



Land rental development via institutional innovation in rural Jiangsu, China



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ABSTRACT

Previous studies have demonstrated that there are two important preconditions for encouraging land rental in agriculture: out-migration and the enhancement of security and transferability of land rights. Focusing on the latter, we scrutinize the impacts of institutions aimed at facilitating land use dynamism, particularly the Rural Shareholding Cooperatives (RSCs), which have been established recently at the local level in rural China. In general, we find that RSCs can pave the way for the extension of property rights to farmland and promote more efficient land use patterns. Using survey data collected from 300 village committees in rural Jiangsu province, we estimate the effectiveness of RSCs in encouraging land rental. Our analysis reveals that RSCs can serve as intermediate agents for reducing transaction costs associated with exchange of land use rights and, thereby, not only encourage land rental/consolidation activities but also enable the entry of non-farm household entities into the farm business.

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Introduction

Security and transferability of land rights are important prerequisites for encouraging the development of land rental markets in agriculture. When these rights are ambiguous or contested, lessors and lessees may be averse to participating in otherwise beneficial transactions, with the consequence that land use inefficiency will persist (Deininger and Binswanger, 2001; Deininger and Feder, 2009). Another precondition for promoting land rental is the out-migration of rural people associated with economic growth. This is particularly relevant in many Asian developing countries whose farm sectors are characterized by small landholdings and overemployment. Uneven decreases in agricultural labor among farms are likely to alter the land-labor ratio and provide impetus for inter-farm reallocation of labor and/or land. However, there is an established view that the farm labor market does not work efficiently in the real world because supervising and managing hired workers involve high transaction costs, especially in spatially dispersed agricultural environments (Carter and Yao, 2002; Eswaran and Kotwal, 1985; Otsuka, 2007).

Moreover, land rental does not automatically remedy land use inefficiency associated with the inter-household productivity

differential, because pervasive market failure caused by high transaction costs and imperfect information inhibit the process of efficiency-enhancing land reallocation (Ravallion and Van de Walle, 2006; Skoufias, 1995). Even 'arm's length' transactions do not necessarily result in efficient land use if farm expansion is achieved by taking on non-adjacent pieces of farmland. As described by Deininger and Jin (2005), Yao (2000), and others, organizational intermediation in transactions that helps to lower transaction costs and information asymmetry is of great importance for the development of land rental markets and consolidation of scattered plots of farmland.

Since the mid-2000s, China's land rental markets in agriculture have developed quite rapidly in the suburbs of metropolitan and coastal areas, and in some grain growing regions. The driving forces behind this movement are institutional reform of land rights and the mass exodus of rural people to urban centers. As has been pointed out in many studies, institutional reform of land rights facilitates land tenure security, while the willingness of rural people to relocate enhances the opportunity to subcontract their land during their absence (e.g., Benjamin and Brandt, 2002; Brandt et al., 2004; Carter and Yao, 2002; Deininger and Jin, 2005; Jin and Deininger, 2009; Kimura et al., 2011; Kung, 2002; Yao, 2000; Zhang et al., 2004).

Complementing these empirical findings, we focus on the institutional support that has developed to facilitate such land transactions. Specifically, we studied the impact of local organizations

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known as Rural Shareholding Cooperatives (RSCs), which increasingly serve an intermediate role in land exchange. Previous studies of RSCs have evaluated their role in farmland conversion, but have not considered their institutional impact on land rental in agriculture. This study aims to fill this gap in the literature. Our econometric analyses, based on the treatment effect model, suggest that RSCs established recently at the grass-roots level make a substantial contribution to land rental/consolidation and the entry of non-farm household entities into farm management. This has important implications for Chinese agriculture, which is characterized by small landholdings and excessive fragmentation of farmland (Tan et al., 2006). In order for Chinese agricultural production to be sustained, and its international competitiveness improved in a situation of increasing opportunity costs of farm labor, it is necessary to achieve economies of scale by expanding the size of individual farms and consolidating scattered plots of land into operational units of sufficient size (Otsuka, 2014).

The remainder of this paper is organized as follows. The next section outlines the institutional aspects of land right reforms and rental markets in rural China. The third section briefly describes our study site and the main findings from our village survey. The fourth section contains a concise overview of the treatment effect model and presents the estimation results of the parametric and semi-parametric methods. Finally, the fifth section concludes with a brief summary of our results and provides some policy implications.

Land rights reforms and rental markets

Collectively owned land system and land reallocation

With the collapse of the People's Commune System and implementation of the Household Responsibility System (HRS) in the early 1980s, the farm management system in China changed dramatically. Farmers were allowed to grow crops at their discretion and retain their farm income as long as they met tax and grain quota delivery obligations. The right to farm management and the claim on residual farm income raised their incentives to work hard, and thereby boosted agricultural productivity. However, some economists argue that the reform of this era was incomplete, because land ownership remained vested in rural collectives and, as a result, ambiguity in property rights persisted (Carter and Yao, 2002; Lohmar, 2006). Even today, the Chinese Communist Party (CCP) shows no inclination to consider outright privatization of rural land.

Under the current institutional framework, people who are registered as farmers in rural communities have two kinds of land rights: contract rights and use rights. Since land use restrictions, such as the production quota and agricultural taxes, have been abolished altogether, the land contract rights granted automatically to rural citizens at birth have come to serve a purpose similar to land deeds or titles. The Land Management Law (LML), amended in 1998, stipulates that rural collectives should issue certificates to formalize this 'natural' land right. At the same time, land use rights became transferable, with the consequence that transactions involving these rights can be considered to be a form of land rental. When the HRS was introduced, land contracts were initially granted for a period of three years. These were extended to 15 years in 1984, and extended again in 1993 for an additional 30 years after the initial term expired (this 30-year term was formally codified in 1998). In 2008, the CCP extended the contract duration to an unspecified "long term" (Wang et al., 2011), and additionally, farm households were entitled to inherit their contract rights.

Although the central government has been actively committed to land tenure security for farm households, rural collectives at

the local level used to confiscate contract rights routinely from some households and redistributed them to others (Brandt et al., 2004). This administrative measure, referred to as land reallocation, was designed to equalize per capita land access in response to household demographic change, and thereby, to prevent inter-household income imbalances from arising.¹ Zhang (2008) reports that the frequency of village-wide reallocation during the 1980s and 1990s was once every 8–10 years, supplemented by partial small-scale reallocation. A serious problem arising from administrative land reallocation was that rural people who temporarily ceased farming for some reason placed themselves at higher risk of having their land contract rights revoked. This uncertainty and insecurity was to the detriment of sound development of the land rental market (Deininger and Jin, 2005; Feng et al., 2010; Krusekopf, 2002; Tao and Xu, 2007). Farmers' anxiety was compounded by the fact that most rural people migrated out on the presumption their stay in cities was temporary and they would return to their home village eventually. Consequently, risk aversion discouraged them from participating openly in land markets, with many preferring to exchange land usufruct within close-knit groups or on an underground basis in their communities (Wang et al., 2011).² Responding to this, amendments to the LML in 2003 prohibited rural collectives from conducting reallocation when land contract rights are still valid.

Land rental markets

It was not until the mid-1980s that China's policymakers legitimized the transactions of land use rights (Article 2 of the LML).³ The reason for their hesitant attitude toward land rental was that they were greatly concerned about the emergence of landless tenants and harmful forms of economic stratification among rural populations (Liu et al., 1998). The land rental model originally envisaged by the central government involved arm's length transactions within the same community. Amendments to the LML in 1998 stipulate that a two-thirds majority of villagers is needed for any non-members of the collective to acquire land use rights. Accordingly, land transactions mediated through the open market remained minimal throughout the 1980s and most of the 1990s (Zhang, 2008). However, in the late 1990s, urban migrants in China outnumbered rural workers employed by township and village enterprises in local areas, a phenomenon which spurred the development of land rental markets. It should be noted, however, that was but one of many enabling elements that could potentially facilitate market-based land exchanges.

As described earlier in this section, the confiscation of land contract rights by rural collectives in the process of administrative reallocation would undermine farmers' incentive to rent out their land. In order for land rental markets to develop, the government had to ensure the separation between land contract rights and land use rights, and then guarantee the former very convincingly. The land rights realignment program over the past two decades has effectively addressed this through the lengthening of contract

¹ Rental markets and administrative reallocations are, in principle, substitute mechanisms, as long as efficient resource allocation is realized in the process of equalizing the land-labor ratio across households (Benjamin and Brandt, 2002; Brandt et al., 2004). However, Brandt et al. (2004) express the view that, in practice, administrative reallocation often leaves significant gains from land exchange unexploited.

² According to Lohmar (2006) and Zhang and Makeham (1992), some farmers with off-farm employment pay rewards to others to keep their land in production and fulfill their grain quota delivery obligations. The effects of land tenure insecurity and farmers' inability to use landholdings as collateral on land improving investments are important subjects to be explored, although they are not addressed in this study.

³ The central government promulgated the Rural Land Contract Law in 2002, which gave official approval for market-based land exchanges.

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