

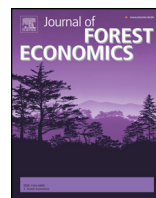


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# Situating community forestry enterprises within New Institutional Economic theory: What are the implications for their organization?



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### ABSTRACT

Community forestry enterprises (CFEs) have gained considerable traction with rural development and forestry practitioners as models for community development, poverty alleviation, and conservation. This paper uses New Institutional Economic theory to identify the key organizational features and potential inherent weaknesses of CFEs. NIE theory focuses on arguments of economic efficiency, specifically transaction cost reductions that serve as incentives for collective action by groups of owners. Examples are given to show how the organization of CFEs reduced transaction costs stemming from interactions with industrial loggers and service providers. However, the creation of these community enterprises goes beyond simple transaction cost reductions and economic justifications. Additional unquantifiable benefits, such as self-determination, control over resources that communities have historically used, application of acquired skills, political representation, and application of acquired skills to name a few, are also secured through community ownership. These benefits however do not come without a cost. As enterprises where ownership rights are incomplete or ill-defined and which do not operate with the incentives of investor-owned firms, CFEs have little to no initial capital pool and experience considerable investment limitations due to limited wealth, horizon problems, and unsolved issues with moral hazard vis-à-vis banks. CFEs also face important management and collective decision-making challenges. In spite of their institutional weaknesses, it is apparent that many societies have decided that the benefits of community ownership far outweigh their ownership costs. State intervention and policy have played an important role in building the necessary supportive framework for the development of these enterprises. NIE as a dominant model for understanding alternative entrepreneurial forms was useful for identifying some important aspects of CFEs that, in a profit-driven economy, can constitute weaknesses that place them at a disadvantage with investor-owned firms. This analysis informs where policy should be targeted if CFEs are to be supported and fostered.

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## Introduction

Approximately 30% of forests in low and middle income countries are currently under ownership and/or management by indigenous and local communities (RRI, 2014). Factors such as decades of failed state management of forests, the 1987 Brundtland Commission Report, the 1992 Rio Declaration on Environment and Development, and groundbreaking research on the abilities of local users to manage natural resources successfully (see Ostrom, 1990) exerted considerable pressure for devolution of forest ownership and management rights to local users (Agrawal and Gibson, 1999; Dressler et al., 2015; Larson et al., 2010). This is a major shift from 20th century state forest policies that placed higher priority on national, colonial, or private sector interests and which rarely achieved claimed objectives of forest protection and rational use (Donovan et al., 2006; Larson et al., 2010). ‘Locally-controlled forestry’ has become a key theme in the international rural development agenda (Macqueen et al., 2012).

Developments in the global economy are presenting these ‘new’ forest owners with opportunities and challenges, domestically and internationally. Neoliberal economic restructuring since the 1970s has wielded considerable influence over conservation policy and practice, pressuring toward the use of market-based interventions (Roth and Dressler, 2012). Successive negotiations of the General Agreement on Tariffs and Trade (GATT) and the establishment of the World Trade Organization (WTO) have made industrialized country markets more accessible for developing countries (Donovan et al., 2008). Forest-related markets, production dynamics and supply chains are evolving (Molnar et al., 2008). Although there continues to be an important debate as to whether markets are positive or negative for natural resources and their owners (Belsky, 2015; Pacheco and Paudel, 2010), engagement of forest communities with markets is considered an inevitable trend (Richards, 1997). Few community-managed regimes remain isolated from external actors, including markets (Barnes and Van Laerhoven, 2015; Morrow and Hull, 1996). There is also growing enthusiasm for poverty-alleviation and local development effects that commercial opportunities may have for communities (Donovan et al., 2006; Kozak, 2007). It has been argued that one of the ways of targeting poverty reduction and conservation is by developing capacities of the rural poor to organize viable businesses capable of engaging with markets and commercializing goods and services (Donovan et al., 2008; Gilmour, 2016; Pokorny et al., 2012). NGOs, development agencies and governments are increasingly supporting start-ups of community-owned commercial ventures as part of their local development strategies. Thanks to these efforts, there has been a shift in the organization of production from large-scale industrial forestry to landholder-based and community forestry (Forster et al., 2003; Harrison et al., 2002; Molnar et al., 2007).

Much like the difficulty in scoping and defining the term ‘community forestry’ (Cronkleton et al., 2013), forms of market engagement by forest owners cannot be reduced to simple definitions, forces or formulations (Belsky, 2015). Trends in community forest management evolve in different regions at different rates (Wiersum et al., 2013). Market engagement is highly contingent on different types of forest management arrangements especially those offered to rural people through projects or policy (Cronkleton et al., 2013). NGOs, development agencies and practitioners wield considerable influence on the adoption of preferred models, as do state regulations and the institutional arrangements that constitute ‘community’ (Cronkleton et al., 2013; Pacheco, 2012; Pacheco et al., 2008). The array of forest products and services amenable to commercialization is also very diverse (Anderson et al., 2015). Small and medium, community-based forest enterprises (CFEs) based on collective or common ownership of the forest asset are a specific form of market engagement that has expanded dramatically in developing countries and contribute significantly to local employment in forest based economies (Molnar et al., 2008; Kozak, 2007). CFEs are engaged in the production of commercial timber,<sup>1</sup> ideally in compliance with sustainable timber norms designed for industrial forestry firms (Cronkleton et al., 2013). Collective management of forest resources is favored over individual ownership due to its advantages in economies of scale and standardization of community-level decisions, for example in forestry reforms in Bolivia, Guatemala and Cameroon (Cronkleton et al., 2013; Lescuyer, 2013) and in Mexico where 80% of forests are local communal property<sup>2</sup> (Antinori and Bray, 2005; Bray et al., 2006). However, commonly or collectively-owned forests also represent one of the biggest social coordination challenges for communities (Bluffstone et al., 2013).

Several authors and experts suggest that a key way in which decision-making about farm-forest landscapes can be improved to reflect diverse interests is through the implementation of community-based business models in the farm-forest sector (Macqueen et al., 2015; Sist et al., 2014; Tomaselli and Hajjar, 2011). Community-owned firms stand in contrast to traditional, investor-owned logging businesses that have been privileged by forest policy in developing countries until recently (Sist et al., 2014; Cronkleton et al., 2013). Given these trends, it has become relevant to understand the real and potential role of communities in producing timber for commercial purposes and how local resource management functions in the economy in general (Antinori and Bray, 2005; Antinori and Rausser, 2008). Community ownership of forest enterprises adds to the institutional and organizational variety that increasingly characterizes economic systems (Borzaga et al., 2010) yet surprisingly little has been written about these firms as an alternative form of enterprise ownership with specific attributes and behavior.

Due to core assumptions of self-interested individuals and profit maximization in firms, orthodox microeconomic theory has little applicability to the study of these types of enterprises in market economies (Borzaga et al., 2009). This is reiterated by Ostrom who argued that theories of the firm are unsuitable for studying common property regimes because they assume

<sup>1</sup> Production of non-timber forest products and ecosystem services such as carbon sequestration is also possible.

<sup>2</sup> Common property driven by Article 27 of the Constitution of 1917 in the forms of ejido and comunidad governance systems has provided the social matrix for the emergence of CFE management institutions in Mexico (Antinori and Bray, 2005). Timber extraction and commercialization have relatively recently experienced divisions but forests continue to be common property (Bray et al., 2006). There are some documented cases of enterprises erected on the base of private property (see Antinori and Bray, 2005).

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