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THE EFFECTS OF PROPERTY TITLING IN LANGA TOWNSHIP, SOUTH AFRICA

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Enterprise Africa! is a research project that investigates, analyzes, and reports on enterprise-based solutions to poverty in Africa. The project is uncovering some of the hidden success stories in Africa – stories of people and policies that make a difference in the lives of Africa’s people today. In essence, it documents African solutions to Africa’s problems. These success stories involve intrepid, committed entrepreneurs across the continent, who are developing an amazing array of businesses – from the smallest-scale shops to multinational corporations – and the institutions that support them. These entrepreneurs are promoting economic growth and are an unheralded key to poverty alleviation. *Enterprise Africa!* is a joint initiative with the *Free Market Foundation of Southern Africa* and the *Institute of Economic Affairs* of London, England, and is supported by a generous grant from the *John Templeton Foundation*.

For more information about the *Enterprise Africa!* project visit us online at <www.mercatus.org/enterpriseafrica> or contact Karol Boudreaux at (703) 993-4941 or kboudrea@gmu.edu

Cover photo: Susan Anderson—Artisans at work on a house in Langa. All photos are property of the Mercatus Center.

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SOUTH AFRICA

KAROL BOUDREAUX

EXECUTIVE SUMMARY

Do titling programs hold the key to security of property rights for the developing world? South Africa offers an instructive case in point. Successive South African governments have worked to provide legal title to previously disenfranchised citizens. In Langa Township, one of South Africa's oldest townships, titling efforts have been underway for well over a decade. Today, most homes—though not shacks—have titles. Can this policy serve as an example for others to follow? Has this government policy led to economic growth and poverty alleviation for Langa's residents?

The answer is a qualified yes. By creating secure property rights in houses, the South African government has created incentives for owners to improve their homes and to use them for home-based businesses, thus creating jobs and income in poor communities. However, more needs to be done. Few Langa residents use their titles as collateral for commercial loans, still preferring to rely on personal savings and savings clubs.

Titling is not enough. Institutional weaknesses make the use of title as collateral too risky for many Langa residents. The formal transfer of property is too expensive, and regulatory burdens make it costly to grow and expand small businesses.

Formal titling is a step in the right direction toward realizing the benefits of property rights for development. But policymakers need to take the next step in property reform to realize the potential in increased economic growth and poverty alleviation. They can do this by focusing on reducing transaction costs for property transfers, such as removing the conveyancing monopoly in South Africa. The government should also reduce regulatory burdens that make it difficult to grow a business and move into the formal sector. Reforms such as these would make real property transfers more secure and enable even more of the benefits that entails.

ENTERPRISE AFRICA! RESEARCH APPROACH

LOCAL SOLUTIONS FROM LOCAL KNOWLEDGE

This study, as with all the studies conducted by the *Enterprise Africa!* research team is based largely on information gathered in Africa from Africans. Our core research team was comprised of the Mercatus Center's Karol Boudreaux and Susan Anderson, and South African-based Free Market Foundation's Eustace Davie, Temba Nolutshungu, and Jasson Urbach. The unique approach of the *Enterprise Africa!* team helps ensure that our studies reflect what's actually happening in the communities in which we work, rather than an outside view of how things might be.



The Team in Langa

For *The effects of property titling in Langa Township* research team members from FMF drew from their many years of experience with land titling and property reform in South Africa. Their familiarity with Langa Township, where Temba Nolutshungu was raised, and relationships with residents of Langa and surrounding townships afforded invaluable access to the history and personal experience of community members, which inform the resulting study. In addition to the local information, the team incorporated insights from the existing literature on property reforms in South Africa and other countries and communities. The team also arranged conversations with lawmakers and government officials charged with implementing property reforms in South Africa.

With the groundwork for a productive stint of field work laid, Mercatus Center researchers joined fellow team members in South Africa to speak with several dozens of business owners and residents in Langa and surrounding townships as well as officials in relevant government posts.

With the groundwork for a productive stint of field work laid, Mercatus Center researchers joined fellow team members in South Africa to speak with several dozens of business owners and residents in Langa and surrounding townships as well as officials in relevant government posts.

This local information was then cross-referenced with literature and other relevant data. The picture that emerged was captured and peer-reviewed by colleagues in South Africa and the United States. The goal of our study is to provide a unique view of how the institutional environment created by local policy enables or inhibits productive enterprise-based solutions to poverty, and ultimately affects the well being of members of the community in question. Our unique approach to this research, which relies substantially on local experience and knowledge, helps to ensure that the picture we paint is tied to the world it intends to depict.



Marcelle and Jasson

THE EFFECTS OF PROPERTY TITLING IN LANGA TOWNSHIP, SOUTH AFRICA*

INTRODUCTION

Stretched out behind the gray towers of Athlone power plant lies the black township of Langa. It is one of the oldest townships in Cape Town, the product of a long history of racial separation, segregation, and oppression.

Within the borders of Langa an interesting experiment has taken place over the past twenty-five years. Beginning in the late 1970s, the government of South Africa attempted to provide residents with increased tenure security in their homes. The first steps involved issuing long-term leases to occupants. In 1986, the government introduced legislation to allow black urban dwellers, such as the residents of Langa, to purchase freehold title to their homes.¹ The post-apartheid ANC government transferred significant numbers of titles to occupants.

Today, many of the non-squatter houses in Langa are under freehold title. The decision to promote homeownership was taken deliberately by both the apartheid-era National Party government (in its waning days) and by the ANC government. The policy of transferring title to occupants was a direct attempt to promote economic growth and poverty alleviation by giving occupants a greater stake in society—as homeowners. Government policy makers believed that once occupants had secure title to their houses, they would leverage this asset in economically creative ways and begin to pull themselves and their families out of poverty.

Although this policy was implemented before the publication of Hernando de Soto’s work on the role titling plays in promoting economic growth, it reflects a similar logic.² In *The Mystery of Capital*, de Soto argues that informal property rights³ are a drag on economic development. He

* We wish to thank the many homeowners, business owners, and public officials who took the time to speak with us and share their stories. Their input was invaluable.

¹ “Freehold” title is the right of title to land for an uncertain duration. In 2001, there were 3,172 formal, residential properties in Langa (i.e., homes, not shacks or commercial property). Of these, 780 were unregistered, and 30 were owned by banks. Personal communication from Mr. Jens Kuhn, Research Manager: Housing—City of Cape Town, October 13, 2005.

² Hernando de Soto, 2000, *The Mystery of Capital*, New York: Basic Books.

³ Informal property rights are those limited rights individuals hold who own or occupy a particular place or thing. In de Soto’s work, someone has an informal right to property if they lack a formal, *de jure* title to the thing or place. Lack of title means the informal owner cannot use the property as collateral for a commercial loan.

says that informal rights represent “dead capital.” People who possess dead capital cannot use it to secure the financing necessary to build or support a business, to invest in education, or to pursue other ventures.

What the developing world needs to do, de Soto argues, is to turn the huge amount of dead capital found there into living, useful capital—primarily via titling. This has been a strategic goal of the South African government for many years. While many have hailed de Soto’s thesis—informal property represents dead capital that can be brought to life via titling and formalization—as an important key to economic development, this study suggests that it is not a panacea. Instead, we argue that the South African government’s policy of providing secure title to housing for many citizens is a necessary but not sufficient condition for economic growth.

THE PURPOSE OF THIS STUDY

The purpose of this study is to trace the effects of the South African government’s policy of transferring freehold title from the public sector to township residents in Langa, outside Cape Town. We also look for lessons that the Langa experience offers to policymakers elsewhere who, in response to the great interest raised by de Soto’s work, are adopting titling policies in order to promote economic growth and alleviate poverty.

For approximately 10 years, the ANC government’s housing policy has promoted freehold title

as a means of more effectively alleviating poverty among its citizens. Between the late 1970s and the mid-1980s, black South Africans only had access to long-term property leases. Starting in the mid-1980s, the government passed legislation allowing them to acquire freehold title from the government. For the past 30 years, South African governments have been attempting to provide greater tenure security to urban dwelling black citizens.

This study investigates whether the residents of Langa Township are experiencing the benefits that increased tenure security was expected to deliver. Recent studies have identified problems that exist in the real estate markets in South African townships (Finmark Trust, 2005). These studies were based on survey data that may not fully capture the on-the-ground experiences of residents of Langa. This study fills a gap in research on the effects of titling by focusing on one specific township and by relying on qualitative data gathered during visits to the township in October 2005.

This study highlights the ways that some Langa residents have expended resources improving their homes, providing work for artisans, supporting home-supply stores and their employees, and creating wealth in the process. Still other residents have used their homes as a secure location for a business. Incremental house improvement and business development are the norm. At this time, there appears to be very little use of titles as collateral for commercial loans. However, this

result mirrors the U.S. experience, where the majority of start-up capital for small businesses comes from personal savings, not from commercial loans.

Having a secure title to property does create incentives to improve property. And, secure title does provide some homeowners with space for business activities—renting shacks in backyards, opening restaurants, or starting a welding business, for example. However, this study suggests that it is unrealistic to assume that homeowners in the developing world will immediately use their titles as collateral for commercial loans that, in turn, promote economic growth. Institutional weaknesses and constraints make this strategy too risky for many informally employed homeowners. It is more likely, we suggest, that township homeowners and business owners will turn to commercial lending after establishing credit histories—as is happening now with Mzansi accounts—or if they have appropriate incentives to expand and grow businesses.⁴ Titles are likely to prove valuable as collateral for commercial loans as long as the institutional environment in South Africa is conducive to the formation and expansion of formal businesses. To the extent, however, that the

institutional environment encourages informality (by making the costs of operating as a formal business quite high) as it does now, we would expect that homeowners would continue to use titles as collateral only rarely.

This suggests that South African policy makers, and other policy makers involved with titling programs, should focus on creating an institutional environment that provides people with secure, divisible property rights that allow them to use their property in creative ways, to save, and to grow their small businesses. People with secure property rights have incentives to invest, albeit incrementally, to act entrepreneurially, and to start businesses. This smaller-scale economic growth is essential in developing nations. However, to grow businesses requires an institutional environment in which labor markets are relatively free, people are free to enter into contracts, and the rule of law is enforced.

We conclude that the official policy of transferring title to Langa residents has helped to promote some economic activity and alleviate poverty to a degree, but that further institutional changes need to take place for the policy to have a broader and deeper impact.

⁴ A Mzansi account is a small-sized, low-fee bank savings account open to the informally employed and offered by a group of major South African banks in conjunction with the South African post office. By some estimates, over 1.5 million such accounts were opened between October 2004 and August 2005. See “Mzansi: SA banking spreads its net,” *South Africa.Info*, September 8, 2005, available at: <http://www.southafrica.info/public_services/citizens/consumer_services/mzansi.htm>.

A. THE ROLE OF PROPERTY RIGHTS IN ECONOMIC DEVELOPMENT

Successive South African governments have tried to alleviate poverty for many of the nations' citizens by providing them with secure title to real property. Discussions of the role secure property rights play in promoting economic development are relatively new in the development literature.⁵ However, the insight that people who have secure rights over a resource tend to invest in and conserve it is longstanding.

The connection between property rights and economic development can be summarized in the following manner:

- property rights provide individuals with incentives to maintain and improve property;
- property rights enable individuals to allocate scarce resources; and
- property rights promote human flourishing and empowerment.⁶

Property rights create positive incentives for people to maintain and improve their property.⁷ These incentives exist because people who are free to trade their property with others are more likely to be rewarded for these efforts than are people who neglect property. In addition, people who feel secure that others will not expropriate their property will invest more in that property than will people with insecure rights.

Of primary importance to economic outcomes are the *economic institutions* in society such as the structure of property rights and the presence and perfection of markets. Economic institutions are important because they influence the structure of economic incentives in society. Without property rights, individuals will not have the incentive to invest in physical or human capital or adopt more efficient technologies... Societies with economic institutions that facilitate and encourage factor accumulation, innovation, and the efficient allocation of resources will prosper.⁸

⁵ For example, the World Bank's *World Development Report 2005*, lists property rights as one of the basic requirements for a healthy investment climate and for economic growth. Available at: <http://siteresources.worldbank.org/INTWDR2005/Resources/complete_report.pdf>.

⁶ See Karol Boudreaux, 2005, "The Role of Property Rights as an Institution: Implications for Development Policy," *Mercatus Policy Series*, Policy Primer No. 2, available at: <<http://www.mercatus.org/pdf/materials/1160.pdf>>.

⁷ There is increasing evidence that people tend to invest more when their property rights are more secure. See Klaus Deininger, 2003, *Land Policies for Growth and Poverty Reduction*, Oxford University Press and the International Bank for Reconstruction and Development/World Bank: New York, Washington, D.C.

⁸ Daron Acemolgu, James Robinson and Simon Johnson, 2004, "Institutions as the Fundamental Cause of Long-Run Growth," *NBER Working Paper No. 10481*, available at: <<http://papers.nber.org/papers/w10481.pdf>>.

For these reasons, people will spend money and exert effort to maintain and improve the house they own, but they will tend *not* to spend money or exert the same amount of effort to maintain a house they rent. House owners directly benefit from their efforts if and when they choose to sell the house. A well-maintained house would command a higher price than a house with a leaking roof or broken furnace. Because they do not own the house, renters would not benefit directly by taking good care of it and so have fewer incentives to spend time and resources maintaining it.

Property rights help to allocate scarce resources because they provide the basis for trade and for markets. When people have strong ownership rights in resources, tangible and intangible, including their labor, they are empowered to decide how to use and allocate these resources. When these rights exist in an institutional environment that supports freedom of contract and a rule of law, people have incentives to transfer resources voluntarily to people who value them most highly. Because people can gain from such trades, they will be alert to use

resources in ways that others value. This alertness is the basis of entrepreneurial behavior. Entrepreneurship and trade flourish in economically free societies, and they provide much of the basis for economic growth.⁹

Secure property rights also empower those who hold them. When individuals hold secure rights to property, they—not some centralized authority—make decisions about how to use and allocate this property. Property rights serve the vital function of decentralizing power, economic and political power, and creating autonomous space for individuals. When people have greater scope to make decisions about how to use their resources, when they are less subject to the oppressive acts of others, they have greater scope to pursue their unique dreams creatively.¹⁰ In this way, property rights promote human flourishing.

Formal titles to property are one avenue to provide increased tenure security. A formal title provides *de jure* recognition by a government that the title holder has a very thick bundle of rights in the property that is identified on the title.

⁹ See James Gwartney and Robert Lawson, *Economic Freedom of the World 2005 Annual Report*, The Fraser Institute and Cato Institute, available at: <<http://freetheworld.com>>, and Mark Miles, Kim Holmes, Mary Anastasia O'Grady, Ana Isabel Eiras, and Anthony B. Kim, *The Heritage/Wall Street Journal 2006 Index of Economic Freedom*, available at: <<http://heritage.org/research/features/index/>>. See also, Israel M. Kirzner and Frederic E. Sautet, "The Role of Entrepreneurship in Markets: Implications for Policy," *Mercatus Policy Series*, Policy Primer (forthcoming, 2006).

¹⁰ For a recent example of how a lack of strong property rights can lead to abuse, see, Jim Yardley, "China Unveils Plan to Aid Farmers, But Avoids Land Issue," *New York Times*, February 23, 2006, which discusses how Chinese government officials misuse their powers and appropriate land held under leases by Chinese farmers. The article notes that if the farmers, not the government, had ownership rights to the land, the farmers would benefit from sales to real estate developers—not the officials, as is currently the case.

Such a thick bundle of rights may include the right to occupy, sell, bequeath, modify, retain profits from the use of, lease, and/or mortgage the property. When people hold thick bundles of divisible property rights, their property is likely to be more valuable to them because they have greater control over how the property is, or is not, used. And because their bundle of rights is thick, the effort they take to care for the property is directly tied to future reward. They reap any profits that come from using, leasing, or selling the property.

The effort to provide a formal, *de jure* title to a piece of informally held property would involve registering that property. The formal registration of property typically requires that property be carefully described and that any legal encumbrances, such as easements, covenants, or liens that apply to the property be noted. At the time of transfer a survey of the property may need to be filed with the appropriate government office, along with a formal contract known as a title deed. Formal registration of a title deed can be an expensive and cumbersome process. However, assuming the government office that maintains property records is efficient; it provides a great deal of security to future buyers and sellers. Titling also provides predictability—a buyer can more accurately predict what will happen if someone challenges her right to possess or use property if the titling and registration process is dependable.

If, however, the registration process is too costly, some buyers and sellers will avoid it and will transfer property informally. If the use of informal transfers continues to increase, the benefits of costly titling efforts will largely be lost. An undependable, out-of-date deeds register fails to capture the on-the-ground reality of the property environment. For this reason, to a significant extent such a register is useless. The benefits that are supposed to flow from title holding dissipate when transfers take place informally. When property is transferred informally, buyers have less security and less predictability than they would if the transfer was completed following the formal process. And, with a less secure title, it may be more difficult to lease, sell, mortgage, or otherwise use the property in the future.

Still, titling has been seen as one way to provide title holders with incentives to invest in, make profitable use of, and eventually trade their property. Policies that transfer formal title from government entities to private actors are expected to promote economic growth and alleviate poverty. This is the reasoning behind the South African government's policy of providing title to the occupants of the new housing it constructs and transferring title to older housing stock. Because Langa is an old township, this study concentrates on the effects of transferring title over old housing stock from the government (in this case, the City of Cape Town) to the people occupying this housing.

B. CREATING ROOM FOR IMPROVEMENT VIA ENTREPRENEURIAL POLICIES

INSTITUTIONAL BACKGROUND

In 1917, there was no Langa.¹¹ The township, which lies to the south of central Cape Town, sits upon land that used to be open fields. It wasn't until the great influenza epidemic of 1918 that authorities in Cape Town decided to move some of the city's black Africans.

Unlike white South Africans, black residents of Langa were prohibited from buying land. The Cape Town City Council was the owner of the land and the buildings in Langa. This was the result of the Native Lands Act of 1913, which barred black Africans from purchasing or leasing land from non-Africans outside specially designed native reserves.¹²

If you visit Langa today, you will still see the block flats of an earlier era: single-sex, dormitory-style housing called hostels that were provided by the Cape Town City Council for migrant workers. Because the South African government adopted a policy of separating the families of black African migrant workers, allowing only the

men to travel to search for work in urban areas, Langa contained relatively few houses designed for families.

In 1945, the government passed the Native (Urban Areas) Consolidation Act, which provided the basis for highly restrictive labor and movement regulations imposed under the apartheid government. Despite these onerous restrictions on movement, black Africans continued to move to the cities, and by 1946 South African towns contained more blacks than whites. In the decades that followed, the trend continued.

This meant more and more people, primarily men, left the Homelands to look for work in towns and cities.¹³ Between the years 1951 and 1980, the population in black townships increased from 5.6 million to over 10 million people, most of whom were living in squatter housing that often lacked access to water, electricity, and sewage services or in “backyard” housing, tiny shacks behind the homes of relatives.¹⁴ In 1954, the Minister of Native Affairs announced that no more family houses would be built in Langa; instead the focus would shift to hostels. By 1960 there were 25,000 people living in Langa; 18,500 of whom were living in the hostels.¹⁵

¹¹ In the Xhosa language Langa means “sun,” but it is also the first portion of the name of Hlubi chief, Langalibalele, who rebelled against colonial forces. After incarceration on Robben Island, Chief Langalibalele was banished to the government farm Uitvlugt, part of which subsequently became Langa Township. Some say that the original residents of Langa really named the township in honor of this chief who stood up to the colonial powers.

¹² Natives' Land Act of 1913.

¹³ The Homelands were rural areas set aside by the apartheid government for black South Africans to live.

¹⁴ See Leonard Thompson, 2001, *A History of South Africa*, Yale University Press: New Haven, 242.

¹⁵ The population of Langa was 7,436 in 1941; today, it is approximately 200,000. See footnote 26 below.



Langa hostel

The 1971 Bantu Affairs Administration Act¹⁶ shifted the control over housing policy from municipalities to the national government. The national government proceeded to limit the availability of housing loans to municipalities for building black housing in urban areas—a strategy that contributed to the further deterioration of conditions in the townships. A key result of all these policies was the creation of a massive housing shortage for low-income South Africans—a problem that persists to this day.

In an attempt to undo some of the ill consequences of previous policies, in 1978 the government introduced the option of a 99-year lease for black South Africans. In 1984, the Black

Communities Development Act created a statutory right to these leases that could, beginning in 1986, be registered.¹⁷ Royston notes:

[F]ull freehold ownership rights for black urban dwellers were created by the Act in 1986 for the first time. Previous forms of tenure could be converted into ownership... As a result of demands made by civic associations, a process of privatizing state rental stock at no charge to occupants began in earnest, called the ‘transfer of houses’ process.¹⁸

The new homeownership policy was heavily promoted by the Urban Foundation, a non-profit organization with strong ties to the business com-

¹⁶ Bantu Affairs Administration Act 45 of 1971.

¹⁷ Lauren Royston, 2002, “Security of Urban Tenure in South Africa: Overview of Policy and Practice,” in *Holding Their Ground: Secure Land Tenure for Urban Poor in Developing Countries*, Earthscan Publications: Sterling, VA, p. 167.

¹⁸ See Royston, 2002, p. 167, *op.cit.*

munity, in conjunction with the Association of Building Societies, which clearly had an interest in providing more housing to the nations' black citizens. Some private funding was provided to support this effort. These actions resulted in an expansion of private-sector housing and township development.

At the same time, however, the government increased rental fees for government-provided housing, leading to widespread protests. Many renters either refused to pay the increase or stopped paying during boycotts. In addition, a rise in interest rates in the 1980s made it difficult for some new mortgage bond holders to meet their commitments. The rate of default increased, and the banking industry began to grow shy of lending in the townships.¹⁹

With problems mounting (after restrictions on movement known as influx controls were lifted in

1986 squatter settlements near cities mushroomed), the government attempted to accelerate homeownership through a "site and service" effort. Site and service meant the government allocated public lands to create privately developed, individually owned plots.²⁰ The government provided subsidies (7,500 rand, the equivalent of \$2,600 at 1990 exchange rates)²¹ to private developers to develop the land. These developers would sell the "improved" property and transfer title.

A host of problems followed, including scandals over poor-quality construction. Recognizing that something more effective was needed, that housing policy was complex, and that central, provincial, and municipal agencies often had overlapping or contradictory authority,²² the National Housing Forum was created in 1992 with the goal of developing a coherent, non-redundant, effective housing policy.²³ The Forum's work led to the National Housing Accord (1994), which was

¹⁹ Estimates from 2002 suggest that of "300,000 recorded housing-related bank loans extended to township residents in the last decade, nearly one-sixth (or 50,000) are non-performing." See Patrick Meagher and Betty Wilkinson, 2002, "Filling the Gap in South Africa's Small and Micro Credit Market: An Analysis of Major Policy, Legal, and Regulatory Issues," The IRIS Discussion Papers on Institutions & Development, Paper No. 02/11, available at: <http://www.iris.umd.edu/Reader.aspx?TYPE=FORMAL_PUBLICATION&ID=62c8b28f-63ff-461d-81f0-dd4d72daefb5>.

²⁰ The site was the small plot; the service was typically a toilet hook-up, thus, "site and service." The government did not provide a structure on these plots.

²¹ See Peter Wilkinson, 1998, "Housing Policy in South Africa," *Habitat International*, Vol. 22, No. 3, 215-223 and 229. Please note that in all other cases rand was converted at the rate of 6.6 rand/dollar, the prevailing rate in late 2005.

²² See Alan Gilbert, 2002, "'Scan Globally, Reinvent Locally': Reflecting on the Origins of South Africa's Capital Housing Subsidy Policy," *Urban Studies*, Vol. 39, No. 10, 1916.

²³ The proposals adopted by the Housing Forum reflect the influence of South African mathematician Dr. George Ellis, a critic of the apartheid government and its housing policy. He co-authored two key works on the subject: *The Squatter Problem in the Western Cape* and *Low Income Housing Policy in South Africa*.

signed by many stakeholders in South African society and largely adopted by the new Unity government following the historic elections of 1994.

THE ANC GOVERNMENT AND ITS NEW HOUSING POLICY

The ANC-led Government of National Unity that took office in 1994 faced extraordinary problems. Among these were a serious housing shortage, poor quality housing stock, housing located far from jobs and economic opportunity, serious unemployment, and widespread problems of poverty. The new government designed its housing policy, at least in part, to address each of these concerns.

The Housing White Paper of 1994, later adopted into law as the Housing Act of 1997,²⁴ outlines the government's plans for fixing the nation's many housing problems. In terms of the housing shortage, the government committed to providing a million permanent housing units by 1999. It has accomplished this goal (somewhat belatedly) through the provision of RDP houses—small concrete block homes that can be purchased using a government-issued subsidy.²⁵

The capital subsidy program has been a major pillar of post-apartheid housing policy. The subsidy program provides a one-time lump sum payment designed to make housing more affordable for low-income earners. The idea behind the subsidy is this: commercial banks do not lend to these

low-income earners, so the government should step in and provide financing to allow people who fall into particular income categories to purchase a house of their own. The subsidy is set at a rate that should allow people to acquire a plot of land, a basic structure, and basic services. Subsidy recipients are expected to improve, or “top up”, the house after they take up residence.

The White Paper/Housing Act committed the government to a number of other policy goals:

- the development of “sustainable” environments and “viable” households and communities;
- the development of a “normalized” housing market;
- improved access to credit for low-income residents and an improved public-sector/private-sector partnership to provide housing; and
- upgrading efforts, in order to address the problem of poor quality housing stock, among other goals.

Most of these goals have proved difficult to accomplish. While well over a million RDP houses have been built, they do not seem to be working well as “starter” homes that people improve over time.

²⁴ Housing Act 107 of 1997.

²⁵ To date, the government has provided well over 1.5 million homes.

Instead, they are considered undesirable by many, who either sell or abandon the homes and relocate to informal squatter communities.²⁶ Further, there remains a substantial housing backlog. The housing market in townships is problematic, and many low-income residents continue to face difficulties accessing formal, commercial credit.²⁷ Criticism of the government's housing policy has been intense and has, in some cases, turned violent as frustrations mount among South Africa's poor.²⁸

CURRENT HOUSING ISSUES IN LANGA

As noted, Langa is an old, established township with relatively little undeveloped land. This means that the key housing issues the government must grapple with in Langa are:

- ensuring the effective transfer of titles for formal residences from the hands of government to the residents;
- upgrading squatter settlements within

Langa; and

- effectively managing hostel housing.

Of these three prongs, the first, the transfer of title to formal residences, has largely been accomplished.²⁹ Despite it being a slow process, lasting through most of the 1990s, Langa did have some advantages in terms of managing deed transfers. For example, Langa has a housing office, the Langa Housing Office, which traditionally dealt with issues surrounding rental housing (the primary tenure type until the early 1980s). The office handled deed transfers (not the actual registration of deeds, which is managed by a national Registry) and had a good idea of “*bona fide*” owners.³⁰ Additionally, Langa is relatively small, especially as compared with the newer townships like Khayelitsha, and this may have helped facilitate the process.³¹

In 2000, a municipal valuation was completed for

²⁶ The RDP houses are typically 25 sq. meter homes without any internal partitions. Their small size, coupled with minimal amenities, makes them undesirable. The homes are often built in dispersed areas, and people who move into the houses tend to lose access to the deep social networks that exist in informal shack communities. See “State puzzles over how to retain RDP homes for social housing,” *Cape Argus*, August 29, 2005.

²⁷ Ambrose A. Adebayo & Pauline W. Adebayo, 2000, “Sustainable Housing Policy and Practice—Reducing Constraints and Expanding Horizons Within Housing Delivery,” *Proceedings: Strategies for a Sustainable Built Environment*, available at: <<http://www.sustainablesettlement.co.za/event/SSBE/Proceedings/adebayo.pdf>>.

²⁸ For example, see “AHI—South Africa: Why are they rioting?” *Affordable Housing Institute Blog*, June 1, 2005, available at: <http://www.affordablehousinginstitute.org/blogs/za/2005/06/why_are_they_ri.html>; and, “The Winter of Discontent,” SABCNews Special Assignment, June 28, 2005, available at: <<http://www.sabcnews.com/specialassignment/20050628script.html>>.

²⁹ See footnote 1 above.

³⁰ Personal communication from Mr. Jens Kuhn, Research Manager: Housing, Cape Town Housing, January 10, 2006.

³¹ While Khayelitsha has over a million residents, Langa may have closer to 200,000. Interview with Mr. Anthony van Wyck, October 4, 2005, Cape Town, South Africa.

Langa. This valuation showed the “bulk of transfers were complete and owners known.”³² This does not mean, however, that subsequent sales, particularly informal sales, have been properly registered with the national Deeds Registry. In fact, there is good cause to suspect that informal sales are not being properly registered, a point to which we return below. However, it is reasonable to say that in a procedural sense the titling program has largely been a success in Langa.

If titling has been a success in procedural terms in Langa, has it led to the kind of economic activity and poverty alleviation one might expect? In the following section we identify some of the beneficial effects of the government’s titling program for Langa’s residents.

C. TENURE SECURITY AND POVERTY ALLEVIATION

Secure tenure in the form of title to a house provides a critical asset for the poor. As noted above, homeowners have a different set of incentives than do people who are renting housing. Among these are incentives to invest in one’s home and to use it profitably if one can expect to reap the benefits of profitable use. Renters typically have a wider set of

Housing is a critical element in the survival strategy of the poor, providing them with socio-economic stability as well as a source of asset creation and savings. Moreover, in urban areas, housing is an important productive asset that can cushion households against severe poverty, providing an access point to the urban economy, particularly through the establishment of home-based enterprises.³³

restrictions on how they may use property than do homeowners. One potentially profitable way to use one’s home is to develop a home-based business.

In Langa, as in many townships, people often run businesses out of their homes. There is little in the way of commercial real estate in Langa, though there is a commercial strip that is owned and leased by the local government. And, there are few restrictions governing the use of residential property for commercial purposes—giving Langa residents a high degree of freedom in terms of how best to use their house. A recent report suggests that just over 85% of South Africa’s self-employed, many of whom work in the informal sector, work from their homes.³⁴ Using one’s

³² Personal communication from Mr. Jens Kuhn, Research Manager: Housing—City of Cape Town, January 10, 2006.

³³ C.M. Rogerson, 1999, “Local Economic Development and Urban Poverty Alleviation: The Experience of Post-Apartheid South Africa,” *Habitat International* Vol. 23, No. 4, 515.

³⁴ Paul Cichello, 2005, “Hindrances to Self-Employment Activity: Evidence from the 2000 Khayelitsha/Mitchell’s Plain Survey,” *CSSR Working Paper* No. 131, Centre for Social Science Research, University of Cape Town, available at: <http://www.sarpn.org.za/documents/d0001752/CSSR_self-employment_Oct2005.pdf>.



Marcelle and Jasson In front of Lelapa restaurant in Langa

home as a place for commercial activity is a common strategy for dealing with high unemployment—people who cannot find jobs in the formal sector by necessity create their own work, often-times in their homes.³⁵

When people are secure in their ability to remain in their home and are able to make appropriate modifications or additions to the house, they will be more likely to invest in a home-based business. This option may be preferable to renting space from the local government and dealing with government officials, who have a reputation for inefficiency and corruption. If an area has little com-

mercial real estate available, one's home also becomes more attractive as a business location. And, by using one's home, the business owner avoids the problem of paying rent, which can at times be difficult if one is self-employed.

Whether that business is a spaza shop, a restaurant, or a repair shop, the ability to feel secure running a business from one's home is another way in which the titling effort has helped to alleviate poverty in Langa. Sheila Mahloane is a Langa homeowner who has been able to use her home to build a successful business. Sheila did not need to search for commercial real estate to

³⁵ In studies conducted in Peru, in reviewing that country's titling reform efforts, Erica Field has found that people (adults) who have secure title to their homes work more hours per week than do people who lack title, as title holders devote less time to protecting their home from possible invaders or thieves. Moreover, the number of hours children in the house work decreases. See Erica Field, 2002, "Entitled to Work: Urban Property Rights and Labor Supply in Peru," *Princeton University Research Program in Development Studies Working Paper No. 220*, available at: <http://www.wws.princeton.edu/rpds/downloads/field_entitled_to_work.pdf>; and Erica Field, 2003, "Property Rights and Household Time Allocation in Urban Squatter Communities: Evidence from Peru," available at: <<http://www.worldbank.org/urban/symposium2003/docs/papers/field.pdf>>.



Sheila serving lunch

purchase or rent. Because she held title to her home she was able to leverage this asset, using this space to pursue her entrepreneurial dreams.

HOMES AS A PLACE OF BUSINESS

Lelapa sits on a quiet side street in Langa. The restaurant, which has a worldwide reputation among travelers for good food and a friendly atmosphere, is run by Sheila Mahloane and her daughter Monica.

The day we visited Lelapa a large group of Danish visitors came for lunch. Sheila welcomed them in Xhosa, Zulu, and German. Then she told us that we were in her house, 49 Harlem Street, which she has lived in since 1960. Back in the 1960s, nine people shared this one-bedroom house. Today, 50 or 60 can share it for a meal.

Sheila told us that in 1972 she began working as a domestic servant. With no formal education,

this seemed to be her best option. She earned 40 rand per month and worked five days a week. With such a small income she had to get an afternoon job. This raised her monthly earnings to 80 rand, but she decided that she needed to do something to help herself.

One day, while she was at her domestic-servant job, Sheila picked up a stray restaurant receipt. On it she saw that the people for whom she worked had spent 39 rand for two glasses of wine and cheese. She was shocked. This meant that she was working for a month for what these people had paid for two glasses of wine and some cheese. But, she also said, as this is what she had bargained for, she couldn't complain.

She did know, however, that she needed a plan, so she enrolled in night school. This meant she was working a day job, an afternoon job, and then heading straight to school. By the time she got to

her classes, she told us, she was exhausted. And so, “the teacher would start teaching, and I would start sleeping.” She said that night school didn’t work out, but she knew she needed some way to be worth more than two wines and cheese.

She decided to quit her two day jobs and concentrate on school. She still had to earn money though, so she bought some second-hand clothes and began to sell these in Langa. This business turned out to be more profitable than the previous two jobs, allowing her to go to school and support her family.

In 1986, she finally decided to leave the clothing business. She had finished her studies and was offered the food concession at St. Francis High School in Langa. She stayed there for 10 years, but by 1996 she was tired and wanted a change.

Happily for Sheila, change was all around her. The new South Africa was only two years old, and tourists were interested in seeing the townships. Tour companies were not sure though what kind of a reception they would get from the local people, so they simply rode through the townships in large, air-conditioned buses, waving at the township residents as they passed.

Alert to opportunity, Sheila decided that if she and her daughter Monica could turn their home into a restaurant then maybe they could “save” these poor tourists and make a few rand in the process.

But in order to “save” them, she needed money to

renovate her home and make it into a restaurant. She wasn’t able to get a commercial loan because of her long history of self-employment, but this didn’t stop her. Sheila went back to selling clothes: she flew to Bangkok and bought new clothes, which she was able to resell for a profit in the townships. The profits, not as much as she would have liked, nonetheless allowed her to expand the house and purchase the supplies she needed to start the business.

In 1999, after three years of preparation, she and Monica opened Lelapa. “The roots went down,” Sheila said. Over the past six years, the house has been progressively converted into the restaurant. Today, in addition to providing work for herself and Monica, she employs five girls full-time, and she hires high-school boys to play music and sing on some evenings.

Sheila’s story of perseverance and entrepreneurial spirit provides one example of how security of tenure provided a basis for the creation and expansion of a strong business. It is much less likely that Sheila would have been able to turn rental property into a restaurant or make the improvements and changes in the property that she has made. However, with her secure title Sheila *has* invested in her property and now reaps the benefits of using the property in a profitable way. In her case, Sheila has gone from being an employee to being an employer. She provides steady work for five people and part-time work and experience for several more. Sheila’s efforts, and the efforts of other home-based entrepre-



Lunch offering at Lelapa

neers, are attacking poverty in Langa.

HOUSE IMPROVEMENT SPURS ECONOMIC ACTIVITY

The housing process can have important links with the informal sector. The informal construction industry, constituting very small firms and private individuals can itself be a major source of employment much needed by the urban poor.³⁶

Perhaps the most noticeable way that the policy of providing tenure security and title is having an impact on poverty alleviation is through individual efforts to improve a house. So long as property rights are secure, we would expect people to make investments in improving and conserving their property.

In many sections of Langa, a wide variety of house improvements are taking place. Some of these are small-scale upgrades to windows and doors. Some involve the addition of wrought iron fencing to the front of a house. Yet others are more substantial upgrades that involve adding a room or rooms and upgrading the interior space. Exterior improvements are clearly visible throughout Langa, but interior changes are likely to escape a visitor's eyes.

These changes indicate that Langa residents are hiring cabinet-makers, electricians, and tile layers and purchasing appliances, paints, and wallpaper. And, we discovered, Langa residents tend to hire other Langa residents to do the work they themselves can't do. Not only does this keep money moving within the township, importantly, house improvements provide a signal to artisan-entre-

³⁶ See Adebayo & Adebayo, p. 5, *op.cit.*

preneurs to develop or improve their skills. The demand for artisans, bricklayers, carpenters, and masons means that more people have incentives to acquire these skills and to set up shop (normally from their homes) to meet the demand of Langa residents.

INCREMENTAL CHANGE IS THE NORM

One example of the way Langa residents promote a demand for artisans is Mr. Ronald Mhlongo. Mr. Mhlongo has lived in his home since 1984. He described what the house was like back then. It had four rooms (two bedrooms, a kitchen/dining room, and a bathroom). The plaster on the walls was peeling; wind would blow sand through the house; the roof leaked; it was cold and wet. He said that he applied for title in 1988 when the law changed and the city council allowed people to do this. The government sold him the house on terms—he would have a little of his pay deducted at each pay period, and, in this way, he was able to purchase his home and acquire title.

Mr. Mhlongo has made extensive improvements to this humble home. He did this by saving a little money to replaster, and then he saved a bit more to add a ventilator. He added two more rooms (a sitting area/living room and another bedroom) and also a “granny flat” in the back yard serves as bedrooms for two of his sons and for a grandson.

Like many of the people with whom we spoke, Mr. Mhlongo belonged to different savings

clubs.³⁷ He said that sometimes these clubs work fine, but other times they fall apart so he got used to budgeting for projects from his own small savings. This meant that he might buy some bricks when he had a little money, and then go buy a bag of cement later on, then something else, and eventually he would have enough to do something to the house. On his current job, he had hired two men to build a brick fence around his property.

When we asked him if he had ever tried to get a loan from a bank to do this work, he said that he never thought of going to a bank because of the problem of interest. He doesn’t have a permanent job now, and he felt it would be a problem to have to pay interest when he was only working occasionally. He prefers to save and then make improvements.

In our experience, Mr. Mhlongo’s approach to house improvement was typical among Langa residents who have freehold title. In the late 1980s or 1990s, they acquired title to run-down properties that were in desperate need of improvement. With their newly acquired title, people wanted to and had incentives to improve their property. But, they tend to do so only gradually and using small personal savings.

The gradual approach to house improvement may be explained by the fact that many residents work in the informal sector, which makes qualifying for a bank loan difficult because their income can

³⁷ The role of savings clubs is explained below.



Mr. Ronald Mhlongo with his mason, Mr. Tofu, in front of his home in Langa

fluctuate substantially. There are relatively few alternatives to commercial lending in townships. The spread of micro-lending in South Africa has not been as broad as some expected.³⁸ Additionally, people expressed a greater sense of trust with members of savings clubs than they did with unknown bank officials.

For these reasons, among others, traditional banks play little part in the typical Langa house-improvement project. Instead, homeowners slowly improve their properties using personal savings and savings clubs. These improvements, however incremental, increase the value of the property and the homeowners' wealth—wealth that most homeowners expect to hand down to their children.

Homeownership is a path towards wealth creation insofar as it creates incentives to invest in and

improve an asset: one's house. Investing in human capital or in a business can also create wealth. It is possible that people might use title to a house as collateral for a loan that would allow them to invest in human or other capital, but in Langa this seems to happen infrequently. Instead, we found that wealth tends to be created by investing using personal savings.

SAVINGS CLUBS AS SOURCES OF FINANCING

Down the road from Mr. Mhlongo, Rebecca Mokhale is also busy improving. Rebecca is a younger mother with children at home. She has a job, but it's in the informal sector: she is an entrepreneur who makes fat cakes (like doughnuts, but savory). She runs her business out of a container stand by the busy taxi rank in central Langa and has two ladies working for her. Rebecca also works three days a week as domestic help.

³⁸ See Meagher & Wilkinson, *op. cit.*



Mrs. Mokhale's front addition, a verandah, in Langa

Rebecca is one of Langa's newer home owners. She moved into her house in 1999 after spending 10 years in a shack in Langa's Zone 15. The story of how Rebecca came to own a house in Langa is instructive. She bought an old-style, four-room house for 45,000 rand from a friend. She had wanted a house very much, and so when her friend told her the house would be up for sale, she set her sights on it.

By the time the friend was ready to sell, Rebecca had saved 30,000 rand. Her strategy was straightforward: each day she put 100 rand aside from the profits of her fat cake stand. Being a disciplined saver, she was able to set aside almost 3,000 rand per month. Within a year's time, she had the 30,000 rand.

Unfortunately, 30,000 rand wasn't enough. The owner told Rebecca that she would only sell the house for 45,000 rand. Short of cash, Rebecca

was able to borrow another 4,000 rand from friends. This left her 11,000 rand short, but she and the owner reached an agreement that Rebecca would pay the seller the outstanding balance by making a monthly deposit into the seller's bank account. Given this arrangement, Rebecca thought it was wise to have a lawyer involved, and because she works as a domestic for a lawyer, she was able to obtain this person's services. Rebecca's employer performed the formal conveyancing of title for her at a low price, which she paid off in weekly installments.

Rebecca has made other improvements to her home. She has already remodeled the kitchen (see photo above) and bathroom. The exterior of the house has been bricked, and she's got the beginnings of a garage. She has put tiling on the walls and floor and has carpeted some rooms.

When asked how she finds the workers she uses,

Like Ronald Mhlongo, Rebecca Mokhale is a member of a savings club called an *umgalelo* or *gooi-gooi* (pronounced hoy-hoy). She puts 2,000 rand (\$303) per month into this club, as do 11 other people. Each month one of them gets the “pot.” She used her turn with the pot to add an addition to the front of her home that will expand her dining area and add a verandah. But the pot wasn’t enough to finish the job, so she borrowed from a *gooi-gooi* that specializes in lending money to non-members. She has to pay this loan back with 20% interest.

Savings clubs are informal institutions that have evolved to function as an alternative to commercial banking services. When commercial banking services are perceived as too costly, because they are inaccessible for some reason, people may spontaneously develop self-help institutions such as the *umgalelo* to access capital.³⁹ A key rule of the *umgalelo* is timely monthly payment. In essence this is a forced saving rule. Club members exert social pressure on each other to enforce this rule. The result is that most club members pay, and all members benefit. Members have incentives to pay because their reputation within the community is at stake. This incentive may be different with commercial credit because there are no credit bureaus in South Africa; the consequences of non-payment are limited by social norms that make repossession difficult; and some social norms condone non-payment of debts owed to the government (such as rates and service fees).

her reply was typical: she asks her neighbors. With many people remodeling, it’s not difficult to find a contractor, she told us. Overall, she believes that she has had five different artisans work on her home and she has been very happy with each one. She said that it’s better to work this way—with people that you know.

What is interesting about Rebecca’s experience is what it tells us about the property market in

Langa. As in Rebecca’s case, most older houses in Langa sell by word-of-mouth, and the purchase price is paid in cash. Mortgage bonds are not commonly used in these transactions—though some people must resort to bonds, as evidenced by the fact that 30 homes in Langa are owned by banks.⁴⁰

Personal networks are essential for transferring property. The trappings of a “modern” real estate

³⁹ See Laura du Preez and Charlene Clayton, 2004, “You can bank on high costs,” *Personal Finance*, available at: <<http://http.persfin.co.za/index.php?SetId=300&fSectionId=592&fArticleId=2194760>>.

⁴⁰ See footnote 1 above.



Mrs. Mokhale's backyard, with an addition

market—real estate agents, title insurers, and mortgage lenders—are absent in Langa (though common in new, privately developed areas). But, this doesn't mean that homes don't change hands; they do. It means that transfers may not be formally registered at the Deeds Office due to high costs associated with formally transferring property in South Africa. Transaction costs are high because:

- only conveyancing attorneys may formally transfer the title deed to a property;
- legal barriers prohibit price competition among conveyancers, so closing costs are higher than they otherwise would be;
- properties need to be formally surveyed;
- transfer duties add additional costs to the process; and

- sellers must pay arrears for rates and services before a formal transfer can take place, adding yet more costs to the process.

In order to avoid these high transaction costs sellers and buyers rely on informal transfer processes, such as sales using an affidavit. However, these informal sales reduce the security of tenure. A key problem in South Africa is then how to reduce the costliness of the formal process involved in selling a house.

Secure property rights provide incentives to maintain and conserve a resource. These incentives help explain why Langa residents are working hard to improve their homes. One related benefit of secure property rights is that they empower the person who holds them: the person holding the rights makes decisions about how to use and manage a resource. For people whose lives were severely constricted by legal oppres-



Rebecca Mokhale in her upgraded kitchen

sion, such as occurred under apartheid, providing secure property rights is one way to grant them greater autonomy and a freer scope for decision making—something that was sorely lacking under the National Party government.

Mrs. Constance Macozoma is a Langa resident who lived much of her life under apartheid. Her home is on Bhunga Ave, in the oldest section of Langa, where attached row houses line the streets. Her story illustrates both the obstacles that residents of Langa have faced, but it also highlights the empowering nature of property rights.

Back in the mid-1980s, Mrs. Macozoma wasn't even sure she'd be allowed to stay in Langa. After township uprisings in 1985, the National Party government told the people of Langa that they would be moved out. Until such threats were ended, tenure remained extremely insecure. Economic conditions in the 1980s also made

tenure insecure. She recalled that during this time, if you didn't pay your rent, the authorities would throw you and your belongings out of the house and onto the streets. Rather than let this happen, it was often the case that neighbors would help each other meet rent payments.

It was during this era that the local council began to neglect maintenance on the homes in Langa. The result was leaky roofs, warped floors, and generally bad housing conditions. In 1986, when the government began to allow people to take title to their homes, residents of Langa thought that they would get their houses "for free." They didn't realize, she said, that the government wasn't going to help to fix these houses up before they turned them over to the inhabitants.

So, it was up to the residents who acquired title to bear the costs of improvements. She said that they started savings clubs to help each other to fix



Mrs. Constance Macozoma in front of her home on Bhunga Avenue in Langa

up their homes. “In this way you had money.” Mrs. Macozoma went on to say that “the savings club was easier (than a bank). It wasn’t painful.”⁴¹ To this day, she remains a member of savings clubs. “Most people,” she said, “have struggled for their homes. It’s not easy but you feel you’ve done something; you’ve accomplished something by having this home.”

Through a strategy of careful savings and participation in savings clubs, Mrs. Macozoma has been able to replace the floor in her house, improve her kitchen, change the windows in her house, and add on a room. In the process she has employed a number of Langa artisans, adding to the wealth of those workers and improving the value of her

own home. Just like Mr. Mhlongo, however, she hasn’t used her title as collateral for a loan. For someone who struggled so long and hard for a secure place to call her own, maybe the risk of losing one’s home through a loan default is simply too great.

NEW HOMES, NEW JOBS

Finally, it is worth noting that there are also new homes in Langa. These are being developed privately and are expanding the housing supply in this desirable location.⁴² Owners of these new homes face the same incentives as the owners of older housing stock—incentives to conserve and preserve their property in order to maintain and improve the property’s value. Over time, we can

⁴¹ Interview with Constance Macozoma, October 17, 2006, Langa Township, South Africa.

⁴² Langa is located just off the N2, a major highway in Cape Town, and is also fairly close to the city, unlike newer townships.

expect these new owners to expend resources making their homes even more comfortable, more attractive. For many of them, this will mean employing people like the artisans who are busy at work at Rebecca Mokhale and Ronald Mhlongo's homes.

D. WHAT LIMITS THE SUCCESS OF SOUTH AFRICA'S ENTREPRENEURIAL HOUSING POLICY?

The policy of transferring title deeds to residences from the public sector to private individuals has been in effect in South Africa, in one form or another, for two decades. In Langa Township, the occupants of many formal residences now have freehold title to their homes, for the titling transfer process was largely complete by the late 1990s.⁴³

In contrast to what government officials may have expected, evidence seems to indicate that few people leverage the equity in their homes and use their titles as collateral for a commercial loan.⁴⁴ They do, however, use personal savings and savings clubs to build businesses and improve their homes. This finding tracks evidence from the U.S. that suggests most small businesses are also financed with personal savings, not with commercial loans.⁴⁵

For example, the Finmark Trust Township Residential Property Market (TRPM) studies from 2004/2005 found that 75% of investments made in townships are made with personal funds, not with commercial loans.⁴⁶ Further, while there is significant informal economic activity in Langa, the titling policy by itself does not appear

⁴³ We note that while formal residences have title, there are no titles for the informal squatter shacks where many people in Langa still live. This means that the economic benefits one might expect to see in a community filled with titled homes is muted in Langa, where many untitled, informal dwellings exist.

⁴⁴ Other studies reach similar conclusions. For example, see Jean Ensminger, 1997, "Changing Property Rights: Reconciling Formal and Informal Rights to Land in Africa," in *The Frontiers of the New Institutional Economics*, Academic Press: London; Klaus Deininger and Songqing Jin, 2003, "The Impact of Property Rights on Household's Investment, Risk Coping, and Policy Preferences: Evidence from China," *Economic Development and Cultural Change*, Vol. 51; Erica Field and Maximo Torero, 2003, "Do Property Titles Increase Credit Access among the Urban Poor? Evidence a Nationwide Titling Program," available at: <http://econ.ucsd.edu/seminars/seven_ssrc/Field_Torero914.pdf>; Erica Field and Maximo Torero, 2005, "The Impact of Land Titles Over Rural Households," Inter-American Development Bank Working Paper, available at: <<http://www.iadb.org/ove/Documents/uploads/cache/600797.pdf>>; Michael Carter and Pedro Olinto, 2003, "Getting Institutions Right for Whom? Credit constraints and the impact of property rights on the quantity and composition of investment," *American Journal of Agricultural Economics*, Vol. 85, No. 1; L.J. Alston, B.G. Libecap, and R. Schneider, 1996, "The Determinants and Impact of Property Rights: Land Titles on the Brazilian Frontier," *Journal of Law, Economics and Organization*, Vol. 12, No. 1; and Gershon Feder and David Feeny, 1991, "Land Tenure and Property Rights: Theory and Implications for Development Policy," *The World Bank Economic Review*, Vol. 5.

⁴⁵ See Amar Bhide, 2000, *The Origin and Evolution of New Businesses*, Oxford University Press: New York, 29-37.

⁴⁶ See Kecia Rust, 2005, "Dead Capital in the Townships? Looking into the Workings of the Township Residential Property Markets," *Finmark Trust*, 10, available at: <http://www.finmark.org.za/documents/2004/OCTOBER/IHSA_Townships.pdf>.



Newly completed homes in Langa

to have generated a boom in more formal economic activity.

The TRPM project argues that the resale market in townships generally functions poorly. The conclusions from these studies are that:

- township properties are considerably undervalued;
- property owners are not able to realize the economic benefits of homeownership;
- there is a “considerable informal secondary (resale) market” in townships;
- there is a limited supply of finance in old townships;
- the “ease of transactions” in real estate sales is “poor;” and

- overall, the old township real estate market is “dysfunctional.”

The Finmark studies paint a discouraging picture of township real estate markets, with the exception of newer, privately developed areas. They explicitly refer to township capital as “dead capital”—a reference to de Soto’s work on informal property. The Finmark studies point out important concerns. However, it is important to recognize that if the real estate market in an old township such as Langa is “dysfunctional,” this dysfunctionality is a response to institutional constraints that promote informal transfers and that limit the use of commercial credit—constraints related to high transactions costs involved in transferring property, such as conveyancing fees, transfer duties, and the requirement to pay overdue rates and service charges before a formal transfer can take place.

In the next section, we examine some of the reasons why titles alone are not sufficient to create dynamic economic growth and poverty alleviation and why it is essential to understand the surrounding institutional environment and how it hinders or promotes poverty alleviation and economic growth.

WHY PEOPLE DON'T USE TITLES TO SECURE LOANS

Freehold titles provide individuals who hold them with tenure security. In turn, secure tenure provides individuals with incentives to invest in their property, to care for it and maintain it, because by doing so, an individual is more likely to capture future benefits.⁴⁷ When it comes time to sell the house, a well-maintained house would fetch a higher sales price than a poorly maintained house. In addition, when someone holds the rights to mortgage a property, they often use that right to access commercial credit. Loans from a commercial lender can help start a business, pay for medical expenses or education, or some other activity. The right to mortgage property is one of the many “sticks” in the bundle of rights attached to freehold title. So why are more title holders not using this stick to obtain loans and build or expand businesses, improve their homes, or fund education?

We identified many reasons for the pattern of

reliance on personal savings and savings clubs over commercial loans in Langa. Among them are the following:

Risk. People do not want to risk losing their home for these reasons:

- Given the significant housing shortage in South Africa, if one loses one's home, it would be very difficult to find another. The most likely result of losing a home would be that a family would need to move into the house of a relative.
- Many formal residences have an informal shack in the backyard. The shack is either home to a relative or a source of rental income for the homeowner. If the home was lost by foreclosure, the ability to house family members and/or the right to rental income would also be lost.
- Homes also often serve as the locus for a business. If the house is placed at risk by a commercial loan, so too is the place of business.
- The home has a very high cultural value as the family “seat.” Parents and maybe grandparents lived in the house, and typically the current owner wants to keep the home to give to his or her

⁴⁷ See Boudreaux, *op. cit.*

children.⁴⁸

- For people who lived with severe insecurity under apartheid governments, it may be especially valuable to hold ownership rights and the increased sense of security these provide. Black South Africans faced enormous institutional barriers in obtaining formal housing in

the Cape Town area. For those who fought hard to get a house, retaining the house may have a high sentimental value.

Trust issues. People who rely on personal savings do not face trust issues—they presumably trust themselves with the money they save. For people who use a savings club rather than a bank loan, trust and reliability seems to play an

EThandiwe Tolashe works at Maki Dyani’s chicken take-away store. She is a member of an *umgalelo*—a savings club (“*Umgalelo*” means “we put something into a common pot.”) Her club is a much more modest one than Rebecca Mokhale’s: Thandiwe saves 125 rand per month. She said that she uses the money she receives from the club on her house. She has been renovating her house, “slowly, slowly.” When asked about the *umgalelo*, she said, “You join a club with people you know. They put pressure on you to continue contributing.” Thandiwe said that she would do whatever it takes to make her monthly contribution, even borrow from others, because if you’re late with a contribution, you have to pay a fine.⁴⁹



Thandiwe Tolashe

⁴⁸ In our interview with Mr. Mhlongo, he told us that people prefer to stay in Langa. “It’s where their parents were, where their parents died, where they grew up, and they don’t want to lose such a place,” he said. So, even if people move out of Langa, they will still hold onto the family home, even if it’s empty, for the sake of protecting this family property. He said that even those people who are still in rental property consider it “theirs,” as does the community, and that if they move and leave this property vacant, it is nearly impossible for the city to put new tenants in because the property should be kept for the “owners.” Interview with Ronald Mhlongo, October 12, 2005, Langa Township, South Africa.

⁴⁹ Interview with Thandiwe Tolashe, October 12, 2005, Guguletu Township, South Africa.

important role in their choice of how to obtain capital. Members of a savings club can monitor other club members and pressure them to comply. This is similar to the pressure one finds in micro-finance organizations. Club members expect that they will receive their payout because of this very real, albeit informal, pressure. People do not have the same sense of trust with a commercial bank because they lack personal relations with bank personnel.

But, reliance on trust relationships has real drawbacks. Today, informal house sales take place in Langa between a trusting seller and a trusting buyer (as, for example, with Rebecca Mokhale). These parties may, or may not, formally register the property. If they avoid the transactions costs associated with registering property, it will be much more difficult in the future to establish a clear line of title for the property. Trust allows parties to behave informally and avoid the transaction costs associated with formality, but this trust works best when communities are homogenous. As more people move into Langa who have no history in the

township and are “strangers,” the community will become increasingly heterogeneous, and it will become more costly to rely on informal trust arrangements.

Lack of lending activity. People are right to think that commercial banks don’t actively lend to the low-income households. There are several reasons for this:

- As the Banking Council of South Africa had stated in the past: “Originating and administering low-value mortgage loans is very costly relative to the actual loan amounts, and therefore, the interest earned on them is insufficient to cover the costs.”⁵⁰ To date, banks have shown little interest in lenders who earn less than 5,000 rand/month.⁵¹ For banks, this has not been a profitable market, though this may be changing.⁵²
- Banks have been hesitant to lend to people working in the informal sector, given their sporadic income. Many

⁵⁰ See “Serving the Low-Income Markets,” *The Banking Council of South Africa*, available at: <http://196.33.155.136/public/Paint_a_review.cfm?year=1998&index=6>. In an interview, a representative of the Banking Association of South Africa (previously the Banking Council) suggested that the Association will not be able to provide private financing for people who make less than 1,500 rand per month (\$227 U.S.). Mr. Joopie van Honschooten of the Association says that banks can do little terms of lending for such low-income earners. Instead, Mr. van Honschooten believed that such people need social housing (i.e., government-subsidized rental housing) and not a privately owned home. Banks, he told us, can only help “commercially viable” households. Interview with Joopie van Honschooten, September 21, 2005, Johannesburg, South Africa.

⁵¹ See “Editorial,” *Business Day*, February 9, 2006, available at: <<http://allafrica.com/stories/200602090381.html>>.

⁵² See “The hidden wealth of the poor,” *The Economist*, November 3, 2005, which discusses the spread of for-profit financial services from the developed to the developing world.

Langa residents do work in the informal sector and would face this barrier if they applied for a commercial loan.

- Banks charge relatively high fees and provide relatively low returns. Banks charge annual fees on accounts, as well as a fee for each transaction. Banks charge for making a deposit, an anomaly compared with banks in the rest of the world. And, importantly, South Africans pay “far higher interest charges on their home loans than consumers in other countries.”⁵³ This helps explain the relative lack of lending and banking activity in areas such as Langa.
- There is a history in South Africa of defaults in townships followed by real difficulties in repossessing property. Strong social norms and community action work together to prevent evictions and repossession. This makes lending in such areas costlier for banks.⁵⁴
- Lenders require homeowners seeking home improvement loans to prove they are using certified artisans, an understandable policy but one that makes it costlier for homeowners to use commercial loans.

Complexity and costs. For many people, the formalities and complexities involved in getting a house loan are too high. Saving for a down payment can be difficult, and with extremely high mortgage bond (real) interest rates, making monthly payments can present a real hurdle.⁵⁵ In addition, the process is intimidating for many and is costly in terms of time and effort. Grappling with the paperwork involved in applying for a commercial loan can be difficult. Complying with requirements to produce supporting documents can prove complicated. There are few banking facilities in townships, though this seems to be changing with the introduction of banking kiosks. Kiosks are not, however, the same thing as office where one can meet with a loan officer.

Peace of mind. Faced with a choice between two methods of housing finance—the personal savings option and a bank loan, even a loan with minimal compliance hurdles—by and large, the expressed preference is still for the former. People who have built their houses often mention that despite the fact that this route takes an awfully long time—in many cases years—at the end of the day when the house is finished, they do not worry about bond repayments.

Issues related to risk, trust, and perceived complexity represent informal institutional barriers or social norms that may be difficult to modify or

⁵³ See du Preez and Clayton, *op. cit.*

⁵⁴ See Adebayo & Adebayo, p. 6, *op. cit.*

⁵⁵ See du Preez and Clayton, *op. cit.*

overcome. However, we would expect these norms to change over time, as individual homeowners create credit histories and to the extent that the institutional environment in South Africa becomes more conducive to establishing and growing a formal business. However, so long as the institutional environment gives small business owners, such as Shelia Mahloane and others in Langa, incentives to remain small and not grow, we would expect the use of title as collateral to remain relatively low.

OTHER PROBLEMS AND BARRIERS HOMEOWNERS FACE

In addition to the informal barriers outlined above, other more formal institutional barriers exist that impede economic development tied to the benefits of titling. These problems are largely regulatory barriers that could be addressed through policy changes.

The unnecessary costs of government monopoly. People in Langa are not selling their homes as visibly and perhaps as frequently as one might expect. We emphasize that sales do take place, but they take place informally—outside the scope of the formal transfer process that exists in South Africa. The main reason for low levels of formal sales activity in Langa is that selling a house through formal channels is quite costly.

The main culprit is South African lawyers, some of whom have been given a monopoly over the

legal transfer of property. In order for a deed of transfer to be formally registered with the registrar at the Deeds Office in South Africa, the parties to the sale must put their agreement in writing and use the services of a conveyancing attorney. Conveyancing attorneys prepare sales and transfer documents and have them signed and sent to the Deeds Office for review. The Deeds Office records the transfer of ownership and signs the purchasers' new title deed.

Conveyancing attorneys are the *only* people who can register title in the Deeds Office. This monopoly privilege means that conveyancing attorneys are able to charge higher rates than would be possible if the market for these services was competitive. Coupled with transfer duties and stamp duties, this anachronistic legal procedure stymies the formal transfers of property among poorer South Africans. Indeed, the requirements of this process impose disproportionate burdens on the poor, who are less able to afford the costs of supporting conveyancing attorneys. Table 1 highlights the burden faced by individuals transferring lower valued property, as compared to those transferring higher valued property. Recognizing that there are fixed costs associated with the process of transferring property, these rates are, nonetheless, indicative of the burdens faced by individuals selling real estate at the lower end of the market. Given these financial hurdles, it is no surprise then that the house sales that do take place in Langa often happen informally and using affidavits.⁵⁶

⁵⁶ See discussion with Ms. Joy McNab of McNab Realtors below.

TABLE 1

EXAMPLE OF FINANCIAL COSTS ASSOCIATED WITH CONVEYANCING⁵⁷

VALUE OF PROPERTY (IN RANDS)	2000 CONVEYANCING FEE (IN RANDS)	PERCENTAGE
Less than 18,000	760	4.22%
18,001 to 30,000	1,130	3.76%
30,001 to 45,000	1,390	3.08%
45,001 to 70,000	1,640	2.34%

For another view on the real estate market in Langa, we met with Ms. Joy McNab and Mr. Thabo Manganyi of Joy McNab Realtors in Cape Town.

Joy told us that there are “NO” homes for sale in Langa. But this isn’t the only, or even the primary problem, she sees in the Langa market. A bigger problem, she said, is that she does not see people making the kinds of improvements to their property that one would hope to see—gardens and second stories added onto homes. And Langa has not upgraded its commercial strip to make it a more attractive shopping location.

Thabo also sees little movement in the Langa real estate market. He noted that the new houses in the township have been all sold, an indication of a strong demand for housing in Langa. However, he said there’s little other stock.⁵⁸ He believes that the property in the township is undervalued, in part because there are few useful benchmarks. In Thabo’s opinion, the Langa market is so inactive, it’s hard to tell what things are worth.

Both Joy and Thabo agreed that it can be quite difficult to trace who owns which property in the township. And, they both agreed that a lot of informal trading goes on (an indication that homes are, in fact, for sale, but not via formal channels).

⁵⁷ Warren Smit, 2000, “Investigation of the Various Types of Tenure Applicable to Affordable Housing in the Cape Metropolitan Area,” *Development Action Group*, 19.

⁵⁸ From our experience, stock is available, but it may not be available to an “outsider” real estate agent—instead, it is available through informal social networks. With a private, informal sale, the sales price may not be readily accessible, and this would make it more difficult to an outsider to determine what homes are worth.



Joy McNab discussing the housing market in Langa

When this happens, they told us, and someone wants to sell their house, it is sold for cash. They were concerned these informal sales do not lead to formal registration. Instead, parties to the transfer go to the local police station and fill out an affidavit. The affidavit states that the party selling the house is its owner. It states who the purchaser is and what the purchase price is. The affidavit also states that the seller has the right to sell the house. The police witness the signatures on the affidavit, money changes hands, and after this informal process, the purchaser takes possession of the house.

Because this process works outside formal channels, these transactions are almost certainly not recorded in the deeds registry—another strong reason to end the conveyancing monopoly. If conveyancing were easier and less expensive, costs associated with selling property would be lower. As a result, fewer of these informal trans-

fers would take place and the deeds registry would be more dependable.

The current process for transferring property imposes significant transactions costs on sellers. It is not surprising that sellers seek ways to avoid these costs. In order to effectively address the problem of informal sales, the government must identify ways to reduce transactions costs associated with the sale of real property. Once this happens, we can expect people to respond by using the formal channels for transfer of property more often. Current norms that lead people to transfer property informally should be replaced by a growing reliance on formal methods of transfer.

Another issue that may limit the formal transfer of property in Langa and that may limit the homeowners' abilities to leverage titles to their homes is the limited availability of commercial credit, including micro-lending. We address this concern below.

“The Councilors are a nightmare.”

Conveyancing costs are not the only problems that limit the sale of houses in Langa and keep house values lower than they might otherwise be. Another category of obstacles that homeowners face is associated with the capacity and responsiveness of the local government. Local government does not do enough in Langa to provide a safe and clean local environment, and it places roadblocks in the path of commercial and residential property development.

Lack of services. Across South Africa, local governments are criticized for lacking capacity to perform their basic functions: maintaining law and order, maintaining local infrastructure, providing electricity and trash and water services. A key reason for these failures is that local governments have a poor record of effectively collecting “rates”—the local taxes that support local government activities—and service charges for water, trash collection, and electricity use. Because so many South Africans are informally employed, it may be difficult for them to make regular payments.

Some fall behind in payments or stop paying. Neighbors learn that the person next door isn’t paying, yet continues to receive water and electricity, so they stop paying. People see that the quality of service is poor so they too don’t pay. And, because social norms thwart repossession efforts, homeowners worry little that failure to pay mortgage bonds will lead to the loss of their homes.⁵⁹

And yet, unless you can prove that you have paid these rates for the three-year period preceding the sale of a house, the sale cannot formally take place. If people do not want to (or are unable to) pay back rates or service charges, in addition to conveyancing fees and transfer duties, they are more likely to sell via informal processes, such as the affidavit of sale. The requirement that owners prove they have fully paid rates and service fees before a formal transfer of title can take place creates barriers for many potential sales.

Figures on the municipal debt levels are staggering.⁶⁰ This revenue shortfall means that

⁵⁹ See Douglas B. Diamond, 2002, “A Community Reinvestment Act for South Africa,” *National Housing Finance Corporation*, Occasional Paper No. 2, 11, available at: <http://housingstudies.wits.ac.za/comm_r_act.pdf>.

⁶⁰ In South Africa, local governments are responsible for stimulating local economic development and for providing people with basic services. The basic services include water, electricity, sanitation, affordable housing, and basic health care. There is an enormous backlog in the extension of these services to historically disadvantaged communities, a daunting task for which the municipalities facing the highest backlogs have the lowest capacity to deliver. Rates of payment for local government services are low, and the cumulative arrears owed to local governments now amount to half of total local government annual revenue. See <<http://www.sn.apc.org/usaidsa/uss01.html>>. In the Auditor General’s report for the fiscal year ending June 30, 2003, municipal debt totaled 32 billion rand. The current figure is probably closer to 40 billion rand. Describing the debt as a “phenomenal amount of money,” the Auditor General cited the lack of skilled personnel as one of the key factors behind the failure to collect debt. See <http://www.da.org.za/da/Site/Eng/campaigns/DOCS/SA_Awards4.doc>.



Nam Mangaliso at the store

local governments have limited abilities to fund and provide essential services, such as keeping the electricity running and clearing the trash from streets. Thus the local government, known as a council, has a very difficult time upgrading the community—improving roads, lighting, sidewalks, etc.⁶¹ The local environment in Langa isn't as clean as it would be if the local council worked more efficiently, and this in turn keeps property values lower than they otherwise would be.

For example, Vicky Mangaliso runs a thriving butchery in Langa's commercial strip with her brother Nam. In conversations about her business, she told us that a major problem she and Nam face is poor trash collection, which

leads to problems with rats and other pests. The council in Langa doesn't do a good job of collecting the trash, so she and Nam need to spend their own money fighting vermin. Even if they do all they can, if neighboring store owners aren't as vigilant, the problems continue. So resources that could be spent improving the butchery must instead be used to do what local government can't do.

Given the size and scope of the informal sector in South Africa, collecting rates is extremely difficult. One approach to this problem of poor local services might be to reduce the burden on local governments by privatizing more of these activities. This would require homeowners to pay a private company for trash collection and elec-

⁶¹ Interview with Willem du Toit, October 10, 2006, Cape Town, South Africa.

tricity.⁶² The private company, rather than local government, would be accountable to homeowners for the quality of service rendered. Homeowners would face different incentives in terms of payment. Presumably, a service would continue to be provided so long as a homeowner paid according to terms worked out privately with the service provider. Recognizing the high level of informal employment in townships, one would expect private service providers to adopt a flexible payment approach for such customers.

Obstructionist behavior. Few people with whom we spoke had anything positive to say about the behavior of council officials. Instead, the common sense was that these officials are imperious and obstructionist. This unhelpful behavior seems to manifest itself most clearly when it comes to issuing permits to expand or change a house or business.

Mr. Ronald Mhlongo explained the process of applying for building permit to us. He said that you are supposed to take a plan to the council and officials either approve it, modify it, or reject it. A draftsman is supposed to draw up these plans. This, of course, is another expense for the homeowner. Mr. Mhlongo also told us that there are no draftsmen in

Langa or in nearby Guguletu Township so you must travel outside the townships to hire someone. He said the council might take months to approve a plan and so some people just ignore the process and go ahead and build.

We repeatedly heard stories like Mr. Mhlongo's—that council officials will routinely take months, sometimes years, to make a decision on whether or not a homeowner can add a room or a business can expand. To the extent that council officials impose these kinds of costs on residents, they hinder local development.

Problems related to crime. Unlike in the U.S., policing is the primary responsibility of the provincial and central governments in South Africa; it is not a local government function. The South African Police Service has overarching responsibility for police activities. However, Cape Town has a well-regarded municipal police force. Residents of Langa think more highly of the Cape Town police than the provincial and central police.

Compared to other black townships in the Cape Town area, Langa has relatively low crime rates. However, compared to more affluent locations around Cape Town, the rates are high.⁶³ Higher

⁶² Privatizing water services present particular challenges as the South African Constitution contains rights to certain amounts of water for free.

⁶³ To see information on numbers of crimes committed in Langa versus Guguletu, Nyanga, or Mitchell's Plain see: <http://www.saps.gov.za/statistics/reports/crimestats/2005/western_cape.htm#Southern%20Cape>. At this same site you will find information on numbers of crimes committed in more affluent areas such as Camps Bay.

crime rates reduce the value of property, making titles a less valuable asset than they are for people who live in low-crime areas. The crime rate in Langa, while lower than in near by townships, is still high enough that it imposes costs on business owners and on local residents.

For example, in Vicky Mangaliso's case, she would like to stay open later in the evenings but is too concerned about crime to do that now. This means that she closes her shop around 7 p.m. instead of 9 or 10 p.m. in the evenings. Vicky also noted that she could save money by buying her meat directly from the producer and omitting the services of a middleman, but this is impossible because the producer is too concerned about crime to make deliveries in Langa.

In a high crime environment, homeowners may limit their home improvement projects. If your house is too nice (if, for example, you add a second story or maybe a garden—as Joy McNab would like) you may signal to possible thieves that you have money and are a good target. To some extent, the relatively low crime rates in Langa may reflect effective self-policing in the community. Many Langa residents have lived in the township for decades. They know neighbors and neighbors' children and will monitor what happens in their area. This self-monitoring is a

benefit to Langa residents. In addition, more effective law enforcement would be a major benefit to the residents and business owners in Langa.

Access to financing. Many point to the lack of mortgage financing for low-income earners as a problem in the South African environment. We have discussed above some of the reasons why there is relatively little lending activity in townships like Langa. While it remains true that banks to date have done relatively little to lend to those earning less than 5,000 rands per month, change may be on the horizon. The poor may be bad credit risks, and banks may have done too little to determine credit histories, but some critics point to regulatory barriers, the lack of proper framework to support such banking services, usury laws, corruption, and erratic law enforcement as equally important problems.⁶⁴ Addressing these concerns may allow for greater experimentation in credit markets and increased borrowing options for the poor. There is evidence that large banks in the developing world are increasingly entering the market to serve low-income borrowers. Assuming this trend also develops in South Africa, the credit market should thicken in ways that benefit township owners in Langa and elsewhere.

The high cost of formality. Just like Americans,

⁶⁴ See "The Hidden Wealth of the Poor," *op. cit.*

South Africans can start businesses. However, while it is relatively easy and inexpensive for Americans to create a formal business, it is costly for South Africans to do the same, so many entrepreneurs opt to open informal businesses. If government policies made it easier for small businesses to grow and expand, the pace of economic development should increase.

According to the World Bank's annual *Doing Business* report, South African entrepreneurs can expect to go through nine steps, taking an average of 38 days, at a cost equal to 8.6 per cent of GNP *per capita* (which amounts to a total cost of \$312.88/business), to start a business.⁶⁵ In contrast, the average American entrepreneur can expect to go through five steps, taking an average of five days, at a cost of 0.5 per cent of GNP *per capita* (which amounts to a total cost of \$210.00/business), to launch a business. The greater complexity and costliness of this start-up process provides incentives for businesses in South Africa to operate informally.

In addition, the costs of growing a business are much higher for South Africans than for Americans. Labor laws, minimum wage laws, licensing and permitting requirements, and other regulatory requirements apply to larger businesses, increase the costs of moving from the informal

to the formal sector, and so provide disincentives to grow and formalize.

Again, according to the *Doing Business* reports, the average South African employer faces a Difficulty of Hiring index of 56 out of 100, as opposed to 0 in the U.S. In the area of Rigidity of Hours, South Africa scored 40, whereas the States received a 0. In the area of Difficulty of Firing an Individual, South Africa scored 60. In comparison the U.S. received a 10. With regards to the Overall Rigidity of Employment index, which is an average of the three indices, South Africa received 52 compared with the United States' score of 3.⁶⁶ It takes 18 steps and 176 days to complete the licensing and permit requirements for ongoing operations in South Africa. In contrast, it takes 19 steps and 70 days to complete the process in the United States.

These figures highlight a continuing problem with the institutional environment in South Africa: the high costs associated with creating and running a formal business. Red tape continues to stymie economic development, and it provides incentives to entrepreneurs to start and stay in the informal sector. These institutional concerns must be addressed if the South African government wishes to further unleash the entrepreneurial drive of its citizens.

⁶⁵ See "Doing Business: Snapshot Report, South Africa," 2005, World Bank, available at: <<http://www.doingbusiness.org/ExploreEconomies/Default.aspx?economyid=172>>.

⁶⁶ For more on this topic see Jasson Urbach, 2005, "Costs reduce formal jobs and push people into the informal sector," *Free Market Foundation*, July 5, 2005, available at: <<http://www.freemarketfoundation.com/ShowArticle.asp?ArticleType=Bulletin&ArticleId=2335>>.

E. POLICY IMPLICATIONS

Property goes beyond possession and ownership. It is essentially about building institutions. Like government and money, formal property is established through human agreements for very specific utilitarian purposes.⁶⁷

The problems outlined above suggest that in order for titling programs to have the greatest positive impact they must take place in an institutional environment that:

- allows for relatively easy and low-cost formal transfers;
- encourages the creative use of property;
- encourages the growth and expansion of businesses; and
- provides opportunities for individuals to work with local officials to improve their local environment.

For many homeowners who work in the informal economy, it is simply too risky to use title to their house as collateral. South Africans are, by no means, alone in this concern. In the U.S.,

most capital used to start a business comes from personal and family savings, not from loans secured with title to a house.⁶⁸ It is risky for American entrepreneurs to use title to their home as collateral also. This reasonable concern means that the government should not assume that providing title, by itself, is enough to promote economic growth and development. *Titling may be a necessary, but not a sufficient, means to spur economic activity.*

The government needs to provide secure title that can be registered in a relatively low cost manner. If homeowners transfer property informally, as they are currently doing in Langa, the benefits of costly titling efforts will largely be lost. An undependable, out-of-date deeds register fails to capture the on-the-ground reality of the property environment. For this reason, such a register is, to a significant extent, useless. In order to provide homeowners with greater incentives to use the formal transfer and registration process, the government should look for ways to reduce transactions costs. Government officials should also focus on developing policies and programs that promote security and predictability within the transfer process. However, they must also broaden their concerns beyond providing title—a valuable first step—to reducing red tape and the high cost of formality, so that more South Africans have incentives to use their property in creative ways.

⁶⁷ Hernando de Soto, 2001, “Dead Capital and the Poor,” *SAIS Review* Vol. 21, No. 1, 11.

⁶⁸ See Bhide, *op. cit.*

Our experiences in Langa suggest that the efforts of the South African government to provide title to a house to many citizens have produced real benefits to homeowners and to local artisans but that these benefits are not tied to the use of title as collateral. Instead, they are tied to the incremental improvements and business development efforts that homeowners undertake. Homeowners are reluctant to use their title as collateral for commercial credit, but they will save and invest. In the current institutional environment, however, homeowners who run a home-based business face disincentives to move their business into the formal sector. And, due to high transactions costs, homeowners face disincentives to use the formal transfer process. This leads to increased insecurity and reduced stability and predictability in the real estate market. These insights suggest that policy makers should consider adopting the following initiatives if they wish to strengthen the link between titling programs, and economic development and poverty alleviation:

- **Remove the government-created monopoly for conveyancing attorneys.** There is simply no good reason why one specialized type of attorney should be

required to transfer a title deed. While the person transferring title must be properly trained to identify possible problems in any given record, a specialized attorney is not needed to do this. A well-trained legal assistant could do the same work at a much lower cost. The key concern should be to ensure the legal reliability of the transfer, *not* to provide a monopoly privilege to a small group. If government officials want more homeowners to follow this formal process, they should consider: abolishing the conveyancing monopoly and introducing more competition into the conveyancing market.⁶⁹ If the government wants to ensure that more property is transferred in ways that promote security, dependability, and predictability for sellers and buyers, it should focus on reducing the cost of the transfer process.

- **Make it easier for small businesses, started with personal savings, to grow.** Residents of Langa readily start businesses, but the high cost of creating and maintaining a formal business in South Africa means these businesses are

⁶⁹ New Zealand has recently removed the special privilege that attorneys once held to formally transfer property. Today, specialist non-lawyers (known in New Zealand as conveyancers) have the legal right to convey property. The effect of this law removing this previous privilege is to provide consumers with more choice and make the conveyancing market in New Zealand more competitive. See Kevin Taylor, 2003, "Lawyer Reform a Step Forward," *New Zealand Herald*, July 30, 2003, available at: <http://www.nzherald.co.nz/section/story.cfm?c_id=1&objectid=3-515360>.

likely to be and remain informal. South Africa has a host of policies that raise the costs of doing business in the country, and these policies create disincentives for businesses to formalize and grow. Government should do more to make it easier for South Africans to enter formally into a business, employ workers, and fire workers when necessary. They should also work to reduce the costs associated with regulatory compliance.

- **Focus on improving services at municipal level.** Local government capacity must be addressed in order to upgrade the environment in townships like Langa and across South Africa. This might mean providing increased opportunities for private businesses to compete to provide services that are now the responsibility of local government. If services such as trash collection and electricity were offered privately to township residents, a different set of incentives from those that currently operate would exist. Homeowners would have less incentive to avoid payment, because there would be real consequences to a failure to pay. Private companies, for their part, would have incentives to develop flexible payment options in recognition of the large number of homeowners who work in the informal sector. Providing these services privately should increase the quality of services

homeowners receive because of increased competition. This would relieve strain on local governments. At the same time, policy makers should focus on improving councilor accountability and government transparency at the local level in order to promote competition among localities and to present residents with the best possible information concerning the efficiency of the local government.

- **Make it easier for artisans to become certified.** Requirements that artisans receive formal education and be tested to become certified, while well-meaning, may have the unintended consequence of making it much more difficult for low-income individuals and those with limited formal education to enter into a craft. It may be more appropriate to adopt a certification process that allows for artisans to be peer-reviewed by other, already-certified craftsmen. Another option would be for artisans to be tested by means of a practicum, rather than a formal, written test. For many artisans, proving they know how to do their jobs competently may be much less daunting than having to attend classes and take a test. Finding a reasonable accommodation, such as a practicum, for such individuals would have the benefit of making their services acceptable for banks, who do not lend for home improvements unless artisans are certified.

CONCLUSION

I can tell you that in every country, the law is hostile to the poor. It has not been made for the poor, and it is inaccessible to them. So the next thing that you have to understand is that the number one instrument is law. It doesn't have to do with mapping. It doesn't have to do with surveying. It doesn't have to do with traditional titling. It doesn't have to do with homes. It has to do with law and the possibility of creating a legal system that will make the poor want to enter it so they can start leveraging things and connecting to the real market economy. And that involves understanding that you have to do reforms that go beyond titling, that have to do with literally integrating the extralegal system.⁷⁰

Hernando de Soto is surely right to say that improving the lives of the poor in the developing world, in places like Langa Township, has to do with more than mere titling—it has to do with developing a “larger formalization process that converts ‘property’ into ‘capital.’”⁷¹ The South African government’s long-standing policy of transferring title from the public sector to private

individuals has been an important step on the road towards formalization and improved economic development and poverty alleviation. But, the policy represents only the beginning phases of a journey. As de Soto suggests, titling by itself cannot miraculously whisk the poor from the world of extralegality (or informality) to the doorsteps of the formal, commercial world—much more is needed.

Evidence from the U.S. suggests that the start-up capital for most small businesses comes from personal savings. This same pattern applies in Langa Township. Important differences exist, however, between the experiences of the typical American small business owner and a small business owner in Langa. The township business owner is much more likely to be operating informally because the costs associated with running a formal business, employing labor, and complying with regulations discourage them from expanding their operations. This is where government policies to promote economic growth and alleviate poverty should focus.

Because the use of house titles as collateral for commercial loans is risky, it is likely that the use of such loans will remain low so long as these institutional constraints remain. In economies with high levels of informality, people perceive

⁷⁰ Interview with Hernando de Soto, 2003, “Fighting Poverty with Property Law,” *ADB Review*, Vol. 32, available at: <http://www.adb.org/Documents/Periodicals/ADB_Review/2003/vol35_2/Hernando_de_Soto_Vision.asp>.

⁷¹ See de Soto, 2001, p.12, *op. cit.*

the strategy of using title as collateral as risky—just as they do in economies with high levels of formality. People may be more likely to use title as collateral after establishing a credit or once a business is established.

So long as they are employed informally, have little credit history, and/or face an institutional environment that provides disincentives to formalize, people may prefer to use personal savings and savings clubs to finance home improvement and business development. Until greater opportunity exists for formal employment, people will likely continue to rely on personal savings and savings clubs to build businesses and improve their homes.

For titling policies to have the greatest likelihood of promoting more economic development and poverty alleviation, they should be accompanied by complementary institutional reforms that reduce the costs of property transfers, make it easier to grow small businesses, and generate increased accountability and improved service provision at the local level. Ideally, the government should focus on developing an institutional environment that:

- abolishes the property conveyancing monopoly;
- allows for lower-cost legally reliable property transfers;
- makes it easier for small, informal businesses to grow and expand;
- provides increased opportunities for formal employment; and
- provides for the alternative provision of local services.

The lesson of Langa Township is that while titling helps to put some life into what might be called dead capital, by itself the titling policy should not be viewed as the solution to economic growth in South Africa. Titles provide the security and incentives needed to promote incremental improvements and to start small businesses, but real institutional reform is needed to encourage homeowners to transfer property via formal channels and to encourage business owners to grow and expand their businesses.

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