The Reverse Effect

Securing land tenure makes it possible to reduce poverty in developing countries. It does so by providing households with the opportunity to translate their property into collateral, giving them access to credit at reasonable rates of interest. This is asserted today by so many so often that has become a generally accepted and undeniable truth. Experts have understood the close correlation between security of tenure and poverty eradication for more than three decades. But it was the seminal work of Hernando de Soto in his book The Mystery of Capital: Why Capitalism Triumphs in the West and Fails Everywhere Else (London: Bantam Press/Random House, 2000) which made these ideas easily accessible and understandable to policy and decision-makers. So articulate is De Soto in his presentation of the straight line of reasoning linking security of tenure with poverty eradication that he has affected many a mindset. The mechanism is propelled forward like a three-stage rocket: first property is transferred into collateral, enabling access to cheap credit, credit is then translated into investment, and finally investment is harvested as increased income.

Property
The line of thinking may be clear-cut, but implementation is no piece of cake. At the first stage of the money- generating rocket is property. How do people, particularly banks, ascertain that a poor farmer in a West African country legitimately owns a particular piece of land? Announcements such as ‘This land is not for sale nor for lease’ are a common sight, chalked on walls or fences as proof that there are folk who do not stick to selling what belongs to them. Prerequisite for securing a person’s right to a piece of land are proper laws, a well-functioning land administration system (LAS) and good governance. Indeed, the last decade has witnessed augmented activity in establishing LAS in developing countries all over the world, often supported by the World Bank, United Nations and the European Union. However, why should a poor farmer register his land when everyone in the village knows he is the rightful owner and registration will cost money, lots of it; money that is not available? This is the first hurdle.

Valuation
The second stage of the rocket involves land accepted by a bank as collateral being translated into money. How should property be valued? There are two basic methods. The first, and common practice in developed countries, is by determining its market value. An appraiser adjusts the value by comparison with similar objects recently transferred. However, in many developing countries the land market is not as well developed as in western countries, and therefore it is widely advocated that high priority should be given to establishing a land market in these countries. A second method is by assessing the productive capacity of land and the market value of the harvest, but this demands other expertise, and the world market for agricultural products is unstable. A loan comes at a price. Interest rate is basically determined by two main parameters: official rate, linked to level of inflation, and risk. A bank requires not only security of tenure, but also a guarantee that the farmer has sufficient present and future income to incrementally repay loan and interest. Although any default on repayment metamorphoses the bank from money provider into owner, it will not appreciate the role reversal; these are bankers, not farmers. A bank wants to be pretty sure that a farmer can settle his debts.

Invest
In the third stage the money is invested so that earnings minus interest and progress payments are higher than the farmer’s previous income. The money enables him to increase his harvest by improving production methods and buying fertilisers and more disease-resistant seeds. He can invest in techniques to enable him to pound and dry yam or cassava himself, allowing his wife to sell the products at market months after harvest, when the prices are likely to be higher. The loan might help him buy a milling machine, and the value so added might provide higher income per kilogram of harvest.

Or Spend
Poor farmers and their wives are only human. They realise that there is a long way to go from winning security of tenure to becoming wealthier. It may take years and years, a decade even - while a shorter route exists, at least apparently. Borrowing from the bank makes it possible to spend more; the money can be used (some erroneously say ‘invested’) to buy, for example, the status symbol of a 100-cc Chinese-made motorbike. Instant gratification. Why take the long road? A loan does not make a farmer richer. It might, if properly invested, be the engine for earning more money in the future. Used for consumption, however, it only makes him poorer. His income fails to increase, while he is loaded down with debt. Consumption increases per capita Gross Domestic Product (GDP), one of the main indicators of the Millennium Development Goals; this is the result of how GDP is defined. As a result, the weird situation may arise of poverty being statistically shown as successfully addressed, while the poor become poorer.