Scarcity Rents and Rent Seeking

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Abstract

This note looks at Rent, Scarcity Rent, and Rent Seeking

1 Rent

Definition 1 *Rent is a form of income.*

The concept of rent as a payment for scarcity goes back to the Classical Economist David Ricardo who used "rent" to explain why land (when scarce) earns a form of income that is best measured by its marginal productivity.

Therefore the definition of scarcity rents would be the following:

Definition 2 *Scarcity Rent is the rent that accrues to the owner of a natural resource just because it is scarce.*

Throughout history land has been scarce and thus has had a value. Figure 1. shows the Market for land. Lets assume that Po is equal to the marginal cost of the least productive land. Therfore, if the owner of the least productive charges Po then the amount of land rented, bought, used from him will be Qo. However, land is not a homogeneous commodity or good because there are different types of land, i.e. land has different quality and we can measure that by its marginal productivity. Higher quality land will be more productive than lower quality land. Therefore, higher quality land will command a higher price.

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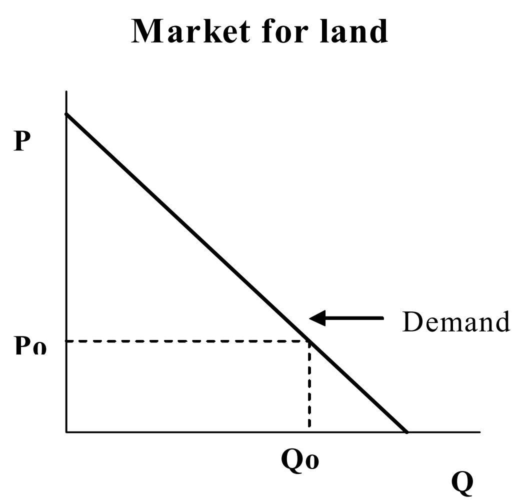

Figure 1. Market for Land

The owner of higher quality land will realize that his land commands a higher price because as, our friend, David Ricardo established the price, income, rent of such land should be equal to its marginal productivity.

Graphically, the owner of higher quality land will charge a higher price because, among other things, there is not as much high quality land as there is low quality land, and it has higher marginal productivity. Figure 2. shows this situation where the owner of higher quality land charges a higher price (Pi) and obtains rents, the filled rectangle, above the price of lower quality land. This situation can continue until we get all the way to the very best land, with respect to quality, which would command a very high price.

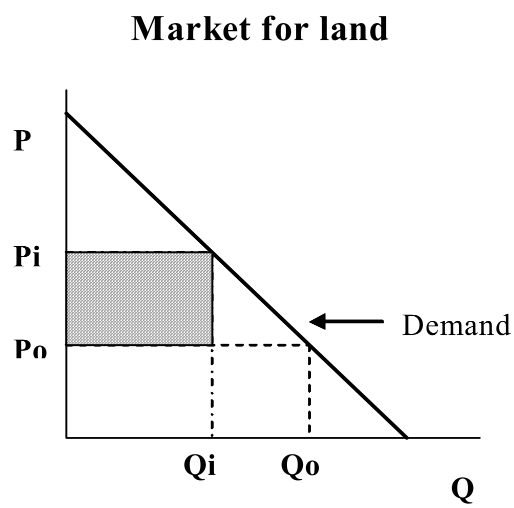

Figure 2. Market for land and Scarcity Rents

2 Rent Seeking

Rent Seeking is a type of behavior incurred by economic agents that devote productive resources like money, time, or any other type of resource that could be used productively, to try and appropriate non-productive rents. The example here would be trying to impose barriers to entry in a market in order for the firm already established in the market to obtain monopoly rents.

Figure 1. above is also useful in explaining this situation, imagine that the market for land is a competitive market. Therefore, Po and Qo would be the competitive price and quantity. Once someone tries to impose some type of barrier to entry such as a quality control inspection test or something similar, and they are successful, then they would be able to appropriate the rents generated by the increase in price whichi are depicted in Figure 2. as the filled in rectangle.[1]

References

[1] Sterner, Thomas. "Policy Instruments for Environmental and Natural Resource Management" Resource for the Future, Washington, DC, 2003

[2] Tientenberg, Tom. "Environmental Economics and Policy" Addison Wesley. Boston. 2001.

[1] The graphs were used to illustrate two different situations, i.e. Scarcity and Rent Seeking. These situations are independent of each other. Any one of them could happen irrespective of the other.