecting its economy. Unlike the appropriation of land rent, all other taxes directly affect industry and commerce.

Historically, this is evident in the political history of Europe, from the impacts of Roman occupation to modern times. The Dark Ages (600 - 800 AD) were actually closed by the surrender of land title to the feudal lords who offered no direct economic rewards apart from the promise of defense. Owners willingly transferred title to their own land to the feudal lords in return for security. The result was that they they were able to live on what was left of their product after paying rent, and the rent funded the primitive governmental functions of law and order and security against foreign invasion. The outcome of that process actually improved the lot of the land user considerably. The rents, especially under Christian lords, were paid out of excess and considerably easier to suffer than the regular invasions that previously characterised the period.

In addition, due to the re-establishment of peace and order, production actually flourished making possible the massive developments in agricultural productivity that marked the early Medieval period (800-1100AD) (Atack 1995). This could suggest that such a form of taxation may improve the performance of the productive economy by funding various community supports, however one must exercise extreme caution before making too much of the advantages of land rents as tax.

Empirically, the NSW Western division lands are state leasehold and should behave as a perfect example of George's land tax prescriptions. The politics of democracy appears to have been responsible for the erosion of state rental incomes to the point where these properties command freehold-like prices. The situation in Queensland is similar and was responsible for much of the concern by Western leaseholders regarding the the Wik people's customary title claim (Small, 1998). Likewise, the Australian Capital Territory is state leasehold that began as an explicitly Georgist enterprise that had failed in about half a century (Brennan, 1971). In other countries where Georgist

land tax initiatives their effectiveness has been short lived, suggesting their political vulnerability. Historical examples notably the many instances of feudalism, were also marked by eventual failure.

The political vulnerability of land tax demonstrates the shortcomings of state control of what is essentially an ethical issue. If land rents should be consciously directed to providing for the common good, and there appears to be a good case in that direction, it is not sufficient to rely on the state, even in a democracy such as Australia, to impose such a policy. It would appear that unless it is the active will of sufficient people in positions of power, it will fail. The conclusion here is that it is education, the promotion of a suitable ethic, and most importantly its voluntary adoption that would effect a real solution.

In the modern context, the failure of Georgism to recognise the rising importance of other rents, principally corporate super-normal profits and money interest is highly problematic. The rising importance of these returns means that even if land rents were adopted as the tax base, many of the problems land tax is supposed to control would continue through the other participants in what are essentially Ricardian land rents.

In practice, rents themselves are influenced by several factors that are socially originated. George's analysis focused on the fact that society itself was the major cause of land value and concluded that if society was the efficient cause of land value, then it should be the title holder. (Charles 1991) documented the way that historically land rents have been the dominant source of public funding up until this century, though their importance has exhibited a long term decay.

13.5.3 Infrastructure funding

A more concrete nexus between land rents and public action is visible in the case of publicly funded infrastructure and this has been examined in chapter 10. This appears to warrant separate treatment and introduces some of the issues supporting the argument in favour of land rents as a tax base.

Adjacent infrastructure has no material impact on a particular land parcel, but can greatly influence its productivity and therefore its rental. (Yinger 1982) recognised that where local taxes are not sufficient to balance the utility of local infrastructure, prices will be bid up. While this may benefit those who own the property at the time, subsequent owners find the balance between amenity and cost (as purchase price plus local taxes) restored. For these latter owners, if the amenities are funded from other taxes, such as income tax, they may be effectively paying for the amenity twice. Also, persons paying income tax in remote parts of the country will be funding the capital

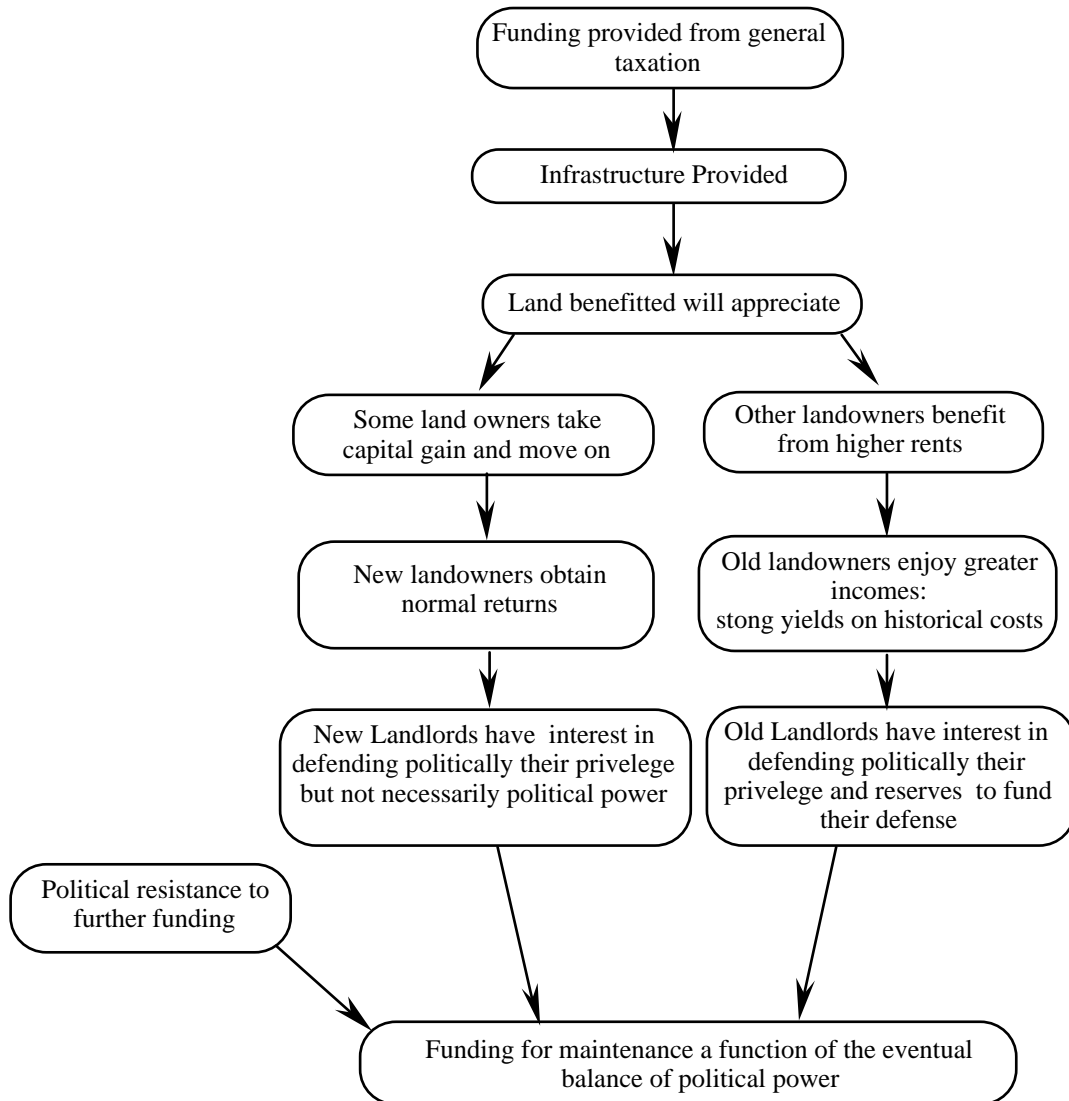
appreciation of land benefited by public infrastructure spending that may be the result of political, rather than equity decisions.

The inference here is that rents will be stabilised when local taxes are raised to equal the amenity flowing from local infrastructure spending. It is not clear whether this is strictly speaking a tax, or simply a fee for service¹³⁴. The rental increment due to public infrastructure spending can be diverted from landowners without either harming them, or adversely affecting the local economy. In fact, if responsibly planned, the infrastructure will probably be a stimulus for the local economy. On this basis, value capture through a levy on land rents is a sound strategy for public infrastructure funding (Small 1997).

Failure to maintain local taxes in proportion to local infrastructure is not uncommon and leads to mis-matching that results in implicit wealth transfers from those who actually fund local infrastructure to the landowners who enjoy the capital growth. Not only does it produce wealth transfers, but also compromises the funding needed for maintenance. Once infrastructure funding is dislocated from its beneficiaries, those taxed may be expected to resist further funding for maintenance. If the beneficiaries are politically powerful, they will be able to resist the pressure, but this places the maintenance of infrastructure at the mercy of the political market which operates quite independently of the physical needs of the community affected.

¹³⁴Some fees paid to the government are not considered to be taxes because there is an explicit link between the fee and the benefit. Postage stamps and garbage collection fees come within this category.

Exhibit 13.10 Political Effects of Inappropriate Infrastructure Funding



Local government areas in the far north east corner of NSW have been considering the removal of tarred pavement on several minor roads over the last decade. Despite the benefits to the local community of paved roads, the fact that funding comes largely from federal sources has made the maintenance of the earlier investment in pavement uncertain. (Brennan 1971) chronicled the way that the contraction of effective rents in leasehold Canberra has produced public funding difficulties that the original leasehold scheme should have made unnecessary. Politically, the beneficiaries of the initial infrastructure may no longer have a personal interest, having sold out with a capital gain. In analysing the Australian Wik problem¹³⁵ (Small 1998) has demonstrated how much of the problem originated from a failure of the State to levy market rents on its

¹³⁵The case takes its name from the aboriginal Wik people who mounted a customary title claim against Western leasehold estates.

statutory leaseholds. Unfortunately, the beneficiaries of these effects have often taken their capital gains and are no longer part of the local economy, leaving the current title holders poorly positioned to accommodate the challenge, either politically or economically. Exhibit 13.10 shows how there may be two types of landowners when a challenge confronts landowners who have benefited from some public policy. The outcome will depend on the balance of political power between the three groups.

13.5.4 Foreign investment and savings

Exploring the example of land rents being taken out of the economy one step further, there is an economic argument that applies to all foreign interests in a local economy that would suggest that the foreign appropriation of land rents, or other significant profits, necessarily impedes the local economy, at least in the long term. Productivity, as use in this discussion, relates to the total sales of what is produced by the economy. In a closed economy sales must be paid for out of the incomes of the producers, hence the total of those incomes equals the sum of the factor costs, if the sales are local and the rents go out of the country, the local economy's ability to purchase its own product will be compromised. This will necessarily lead eventually to apparent over production¹³⁶, falling prices and the collapse of local industry. This effect will not be apparent if sales can also be made outside the economy, or if money can be borrowed against the future to re-inject liquidity into the market.

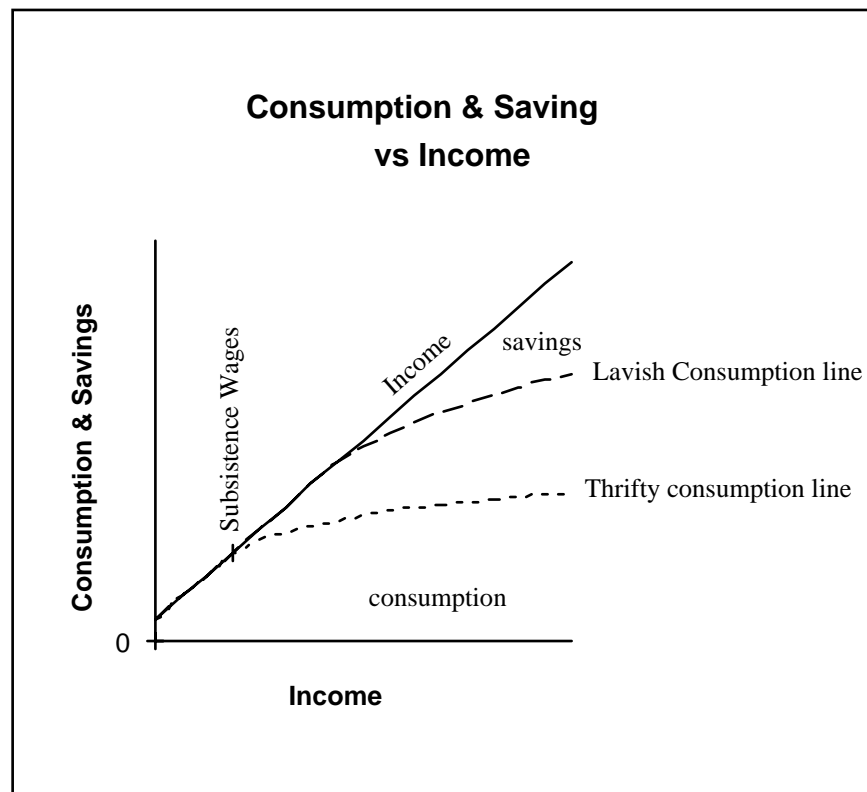
This effect may also be applied to local distribution. Ricardian rent theory suggests that savings must be made out of rent¹³⁷, being part of the return from production that is not used as consumption. Interpretation via rent theory informs the problem that is well known the *paradox of thrift*. By definition, all wages will be consumed (a condition of subsistence). The rental earnings carry no such necessary destination. If privately appropriated, depending on the concentration of ownership, only part will be used by landlords, or other rent-takers, for consumption. The remainder will be saved or used for investment. Exhibit 13.14 outlines a conceptual model of consumption at various levels of income. It is assumed that no effective savings occurs at or below subsistence wages. Above subsistence some savings may occur depending on the prudential judgements of the person. A thrifty person may use increased income for moderate increases in consumption, while a lavish person may consume considerably

¹³⁶This is over-production in the sense adopted by economists. It refers to production beyond the willingness of the society to purchase. Economic thought views willingness in terms of willingness to pay and if the society does not have money, then despite their very real demand, they may display low economic demand. (Sen 1981) dealt with this anomaly in his discussion of entitlement, and the failure of market economics to recognise that the market will not solve the distribution problem in situations wherein members have material needs but not the economic resources sufficient to *entitle* them to a reasonable share of the products available to meet those needs.

¹³⁷Savings here may be considered as savings that is beyond what will be consumed in the long term. Savings to cover old age such as superannuation may be considered to be a part of subsistence.

more of his super-subsistence income. As incomes rise further, there will come a point where even the lavish person will begin to devote an increasing proportion of his income to long term savings. Long term saving must come from super-subsistence income, which must be rent in Ricardian theory.

Exhibit 13.14 Consumption versus Income

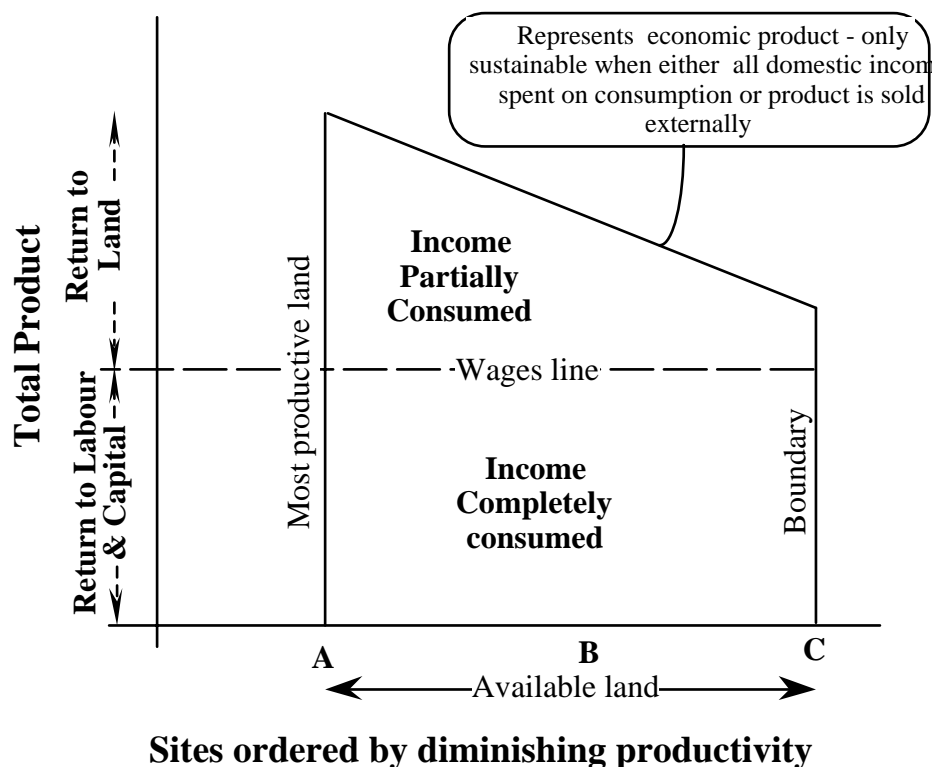


In a closed economy, the degree to which rental income is not consumed is the degree to which an economy will not clear its product. The value of the product is derived from its sale to purchasers who have entitlements equal to their incomes, either from wages or rents. This is illustrated in Exhibit 13.14. If liquidity (purchasing power) is lost from the economy either money must be borrowed against the future or foreign markets exploited, otherwise prices will collapse. Keynes popularised the strategy of borrowing against the future and it is sustainable so long as expansion continues. While there may be grounds for monetary expansion purely as a stimulus for economic growth, its necessity for clearing markets as a result of savings losses should be recognised as a separate issue. Douglas (1974) recognised the problem of the apparent monetary short fall but failed to analyse its source. His creative money-centred remedy became a significant political movement in North America but was essentially flawed and is now discredited.

The drive towards globalization may be interpreted as partly necessitated by the need to find new markets for products that cannot be consumed in their domestic markets. It is also driven by a desire to appropriate rents from fresh markets that have some capacity for investment exploitation. The eventual difficulty of both globalization and reliance on monetary growth will be their dependence on growth to solve the problem of local rents that are not consumed. This would appear to be very important for the operation of capitalism, which relies on the concentration of wealth through various forms of savings for corporate growth.

While it may appear to challenge the value of savings and investment, this conclusion should not be taken too hastily. Exhibit 13.15 dissects savings and this dissection will be briefly reviewed in terms of its relevance to Ricardian rent theory. There are two types of saving and two types of investment, and consideration of the behaviour of each is useful if the problem of over-production is to be avoided. Savings can either be in the form of money, or of product. Modern Western societies do not save product to a great extent, although it is a valid way to provide for future uncertainty.

Exhibit 13.14 Source of Real Savings

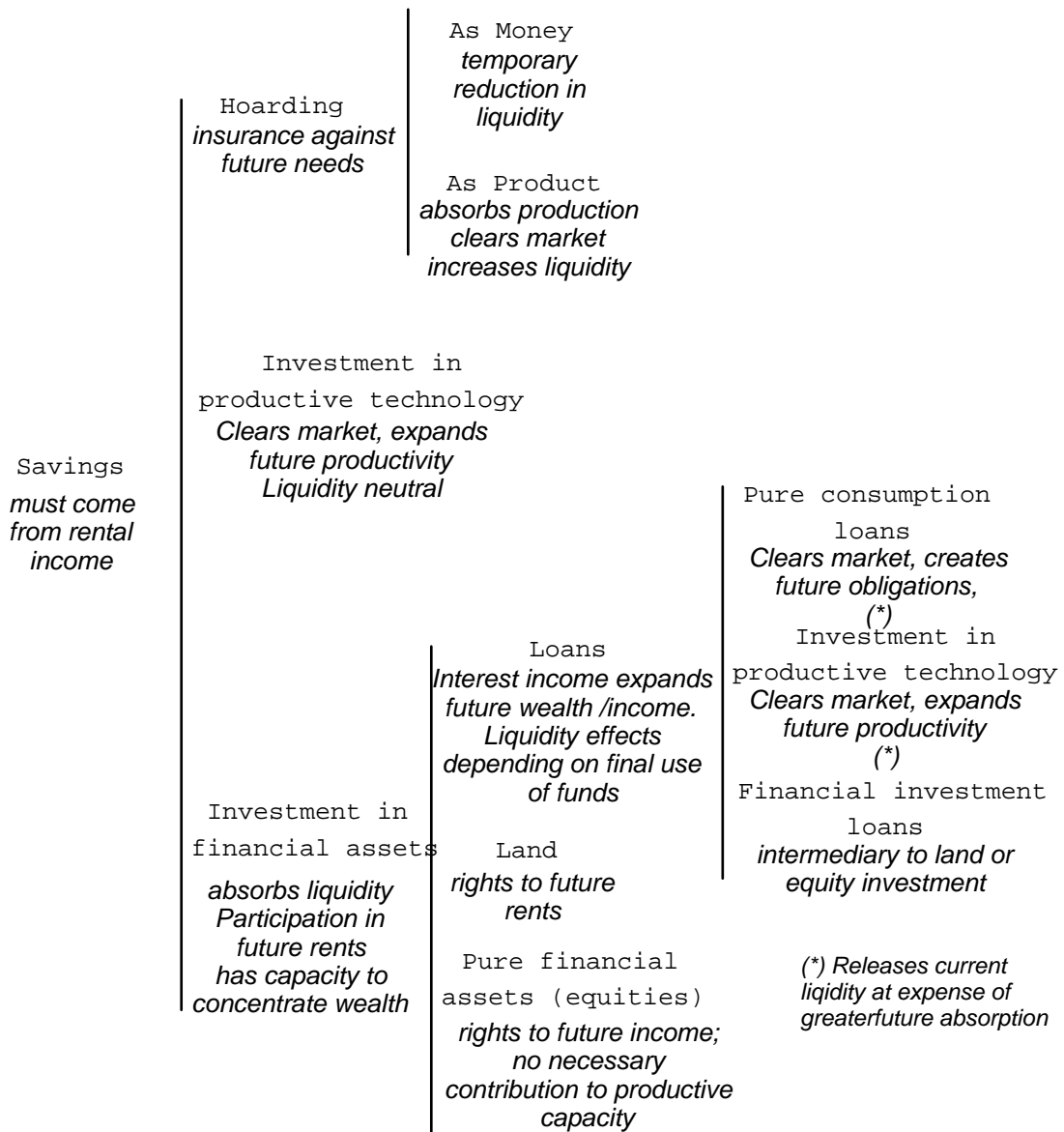


When product is saved directly, say by a landowner stockpiling grain or a corporation manufacturing its own plant and machinery, the product is not released

onto the market, so the market does not have to find the funds to purchase it. Consequently, it cannot precipitate economic recession. To the extent that owners must still pay wages for the production of the product stored, liquidity may even be expanded. The expanded liquidity will either be used for consumption, which may be inflationary, or saved.

When the product is sold the income can be saved in several ways, some of which do not stimulate the paradox of thrift problem. The schema shown in Exhibit 13.15 examines the various forms of savings and their effects. Money can be stored like grain, in vaults, or it can be loaned. The former compromises liquidity and eventually there will be insufficient liquidity in the economy to purchase the available products, resulting in an over-supply effect. Money loans can be for various forms of consumption or financial investment. Savings that are loaned to purchase either consumer or productive goods contribute to clearing the market. Loans for financial investment have the same impact as direct financial investment.

Financial investment includes three species, loans, investments in land and in equities (especially shares traded in the secondary markets). Except for loans that are used for consumption or the purchase of productive technology, these absorb liquidity. Loans all include the future absorption of more money than they release in the present. For this reason borrowing to balance liquidity present needs and clear markets will necessarily roll up problems for the future.

Exhibit 13.15 Savings Schema

Financial investments in land or existing equities do not contribute to consumption, and therefore does not contribute to clearing the economy's current product. They all expand the income rights of the holder to a greater future share of the economy's product without increasing that product. Because they are funded from rents, they accelerate the concentration of wealth without any new productive capacity¹³⁸; investment in the stock exchange may increase one's eventual income, but does not add

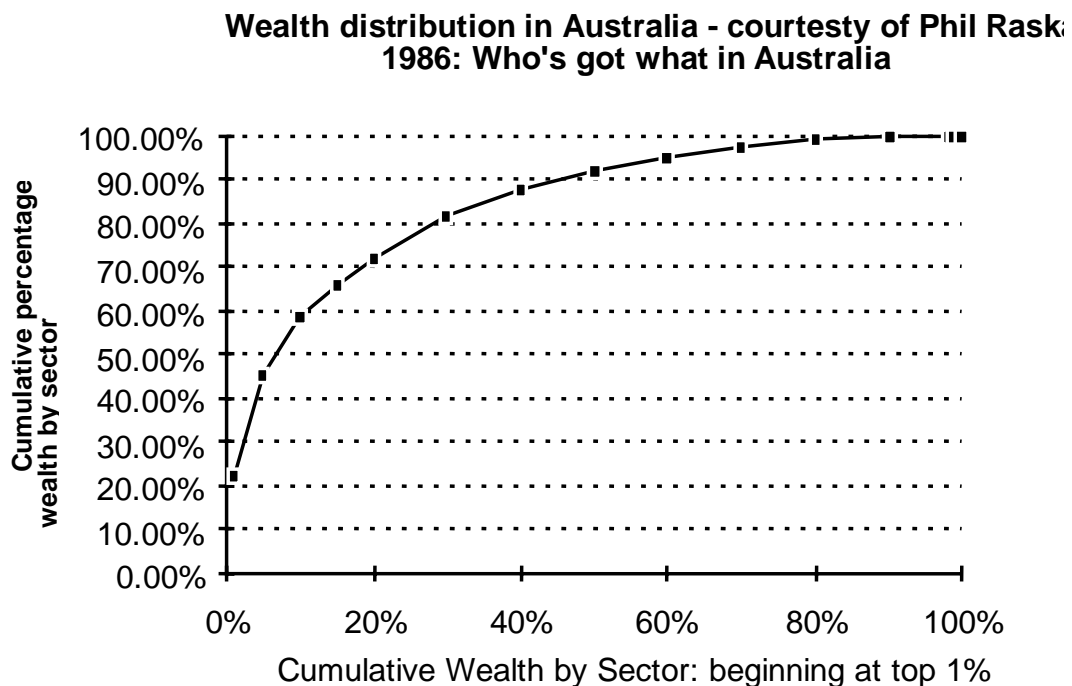
¹³⁸While it may be argued that loans for consumption or productive capacity clear present markets and may enhance future productive capacity, the emphasis here is on the return to money, the interest income. This return is not productive in itself but does create an expanded wealth share for its owner. It may be contrasted to direct

directly to the capitalisation of the firms whose shares are purchased. No new machines are purchased, yet the investment will very likely fuel capital growth.

This analysis reveals two important points regarding the use of rents. Firstly, when they are not used for consumption, they produce strains on the economy. Secondly, in addition, when they are directed towards investment in either equities or land they concentrate wealth.

The concentration of wealth not only means a concentration of economic power, often leading to concentration of political power but also dysfunction of the economy as Mueller (1998) observed "*...in economics, a broad distribution of wealth is technically a prior condition, not the inevitable outcome, of a properly functioning market economy*" (p.238). Land ownership beyond what can be personally used has been shown to be a source of considerable non-productive dysfunctional rent-taking (Brennan 1971) and has been argued against for some time (Tollemache 1913).

Exhibit 13.16 Australian Wealth distribution 1986



Raskall (1986) researched the distribution of wealth in Australia using probate data and produced the distribution shown in Exhibit 13.16. Wealth distribution is a key item

of data in evaluating the misuse of conventional property, though it is rarely gathered by public organisations such as the Australian Bureau of Statistics (ABS). Income distributions are often presented as a proxy for wealth distributions, but incomes tend to be written down for taxation purposes. It is widely understood that many of Australia's wealthiest families have taxable incomes equivalent to the working poor. Raskall's data demonstrates the degree of wealth concentration in Australia, the top 5% owning 45% of all conventional property in the country. By comparison, the next 5% own only 13% of the country's wealth, about the same as the entire bottom 60%.

The non-consumption of rental income and its wealth concentration effect can be seen in some economic cycles. In boom times, production will increase and wealth will concentrate, usually fuelled by expanding monetary supply largely sourced from debt. A point will come when the monetary expansion will falter due to the limits of debt funding. The level of wealth concentration and the inability of the market to clear itself results in apparent over-supply, production becomes impossible and depression sets in, possibly attended by a failure of the banking sector. This process appears to explain both the 1890's and 1930's depression and (Das 1993) has found a correlation between wealth distribution and economic cycles that would support this general thesis. Das found that economic depressions tend to follow these concentrations and have the effect of redistributing them.

The history of Japan is interesting in that it contains two periods of land redistribution, the most recent being by Macarthur following World War II. On each occasion it had a marked stimulus on the Japanese economy. The existence of a frontier in the USA had the effect of preventing wealth concentration and has been shown to have contributed to the economic success of that country until well after the frontier closed.

Ricardian rent theory therefore identifies which category of income is capable of producing the paradox of thrift effect, the long term concentration of wealth with its various dysfunctions possibly including being one cause of economic cycles.

13.5.5 Money and rent

Money is a complex topic and beyond the scope of this thesis, however it does have a bearing on rent allocations which deserves some mention. It has been seen that debt leverage is a source of economic rent, but this does not explain the origin of income from money loans. Given the definition of subsistence wages, it should be apparent that debt costs must be a participation in what is naturally land rent.

Money borrowed to buy land obviously takes its interest out of the land rental income, but loans taken by tenants will also come out of rents. Consider an agricultural

example for simplicity. Assume a new farming technology becomes available that requires investment in new equipment, say a tractor. Tenants do not have the financial reserves to buy the technology but borrow with the intention of repaying the loan out of the increased product resulting from its use.

Were the tractors free, production would increase universally. At first this would increase tenant income but eventually it would be taken in rent. If the tractors were purchased with zero interest borrowings a similar result would occur, except that the cost of the tractor could not be taken as rent by the landlord because this was previously committed to the lender and if taken as rent would leave the tenants below subsistence. Likewise the interest cost represents an amount that would be absorbed by land rent if not previously committed to a third party. The actual interest rate is not significant, and could vary widely, so long as tenants were able to retain it from rent commitments.

It has been seen that rent has the capacity to concentrate wealth, at least where it is earned in sufficient quantity to exceed the recipient's consumption preferences. Rent also has no cost of supply. Money has the same characteristics¹³⁹. and has the advantage of being considerably more flexible. Suffice to say, money participates in rent. Some authors have focused on money as the primary source of economic distortion but this is largely because of its visibility. It is apparent that global indebtedness has risen alarmingly in recent years which does mean that creditors have coincidentally acquired greater influence, however it is not clear if this is out of proportion with other major concentrations of wealth. It would seem that the underlying concentration of wealth and economic power which is the issue, not money alone.

13.5.6 Apparent taxation and savings out of wages

It should be evident that taxation also cannot be taken from subsistence wages. If wages are set so low as to only leave the worker with sufficient income to survive, and maintain a stable economic position, then the state will not be able to impose any taxation on wage earnings. For similar reasons, normal profits cannot be taxed without causing erosion of equity values. Therefore taxation in any form must be derived from participation in land rents.

This is not to say that income tax is impossible, rather that although it is paid by producers and workers, it is not actually a part of their essential income, but a part of

¹³⁹The possibility of alternative income has resulted in the invention of *opportunity cost* as money's cost of supply. The validity of opportunity cost cannot stand alone, as it is dependent on the nature of the alternate uses. For money it must be an alternate loan which leads nowhere. Further exploration of this issue requires consideration of money usury which is beyond the scope of this study.

land rent that has diffused into their pay packets to pay the tax. In the absence of the obligation to pay tax it would have otherwise been absorbed by land rent. This is not surprising, given the definition of wages as the subsistence income for the working sector, it means that when taxes are introduced of any kind, rents will suffer. The effect of a taxes diminishing rental levels may be difficult to perceive in practice because of the flexibility of people and the gradual introduction of most taxes.

The introduction of a new tax, such as the immanent introduction of the Australian Goods and Services Tax (GST) may not be easily apparent because its effects on rents may take some time to take effect. The GST is further complicated by the fact that it is supposedly matched by reductions in other taxes. If this is in fact true, then the net effect of the GST on rents may be negligible. In particular, Ricardian theory would appear to suggest that a GST on rents should not be possible, because a rent increase would depress wages, that the theory suggests cannot be done. However, if apparent wages contain a component that is land rent sufficient to pay the previous taxes, and these latter taxes are removed or diminished, then that amount of land rent could be taken back by landlords to pay the new tax.

The point here is that apparent wages and rents are distinct from the essential Ricardian wages and rents, making empirical observation of these quantities difficult. Consequently, it may be expected that the quantities that Ricardo was considering are not easily integrated into positive economics. While this is a significant problem when working within a positivist paradigm, to ignore the potential explanatory power of the Ricardian dissection between wages and rent is to put aside a valuable insight into the economic process.

If super-normal profits and taxes participate in land rents, which the notion of a subsistence wage suggests, this does not necessarily imply that such a participation is in any way uniform across land productivity. The study of the relationship between the distribution of super-normal profit, taxation and site productivity is beyond the scope of this study, however, it would appear reasonable to assume that in practice it may be significantly influenced by practical market inefficiencies.

The distribution of returns between wages (and normal profits), land rents, taxation and super-normal profits are shown schematically in Exhibit 13.17. In addition to super-normal profits and taxation, it is suggested that other non-productive activities in the society, such as Bhagwatti's directly unproductive occupations and interest incomes from debt, are all participations in land rent.

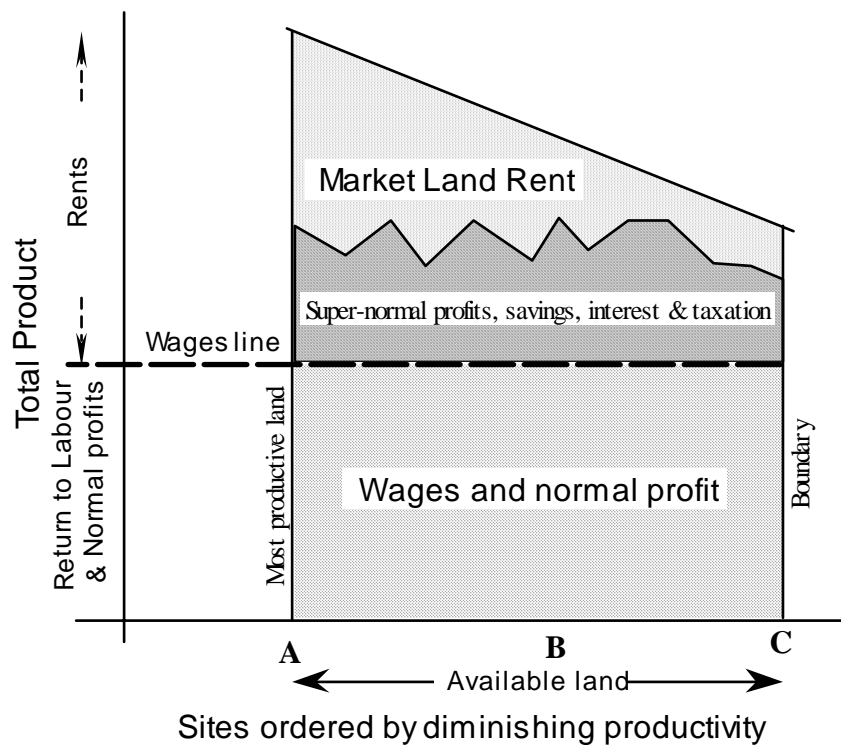
Overall, it has been shown that, given the definition of wages, non-land rents taxes and other non-productive occupations must all be participations in land rents. This creates a difficulty in terminology between normative and positive conceptualization's

of both wages and rents. Positive wages include land rent components such as the following:

- An amount equal to the taxes paid by the worker at all levels.
- An amount equal to any net savings made by individuals.
- An amount equal to the cost of residential rent.

In addition to the above that cause positive wages to overestimate normative (real) wages, positive wages may also underestimate real wages by the value of state redistributions through public welfare

Exhibit 13.17 Non-wage distributions as participations in land rent



13.6 CONCLUSION

The notion of subsistence wages has been explored and found to be a social/political construct rather than the pure product of economic processes. Subsistence income may be considered as the minimum income above poverty where the latter must be understood in both absolute and relative terms. Poverty absolutely is the inability to meet the bare minimum level of material needs necessary for human survival. Poverty relatively understood is derived from the social dimension of human nature and relates to the inability to participate in the appropriate proportion of the community's goods and services.

Various sources of economic rent have been reviewed and found to reduce to three types, land-like rents, production efficiency rents and market failure rents. Combining these can produce a market supply function that overcomes most of the problems inherent in the conventional explanation of the supply function derived from marginalist theory and the theory of the firm. Given that production efficiency rents are believed to dissipate quickly, the only perennial rents are land-like rents and market failure rents.

The issue of taxation has been introduced. The clear relationship between public infrastructure and land taxation has been explored and some of the issues discussed showing the desirability of matching local taxes to local amenity. Investigation into the issue of foreign investment and the problem of market clearing has shown that when rental income is not used within the economy various problems arise. The problem of saving and its relationship to rent has been considered and seen to produce similar problems to foreign ownership. It has been shown that, given the notion of subsistence wages, all saving must come from land rents. Although some types of saving (such as the retention of some product from market, or money loans to others for the purchase of products), several types of savings produce longer term problems. It has been suggested that the use of rents to purchase additional rent producing assets concentrates wealth and appears to be at least one cause of economic fluctuations.

Overall, it has been shown that Ricardian rental theory provides an understanding of normative (real) wages and the tension between these and the various participants in land rents. A disadvantage of this analysis is that it tends to provide normative understandings that are not necessarily reflected in positive values. Positive wages include components of land rent sufficient to fund the worker's taxation, savings and domestic real estate needs and ignore the benefits of governmental income redistributions. Positive rents do not include the various economic rents, taxations and support costs that are funded from real rents.

13.7 CONTRIBUTION TO THE SUPPORT OF THE THESIS HYPOTHESES

	Hypothesis	Conclusion
1.5.21	In practice, the resolution of the actual level of the subsistence wage is social/political.	Supported
1.5.22	The behaviour of productivity (and hence use value) differs between land and products	Supported
1.5.23	Rent taking in land is distinct but related to other (economic) rent taking.	Supported
1.5.24	Supernormal profit, interest on debt, and taxation are all naturally paid out of rent.	Supported

Chapter 14

The Social Economy of Land

The purpose of this chapter is to draw together the conclusions developed in this thesis.

14.1 SUMMARY OF SUPPORT FOR THESIS HYPOTHESES:

	Hypothesis	Treatment
1.5.1	The treatment of property in land is highly varied by different cultures.	Ch. 4
1.5.2	The majority of cultural practices in land may be reduced to common underlying principles relating to the social destination of land income.	Ch. 4
1.5.3	The social destination of land income is an ethic that is linked to a constellation of social ethics capable of being summarised within the notion of solidarity.	Ch. 4
1.5.4	Current Western treatment of land is culturally distinct from the majority of distinct cultural resolutions of property in land.	Ch. 4
1.5.5	The Western notion of property is positive and historically recent.	Ch. 5
1.5.6	The construction of modern market theory is evidence of its reliance on morals.	Ch. 6
1.5.7	Popular sentiment does not support pricing from use value.	Ch. 8
1.5.7.1	Modern market theory is based on a positivist methodology, yet fails positivist tests.	Ch. 6&8
1.5.8	Modern market theory is successful as a species of social psychology.	Ch. 6
1.5.9	Trade is initiated by the desire of the consumer, as final cause of production.	Ch. 9
1.5.10	Pricing by the market is not suitable for natural property	Ch. 9
1.5.11	Commodity use value lifts price above normal costs in current market practice.	Ch. 6 & 9
1.5.12	Price naturally derived from cost.	Ch. 9
1.5.13	Conventional property is priced as the difference between demand and the return to natural property	Ch. 9
1.5.14	Supernormal profit results from the fact that sale is made for utility based prices but production is based on costs	Ch. 9
1.5.15	Land rent is the differential between socially accepted subsistence and net site product. SUPPORTED INDICATING POLITICAL, NOT ECONOMIC SUBSISTENCE	Ch. 10&12
1.5.16	Rents will find equilibrium at levels that absorb marginal productivity.	Ch. 10&12
1.5.17	Rents will find equilibrium at levels that normalise returns to other factors. NOT SUPPORTED	Ch. 10&12
1.5.18	Productivity increases will tend to be absorbed by rents	Ch. 10&12
1.5.19	Land prices are a function of capitalised rents.	Ch. 10&12
1.5.20	Land rents are not derived from land values	Ch. 10&12
1.5.21	In practice, the resolution of the actual level of the subsistence wage is social/political.	Ch. 12&13
1.5.22	The behaviour of productivity (and hence use value) differs between land and products	Ch. 13
1.5.23	Rent taking in land is distinct but related to other (economic) rent taking.	Ch. 13
1.5.24	Supernormal profit, interest on debt, and taxation are all naturally paid out of rent.	Ch. 13
1.5.25	Private property in land is licit subject to social destination of super-normal income.	Ch. 9 & 14

All of the proposed hypotheses for the thesis, except hypothesis 1.5.17 have been supported by this thesis up to this point. Hypothesis 1.5.15 was supported, but not in

Ricardian terms. The combined impact of these two unexpected results has led to rejection of the *natural law* interpretation of Ricardo's rent theory with respect to the setting of the wages line. The results otherwise still support a conclusion regarding behaviour that would be consistent with the identification of an intellectual virtue. Rent formation behaviour appears to follow law-like predictable tendencies consistent with other free human actions. Similar to moral behaviour, this does not suggest deterministic causality, but the operation of reason in evaluating best action in particular situations.

Hypothesis 1.5.25 was supported in Chapter 9 and its support will be further developed in this chapter. The implications for all of the findings to this point will be used to outline an Aristotelian construction of the social economy of land.

14.2 SUMMARY OF CONCLUSIONS TO THIS POINT

It has been shown in Chapter 9 that wages do not suit market determination because the natural property that follows from labour is not a negotiable quantity in the same way that conventional property is. Natural property pertains to life itself, whereas conventional property is a positive privilege that assists human stewardship of natural resources and the realisation of super-material human ends.

Also in Chapter 9 it was shown that title to products could be understood in terms of Aristotelian causality, revealing that although cost-based pricing was natural and economically effective, it could not price the material cause. The material cause, land, could only be priced as the differential between sale of the final product and its wage cost. This appeared to provide a strong ground for the use of the market in determining product price. While the market appears to have thus found a licit place in the operation of the economy, it was shown that the virtue of self-restraint was both necessary for it just operation and conducive to the optimum utilitarian outcome.

The pricing of land was noted to be a function of its necessity, scarcity and varied productivities and Chapters 10, 11, and 12 explored the implications of these aspects of the nature of land on its operation in the economy. Generally, the conclusion from the sum of these chapters was that land did normalise the return to wages (understood to include normal profit) but that the threshold between wages and land rent was set by exogenous factors. The dominant exogenous factors in a liberal efficient market economy were either the existence of a free frontier, or the lowest socially acceptable income sufficient for survival. A free frontier pushed the wages/rent threshold to its maximum level, while the material capacity of working persons to survive provided a lower bound. Historical instances of both cases were cited, especially as they co-existed in the nineteenth century on either side of the Atlantic Ocean.

The experimental investigation of Ricardo's rent theory discussed in Chapter 12 revealed that even in an environment that was expected to return subsistence wages, a slight political advantage enabled tenants to maintain wage levels that were significantly above expectations. This agreed with historical, and other evidence suggesting that factors exogenous to economic forces were the practical means of setting a socially acceptable return to wages. These included public welfare payments for unemployment, minimum wages rates and the pre-Enclosure commons. All of these are ultimately political in nature and follow from the requirement for some social institution to enforce restraint by those whose conventional property rights give them an implicit political advantage.

14.3 SELF-RESTRAINT

The suggestion of restraint of those with conventional property rights resonates with the finding in Chapter 9 that restraint in the market was also beneficial. In that case it was found that although purchasers' needs tended to place them in a politically weaker position in the market, with respect to vendors, the use of their need in setting prices was dysfunctional, unnatural and unjust. Similarly the need of workers for income was shown to necessarily place them in an inferior bargaining position with respect to employers. Despite the need for restraint (that runs counter to the liberal capitalist position) it was argued that external restraint was inappropriate and led to various other problems (which runs counter to the socialist position). Between these extremes was argued self-restraint. This was shown to be consistent with civilised behaviour generally, and therefore befitting the human person and consistent with the ethical capacities of human nature.

While the failure of restraint was shown as problematic in the case of the market, its failure in the case of land is also evident. The evidence from Greece and Rome is too subtle for this thesis, but George's critique of the West's use of land demonstrated the shortcomings of land tenure without responsibility to the community. Rogers was no friend of George, despite being a contemporary and his data on England confirmed George's misgivings better than George himself was able to do.

The argument for self-restraint seems to need a slightly different treatment in the case of land. Many cultures have maintained practices that could be shown to incorporate this virtue, as shown in Chapter 4. However, it would appear that there is a historical pressure that gnaws at that ethic that has often proven to be the undoing of the ethical administration of land property. Feudalism, as it has occurred in its many historical and cultural manifestations, is perhaps the best developed system for the natural administration of land. The land owner, whether it was the emperor of Japan or the king of England, personally owned considerable conventional property, but

accepted responsibility for the application of its revenues for the common good. These applications included the provisions of civic, political, cultural, welfare and religious goods. The emperor's title afforded him considerable power, which was distributed through his vassals. The history of Japan parallels England and many other feudal societies. When the leaders were ethical, the system flourished, but when they succumbed to the temptations available through their power, their personal rewards were short lived and their societies were weakened.

The modern West is built on the rubble of feudalism and maintains a carefully groomed distaste for that system. While this reactionary sentiment is complex and well beyond the scope of this thesis, it should still be acknowledged if a genuinely disinterested social economics of land is to be attempted. While corrupt lords may have been the undoing of an otherwise just and prosperous society, one that Rogers told us had perhaps the best comparative wage justice of the second millennium, this does not betray the system itself. Human frailty appears to be a better choice of culprit. In this light, the modern understanding of property has difficulty asserting its superiority.

This leads back to George. However, with George there is a curious parallel with Marx. Both men recognised the dysfunctions of the economic system that ruled modernity in the nineteenth century. At least they both recognised that it militated against the actual producers in the community and generally weakened the economy for the benefit of a few. Marx saw the employers as the villains, and behind them most of those who inhabited the economy's superstructure. George restrained his criticism to the land owners. It has been shown in this thesis that trade is disordered, which supports Marx and also that the unrestrained private enjoyment of land rent is similarly disordered, that supports George. However, their respective remedies have also been rejected. Despite disliking Marx's socialism, George did not seem to be aware that his remedy was also based on an approach that failed to engage both the capacities and frailties of human nature.

George's land taxation remedy has considerable merit, but it suffers two flaws. Firstly, it ignores other rents and participants in land rent and secondly, far more importantly, it constitutes an attempt at external restraint. External restraint failed for the socialists because it assumes that humans can be effectively restrained *en masse*, and that the restraining agency will be free of the moral flaws that beset the community. In practice it must mean that the state appropriates the powers that are considered unmanageable by individuals without realising that the state is managed by flesh and blood persons with the same frailties. These are political considerations that lead into consideration of the relationship between ethics and the law. It can be argued that the law exists in order to make it easier for a society to practice its shared moral values (Devlin, 1965), to the extent that it has been said that the law does not constrain the

good man. The implications are that the society must actively hold the morals that its laws support. The moral set would appear to be prior. While laws have a place in helping the weak of will, it would seem inadequate in marshalling the behaviour of the entire society. Likewise, if power is concentrated in the machinery of state, then the manipulation of that machinery would appear the reasonable strategy for the same group that otherwise would abuse power elsewhere.

Evidence of the failure of George's remedy in the places where it has taken root in Australia reflect this fundamental flaw. The external restraint implicit in land tax does have some effect, but like the socialist external restraint it fails in the face of the forces that shape the direction of the state. The failure of the rural leaseholds was largely the success of Australia's National Party (formerly the Country Party) which held power in coalition over much of the last fifty years. Without criticising this party, its success in winning a better deal for its supporters (in the form of progressively diminishing real, rural, state rents) is most reasonable, at least in the short term. The tenants elected landlords who would give them a better deal.

Likewise a different interest group was the undoing of state leasehold in the Australian Capital Territory (ACT). As the home of the public servant who administered the leasehold system and distant from the major Australian electorates, rents in the ACT were destined to fall. The rent collectors may not have been the owners, but they had their ear and neither seemed to maintain a clear idea of how the system was supposed to operate. There were also many influential corporate tenants who also did not approve of the arrangement (Brennan, 1971). NSW local rates appear to have suffered similarly, slipping in importance for local government revenue, despite their theoretical benefits. These examples are not meant to be indictments of the parties involved, but merely indications of how external restraint fails when it is not under-pinned by a lively attachment to the ethics that underlie them.

The conclusion here must be that ethical behaviour with respect to land, and all commerce, must be based on a lively attachment to the moral foundations that underlie what can be shown to be just. The moral foundation of economic behaviour was discovered by Aristotle to be the relationships found within the family. These are based on love and expressed in solidarity. St. Bonaventure observed that *"If one does not love one's neighbour, it is not easy to do him justice"* (Langholm, 1992, p. 155). Justice in economics would therefore appear to proceed from solidarity.

14.4 THE JUST WAGE

Ederer (1995) quoted examples of objective evaluations of just wages. His examples were not drawn from the usual industrial relations enquiries into minimum wages which may reflect the way that the apparent resistance to the possibility of a

scientific¹⁴⁰ determination of wages is obscured by political factors. As it was shown in Chapter 10, land rent competes with wages in an apparently zero-sum distribution. While this indicates that the task is objective and possible it does not provide a theoretical structure for the establishment of a just wage.

Through most of this thesis, wages have been associated with cost. This is especially apparent in Chapter 9 where utility and cost were compared as a basis for justice in exchange. This use of the term cost follows common practice in the discussion of price, however it is not strictly true and a theory of the social economy of land requires attention to the real nature of wages. In some cases, the factor inputs for production are genuine costs, irreplaceable raw materials may be consumed which would be a real cost. Labour can be thought of in two ways, either as toil, which is negative, or the purpose of toil, which is income, a positive thing. In some cases the cost of toil is appropriate, especially when the particular tasks are especially onerous. In most cases, a day's work may leave a person weary, which may be argued to be natural, but not spent. For many persons, their work carries some intrinsic reward and provides an income for an activity that may well be their most passionate personal interest. This would appear to be almost cost free labour.

Sen (1981) analysed some of the most humanly costly failures in the history of modern economics and concluded that the absence of a notion of *entitlement* from the political economy of the modern West explained much of the vulnerability of its victims. It has been shown that conscientious intention to participate in the economy is sufficient to generate a licit claim for an income. The shop assistant is paid even when the shop is empty. This leads back to the Aristotelian notion of income and suggests a direction for the resolution of the problem of the just wage.

Aristotle recognised that the end of labour was an income and income was actually the event of living. A larger income means a more comfortable life or its sustenance for longer. Income is the experience of life that one enjoys. Fisher (1930/1977) adopted this understanding on income. Wages are therefore an entitlement to a particular standard of living. Savings make sense in this construction as intended to provide for life sometime in the future¹⁴¹.

The question of the just wage therefore relates to what standard of living the ordinary person is entitled to as a result of the conscientious intention to participate in society. This can be informed by a return to human nature and what is proper to it.

¹⁴⁰The *certain knowledge through cause* science rather than the modern/empiricist type

¹⁴¹A curious feature of this understanding of wages is that wages cease to be a cost, and reveal themselves to be a utility, which places a certain irony behind the debate regarding utility or cost based prices. More usefully, it means that the compromise between demand and supply are both in the same terms, utility which is dimensionally consistent.

All persons come into the world with the properties of human nature. One of these properties is material mortality. People also find themselves in a social context, with parents who immediately communicate certain conventional properties to the person. These may include conventional property, or power. A prince is a human that is born into a particular set of positive circumstances. Removing the conventional properties leaves humanity, material existence and social connection. The argument for conventional property began with the observation that the world, as everything that is not human, is naturally common, even though it may be licitly taken for private ownership.

Connecting this to the social nature of the person means that the person is born with an entitlement to a standard of living of exactly the same basic level as anyone else in the society, unless that person contributes to the society in some extraordinary way. Some of the forms of extraordinary contribution have already been considered, they include extraordinary responsibility, risk, skill/ability and also the reward for extraordinary personal cost outlined above.

14.5 DISTRIBUTION IN PRACTICE

The theoretical distribution by factors, even when constructed through an examination of fractional titles via causality, is not completely adequate in practice. Chapter 13 resolved the various components into wages and items that participated in land rent. Adopting that dissection, the final sale of a consumer good can be subdivided as shown in exhibit 14.1.

Assuming the sale price is a given¹⁴², the major classes of distribution are wages, rents and taxation. It has been argued, following the Ricardian rent theory and an efficient market, that wages will settle on prices somewhere near the minimum capable of sustaining the life of the worker. They will however find some degree of objective stability at this level, ignoring long term political reactions. In practice the minimum is socially determined by forces that are outside of the economy proper. Wages in this context include returns such as risk or responsibility that have been shown to deserve a licit return.

Transient economic rents may be viewed as natural consequences of innovation and development that increase productive efficiency. They may be considered as licit returns to cover investment in these developments. Once development has been paid for, these rents could be expected to dissolve, either through wage increases, or product price reductions. It has been shown that in a liberal free market productivity increases will not remain with ages but will be absorbed by either land or monopolistic/political

¹⁴²Its value can be used as a benchmark for value, which is consistent with wages as an expression of utility.

rents. In the long term, these transient rents will occasionally appear due to change, but may be considered as benign and deserve no further treatment.

If wages are set by survival needs or some social mechanism, then taxation must be taken from rents, although it is only necessary to accept that it comes from non-wage incomes. Taxes are generally accepted as being conventional; they exist as the positive decision of the state to raise income. While they generally operate within the economy, they can be considered to be an exogenously determined component of distribution.

Exhibit 14.1:
Distribution by Wages and Rents

←..... Product Sale Revenue→				
Wages & Normal Profits <i>Set by human capacity to survive or external social/political mechanism</i>	Transient productivity related rents <i>Set by production innovation, provide remuneration for productivity investment</i>	Taxation & donations <i>Taxation conventional; Donations a personal willing of the common good</i>	Monopolistic /Political Rents & Financial Returns <i>Maintained by misuse of power or the acceptance of pure interest</i>	Land Rents <i>Set by demand, necessity of land & varied site productivity - the margin between product price and other factors</i>
Rewards for productivity		Social funding of the common good	Returns to political and conventional power	

All other non-land incomes rents have been grouped together. They may be considered as being derived from three sources, monopolistic control of markets, corporate incomes and the social acceptance of pure interest. These are not mutually exclusive categories. Their importance for the social economy of land is that they represent prior claims on the available non-wage income available in the community. Ultimately they are set by interest rates and power balances within the economy and elsewhere.

Land rents are simply the residual after the rest have been taken. Although they are a residual, they are not politically secondary. The English House of Lords was established as the political representation of land interests. In Australia the Country Party was largely established by the squatters and other rural land owners. Economically, Smith described land as a monopoly. As such it must be able to

maximise its share of distribution. If product sale revenue is fixed, then this must mean normalising the returns to the other groups.

The first two groupings can be seen to relate to productivity. It should be evident that they include the common level of material support for all conscientious members of society, even those who derive the majority of their income from other sources.

The grouping labelled taxation can be broadened to include the funding of all activities that do not contribute to economic production, but do contribute to the common good.

The remaining groupings control the residual share of total income. They are not entitled to them as a result of any natural property. Personal natural property is accounted for by the first two groupings and social realisation of the common good, the second dimension of human nature, is supplied through the third group. The returns to this group result from conventional property and various political and economic powers. They have been shown in Chapter 13 to tend to reinforce themselves through re-investment. It has been shown that the licit destinations of these incomes is actually the social funding of the common good. That chapter also condensed rents into a single function that while appearing similar to Ricardo's land rental function, was actually the summation of all rents. Assuming that transient rents have no significance as long term rents, the rents comprising the summation may be taken as only being perennial rents. The following discussion of the wage threshold problem may be taken to include all perennial rents unless otherwise specified. Policy regarding the social economy of land will generally relate to land rents alone.

Two issues remain from this analysis. The first is the location of the threshold between wage and non-wage incomes (the wages line in Ricardian rental theory), and secondly, social mechanisms for the encouragement of non-wage income towards its licit end.

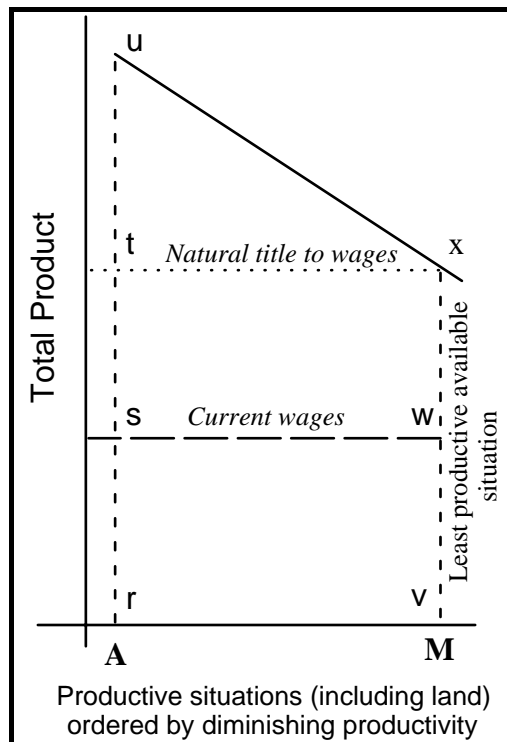
14.6 THE WAGE THRESHOLD PROBLEM

Chapter 10 included discussion of the way that the closing of the frontier caused a rapid transformation of wages from being set by the margin to being set by subsistence. These may be considered to be the upper and lower natural limits of wages. The lower limit has already been discussed exhaustively, but the upper limit deserves a little more attention.

It was observed that wage levels near this limit have been correlated to the rapid economic growth of countries such as the USA. The fact that this situation also has the effects of facilitating a wide distribution of property and a relatively high ratio of wage versus non-wage income appear to be evidence that it is a superior economic situation.

This evidence warrants considerably more development before it could be absolutely convincing.

Exhibit 14.2
The Extent of Natural Title to Wages



The wages line cannot rise above the level set by the margin. This is shown in Exhibit 14.2 as point x. If wages are currently v-w, they could rise as high as v-x and satisfy the criterion of representing the common right of persons¹⁴³. If it were to rise above v-x, then some persons would be denied their common share.

Conventional property can have no power over natural property, because positive law cannot contradict natural law. While it can be shown that the common natural personal property of all persons to income cannot exceed level v-x, there is no apparent reason why it would naturally fall below this level. While other rents may contribute to the increment w-x, land is the most dominant because of its natural and perennial productivity gradient and its necessity for life.

¹⁴³It is important not to lose sight of the fact that wages here does not represent some uniform wage for all persons, but the basic income right that is the natural property of all humans conscientiously willing to be a part of society. Actual individual incomes will vary with risk, responsibility, skill, extraordinary burdens, etc. These loadings are paid out of this total and their settings are the result of a separate set of considerations.

This is not to say that a wages level that provides a basic income based on the line $t-x$ across the entire economy, precludes the application of some of this income to the social realisation of the common good. It does remain the right of the persons who hold the natural title to this income to make these decisions, which is a major change in the political balance that is now generally found. Also, the increase in wages from their present level (along $s-w$ in the exhibit) gives the recipients earnings that could be expected to be invested in productive assets.

Any increase in wages means an equivalent reduction in the value of land. The limiting point x in the exhibit means that the least productive land would have nil private value, similar to the value of frontier land where that has existed. While an increase in wages may be welcomed, the reduction in land values may be expected to be resisted. Regardless of the strategies selected for the final common use of land property, the transition would need to be gentle and well understood. Appendix 5 contains discussion of a proposal for the transition of rents on statutory leaseholds back to their legal levels. In that discussion, a depreciation rate of about 3% is examined on the basis that it equates to the level of depreciation encountered for buildings, which may be reasonably be compared to land. The discussion in the appendix also considers other possibilities and issues. The critical issue is the need to reformulate existing land property parallel to other physical assets, and in so doing set it on a long-term program similar to other physical assets. In this way existing conventional property institutions are respected while still managing an overall transition to a more ethical system.

REVIEW OF SOME PRACTICAL STRATEGIES FOR THE SOCIAL ECONOMY OF LAND

It has been shown in Chapter 9 that the natural destination of income from conventional property is the common good. This confirms the practices found in many cultures with respect to their land property. It has also been shown that this licit application of income from conventional property relies on a widely held ethic based on the relationships within the family. Fundamentally, this suggests that it be only when the values of the family and its operation are publicly embraced, that just treatment in economics will be possible.

This should resonate with the basic theme found behind the neoconservative movement that identifies a distinction between the moral and economic spheres. A precondition for economic order is virtuous intent. Unlike the neoconservative movement, this thesis has found that economic mechanisms, such as the market and land property, have social/political connections that can only be understood in moral terms. Hence, virtuous intent is only a starting point, onto which must be added an

understanding of the social/political implications of economic institutions. Economics is permeated with direct moral significance. It has been found that the Realist/Aristotelian metaphysics provides the methodology for understanding property that is capable of revealing the moral embeddedness of economics.

This clearly points to the importance of further developing and propagating an Aristotelian/Realist social economics as an educational priority. It also points to the necessity for moral education as a foundation to general education and public discourse.

In addition to the fundamental conclusion that just treatment of land will be realised through a general promotion of morality and social economics, specific institutions and public policy do have a necessary place. Throughout this thesis, various strategies for the resolution of the social economy of land have been mentioned. A representative selection will now be reviewed in terms of their strengths, shortcomings and potential contribution to a sound social economy of land.

It should be noted that several of the strategies discussed have little initial apparent connection to property in land. Apart from their significance becoming more apparent on investigation, they illustrate that there are many possible avenues for facilitating the responsible economic use of land property. For this reason it is suggested different communities may adopt different combinations and expressions of policies such as these and all reach the same essential resolution of the property problem.

Land Tax

The transition from transaction based taxes to land tax would provide for the social destination of land rents through the state.

Three shortcomings may be noted as follows:

- 1) If all the income from conventional property was directed to the state, then the funding of important non-economic contributions to the common good, such as cultural, artistic and religious goods would either be constrained, placed under state control, or dependent on the charity of donations from wages. Only about a century or so ago, the government of the USA was making available title to tracts of land to support the funding of universities. In earlier times hospitals were funded the same way, as was the Church. Land tax could centralise State authority over the expression over a variety of other common goods that may not be useful.
- 2) All systems of government appear to be exposed to the human frailties of those who actually manage formal political power. The evidence from Australia suggests that democracy is not a sufficient defence against the political corruption of what may begin as a sound land-tax system.

3) Land tax may be a component institution within a sound social economy, but its traditional omission of concern for other rents has proven to be a shortcoming, especially given the ascendancy of the importance of these rents in recent times.

Land tax in some form appears to be a sound strategy. This thesis has not examined it in great detail, however Appendix 5 illustrates the way that it may be the foundation of a practical resolution of Australia's customary title problem.

There would appear to be some merit in targeting some classes of land use more specifically. For example, commercial and industrial land may be more suitable than agricultural and residential land. Also there may be good reason for differential treatment between owner-occupied land and investment land. These possibilities deserve specific study.

Minimum Wage levels

A variety of methods of setting the basic wage have been attempted. Once it is recognised that the setting of the basic return to labour is a convention that is arithmetically related to land rents, and not necessarily a long term disincentive to corporate profitability, the political terms of its setting are far less constrained. Chapter 13 concluded that the wages line was the result of pressure by various forms of conventional property that necessarily hold the balance of power in the labour market. Chapter 9 had previously shown that the market as an institution leaves labour politically inferior. By contrast, the value of land, capitalised from its rent, originates from the difference between product price and labour cost. Unlike labour, it has no necessary value.

If land has no necessary value, depends on the level of wages, and its loss in value causes no natural harm¹⁴⁴, then an increase in wages means an equivalent reduction in land values. A reduction in land values is a consequence of all measures designed to redirect land income to the common good, so it is not a specific shortcoming of elevated minimum wages.

Two shortcomings of increases in minimum wages may be noted:

- 1) Increases in wage levels could be absorbed as higher consumer spending and a considerable portion of the result are lost off shore as returns to foreign corporations or foreign sourced goods.
- 2) Rapid changes may be disruptive. Like all policy changes, they will be best introduced gradually.

¹⁴⁴Its loss does mean a real loss of income to those accustomed to receiving it. This could be ruinous, especially when debt was used in its procurement.

- 3) With higher wages, the opportunities for inter-occupational anomalies may be expanded.
- 4) Elevated wages may be absorbed by growth in residential land prices. This was one of the major outcomes of family income growth in Sydney between 1970 and 1990.

Practical implementation may follow two principles. The first is gradual implementation, say a growth rate in wages at 1% above economic growth, or set in such a way as to result in a maximum growth in land values of nil.

Probate Taxes

The right to transfer conventional property to one's heirs lies deep in the Western psyche. Providing for one's children is a natural, meritorious, human sentiment, but it may be argued that passing down economic privileges that may concentrate over time does considerably more than provide a comfortable future for one's heirs. It would appear that probate taxes that are set with a high enough starting threshold to provide reasonably for one's dependants would be a reasonable form of taxation. Above a suitable threshold, they could be very progressive without harm.

Probate taxes have the advantages that they have the capacity to return wealth from all forms of conventional property to the community. By operating between generations they are not a disincentive for any individual motivated to provide for himself well through hard work.

Existing probate taxes suffer from the following shortcomings:

- 1) Because the wealthy are both hardest hit and most influential, the resilience of probate taxes to political erosion is poor.
- 2) Through political manipulation, existing wealth thresholds are low, which mean that they militate inordinately against the ordinary person.
- 3) The notion of a wealth tax is abhorrent to some because it implies the forceful socialisation of private property and the fruit of toil. A proper understanding of the nature of property and its use in designing a sensitive taxation strategy could overcome this criticism.

A practical and just probate tax could be designed along the lines outlined above. Because people tend to fall due for the payment of these taxes at random, their benefit could begin without substantial delay. Using Raskall's data¹⁴⁵, it would appear that a death duty that collected half of the wealth of those in the top 10% of the community

¹⁴⁵Presented in Exhibit 13.16.

would return about a third of the country's wealth to the community. The legitimacy of a probate tax depends on the definition of property. Using the modern positive definition it would be removing a licit possession, but using any other cultural definition surveyed in this thesis, or a definition grounded in Aristotelian/Realist metaphysics, it would not. Examination of the current modern understanding of property, as a positive institution largely grounded on possession, reveals that a positive statute effectively reframing conventional property as a life tenure would actually introduce no inconsistencies. The problem of drafting a suitably *leak-proof* statute is a separate issue.

Customary Title

Simple collective title to land would appear to solve the land problem most elegantly; however, they only suit small and relatively uncomplicated societies. Small (1998b) illustrated the way that small customary title units can be integrated into larger communities using land tax as an integrating mechanism. The development of an explicit interpretation of customary title in terms of leasehold rights could solve many of the problems at the interface between customary and Western culture with respect to economic, political and financial issues.

Feudalism

It has been shown that this form of land tenure has found extensive expression throughout the world. It appears to have spontaneously developed the connection between land wealth and the provision of common good. In most instances the leader, whether emperor or tribal chief, holds the land personally on the understanding that he has the responsibility to provide a spectrum of public goods and moral leadership. The failures of feudal systems seem to often result from the failure of their leaders.

An important feature of feudal systems is their tendency to make explicit connection between private property in land and its common use for the good of the community. Aristotle focused on the usefulness of property in land for the way that it facilitated military ends. The Greeks appear to have introduced private property as a strategy to enable citizens to more fully participate in the life of the city, reflecting a confidence that property owners would contribute to the common good of the city.

A key element in the feudal system is the connection between property ownership and civic responsibility. This element is highly important and may be incorporated into Western cultures. It illustrates that wealth is not intrinsically evil. Wealthy families have always existed in most cultures and have often acted in many leadership capacities. The virtue of magnanimity has long been respected in Western thought and

obviously needs a backing of conventional wealth for its exercise. This leads on to the importance of encouraging voluntary contribution to the common good.

The remuneration of the corporation chief executive officers may be interpreted as an example of income linked to leadership responsibilities. Some organisation theory implies the effectiveness of organisational leaders who inspire quality performance. Too much should not be made of this analogy with aristocratic roles, however it does contrast strongly to the shareholders of the same corporations whose income is totally independent of any leadership expectation.

Voluntary contribution

A morally aware society may be expected to be able to voluntarily will the social application of the income from conventional property. West does not immediately appear to reflect this possibility, however it is evident to some extent. The support of a variety of important contributors to the common good is done by individuals. This ranges from the philanthropy of the very wealthy to the humble coins on a plate in a local church.

The disadvantage of relying on voluntary contributions from conventional property is that conventional property tends to concentrate in the hands of persons who do not embrace the ethic of solidarity. This means that some external controls on excessive abuse of conventional property will probably always be necessary

The provision of opportunities for voluntary action is an important and necessary way of respecting human freedom. It also encourages a lively awareness of the issues and values pertaining to freely willing to support others or the common good.

State Leasehold land title

State leasehold title is a strategy that lies midway between comprehensive land taxation and feudal title. Landowners have the private right to the land, but its rent is taken by the state. This title system suits former socialist or feudal systems and has some potential as a means of integrating customary tenure systems into Western development opportunities.

Leasehold title means that the occupier's interest in the land is co-extensive with capital improvements, which links with the Islamic theory of property.

The shortcomings of state leasehold have already been examined and relate to the circularity between citizens as leaseholders and the state as landlord where the former elects the latter.

State leasehold would appear to have potential as a land title system in emerging economies including former socialist countries. It is the title system being adopted in mainland China.

Wide distribution of property

A number of recent Western theorists have recommended policies aimed at the wide distribution of property including Roepke, Chesterton, Dawson, and Tollemache. The notion of making property available in units capable of supporting single working units, eg. family farms, has the advantage of naturally raising the wages line and democratising conventional property.

The disadvantage of promoting wide distribution of property is that it has the habit of re-concentrating. Japan is an outstanding of this. A secondary problem is the difficulty of smaller units of production competing with larger ones and also the problem of the ownership of the land under the operation of large corporations. It could be argued that concurrent strategies aimed at broad stock ownership might solve this problem.

The elevation of the wages line has the effect of returning to working people most of the advantages of property and by lowering the value of property would make it more affordable. It would seem appropriate for all people to have the opportunity to own the land that they use for their home and in many cases the land below their workplace as well. While secure and permanent title to these properties appears sound, the capacity to profit on their purchase and sale by any more than the value of undepreciated improvements would go some distance to undoing the long term effectiveness of such an opportunity.

Owner occupation of property

The limitation of ownership to occupiers is a specific strategy for encouraging its broad ownership. The limitation of prospective purchasers also serves to promote lower land prices and hence greater availability.

The question of pricing and of the social destination of the super-normal returns from conventional property is also not adequately addressed by limiting ownership to occupiers. The system also resonates with the Islamic notion of property and may have potential in a culturally sensitive restructuring of some customary title systems.

Corporate Restructure

The invention of the limited liability company has established a structure for financial association capable of the realisation of virtually unlimited economies of

scale. This has facilitated improvements in productivity that would appear to have been impossible otherwise.

Successful corporations tend to grow. They also tend to absorb smaller corporations. This process has the effect of concentrating ownership and property income.

Corporations are major landowners and the object of their existence is to maximise the wealth of their shareholders. Corporations are significant landowners, with apparently up to 40% of their assets represented by land. Wealth maximisation reflects self-interest and because of the relationship between the corporation and its shareholders, the corporations cannot know the shareholders normal income thresholds. Any initiative that attempts to encourage control of super-normal income will have difficulty with corporate profits. While it may be argued that this may be solved by limiting such measures to individuals, and therefore to shareholders, it then must be accepted that corporate profits must be treated in the same way as land income. This may have further complications if part of the corporate profit is not land-related. This thesis is not intended to study the social economy of corporations or of the closely related question of financial incomes, but it must be recognised that a complete social economy of land must also deal with the connections between corporate income and the land factor.

CONCLUSION

The social economy of land has been shown to proceed from community understanding of the common use requirement of conventional property. This implies two basic issues, the development of a lively community understanding and respect for the issues that underlie just treatment of property and a methodology for the determination of the threshold between personal labour-derived property and common property.

It has been found that the returns to conventional property tend to hold economic, and consequently other forms of power, and they take their share of the available income as a residue after the productive elements in the distribution equation take their share. Despite being a residue, conventional property is dominant in the market and if left alone would reduce wages to minimal levels. The level of wages is set by political or social institutions that are exogenous to the economics of the market. Any gain to wages is a loss to conventional property. Land itself tends to be the residue after other rent-takers and financial interests take their returns, which are themselves determined by the social acceptance of interest rate regimes and other mechanisms that sustain permanent super-normal rents.

Wages were found to naturally follow from the natural property workers have in products. Its extent was shown to follow from the interaction of positive and natural law and suggests a level that would make the least productive available situation rent-free. This would imply the increase in wages and equivalent reduction in land values. Such a transition could only be reasonably attempted slowly and would eventually lead to a considerable reduction in land values. Transition strategies that respect existing institutions were suggested.

A selection of policies for the common use of conventional property have been discussed. All showed some capacity for promoting the sound social economy of land, though most also carried significant shortcomings if relied upon exclusively. Overall, the social economy of land relies on the virtue of solidarity and a social awareness that the just treatment of one's neighbour involves the self-restraint of those who control conventional property such that its use, manifested economically as its rent, is consciously applied to the common good.

Overall, this thesis has demonstrated the effectiveness of Aristotelian/Realist metaphysics and moral methodology for the understanding of social economic issues. It has shown that this methodology is capable of integrating social and economic considerations in a manner that is rationally defensible. Furthermore, it has demonstrated the positive shortcomings of key elements of positive economics and has suggested an alternative that is objective, knowable and conformed to the dignity of human nature. The construction of the social economics of land that this thesis has worked towards is capable of interpreting the property institutions of all cultures studied, though its evaluation of some is less than complimentary. The policy suggestions considered do not infer either the promotion of a single economic model, or the extreme treatment of land property. Persons operating within almost any economic culture can behave in harmony with the principles for economic justice developed in this thesis. All that is required is the intention to will solidarity, and some awareness of the relationships. Many people already do. Although there is considerably more work to do, and these prescriptions are not likely to bring about the revision of the Western property institution within the foreseeable future, they suggest a defensible moral approach to the problem of economics. It is hoped that this line of research can contribute to raising economics from its currently well-deserved title of *the dismal science* to something more befitting human dignity.

Appendix 1 Rental Market Simulation Experiment Facilitator's Notes

Note: These notes are for the general running of a particular session of the simulation. Particular parameters may be varied for particular runs of the simulation.

RUN TIME: 2 HOURS

LAND SUPPLY:

Adjust the supply of land so that some tenants will be forced onto the commons. With all super-marginal land in use 60 subjects are accommodated. If the class size is greater, increase the number of grade 11 lots such that there are at least two more than needed:

$$\text{Number of grade 11 lots} = \text{class size} - 58$$

If the class size is smaller than 60 subtract super-normal *parcels* to leave between 1 & 5 subjects on grade 11 land. (each additional parcel occupies 6 players).

PRELIMINARY

Hand out homework sheets before the class. This will include:

- Text and background
- Homework questions (stress that they must be done before class)
- Tenant's record sheet

At the beginning of class:

- Distribute (homework) answer sheets / tender sheets
- Students to transfer homework answers onto hand-in sheet
- Collect hand-in sheets

PHASE 1: TENDER (OR AUCTION) SALE:

- For Auctions:
 - 1 Call auction beginning with most valuable parcel.
 - 2 Continue from step 6.
- For tender sales:
 - 1 Ask subjects to complete a tender form (homework answers + tender bids + WIMP option).
 - 2 Sort tenders by name.
 - 3 Starting with grade one, call for maximum bid, check with tender sheet (this is faster than finding it yourself).
 - 4 Invite checks that no higher bids have been made.
 - 6 Mark certificate of title (Landlords return sheet), hand to winner and note on overhead summary.
 - 7 Repeat for remaining super-normal parcels.

8 Locate landlords in accessible positions around room.

PHASE 2: RENTAL YEARS 1-4

- Allow 15 minutes for rental negotiation between landlords and prospective tenants to establish rents.
 - >> Ensure everyone is allocated land
 - >> Demonstrate tenants' and land lords' record sheets
 - >> Record rents
 - >> Display rents by land grade and discuss excesses and deficiencies
 - >>> Warn tenants of prospects of poverty
 - >>> Warn Landlords of opportunities missed

Repeat for years 2, 3 & 4

Note: By this time rents should have stabilised and marginal land taken up.

PHASE 3: SHAKE DOWN OF LAND LORDS AND SECOND FOUR YEARS

- Inform class that some land may be taken out of production for infrastructure development leading to improved productivity, such that:
 - >> Some tenants will be forced onto grade 12 land.
 - >> Every lot will be **B20** more productive.
 - (>> *Control group only: capital costs increased by B20, i.e. nil net productivity increase*)
- Invite tenders for **individual** lots of grade 11 land on 4 year pay back terms.
 - Single lot owners assumed to be owner occupiers.
- Check Landlords for solvency.
 - >> Bankrupt any who have not made enough to pay for purchase.
 - >>> *Class break possible at this point <<<*
- Allocate some (3-5) lots to owner occupiers. (these have no further involvement in the market and their data sheets may be collected and the owners given an early mark.
- Take sufficient land out of production from bankrupted players (each parcel adds 6 players to the tenant group), or resume grade 11 lots **to force about 5 tenants onto grade 12** land.
- Inform class of the number of persons relative to supply (i.e. "*X number of players will have to work grade 12 land*")
 - Offer for tender 2 grade 11 lots (if available)

Run for another four years (5-8) or to end of available time.

Appendix 2 Rent Experiment Subject Briefing Notes

>>>> Read notes and attempt questions before class

The next class will be a practical simulation of a rental market. It will explore the behaviour of two sectors which utilise land, tenants and landlords. Students will have the competitive opportunity to locate themselves in the market, with the goal being to find the student who can be the most successful user of land. Success will be measured by amassing surplus wealth.

The exercise will consist of four parts:

- 1) Homework exercise: these notes will be read and the exercises attempted. This should give players a basic familiarity with the market and its processes.
- 2) Auction: Students will be able to bid for parcels of land at auction to become landlords. Land owners must be able to pay off their land out of surplus income over four years or they will be considered bankrupt.
Students who fail to secure land will be able to use land as tenants.
- 3) Leasing and production for years 1 - 4. This will be a critical time for all players to establish a market and for landlords to earn sufficient rental surplus to pay for their land. Landlords will be striving to recover their purchase price while tenants will be striving to find the most competitive rents.
- 4) Leasing and production for years 5 - 8. After the shakedown at the end of year 4 due to some foreclosures, some land owners may disappear and some land will be taken out of use. Other structural changes during this time will make it a turbulent period. Winners will be those who can read and respond to the market and its opportunities rapidly.
- 5) Debriefing: Analysis of the events and the quality of various decisions will be attempted as well as an estimate of the relative success of various players. Learning opportunities during this phase are critical to understanding market behaviour.

It is important that each student reads carefully the notes below in order to be able to make the best commercial decisions in the market.

Assessment: A class mark will be awarded for this exercise, based on the homework questions, and mastery of the market. Bonus marks will be awarded for the best achievers according to the following schema:

- | | |
|--|------------------|
| i) Highest overall amassed wealth | plus four marks |
| ii) Most successful tenant | plus two marks |
| iii) Most successful player at the end of year four | plus two marks |
| iv) Players maintaining at least subsistence level for each year | plus one mark |
| v) Bankrupt landlord at end of year four | minus four marks |
| vi) Tenants closing the exercise with negative amassed wealth | minus two marks |
| vii) Homework | grade out of two |
| viii) Quality of record keeping through exercise | grade out of two |

Where two or more players draw a tie for items (i)-(iv), the bonuses will be three and one marks respectively.

Wipeout Insurance Management Provision Option

Students who are not comfortable with the competitive assessment may opt out of opportunities (i) -(vi) and their grade will rely on items (vii) & (viii) but they will be precluded from bidding for land. Students wishing to take this option should mark the appropriate box on the tender sheet at the beginning of the exercise.

Consider the assessment carefully, prudent players should have no difficulty earning 5 marks towards their final assessment {items (iv,vii &viii)}. Ambitious property

players may earn additional bonuses (i)-(iii) of up to six additional marks. This has the potential to significantly improve your end of year result. Caution is necessary to avoid items (v) & (vi).

The Economy:

There are only two sectors in the economy, tenants and landlords. Productivity is uniform for each grade of land and all production is for sale.

The currency unit will be bags of gold (**B**). All costs and revenues are annual amounts.

The land must be worked using capital equipment that will require an annual service cost of **B20**. Any product above this is available as either wages or rent.

Each person requires a personal consumption of **B30** to live at a subsistence level, any additional income may be saved as amassed wealth.

Landlords obtain income through charging rent. Any amount received above their subsistence costs will be saved as amassed wealth (savings for year equals total rent less **B30**). They must pay for the land they buy out of their amassed wealth.

Tenants obtain income as the remainder after working the land and paying for rent and capital costs. (Income = product - rent - capital expenses). Savings for the year will be income less **B30**.

The land is divided into 13 grades. Grade 1 land is the most productive, while grade 13 land will not support subsistence.

The available land is shown in the table below:

Table 1

Grade	Parcels	Lots	Product	<i>Max. Rent</i>	<i>Max. bid</i>	
1	1	5	150			
2	1	5	140			
3	1	5	130			
4	1	5	120			
5	1	5	110			
6	1	5	100			
7	1	5	90			
8	1	5	80			
9	1	5	70			
10	1	5	60			
11	<i>state</i>	10	50			
12	<i>state</i>	10	45			
13	<i>state</i>	10	40			

There is only one parcel of each of the grades 1-10 and these will be sold by tender by the state at the beginning of the exercise. Depending on the number participating, not all parcels will be sold causing at least one tenant will necessarily have to occupy land of grades 11-13.

Grade 11 land produces only **B50** which is only sufficient to service the costs of capital equipment and wages. Because a tenant could not work grade 11 land and afford to pay rent without living below subsistence, this land is state commons and available at no charge to anyone who may want to use it. The state also owns all the

grade 12 & 13 land which is also available to anyone who may wish to use it, on similar conditions.

The supply of common land is limited and it may be absorbed over time for public works (infrastructure), or released onto the private market as the state sees fit for the common good.

There are so many people in the society that all the land including some grade 11 lots will be used. This means that some people will be occupying land that produces no surplus above the requirements of wages and capital, but on which the state charges no rent. There is sufficient land at grade 11 that no one should need to use grade 12 land in the first year at least.

The labour involved in working a single lot represents the full time occupation of a working family. Landlords are wholly devoted to the administration of their portfolios and do not work land.

Tenants who fail to secure a lot in any year will be deemed public paupers and given **£15** by the state as welfare support.

Untenanted land is fallow, has no product and earns its owner no income.

Bidding for land

Each parcel will consist of five lots of equal productivity. Different parcels will consist of land of different productivity. As there is good market knowledge, the productivity of each parcel is known to all.

It is believed that being a landlord is less arduous and potentially more profitable, hence it may be expected that the tendering will be quite competitive. Landlords must pay for their land out of surplus income in the first four years of ownership. Failure to pay for land in four years will result in its forfeiture without compensation. Bankrupted landlords become tenants and may not bid for land again.

Prospective tenderers must calculate their bids for each parcel prior to the exercise. This will depend on estimates of the rental income of the parcels. If an estimate is too low, it will be outbid. If the estimate is too high, the 'winner' will pay too much for the land and will not be able to realise the necessary rental income, leading to bankruptcy.

You may enter tenders for all parcels but may only own one. Tenders will be let, beginning with the most productive land. On winning a parcel, no further bids from that winning tenderer will be considered. Bidders who fail to obtain land will become tenants. In the case of tied maximum bids, tenderers may withdraw, otherwise random selection will be made.

Maximum bid computation example: An investor is considering the purchase of a parcel of 5 grade 3 lots. She assumes a rental of **£70** per lot. Her net surplus income is computed below to be **£320** per annum, as shown:

Table 2

Grade of land:		3
	Gross product per lot	130
	<i>estimated rental income</i>	70
(x5=)	<i>total rental income</i>	350
	Less Subsistence costs	30
	<i>surplus wealth</i>	320
(x4=)	<i>maximum bid price</i>	1280

Such an investor could bid a maximum of **B1,280** for the parcel and pay off the parcel in four years if she manages to realise her estimated rent.

Landlords

Landlords must obtain sufficient rental income to pay off the purchase price of their land in four years, or they will be bankrupted and their land forfeited to the state. Any surplus will be counted as savings, or amassed wealth. Once the land is paid for all rental is available to the landlord.

Tenants

Tenants lease land on a strictly annual basis. They use the land for its highest and best use, and realise the product listed for the particular grade of land. Full market knowledge is available, so all tenants have the knowledge to fully utilise the land. From their product they must then pay rent (which is negotiated annually with the landlord) and also pay for the use of capital equipment, a fixed annual amount of **B20**. The remainder is their income.

A personal consumption of **B30** is required for reasonable subsistence. Any surplus will be saved as amassed wealth. Where income is below **B30**, the entire amount will be consumed. A personal consumption level of **B25** is considered a survival level only, while levels **B20** and below would warrant some form of supplement, such as through begging.

For Example: the annual personal income of a person occupying grade 3 land and paying **B70** in rent will be calculated as follows:

Table 4

Grade of land:		3
	Gross product	130
Less	Rental	70
	<i>income after rent</i>	60
Less	Capital costs	20
	<i>gross personal income</i>	40
	Subsistence costs	30
	<i>net surplus income</i>	10

This person has a reasonable personal consumption level and savings of **B10** for the year.

Rental markets years 1-4:

Once the land has been taken up, time will be allowed for tenants to negotiate rents with landlords for the first year (15 minutes). These will be recorded, displayed and briefly discussed.

Tenants will then be able to negotiate rents for year 2. There is no compulsion for tenants to stay on any particular site. Rents for year 2 will be recorded, displayed and briefly discussed.

Years 3 & 4 will be similarly treated.

At the end of year four landlords will be held to account for the cost of their purchase. Any landlords who fail to pay for their parcel will be bankrupted and forfeit their holdings.

Years 5 and following:

At the beginning of year five the state may decide to do any, or all of the following:

- Auction, or otherwise alienate any defaulted land if it considers such would be in the interests of the common good.
- Give tenants the opportunity to bid for some individual lots of grade 11, 12 or 13 land. If this is done, these purchases must also be paid for out of net surplus income over the following four years. Sale of these grades will be strictly on the basis of single lot parcels.
- Withdraw forfeited land or parts of the commons for infrastructure use. Public infrastructure development, if undertaken, will increase productivity across the board and new data will be displayed as appropriate.

Tenants will then seek annual leases for year five and the exercise will continue for a further four years, similar to years 1-4.

ANSWER THE FOLLOWING QUESTIONS BEFORE CLASS:

- 1) Why will no one occupy any grade 12 land while there is grade 11 land available?

- 2) What is the *net surplus income* for a tenant occupying a grade 6 lot and paying a rent of **B55**? _____
- 3) Would the tenant in question 2 be better off on the commons? _____
- 4) What would be the net surplus income of a landlord who is able to lease all of his five lots of grade 6 land at a rental of **B55**? _____
- 5) Assuming that there was common land available at grade 11, would the landlord in question 4 have any tenants? _____
- 6) What is the maximum rent that the landlord in question 4 can ask before his tenants begin to move onto the commons? _____
- 7) A land investor is considering his bidding strategy for a parcel of five lots of grade 6 land. He assumes a rental of **B45**. What is his maximum bid? _____
- 8) >>>> *In the blank spaces provided in table 1:*
- (i) estimate the maximum rental that could be charged before driving tenants onto the commons and
- (ii) compute the maximum bids for each of the parcels.
- 9) If land is taken out of production some tenants may be forced onto grade 12 land.
- i) How will rents be affected? _____
- ii) In the situation outlined in question 9, would it be in the interests of tenants of grade 11 commons to secure their tenure? _____
- iii) What price could be expected for grade 11 land in this situation? _____
- 10) By how much would tenants' net income (after capital costs and rent) increase if productivity on a particular grade of land were to increase by **B15**? _____

Appendix 3 Rental Experiment Record Forms

Class Summary Sheet

Used on an overhead projector to track rental through the experiment as feedback to participants.

Total Net surplus income by year

Parcel 1 Grade	Lots	1	2	3	4	Price	Total	Net Profit	5	6	7	8	9
1	5												
2	5												
3	5												
4	5												
5	5												
6	5												
7	5												
8	5												
9	5												
10	5												
11													
12													
13													

Average Rental per parcel

Grade	Marg. Rent	1	2	3	4	Prod- uct	Marg. income pa	Marg. bid	5	6	7	8	9
1	100					150	470	1880					
2	90					140	420	1680					
3	80					130	370	1480					
4	70					120	320	1280					
5	60					110	270	1080					
6	50					100	220	880					
7	40					90	170	680					
8	30					80	120	480					
9	20					70	70	280					
10	10					60	20	80					
11	0					50							
12	-5					45							
13	-10					40							

LANDLORD'S RECORD SHEET

Certificate of title and rental record, completed by landlords with annual data summarised onto class summary sheet.

Landlord's Annual return sheet																					
<table border="1" style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 33%;">Price</td> <td style="width: 16.5%;">Grade:</td> <td style="width: 50.5%;">Product</td> </tr> <tr> <td> </td> <td> </td> <td> </td> </tr> </table>			Price	Grade:	Product				<table border="1" style="width: 100%; border-collapse: collapse;"> <tr> <td colspan="2">Owner:</td> </tr> <tr> <td colspan="2">Student No:</td> </tr> <tr> <td>Class:</td> <td>Date:</td> </tr> </table>							Owner:		Student No:		Class:	Date:
Price	Grade:	Product																			
Owner:																					
Student No:																					
Class:	Date:																				
Year	1	2	3	4	5	6	7	8	9												
Rental lot 1	Tenant**																				
	Rent																				
Rental lot 2	Tenant																				
	Rent																				
Rental lot 3	Tenant																				
	Rent																				
Rental lot 4	Tenant																				
	Rent																				
Rental lot 5	Tenant																				
	Rent																				
Total Rental																					
Less subsistence																					
Net surplus income																					
Gross amassed wealth=					Amassed wealth years 5-end=																
less cost of aquisition=					Add net amassed from year 4																
net amassed wealth=					<i>Total</i>																
Average rental *																					

* Average rental is the total rental divided by number of lots leased (five normally).

** Note tenant's name as <Given name><Surname initial>.

TENANT'S RECORD SHEET

Completed by tenants to track accuracy and for final awards.

<h2 style="margin: 0;">Tenant's Annual return sheet</h2>		Name: _____						
		Student # _____	Class _____					
		Date: _____						
Year	1	2	3	4	5	6	7	8
Grade								
Product								
less rental								
net product								
Less capital cost								
gross income								
Less subsistence								
Net surplus income								
	total net surplus years 1-4 =				Total net surplus years 5-8=			
				Surplus yrs. 1-4 b/f:			
	(grade 11 acquisition cost)* <input style="width: 50px; height: 20px;" type="text"/>				total amassed wealth			
					=====			
Comments								

*if commons purchased

Appendix 4 Rental Market Simulation Experiment Results by Run

16553 1999 Final Run 1

No. Parcels:	6
Prod. Inc.	10
Fixed costs	20
Subsistence:	30

Notes: 5 years 33 subjects
 Tenant cartel suspected by landlords
 Net productivity increase of B10 after year 4
 Collusion evident @ parcel #6
 B50 commons available after yr.4
 Parcels sold by tender

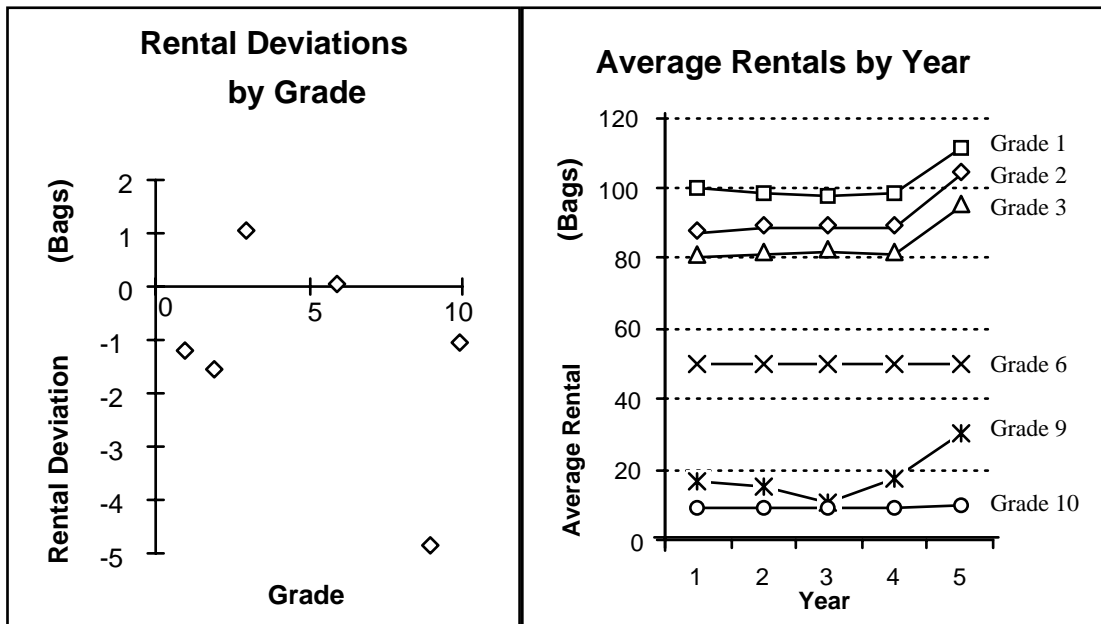
	Bid Price	4 year Earnings	Profit /Loss	Gross Parcel Rents					lots let					
				1	2	3	4	5	1	2	3	4	5	
1	1880	1559.5	(321)	500	492	490.	197	556	5	5	5	2	5	
2	1680	1559	(121)	435	355	445	444	311	5	4	5	5	3	
3	1480	1092.5	(388)	400	324.5	164	324	285	5	4	2	4	3	
6	880	880	0	250	250	250	250	250	5	5	5	5	5	collusion evident
9	280	153	(127)	83	75	43.5	71.5	150	5	5	4	4	5	
10	80	40.5	(40)	27	45	44.5	44	51	3	5	5	5	5	

*Parcels 4,5,7, & 8 not released

	Gross Product		R* Rent	Average Rentals					Rentals above Rational					average	
	yr.1-4	yr 5+		1	2	3	4	5	1	2	3	4	5	yr1-4	5+
1	150	160	100	100	98.4	98.1	98.5	111.2	0.0	-1.6	-1.9	-1.5	11.2	98.8	111.2
2	140	150	90	87.0	88.8	89.0	88.8	103.7	-3.0	-1.3	-1.0	-1.2	13.7	88.4	103.7
3	130	140	80	80.0	81.1	82.0	81.0	95.0	0.0	1.1	2.0	1.0	15	81.0	95.0
6	100	110	50	50.0	50.0	50.0	50.0	50.0	0.0	0.0	0.0	0.0	0	50.0	50.0
9	70	80	20	16.6	15.0	10.9	17.9	30.0	-3.4	-5.0	-9.1	-2.1	10	15.1	30.0
10	60	70	10	9	9	8.9	8.8	10.2	-1.0	-1.0	-1.1	-1.2	0.2	8.9	10.2

R* Rent is the theoretical rational rents based on subsistence income to tenants

Mean yrs.1-4:	-1.3	-1.2	-1.3	-1.9	-0.8	8.3
as pop.est.=	2.15	1.58	2.07	3.81	1.13	6.63
of pop.=	2.25	of yr.5 pop.=				6.05



16150 Final Run 2
1999

No. Parcels:	9
Prod. Inc.	0
Fixed costs	20
Subsistence:	30

Notes:
5 years 58 subjects
Nil net productivity increase after year 4
Fixed (capital) costs = 20
Collusion evident, especially in parcel #2
Parcels sold by tender

	Bid Price	4 year Income	Prof it / Loss	Gross Parcel Rents					lots let					
				1	2	3	4	5	1	2	3	4	5	
1	1880	1866	(14)	492	498	498	498	497	5	5	5	5	5	collusion evident collusion evident
2	1680	1680	0	450	450	450	450	250	5	5	5	5	5	
3	1480	1480	0	398	398	402	402	373	5	5	5	5	5	
4	1280	1273.0	-7	347.5	345.0	347.5	353	349	5	5	5	5	5	
5														
6	880	864	(16)	248	246	243	247	250	5	5	5	5	5	Yr.5:maverick tenant
7	680	623	(57)	157	186	195	205	230	4	5	5	5	5	
8	460	464	4	144	145	148	147	146.5	5	5	5	5	5	
9	220	264.5	45	95	99.5	95	95	95	5	5	5	5	5	
10	60	60	0	46	45	44.5	44.5	51	5	5	5	5	5	

Grade 5 parcel not released

	Gross Product		R* Rent	Average Rentals					Rentals above Rational					Average s		
	1-4	5+		1	2	3	4	5	1	2	3	4	5	yr1-4	5+	1-4
1	150	150	100	98.4	99.6	99.6	99.6	99.4	-1.6	-0.4	-0.4	-0.4	-0.6	99.3	99.4	0.52
2	140	140	90	90	90	90	90	50	0.0	0.0	0.0	0.0	-40	90.0	50	0.00
3	130	130	80	79.6	79.6	80.4	80.4	74.6	-0.4	-0.4	0.4	0.4	-5.4	80.0	74.6	0.40
4	120	120	70	69.5	68.99	69.5	70.6	69.8	-0.5	-1.0	-0.5	0.6	-0.2	69.6	69.8	0.59
6	100	100	50	49.6	49.2	48.6	49.4	50	-0.4	-0.8	-1.4	-0.6	0	49.2	50	0.37
7	90	90	40	39.25	37.2	39	41	46	-0.8	-2.8	-1.0	1.0	6	39.1	46	1.35
8	80	80	30	28.8	29	29.6	29.4	29.3	-1.2	-1.0	-0.4	-0.6	-0.7	29.2	29.3	0.32
9	70	70	20	19	19.9	19	19	19	-1.0	-0.1	-1.0	-1.0	-1	19.2	19	0.39
10	60	60	10	9.2	9	8.9	8.9	10.2	-0.8	-1.0	-1.1	-1.1	0.2	9.0	10.2	0.12

R*Rent: Rational maximum rent vide Ricardian rent theory

Mean yrs.1-4:	-0.6	-0.7	-0.8	-0.6	-0.2	-4.6
as pop.est.=	0.66	0.48	0.83	0.58	0.73	13.57
of pop.=	0.69	std.Dev yr.5 pop.=				12.80

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16150 Final
 1999 Run 2

No. Parcels:	9
Prod. Inc.	0
Fixed costs	20
Subsistence:	30

Notes:
 5 years 58 subjects
 Nil net productivity increase after year 4
 Fixed (capital) costs = 20
 Collusion evident, especially in parcel #2
 Parcels sold by tender

	Bid Price	4 year Income	Profit / Loss	Gross Parcel Rents					lots let				
				1	2	3	4	5	1	2	3	4	5
1	1880	1866	(14)	492	498	498	498	497	5	5	5	5	5
2	1680	1680	0	450	450	450	450	250	5	5	5	5	5
3	1480	1480	0	398	398	402	402	373	5	5	5	5	5
4	1280	1273.0	-7	347.5	345.0	347.5	353	349	5	5	5	5	5
5													
6	880	864	(16)	248	246	243	247	250	5	5	5	5	5
7	680	623	(57)	157	186	195	205	230	4	5	5	5	5
8	460	464	4	144	145	148	147	146.5	5	5	5	5	5
9	220	264.5	45	95	99.5	95	95	95	5	5	5	5	5
10	60	60	0	46	45	44.5	44.5	51	5	5	5	5	5

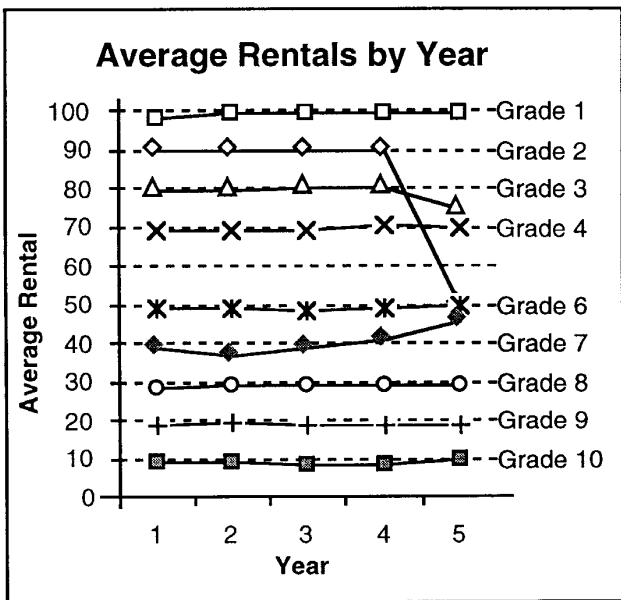
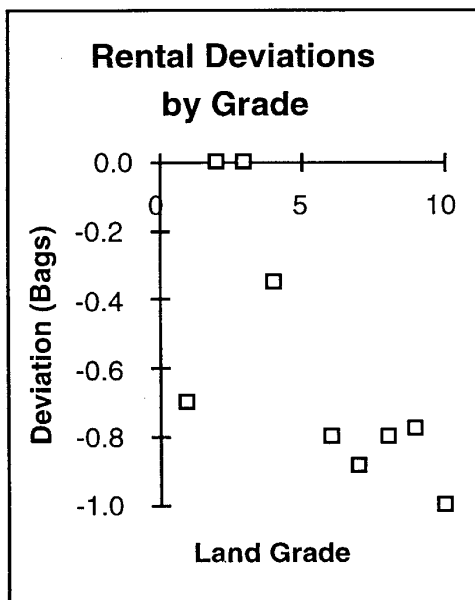
collusion evident
 collusion evident
 Yr.5:maverick tenant

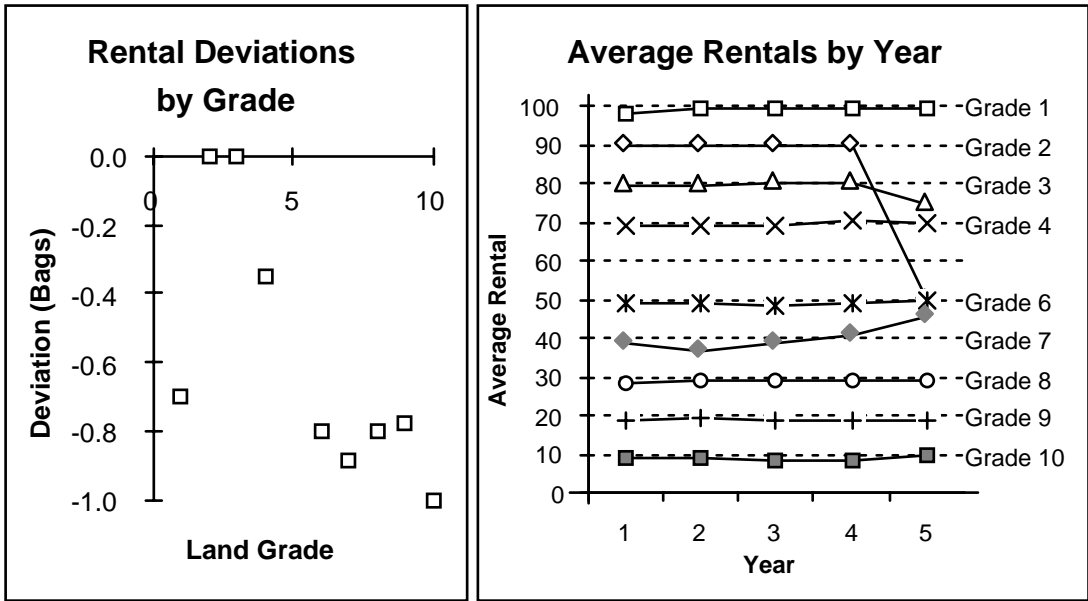
Grade 5 parcel not released

	Gross Product		R* Rent	Average Rentals					Rentals above Rational					Average		s
	1-4	5+		1	2	3	4	5	1	2	3	4	5	yr1-4	5+	
1	150	150	100	98.4	99.6	99.6	99.6	99.4	-1.6	-0.4	-0.4	-0.4	-0.6	99.3	99.4	0.52
2	140	140	90	90	90	90	90	50	0.0	0.0	0.0	0.0	-40	90.0	50	0.00
3	130	130	80	79.6	79.6	80.4	80.4	74.6	-0.4	-0.4	0.4	0.4	-5.4	80.0	74.6	0.40
4	120	120	70	69.5	68.99	69.5	70.6	69.8	-0.5	-1.0	-0.5	0.6	-0.2	69.6	69.8	0.59
6	100	100	50	49.6	49.2	48.6	49.4	50	-0.4	-0.8	-1.4	-0.6	0	49.2	50	0.37
7	90	90	40	39.25	37.2	39	41	46	-0.8	-2.8	-1.0	1.0	6	39.1	46	1.35
8	80	80	30	28.8	29	29.6	29.4	29.3	-1.2	-1.0	-0.4	-0.6	-0.7	29.2	29.3	0.32
9	70	70	20	19	19.9	19	19	19	-1.0	-0.1	-1.0	-1.0	-1	19.2	19	0.39
10	60	60	10	9.2	9	8.9	8.9	10.2	-0.8	-1.0	-1.1	-1.1	0.2	9.0	10.2	0.12

R*Rent: Rational maximum rent vide Ricardian rent theory

Mean yrs.1-4:	-0.6	-0.7	-0.8	-0.6	-0.2	-4.6
σ as pop.est.=	0.66	0.48	0.83	0.58	0.73	13.57
σ of pop.=	0.69	std.Dev yr.5 pop.= 12.80				





16150 1997 Pilot 1

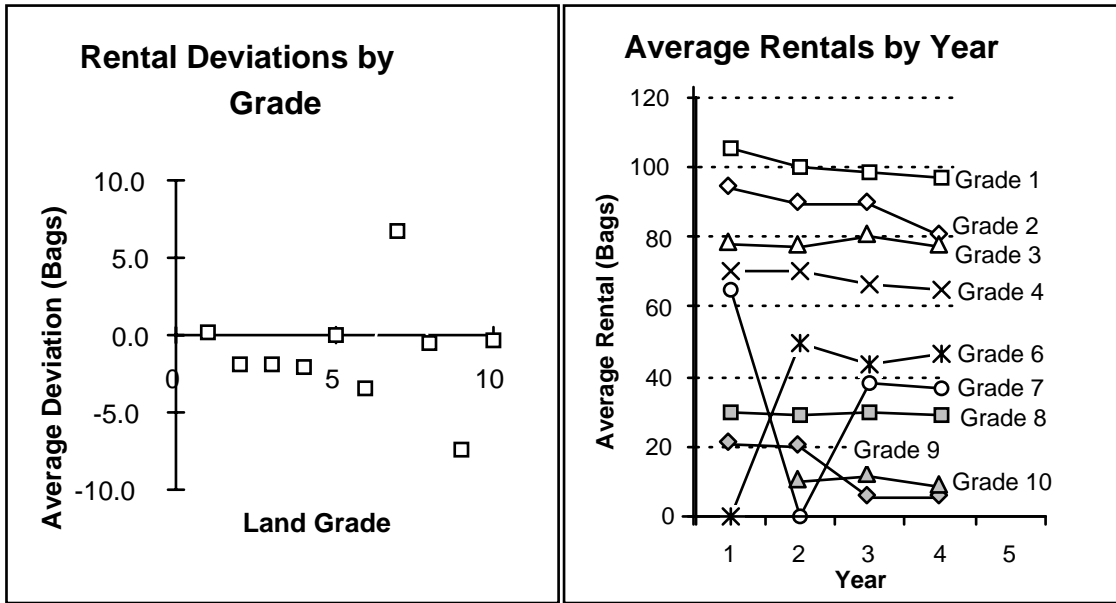
Notes: 4 years 59 subjects
 Considerable reliance on the commons
 No variation in productivity
 Parcels auctioned

No.Parcels:	9
Prod. Inc.	0
Fixed costs	20
Subsistence	30

	Bid Price	4 year Earnings	Profit / Loss	Gross Parcel Rents					lots let				
				1	2	3	4	5	1	2	3	4	5
1	1950	1482	(468)	525	100	492	485		5	1	5	5	
2	1815	1563	(252)	469	446	448	320		5	5	5	4	
3	1700	1442	(258)	388	387	402	385		5	5	5	5	
4	1626	1442	(258)	210	350	332	325		3	5	5	5	
5													
6	1420	491.2	(929)	0	248.	129.5	233.		0	5	3	5	
					5		2						
7	1323	491.2	(929)	325	0	192	183		5	0	5	5	
8	1040	491.2	(929)	150	145	147.5	145		5	5	5	5	
9	610	131	(479)	101	100	25	25		5	5	5	5	
10	290	24.5	(266)		49.5	55	40			5	5	5	

	Gross Product		R* Rent	Average Rentals					Rentals above Rational					Ave.	
	1-4	yr 5+		1	2	3	4	0	1	2	3	4	0	1-4	1-4
1	150	150	100	105	100	98.4	97		5.0	0.0	-1.6	-3.0		100.1	3.02
2	140	140	90	93.8	89.2	89.6	80		3.8	-0.8	-0.4	-10.0		88.2	5.04
3	130	130	80	77.6	77.4	80.4	77		-2.4	-2.6	0.4	-3.0		78.1	1.35
4	120	120	70	70	70	66.4	65		0.0	0.0	-3.6	-5.0		67.9	2.21
5	110	110													
6	100	100	50		49.7	43.2	46.			-0.3	-6.8	-3.4		46.5	2.67
					6										
7	90	90	40	65		38.4	36.		25.0		-1.6	-3.4		46.7	12.98
					6										
8	80	80	30	30	29	29.5	29		0.0	-1.0	-0.5	-1.0		29.4	0.41
9	70	70	20	20.2	20	5	5		0.2	0.0	-15.0	-15.0		12.6	7.55
10	60	60	10		9.9	11	8			-0.1	1.0	-2.0		9.6	1.24

Mean yrs.1-4:	-1.4	4.5	-0.6	-3.1	-5.1	
as pop.est.=	4.96	9.38	0.90	5.04	4.52	
of pop.=	6.37					



16150 1998 Pilot Run 2

Notes: 7 years 55 subjects Parcels Auctioned

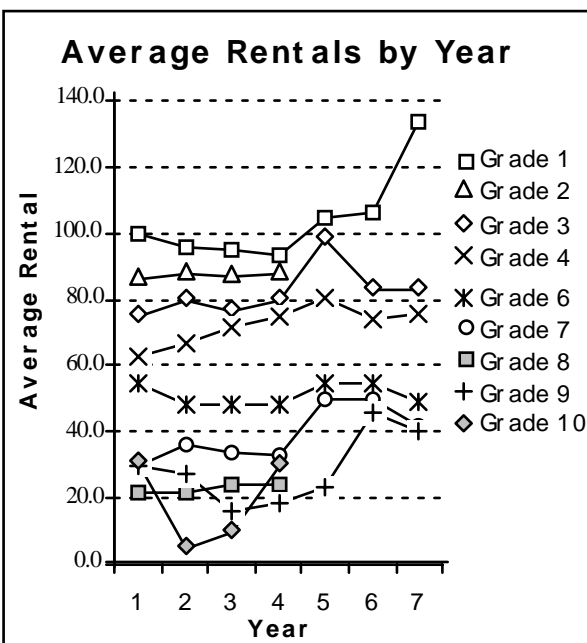
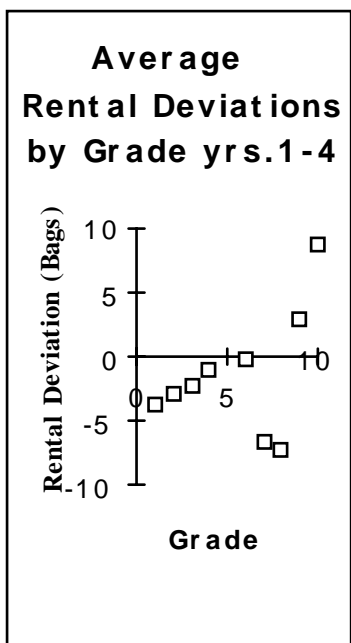
No. Parcels:	9/6
Prod. Inc.	10
Fixed costs	20
Subsistence	30
:	

Some parcels removed @ yr.5 Soft reward structure
 Tenants forced to grades 12 & 13 (B45 & B40)
 Implicit margin level depressed B10
 note wide std.deviation in all years

	Bid Price	4 year Earning	Profit /Loss	Gross Parcel Rents							lots let						
				1	2	3	4	5	6	7	1	2	3	4	5	6	7
1	1920	1806	(114)	500	481	477	468	525	530	670	5	5	5	5	5	5	5
2	1790	1622	(168)	430	440	434	438				5	5	5	5			
3	1720	1436	(284)	375	398	383	400	197	416	415	5	5	5	5	2	5	5
4	1655	1260	(395)	315	332	358	375	403	370	380	5	5	5	5	5	5	5
5																	
6	1586	876	(710)	275	240	240	241	273	275	247	5	5	5	5	5	5	5
7	1215	373	(842)	119	73	135	166	250	250	210	4	2	4	5	5	5	5
8	855	336	(519)	107	109	120	120				5	5	5	5			
9	510	185	(325)	120	81	48	56	115	230	201	4	3	3	3	5	5	5
10	370	181	(189)	123	20	38	120				4	4	4	4			

	Gross Prodct		R* Rent	Average Rentals							Rentals above Rational						
	yr.1-4	yr.5+		1	2	3	4	5	6	7	1	2	3	4	5	6	7
1	150	160	100	100.0	96.2	95.4	93.6	105	106	134	0.0	-3.8	-4.6	-6.4	5	6	34
2	140	150	90	86.0	88.0	86.8	87.6				-4.0	-2.0	-3.2	-2.4			
3	130	140	80	75.0	79.6	76.6	80.0	98.5	83.2	83	-5.0	-0.4	-3.4	0.0	18.5	3.2	3
4	120	130	70	63.0	66.4	71.6	75.0	80.6	74	76	-7.0	-3.6	1.6	5.0	10.6	4	6
6	100	110	50	55.0	48.0	48.0	48.2	54.6	55	49.4	5.0	-2.0	-2.0	-1.8	4.6	5	-0.6
7	90	100	40	29.8	36.5	33.8	33.2	50	50	42	-10.3	-3.5	-6.3	-6.8	10	10	2
8	80	90	30	21.4	21.8	24.0	24.0				-8.6	-8.2	-6.0	-6.0			
9	70	80	20	30.0	27.0	16.0	18.7	23	46	40.2	10.0	7.0	-4.0	-1.3	3	26	20.2
10	60	70	10	30.8	5.0	9.5	30.0				20.8	-5.0	-0.5	20.0			

Mean yrs.1-4:	-1.4	0.1	-2.4	-3.2	0.0	8.6	9.0	10.8
as pop.est.=	6.30	10.15	4.15	2.54	8.36	5.73	8.64	13.55
of pop.=	6.77	mean yr. 5-7=		9.47	; 9.04			



16152 1998 Pilot Run 3

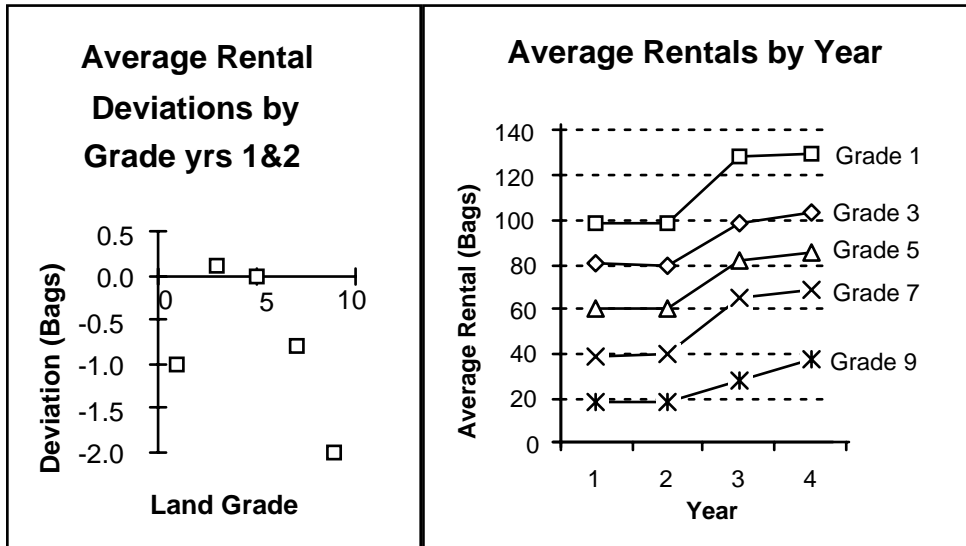
Notes: 4 years 34 subjects
 Productivity increased by B30 year 3
 Fixed (capital) costs = 30
 Parcels sold by tender with prospect of prod. increase

No. Parcels:	6
Prod. Inc.	30
Fixed costs	30
Subsistence:	30

	Bid Price	4 year Earnings	Profit /Loss	Gross Parcel Rents				lots let			
				1	2	3	4	1	2	3	4
1	2800	2164	(636)	495	495	646	648	5	5	5	5
2											
3	2080	1690	(390)	402.5	398.5	493	516	5	5	5	5
4											
5	1900	1319	(581)	300	300	412	427	5	5	5	5
6											
7	1080	942	(138)	195	197	325	345	5	5	5	5
8											
9	780	386	(394)	91	89	138	188	5	5	5	5
10											

	Gross Product		R* Rent	Average Rentals					Rentals above Rational					Average	
	yr.1/2	yr 3/4		1	2	3	4	5	1	2	3	4	5	yr1-2	3-4
1	160	190	100	99	99	129.2	129.6		-1.0	-1	29.2	29.6		99.0	129.4
2	150	180													
3	140	170	80	80.5	79.7	98.6	103.2		0.5	-0.3	18.6	23.2		80.1	100.9
4	130	160													
5	120	150	60	60	60	82.4	85.4		0.0	0	22.4	25.4		60.0	83.9
6	110	140													
7	100	130	40	39	39.4	65	69		-1.0	-0.6	25.0	29.0		39.2	67.0
8	90	120													
9	80	110	20	18.2	17.8	27.6	37.6		-1.8	-2.2	7.6	17.6		18.0	32.6
10	70	100													

Mean yrs.1/2:	-0.7		-0.7	-0.8	20.6	25.0
as pop.est.=	0.88		0.91	0.86	8.21	4.88
of pop.=	0.84		of yr.3/4		6.43	
			pop.=			



Appendix 1 Publications by the Author Related this Thesis

Several chapters or parts of chapters in this thesis have been adapted from existing conference papers and journal articles by the author as follows.

The entire Chapter Two, dealing with cultural practices in land, was presented in Auckland, New Zealand as (Small 1997a) and later revised and published as (Small 1997b). A development of the conclusions from that work, integrating the general conclusions of this thesis was presented as a policy strategy in Perth, Western Australia as (Small 1998b).

The critique of Market theory (Chapter 6) and the metaphysical construction of product title rights (Chapter 9) comprised a paper presented at Steubenville, USA as (Small 1998a). The critique of market theory leading to the conclusion that market theory is successful social psychology from that paper revised and is currently under review for publication in the Catholic Social Science Review.

The treatment of infrastructure in Chapter 13 has been drawn from work found in (Small 1997c; Small 1999a; Small et al. 1996). The argument regarding the long term economics of fertility restraint was presented at Steubenville, USA as (Small 1997e). It was revised has been published as (Small 1997f).

Chapters 11 and 12, the experimental study of Ricardo's rent theory were presented as a single paper as (Small 1999b) in Sydney focusing on its experimental validity and later a revised version with analysis similar to that found in Chapter 12 was presented at Cambridge, UK as (Small and Oluwoye 1999). A shorter version is being prepared for publication.

It was the author's original intention to include a more complete treatment and analysis of policy options following the conclusions in Chapter 14. This was to have been done by adding as appendices (Small 1997d; Small 1998b; Small 1999a; Small et al. 1996). However, it is considered that the length of the present work prohibits such addenda.

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