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COMMENTARY

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China's New Market in Land

By ROY L. PROSTERMAN

It passed almost unnoticed in the media, but what may be China's most important piece of market-creating legislation went into effect last Saturday. The new Rural Land Contracting Law, adopted in August 2002, fundamentally transforms the nature of the land rights held by China's nearly 210 million farm households, for the first time giving them something approaching owner-like rights to the land they farm.

This important reform should help address what outgoing Chinese Premier Zhu Rongji has often called his "biggest headache" -- the task of increasing the income of farmers. That's because the spectacular growth achieved by China during its more than two decades of reform and opening has disproportionately benefited urban residents and, in recent years, the gap between urban and rural standards of living has continued to widen.

Although China broke up its collective farms in the early 1980s under a program known as the household-responsibility system, ownership of rural land has remained with the former collective, typically at the village level. Each village household was allocated a share of village land based on the size of their household, and permitted to retain or market any surplus beyond a state quota.

But these rights to use village land suffered greatly from the fact that local officials could frequently and unpredictably "readjust" them, taking away and granting land parcels on the basis of changes in household size. Because of these readjustments, farmers could never be certain of their tenure on any individual piece of land. Interviews which I have conducted in Chinese villages since 1987 found that this insecurity forestalled nearly all long-term investments by farmers, such as irrigation wells, drainage, tree planting or greenhouses.

Now, as a result of the new law, farm households will receive 30-year land-use rights, backed by written contracts and user certificates. These will be free from the threat of readjustment in all but extreme cases, such as natural disasters. Chinese farmers see such "one-generation" rights as sufficient to justify nearly all the needed investments. The law also allows farmers to engage in a broad range of transactions involving their land rights and imposes specific and harsh penalties on local officials who interfere with farmers' rights.

Such secure and highly marketable 30-year rights should provide the essential spark to drive the engine of rural consumption and boost economic development in China.

One need look no farther than Taiwan for an example of this. In the decade following the island's successful land-to-the-tiller program from 1949-53 (in which former tenant farmers received

secure, long-term rights to the land they farmed), annual rice yields increased by an average of 60%. During the same period, farm household incomes, further amplified by diversification into higher value-added crops, increased by an average of 150%. These rising incomes were almost immediately translated into substantial increases in consumption of basic consumer goods such as clothing, furniture and bicycles.

Over the longer term, huge increases in the value of Taiwan's secure and transactable land rights, combined with the availability of mortgage credit, provided the capital required to transform farmers into entrepreneurs as well as consumers. Now, as I discovered during fieldwork three years ago, the vast majority of Taiwan's farmers own a car, computer and cellular phone, have bought stocks and have traveled overseas.

The current population of rural China represents a potential market that is 40 times the size of Taiwan. By bringing to life the "dead capital" (to use Peruvian economist Hernando de Soto's phrase) currently tied up in the land, the new law will make this market a reality.

Research on comparable land markets elsewhere in Asia indicates that a conservative short-term estimate for the value of China's 130 million hectares of agricultural land is \$500-600 billion. That should be enough to put smiles on faces in boardrooms around the globe, not to mention the leaders' compound in Zhongnanhai.

Mr. Prosterman is president of the Seattle-based Rural Development Institute and professor of law at the University of Washington.