



## LIVING WITH CONSTRAINTS: RUSSIA'S AGRICULTURAL LAND MARKET

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### Paper privatization

IN RUSSIA, PRIVATE OWNERSHIP OF LAND used for agricultural production was made legal in 1990. Independent peasant farms began to emerge, and land in the former collective and state farms (*kolkhozes* and *sovkhozes*) was divided among the member-employees in the form of land shares, which are paper certificates that entitle the individual to a certain amount of land in an unspecified location. In other words, land shares impart the *right* to a land plot and are used as proxies for physical plots. This kind of “paper privatization” did not involve immediate distribution of land plots to new owners. The law stipulated, however, that owners of land shares could leave the former collective and establish a peasant farm on a land plot equal in size to their land share. Pending the withdrawal of a physical plot, agricultural land represented by all the paper shares was considered to be in “joint shared ownership.” Even with this legal basis for the privatization of agricultural land, the legal ban on buying and selling land—a precondition for the development of a land market—was not lifted until 2003. As a consequence, most agricultural land is used by those who do not actually own the land.

No statistical data are available on transactions in agricultural land or land shares. Nor is there information on the terms of land transactions, the composition of buyers and sellers, or supply and demand. Therefore, in 2003, BASIS researchers carried out questionnaire-based surveys in three regions that differ by the level of agricultural development and natural condi-

tions. One region is agriculturally depressed, the second shows medium agricultural development, and the third is a region of highly developed agriculture. The surveys covered three basic agricultural organizational forms: corporate farms, which average 4100 hectares, peasant farms, which average 270 hectares, and household plots, which average 2.6 hectares (see **BASIS Brief 34** on farm structures). Evidence from the surveys establishes an emerging picture of the land market in Russia and its constraints. Based on our findings, we created a set of policy recommendations that address these constraints, especially the institutional constraints and their impact on land turnover.

### Demand

Our findings show that 93% of land in household plots is owned. On peasant farms, only 42% of land is owned, and it consists of land shares and land plots allotted without payment to the family members during privatization, as well as shares and plots purchased over time from other landowners. On corporate farms, owned land consists of land shares invested by members in the equity capital of the agricultural corporation and it constitutes less than 2% according to official statistics for all Russia. Land leasing is predominant among corporate and peasant farms, with the share of leased land, on average, approximately 60% of the total area of agricultural land used.

In all of Russia, about 5% of agricultural land is transacted annually. Our survey covering 553 farms

showed 86 land transactions during one year, with frequency of transactions virtually the same across the three farm types. Only three cases involved buying and selling land; the other 83 transactions involved leasing land. Without doubt, leasing is the dominant form of transaction in land markets across Russia, and most of these transactions remain outside the scope of official statistics. The survey did not detect dependence of the frequency of land transactions to proximity to the regional center, yet there are particularly active land markets in the Moscow Oblast, where farmland is bought for non-agricultural purposes, which we identified as a serious policy issue.

The observed situation of few transactions does not necessarily reflect a satisfied demand for land. In general, in all three survey regions, peasant farmers and owners of household plots show a willingness to enlarge their holdings, with peasant farmers demonstrating the highest demand. In the agriculturally depressed survey region, 45% of corporate farms plan to reduce the use of land and only 3% plan to enlarge it. A similar trend is observed in the region with medium agricultural development, suggesting that corporate farms in agriculturally less-developed regions probably will release land when they re-register their use rights in state land and lease contracts for land shares, as mandated by a new law. Some of this land will be absorbed by peasant farmers, yet peasant farms are a very small segment compared to corporate farms, and much of the land released may remain unused. An opposite situation is likely in the study region that has highly developed agriculture. Here, there will be no unused agricultural land, and unsatisfied demand for land may arise. In this region and similarly fertile ones across Russia, there is a clear demand for land for large-scale agricultural production.

## Constraints

Most respondents did not know the prevailing land prices, which indicates that there are no established prices for land—that is, no benchmark to help rural people decide whether to sell or lease land. The issue of the market price of land is important because federal law mandates using market prices when partitioning land currently held in joint shared ownership, and disputes are resolved by applying the market price of specific plots. Lack of consistent prices could be a severe barrier to partitioning joint shared land and withdrawing land for individual farming. A similar

problem arises with the buyout of land that was formerly given in permanent use. According to the law, state land should be bought on the basis of market prices. The state is therefore obliged to set calculated (normative) prices, but these normative prices and the rules of their calculation are not publicly available.

High registration costs and complex procedures seem to be an obstacle to land transactions. Most (84%) of the peasant farmers in the more agriculturally developed region regard these issues as a major problem. Analysis of registration procedures shows that numerous administrative and organizational restrictions have been created. In the system in force until 1998, all procedures were carried out by district committees, which kept the land redistribution maps, lists of shared landowners, copies of land ownership certificates, and other documents confirming land rights. The committees also registered transactions of land shares and land plots. Today, however, three organizational levels are involved in registering land transactions: the aforementioned district committees, cadastral chambers, and registration chambers. The cadastral chambers register land plots. The registration chambers register use rights and transactions. Previously issued certificates of land ownership rights theoretically have the same validity as new entries. In practice, however, each new transaction requires full registration of the previous rights. This involves presenting a full set of documents issued at the time of original privatization, including old cadastral plans of the land plots that became joint shared ownership. The first transaction (leasing or sale) immediately triggers the need to go through the entire process of formal registration of previous rights.

The new system suffers from at least two serious problems. The first is the refusal of the cadastral chambers to issue registry extracts for land plots in joint shared ownership. As a result, the whole area in joint shared ownership has to be surveyed anew. This is not only very expensive, but it also takes at least two months to complete. The second problem is the multi-step and opaque operation of the registration and cadastral chambers. These bodies develop internal instructions that are not always compatible with the relevant law and require additional documents that were not envisaged by the law. These problems sharply increase transactions costs.

Registering land rights or converting land shares into a plot requires going through at least eight bureaucratic organizations and can take six months. Selling a land

share requires dealing with at least four organizations and takes more than three months. These are “best case” scenarios. Usually the time delays are substantially longer. Withdrawal of a single land plot from joint shared ownership can require one year of constant interaction with the bureaucracy.

Costs of registering previously existing ownership rights varies widely. Theoretically the total shared area is already registered in the cadastre and the applicant only has to pay 100 rubles to get the cadastral extract for his land share. In practice, however, officials often require a full survey to identify the individual plot, a process that becomes too expensive for a private landowner. The cost of the entire procedure of converting a land share into a plot of land can be estimated by comparing the market price of a land share with the market price of a registered plot in the same area. For example, in a rural district near Moscow, the price of a plot is double the price of a land share before conversion.

Large corporate farms that can afford to hire advisors and have specialized staff responsible for registering transactions are in an advantageous position. This is a typical example of market asymmetry, where some agents have more information than others. Meanwhile, having neither the time nor money to register land, many land-share owners, peasant farmers, and former collectives give up their rights or use land that is not legally registered.

Other constraints to the land market were identified. In theory, agricultural land is protected by law, yet in practice nothing prevents it from being rezoned into non-agricultural land. Buying cheap agricultural land can result in a substantial profit when the plots are sold for country cottages near Moscow or other desirable locations. For example, 0.01 hectare of agricultural land can be bought for US\$3-10, but after rezoning the same plot can be sold for residential construction for more than US\$500. Ultimately, the stock of agricultural land in some regions may be severely depleted by such transactions.

Mortgaging agricultural land is now legal, yet the law imposes requirements that are barely relevant to the existing situation. Only a land plot can be mortgaged, and yet most agricultural land is in joint shared ownership. Only owned land can be mortgaged, and yet owned land accounts for a mere fraction of agricultural land used by corporate farms. To mortgage a specific plot, the entire area has to be surveyed, the

plot has to be registered as a separate object, and the ownership rights have to be registered—procedures that cost much time and money. The mortgaged property must be insured by the borrower or else the lender can demand immediate repayment of the loan, and yet insurance companies do not provide this service because they do not know how to assess the risks. Each of these issues constitutes a serious obstacle to collateralizing agricultural land.

## A shrinking sector

Agricultural land is mainly owned by the rural population: workers and pensioners of corporate farms created by reorganization of *kolkhozes* and *sovkhozes*. These owners are generally poor. According to official data, agricultural wages remain at 40% of the national average (see **BASIS Brief 37** on agricultural labor). In April 2002, 51% of agricultural workers earned fewer than 1,000 rubles per month; by comparison, the minimum price of land (in the form of land shares, before conversion into plots) in the Moscow Oblast is 10,000 rubles per hectare, and the average land share is 3-4 hectares. Land shares have become a valuable commodity in impoverished areas, with the price often comparable to one to three years of wages or pensions that a rural person receives. Clearly, many rural owners would be willing to sell their land if there were buyers.

There were not many buyers during the initial stages of land privatization. Many heirs, therefore, never bothered to register the rights to their inherited land because registration would only lead to a tax without any increase of income. According to calculations for four corporate farms in the Moscow Oblast, the dead “owned” nearly 30% of land shares as of 2004. Recently, however, as demand for land shares materialized, heirs began to register their rights to the inherited land.

What type of buyers created this new demand? Analysis of the high demand for land in regions close to Moscow, suggests that surplus cash accumulated in other sectors of the economy may encourage non-agricultural businesses to buy land from rural landowners. Available data suggest the following: surplus profits that are not used for investment in assets are increasing, deposits in Russian banks are becoming less attractive, and the decrease of the dollar/ruble exchange rate drives depositors away from foreign-currency accounts. These factors, coupled with experts predicting an imminent fall in real estate



## B A S I S B r i e f s

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Publication made possible  
by support in part from  
the US Agency for  
International Development  
(USAID) Grant No.  
LAG-A-00-96-90016-00  
through BASIS CRSP.



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Edited and layout by  
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prices, drive businesses to search for new investment opportunities. The demand for suburban homes and the poverty of rural land-share owners make it possible for non-agricultural businesses to buy agricultural land (see also **BASIS Brief 35**).

Traditional agricultural producers are uncompetitive in the land market. To compete against those who buy land for non-agricultural purposes, lease payments from corporate farms and peasant farmers should at least be equal to the bank interest rate on the market value of a land share—on average, 1,000 rubles per hectare. Given the generally low profitability of agricultural land, Russian agricultural producers cannot afford such payments and will continue to sell to outside buyers in the future.

### Policy recommendations

A vigorous and functional market in agricultural land can enlarge individual holdings and increase production efficiency. Yet the BASIS research shows that, in Russia, access to market information is limited or difficult to obtain, transactions are marred by complex bureaucratic procedures and high costs, and agricultural land is often used for non-agricultural purposes. Below we outline ways to combat these problems.

*Create a market information system.* Introduce standard reporting requirements for organizations that deal with registration of ownership rights and transactions in land shares and land plots. Specify in law the sources of public data on market prices that will be available on websites of relevant organizations. Finally, establish an authority for conducting market-price surveys and collecting price information needed for re-registration of previous rights for permanent use of land.

*Reduce transactions costs.* Introduce a simplified cadastral registration procedure that allows varying degrees of detail in the description of land plots by owner's consent, utilizes available information in

district committees for land resources and land planning, cadastral chambers, and land-surveying institutes, and enables land users and landowners to access cartographic data banks created at taxpayers' expense. Establish a procedure for registration in the Central State Register of Rights on the basis of documents issued to landowners before 1998, without any additional demands from landowners and land users. Finally, develop a single and complete set of clear requirements for documents from applicants, and issue binding regulations that oblige officials to publish a full list of required actions.

*Protect agricultural land from non-agricultural uses.* Establish a legal procedure for rezoning agricultural land. Establish zoning rules for rural areas identifying where construction is allowed. Amend the relevant laws so as to preclude non-agricultural construction on agricultural land and restrict the construction of garden houses to designated zones. Finally, establish standard procedures for controlling the designated use of agricultural land and criteria for identifying unused or improperly used land.



### Further reading

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