

Land Markets - Why are They Required and How Will They Develop?

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SUMMARY

Land is unlike other commodities that can be bought and sold in that it is immovable. Buildings upon it can be dismantled and moved elsewhere but the land on which they stand cannot be moved. Only the rights to use the land can be bought and sold.

Land markets exist when and wherever it is possible to exchange rights in land for agreed amounts of money or services rendered. The ability and capacity of banks and other financial institutions to lend money is underpinned by an efficient land market, which in turn requires an efficient land administration system.

The efficiency of the land market varies across the world together with its openness to public scrutiny and support for the concepts of sustainable development. In less economically developed societies, and in particular where informal settlements exist, it has not always been possible to develop an effective land market and this leads to under-capitalisation. In order for a land market to develop and be maintained a number of critical factors need to be in place. In addition to clear policies and enforceable laws, the institutional framework needs to provide for consistent, responsible and accountable decision-making within the overall national land policy. There must also be a land registration system that is affordable so that all citizens, especially women and minority groups, rich and poor, can have access to it.

Continued globalisation will inevitably impact land markets especially as information technology, including web based services, provides greater access to national land information services.

This paper examines the current development of land markets and why they are required; and then explores how these systems might develop, taking into consideration the introduction of electronic conveyancing, global monetary transactions, and pan-European land information services. Finally the paper asks how these developments will impact the less developed economies.

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1. INTRODUCTION

Land is part of the culture of a nation and at both a national and individual level people are prepared to fight to defend it. Throughout history, the ownership of land has often been a sensitive and politically controversial issue. Perhaps one reason for this is that land is unlike other commodities that can be bought and sold in that it is immovable. Buildings upon it can be dismantled and moved, even the soil can be dug up and taken away but the space from which they come cannot be moved.

Some argue that governments should determine who is allowed to own land. Others maintain that, although a regulatory framework should be established by the state, the best way to achieve the optimum form of land use is through the operation of free market forces. This paper explores some of the issues surrounding the operation of land markets.

2. LAND MARKETS – WHAT ARE THEY?

Land markets exist when and wherever it is possible to exchange rights in land, usually for agreed amounts of money. Without an integrated and formalised real property system, a modern economy is not viable since the ability to create national wealth is severely restricted. An efficient land market underpins the capacity of banks and other financial organisations to lend money and for landowners to invest. Less economically developed societies have, for various political and cultural reasons, failed to create an efficient land market. As a result, such societies tend to be under-capitalised.

In one sense land is something physical, a geological or biological part of the earth. In many juridical systems the legal profession defines the land in a very different way as an abstract set of property rights that govern the use of the land and the ability of the owner to acquire or dispose of these rights. These rights may be considered to extend ‘from the centre of the Earth to the infinite in the sky’ and include all things in permanent contact with the soil such as buildings, minerals and vegetation. In some societies, however, land is deemed to exclude buildings and other man-made features.

With a few exceptions (such as Antarctica) the ultimate owner of the land is the state, which retains the right to acquire private property for public purposes and to control the manner in which the land is used, for instance through planning legislation. The state may also retain the rights to minerals and hydrocarbons. Subject to this, many societies permit private land ownership with rights held either in freehold, which represents the maximum degree of freedom for the landowner, or leasehold in which there are greater limitations on how and

when the land may be used. Where private rights in land are recognised, they may be exchanged for a consideration, usually money. A land market can be said to exist when the number of these transactions passes a critical threshold (see Figure 1).

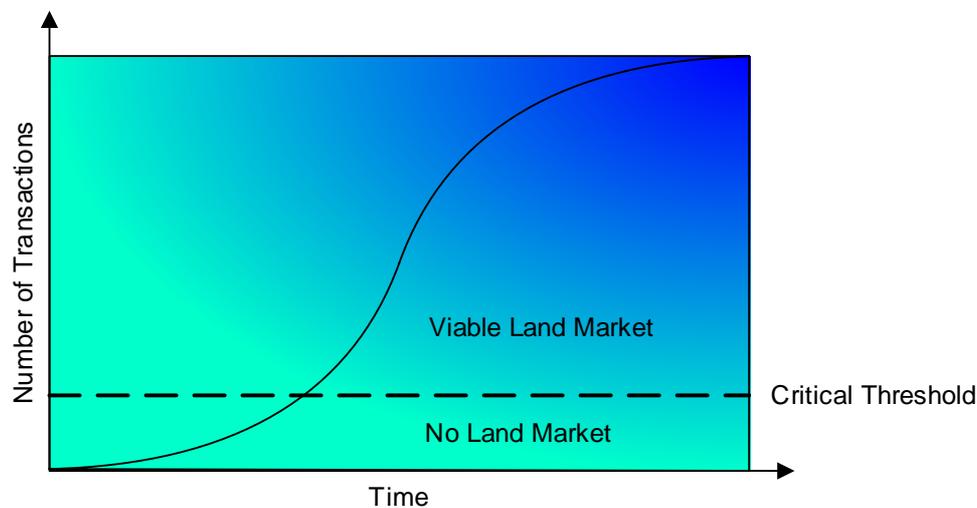


Figure 1: Transitions in Lifecycle of Land Markets

Land markets are generally regulated through land tenure and land administration systems. Key elements in any land tenure system include the extent to which land can be bought or sold; whether it can be used as collateral and if so who then takes over a property if any loans on the land cannot be repaid; who has rights of access to or passage through the land; the rules governing inheritance; and the extent of additional use rights and obligations.

Land administration systems enable security of tenure to be guaranteed and this is achieved in a number of ways, the details of which are beyond the scope of this paper. Weaknesses in any land administration system affect the level of trust that is an essential component of a land market. As van der Molen (van der Molen, 2006) argued, the impact of such weaknesses can have extensive consequences:

“In the absence of an in-depth understanding of land tenure arrangements it will prove difficult, if not impossible, to identify the processes involved in the determination, recording and dissemination of information about tenure arrangements required for the provision of the services needed to ensure for the requisite security of tenure, markets, planning, taxation and management of resources”.

Dealings in the land market involve a change in ownership of the rights in land. Ownership (who holds the rights?) differs from land tenure. Although commonly described as such, the idea that land tenure is about the man-land relationship needs some clarification. A labourer paid to work in the fields has a man-land relationship but this has no particular bearing on the

nature of the land tenure that is associated with the fields that he is working. Conditions of employment will be his primary concern and it is the consequences of his labour that may have an effect on the use rights associated with the tenure. When it is said that ‘security of tenure’ is a necessity for stable economic development, the reference is to the security or safety with which an individual or organization can maintain possession or occupancy of the land. Thus a tenant in occupation of an apartment will expect the law to provide protection against the excesses of a landlord who is the owner of the apartment.

Land markets must operate within a framework of law that is accepted by all parties concerned. As S. R. Simpson (Simpson 1976) observed:

“...the significant point is that security of tenure, that vital consideration when good land use is concerned, can be, and frequently is, enjoyed without any concrete evidence of title other than occupation. In those countries where individual property rights are recognized and the rule of law prevails, the courts will uphold occupation against anybody – including the State or the Government – other than a person who can prove a better right. In fact, provided that nobody else can produce evidence establishing some right, the courts will not require any proof from the occupier, for there is much truth in the old saying that ‘possession is nine points of the law’”.

3. LAND MARKETS – WHY ARE THEY REQUIRED?

Land markets are a fact of life in most developed societies, yet surprisingly their impact is not well documented. As Cheshire and Sheppard (Cheshire and Sheppard 2004) have pointed out:

“Land markets have implications for welfare and social issues such as segregation going far beyond the shelter houses provide. They are tightly regulated. Yet economists devote comparatively modest amounts of attention to their analysis.”

Land markets are important because all economic development depends to some degree on the availability of land - even a computer software developer working in ‘virtual reality’ needs an office or other workspace. Industries need sites for factories, distribution or retail centres, while in agrarian societies the quality of the land is a key factor in creating a livelihood. Every citizen needs somewhere to eat and somewhere to sleep and families require a defensible space in which they can find peace and privacy.

Land markets are mechanisms that, provided there are appropriate institutional checks and balances, allocate ownership and use rights in a manner that allows land and its associated assets to be used in the most economic way. Given secure land rights, land markets can increase the incentive for people to invest and for financial institutions to lend, since land can be used as collateral as well as being the basis for production. An efficient and effective land market can improve the performance of a nation’s economy and increase prosperity - in the

UK, for example, property related services are estimated to contribute 9% of GDP to the economy (RICS, 2002).

The levels of investment and the impact of land markets vary across the globe. In general the positive economic consequences have been most noticeable in Europe and North America. In much of Africa, market activity is limited - in Southern Africa for example, land sales among smallholders are rare while in East Africa there has been some buying and selling of land. In general, throughout Africa, individuals often acquire formal land rights through the market while land rights that are acquired through traditional forms of gift or inheritance remain under communal or customary tenure. In Latin America the markets have been biased by the fact that access to capital is easier for the wealthy and this has segmented the market, leaving many people landless and in poverty.

The longer-term investment in land markets in developed countries has been considered to be one of the major factors that underpin modern economies. However, on their own, land markets are not a panacea.

There are conflicting views on how well those who are poor can benefit from the land market and access to capital since formal systems may not operate very effectively for poorer households and small farms. There is a danger that land markets may lead to more poor people becoming landless with the concentration of land into the hands of the rich. There are also divergent views as to how to prevent land grabbing and asset stripping. Land markets in developing countries tend to flourish best in urban and peri-urban areas where commercial opportunities are high and migration can stimulate land market development.

Land markets help to make the valuation of land and real property more transparent. The estimated value of a property will depend upon on a variety of factors, including the purpose for which the property is being evaluated. There are international standards of valuation that may be used to determine the best estimate of the value of real estate and these standards help to support the growth of cross-border mortgage investment and the growth of secondary mortgaging. The market value of property needs to be known when transactions take place not only to ensure a fair price and underpin the mortgage system but also when compensation needs to be paid for land that is compulsorily acquired by the State, and when taxes are assessed.

An efficient and effective land market will allow landowners to turn their assets into capital that can be used for other purposes (see Figure 2). The money released through the mortgage system can be used to finance alternative forms of investment. In Spain, for example, it is estimated that at least 56% of the money in circulation has been made available through the real estate market (UNECE, 2005).

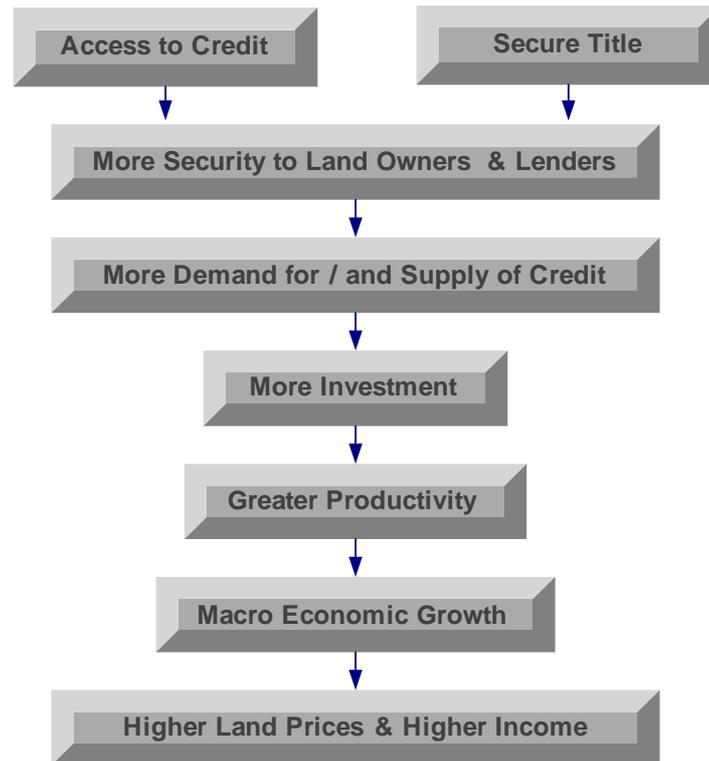


Figure 2: The Connection Between Good Title & Prosperity

4. LAND MARKETS – HOW WILL THEY DEVELOP?

The efficiency of the land market varies across the world together with its openness to public scrutiny and support for the concepts of sustainable development. In less economically developed societies, and in particular where informal settlements exist, it has not always been possible to develop an effective land market and this leads to under-capitalisation. In order for a land market to develop and to be maintained, a number of critical factors need to be in place. In addition to clear policies and enforceable laws, the institutional framework needs to provide for consistent, responsible and accountable decision-making within the overall national land policy. There must also be a land registration system that is affordable so that all citizens, especially women and minority groups, rich and poor, can have access to it.

The development of land markets has historically been closely linked to the development of a nation, its economic well-being and the quality of life of its citizens. Will this trend continue? Some commentators suggest that the continued and recently rapid rise in property prices cannot be sustained. This will lead to a situation where property price may fall: a situation that creates negative equity and reduced economic growth. If this happens then there may be global consequences since land markets now extend across international borders; as is evidenced in Europe where the European Land Information Service (EULIS) is being

developed to exchange real property data throughout the European Union (EU). Its aim is to promote the economy of the EU by breaking down barriers to cross-border lending, enabling more competition in the secured credit and real property markets, giving more choice to borrowers, providing links with non-EU countries and encouraging the spread of best practice.

The EULIS project recognises subsidiarity and seeks to retain national differences, for example, with regard to systems of land tenure while allowing for the open exchange of land and property-related information. In many countries, however, opening land markets to foreigners gives rise to concern because indigenous people fear that this will adversely affect their culture and that they will not be able to compete with the external economic forces.

The trend towards globalisation means that land markets should be seen in an international rather than a national or regional context. Access to land for development is necessary if countries are to attract foreign direct investment. An efficient land market with equal rights for all citizens will enable a country to participate in the global economy and gain acceptance on the world stage as an equal partner. Many countries are now establishing legislation and policies that provide for web-based access to all land information. Where web-based access is not possible, appropriate conventional channels must be provided that allow open and timely access to the information at affordable prices so that corporate investors do not have an unfair advantage over the local communities.

5. LAND MARKETS – HOW DO THEY IMPACT LESS DEVELOPED ECONOMIES?

Land markets require the injection of capital to enable them to function. This can be generated from a number of sources. The corporate investor can normally gain access to capital or credit to fund acquisitions. Communities or individuals may find it difficult to acquire collateral against which to borrow monies to finance the acquisition of land and thus enter the land market. Many of the countries in former Eastern Europe have needed to ensure that sufficient land and property is locally owned so that it can be used as collateral to raise funds that can be used for investment. Land can be mortgaged to release funds for the further development of other current assets or to support investment in a business or other venture, thereby stimulating the economy and potentially the quality of life of the individual citizens.

De Soto, in his attempt to unravel what he calls the “mystery of capital” (De Soto 2000) concludes that even in areas of great poverty there is great potential wealth. The poor cannot convert what he describes as “dead capital” into its real asset value, which is possibly worth trillions of dollars. He suggests that many poor people who do not live in the rich western economies are every bit as intelligent, innately skilled and hardworking as those in successful economies, but remain poor because of what he describes as the “Bell Jar Effect”. This occurs where those inside become rich because they are able to exploit property, but those outside are excluded by invisible barriers such as access to expert lawyers and the ability to navigate

the red tape of their property systems. The poor have no access to formal land markets and little or no access to credit.

Having a formal structure in place is necessary, but not sufficient to trigger the creation of greater wealth for more people. For land markets to work there must be the political will and the empowerment of all people to permit and encourage them to take part. This may necessitate some state intervention in the otherwise free market processes. Countries introducing a land market should ensure provision is made for capacity building to provide the new skills necessary to support the market, including general management skills.

In North Vietnam (Mekong Economics, 2004) a project was undertaken to assess the impact of De Soto's theory that land markets can be used to provide capital in under capitalised areas. The objectives of the project were to make the land market more efficient and effective so that it can be accessed by the poor and to understand why households choose to participate in the informal market rather than the formal market. The intention was to test whether an efficient and effective formal land market with supporting land administration infrastructure would serve the poor by providing them with access to land, security of tenure, improved environmental and land-use management and information to better inform policy development.

The report found that: the present procedures were long and complex; that there were benefits from economies of scale; that local government officials have an important role to play in administering the system; that many land transactions were carried out on a formal basis and that the formal costs of and transactions were not considered to be high; but the poor participated very little in land market activities. It also found that the level of understanding of the formal market procedures was relatively low hence the continued existence of informal markets. Conversely, it was found that commune representatives had a good grasp of what was actually going on at the grass roots level.

6. CONCLUSIONS

Ever increasing globalisation will almost certainly impact land markets especially as information technology, including web-based services, provides greater access to national land information services. Within the worldwide diversity of approaches to land markets a number of common themes are present when a thriving and efficient land market exists. There must be a sound land administration system, good land policy and a legal framework in place to underpin the land market. A fair and open land market needs guaranteed security of land rights; low transaction costs for all users; access to credit; transparency with openness and ease of access to all; protection of minorities; opportunities to raise revenues through land and property taxes; and support for environmental sustainability. It also can benefit from public/private partnerships that provide value-for-money services.

To encourage and support the land market it may be necessary for governments or international donors to provide start-up finance that will lead towards a self-financing status. Capacity building will be necessary to ensure that the appropriate skill sets are available as the market develops.

As societies become more complex, the range of interests in land and the types of transaction that take place become more complicated. In addition to simple sales and rental transactions, there may be first and secondary mortgages, environmental obligations, agricultural quotas etc. all of which may be bought or sold in the market place. Increasingly, cadastral records are not only used to support land transfers or land taxation, but as an information base for the marketing of non landownership-related goods and services, such as selling insurance policies or household effects.

Future trends in such a complex area are difficult to predict. However, it is clear that globalisation will mean that land markets will be seen in an international context and that governments will be encouraged to see land markets in a holistic way that includes environmental policy. Today there is pressure from a number of sources to address the issue of the property rights of those living in informal settlements. In addition, there is a need to improve the openness and accessibility of good quality land information for the benefit of all and to reduce the cost of both information and registration of land and property transactions. Developments in these areas will occur in the short to medium term. In the less developed economies the development of an efficient and effective land market may well be one of the most essential factors that will determine the economic stability of the national economy.

Perhaps one of the most far-reaching impacts of the land market is that it should lead to 'better citizenship'. Private land ownership is seen to encourage entrepreneurship and commitment and reduced dependency on the state, allowing governments to focus on their other responsibilities. Those who practice good stewardship of the land tend to engage in the whole social and democratic process. An efficient land market can create more favourable conditions within a country which, when combined with other economic and social factors, should encourage better citizenship and a better society.

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BIOGRAPHICAL NOTES

Rob Mahoney FRICS, FBCartS is Principal of MahGeo, an independent GI and LIS Consultancy. Rob is a Fellow of The Royal Institution of Chartered Surveyors and current Chairman of the RICS' Faculties and Forums Board. Rob has extensive experience in the management of land information, and land registration, together with the associated technologies and business processes. He has been engaged upon a wide variety of successful projects worldwide. He is also a former member of the UK Government's GI Information Panel.

Peter Dale retired as Professor in Land Information Management at University College London in 2001 since when he has retained his interest in land administration, helping to produce two important documents for the UNECE Working Party on Land Administration. He has been an international figure in the world of the cadastre for many years having studied and published widely in the field. He served as President of the International Federation of Surveyors from 1995-1999 when he was made an Honorary President.

Robin McLaren is director of Know Edge Ltd a UK based, independent management consulting company formed in 1986 specialising in optimising the business benefits of investments in Geographic Information (GI) systems and services. Robin has been at the forefront of the GIS revolution and is recognised as a world expert in Land Information Management and has worked extensively in Eastern Europe and world-wide to strengthen land tenure to support economic reforms. Robin has recently supported the UK Government in formulating a UK GI Strategy.

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