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Broadening Access and Strengthening Input Market Systems

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Innovating Institutions to Help Land Reform Beneficiaries

by **Mike Lyne** lyne@nu.ac.za *and* **Michael Roth** mjroth@facstaff.wisc.edu
with assistance from **Malcolm Childress** *and* **Roman Mogilevsky**

Group ownership of land resources

Central Asia and Southern Africa are undergoing political and economic transition, the former from state and collective farm ownership to private groups and individuals, and the latter to redress the apartheid and colonial heritage of racially-biased and unequal landownership. Despite different histories and policy contexts, countries in these regions share a core problem: poor people in rural areas are unable to make productive use of their land resources.

The problem is most acute where it has not been feasible to privatize land, water, infrastructure, or movable assets to individual owners. Many beneficiaries of land reform in these regions find themselves co-owning resources, often in diverse groups that lack the constitutional rules and operational arrangements needed for effective management. Historically, these cooperative ownership models have led to low productivity, free ridership, and an inability to encourage investment by the co-owners or external financiers.

Yet, as demonstrated by some successful arrangements in South Africa as well as globally, group ownership need not be unproductive or unprofitable. By helping to identify and resolve the social, institutional, and organizational problems associated with group ownership in the Kyrgyz Republic and South Africa, BASIS endeavors to develop institutional models that increase enterprise profitability and improve the livelihoods and asset holdings of the rural poor.

Problems with land reform and farm restructuring

In South Africa, progress with land reform has fallen far short of the goals set by the government. In 1994, the post-apartheid government projected land redistribution at the rate of six million hectares per year. Between 1994 and 2000, just one million hectares was redistributed. In the province of KwaZulu-Natal, where BASIS has monitored farm transactions since 1997, less than 0.5% of the farmland owned by whites has transferred to historically-disadvantaged people each year despite the presence of an active land market and the availability of public grants to purchase land on a willing buyer-willing seller basis. Two obstacles have contributed to the slow pace of land reform. It is expensive to subdivide commercial farms and to survey, register, and transfer smaller units to aspiring farmers. Prospective farmers also lack capital and are unable to finance land with conventional mortgage loans from commercial banks due to cash flow problems caused by high nominal interest rates.

Most of the disadvantaged people who have acquired farmland have done so by pooling resources and purchasing farms collectively, a trend that is likely to continue even if the inflation rate falls and the statutory costs associated with subdivision, registration, and transfer of farmland decline. From 1997-2001, more than half the farmland purchased by historically-disadvantaged people in KwaZulu-Natal transferred to groups, not individuals. This poses a major challenge to policymakers, since farms acquired by groups of land reform beneficiaries already show symptoms of becoming open access resources.

In the Kyrgyz Republic, the agricultural transition is unfolding rapidly, with swift and far-reaching structural change. Between independence in 1991 and January 2000, 47% of the arable land formerly held by state and collective farms had been transferred to 69,000 small- and medium-sized farms (usually operated by groups of families). The other 53% is managed by 600 corporate-collective farm enterprises that have many of the same features as their predecessors but operate under a variety of new legal forms.

The economic conditions facing these enterprises are severe. The collapse of the Soviet system of production and distribution has left Kyrgyz agriculture starved for operating capital and long-term investment. Farm enterprises that managed to stay afloat with depreciating capital stock and self-financing during the 1990s presently are challenged in attracting new sources of capital and moving beyond subsistence into profitable commercial activities.

Sustainable growth in both countries will be difficult to achieve without improving the efficiency of these emerging enterprises and increasing public and private investment. To a large extent, these improvements will depend on the ability of the newly created, member-owned enterprises to innovate and expand under adverse economic conditions.

New institutional models

South Africa and the Kyrgyz Republic share a number of similarities that unite their search for institutional innovations that improve group or community access to physical and environmental resources. Group ownership of land and water resources and fixed improvements is emerging as a prevalent model in both transitions. Factors such as organizational inefficiency, free riding, weak legal framework, and moral hazard constrain the willingness and ability of groups to finance the investments needed to sustain farm earnings. New land reform beneficiaries need assistance in determining the type of legal entity to choose, organizational structures to adopt, strategies to increase farm investment and acquire business training, and ways to finance working capital and long-term investments.

Group ownership brings forth images of the dismal performance of cooperatives and collectives, particularly in Central America and countries of the former Soviet Union. Recent literature on "New-Age Cooperatives" has helped identify some institutional and organizational reasons for the poor performance of joint ventures that operate like traditional cooperatives. A notable exception to the general lack of progress in reform efforts is the success of farm worker equity schemes in South Africa's Western Cape province. These schemes have redistributed commercial farmland and wealth while improving agricultural performance.

Figure 1. Expected viability of rural enterprises

		Macro or meso policy environment	
		Kyrgyz Rep.: Constrained	**South Africa: Enabling**
Organizational/institutional arrangements	**Sub-optimal arrangements**: Large beneficiary group Non-transferable shareholdings No external capital Weak accountability Poorly defined property rights Non-proportional income sharing	Unsuccessful	Minimally successful
	Optimal arrangements: Small beneficiary group Transferable shareholdings External capital Strong accountability Well defined property rights Proportional income sharing	Minimally successful	Successful

An equity scheme is a private company in which financial equity is owned by workers, managers, and other investors in the form of tradable shares that define their individual rights to vote for directors and to benefit from the profits and capital gains generated by the company. This is quite distinct from a cooperative or collective farming enterprise where voting and benefit rights are egalitarian and nonmarketable, resulting in free-rider problems that undermine members' incentives to invest time and money in the enterprise. Equity schemes have been able to attract additional finance from commercial banks—partly because they are managed by experienced farmers (frequently white former farm owners) and their assets can be repossessed and sold in the event of loan default.

Figure 1 (facing page) summarizes characteristics of organizational and institutional arrangements that tend to constrain or enable economic growth. The policy environment that conditions incentives, legal certainty, and profitability further shapes the effectiveness of these arrangements. The likelihood of equity sharing enterprises succeeding will be higher in South Africa than in the Kyrgyz Republic because the former country's policy environment is more enabling for creating profits that help ensure the enterprises' sustainability. By studying a range of well- to poorly-functioning enterprises within each country, BASIS will be able to isolate best organizational and institutional practices for policy dissemination regardless of the policy environment. However, in addition, by studying enterprises within two sharply different policy domains, BASIS will endeavor to learn how key policy instruments and sequencing in enabling economies (South Africa) can be adapted to policy constrained economies (Kyrgyz Republic) to help accelerate enterprise growth and ensure the likelihood of success.

Designing rural enterprises

In order to identify and resolve the social, institutional, and organizational problems associated with group ownership in the Kyrgyz Republic and South Africa, BASIS researchers will select 10-12 enterprises for case study research in each country. These will represent a cross-section of enterprises ranging from relatively successful to unsuccessful. This variation is expected to reveal important differences in indicator variables, such as financial performance, enterprise type, use of external finance, relative shareholdings of beneficiaries, geographic region, size and gender composition of the beneficiary group, and choice of legal entities and business organization.

This BASIS project will endeavor to:

- identify the institutional and financial problems that constrain the operation of equity-sharing enterprises created under privatization and land reform programs,
- determine best institutional practices that broaden and deepen beneficiaries' access to resources and encourage their productive use,
- apply these best practices to the design or redesign of a limited number of equity-sharing enterprises, and,
- assess how these organizational and institutional innovations, combined with greater land and financial market integration, can improve economic and environmental performance.

BASIS hypothesizes that innovative institutions in flexible policy environments will be the most successful of the institutions analyzed. But what combinations of organizational structures, constitutional rules, and operational arrangements are most successful? Analysis will identify specific arrangements that positively impact the performance of each enterprise, where performance will be measured in terms of financial health, sound business practice, investment, environmental sustainability, and empowerment of beneficiaries, especially women.

Results of this analysis will be used to design (or redesign) and facilitate the development of one or two equity sharing enterprises in each country. It is anticipated that the institutional solutions applied during the facilitation phase of this project will:

- convert weak cooperative farms into equity sharing enterprises where management works on behalf of the beneficiary members,
- clarify and assign individual rights to property and benefit streams, and,
- establish incentive structures that encourage investment by members and external financiers (e.g., by making voting and benefit rights proportional to individual investment, and by establishing managerial accountability through a transparent electoral process and independent financial audit).

By working with local institutions and stakeholders (Figure 2 next page), the researchers will oversee the negotiation, mediation, and training aspects of project facilitation, and assist decision-making on organizational arrangements, preparation of constitutions and business plans, and securing finance. Beneficiary performance in the new equity-sharing enterprises will be monitored, modifications made to enterprises as needed, and performance assessed.

Impacts

BASIS will provide policymakers with institutional recommendations for successful farming, ecotourism, and agribusiness ventures in cases where resources, infrastructure, and lumpy assets cannot be privatized to individual owner-operators. Work on facilitating new experimental enterprises will help test these

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Authors

Mike Lyne
University of Natal-Pietermaritzburg, South Africa

Michael Roth

Malcolm Childress
Land Tenure Center, University of Wisconsin-Madison, USA

Roman Mogilevsky
Center for Social and Economic Research, Kyrgyz Republic

Other institutions involved
Rural Development Institute, USA

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Comments encouraged:
Department of Agricultural and Applied Economics, University of Wisconsin, Madison, WI 53706 USA
basis-me@facstaff.wisc.edu
tel: +608-262-5538
fax: +608-262-4376
http://www.basis.wisc.edu

recommendations and ultimately benefit new land reform beneficiaries.

South Africa is further ahead in its land policy framework, particularly with laws and regulations governing group enterprises. South Africa also has a more robust market in land and financial capital, which, combined with a more enabling policy and legal framework, give it greater freedom in designing and implementing policy interventions. Because of these differences, lessons learned in South Africa will be used to help inform the more slowly developing Kyrgyz program.

Figure 2. Local institutions and stakeholders

Kyrgyz Republic

Ministry of Agriculture and Water Resources
Rural Advisory Development Service

South Africa

Department of Land Affairs
Ingonyama Trust Board
Institute of Natural Resources
Ithala Bank
Land Reform Credit Facility
Lima Rural Development Foundation

In South Africa, design of the new enterprises will involve Ithala Bank and the Land Reform Credit Facility as financiers. The Ingonyama Trust Board will play a central role because it is legally responsible for brokering long-term leases over communal land. Lima Rural Development Foundation will be involved in the facilitation of new equity enterprises. The Department of Land Affairs will assist with selecting the pilot projects and approving grants to beneficiary households.

In the Kyrgyz Republic, Ministry of Agriculture and Water Resources (MAWR) personnel will be involved in analytical roles working with the case study and survey data. Training programs on best practices will be developed jointly with the MAWR's Republican Center for Land and Agrarian Reform and the Rural Advisory Development Service. The MAWR also will assist with selecting model enterprises and identifying sources of financial capital.

This project will benefit the rural poor at three levels. First, the facilitation of new equity-sharing enterprises will directly benefit the land reform beneficiaries involved. Second, improvements in legal and organizational structures will strengthen women's rights and decision-making as shareholders within these enterprises. Third, involving government and NGOs in the research, facilitation, and dissemination will help sustain and extend project impacts. Through this process of collaborative research, capacity strengthening, and engaging stakeholders in the facilitation of new enterprises, BASIS seeks to expand opportunities for the poor and make these opportunities sustainable beyond the life of the project.

Suggested reading

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