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Viewpoint: Compound growth and land: what are the implications for planning?

Matthew Cocks

Introduction

The significant property price rises seen in the UK since the mid-1990s are part of a wider global trend and whilst the issue is frequently presented as one of house price rises the explanation for the phenomenon lies largely in increasing land values. Land values are rising across both urban and rural land in many parts of the world. In a recent study, Knoll *et al* (2014) examined house price rises in 14 advanced economies since 1870. They found that real house prices stayed constant from the 19th to the mid-20th century, but rose distinctly during the second half of the 20th century, and particularly since the 1980s. Their analysis suggests that rising land values explain around 80% of the house price rises which were witnessed in those countries during this period; in contrast to other possible explanatory factors, such as materials and labour costs. Rural land has also seen significant rises. For example, the Royal Institute of Chartered Surveyors (RICS) reported in August 2016 that between 2004 and 2015 pasture land prices in England and Wales tripled (AHDB, 2016). The concern of this Viewpoint is with the potential implications of this trend for planners in the immediate context, and also the planning profession as a whole into the future.

Speculating about speculation

In his recent contributions to the intellectual discourse David Harvey has suggested why these significant land value rises may be occurring. In considering the growth of the world economy since industrialisation Harvey notes that a number of economic historians, whilst not aligning precisely on their estimations of the figures of size and growth rate, do indicate that the global economy has shown signs of having historically grown at a compound rate (Maddison, 2007). In contrast to a linear rate of growth, under the conditions of compound growth the overall size of economic output initially increases at insignificant increments, but at a certain point rises more rapidly, from which it then increases at an increasing rate. It is suggested by Harvey (2014) that the 1970s was a key inflection point, at which growth began to particularly accelerate.

From his characteristic position interpreting Marx's writings Harvey suggests that within a system of capitalism there is a continual requirement for reinvestment opportunities (in Marxian terms, the 'absorption of capital surplus'). Without these opportunities a capitalist system cannot function. In order to make a reasonable return on these investments the owners of capital require the overall economy to be growing. Harvey suggests that the commonly accepted rate at which an economy is required to grow in order for most capitalists to make a reasonable profit on their investments is around 3% (the target rate for economic growth endorsed by the financial press). A key implication is that, under the conditions of compound growth, the requirement for surplus absorption also reflects this growth rate. Therefore, since the 1970s, at the level of the world economy there has been a continuingly increasing requirement for capital investment opportunities in order for capitalists to make a suitable profit and the overall system to be maintained. The implications of this are spelt out by Harvey:

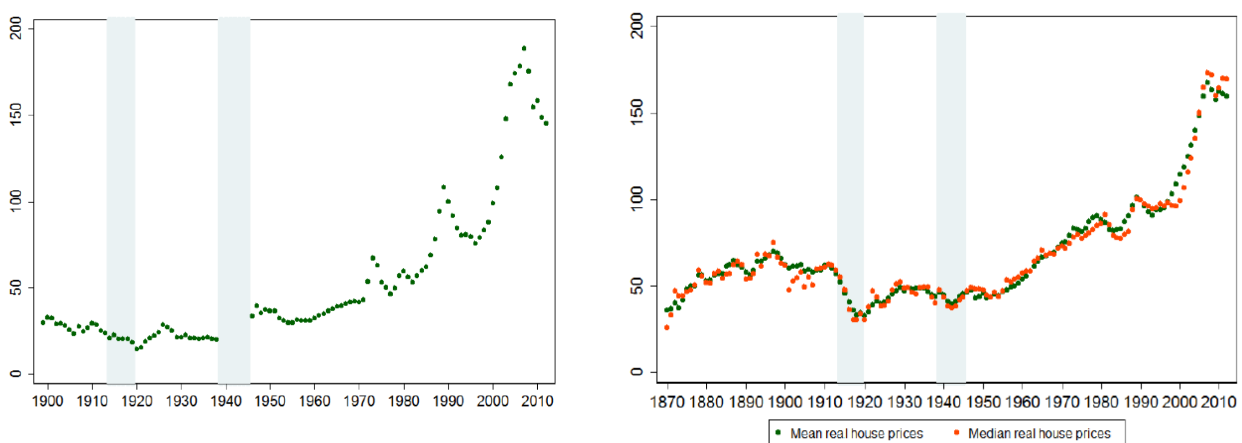
> "To keep a satisfactory growth rate right now would mean finding profitable investment opportunities for an extra nearly $2 trillion compared to the 'mere' $6 billion that was needed in 1970. By the time 2030 rolls around, when estimates suggest the global economy could be more than $96 trillion, profitable investment opportunities of close to $3 trillion will be needed. Thereafter the numbers become astronomical." (2014, p. 228)

The accelerating requirement for investment opportunities since the 1970s has been supported by the various neoliberal state projects the world over. Indeed, Harvey argues that the privatisation of state assets and 'enclosure' of a range of formerly common goods (such as water and other utilities) has played a significant role in opening up opportunities for the absorption of capital surplus. However, Harvey adds that we are potentially nearing a global limit on commodification and enclosure potential:

> "…when everything – but everything – is commodified and monetised, then there is a limit beyond which this process of expansion cannot go. How close we are to that limit right now is hard to judge but nearly four decades of neoliberal privatisation strategies have already accomplished a great deal and in many parts of the world there is not much left to enclose and privatise." (2014, p. 235)

The impact upon land prices in this situation relates to the role of land as an investment opportunity. In recent decades, Harvey suggests, investor preferences have tended towards a focus on assets rather than production, signalling a shift of capital away from productive activity to becoming rentier (Böhm, no date). In this new 'rentier economy' control over assets becomes significant and the particular asset of land (along with other major asset markets, such as art) finds itself increasingly under the investor's spotlight. In the context of compound growth, this focus on investment in assets continues to intensify (population growth being another significant factor; not addressed here but considered by Harvey, 2014). Indeed, with the exception of the years immediately following financial crises, Knoll *et al*'s historic analysis of house price rises in both the UK and 14 countries overall shows indications of a compound growth pattern (Figure 1).

<u>Figure 1. Mean and median real house prices, UK (1900-2012) and 14 countries (1870-2010)</u>



Notes: Index, 1990=100. The years of the two world wars are shown with shading.

Source: Knoll et al, 2014, p. 14 (UK) and p. 16

Implications for planners

If the explanation behind the sharp rises in land and property values since the 1990s lies in the requirement for increasing surplus absorption opportunities within a context of the compound growth of the global economy, this leads to the conclusion that the land value rises witnessed to date could only be the beginning of something much more dramatic. Unless investor preferences move away from asset markets (either by choice or force) there is the potential for land values to grow in profoundly large increments over the coming decades. If this does happen, what are the implications for planners? I'll consider two potential sets of implications below. Firstly, the more immediate implications for the day-to-day operation of planners, and secondly, the wider implications for the planning profession as a whole; and particularly in terms of its role in public debate.

For local authority planners in the current context, significant acceleration of land and property values presents potentially both opportunities and concerns. Speculative land acquisition and development is likely to increase and the high and rapidly increasing rates of return on such investments (unless additional taxes are imposed at some future stage) may provide a stronger negotiating position for planners during the development process – for example, in the UK negotiations around section 106 agreements and the setting of Community Infrastructure Levy (CIL) rates. The same principle applies to the position of planners in requiring other 'quality of place' features in new developments. Land owned by public authorities will also be gaining in value and allow increasing income streams for local and national government through appropriately targeted renting/leasing. However, the challenges may be particularly concentrated in areas related to social justice, where rapidly rising dwelling prices will lead to ever higher private rental costs for those in society who do not own land. Socio-economic inequalities across society will likely be increased and a continually clearer dividing line emerge between land owners and the rest. This is of course a phenomenon already in existence, but one that could be significantly accentuated. A greater need for social renting to house those who cannot pay market rent or are not able to raise the deposit capital to borrow would of course be inevitable.

Another immediate question for planners would be the feasibility of greenbelts within such a context. Local governments are already under significant pressure to release greenbelt land; particularly in certain locations, such as London. Whilst this pressure may take the form of various narratives based around a crisis of housing supply, perhaps an underpinning driver is the compounding global pressure from the owners of capital (directly or indirectly through, for example, investment institutions) for surplus absorption in land ownership and development. If such pressures are only to increase over the coming decades - and at increasing rates – it is a question as to how realistic stringent urban containment policies can be unless wider measures are taken to curb the underlying cause of the pressure or provide other outlets for it; such as loosening height restrictions or increasing public spending on brownfield land assembly and preparation.

This leads to the implications for the planning profession as a whole. The planning system in a number of countries has its historic roots in 19th century social reform movements and is underpinned by the impetus to manage land use in more efficient, healthier and fairer ways. Indeed, one of the founding fathers of the profession, Sir Ebenezer Howard, famously included co-operative land value capture mechanisms in his highly influential garden city concept and the 1947 Town and

Country Planning Act - the basis for the planning system in the UK – was influenced by detailed considerations of the relationship between land and the wider public interest (see below). The potentially harmful impacts (socially, environmentally and economically) of significantly increasing land values potentially presents a call to the planning profession to play a much more prominent role in making the public argument for a reconsideration of the relationship between land, property, taxation, wealth and desert. Indeed, putting the prospect of compound growth aside, even the situation at present suggests the need for a serious revisiting of these relationships. A recent report by Savills noted that UK residential property has become an increasingly important store of wealth with the total housing stock of the country now worth over £6 trillion. This figure was reported to have risen by over £1.6 trillion since 2005 and £1.2 trillion of this rise occurred over the past three years alone (Savills, 2016) – also providing an indication that the longer-term trajectories shown in Knoll *et al*'s graphs above have been only temporarily disturbed by the 2007/8 financial crisis.

In a society which is already increasingly divided by wage-related income there are substantive issues around fairness to be considered in light of these trends. A number of politically-aligned and generally little-known campaign groups have existed for some time in the UK context calling for a fairer system of land taxation. Primary amongst these are the Labour Land Campaign and the Liberal Democrats ALTER (Action for Land Taxation and Economic Reform) which both promote the adoption of a system of Land Value Taxation; something already in existence in a number of countries. It is uncontroversial to note that an individual's claim to land is often heavily influenced by factors of what Ronald Dworkin terms 'brute luck' – whether good or bad luck (Dworkin, 2000). Primarily, an individual's family of birth affects their starting point, but also the fact that existing ownership of land tends to provide the advantages required for further appropriation of land. In a context of sharply increasing land values, the ownership of land confers ever greater advantages in terms of the ability of the owners of that land to appropriate increasing wealth without any effort on their part. To take a simple example, a straight-forward extrapolation of the trend shown in Knoll *et al*'s graph suggests that by 2030 mean house prices in the 14 countries they studied could be around 475% of their 1990 levels. By 2040 this could be 675%. If this were to occur, a house purchased in 2016 for €150,000 would be worth around €400,000 by 2040 (€250,000 difference). A house purchased in 2016 for €450,000 by that time would be worth about €1.2 million (€750,000 difference).

Where income and wealth are being gained from simply the ownership of land over time, there is a compelling case for (re)evaluating where this return is going and how appropriate taxation mechanisms (or other regulations/policies) can allow a fairer channelling of these gains for the benefit of society as a whole. In the example case above, over the 24 year period the owners of the €450,000 property will have gained an additional half a million Euros of wealth to the owners of the €150,000 property through no additional labour, talent, effort, risk or expenditure on their part during that period (other than on slightly higher maintenance costs and insurance/heating/ bills etc as a result of the property possibly being physically larger – bills they may not be paying anyway if they are landlords). Whilst some groups in society may consider this to be a fair outcome, it is likely that the vast majority would consider it to be unjust and be prepared to support the argument that at least a reasonable portion of this gain should be channelled into infrastructure, public services or other forms of redistributive or socially profitable state activity.

Internationally, the ways in which governments tax land and property varies widely. In the UK, for example, such taxes primarily take the form of transaction taxes (mainly stamp duty land tax, inheritance tax and capital gains tax), locally levied service charges oriented towards the users rather than owners of property (council tax and business rates), taxes on rental profits (for both property businesses and personally owned property) and the contributions during the land development process mentioned above (section 106 agreements and the more recent CIL). Recent OECD data reports that the UK actually has the highest tax on land of any of its members; both as a proportion of total taxation and GDP. At present, 12.7% of total tax revenues are from property related taxes, and recent reforms have increased this proportion. Land taxes in some forms can be regressive and hamper economic growth, but correctly targeted there is a distinct moral and even economic logic for strengthening levies. The justification for land taxes of different kinds varies in each case, and some are clearer than others. However, the primary issue in light of increasing land values would be the specific capture of at least some of the increase in value.

Finally, the relationship between land value affected by planning policy and taxation is one of particular relevance to the planning community, and a consideration which goes back to the early formation of national planning systems during the first half of the twentieth century. In the UK, the report of the British government's 1941 'Expert Committee on Compensation and Betterment' (chaired by Justice Uthwatt) was an important influence on the 1947 Town and Country Planning Act. The report considered, in part, the issue of 'betterment' (increases in land value as a result of state activity). After considering the various difficulties in implementing such a tax, the report settled on the recommendation for a periodic levy on annual increases in annual 'site values' (essentially the letting value). Revaluations of all site values would take place every 5 years and the increase would be subject to a 75% levy for each of the following 5 years after the revaluation (Brock, 2010). Essentially the proposal was a land value tax, but it was not implemented and the 1947 Act instead imposed a development charge which was then abolished six years later (Ward, 2004). Land values were static at the time of the Uthwatt report and so its considerations primarily related to land uplift as a result of state activity. However, in the present context of sharply increasingly land values (even with no related state intervention) and with the added prospect of these compounding into the future, it could be a useful exercise to revisit some of the principles considered by the Uthwatt team, including their recommendations.

Conclusions

The possibility that the global economy is growing at a compound rate and the consequent influence of this on land values presents an important and presently under-considered new context for planners, as well as society as a whole. Current trends are already indicating significantly increasing values, and if the explanation lies in compound global growth and the related requirement on the part of the owners of capital for surplus absorption opportunities then, if left unchecked, such trends could potentially increase in almost unimaginable trajectories over the coming decades. For planners, it will be important to have a clear grasp of these trends and where they may be heading; both for the purposes of gaining leverage in development negotiations in the present context, and also in participating in debates around wider policy or taxation alterations in the longer term. Whilst a number of the issues discussed in this Viewpoint are perennial, and in some cases go back

hundreds of years, the onset of potentially compounding land values presents an impetus to the debate historically before unknown.

In particular, the case is strong for a general reorientation of taxation towards land value increases and away from other more traditional forms. A recent study by the University of Cambridge on the macro economic impacts of the British exit from the European Union predict that in 2025 British wages will be no higher than they were in 2004 (Gudgin *et al*, 2016). As mentioned above, over recent years there has also been a movement on the part of investors away from productive activity and towards other more immediately profitable forms of investment (see also Hutton, 2015). There is therefore a present argument for shifting taxation away from income and production (areas of human activity which involve effort, talent, risk etc) and towards land value increases. This would go some way towards creating the fairer society the planning profession was established to bring about.

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