



## LECTURE EIGHT - PART TWO

## Land And Rent

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- Suppose you want to build your dream house.
- It's a 6000-square foot mansion with five bedrooms, four baths, three tennis courts, two swimming pools, and an entertainment center that would make Walt Disney blush.
- The only problem, of course, is that you need an acre of land to build it on.

## Differing Land Rents

- If you want to build your dream house where Clint Eastwood hangs out in Carmel, California, that one-acre lot might cost you over three million dollars.
- Of course, if you decide that that is not quite in your budget, you could settle for an acre of land in rural Mississippi for about \$500.



## How Is Land Priced?

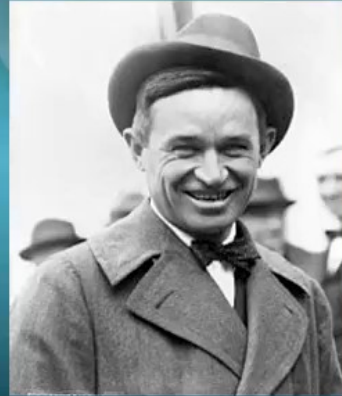
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- So what accounts for this big difference in price for an acre of dirt?
- More fundamentally, how is land priced in the real estate market?



## Why Land Is Different

- To answer this question, let's first talk about what makes land different from most other factors of production.
- What do you think that difference is?
- **Hint:** Will Rogers once said "Land is a good investment: they ain't making it no more."



## Quantity Is Fixed

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- The essential feature of land is that its quantity is fixed and completely unresponsive to price.
- This essential feature leads us to our first definition:



## Pure Economic Rent

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- The price paid for the use of land and other natural resources which are completely fixed in supply.
- It is the fixed nature of the supply of land that makes rental payments clearly distinguishable from the prices paid to the other factors of production.

## An Important Point

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- Pure economic rent, as defined by economists, is not the same thing as the rent people pay for their homes or apartments.



## Rent Versus Economic Rent

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- The rental payment you make to your landlord typically includes compensation for:
  1. The use of capital such as the building structure
  2. Labor, including building maintenance and management;
  3. The use of utility services such as water, electricity, and gas.

### Key Point

In most cases, only a very small fraction of your rental payment represents pure economic rent, as we have defined it!

## Elasticity Of Land



- Having defined the concept of pure economic rent, let's now examine how rent is determined in the market.

### Exercise

Given that the supply of land is fixed, how would you draw the supply curve and what would its elasticity be?

Pause the presentation to do this exercise.

