

Article

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Property Rights, Law, and Economic Development

Abstract: This article explores the relationship between property rights and economic performance. Property rights, or more precisely, formal, individualized property rights, have long been regarded as the fundamental precondition for sustainable economic growth. However, the available empirical evidence shows that formal private ownership fails to bring about desirable economic outcomes in most developing countries despite the advantages claimed by numerous economists and lawyers. This puzzle can be addressed by taking into consideration such factors as the functioning of related markets, the influence of social norms, and the role of the state.

Keywords: property rights, law, economic performance, norms, state

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1 Introduction

This article addresses the role of property rights in economic development. The notion that property rights profoundly influence economic performance is an old idea dating back to the late eighteenth century when Adam Smith wrote his *An Inquiry into the Nature and Causes of the Wealth of Nations*. According to Adam Smith, security of property rights against expropriation by fellow citizens or the state is an important condition for encouraging individuals to invest and accumulate capital, which, in turn, would boost economic growth. Smith's wisdom remains relevant and has been reinvigorated by contemporary economists, especially new institutional economists, who have used history and theory to make the case that property rights are crucial to long-run economic success or failure.

Ronald Coase, the founder of new institutional economics, pioneered a theoretical framework for understanding the effects of property rights in his

“The Problem of Social Cost”.¹ Coase’s seminal work was gradually extended and refined by Alchian,² Demsetz,³ Furubotn and Pejovich,⁴ De Alessi,⁵ Barzel,⁶ and others and eventually yielded a general approach that focuses on the relationship between property rights and the allocation and use of resources. According to the Coasean analysis, property rights are crucial to economic performance: “in all societies, primitive and modern, property rights are an important part of social technology that helps to determine economic efficiency.”⁷

The virtue of property rights, especially private property rights enforced by the state or formal private property rights (henceforth FPPR), has been further manifested by numerous historical and comparative studies. For example, in their influential book, North and Thomas⁸ attribute the rise of the western world, and particularly the success of the Netherlands and England, to the creation and development of effective private ownership in those countries and the resulting incentives necessary for sustained growth. This view is shared and extended by North,⁹ Rosenberg and Birdzell,¹⁰ and Pipes.¹¹ Compared to an economy based on private ownership, or so-called capitalism, the communist system, with a prevalence of state ownership, suffered from significant economic inefficiency and welfare loss, which finally wiped that system out.¹²

1 Ronald H. Coase, *The Problem of Social Cost*, 3 *Journal of Law and Economics* (1960), 1–44.

2 Armen A. Alchian, *Some Economics of Property Rights*, 30 *Il Politico* (1965), 816–829.

3 Harold Demsetz, *Toward a Theory of Property Rights*, 57 *American Economic Review* (1967), 347–359.

4 Eirik G. Furubotn and Svetozar Pejovich, *Property Rights and Economic Theory: A Survey of Recent Literature*, 10 *Journal of Economic Literature* (1972), 1137–1162.

5 Louis De Alessi, *The Economics of Property Rights: A Review of the Evidence*, 2 *Research in Law and Economics* (1980), 1–47.

6 Yoram Barzel, *Economic Analysis of Property Rights* (Cambridge: Cambridge University Press, 1997).

7 Martin J. Bailey, “Property Rights in Aboriginal Societies”, in Peter Newman (ed.), *The New Palgrave Dictionary of Economics and Law* (London: Macmillan Reference LTD, 1998), 155–157.

8 Douglass C. North and Robert Paul Thomas, *The Rise of the Western World: A New Economic History* (New York: Cambridge University Press, 1973).

9 Douglass C. North, *Structure and Change in Economic History* (New York: W.W. Norton & Company, 1981).

10 Nathan Rosenberg and L. E. Birdzell Jr., *How the West Grew Rich: The Economic Transformation of the Industrial World* (New York: Basic Books, 1986).

11 Richard Pipes, *Property and Freedom* (London: The Harvill Press, 1999).

12 See, for instance, Svetozar Pejovich, *The Economics of Property Rights: Towards a Theory of Comparative Systems* (Dordrecht: Kluwer Academic Publishers, 1990); Janos Kornai, *The Socialist System: The Political Economy of Communism* (Princeton, NJ: Princeton University Press, 1992).

However, in empirical studies concerning the effects of formal private ownership, particularly those conducted on the microlevel in developing countries, the picture is mixed: although many of the studies report positive and significant effects of FPPR on investment and other measures of economic performance, others fail to find a strong link between FPPR and economic outcomes. Consequently, as Besley admits, in spite of its theoretical importance, empirical support for the significance of private property for economic outcomes remains limited.¹³

Why does this discrepancy exist? Why have institutions of property rights in general, and FPPR in particular, whose significance has been endorsed by numerous theoretical and historical studies, failed to demonstrate its positive effects in many developing countries? These questions will be tentatively answered in this article by examining the institutional context within which a regime of FPPR emerges, functions, and evolves. In other words, property rights will be treated endogenously rather than exogenously: after surveying theoretical and empirical studies on the relationship between property rights and economic performance, we will build a simple cost–benefit analysis framework to explore the fundamental factors that may determine the effectiveness and efficiency of the FPPR regime, such as the functioning of related markets, the influence of social norms, and the role of the state.

Our study will help us to understand the role of property rights in a more balanced way. We will show that the alleged benefits of formal private ownership cannot be taken for granted when such factors as the cost of creating and maintaining a formal property regime, the complicated interaction between law and social norms, and the effectiveness of the state are taken into consideration. In other words, FPPR will not emerge and function just because they are *demande*d; they have to be *supplied* by the state in a cost-effective manner. States in the developing world, however, frequently fail to complete this task. The failure in the supply side of property rights therefore implies that FPPR might cause rather than solve economic problems in many developing and transitional countries.

The rest of the article is organized as follows. Section 2 discusses theoretical arguments on the desirability of formal private ownership. Section 3 reviews empirical studies on the relationship between formal private ownership and economic performance. Section 4 offers some explanations of the failure of formal private ownership in most developing countries. Finally, we conclude in Section 5.

¹³ Timothy Besley, “Investment Incentives and Property Rights”, in Peter Newman (ed.), *The New Palgrave Dictionary of Economics and Law* (London: Macmillan Reference LTD, 1998).

2 Property rights and economic performance: theory

In the state of open access, where no one has the legal right to exclude anyone from using a resource, nobody owns the resource, so the external cost in terms of reduced resource availability is not internalized by individual users. An obvious and straightforward solution to open access is to create and distribute private ownership, through which an externality can be internalized to a great extent. Under perfect private ownership, owners capture the full benefits of their decisions and bear the corresponding costs by excluding anyone else from using the resource, so they face a strong incentive for optimal asset use, maintenance, and investment.¹⁴ In addition, private property rights are extolled because resources governed by this regime are transferable to others by sale or gift at mutually agreed-upon terms. Transferability, then, acts as an effective mechanism through which resources can move from less productive to more productive owners.¹⁵ Compared with other forms of property rights such as common property regimes,¹⁶ private ownership reduces the costs of delineating rights and monitoring for compliance because “monitoring boundary crossings is easier than monitoring the behavior of persons situated inside boundaries.”¹⁷

Private ownership is usually enforced by public authorities, such as courts, and hence can be characterized as a claim enforceable against others by formal law. Formal property rights defined and enforced by the state – an organization “which has a comparative advantage in violence”¹⁸ – are believed to be clearer and more secure than informal property rights enforced by private power or community-based norms, and hence the former are more helpful for economic growth. First, as a (credible) third party, the state can lower the transaction costs related to property rights by developing an impersonal judicial system, which will help to capture important economies of scale by providing more standardized enforcement of property rights to more people in a broader territory and make the punishment of wrongdoing more credible by isolating the enforcers from the enforced parties.

¹⁴ Demsetz (1967), *supra* note 3.

¹⁵ Richard A. Posner, *Economic Analysis of Law* (New York: Aspen Publishers, 2002).

¹⁶ Common property rights may be viewed as an intermediate step between open access and private ownership, emerging as an institutional solution when a resource is sufficiently valuable to justify the cost of organizing a user group, but not the cost of defining and enforcing private property rights. A fundamental problem for community members is the task of designing an effective internal governance structure to prevent excessive use and to ensure continued maintenance and improvement.

¹⁷ Robert C. Ellickson, *Property in Land*, 102 *Yale Law Journal* (1993), 1315–1400.

¹⁸ North (1981), *supra* note 9.

Second, informal substitutes for legal enforcement of property rights can function only to a limited extent and result in inefficient outcomes in some cases; for example, reliance on extralegal norms for enforcement may limit one's possible business partners to a small number of individuals with whom one is familiar, preventing potentially mutually beneficial exchanges involving strangers.¹⁹

More specifically, there are five channels through which FPPR can affect economic activities. The first claim is that private property encourages individuals to use their resources in the most socially efficient way because, under a private property regime, all costs and benefits of individual action are internalized by decision makers.²⁰ As studies on open access have shown, without private property rights, resources are highly prone to over-exploitation and degradation, especially when population densities increase or if resources are commercially valuable.²¹

The second mechanism through which private property influences economic efficiency is that, where property is relatively secure, resources will be maintained in productive uses rather than being diverted to unproductive uses such as invasion and self-defense.²² Even in developed countries with well-functioning governments, private protection of property rights, such as private security guards hired by firms and neighborhood-watch groups organized by homeowners, is not uncommon. In some extreme cases where the government does not enforce property rights, individuals will seek out an alternative enforcer of property rights, such as organized crime in Japan and Sicily. These organizations frequently employ threats and sometimes violence.²³

The third channel, which has attracted the most attention in theoretical and empirical research, concerns the effects of property rights on investment. Property rights, or more precisely, security of property, influence investment decisions in two ways.²⁴ First, the values of all investments attached to an asset

¹⁹ Frank B. Cross, *Law and Economic Growth*, 80 *Texas Law Review* (2002), 1737–1775.

²⁰ See, for instance, Demsetz (1967), *supra* note 3; Armen A. Alchian and Harold Demsetz, *The Property Rights Paradigm*, 33 *Journal of Economic History* (1973), 16–27.

²¹ See, for instance, Garrett Hardin, *The Tragedy of the Commons*, 162 *Science* (1968), 1243–1248.

²² See, for instance, Stergios Skaperdas, *Cooperation, Conflict, and Power in the Absence of Property Rights*, 82 *American Economic Review* (1992), 720–739; Herschel Grossman and Minseong Kim, *Swords or Plowshares? A Theory of the Security of Claims to Property*, 103 *Journal of Political Economy* (1995), 1275–1288.

²³ Curtis J. Milhaupt and Mark D. West, *The Dark Side of Private Ordering: An Institutional and Empirical Analysis of Organized Crime*, 67 *University of Chicago Law Review* (2000), 41–98; Diego Gambetta, *The Sicilian Mafia: The Business of Private Protection* (Cambridge, MA: Harvard University Press, 1993).

²⁴ See, for instance, Omotunde E.G. Johnson, *Economic Analysis, the Legal Framework and Land Tenure Systems*, 15 *Journal of Law and Economics* (1972), 259–276; Besley (1998), *supra* note 13.

will decline when the asset faces the risk of expropriation, and hence, the volume of such investments will be reduced. Second, the risk of expropriation changes the relative returns on different investments, diverting investments toward assets that are less uncertain but less productive. For example, investments move from fixed assets, such as trees and irrigation, to more portable assets, such as livestock, and from long-term to short-term projects.

Assets with formal titles, for example, registered or titled lands, are widely believed to improve access to credit for their owners.²⁵ When a lender is assured that an asset pledged as collateral is secure and free of competing claims, he will become more willing to make loans based on the collateral, reducing the lender's cost of information regarding the borrower's creditworthiness and the risk of default. Consequently, the interest rate for the borrower is lowered and the volume of credit offered is expanded, encouraging investment in assets.

Finally, when property rights are clear and secure, the transaction costs involved in identifying the real owner of the property and making and enforcing a lease or sale contract are reduced to the extent that property markets can function effectively in transferring the property from less efficient uses to more efficient uses.²⁶ In addition, improving the transferability of property can improve investment incentives when the gains from trade increase the owner's marginal return to the property²⁷; a well-developed property market is also conducive to the development of financial markets by making collateral-based credit more extensive.

3 Property rights and economic performance: evidence

Numerous academic efforts have examined the effects of property rights, particularly FPPR, on economic performance empirically along the five dimensions we have discussed. Some studies of the relationship between property rights and resource management confirm the superiority of private property rights over open access (and common ownership) in guiding efficient resource use. In one

²⁵ See, for instance, David A. Atwood, *Land Registration in Africa: The Impact on Agricultural Production*, 18 *World Development* (1990), 659–671; Besley (1998), *supra* note 13; Klaus Deininger, *Land Policies for Growth and Poverty Reduction* (Washington, DC: The World Bank, 2003).

²⁶ See, for instance, Johnson (1972), *supra* note 24; Richard Barrows and Michael Roth, *Land Tenure and Investment in African Agriculture: Theory and Evidence*, 28 *Journal of Modern African Studies* (1990), 265–297; Deininger (2003), *supra* note 25.

²⁷ Besley (1998), *supra* note 13.

of the pioneering works on this topic, Bottomley²⁸ finds that Arab tribesmen in the Libyan province of Tripolitania used communal land for low-valued uses, such as growing occasional crops of barley and grazing privately owned sheep and goats, rather than for more profitable activities, such as almond-tree planting. Using both cross-sectional and time series data from the U.S. East Coast and Gulf Coast oyster industry, Agnello and Donnelley²⁹ show that labor productivity was higher in privately leased oyster grounds than in government-regulated open-access grounds. Anderson and Lueck³⁰ exploit a sample of 39 Indian reservations to estimate the effect of land tenure on agricultural productivity. They find that the per-acre value of agricultural output is 85–90% lower on tribal-trust land than on fee-simple land and 30–40% lower on individual-trust land than on fee-simple land.³¹ Grafton, Squires, and Fox³² test for changes in efficiency in the same resource (the British Columbia halibut fishery) following privatization of property rights, and they find that privatization leads not only to efficient input usage but also to a substantial producer surplus. In addition to negative effects on productivity, common ownership is demonstrated to be ineffective in controlling resource over-exploitation problems and hence conducive to land degradation and resource depletion.³³

There are plenty of cases, however, that challenge the reported inefficiency of common property in resource allocation and exploitation.³⁴ For example, in Töbel, Switzerland, a village of only 600 people, communal space for cattle

28 Anthony Bottomley, *The Effect of the Common Ownership of Land Upon Resource Allocation in TripoliTania*, 39 *Land Economics* (1963), 91–95.

29 Richard J. Agnello and Lawrence P. Donnelley, *Property Rights and Efficiency in the Oyster Industry*, 18 *Journal of Law and Economics* (1975), 521–533.

30 Terry L. Anderson and Dean Lueck, *Land Tenure and Agriculture Productivity on Indian Reservations*, 35 *Journal of Law and Economics* (1992), 427–454.

31 Tribal-trust land is managed by the tribe subject to trust constraints administered by the Bureau of Indian Affairs (BIA). Under fee simple, the land is privately owned by individuals who are free to use, lease, and sell it. Under individual trust, the land is held by individual Indians, but their rights are subject to trust constraints administered by the BIA.

32 R. Quentin Grafton, Dale Squires, and Kevin J. Fox, *Private Property and Economic Efficiency: A Study of a Common-Pool Resource*, 43 *Journal of Law and Economics* (2000), 679–713.

33 See, for instance, Ramón López, *Environmental Externalities in Traditional Agriculture and the Impact of Trade Liberalization: The Case of Ghana*, 53 *Journal of Development Economics* (1997), 17–39; Vinod Ahuja, *Land Degradation, Agricultural Productivity and Common Property: Evidence from Côte d'Ivoire*, 3 *Environment and Development Economics* (1998), 7–34.

34 See, for instance, Elinor Ostrom, *Governing the Commons: The Evolution of Institutions for Collective Action* (New York: Cambridge University Press, 1990); Jean-Marie Baland and Jean-Philippe Platteau, *Halting Degradation of Natural Resources: Is There a Role for Rural Communities* (Oxford: FAO and Clarendon Press, 1996).

grazing is regulated by an alp association, which is governed by the villagers themselves. Although yields are relatively low, the land in Töbel has maintained its productivity for many centuries, and overgrazing has been prevented by tight controls. Furthermore, some studies find that privatization of resources has not served as a panacea for their conservation; in fact, in many cases, it has contributed to accelerated destruction of resources. For example, in India, privatization of land accelerated the destruction of native vegetation.³⁵

There is clear evidence that individuals will divert resources to unproductive uses, such as inefficient investment, expensive self-protection, and even violent conflict, when property rights are insecure. For example, De Vany and Sanchez³⁶ find that ejidatarios³⁷ in Mexico exhibit higher fertility than comparable groups because children help the parents to secure their rights to land. The relationship between land security and fertility can also be observed in Thailand, the Philippines, Iran, Egypt, and India.³⁸ By a similar token, Field³⁹ shows that a titling program issued by the Peruvian government with the aim of converting informal property in urban squatter settlements into formal property has greatly reduced the human resources that untitled households devote to maintaining tenure security through informal means. This change resulted in both an increase in total labor force hours and a reallocation of work hours from inside the home to the outside labor market. In Buenos Aires, Argentina, when squatters obtained formal land rights as a result of an expropriation law enacted by Congress in 1984, this change was found to increase squatters' housing investments, reduce household sizes, and improve the education of their children.⁴⁰

The empirical linkage between property rights and investment has been of the utmost concern to economists and is the subject of numerous studies

35 N.S. Jodha, *Common Property Resources: A Missing Dimension of Development Strategies*, World Bank Discussion Paper, No. 169 (1992).

36 Arthur De Vany and Nicolas Sanchez, *Land Tenure Structures and Fertility in Mexico*, 61 *Review of Economics and Statistics* (1979), 67–72.

37 An ejidatario is a member of an ejido, an agrarian community that has received and continues to hold land in accordance with the agrarian law established after the Mexican Revolution. In a typical ejido, all rights to crop lands are granted to individual families on a usufruct basis. The land cannot be sold, leased, mortgaged, or disposed of in any similar fashion. Rights to these lands may be passed on to heirs, but they may also be lost if the land is not under cultivation for two consecutive years.

38 Shannon Stokes, Wayne A. Schutjer, and Rodolfo A. Bulatao, *Is the Relationship between Landholding and Fertility Spurious? A Response to Cain*, 40 *Population Studies* (1986), 305–311.

39 Erica Field, *Entitled to Work: Urban Property Rights and Labor Supply in Peru*, 122 *Quarterly Journal of Economics* (2007), 1561–1602.

40 Sebastian Galiani and Ernesto Scharfrodsky, *Property Rights for the Poor: Effects of Land Titling*, Working Paper (Universidad Torcuato Di Tella, 2006).

covering the majority of developing countries; unfortunately, the evidence does not systematically confirm the linkage that the theory suggests. The evidence from Asian and Latin American countries is stronger. For example, Feder and Onchan⁴¹ find that, in two provinces in Thailand, farmland security (possession of land title) implies greater capital formation, higher capital/land ratios, and higher levels of land improvement. In China, Li et al.⁴² and Jacoby et al.⁴³ use household data from northeast China to show that land tenure security significantly affects land-specific investment, specifically investment in soil quality (organic fertilizer). In India, Pender and Kerr⁴⁴ find that soil and water conservation investment is significantly lower on leased land in two of the study villages and lower on plots that are subject to sales restrictions in one village. In Vietnam, the land law of 1993, which gave households the power to exchange, transfer, lease, inherit, and mortgage their land-use rights, is found to lead to a significant increase in the share of total area devoted to multi-year crops and to some increase in irrigation investment.⁴⁵ In Brazil, the results of the household survey confirm that ownership security (i.e., whether the farmer holds the title to his land) plays an important role in promoting investment in land improvements.⁴⁶ Land titling and registration are also found to be associated with increased investments in Guatemala and Nicaragua.⁴⁷ In addition to rural areas, tenure security is demonstrated to influence residential investment in urban squatter neighborhoods in Peru and Argentina.⁴⁸

41 Gershon Feder and Tongroj Onchan, *Land Ownership Security and Farm Investment in Thailand*, 69 *American Journal of Agricultural Economics* (1987), 311–320.

42 Guo Li, Scott Rozelle, and Loren Brandt, *Tenure, Land Rights, and Farmer Investment Incentives in China*, 19 *Agricultural Economics* (1998), 63–71.

43 Hanan G. Jacoby, Guo Li, and Scott Rozelle, *Hazards of Expropriation: Tenure Insecurity and Investment in Rural China*, 92 *American Economic Review* (2002), 1420–1447.

44 John L. Pender and John M. Kerr, *Determinants of Farmers' Indigenous Soil and Water Conservation Investments in Semi-Arid India*, 19 *Agricultural Economics* (1998), 113–125.

45 Quy-Toan Do and Lakshmi Iyer, *Land Rights and Economic Development: Evidence from Vietnam*, World Bank Policy Research Working Paper No. 3120 (2003).

46 Lee J. Alston, Gary D. Libecap, and Robert Schneider, *The Determinants and Impact of Property Rights: Land Titles on the Brazilian Frontier*, 12 *Journal of Law, Economics, and Organization* (1996), 25–61.

47 Thomas Schweigert, *Land Title, Tenure Security, Investment and Farm Output: Evidence from Guatemala*, 40 *Journal of Developing Areas* (2006), 115–126; Klaus Deininger and Juan Sebastian Chamorro, *Investment and Equity Effects of Land Regularisation: The Case of Nicaragua*, 30 *Agricultural Economics* (2004), 101–116.

48 Erica Field, *Property Rights and Investment in Urban Slums*, 3 *Journal of the European Economic Association* (2005), 279–290; Galiani and Scharrogradsky (2006), *supra* note 40.

For Africa, the picture is more mixed. An early study reviews empirical evidence from Kenya, Uganda, and Zimbabwe and concludes that “there is little empirical evidence to support the hypothesis that registration, through increased tenure security, has increased investment in agriculture.”⁴⁹ Migot-Adholla et al.⁵⁰ use cross-sectional evidence from Ghana, Kenya, and Rwanda in 1987–1988 to show that the relationship between land rights (the level of individualization of land rights, especially the extent of transfer or alienation rights) and land improvements is far from clear. The relative insignificance of the effects of land ownership on investments is further supported by findings from Uganda⁵¹ and Madagascar.⁵² By contrast, in a very influential paper, Besley⁵³ uses data from two regions of Ghana (Wassa and Anloga) and finds that land improvements in Wassa (in the form of tree planting) are significantly related to land rights, whereas land improvements in Angola (including drainage and continuous fertilizing) have no such relationship. Similarly, Gavian and Fafchamps⁵⁴ find evidence that tenure insecurity incites farmers to divert scarce manure resources to more secure fields (owned fields rather than borrowed fields) whenever they can. Furthermore, Place and Otsuka⁵⁵ confirm the effects of tenure security on incentives for making long-term investments to boost agricultural production in their study of Malawi.

The evidence on the credit effects of formal property rights is also ambiguous. An early study conducted by Feder and Onchan⁵⁶ shows that farm land security in Thailand (possession of land title) increased access to institutional

⁴⁹ Barrows and Roth (1990), *supra* note 26.

⁵⁰ Shem Migot-Adholla, Peter Hazell, Benoît Blarel, and Frank Place, *Indigenous Land Rights Systems in Sub-Saharan Africa: A Constraint on Productivity*, 5 World Bank Economic Review (1991), 155–175.

⁵¹ Frank Place and Keijiro Otsuka, *Land Tenure Systems and Their Impacts on Agricultural Investments and Productivity in Uganda*, 38 Journal Development Studies (2002), 105–128; John L. Pender, Ephraim Nkonya, Pamela Jagger, Dick Sserunkuuma, and Henry Ssali, *Strategies to Increase Agricultural Productivity and Reduce Land Degradation: Evidence from Uganda*, 31 Agricultural Economics (2004), 181–195.

⁵² Hanan G. Jacoby and Bart Minten, *Is Land Titling in Sub-Saharan Africa Cost-Effective? Evidence from Madagascar*, 21 World Bank Economic Review (2007), 461–485.

⁵³ Timothy Besley, *Property Rights and Investment Incentives: Theory and Evidence from Ghana*, 103 Journal of Political Economy (1995), 903–937.

⁵⁴ Sarah Gavian and Marcel Fafchamps, *Land Tenure and Allocative Efficiency in Niger*, 78 American Journal of Agricultural Economics (1996), 460–471.

⁵⁵ Frank Place and Keijiro Otsuka, *Tenure, Agricultural Investment, and Productivity in the Customary Tenure Sector of Malawi*, 50 Economic Development and Cultural Change (2001), 77–99.

⁵⁶ Feder and Onchan (1987), *supra* note 41.

credit, yielding greater capital formation. In Peru, land titling is found to be associated with a 9- to 10-percentage-point increase in approval rates from the public sector bank for loans to be used for housing construction materials.⁵⁷ In Argentina, the evidence indicates a positive (but modest) effect of land titling on access to mortgage credit and no effect on access to other forms of credit, such as credit cards and bank accounts.⁵⁸ Again, empirical studies in rural Africa fail to find a significant relationship between the possession of a title and the use of formal credit.⁵⁹

In some studies, land titling is claimed to stimulate land transactions and increase the value of titled property relative to untitled property. For example, Jimenez⁶⁰ compares unit housing prices between the non-squatter (formal) sector and the squatter (informal) sector in the city of Davao, the Philippines, and finds that unit dwelling prices are 58% higher in the formal sector than in the informal sector. Based on interviews with real estate brokers in Jakarta, Dowall and Leaf⁶¹ show that land prices were affected strongly by the level of tenure security. Feder and Nishio⁶² report that 3–4 years after the issuance of title deeds under the Land Titling Project, the land market in Thailand was more active in the project area compared with the non-project area. In Brazil, Alston et al.⁶³ find that the effect of a title on land value is positive and significant. In Nicaragua, registration is found to increase land values by 30%.⁶⁴ In Ecuador, Lanjouw and Levy⁶⁵ find that holding a title is associated with a sizable increase in the market value of properties (on average, 23.5% of untitled property values).

On the other hand, the evidence shows that formal property rights are not a prerequisite for the development of an active land market, especially in African

⁵⁷ Erica Field and Maximo Torero, *Do Property Titles Increase Credit Access Among the Urban Poor? Evidence from a Nationwide Titling Program*, Working Paper, (Harvard University, 2004).

⁵⁸ Galiani and Scharrodsky (2006), *supra* note 40.

⁵⁹ Migot-Adholla et al. (1991), *supra* note 50; Frank Place and Peter Hazell, *Productivity Effects of Indigenous Land Tenure Systems in Sub-Saharan Africa*, 75 *American Journal of Agricultural Economics* (1993), 10–19; Thomas C. Pinckney and Peter K. Kimuyu, *Land Tenure Reform in East Africa: Good, Bad, or Unimportant*, 3 *Journal of African Economics* (1994), 1–28.

⁶⁰ Emmanuel Jimenez, *Tenure Security and Urban Squatting*, 66 *Review of Economics and Statistics* (1984), 556–567.

⁶¹ David E. Dowall and Michael Leaf, *The Price of Land for Housing in Jakarta*, 28 *Urban Studies* (1991), 707–722.

⁶² Gershon Feder and Akihiko Nishio, *The Benefits of Land Registration and Titling: Economic and Social Perspectives*, 15 *Land Use Policy* (1999), 25–43.

⁶³ Alston et al. (1996), *supra* note 46.

⁶⁴ Deininger and Chamorro (2004), *supra* note 47.

⁶⁵ Jean O. Lanjouw and Philip I. Levy, *Untitled: A Study of Formal and Informal Property Rights in Urban Ecuador*, 112 *Economic Journal* (2002), 986–1019.

countries. In Kenya, a well-functioning land market has not been created as a result of land registration.⁶⁶ A survey of 16 different areas of 6 African countries with titling programs (Kenya, Rwanda, Burundi, Uganda, Malawi, and Zambia) showed that, on average, only 16% of the land parcels were acquired through market purchases, whereas 63% were obtained through inheritances and various kinds of gift transfers and the rest through other means, primarily state allocation.⁶⁷ Similarly, in Ho Chi Minh City (HCMC), Vietnam, Kim⁶⁸ shows that a real estate market continued to flourish in spite of the fact that about half of houses did not have legal titles.

4 Why formal private property rights may fail

4.1 Malfunctioning or nonexistence of related factor markets

Whether FPPR can bring about desirable economic outcomes, as many economists and lawyers expect, depends strongly on the existence and operation of related factor markets, such as credit markets, labor markets, and insurance markets, which cannot be created or maintained by a property rights regime per se. For example, Feder and Feeny⁶⁹ find that most of the impact of land ownership on investment in Thailand “stemmed from the fact titles increased farmer’s access to credit, rather than from the elimination of actual risk to the land rights of the farmers.” Deininger⁷⁰ also argues that land rental markets and land sales markets will not work well if there are imperfections in the aforementioned factor markets. Therefore, when factor markets cannot be introduced or sustained or there are significant distortions and imperfections in these markets, as we can see in many developing countries, the effects of property rights tend to be invalidated.

Taking credit markets as an example, the World Bank⁷¹ reports that most African countries opted to create at least one large state bank after gaining their

⁶⁶ Barrows and Roth (1990), *supra* note 26.

⁶⁷ Jean-Philippe Platteau, *Institutions, Social Norms, and Economic Development* (Amsterdam: Harwood Academic Publishers, 2000).

⁶⁸ Annette M. Kim, *A Market without the “Right” Property Rights: Ho Chi Minh City, Vietnam’s Newly-Emerged Private Real Estate Market*, 12 *Economics of Transition* (2004), 275–305.

⁶⁹ Gershon Feder and David Feeny, *Land Tenure and Property Rights: Theory and Implications for Development Policy*, 5 *World Bank Economic Review* (1991), 135–153.

⁷⁰ Deininger (2003), *supra* note 25.

⁷¹ World Bank, *Finance for Growth: Policy Choices in a Volatile World* (New York: Oxford University Press, 2001).

independence to support indigenous industries and state ventures and to make banking services available for the broad population, including those in rural areas. In many countries, these large state banks still dominate the banking sector. After decades of politicized management and soft budget constraints, they have found it difficult to restructure or privatize. Higher government ownership of banks is shown, however, to be associated with slower financial development⁷² and with lower efficiency and stability of the banking sector.⁷³

Financial market distortions impose significant barriers on access to financing for households and small and medium enterprises (SMEs). Beck et al.⁷⁴ report that although more than 90% of households in several European countries have a bank account, less than half of households in many developing countries have one, and in many African countries fewer than one in five households has an account. In addition, small firms report lack of financing to be one of the most important business constraints they face: for example, fewer than 20% of small firms use external financing. In that case, the impact of land title or registration on credit-related increases in capital investment will be reduced substantially, as Atwood⁷⁵ argues.

In addition, where informal credit markets function well and can substitute for the formal markets to a great extent, land titling will also be of limited value. For example, in one Thai province where informal lending was predominant, Feder and Onchan⁷⁶ find that the impact of land titling on credit access was negligible. Atwood⁷⁷ also argues that although informal lenders in other parts of the world may accept informal, unregistered land claims as collateral if the lenders are close enough to the community to have low-cost information on the legitimacy of informal land claims and if they can foreclose on land when a borrower defaults, informal lending in Africa is seldom, if ever, secured by land, but rather by other property or by a combination of social custom and goodwill.

Finally, when the judicial system is ineffective or partial, when people do not recognize formal land ownership as legitimate or accept its distributive consequences, or when administrative agencies fail to maintain a valid titling

⁷² See, for instance, Rafael La Porta, Florencio Lopez-de-Silanes, and Andrei Shleifer, *Government Ownership of Banks*, 57 *Journal of Finance* (2002), 265–301.

⁷³ See, for instance, James R. Barth, Gerard Caprio Jr., and Ross Levine, *Bank Regulation and Supervision: What Works Best*, 13 *Journal of Financial Intermediation* (2004), 205–248.

⁷⁴ Thorsten Beck, Asli Demirgüç-Kunt, and Patrick Honohan, *Access to Financial Services: Measurement, Impact, and Policies*, 24 *World Bank Research Observer* (2009), 119–145.

⁷⁵ Atwood (1990), *supra* note 25.

⁷⁶ Feder and Onchan (1987), *supra* note 41.

⁷⁷ Atwood (1990), *supra* note 25.

and registration system, titled land will not be considered as a reliable form of collateral by lenders because it is difficult to foreclose.⁷⁸

4.2 Costs of formal property rights

Creating and maintaining a formal property regime involves a variety of costs, including the costs of establishing a property registration system. An effective land title registration system is, however, expensive. Establishment of the system will likely take several years to complete and will consume valuable physical and human resources that could otherwise be used for other socially desirable projects. Moreover, operation and maintenance of the system, once established, will require significant additional resources. In the World Bank's 2008 "Doing Business" report, the mean cost associated with property registration in 173 countries amounted to 6.6% of the property's value, and the mean waiting time was 81 days. The cost of registering property is highly bimodal; whereas it is 2% or less of property values in 32 cases, it amounts to 5 or 10% and over 10% of property values in 92 and 41 cases, respectively.⁷⁹ In some extreme cases, such as Syria, the cost of registering property is about 28.05% of property value, while in Kiribati it takes 523 days to register property. Consequently, as Barnes and Griffith-Charles⁸⁰ show, when the costs exceed the benefits (in terms of increased security) that users obtain from registering, they will return to the informal system to convey and divide their land, and the sustainability of the land registry system will be seriously compromised by this process of "deformalization."

In addition to the direct costs of a land registration system, the discrepancies between title documents and reality resulting from ineffective operation of this system constitute another major disappointment of the land titling programs in developing countries.⁸¹ Without sufficient administrative capabilities, succession and other transfers of title have gone largely unregistered, so the land registration system poorly reflects the present-day reality, thus destroying the utility of the system and engendering new uncertainties. In some other cases,

⁷⁸ See, for instance, Platteau (2000), *supra* note 67.

⁷⁹ Klaus Deininger and Gershon Feder, *Land Registration, Governance, and Development: Evidence and Implications for Policy*, 24 World Bank Research Observer (2009), 233–266.

⁸⁰ Grenville Barnes and Charisse Griffith-Charles, *Assessing the Formal Land Market and Deformalization of Property in St. Lucia*, 24 Land Use Policy (2007), 494–501.

⁸¹ See, for instance, Platteau (2000), *supra* note 67; Michael Trebilcock and Paul-Erik Veel, *Property Rights and Development: The Contingent Case for Formalization*, 30 University of Pennsylvania Journal of International Law (2008), 397–481.

such as in Nicaragua and Bolivia, the title to the same piece of land is delivered to separate parties when more than one government agency has the authority to title land but there is neither a clear distinction between their geographic jurisdictions nor any cooperation between the two agencies.⁸² Finally, in some Latin American countries, such as Guatemala, over-centralization of registry institutions renders the registration service highly inaccessible for residents of remote areas.

4.3 Property law and customary land system

In many developing countries, customary land ownership continues to be more important in governing land issues than formal property law is.⁸³ Generally, in most African countries, the formal land system covers at most between 2 and 10% of the total land area.⁸⁴ In addition, the customary law tenure is found to be flexible enough to adapt to a new environment and secure enough to warrant land-related investments. Studies from all parts of Africa indicate that, under normal circumstances, customary land ownership guarantees basic tenure security (measured in terms of use rights and transfer rights) to all villagers (even migrants), and it is sufficient to induce investment; there would be no increased security under formal title and therefore no direct impact on investment.⁸⁵ It is also not surprising to find an ambiguous relationship between land markets and land titling given the fact that market-style land transfers have developed in customary regimes, especially where land is relatively scarce and the efficiency gains from market transfers are high.⁸⁶

When the state in the developing world tries to replace customary land tenure with formal property law but fails to fill the gap in provision of important

82 Grenville Barnes, David Stanfield, and Kevin Barthel, *Land Registration Modernization in Developing Economies: A Discussion of the Main Problems in Central/Eastern Europe, Latin America, and the Caribbean*, 12 *URISA Journal*, no. 4 (2000), 33–42.

83 See, for instance, Barrows and Roth (1990), *supra* note 26; Pinckney and Kimuyu (1994), *supra* note 59.

84 Deininger (2003), *supra* note 25.

85 See, for instance, Atwood (1990), *supra* note 25; Pinckney and Kimuyu (1994), *supra* note 59; Frank Place, *Land Tenure and Agricultural Productivity in Africa: A Comparative Analysis of the Economics Literature and Recent Policy Strategies and Reforms*, 37 *World Development* (2009), 1326–1336.

86 See, for instance, Catherine André and Jean-Philippe Platteau, *Land Relations under Unbearable Stress: Rwanda Caught in the Malthusian Trap*, 34 *Journal of Economic Behavior and Organization* (1998), 1–47; Platteau (2000), *supra* note 67.

social services left by the withdrawal of a communal regime, such as the social safety net function performed by communal land, a significant efficiency loss will be incurred. As Bromley and Chavas⁸⁷ state, the absence of a right to exclude someone desperately in need of the means of life means that risks are more effectively pooled, and a common property regime can therefore be seen as an integral part of risk sharing strategies. Therefore, where incomplete insurance markets exist because of either information asymmetries or limits of contract, if individuals are sufficiently risk averse and the efficiency gains from privatization are sufficiently limited, privatization of communal land can be welfare-decreasing.⁸⁸

As Meinzen-Dick and Mwangi⁸⁹ show, in many rural communities that remain largely dependent on agriculture and natural resources for their livelihoods, property rights to land are better understood as a “web of interests,” with many different parties having a right to use, regulate, or manage the resource. Therefore, most land is subject to multiple and overlapping claims by several different kinds of groups. In addition, customary land tenure is considered to be adaptive, flexible, and dynamic, given the fact that “land rights are subject to intermittent or on-going negotiation, and tenure security depends more on a person’s standing with his/her relatives and neighbors than on the way in which a claim was originally acquired.”⁹⁰ It is very hard, or even impossible, to codify and register the complex bundles of rights associated with given parcels, especially in view of the high information and transaction costs faced by most developing countries. When customary group rights are extinguished by formalization, the state’s failure to record all existing land rights will therefore lead to a cutting of this web, and legitimate claimants, such as women, youth, and seasonal users, among others, may be denied legal recognition of their traditional rights to land. The formalization of property rights thus becomes an important source of social conflict.

In some other cases, land tenure formalization may even be regarded as illegitimate when the elites manipulate titling programs to the extent that poor or otherwise vulnerable land users are dispossessed of their rights to land. In Barrows and Roth’s words, “registration effectively provided a mechanism for

87 Daniel W. Bromley and Jean-Paul Chavas, *On Risk, Transactions and Economic Development in the Semi-arid Tropics*, 37 *Economic Development and Cultural Change* (1989), 719–736.

88 See, for instance, Jean-Philippe Platteau and Patrick Francois, *Commons as Insurance and the Welfare Impact of Privatization*, 89 *Journal of Public Economics* (2005), 211–231.

89 Ruth Meinzen-Dick and Esther Mwangi, *Cutting the Web of Interests: Pitfalls of Formalizing Property Rights*, 26 *Land Use Policy* (2008), 36–43.

90 Sara Berry, *Tomatoes, Land and Hearsay: Property and History in Asante in the Time of Structural Adjustment*, 25 *World Development* (1997), 1225–1241.

transfer of wealth to those with better social or economic positions, thereby creating tenure insecurity for less influential right-holders.”⁹¹ Therefore, the transition from customary land tenure to formalized individual ownership becomes a “race for the prize,” and “it is mostly the wealthy, the powerful, and the informed who succeed in a race contested under such murky conditions.”⁹² Insofar as it encourages unequal capture of land by powerful elites, formalization of land rights will inevitably be rejected by those whose traditional claims are weakened or even denied in the process of formalization (by accident or design), and debates and conflicts will then continue to plague the society. As a consequence, valuable resources are wasted on unproductive uses, such as pervasive recourse to courts, exclusion of other users through various types of enclosure, and even illicit and semi-criminal acts of theft.⁹³ In some extreme cases, even apparently trivial land conflicts can be kept alive for generations and may suddenly erupt into large-scale civil strife and violence.⁹⁴

Generally speaking, when most developing countries try to replace the customary land system with formal (individualized) land rights, their supply-side constraints, such as insufficient budget, incompetent agencies, and inadequate legitimacy, will frequently cause so-called legal pluralism.⁹⁵ For example, in Kenya, Barrows and Roth show that “the land law failed to gain popular understanding or acceptance, individuals continued to convey rights to land according to customary law, and a gap developed between the control of rights as reflected in the land register and as recognized by most local communities.”⁹⁶ Under legal pluralism, the question of which institution must define and enforce property rights becomes ambiguous because “traditional authorities have lost much of their power of control over land, but the state has not developed the capacity to take full control.”⁹⁷ Instead of complementing each other, formal and informal land institutions compete with each other, and this parallel system

⁹¹ Barrows and Roth (1990), *supra* note 26.

⁹² Tor A. Benjaminsen and Espen Sjaastad, *Race for the Prize: Land Transactions and Rent Appropriation in the Malian Cotton Zone*, 14 *European Journal of Development Research* (2002), 129–152.

⁹³ See, for instance, Pauline E. Peters, *Inequality and Social Conflict over Land in Africa*, 4 *Journal of Agrarian Change*, no. 3 (2004), 269–314.

⁹⁴ See, for instance, André and Platteau (1998), *supra* note 86; Ben K. Fred-Mensah, *Capturing Ambiguities: Communal Conflict Management Alternative in Ghana*, 27 *World Development* (1999), 951–965.

⁹⁵ Daniel Fitzpatrick, *Evolution and Chaos in Property Rights Systems: The Third World Tragedy of Contested Access*, 115 *Yale Law Journal* (2006), 996–1048.

⁹⁶ Barrows and Roth (1990), *supra* note 26.

⁹⁷ Fred-Mensah (1999), *supra* note 94.

will give rise to “institutional shopping,” a term used to describe the situation in which different parties pursue disputes through different channels (e.g., formal vs. informal, legal vs. administrative).⁹⁸

Legal pluralism, institutional ambiguity, and institutional shopping will further undermine social conditions that enable customary land tenure to function effectively, such as norms of reciprocity and cooperation, low-cost internal governance mechanisms, and informal sanction systems.⁹⁹ Norm-based common property arrangements may therefore become dysfunctional, or even break down, especially under pressure from rising resource values. On the other hand, legal pluralism may also damage the legitimacy and credibility of formal property systems, leading to efficiency costs, in view of local people’s determined resistance to drastic reshuffling of land rights. In the worst-case scenario, the norm-based resource governance system will disintegrate without the provision of effective substitutes by the state, and open access (and resource depletion) will follow.

4.4 Property law and the state

The importance and desirability of the state has been endorsed by social scientists since Thomas Hobbes, given its allegedly irreplaceable role in maintaining social order, providing public goods and services, and redressing market failure. Although they are far from perfect, states in the developed world indeed conform to such stereotypes and effectively fulfill their responsibilities. Unfortunately, worldwide, properly functioning governments that protect property rights and supply public goods are the exception, not the rule.¹⁰⁰ For example, according to the 2010 Failed States Index compiled by Foreign Policy magazine and the Fund of Peace, nearly 21% of the world’s countries (37 countries) are “failing states.” In them, governments are often ultra-predatory, dysfunctional, and threatening collapse. Another 51% of the world’s countries (91 countries) are states in imminent danger of failing. If these measures are correct, in over half of the world, states are either critically or dangerously dysfunctional.

⁹⁸ Deininger (2003) *supra* note 25; Deininger and Feder (2009), *supra* note 79.

⁹⁹ Fitzpatrick (2006), *supra* note 95.

¹⁰⁰ See, for instance, Peter T. Leeson, *Better Off Stateless: Somalia Before and After Government Collapse*, 35 *Journal of Comparative Economics* (2007), 689–710; Peter T. Leeson and Claudia R. Williamson, *Anarchy and Development: An Application of the Theory of Second Best*, 2 *Law and Development Review*, no. 1 (2009), 76–96.

Weak and failed states cannot be expected to perform the functions that they are supposed to, such as defining and protecting property rights, because their governments lack either the capacity or the incentives required for an effective governance mechanism.¹⁰¹ Weak countries therefore fail to create and maintain a variety of institutions that are directly or indirectly responsible for the functioning of a formal property rights regime, such as a reliable and inexpensive land titling system, a competent and uncorrupt judiciary, and a functional police force.¹⁰² In some extreme cases, the effects of weak states are so detrimental that they are said to “kill growth”¹⁰³ and are better replaced by a state of anarchy.¹⁰⁴

More generally, weak states are susceptible to capture by powerful elites and therefore easily become a vehicle for rent seeking. As the models of Glaeser et al.,¹⁰⁵ Polishchuk and Savvateev,¹⁰⁶ and Sonin¹⁰⁷ have shown, in an institutional environment where the state is likely to be captured, influential elites and/or rich agents can subvert the political, regulatory, and legal institutions of society for their own benefit. In that case, they have no interest in, and even object to, strong protection of property rights provided by the state in a non-discriminatory manner. On the one hand, they can protect their own property by appealing to their de facto political power or other available strategies that can be used to shelter them from expropriation.¹⁰⁸ On the other hand, they will benefit from weak protection of property rights, which allows them to engage in

101 See, for instance, Daron Acemoglu, *Politics and Economics in Weak and Strong States*, 52 *Journal of Monetary Economics* (2005), 1199–1226.

102 See, for instance, Trebilcock and Veel (2008), *supra* note 81.

103 William Easterly, *The Elusive Quest for Growth: Economist's Adventures and Misadventures in the Tropics* (Cambridge, MA: MIT Press, 2002).

104 Leeson (2007), *supra* note 100; Leeson and Williamson (2009), *supra* note 100.

105 Edward Glaeser, Jose Scheinkman, and Andrei Shleifer, *The Injustice of Inequality*, 50 *Journal of Monetary Economics* (2003), 199–222.

106 Leonid Polishchuk and Alexei Savvateev, *Spontaneous (Non)Emergence of Property Rights*, 12 *Economics of Transition* (2004), 103–127.

107 Konstantin Sonin, *Why the Rich May Favor Poor Protection of Property Rights*, 31 *Journal of Comparative Economics* (2003), 715–731.

108 For example, during the political instability resulting from the Mexican Revolution, the Mexican oil industry effectively defended its property rights by making use of two powerful weapons. First, the oil companies made effective appeals to the U.S. government to intervene on their behalf. Second, they were able to coordinate their actions, which meant that they could threaten the Mexican government with production boycotts. For more details, see Stephen Haber, Noel Maurer, and Armando Razo, *When the Law Does Not Matter: The Rise and Decline of the Mexican Oil Industry*, 63 *Journal of Economic History* (2003), 1–32.

profitable but unproductive activities such as rent seeking or other redistributive action.

The evidence from transition economies shows that public officials in high-capture economies appear to have created a private market for the provision of typically public goods, such as the security of property rights, and for rent-seeking opportunities that a relatively small number of firms can obtain through capture. State capture generates individualized gains to captor firms while being associated with large social costs for the rest of the economy in deteriorating sales and investment growth.¹⁰⁹ In Russia, the public property rights enforcement mechanism has been replaced by private (mafia-type) enforcement to the extent that the state and the government are claimed to have effectively been “privatized”.¹¹⁰ Consequently, markets are subject to extremely high transaction costs because the number of participants in each segment of the divided market (caused by private enforcement) is strictly limited and the flows of goods, capital, labor, and information are severely disrupted; the intrinsic uncertainty inherent in the private enforcement systems orients the economy toward extremely short-term profit maximization; and many small businesses and much of the population are driven to the shadow economy when they feel that they are being unfairly taxed and exploited by small but well-organized pressure groups.

In the developing world, especially the post-colonial states of Africa, rulers rely on alliances with local strongmen, whom they allow to exploit local economic opportunities, hence creating a so-called neo-patrimonial system of governance. In some extreme cases, as with Mobutu Sese Seko of Zaire, a neo-patrimonial regime results in the theft of a large part of the society’s resources by a single individual, whereas in others, it merely amounts to rent seeking; that is, use of the public sector to reallocate property rights to the benefit of a particular interest.¹¹¹ For example, in Northwest Cameroon, land conflicts have increased because local elites seek to acquire large tracts of land under individual title, a process facilitated by the 1974 land ordinance and by the links between local elites and national politics. In Kenya, a critical contributing factor to the growing social inequality in access to land is the capacity of the patron–client chains that link the national elite to the local level to gain control over

109 See, for instance, Joel S. Hellman, Geraint Jones, and Daniel Kaufmann, *Seize the State, Seize the Day: State Capture and Influence in Transition Economies*, 31 *Journal of Comparative Economics* (2003), 751–773.

110 Serguey Braguinsky, *Enforcement of Property Rights during the Russian Transition: Problems and Some Approaches to a New Liberal Solution*, 28 *Journal of Legal Studies* (1999), 515–544.

111 Francis Fukuyama, *State-Building: Governance and World Order in the 21st Century* (Ithaca, NY: Cornell University Press, 2004).

resources that offer opportunities for accumulation. In Nigeria, political and civil elites benefit disproportionately from the 1978 Land Use Decree by manipulating the allocation authorities. Finally, in Somalia, the tragic civil strife is rooted in an earlier process of land occupation and expropriation by the state and its governing elites; in particular, the Land Law of 1975 enables those with privileged access to the mechanisms of registration to obtain titles to land that local farmers had used for generations.¹¹²

In summary, good governance, such as a consistent legal and institutional framework, broad access to information, and competent and impartial agencies, is a necessary precondition for the functioning of formal property rights. However, many developing countries can be characterized by serious deficiencies in governance, and the state's monopoly on the exercise of power may therefore be abused to appropriate property or to assist in the unfair acquisition of land by elites.¹¹³ The property law enacted and enforced by the state will then become a so-called empty institution¹¹⁴ rather than a credible institution that property owners can appeal to in case of invasion, regardless of whether the invader is a government official or ordinary citizen.

5 Conclusion

In economics and jurisprudence, property rights in general and property law in particular have long been regarded as the fundamental preconditions for sustainable economic growth and used to explain the differences in economic performance across countries. Property rights, or more precisely, formal, individualized property rights are expected to encourage efficient resource management, to stimulate investments in production and innovation, and hence to push the economy to a faster growth trajectory. The alleged desirability of formal private ownership has been embraced by a large number of economists and lawyers, who present numerous pieces of supportive evidence from historical and comparative perspectives (primarily on the macrolevel), building a theoretical foundation for policy recommendations submitted to developing countries.¹¹⁵

¹¹² Peters (2004), *supra* note 93.

¹¹³ See, for instance, Deininger and Feder (2009), *supra* note 79.

¹¹⁴ Peter Ho, *Institutions in Transition: Land Ownership, Property Rights, and Social Conflict in China* (New York: Oxford University Press, 2005).

¹¹⁵ World Bank, *Building Institutions for Markets* (World Development Report 2002) (New York: Oxford University Press, 2002).

When we look at studies conducted on the microlevel, especially those from African countries, however, the picture is more mixed. Whereas some of the studies report positive and significant effects of formal private ownership on investment and other measures of economic performance, others fail to find a strong link between individualized property and economic outcomes. In general, three factors can account for the failure or insignificance of formal property rights in most developing countries. First, the malfunctioning or even nonexistence of other factor markets, particularly financial markets, tends to invalidate the effects of formal private ownership. Second, the merits of formal property rights may frequently be outweighed by their costs, which include both the direct costs of defining, measuring, and enforcing property rights through the use of state power and opportunity costs in terms of the forgone benefits supplied by customary (common) property regimes such as scale economies or risk reduction. Finally, when the state is captured by the elites and degenerates into a mechanism of rent seeking, or when the state itself acts as a tyrannical leviathan whose interests are mainly in exploitation, plunder, and confiscation, property owners will cease to recognize property law, then move to the underworld economy and rely completely on private enforcers.

The main point here is not a simple conclusion, such as that property rights do or do not matter, but rather an exhortation to pay more attention to the complexity inherent in the functioning of property rights, such as their dependence on the extent and depth of the market, their dynamic rather than static character, and their complicated interactions with the economy, polity, and society. It is therefore too optimistic, or even naïve, to embrace property privatization and formalization as a panacea for economic backwardness given the context-contingent and environment-dependent nature of property rights, which is hard to generalize into an optimal model of a property regime.

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