Land Market Issues: The Mystery of Capitalism Revisited

Policy Instruments

Chapters 3–5 each consider one of the policy instruments used to affect shelter provision—land policy, finance, and subsidies. In each case we review the changing policy environment, the Bank’s experience, and then try to distill lessons about what has worked and not worked. However, before turning to land market policies, we present yet another instrument through which the Bank can and has provided assistance—that is, through technology (box 3.1).

Box 3.1 Satellite Images, Maps, and GIS

Remote sensing or satellite images, maps derived from these, and GIS (geographic information systems) have been used in a number of Bank operations. Satellite images were used in Angola to produce the first updated maps available to local authorities in Lobito Benguela since 1975. The level of resolution was very low at the time, but combining the images with “windshield surveys” allowed the team to estimate, with reasonable accuracy, the number of people without access to water and the distances required for rehabilitation and development of water systems to the low-income periphery of the port city of Lobito. A how-to manual on simple computer imaging and mapping was issued based on this experience (Pazner, Thies, and Chavez 1993). At present, the Kabul Development Plan is using Ikonos satellite imagery at 1 meter resolution for 2002 and 2004 to facilitate spatial data gathering and processing. Maps created by combining satellite imagery with topographical data will divide the city into homogenous neighborhoods, or planning zones, following the administrative boundaries of districts and gozars, and provide the background for thematic maps. These include existing land use (dwelling typology and socioeconomic data); population density and population movement; land value and available government-owned land; existing and
planned infrastructure coverage, including community and social facilities, particularly schools and health clinics; and, based on all of the above, a basic priority needs assessment. The project will strengthen the city government’s planning capacity and help it to formulate a spatial strategy concerning the densification of existing neighborhoods and the expansion of the city in new areas. The strategy will be made concrete in land use and housing regulations, a zoning map, land use and land subdivision regulations, and investment plans.

Source: Authors.

Urban Land Policy: Is Titling the Answer?

The 1993 World Bank shelter paper *Housing: Enabling Markets to Work* stressed the importance of appropriate land market regulation and large-scale urban property rights development, including land tenure regularization in informal settlements. The approach was in some ways similar to that of the earlier Bank study *Shelter*, although the earlier paper seemed to be of two minds on the topic. On one hand, it suggested that land costs were likely to be a very small part of shelter costs. However, it simultaneously argued that the development of security of tenure is a prerequisite for land to be delivered at the scale needed. Thus, while the early Bank view was that institutional issues relating to land supply in urban areas was important, it also held that these costs were not likely to be substantial.

In the years since *Housing: Enabling Markets to Work*, international interest in urban land management has increased substantially. For example, building on a 1992 policy paper on land market issues, the Urban Management Program produced several other publications in the mid-1990s. These papers were followed by the launch of the Global Campaign for Secure Tenure by UN-HABITAT, and the establishment of the Millennium Development Goals in 2000, which pinpointed tenure security improvements for slum dwellers as a target. Also in 2000, Hernando de Soto published the controversial bestseller *The Mystery of Capital*, which placed urban property rights issues back into the development community spotlight and led to renewed interest in land titling programs. This was followed by a World Bank Policy Research Report on land policies in 2003 (Deininger 2003). Finally, in the last two years, *The Economist* has published a regular international housing price index, and the European Central Bank and the Bank for International Settlements have undertaken studies of land prices out of concern for the effects the EU may have on housing and land costs.

This growing body of research and policy interest has provided an unambiguous answer to the question of whether land prices play an important
role in the cost of housing. In particular, a significant body of empirical work on both developed and developing countries indicates that land market policies not only drive much of the increases observed in housing prices, but they also account for a large fraction of total housing costs (Buckley and Kalarickal 2005). What is still disputed, however, is whether titles matter as much as claimed by de Soto.5

To answer this question, it is useful to begin with recent analyses of de Soto’s arguments. He contends that secure property rights to land explain why capitalism has been such a productive economic system in the West. And more importantly, he emphasizes the corollary of this argument, i.e., that the absence of titles explains the failure of capitalism to take hold in much of the developing world. De Soto makes an interesting, even compelling, case that property rights as embodied in titles are an essential mechanism for converting assets to usable wealth. Titles, de Soto argues, “capture and organize all the relevant information required to conceptualize the potential value of an asset and so allows us to control it” (de Soto 2000, p. 47). He estimates that if developing countries could provide secure property rights to residential property, they would be able to effectively “unlock” $9.3 trillion of what he calls “dead capital.”

While there are good reasons to agree that improving property rights should be an essential part of reform, there are also a range of practical problems that potentially reduce the seemingly large gains. Among these problems are:

- Titling is often a costly process. It is not just a matter of formalizing informal arrangements that already exist. Very often, contradictory claims of ownership succeed the announcements of titling programs. As Woodruff (2001) shows, the costs of adjudicating these claims may abrogate the gains from titling.
- Much of the land on which informal houses are built is obtained through illegal squatting on private property, and compensation is not paid to existing owners. Therefore, any titling program will have to consider providing amnesty for those who benefited from invasions. Whether such a process will result in greater respect for property rights is open to question.
- As Lee-Smith’s (1997) analysis of property contracts in Kenya shows, this sort of contract’s value depends in large part on existing and often unwritten contracts, such as the degree of access women have to property. The broader web of societal contracts and constraints, as well as a wide variety of political economy issues, may well reduce the value given to property titles in isolation.
- A title is less valuable if it cannot be used as collateral. Such a result occurs whenever there is no effective formal financial system, as is the case in many developing countries. Moreover, even if a formal financial sector is functioning, very often many of those who live in informal housing
are self-employed or work in the informal sector, so that it is difficult for them to show proof of income—a necessary condition to obtain credit from formal financial institutions. The result is that in most developing countries, the collateral value of property title remains low.

- The articles in Payne (2002) argue persuasively that in most developing countries, what may be termed the anthropological perspective on tenure—that is, a continuum of tenure categories with different levels of security of tenure—applies. Across this spectrum, some may value titles much more strongly than others. Once again, no simple policy reform will change this situation.

These implementation problems with unlocking the wealth locked in urban land holdings do not mean that de Soto’s basic point is in question, nor do they mean that housing policy should not include reforms to improve tenure and the legal framework for individual ownership. Undoubtedly, in many cases, formal titles are a necessary condition to developing a fully functional housing market, particularly a housing finance system, but they are not a sufficient condition to unlock the trillions of dollars that are said to be locked up in dead assets. Moreover, simpler approaches to alleviating

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**Box 3.2 Street Addressing in Maputo, Mozambique**

“Adresse,” or street addressing, was introduced in Mozambique by the French Cooperation, in connection with the first World Bank urban rehabilitation project. In three years it covered most of the metropolitan area and was not only a self-sustaining operation but a profit center for the participating municipalities. The benefits it brought to municipal management and to the utilities worked as advertised. One unforeseen use of the system, which provided names or numbers to streets and numbered all properties, came during a cholera epidemic. When patients arrived in hospitals and clinics throughout the city, the government assumed there were multiple outbreaks. Someone proposed asking the patients their address, rather than assuming that they lived near the facility they were in. Indeed, people had not gone to the nearest facility, but rather where they knew somebody who could help them, even if it was across town. When the addresses were compiled, it became clear there was a single source of contamination, a slum near the city center. The area was drained and the threat of the disease controlled thanks in part to the addressing system. Street addressing has taken root in over twenty countries in Africa and in Cambodia, mostly in francophone areas.7

*Source: Farvacque-Vitkovic et al. (2005).*
tenure insecurity are often available and, depending on the existing constraints, there are a variety of tenure instruments that can be employed to convey property rights or freedoms. In addition, because many of these instruments do not require prior physical planning, infrastructure servicing, and surveying of the settlements, they are often an advantageous strategy from the perspective of widespread coverage at reduced costs. Box 3.2 discusses one of the simplest ways some of these gains can be realized.

In short, while capitalism may well be mysterious, it is so in subtle ways. The poor are not impoverished because a simple housing market improvement has been ignored or simply misunderstood. If it is not just titles that constrain housing and land markets in developing countries, what is it? The accumulating evidence is that the constraints placed, sometimes inadvertently, on urban land markets by policy makers have deleterious spillover effects on the workings of the urban economy. In other words, de Soto’s major point—that urban land markets are an enormous constraint on development—is right, even if the situation is much more complex than he suggests.

In what follows, we present snapshots of how these constraints on urban land markets prevent them from working in a number of cities. The objectives are first, to provide a sense of the cascading effect that land market policies can have on cities, the poor, and the effectiveness of shelter assistance in such places; and second, to suggest just how complex and idiosyncratic these interventions can be. In effect, like de Soto, we examine the constraints on buying, selling, and improving urban property that derive from urban land policy distortions.

Unresponsive Public Holders of Urban Land Often Make It Impossible to Buy Property

Public sector land use in many cities of the developing world is often not responsive to demand. Under various ministries—defense, railroads, agriculture, urban development, industry, housing, etc.—the public sector often holds a significant share of a city’s accessible land in ways that are indifferent and unresponsive to demand. The result is that the limited amount of available land is much more expensive.

Results observed in Dhaka, Bangladesh are perhaps extreme in this regard, but not unusual. As the World Bank (2004c) shows, policies in Dhaka have resulted in land prices similar to those observed in New York City. Certainly, the city’s rapid population growth feeds these prices. But more than just demographic pressure is involved. Almost certainly, the land holding patterns of many public bodies dictate these prices. For example, as shown in maps 3.1 (page 83) and 3.2 (page 85), large amounts of public land in the central Dhaka remain undeveloped. Government-owned lands as well as other locations are occupied by government-related activities
with no or very little available for construction (this is the case of the Tejgaon airport, the military cantonment, and land tracks left for future construction of public buildings). Such activities may characterize as much as 20 percent of the land in the inner city area. Other centrally-located areas, such as the areas containing public housing, are developed at very low densities in relation to land prices. Rarely do building densities correspond to underlying land costs. This is the case of the university area, located in the heart of the city, and other residential areas for civil servants and government workers. In more price-responsive economies, these properties would be redeveloped and put to different uses, so that the same land supply could be used to provide much more housing.

A consequence of this scarcity of formal serviced land has been the development of the city almost entirely by the informal sector. As shown by the maps, most of the new urbanization since the mid-1980s has occurred without any heed to planning regulations and without any planning enforcement. The yellow areas in the maps correspond to land that has been developed in this way—that is, illegally. The dominance of informal delivery systems over the formal system indicates that formal market solutions are available to few residents of the city. The majority of residents must rely, in one way or another, on those who have gained control over the land. Formal finance and direct connection to utility providers are not available; instead, they done informally in the breach.

In short, because of these policies, few people are able to formally buy or even legally rent shelter in Bangladesh’s largest cities. Informal trades take place but the sorts of trades that would put the land to alternative uses cannot readily be undertaken. To see why, it is useful to trace through one more example of how nonmarket solutions work in another city. We use is Mumbai as an example to explain why inappropriate regulation restricts not only the purchase but also the redevelopment of land.

**Inappropriate Regulations Often Restrict the Ability to Sell Urban Property**

Since the early 1990s, Mumbai, India’s largest city, has lost more than 300,000 manufacturing jobs. The textile mills that were the source of the city’s wealth in the late 19th century and beginning of the 20th century have been closed, and the petrochemical industry migrated to the neighboring state of Gujarat, and the port declined in importance and shipping volume. These sorts of shocks are always difficult for a city and its poorer citizens to bear, but in Mumbai the decidedly nonmarket land regulations had particularly deleterious effects on the low-wage workers who lost their jobs. In effect, urban land use regulations designed to help these families made them, as we will explain, house rich and cash poor. Ultimately, the
Box 3.3 Freezing Mumbai’s Housing Stock

Tracing the way in which Mumbai’s urban land use controls affect poor households requires some elaboration of the broader set of housing and land market regulations. The first regulation to consider is the city’s restriction on building heights. Mumbai, like many Indian cities, imposes severe restrictions on how tall buildings can be, limiting them to less than one-tenth of the height that is permissible in many other Asian cities. The figure below shows that the inability to build upwards means that the city expands horizontally (the darker line in the figure). It also means, as shown by Bertaud and Brueckner (2005), that housing costs in the constrained area increase sometimes markedly.

Bertaud and Brueckner estimate that the restrictions in Bangalore increase costs by 3 to 6 percent of the median family’s income. Bertaud, Buckley, and Owens (2003) apply this same framework to Mumbai’s much more topographically constricted land mass and its more restrictive limitations on building heights and find that the restrictions bid up housing costs for lower income families by as much as 15 to 20 percent of income. However, as long as the people living in the city—even if they are renters—do not have to pay these prices, the policy has no direct effect on them. This is exactly what policy makers aimed to achieve to protect the tenants from high costs. They imposed binding rent controls on the city, so

Source: Bertaud and Brueckner (2005).
Note: FAR means floor area ratio, a measure of the amount of floor area that can be developed in a given land area.
policies drove workers into informal sector jobs and the city’s fixed capital stock was prevented from adjusting to the evolving demands of the city’s talented labor force. Cumulatively, as shown in box 3.3, regulatory policies made these workers much less able to adjust to the changed economic environment.

The story of Mumbai is just one example of nonmarket interventions in a land market that few can afford. Undoubtedly, there are infinite ways that land market restrictions can feed into other aspects of the urban economy, but consider two: finance and subsidies.

- When land is expensive, organizations like Grameen Bank, one of the world’s most successful lenders for microenterprise finance, are unable to make loans in cities like Dhaka, even though such loans account for the bank’s largest single asset. Land prices in the city are simply too prohibitive for the bank to provide finance.

- When land prices are many times what they would be in the absence of regulatory controls, it follows the number of people who can be served with subsidy assistance is much smaller.

Hence, urban land market constraints of this sort can have important, adverse spillover effects on a city’s economy, as well as decrease the effectiveness of other instruments that can help address these problems.
Box 3.4 Standards and Affordability:  
An Example from Addis Ababa

The figures below show (a) the relationship between construction costs for different types of construction and household income in Addis Ababa; and (b) the distribution of households over the income range. Together, they show how standards in the formal market put housing in the formal (chicka) sector beyond the reach of the majority of people. The top figure shows that a formal house of 25 square meters on a mandated minimum 75 square meter plot in a suburban area would be affordable to households with a monthly income above 1,400 birr. However, an informal construction of 25 square meters built on the same plot is affordable to households with an income of 1,000 birr.
Regulations Often Make Even Titled Property Development Illegal

Regulation, zoning, and minimum standards are key policy levers for affecting the operation of urban land markets and particularly access to shelter and land by the poor. There is ample evidence that when formal land development parameters (such as minimum plot sizes, setbacks, and infrastructure servicing standards) are not benchmarked against what the local population can afford to pay, most households (not just poor households) are excluded from access to formal land ownership. See box 3.4 for a study of such conditions in Addis Ababa. Thus, inappropriate regulation often renders dwelling construction and improvements illegal, regardless of whether the underlying plot is titled. The result is that even titled owners have reduced incentives to rehabilitate their ultimately illegal units. More realistic and appropriate regulation and standards are needed to address this constraint, particularly standards that would allow for incremental improvement. Payne and Majale (2004) discuss a methodology for computing the effects of such regulations.

Without downward revisions in standards, all of de Soto’s constraints on land use are realized: it is very difficult to buy property, it is similarly difficult to sell property to someone who would put the land to a different use, and it is unattractive to invest in property once title has been acquired because the standards are so high that the property does not satisfy legal codes. To make things worse, many of these places also have poor enforcement of contracts, incomplete or absent land registry systems, and ineffective conflict resolution mechanisms. In such places, it is an exaggeration to say that a land market even exists.
Some Difficult Questions

The evidence presented in this chapter addresses only in part some of the difficult policy questions which clearly need further empirical enquiry. These questions include:

• How can adequate, suitably-located land be developed within the financial reach of the majority of the urban population?
• How can the tenure security of informal settlers be safeguarded without losing the public sector’s ability to provide high value infrastructure services and redevelopment options in prime urban locations?
• Can development standards and zoning be made less restrictive without compromising environmental, public health, and disaster preparedness?

Some tentative answers about what has been learned in relation to these and other crucial issues are presented in the concluding section, but clearly, there are no universally applicable answers.

Lessons Learned

What Has Worked...

There are, as detailed in the text, a variety of methods to improve shelter conditions. However, in most places, formal titling does not seem to be the most important first step to take in many places. The attempt to provide more flexible ways to assure slum dwellers that they will not have their shelter demolished is an extremely important step forward and should be a prerequisite for the development of policy. However, in densely populated megacities where the value of land put to different uses is likely to be high, formal titles are likely to be considerably more valuable.

Less conventional interventions such as land readjustment and land swaps have not been adequately explored as instruments of intervention in land markets. In land readjustment schemes, multiple owners of land pool their plots to facilitate the development or rationalization of infrastructure and public spaces. Readjustment schemes have been widely practiced in Germany, Japan, the Republic of Korea, Nepal, Singapore, and elsewhere, and offer considerable potential for pursuing the dual objectives of enhancing tenure security and land use efficiency.

While the experience with land acquisition has at best been mixed, the new ability of the Bank to lend for this purpose (since April 2004) is a significant development that has the potential to enhance the governance of this process and to facilitate interventions on more strategically located land in future projects.
The cross-cutting nature of urban land issues makes integrated institutional approaches crucial to the success of interventions. But such arrangements are not easily forged; in fact, their absence has undermined the success of several Bank projects. Project experience indicates that the process becomes easily derailed when appropriately integrated approaches are not adopted. The Morocco Land Development Project, for example, highlighted the need for such an integrated institutional arrangement. The advantages of integrated operations between land registration and land administration have also been seen in several cadastre-related projects in Europe and Central Asia, Latin America and the Caribbean, and elsewhere. In a broader context, however, institutional arrangements for urban land administration need to be conceived in the context of what are often new, unconventional, and therefore less familiar roles for the state. Participation of the private sector in the land development process is also necessary. Examples of where such roles come into play are land readjustment, joint venture approaches to sites-and-services projects, and the upgrading of informal settlements on private land.

Redressing imbalances of powers of implementing agencies can also be important. For instance, in the Third Structural Adjustment Credit to Georgia, the land ownership reform component performed at a highly satisfactory level; land registration was completed for 3,000 enterprises. A key element of this success was the amendment of a law governing the administration and disposition of state-owned nonagricultural land.
Map 3.1 Land Use in Dhaka City, 1984

This map was produced by the Bangladesh Government. The boundaries, colors, presentations, and other information shown on this map do not imply, on the part of the World Bank, any judgment on the legality of any territory, or any endorsement or acceptance of such boundaries.
Map 3.2 Land Use in Dhaka City, 2004