

Land Markets and Public Policy: A Conceptual Framework*

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INTRODUCTION

Imperfections and failures commonly observed in land markets often compel policy-makers to search for a framework of public intervention. In particular, in developing countries where resources are scarce, inequality persists, and rapid spatial transformation takes place, problems in land markets create an agenda of unusual complexity and urgency for public policy.

Policy-makers in different countries have approached land-use problems with different intervention strategies. In the past, most countries in the developing world have attempted to guide or control actors in land markets by incentives and regulations. In addition, several developing countries have recently increased the level of public intervention by instituting public land acquisition as an alternative strategy to control land-use.

The use of various public intervention measures in land markets is based on the premise that the public sector can deal with land-use decisions effectively through a set of explicit land policy measures. Various studies on land-use policies conducted in the past have attempted to detect the direct causal relations between explicit land-use policies and consequences in land-use patterns. A crucial drawback of this attempt is that it does not provide a proper account of the land-use impacts arising from a number of implicit land policies. Thus, studies linking explicit land-use policies to land-use decisions often misinterpret the source of success or failure in land-use planning. Policy implications of this misinterpretation are significant. Public resources can be mistakenly directed to land policies which may have little effect on overall pattern of land use.

This paper sets forth a conceptual framework to analyse the nature and effectiveness of land policies in the process of national development. It begins with a general discussion of rationale for public intervention in land markets. Then, three different strategies of explicit land policies are described and relevant examples are provided. This is followed by a discussion of three types of implicit land policies which affect allocation of land. Finally, an integrative framework for evaluating the effectiveness of land-use policies is developed. The integrative framework presents the concepts of dominance and consistency in policy-making and implementation processes. The framework is recommended for analysis of country case studies.

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RATIONALE FOR LAND POLICIES

Free market ideologists often argue that there is no reason for the public sector to intervene in land markets. They believe that untrammelled land markets are the best means of allocating land among competing users. However, there are at least three categories of rationale for public intervention into the free operation of land markets. They are: (1) land market imperfection and failure; (2) distributional aspects of land ownership; and (3) severe disequilibria in land markets.

In an ideal market economy, optimising individuals and firms under perfect competition would lead to an efficient allocation of resources. However, realities impede the function of land markets to allocate land in a socially optimal or desirable way. First of all, many of the conditions for perfect competition are frequently violated in land markets. For example, the special characteristics of land and real estate properties as a commodity — durability, immobility, and transaction barriers — transgress the assumptions of perfectly competitive markets. In addition, even under perfect competition, markets often fail; existence of externalities and public goods associated with land use prevents market mechanisms from achieving optimum allocation of land among competing users. It is often observed that geographical spill-overs between incompatible land-use activities give rise to inefficiency.

In an unlikely situation, where land markets operate under perfect competition and without failure, there are other reasons to question the function of markets to deal with land-use in a socially desirable fashion. Land is an important form of asset for households and its value increases faster than general price indexes. Consequently, distribution of land ownership bears significant implications to equity. Pure market forces, however, tend to ignore distributional aspects of land-use. Furthermore, as an essential input to production of shelter, land is an indispensable resource to meet the basic needs of the populace. In developing countries, purchasing a minimum quantity of decent housing in the market is beyond the means of a large proportion of the population.

It is also worth noting that, in rapidly urbanising countries, land markets can easily fall into disequilibria. Many primate cities in developing countries have almost doubled their population during the last two decades, and the trends are expected to continue. Resource limitation in the private sector may cause the supply of improved land to lag substantially behind the demand created by sudden urban growth. Once the disequilibrium in land markets becomes a chronic phenomenon, it reduces the risk of holdout and speculation. This circumstance will hamper further the supply of improved land.

THREE STRATEGIES OF EXPLICIT POLICY INTERVENTION IN LAND MARKETS

The difficulties inherent in land markets to bring about a socially optimal or desirable pattern of land-use provide policy-makers with both economic rationale and political motivation to initiate policy intervention. A variety of *explicit land policies* can be formulated and put into effect to deal with problems of land-use. By “explicit” is meant that policies are deliberately designed to achieve certain goals of land-use. One of the key factors which affect the design of a strategy of intervention in land markets is the degree of confidence in the market system. Reliability of the market function perceived by policy-makers is an important determinant of the depth and direction of policy intervention.

Broadly, there are three basic approaches in public intervention into land markets: (1) market incentives; (2) regulatory measures; and (3) direct public ownership.

First, at the lowest level of intervention, market incentives, both positive and negative, are used to either facilitate or discourage the behaviour of sellers and buyers in land markets. The strategy of market incentives is embedded in reasonable trust for the capability of markets. It attempts to spur smooth and efficient transactions and to affect distribution of resources by means of economic incentives and disincentives. Typical policy instruments embrace the land value increment tax, property tax, housing subsidy, land development subsidy, *etc.*

The next level of intervention strategy involves explicit control over the behaviour of private agents by regulatory measures. The public sector's confidence in the market is weaker relative to the incentive approach. The strategy of regulation establishes directives, standards and rules to which participants in the land market are required to conform. The government resorts to such policy instruments as zoning, subdivision control, green-belts, permit control, rent control, maximum land holding, and licensing of land developers and intermediaries.

A strategy of the deepest level of public intervention is represented by direct engagement of the public sector in land development. The public sector doubts the capacity of the market system to promote desired goals of land policy and is directly involved in buying, developing, and disposing of land. The scope and nature of direct acquisition and development policy vary substantially. On a small scale, local institutions may participate in land acquisition and development to provide low-income housing, infrastructure, and community service facilities. Governments at various levels can be in charge of industrial estate development or land readjustment projects. The central government may also adopt a nationwide system of land acquisition and disposal. In an extreme case, the government may nationalise all lands in its territory and allocate them through bureaucratic management. Various policy tools such as eminent domain, condemnation, purchase less than fee, normal purchase, leaseholds, *etc.* can be employed to set up a system of public land acquisition and development.

IMPLICIT POLICIES IN LAND MARKETS

The *explicit land policies* are only a subset of a variety of public policies. There are a number of other public policies which are not explicitly directed toward the goals of land-use but lead to inevitable influence over land-use decisions. These can be termed *implicit land policies*.

Implicit land-use policies can also be classified by three categories. First, there are public policies using market incentives which create impacts on land-use. For example, investment tax credit is a policy measure designed to facilitate private investment. But, it may induce growth and expansion of firms in specific areas. Other examples would include tax benefits for export commodities, and special tax provisions for foreign investment.

Second, there are regulations addressed to policy issues other than land-use, which create land-use impacts. Examples are import restrictions on certain goods, anti-trust measures and free export zones.

The third type of implicit land policies relates to direct ownership. Direct public ownership of land for military bases and other defense activities, for example, is clearly concerned with the goal of national security, but exercises considerable influence on land-use pattern.

INTEGRATIVE FRAMEWORK FOR EVALUATION OF LAND POLICIES

The preceding two sections can be summarised in a form of classification system for land policy measures. There are two criterion variables: the level of public intervention; and the explicitness of land-use goals. This classification system leads to a matrix of land policy measures (Table 1). For a country, all existing land policy measures can be classified under this system.

In order to detect the true source of policy impacts on land-use, it is necessary to investigate the dynamics of land-use decisions in a broad context of national policy-making. An analysis exclusively focused on explicit land policy measures may not be able to identify the true sources of changes in land-use patterns.

There are three crucial elements of national policy-making which deserve attention in discussing land policies in development processes. These are diagrammatically presented in Fig. 1. The first element is the national priority

Table 1. Classification of land policy measures

Explicitness of land-use goals	Level of intervention		
	Market incentives	Regulatory measures	Direct ownership
Explicit land policies	Land value increment tax	Zoning	Public land banking
	Property tax	Subdivision control	Public industrial estate
	Housing subsidy	Green belts	Land readjustment
		Maximum land holding	Nationalisation of land
Implicit land policies	Investment tax credit	Licensing of developers and intermediaries	Import restriction
	Tax benefit for export	Anti-trust measures	Military base
	Tax benefit for foreign investment	Free export zone	

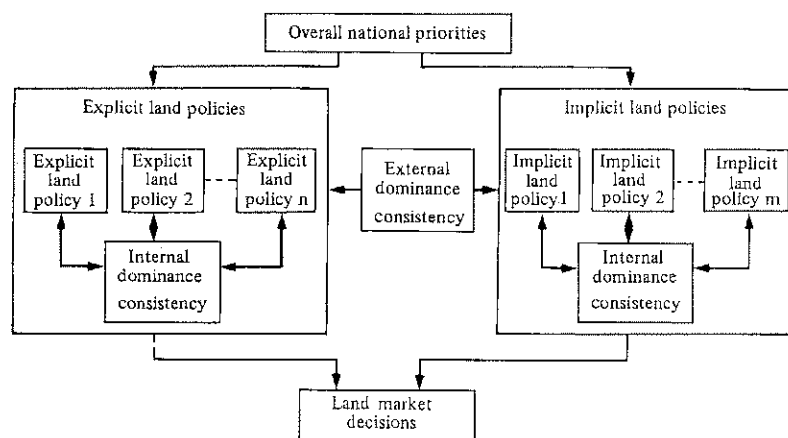


Fig. 1. National policy context for land-use.

concerning goals in policy-making and development planning. The priorities set by a country determine the overall direction of policy decisions and serve as a key guideline to resolve conflicts among different policies. The second includes the purpose, types, number, and significance of explicit and implicit policies which are put into effect. If there exist a large number of implicit policies which generate significant land-use impacts, a small number of explicit policies — however well-designed and effectively implemented — would not affect the land-use decisions in a significant manner. Third, it is also important to examine the relationship among various land policies. Two analytical concepts are proposed here. One is the concept of “dominance”. A particular policy may have a sweeping power — dominance — over others. In this case, the dominating policy with a specific goal will nullify other policies addressed to other goals. The other concept is “consistency”. If explicit and implicit policy measures are consistent with respect to certain goals of land-use, the possibility of obtaining the stated goals of land-use increases. However, if there exists a high level of inconsistency among various land policy measures, it is difficult to expect the desired goals of land-use achieved. The concepts of dominance and consistency can be applied to relationships between explicit and implicit policies as well as relationships between policies within the group of explicit or implicit policies. The former type of application can be termed *external* dominance and consistency, and the latter *internal* dominance and consistency.

SUMMARY

This paper presented a conceptual framework to analyse the nature and effectiveness of land policies in a broad context of national policy-making. Special attention was given to the way in which explicit and implicit land-use policies affect land-use decisions. A classification system of land-use policies was developed and the concepts of dominance and consistency were presented. The system and concepts can be usefully applied for empirical investigations.

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