

# Dead Capital and the Sea: Post-Tsunami Relief for the Southeast Asian Informal Economy

BY KEVIN J. FANDL

Several years ago, Hernando de Soto brought to light the vast problem of informal property in the developing world.<sup>1</sup> Informal property constitutes up to 80 percent of all property held by citizens in developing countries, which means that a substantial portion of developing economies operate without the ability to export, guarantee legitimate loans, or grow businesses.<sup>2</sup> Informal property holders often operate under the regulations of community organizations rather than local or national governments. As such, their rights are protected only insofar as their communities remain intact and free of outside influence.

Southeast Asia is home to some of the fastest growing populations and markets in the world. However, in much of the region, property is unregistered and held without legal title. Foreign investors from China and elsewhere are keen to corner these markets with business investments; yet buying up informal property within a communal system is difficult, if not impossible. Private security forces and community defenses often collaborate to prevent outsiders from attempting to commandeer informally held property.

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What happens when this property faces a natural disaster? What community rules and protections apply when substantial portions of communities are washed out to sea? This is a question that must be addressed in the context of the tsunamis that devastated Southeast Asia in December 2004. When large portions of these communities are washed away and no formal titles exist to protect property rights, foreign investors are likely to face fewer barriers to entering local markets, leaving erstwhile informal property holders worse off economically and driving poverty levels to new heights. Governments in Southeast Asia must begin to implement a set of policies that will address these concerns and build a foundation for future economic growth based on formal property markets.

### **The Need for Property Rights**

Property rights are fundamental and must be protected by national and international legal institutions. They allow individuals to hold land, dwellings, and goods in a manner that is understood around the world in terms of value, credit, and security.<sup>3</sup> A right to property is more critical than property itself. Property alone cannot easily be traded, leveraged for credit, or protected against intruders. A legal right to that property, however, can accomplish all of these. That right represents a “consensus between people about how these assets should be held, used, and exchanged.”<sup>4</sup> It establishes a transferable value in the property, converting it to useful capital.

Much of the informally held property in the developing world today is acquired through social or communal relationships, such as informal settlements and squatting, rather than through open market exchange. Property claims of this nature are not recognized by the states in which they are located and bear no transfer rights or protection. Land is owned only to the extent that it is physically occupied and no others successfully challenge the ownership rights. Despite these inherent insecurities, informal property systems are still predominant throughout Southeast Asia.

Securing informal property is easier and less expensive than acquiring formal property in developing countries. Complex, time-consuming, and expensive regulations deter the majority of landowners from seeking formal recognition of the property they occupy. Prohibitively lengthy and costly regulations prevent businesspeople, especially those with few if any liquid assets, from acquiring formal title to

their operations.<sup>5</sup> Many would-be entrepreneurs are thus unable to obtain loans because they lack collateral.<sup>6</sup> As a result, a pool of “dead capital” exists: practically worthless informal property that could be used as collateral if registered formally.<sup>7</sup>

Recognizing the difficulties of obtaining legal property titles, resourceful citizens developed their own systems of land registration to provide limited benefits similar to those that accompany formal property rights. Informal property owners often have their own papers, registration systems, and agreements—all of which are clearly delineated in maps used for informal business transactions.<sup>8</sup> With these systems in place, informal property owners can buy, sell, trade, and leverage property within their communities by using reputation as credit. The result is a property rights system that recognizes a very limited group of people and limits the boundaries of the market to a particular community. Access to formal bank loans or foreign investment is all but impossible.

Settlement communities exist to facilitate trade, preserve community values, and offer widespread protection. They often provide a sense of security by keeping informal ownership records. Unlike wealthier, formal communities that can afford to invest in security systems and private guards, informal communities apply their own security provisions to protect property.<sup>9</sup> In many cases, attempts to expropriate informal property within these communities lead to physical violence.<sup>10</sup>

While this system functions well for small communities despite its extralegal settlement process, it wreaks havoc on national economies, hampering efforts to develop better infrastructure and eradicate poverty. Informal property owners are largely restricted to trading with and seeking assistance from only those within their communities. The formal economy, which produces exports and pays taxes to expand government programs, accounts for such a small portion of the overall national economy that the true worth of the national workforce is unknown, and the full potential of exports and international trade remains hidden.

This situation exists in developing regions worldwide, and Southeast Asia is no exception. In Bangkok, for instance, the informal sector now comprises roughly 60 percent of the total economy, even after having declined during the economic boom of the 1990s.<sup>11</sup> Ac-

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According to the International Labor Organization, 71 percent of all work in Thailand in 2002 was performed in the informal economy.<sup>12</sup> In Vietnam, where the state theoretically owns all land, similarly massive informal markets exist.<sup>13</sup>

Informal economies in Southeast Asia are distinguishable from those in Latin America and Africa primarily because more financial resources are on the line in Southeast Asia as a result of well-developed markets and higher levels of investment. In some Southeast Asian countries, national governments have recognized informal economies and embarked on regulatory reforms to remedy the strain on regional economies. These reforms contributed to Southeast Asia's characterization by the Asian Development Bank (ADB) as the most dynamic area of growth in the world in 2003.<sup>14</sup> The World Bank hailed Thailand, for instance, as having "a world-class system," for allowing property to be registered in only two days and at a cost of only 6 percent of the land value.<sup>15</sup> In Nigeria and Senegal, by contrast, the formal cost of selling property amounts to nearly 30 percent of the land value.

### **Natural Disaster Strikes**

In December 2004 tsunamis enveloped much of Southeast Asia. More than 200,000 people lost their lives as a direct result of the disaster, the impact of which will be felt in the region for years to come. Emergency efforts are underway to repair the damaged coastlines and provide much needed health and food aid to affected countries. However, one of the direct consequences of the disaster, the purge of informal property rights systems, is going largely unnoticed. Entire communities, along with claims to remaining property, were washed away by the tsunamis.

Survivors without formal property rights have lost homes and businesses, but they also have no claim to the land necessary for rebuilding. There is no office in Southeast Asia to which those who lost informal property can go to confirm their property rights. Moreover, the absence of formal claims to land removes a major obstacle for interested investors to secure property. Once land is registered and occupied, the state is more likely to protect that property against competing claims, even those brought by the original informal property owner. Even if competing claims to previously informal property fail to materialize, there are no insurance claims to be made by

informal property owners, meaning they have no access to funds to rebuild or relocate.<sup>16</sup>

### **Impending Threat and the Need for Proper Land Titling**

Land that was once ripe with production now lies dormant, susceptible to foreign claims. Some of the best beachfront property in Southeast Asia is now abandoned or in disrepair. Savvy investors can easily take advantage of this situation by taking physical possession of and acquiring formal property rights to abandoned land. With no formal property rights system in place prior to the disaster, control of the land will lie in the hands of an investor with the ability to access the land and apply for a title. Wealthy investors are better positioned to navigate the complex regulatory processes of developing countries quickly. These investors would not have been able to acquire formal property claims prior to the tsunamis because informal communities maintained internal protections and regulations that prevented outside infiltration. With the majority of this informal infrastructure and any records of its existence gone, investors have an opportunity to move in to seize valuable land.

Establishing and protecting formal property rights in developing countries will not only expand the income potential of individuals now relying upon informal mechanisms. National governments will also benefit from an enlarged formal market that adds revenue for social programs, generates foreign direct investment opportunities as a result of additional formal collateral, and increases export revenue.<sup>17</sup> Informal entrepreneurs unable to secure credit, if given legal titles, could expand their business, receive credit and foreign investment, pay taxes, and produce goods or services for export beyond the local community. In addition, providing formal title to these properties can have a lasting and significant positive impact on the value of the land itself. For example, landowners holding legal titles invest more in their property and are free to enter into long-term rental or lease agreements.<sup>18</sup>

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But registration is only the first step. A recent World Bank survey of world business in 2005 suggested that the economic benefits are much greater when the process of formalizing property rights is accompa-

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nied by improvements in the land registry, the collateral registry, the courts, and employment regulations.<sup>19</sup> Simplifying regulations, making registration more efficient and cost-effective, and educating informal communities about the benefits of registration will rapidly increase the pace of development in many Southeast Asian nations.<sup>20</sup>

Now is a critical time to begin these reforms.<sup>21</sup> The tsunamis that destroyed much of Southeast Asia and its informal economies have rendered property in the region vulnerable to outside interference. The loss of these informal settlements and businesses will have destructive effects on national economies because so much of the formal economy relies on informal production of goods, such as agricultural products and textiles, and because informal economies counterbalance shortfalls in national social support systems with local social safety nets. These communal support systems may now be lost. New investors may have good intentions and desire to replace informal businesses and settlements with productive retail shops or factories. For local informal property owners, however, domestic production that redistributes income is better than the capital flight that accompanies foreign-owned businesses. In essence, dead capital is better than no capital.

Southeast Asian governments must take immediate action to protect exposed land and grant formal titles to previously informal owners.<sup>22</sup> This can be achieved with a two-step process. First, foreign assistance in the form of capacity building should be requested immediately while the influx of aid is at its peak. Capacity building involves assistance that is intended to teach or provide tools to a community or government that will improve the ability to bring about positive economic change. These efforts often take the form of legal or regulatory reform, and in this situation would likely involve training by legal and land administration experts to improve cadastral development. Foreign aid agencies and non-governmental organizations have provided much of the necessary funding for basic food and healthcare following the tsunamis. Their priorities should begin to shift toward the provision of capacity-building assistance to help local communities rebuild. This technical assistance will help to establish a workable land tenure system that accounts for and records all property. Second, a survey of the regions affected must be completed to identify individuals who previously occupied currently uninhabited lands. These surveys, similar to censuses, can be used to map out both the land occupied by surviving informal titleholders as well as land that

has no recognized owner, which should escheat to the state rather than be left to foreign control.

Many successful models and high-tech programs exist to aid in the mapping process, but even basic inquiries into the settlement communities could provide the land demarcations that are necessary to begin the recording process.<sup>23</sup> For example, a project jointly funded by the World Bank, the Australian government (AusAID), and the Royal Thai government worked to accelerate the issuance of land deeds and produce cadastral maps using a uniform mapping system in rural and urban areas of Thailand. The project was completed last year and successfully registered about 13 million parcels with formal deeds.<sup>24</sup> In some other parts of Southeast Asia, reform efforts are underway to register vast informal land markets. However, most projects are gradual and several tsunami-ravaged countries have not initiated such efforts.<sup>25</sup>

With so many informal property records lost, competing claims to remaining land will likely arise. To adjudicate disagreements in the post-tsunami context, efforts to create land settlement agencies must begin immediately.<sup>26</sup> One possibility is the establishment of a land tribunal through which community leaders in each district would hold public town hall-style meetings to hear claims. At these informal property registration tribunals, witnesses would provide evidentiary support for informal property claims and tribunals' decisions would result in formal titling and enforcement by the state. Controls would have to exist to ensure fair decisions, including the careful selection of arbiters as well as guidelines for how best to weigh evidence. All of this could be initiated at a minimal cost with the help of legal technical assistance.<sup>27</sup>

Many development agencies have started organizing requests for capacity-building projects in Southeast Asia, including programs to rebuild local governments in Banda Aceh and provide computers for disaster management.<sup>28</sup> Because many regional governments have their hands full rebuilding in the aftermath of the disaster, international aid agencies and organizations must take the lead in bringing expertise and funding to the region devoted to putting a land tenure system in place. Groups such as the American Bar Association, the World Bank, and international legal societies should recruit attorneys and property experts for the critical first phase of this necessary step in the rebuilding of Southeast Asia.

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At the same time, NGOs and other assistance groups that intend to engage in relief efforts must bear in mind the potential for resistance

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from host country governments. Debt relief, health care, and other priorities may overshadow the importance of informal property registration for the political leadership. Emphasis must be placed

on the economic benefits that could result from reduced regulations, estimated by the World Bank to amount to a 2 percent annual GDP increase, and efficient land registration, which can “significantly increase land values and investment.”<sup>29</sup>

Many informal settlements may be gone for good, but remaining informal landholders can be protected now. Taking these steps immediately is not only the most reasonable approach to restoring pre-tsunami local production, but also provides a framework for growth that will enable increased participation in the formal economy and spur economic development. Rebuilding without focusing on future development needs will squander the vast influx of development aid and place Southeast Asia on a path to stagnant growth.

Taking advantage of this opportunity is one of the most important steps toward the development of the region. Recognizing this fact and acting now will help Southeast Asia to integrate into the world market through economic development and poverty reduction. The tsunamis of 2004 claimed at least 200,000 lives; the resulting impact on informal property holders has the potential to destroy millions more. ■

## NOTES

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<sup>1</sup> Hernando de Soto, *The Mystery of Capital: Why Capitalism Triumphs in the West and Fails Everywhere Else* (New York: Basic Books, 2000).

<sup>2</sup> For example, see Ernesto Zedillo. “Making Businesses Work for the Poor,” *Forbes*, 29 March 2004, 35.

<sup>3</sup> Klaus Deininger, *Land Policies for Growth and Poverty Reduction* (Oxford: Oxford University Press, 2003), 22. Sjaastad and Bromley define property rights more formally as “social conventions backed up by the power of the state or the community (at various levels) that allow individuals or groups to lay ‘a claim to a benefit or income stream that the state will agree to protect through the assignment of duty to others who may cover, or somehow interfere with, the benefit stream.’” Daniel W. Bromley and Espen Sjaastad, “Indigenous Land Rights in Sub-Saharan Africa: Appropriation, Security and Investment Demand,” *World Development* 25:4 (1997): 549-62.

<sup>4</sup> De Soto, *The Mystery of Capital*.

<sup>5</sup> For example, see “In the Shadows,” *The Economist*, 17 June 2004, 76. See also Diana Farrell, “The Hidden

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Dangers of the Informal Economy," *McKinsey Quarterly* 3 (2004): 26-37.

<sup>6</sup> World Bank, *Doing Business in 2005: Removing Obstacles to Growth* (Washington, DC: Oxford University Press and the World Bank, 2004).

<sup>7</sup> Hernando de Soto refers to dead capital as "assets that cannot be used to their fullest." See Hernando de Soto, interview with *ReasonOnline* (<http://reason.com/DeSoto.shtml>). That property is considered dead capital should not be confused with productive capacity. Much of this informal land is used for businesses that are essential to local, and often national, economies. For example, see Kerry A. Dolan, "Waking Dead Capital," *Forbes*, 15 May 2000, 98-105.

<sup>8</sup> Hernando de Soto interview with *ReasonOnline*.

<sup>9</sup> World Bank, *Doing Business in 2005*, 34.

<sup>10</sup> As *ReasonOnline* notes, "If you go and try to expropriate one of these people and send in troops to do so, your soldiers will come back in boxes. There is no way to touch these entrepreneurs. They get together and defend their private property with guns." See Hernando de Soto interview with *ReasonOnline*.

<sup>11</sup> A.T.M. Nurul Amin, "The Informal Sector in Asia from the Decent Work Perspective," International Labor Organization (Geneva: ILO, 2002), 13. Friedrich Schnieder calculates that the informal economy in Thailand, at 52.6 percent of GDP, is the largest informal economy in Southeast Asia, followed by Sri Lanka (44.6 percent of GDP) and the Philippines (43.4 percent). See Friedrich Schneider, "Size and Measurement of the Informal Economy in 110 Countries," *Workshop of Australian National Tax Center* (Washington, DC: World Bank, 2002).

<sup>12</sup> STAT Working Paper 1 (2002): ILO Compendium of Official Statistics on Employment in the Informal Sector, Table 4a [online database], International Labor Organization Bureau of Statistics, 2002. <http://www.ilo.org/public/english/bureau/stat/papers/comp.htm>.

<sup>13</sup> "Land and Freedom: Vietnam's land shortage is leading to all manner of shenanigans," *The Economist*, 13 June 2002, 44.

<sup>14</sup> The ADB reported that GDP growth in 2003 for all of Asia was 6.3 percent, led primarily by China, Thailand, India, and Vietnam. See "Developing Asia and the World," *Asian Development Outlook 2004* (New York, Oxford University Press, 2004), 3.

<sup>15</sup> World Bank, *Doing Business in 2005*, 34.

<sup>16</sup> Less than 1 percent of the affected population in Sri Lanka had property insurance. As a result, few of the 93,000 destroyed houses in the country will be rebuilt using capital from insurance payouts. See "Estimating Losses from the 2004 Southeast Asia Earthquake and Tsunami," *RMS Special Report* (Newark, CA: Risk Management Solutions, 2005).

<sup>17</sup> Kate Dalrymple, Jude Wallace, and Ian Williamson, "Land Policy and Tenure in Southeast Asia," (paper presented at the 3rd Regional FIG Conference, Jakarta, Indonesia, October 2004), 4.

<sup>18</sup> J. Michael Graglia, "At the End of the Beginning: The Formalization of Property Rights in Emerging Markets," 2002 *Chazen Web Journal of International Business* 3 (2002). For another example, see World Bank, *Doing Business in 2005*, 33.

<sup>19</sup> World Bank, *Doing Business in 2005*, 3.

<sup>20</sup> *Ibid.*, 5.

<sup>21</sup> Several relief groups have noted the need for provisions of relief aid to informal landowners. For example, see "Asian Coalition for Housing Rights for British Donors about how to support the Tsunami Relief and Rehabilitation Process in the affected countries of Asia," *Homeless International*, 12 January 2004. [http://www.homeless-international.org/doc\\_docs/ACHR\\_TsunamiReport5513.doc](http://www.homeless-international.org/doc_docs/ACHR_TsunamiReport5513.doc) (hereafter *ACHR Recommendations*).

<sup>22</sup> This point is also made by Chinua Akukwe, "Asia Tsunami Disaster: International Development Implications," *Worldpress.org* 3 March 2005. <http://www.worldpress.org/Asia/2032.cfm>.

<sup>23</sup> For example, see Hernando de Soto, *The Other Path: The Economic Answer to Terrorism* (New York: Perseus Books Group, 2002).

<sup>24</sup> Chakriya Bowman, "Thailand Land Titling Project," (Washington, DC: World Bank, 2004), 1.

<sup>25</sup> For instance, Indonesia, Thailand, Laos, and the Philippines have all undertaken some land reform in the past twenty years. However, many countries, including Malaysia, East Timor, Burma, Cambodia, and Brunei, all of which were affected to some degree by the 2004 tsunamis, have failed to undertake significant land policy reforms aimed at registering informal property. For example, see Chris Grant, "Lessons from SE Asian Cadastral Reform, Land Titling and Land Administration Projects in Supporting Sustainable Development in the Next Millennium," (paper presented at the UN-FIG Conference on Land Tenure and Cadastral Infrastructures for Sustainable Development, Melbourne, Australia, October 1999).

<sup>26</sup> For example, see Anne-Marie Brits, Chris Grant, and Tony Burns, "Comparative Study of Land Administration Systems," (paper presented at the Regional Workshops on Land Policy Issues, June 2002). See also Chakriya Bowman, "Scaling up Poverty Reduction: A Global Learning Process and Conference Thailand Land Titling Project," (paper prepared for the Conference on Upscaling Poverty Reduction, Shanghai, China, May 2004).

<sup>27</sup> *ACHR Recommendations*, 34.

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<sup>28</sup> For example, see "South and Southeast Asia Earthquake and Tsunamis," *USAID Tsunami Reconstruction*. [http://www.usaid.gov/locations/asia\\_near\\_east/tsunami/proposal.html](http://www.usaid.gov/locations/asia_near_east/tsunami/proposal.html). See also "Aceh Emergency Response and Transitional Recovery Program," *Aceh Update Report*, United Nations Development Program. [http://www.undp.or.id/tsunami/view\\_update.asp?date=20050224](http://www.undp.or.id/tsunami/view_update.asp?date=20050224).

<sup>29</sup> World Bank, *Doing Business in 2005*, 33.