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POLICY BRIEF

Leasehold as a Vehicle for Economic Development in Namibia

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Policy conclusions

- At present, commercial financial institutions do not accept registered leasehold over state land as collateral, which means that such leases cannot be traded.
- To use the full potential of leasehold, a land market should be allowed to develop to facilitate the selling of leases.
- A land market is also likely to impact positively on agricultural productivity in the small-scale farming sector by introducing flexibility through the legal sub-leasing of land.
- The allocation of land to resettlement beneficiaries for periods longer than 10 years in the absence of registered leasehold rights creates tenure insecurities and negates the benefits of resettlement.
- The subdivision of agricultural land for resettlement should be subject to the approval of the Ministry of Agriculture, Water and Forestry to ensure that sustainable and economical agricultural production is realised.
- Lease agreements for small-scale farmers should be signed and registered in the Deeds Office in order to have the rights formally transferred and to enable their use as instruments for accessing credit and investments.

1. Introduction

It is often assumed that secure tenure in the form of land titles is a required condition for economic development. This is based on the assumption that secure tenure will enable people to access credit which would not otherwise be available to them, in order to support economic activity and well-functioning land markets. Researchers such as Galiani and Scharfrodsky (2010) have found that at least in some cases the link between formal registration and poverty alleviation had come about due to an increased level of investment rather than access to credit. This would indicate that the form of title that would allow access to credit is less important than the security of tenure.

In order to promote economic development and redress the past imbalances in land ownership, the Namibian Government has introduced a variety of land reform instruments such as the Flexible Land Tenure System, the Affirmative Action Loan Scheme, communal land registration and the National Resettlement Programme. The latter two reforms are geared towards providing long-term leasehold rights on communal land and in former commercial areas.

Under the National Resettlement Programme and section 42 of the Agricultural (Commercial) Land Reform Act No. 6 of 1995 (ACLRA), the State purchases freehold commercial farms on a willing-seller willing-buyer basis, subdivides these into smaller parcels and allocates the parcels to selected beneficiaries. It is expected that leasehold rights will enable smallholder farmers to be economically productive and to enter the mainstream economy by using the lease agreements to access capital and investments to support agricultural production. The National Resettlement Policy (Ministry of Lands, Resettlement and Rehabilitation, 2001) states that *“the leasehold tenure system will be arranged so that the settlers can use the Lease Agreement as collateral to get a loan from lending institutions for agricultural production purposes”* (original emphasis). Long-term leaseholds in both the freehold and non-freehold sectors are regarded as essential for achieving the primary objectives of land reform: integrating previously disadvantaged Namibians into the wider economy and establishing them as independent farmers operating in a commercial environment.

The number of leaseholds allocated has not been adequately determined yet, and preliminary indications vary. However, with more than 5 006 families resettled since 1990 (Ministry of Lands and Resettlement, 2014), it appears that insufficient numbers of leaseholds have been allocated and registered, particularly in view of the fact that the Ministry stresses the importance of *“accord[ing] resettlement beneficiaries entitlement and security of tenure which can afford them an opportunity to access financial assistance and contribute to the national development goals”* (ibid.).

The Ministry of Lands and Resettlement ascribed the slow progress to cumbersome administrative procedures and some beneficiaries refusing to sign leases. The alleged unwillingness of beneficiaries to apply for the registration of leaseholds suggests that the costs of doing so might outweigh the potential benefits. More generally it is worth understanding the processes that could help to explain the perceived unwillingness of beneficiaries to apply for leasehold rights.

2. Institutional framework and transaction costs

Analysis of local-level rights and institutions against the centralised systems that allocate rights and resources is necessary, as research has shown that the beneficiaries' actions might be better explained, or influenced, by having local-level institutions which are relevant to their situations (Enemark & Sevetdal, 1999). The latter have argued that *“local institutions matter”*, and that *“peoples' behaviour patterns are framed more by local than central institutions”*. On the surveyed farms in the communal area of Oshikoto Region, local social, cultural and political considerations played a key role in how the farms were utilised and whether to apply for leasehold rights. This resulted in significant deviations between the *“de facto”* and the *“de jure”* situations on the farms. This is not uncommon and has been documented more extensively by other researchers, such as Barrows and Roth (1990, p. 277) and Moyo and Chambati (2012, p. 50) who found that customary rules around collective land ownership were still prevalent. The same was not observed in the freehold area of Oshikoto.

2.1 Registration of leasehold rights

The researchers analysed the institutional framework for resettlement allocations and the transaction costs in order to analyse the impact of leaseholds on the beneficiaries' ability to access credit and mobilise investments. The first objective is to describe and analyse the legal and institutional leasehold registration framework/process for resettlement allocations as well as the administrative and institutional processes required for registering a long-term lease agreement. Leasehold rights are defined as individual rights which are for a defined period of time and are considered virtually indistinguishable from full property rights.¹ The National Resettlement Policy, the ACLRA and the Communal Land Reform Act No. 5 of 2002 (CLRA) clearly make provision for, and anticipate the allocation of, leasehold rights to beneficiaries.

The third objective of the National Resettlement Policy, fully stated, reads as follows: *“to bring small-holder farmers into the mainstream of the Namibian economy by producing for the open market and to contribute to the country’s Gross Domestic Product”*. The section that describes the occupational rights of beneficiaries in the National Resettlement Programme unequivocally states that the *“Land acquired for resettlement purposes will be provided to beneficiaries on leasehold of 99 years. The leasehold tenure system will be arranged so that settlers can use the Lease Agreement as collateral to get a loan from lending institutions for agricultural purposes.”*

The general provisions of the National Resettlement Policy provide for the survey of resettlement parcels by the Office of the Surveyor-General, and for the Deeds Office to have *“overall responsibility for the assurance of property rights and the provision of services in the registration and safekeeping of lease agreements and other real rights”*.

All this provides a clear, deliberate and precise articulation of the institutional framework within which the rights of resettlement beneficiaries are to be located, and provides for the following key rights explicitly or by inference:

Explicit Rights

1. Resettlement beneficiaries will be provided with leasehold rights.
2. These leasehold rights shall be registered with the Deeds Office.
3. The leasehold rights should be acceptable as collateral for loans from financial institutions.

Inferred Rights

1. The leasehold rights should conform with the basic characteristics of leasehold agreements in the national context.
2. The leasehold rights should serve as the basis for allowing the holders to participate in Namibia’s mainstream economy.
3. The leasehold rights must be transferable.

What this means for the current process of awarding land rights under the National Resettlement Programme – specifically leasehold rights – must be considered in relation to the framework for such rights as determined by the ACLRA and the Deeds Registries Act No. 14 of 2015.

2.2 Subdivision of agricultural land for registration of leaseholds

The Deeds Registries Act No. 14 of 2015 provides the framework for the registration of leasehold rights, while the Subdivision of Agricultural Land Act No. 70 of 1970 (SALA) makes provision for the subdivision of agricultural land. However, the SALA is not applicable to communal land, and a provision in the ACLRA exempts the Ministry of Land Reform (MLR) from requiring the consent of the Minister responsible for Agriculture. This has created an opportunity for agricultural land to

¹ This is important to note as often the local stakeholders, beneficiaries and other researchers (see e.g. Ministry of Land Reform, 2016) did not adequately distinguish between allocation letters and leasehold rights.

be subdivided into non-viable holdings through the resettlement programme. The subdivision of land into parcels which are not economically viable given the predominant agricultural use in the area serves to greatly reduce the potential economic productivity of resettlement beneficiaries, and therefore also their ability to join the mainstream economy. The situation with regard to designated leasehold areas in communal land is less clear. It is the researchers' opinion that once land is designated, and therefore no longer communal, the provisions of the SALA should apply.

2.3 Cost of registering leasehold rights

Douglas C. North (1990) argues that analysts vastly underestimate the impact of institutions on economic productivity, and that the costliness of information is critical to evaluating the cost of the attributes being exchanged. It was found that the registration of lease agreements generates transaction costs that appear to be an impediment to the full implementation of government policy and its legal framework.

Different types of transaction costs can be identified, such as measurement costs, information costs and enforcement costs (North, 1990) as well as search costs, legal costs, administrative costs and uncertainty costs (Quigley, 1996), as reported by Zevenbergen, Frank, and Stubkjaer (2007).

The researchers found that the beneficiaries generally occupied their farms and knew their boundaries as well their neighbours' boundaries, and possessed some form of proof of allocation.² Conflict about the occupants' rights and identities and the spatial extent of their boundaries did not appear to be a significant factor. They considered their rights to be reasonably secure, despite the fact that legally this is not the case. The exception was the group resettlement scheme on Farm Urwald, where increasing informal subdivisions were taking place. The records suggest that the farm was initially subdivided into three leasehold areas, for which survey diagrams exist. Prior to that, an attempt was made to subdivide the farm into 115 plots of 10 hectares each, in accordance with a layout plan which is mentioned in correspondence but could not be traced.

The policy environment encourages the registration of resettlement leasehold rights. The institutional framework allows for, and in some cases requires, the registration of resettlement leaseholds. The requirements are clear and the process is not so complex as to constitute a major impediment to the registration of leaseholds. However, in practice such registration has not happened.

It was found that by April 2016 only six leaseholds had been registered, despite the registration requirements and process being relatively straightforward and transparent. Leasehold agreements were in some instances signed between the State and the beneficiary, but never registered with the Registrar of Deeds, rendering the leases essentially useless for accessing credit. Unsurprisingly, considering the above, it was found that no lessee had used the leasehold rights to access credit or mobilise investments, even though they considered their rights to be generally secure. Instead, those who were able to obtain loans used other forms of collateral such as insurance policies or urban property as surety.

Analysis of the direct transaction costs revealed that they do compare well with international norms, and constituted 5% of the estimated property value. The direct transaction costs in and of themselves were therefore not considered to be a major reason for the non-registration of leaseholds. Comparing the transaction costs with the expected income of resettlement beneficiaries, based on current economic activities, it became evident that direct transaction costs were equivalent to or exceeded the annual potential income of the allotments.

The findings suggest a number of reasons for the lack of registration of leaseholds. There seems to be a general lack of information among beneficiaries about the process and requirements for registration, implementing agencies and financial institutions. This information deficit relates to the value of the allotments, the potential range of economic activities and the leasehold process itself, including information about essential statutory requirements. It was found that the indirect

2 There is evidence suggesting that a large number of allotments across Namibia's regions do not have clear physical boundaries (see Werner & Odendaal, 2010).

costs, information costs and uncertainty costs (derived rights) contribute to the slow uptake of leasehold registration. It also appears that local conditions and customs play a significant role in how beneficiaries understand and respond to these processes.

The second finding relates to financial, technical and other capabilities of the beneficiaries as well as the economic potential of the parcels, rather than the leasehold registration process itself. Analysis of the transaction costs reveals that they are significant in relation to the earning potential of beneficiaries. While there are complaints about the costs associated with registration, it is not so much that these costs are outside the norm, but rather that the beneficiaries are simply unable to afford these costs, given their assets and the range of their plausible economic activities. The option to offer registered leasehold as collateral for loans will not be attractive to farmers and bankers unless the farmers are able to service such loans. This requires that farmers have sufficient assets, which in turn depends on a number of factors, particularly farm size. It is argued that the minimum farm sizes recommended for small-scale farmers are too small to substantially improve their livelihoods while also leaving enough cash flow to maintain farm infrastructure, make capital investments and service a loan.

3. Leasehold as collateral

Access to finance is important for investments in any enterprise, but the nature of leasehold serving as collateral is widely misunderstood.

Fundamental to collateral is the lender's ability to take possession of the leased land "*through a process called foreclosure and sell it to get back the principal (he/she) lent*" (<http://www.investopedia.com>, accessed 11 June 2016). Without an active land market that allows for easy land transfers, collateral has little economic value. "*Banks are not likely to accept as collateral land for which foreclosure in case of default is difficult, costly, or forbidden by law or social custom. In addition, banks are likely to accept land as collateral only in situations where the land market is sufficiently active for foreclosed land to be disposed of fairly easily*" (Atwood, 1990, p. 664). Land must be easily transferred to a person who wants to use it and is prepared to pay a price that is sufficient to cover the outstanding debt. In short, "*if foreclosure is impossible, land loses its attractiveness as collateral*" (Binswanger & Van den Brink, 2005, p. 280).

Currently, Namibia's commercial financial institutions are not accepting registered leaseholds over state land as collateral, as they are not allowed to sell leaseholds in the event of a borrower defaulting.

3.1 Bankability and asset poverty

Making registered leaseholds legally tradable will not be sufficient to obtain credit from financial institutions. First and foremost, an applicant for a loan must be credit worthy and able to service a loan (Bruce, 1986, p. 40). For commercial banks in Namibia, the ability to repay a loan was more important than the form of collateral. None of them entertained security lending (i.e. granting a loan purely on collateral). Agribank also requires applicants for loans from the Post Settlement Support Fund (a dedicated credit facility for resettlement farmers) to complete an 8-page application form including a statement on assets and liabilities and income and expenditure to assess their ability to service a loan (Joint Technical Committee on Post Settlement Support for Resettled Farmers, n.d.a.).

Similar criteria are followed by all financial institutions. The criteria are aimed at reducing the lending risk by ascertaining the overall sustainability of the enterprise for which the loan is intended. Typically, a business plan is required to ensure that the applicant has sufficient financial resources and cash flow to keep his/her enterprise afloat and is able to pay the loan. This requires that, inter alia, beneficiaries have been allocated farm sizes that can be farmed in a financially sustainable manner. The Permanent Technical Team on Land Reform (PTT) (2005b, p. 22) has pointed out that

“there is a cut-off point below which a piece of land cannot be farmed on an economically viable basis”, i.e. where the realistic revenues derived from farming are too small to cover living expenses as well as running and maintenance costs.

Asset poverty is a major impediment to obtaining loans. Several informants stated that they were unable to get loans because they were unable to make repayments due to a shortage of cash (see also Werner & Odendaal, 2010, p. 108 and Ministry of Lands and Resettlement, 2010, p. 37). Cash-flow problems are common among small-scale farmers. For many households the only reliable income streams are monthly pensions and/or remittances from relatives working in towns.

To the extent that these observations are correct, the major impediment to investments on farms is not primarily a tenure or collateral issue, but rather asset poverty. This demands innovative finance instruments to enable asset-poor farmers to obtain loans. Collateral-free loans offered by Agribank go some way to providing access to loans without applicants providing collateral, but this service is likely to support only those farmers who are able to service loans, while those without the abilities to do so remain without access to financial services. The question that has to be answered before considering financial instruments to support asset-poor farmers is whether farmers with insufficient revenue streams to service loans can be sustainably supported.

3.2 Derived rights

In order for leased land to become acceptable as collateral to banks, it must be clear who the registered lessor of the land is. On a formal legal level, this is guaranteed by registering a lease agreement in the Deeds Office. It is not uncommon, however, that the situation on the ground is at variance with the registered right. Frequently, people other than the registered lessee obtain secondary or derived rights to the leased land, a common example being members of the lessee's extended family. The obligation specified in the conditions of lease that beneficiaries have to share water infrastructure if they do not have their own (Ministry of Lands and Resettlement, 2004, p. 5). is also likely to be a cause of concern to financial institutions, since a farmer without water obtains certain rights to resources on another lessee's parcel.

A situation without clear owners who are able to take decisions increases uncertainty costs. For example, it is not uncommon that disputes between a lessee with a water point and a neighbouring beneficiary arise over the use and maintenance of the water point. Such disputes can be amplified when a financial institution seeks to attach the land for resale. This may be a deterrent for a bank that needs to sell the land as swiftly as possible, without having to solve disputes first. Banks may also find it more difficult to find a buyer if the buyer has to share resources with somebody else.

In addition, registered leaseholds do not guarantee that land rights will not be transferred in informal ways which are not captured in land registries. Ways of accessing registered land may include inheritance, loans or rights of usufruct enjoyed by kin. Foreclosure may become difficult where the presence of family members (kin) on mortgaged land makes it politically unfeasible to auction such land. Even where land is auctioned, if the buyers are not kin of the previous owner, fear of reprisals may prevent their taking possession, and *“Governments may not want to oppose such demonstrations lest it should threaten their political basis or the fragile consensus on which their national policies rest”* (Platteau, 1996, pp. 60-61). In Kenya it was observed that government was loathe to evict people from land for which they had fought, due to fear of risking *“the wrath of the true believers in the nationalist struggle”* (ibid., citing Bates, 1989, p. 74). The conclusion is that *“the costs entailed in realising land assets are ... likely to discourage bankers, who usually prefer lending against more reliable streams of income than those found in agriculture”* (Platteau, 2000, p. 62).

3.3 Land market

Collateral in the form of leased land does not have economic value unless the rights can be traded. Atwood (1990, p. 664) has argued that *“collateral itself may only be valuable where there is an active land market which permits easy land transfers”*. Therefore, the development of a land market

in the small-scale farming sector – in both resettlement and non-freehold areas – is a necessary condition for lessees of state land to use their land as collateral.

For understandable reasons, the Namibian Government has been loathe to permit and encourage the development of a land market in both the freehold and non-freehold sectors. There is a political concern that the trading of lease agreements would defeat the objectives of the National Resettlement Programme, and would place leaseholders in communal areas at risk of losing their land. Appropriate regulations governing a land market in the small-scale farming sector will go a long way to reducing such risks and concerns.

A land market is also likely to have other positive impacts on resettlement.

To start with, a land market would make the small-scale farming sector more productive as the current resettlement model would become more flexible. A land market provides a mechanism for small-scale farmers who are no longer able to use their land optimally to legally sub-lease their land. By the same token, stronger farmers who are presently restricted to one farming unit without the option to legally lease in land would be able to do so, and hence expand their businesses. Allowing a land rental market to develop will *“facilitate easy reallocation of land toward more efficient users than current owners, especially if current owners are old, are non-cultivating heirs, are urban beneficiaries of restitutions and so on”* (Deininger, 2003, p. 85).

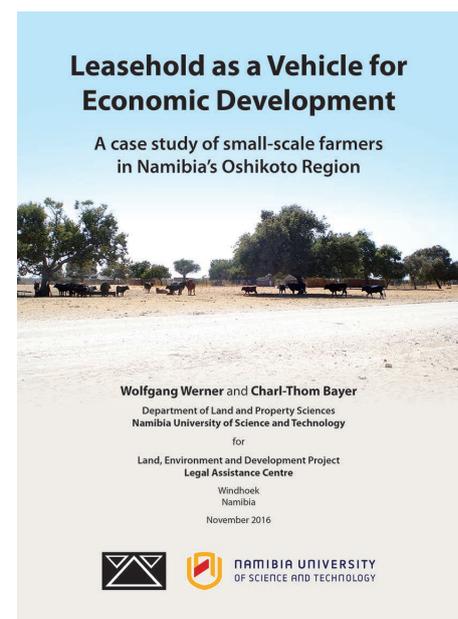
Legalising a land rental market that is growing despite its illegality would also provide legal protection for those sub-leasing land. The illegality of this practice of sub-leasing has resulted in poorer farmers being exploited by richer farmers in terms of rentals, as the Permanent Technical Team on Land Reform documented in 2005 (PTT, 2005b, pp. 52, 69). More recently, the Auditor-General confirmed this trend in his land reform and resettlement audit report for the years 2010-2013. Out of 182 farms visited, his office found that 68% were being sub-leased. The reason cited for this practice was that beneficiaries were unable to maintain their farms (Immanuel, 2015).

Finally, a land rental market would also make it possible for new beneficiaries to benefit from resettlement without having to apply to the Ministry of Land Reform for resettlement. Accessing land through a land rental market has the advantage of requiring *“only a limited capital outlay, thereby leaving some liquidity available for productive investments rather than locking it all up in land”* (Deininger, 2003, p. 85). The number of people interested in sub-leasing resettlement land is not known. The extent of public dissatisfaction with the slow pace of land redistribution indicates that the demand for resettlement land far exceeds the supply.

4. The way forward

Small-scale farmers in both the freehold and non-freehold areas in Namibia need to be provided with access to occasional credit. Preliminary findings presented in this Policy Brief suggest that many asset-poor farmers are unlikely to obtain loans due to their inability to make regular repayments. Registered leaseholds on their own, while important for formalising tenure rights, are not sufficient to provide access to credit and investments unless innovative financial instruments are developed to support them.

For registered leaseholds to serve as collateral, a legal land market must be allowed to develop, and should be regulated to ensure that the underlying equity concerns of the land reform programme are not compromised. Apart from making it possible to use registered leased land as collateral, a land market will provide flexibility to the current resettlement model, which is likely to have a positive impact on productivity in the resettlement sub-sector.



Full report available at www.lac.org.na

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