



In rural areas, land is an essential productive asset and a means to sustain a livelihood. Access to land is important for household welfare, aggregate economic growth, and sustainable reduction of poverty. It is important to *reduce poverty* because in many developing economies access to land allows the poor to make productive use of family labor, improve their nutritional status, smooth consumption, and improve their income and well-being. The contribution of land to *economic*

growth depends on the security, duration, and enforceability of property rights, which determine investment incentives, and on the extent of markets to rent and sell land. In addition, land markets are often an important ingredient in the development of financial markets. This Note discusses several elements of land policy that could help create a framework for efficient land allocation through properly functioning land markets, as well as improve access to land by the poor.

well developed and communal land ownership has traditionally performed an insurance function, individualized property rights may, by depriving certain groups of access to this resource, also carry social costs. To reduce such costs, mechanisms such as communal use of pasture and forest areas or periodic land redistribution are often maintained long after societies have adopted an individualized land rights system. Policy interventions that would change the structure of land tenure, or the way in which individuals can access land, must consider the effects on both efficiency and equity.

Communal Tenure Arrangements. In most societies with a low population density, individuals have usufructuary rights to communal land, but ownership rests with the community. Some economists consider such tenure arrangements as inferior because they might lead to problems of open access and diminished investment incentives. Recent research and empirical evidence, however, indicates that with low population density, communal tenure systems can be a cost-effective means to ensure secure tenure, and that there are many measures short of unfettered individual tenure that could be adopted to enhance productivity and equity.

With a low population density, communal systems have advantages because the cost of establishing, enforcing, and maintaining records of individual plot boundaries is often not commensurate with the limited incremental benefits from full individual ownership. Also, communal resource ownership often provides public goods that may be difficult to realize under a structure with full individual rights. In addition, the magnitude of the disadvantages that have traditionally been associated

Secure Property Rights

Secure property rights are important to increase agricultural output through incentives for investment, effort, and the ability to transfer land at low cost to more efficient producers. In addition, secure property rights are important for equity because it is the poor who are normally least able to defend their property rights. Although there is agreement that a system of enforceable land rights is a key public good that can provide high returns, the most appropriate way to improve tenure security clearly depends on the specific environment.

Conceptual Basis. Secure property rights provide three main benefits. First, secure tenure increases incentives to supply labor, and if the time horizon is long enough, long-term investment. Second, secure land ownership can

increase the supply of formal credit. Land with secure, clearly-defined, and easily-transferable ownership rights is ideal collateral. And third, well-defined ownership rights make it easier to transfer land to more efficient users from those who are not as efficient. Property rights can be very secure, of course, even if they are not defined at the individual level; indeed there are many circumstances where definition of ownership rights at the community level appears to be an adequate arrangement for secure tenure.

Defining individual property rights can be costly. Most immediate are the expenses to physically delineate plots, establish and maintain accurate records, enforce rights, and resolve disputes. In situations where other markets for risk and insurance are not

with communal tenure structures may be more limited, for a number of reasons:

Individual cultivators. In most communal systems arable land is cultivated individually, in some cases even with inheritable use rights, and only pasture and forest or fishing grounds are used by the whole community.

Outsiders prohibited. Although most communal systems prohibit land transactions with outsiders, rental and sales within the community allow members to realize a significant part of the efficiency advantages associated with land transactions.

Potential shortcomings. Some of the potential shortcomings of communal tenure systems are encroachment, a growing number of boundary disputes, and land grabbing by chiefs or other powerful individuals. Rather than changing the property rights regime, documentation of existing rights, clarification of boundaries (with systematic resolution of disputes at the community level), and increased transparency in the administration of land rights may greatly ameliorate such problems.

The critical issue is that efficiency and equity effects of land tenure will depend upon, among other factors, an area's access to infrastructure and markets, and the resulting economic specialization. If access and specialization of the infrastructure are limited, then the scope for capital-intensive investment, use of land as collateral, and efficiency gains from transactions in land markets will also be limited. If cultivators benefit from investing, then low-cost community-based arrangements are generally sufficient to ensure efficient factor use. As population density, access to other markets, and land values increase, then investment, credit access, and impersonal exchange of land become more important, and thereby increase the payoffs from formal mechanisms to define land ownership.

Unrestricted Individual Rights and Formal Titles. One indicator of an insufficient traditional tenure system is when the number of land-related disputes increases. The literature provides guidelines about the circumstances that make formal (titled)

individualized tenure systems a worthwhile arrangement.

First, under the informal system it needs to be apparent that the level of land disputes is reducing the cultivators' perception of secure tenure, as well as their incentives to invest, ability to engage in land transactions that enhance efficiency, or use land as collateral.

Second, many empirical studies point toward access to formal credit as an important benefit of formal title. This benefit will be realized only where at least an incipient formal credit market (allowing use of title as collateral) exists and investment opportunities are available. Empirical studies show that even after titling programs, many small farmers remained beyond the reach of formal credit.

Third, land titling should be systematic and area-based rather than 'on demand' for both reasons of efficiency and equity.

If there are no adequate safeguards, titling can permanently deprive certain groups of their land rights. For this reason, specific attention should be devoted to ensuring that (i) the rights of historically disadvantaged groups (women, indigenous residents, and the poor) are protected, and (ii) land market transactions in a post-titling environment are not likely to be severely biased against the poor or vulnerable.

Land Markets

A key underpinning of the Bank's land policy is the inverse 'farm size productivity relationship,' whereby for many (but not all) types of farming and cropping systems, family-operated farm units are economically more efficient than large farms that rely on wage labor. Family workers have the incentive to exert maximum effort. By shifting land to more productive (family-based) operators, and without other imperfections, transactions in a freely operating land market would improve both efficiency and equity. However, the presence of various policy distortions (for example, subsidized credit), tend to give an artificial advantage to large farms.



For this reason, the Bank has long advocated the elimination of macroeconomic and sectoral policy distortions as a precondition for land markets that are intended to help enhance productivity. It is, however, important to note that in addition to productivity, producers' ability to access credit, inputs, and insurance markets will affect the extent and type of land transactions. In particular, credit constraints may prevent family farmers from translating their productivity advantage into effective demand in either land sales or rental markets.

Markets for Selling Land. Policymakers often conclude that owning land is preferable to renting, but markets to sell land are themselves not free of potential shortcomings.

First, if access to capital markets is imperfect, landless households may not be able to obtain the credit necessary to acquire land from larger farms. Imperfections in the credit market can more than outweigh the productivity advantage of family farmers. In addition, if the land value as collateral in formal credit markets is capitalized into land prices, the



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distortions cannot be tackled, creating markets to sell land in such circumstances may not be desirable.

Markets for Renting Land. Even if imperfect markets for credit and insurance reduce the market opportunities to transfer land from large to small producers, such transactions could still take place in the land rental market. By renting land, landowners would not forgo the credit access associated with land ownership (and could even advance credit they obtain to a tenant under an interlinked contract). Under this arrangement, the family-managed tenant farm is able to show productivity advantages.

Where investment is important, the disincentives to undertake long-term investments that are inherent in short-term rental arrangements could be minimized by adoption of long-term contracts that provide tenants with compensation for visible improvements. Compared to selling land, markets for land rental are less affected by imperfect credit markets, are characterized by lower transaction costs, improve the welfare of people with limited wealth, and can facilitate acquisition of agricultural and management knowledge by tenants as a first step on the 'agricultural ladder.'

Paradoxically, while land rental markets that function well could provide substantial benefits, many countries have severely restricted the scope for land rental especially under share tenancy contracts to prevent 'exploitation' of tenants in what was considered a feudal mode of production. Research has challenged the justification for such interventions by showing that the efficiency losses from share tenancy are, in practice, much lower than assumed. Empirical evidence shows that tenancy restrictions not only failed to achieve their objectives, but often had directly perverse effects.

In spite of these concerns, government-induced restrictions on the functioning of rental markets have become a major source of inefficiency. Analysis

has shown that equity and efficiency of land rental contracts can be enhanced by (i) improved market information and enforcement of contracts; (ii) increased access to other markets and off-farm opportunities; and (iii) augmented bargaining power for tenants. Rather than trying to enforce rental restrictions that are of doubtful value, governments concerned about tenant welfare should dismantle these restrictions.

Land Reform

Long-standing impediments to smoothly functioning land, labor, and product markets contribute to highly unequal land distribution in many countries. Large tracts are not used as productively as they could be under a family-operated farming system, while small producers are confined to marginal and often environmentally fragile lands. Especially in situations where past policy interventions continue to reduce the extent of rental market activity, unequal land distribution is also often linked to social unrest and violence. In this context, policies of land reform have often been adopted to improve the distribution of productive assets, increase aggregate productivity, provide the basis for land rental and sales markets, and solve the political and social problems associated with widespread landlessness.

Historical Experience. Land reform in landlord estates where virtually all the land was already cultivated by tenants differs from the experience in haciendas where labor tenants had access to only a house plot for subsistence, but were needed to supply labor to the landlord's farm. Because tenants already cultivated the land and had access to markets on landlord estates (for example, Taiwan, Korea, or Japan), once it was politically feasible, land reform was relatively easy to implement. It appears to have increased equity and efficiency and provided a starting point for subsequent non-agricultural development. By contrast in haciendas (South Africa and most of Latin America), land reform was very difficult for several reasons:

Change cropping patterns. To shift from extensive, monocropped, and mechanized large farms to a labor-intensive, diversified, and year-round small

equilibrium price of land at given credit costs can exceed the present discounted value of the income stream from the land. Policy distortions such as subsidies and selective tax advantages for large farms work in the same direction.

Second, in a risky environment with imperfect insurance markets, *shocks* such as a drought may be associated with large swings in the supply and demand of land, as well as in land prices. By forcing small farmers to sell land at low prices during crisis and leaving them unable to replenish their asset base afterward, such shocks can pauperize smallholders while land accumulates in less productive large holdings.

Finally, *fixed transaction costs* associated with land sales make it difficult to sell small parcels of land or subdivide large farms for use by many small producers, which makes transactions between landholding classes extremely rare.

For all of these reasons, there are situations when markets to sell land may not lead to a more efficient and equitable allocation of land. If access to land by the poor is an important policy objective and if other policy



Appropriate policies can help improve access to land by the poor.

South Africa, Brazil, Colombia, and Guatemala have taken this opportunity to pilot a decentralized 'negotiated' approach to land reform.

The key element of this approach is a limited one-time grant to poor households interested in establishing a productive enterprise. The main purpose of this grant, which can be used for purchasing land, complementary investments, or technical assistance, is to help the poor overcome the (credit-related) obstacles that would otherwise prevent their participation in land markets.

Based on these planned objectives and the income they generate, beneficiaries negotiate independently with landowners on the modalities (including the purchase price) of a voluntary transfer of land in the market. With an overall cap on the grant size and the possibility to use any money not spent on land acquisition for complementary investments, there is a strong incentive for the purchaser to negotiate a favorable land price. Save for the provision of the grant, regulatory enforcement of the rules of the game, and monitoring and evaluation, there is no substantive role for central government.

Evidence from pilot programs indicates that although there are areas for improvement, a 'negotiated' approach to land reform is faster and cheaper than traditional models, and beneficiaries are more satisfied. While in-depth evaluation of these experiences will be necessary, some preliminary conclusions and challenges have emerged:

Program design. Establishing a limit on the size of the grant and ensuring that it can be used for land purchases as well as complementary investments has proven critical to keep down

costs. Further reducing transfers to existing landowners appears to be possible by integrating the program into a broader set of policies to improve functioning of land markets.

Program benefits. The speed at which beneficiary groups are able to realize benefits is surprising. Diversification, increased scope for investment in perennial crops and small-scale irrigation, land access as a means of self-insurance, and existence of spillovers from land reform beneficiaries to other groups within the locality have all emerged as benefits.

Evaluation. Given the different target groups addressed by programs in various countries, careful evaluation to quantify these effects, isolate beneficial implementation features, and compare the groups reached by land reform to those benefiting from other government programs will be of great interest and will allow immediate feedback about the design of land reform programs.

Conclusion

Throughout much of the developing world, the completion of far-reaching macroeconomic reforms has highlighted the need to tackle structural issues that will facilitate further development. These issues include the definition of property rights to land, the conditions that govern the exchange of such rights, and market and non-market forces through which marginalized parts of the population gain access to land. Policy advice in this situation requires awareness of (i) the advantages as well as pitfalls of individualized land ownership and the costs and benefits of formalizing them; (ii) the relationship between markets for land and other factors of production (including credit) and the implications for land market liberalization; and (iii) the scope and limitations for land reform as one means to quickly improve access to land by the poor.

farming system requires changes in cropping patterns and complementary investments in productive and social infrastructure.

Politics. The low labor intensity of highly mechanized large farms implies a need to select beneficiaries over and above workers already on the farm. Even where individual forms of cultivation were chosen, the selection process often failed to provide appropriate incentives for potential beneficiaries and instead relied heavily on political connections and failed to make use of the experience and resources of local governments. Land acquisition relied heavily on expropriation.

Policy distortions. The continuing presence of policy distortions (for example, credit subsidies for large farmers) that were capitalized in land prices increased the cost of the program and often made it rational for beneficiaries to sell out rather than self-cultivate.

Negotiated Land Reform. Macroeconomic reforms, in particular trade liberalization and the elimination of distortions in favor of large farms, have led to a precipitous drop in land prices in a number of countries (in South Africa and Brazil land prices fell by up to 70 percent). Along with the shift of comparative advantage to more labor-intensive crops and a wave of bankruptcies affecting heavily indebted large farms, the scope for efficiency-enhancing transactions in land markets has improved.

This Note was prepared by Klaus Deininger and Gershon Feder of the World Bank. The Rural Development Note series summarizes good practices and key findings about topics related to rural development. These Notes are distributed widely to Rural Family staff and are also available on the Rural Sector website (<http://essd.worldbank.org/essd/rev/rdvhom.nsf/RuralStrategyHolder?OpenView>). If you are interested in writing a note, please email your idea to Nwanze Okidegbe (nokidegbe@worldbank.org). For additional copies, please contact Melissa Williams at (202) 458-7297. The ideas posed in this series do not necessarily reflect the policies of the World Bank. Edited by Seth Beckerman, original design and layout by Condello Design, both of Pittsburgh, PA. Photographs by Curt Carnemark, World Bank.