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Property Economics versus New Institutional Economics: Alternative Foundations of How to Trigger Economic Development

Otto Steiger

The ex-communist [and developing] countries are advised to move to a market economy, and their leaders wish to do so, but without the appropriate institutions no market economy of any significance is possible. If we knew more about our own economy, we would be in a better position to advise them.

—Ronald Coase, "The Institutional Structure of Production"

What are the core economic principles to be implemented for protected transactions in developing and transitional countries to trigger economic development? In recent decades, two approaches have been developed which claim to answer this question: (i) the theory of property rights, or new institutional economics, originating from Armen Alchian (1977) and Harold Demsetz (1967; see also Alchian and Demsetz 1973) and developed by Nobel laureate Douglass C. North (1973, with Robert P. Thomas; see also North 1981 and 1990)[1] and (ii) the property-based theory of the economy, or property

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economics, developed by Gunnar Heinsohn and Otto Steiger (2004, 2003, 2006a, b, and d; see also Stadermann and Steiger 2001 and Steiger 2006a), with similar contributions by Hernando de Soto (1989 and 2000), Tom Bethell (1998), and Richard Pipes (1999).[2] The analysis of the institution of property forms the core of both schools. They maintain that property is the most important source of economic activity.

Although economic development is only one of the topics of their theoretical framework, both schools claim to answer Richard Easterlin's (1981) seminal question, "Why Isn't the Whole World Developed?" New institutional economics focuses on the traditional dichotomy of economics between *private*, or *individual*, and *common*, or *state*, *property*, both defined as the right to the physical use of resources, including the returns thereon, and the right to their exchange or alienation and that to their change. Challenging this dichotomy as being of secondary importance only, property economics differentiates between *property*, defined as the rights of burdening and encumbrance (or collateralization) and that of exchange (or alienation), rights that do not touch resources, and *possession*, defined as the *only* right to physically use resources and the returns thereon, including the right to change their form and substance. As a right, possession is bound to property.[3]

The term *possession* is unknown to economic scholars of past and present (see, however, Epstein 1998 discussed in the subsection on "The Fundamental Flaw in New Institutional Economics: The Missing Distinction between Possession and Property"), and burdening and encumbrance have never been discussed in their analyses of property—not even in the new institutional economics' theory of property rights.

The paper is organized as follows: the first section presents the fundamentals of property economics, and the second presents those of new institutional economics as alternative explanations of economic activity in the underdeveloped world, whereby institutional economics is analyzed from the viewpoint of the core of property economics—the distinction between property and possession. On the basis of the different approaches to economic development made by the two schools, the third section evaluates reform and development programs of multilateral institutions with a view to their suitability to trigger economic activity.

The Property Theory of the Economy, or Property Economics

Unlike new institutional economics, the school of property economics does not neglect the distinction between property and possession. It rather makes this distinction the basis of its theory, which intends to answer what Heinsohn and Steiger regard as economic theory's core question and, thereby, is fundamental in explaining business or economic activity: which is the loss that has to be compensated by interest? The property theory of the economy accepts neither a temporary loss of goods, as in neoclassical, nor a temporary loss of money, as in Keynesian economics, as being the cause of interest. When money is created in a credit contract, property economics holds, the loss causing

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interest is the loss of an immaterial yield which is called *property premium.* In the money-creating and the money-lending credit contract, property has to be burdened and encumbered. By burdening and encumbrance, the freedom of property is temporarily blocked, that is, the property premium is given up.

The Distinction between Possession and Property

A property premium automatically arises whenever property titles are added to possession titles to resources and goods. This is usually done by discontinuous, not incremental, change. It is a legal act, which makes the difference between mere possessional systems of production and a genuine economy in which agents' activities are always property driven. Correspondingly, the economy, not production as such, disappears when property is abolished. It goes without saying that this theoretical analysis is of utmost importance for the appropriate establishment of property reform programs in the third world and transitional countries.

According to Heinsohn and Steiger, mankind knows three idealized distinctive systems of material reproduction—that is, production, distribution, consumption, and accumulation—only one of which involves economic activities. It is important to note that the three systems are distinguished by their different socio-institutional structures: (i) the customary, or tribal, community regulated collectively by reciprocity and implying redistribution; (ii) the command, or feudal seigniority, regulated by coercive redistribution; and (iii) the property-based society regulated by interest and money in the form of collateral-based contracts and with no redistribution.[4] While the first two systems know of possession only, with common and individual rules of its not-free members—rules that cannot be enforced by independent law—the third system knows of property *in addition* to possession, with common and private rights of its free citizens that can be enforced by independent law. And while the possession-based systems—(i) and (ii)—only allow for the physical use of goods and resources, including the appropriation of the returns thereon and the change of their substance and form—goods and resources which cannot be alienated by sale and lease, the property-based system turns goods and resources into commodities and assets. Unlike mere goods and resources, commodities and assets cannot only be used physically, with the returns thereon appropriated and their substance and form changed, but they can also be sold and leased, burdened and encumbered (see overview in table 1).

With regard to economic development, the difference between the possession-based systems of material reproduction and the property-based system is a fundamental, not a gradual, one. While possession-based communities and seigniorities, like most of today's third world and transitional countries, may run undisturbed for very long periods of time, their lack of genuine property rights condemns them to a mere control of resources. In these territories, accumulation and, hence, economic development require previous savings, while the property-based society enables accumulation without such reduction in consumption by simply burdening and encumbering assets.

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Table 1. The Dividing Line between Possession-Based Systems and the Property-Based Society

Possession-Based Systems with Mere Reproduction	Property-Based Society with Economic Activities
Possession is the basis of material reproduction in animal systems as well as in human systems based on reciprocity (tribal community) or command (feudal/ socialist seigniority), in which property is missing. *Only* possession exists. The informally respectively arbitrarily set rules determine who, in what manner, at what time and place, to what extent, and by exclusion of whom may physically use goods and resources and change their substance and form.	*Property* is the basis of material reproduction in the property society ("capitalism," "market economy," "monetary economy"), where it transforms rules of possession into rights of property. Property exists *in addition* to possession.
Possessory rules refer to the nonlegal material use or control of goods and resources including the returns thereon and their alienation. Alienation here does not mean exchange in the form of sale and lease but only gifts, assignments, and—occasionally—inheritance. Per se these rules are not capable of generating a genuine economy, with interest and money as its most obvious characteristics. Ironically, mainstream economics applies the term "property rights" to mere possessory rules. These rules exist in the form of common and individual—exclusive—rules.	*Property rights* are de jure claims. They entitle their holders to immaterial (nonphysical) capacities which first constitute economic activities: (i) to burden property titles in issuing money against interest; (ii) to encumber these titles as collateral for obtaining money as capital; (iii) to alienate or exchange including sale and lease, and (iv) to enforce. Property rights transform possessory rules into possessory rights regulated by law. Thus, individual rules become private rights. Property rights transform goods and resources into saleable commodities and saleable and rentable assets.
Means of Regulating Material Reproduction (Production, Distribution, Consumption, and Occasional Accumulation)	Means of Regulating Material Reproduction (Production, Distribution, Consumption, and Accumulation)
"Inborn instincts" (animal kingdom); custom an reciprocity (tribal community), and commands or plans (feudal/socialist seigniority) as power relations of nonfree persons are the nonlegal rules of reproduction. Independent courts of law are absent.	Credit, sales, lease, and employment contracts form a legally determined network of rights between free, private individuals on markets necessary for reproduction. Independent courts of law overrule custom and power relations.
Burdening and encumbrance of property titles, interest and money, assets and liabilities, credit and banks, prices and markets are as much absent as the advantage-seeking *homo oeconomicus*. The rules of reciprocity (tribe) or command (nobility, "proletariat's avant-garde") determine the production of goods and their distribution for individual consumption, for common storage, and—occasionally—for common production goods or means of production. Therefore, storage and accumulation requires previous savings or a lower level of individual consumption.	The power to burden and encumber property offers an immaterial yield, the property premium. By burdening property for issuing money-notes—"notated" titles to property—in a credit contract, both lender and borrower have to give up their respective property premium, that is, they temporarily lose the freedom to burden, encumber, or sell it. The encumbrance of the borrower's property secures the lender's claims and, thereby, the circulation of the notes. The burdening of the lender's own capital, the net worth of his property, enables him to withdraw from circulation the notes that have not been paid back and also to redeem the notes.

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Table 1—*Continued*

Possession-Based Systems with Mere Reproduction	Property-Based Society with Economic Activities
Exchange of goods is not a primary task. When exchanged at all, they serve to strengthen loyalty. Interest-free intertemporal lending of goods to overcome individual difficulties is bound to the obligation of mutual assistance. Common difficulties are resolved by handing out rations that are to be replenished later, either voluntarily (tribal community) or by command (feudal seigniority). Possession-based systems are forced to develop a social safety net for its members, although this can be achieved on a very low material level only.	The lender is compensated for his burdening with interest, the borrower for his encumbrance with the money-notes' immaterial yield, the liquidity premium. Their capacity to finally settle contracts, that is, to finally sell or release property is due to the fact that money itself is a title to property of its creator. During the period of the loan, lender and borrower continue the physical use of the possessory side of their burdened assets. Since money is a derivate of assets (property) and not of goods (possession), accumulation can start without previous savings. Although needed, no social safety net can be developed from within the property-based society.

Source: Heinsohn and Steiger 2006a, 26-28.

Property economics verifies its analysis of the lack of property rights in possession-based systems by anthropological studies of tribal communities and economic-historical studies of command seigniorities in antiquity, the Middle Ages, and modern times, especially that of state socialism. Heinsohn and Steiger's approach also reveals why today no worthwhile economic activities take place in the underdeveloped parts of the world.

The Property Theory of Interest and Money, or the Core of Property Economics

Property economics aims to demonstrate the inability of traditional economic research to understand the institution of property and the problem of how to trigger economic activity. Although the eminent mercantilist James Steuart ([1767] 1993) had already developed fundamental insights into the importance of the property title of collateral for a genuine monetary economy, it took more than 200 years, until a few Keynesian economists, with Nobel laureates John Hicks (1981, 153) and Joseph E. Stiglitz (1981, with Andrew Weiss) as the most prominent ones, showed a renewed interest in collateral. However, until now and not unlike new institutional economists, they have failed to understand the essence of this title as a property title.[5]

With the distinction between possession and property in mind, Heinsohn and Steiger have formulated their property theory of the economy as the property theory of interest and money (see also overview in table 1). As each and every agent in this economy needs money, the authors started their approach with the system's bank of issue, today the central bank. As the prime creditor in the economy, this institution, sometimes even the state, has to set the standard necessary in all contracts, the money of account[6] to which the money proper—its banknotes—is related. In the money-creating credit contract,[7] with a commercial bank as its counterparty, the bank of issue has to obey two rules: (i) to secure its loans and, thereby, safeguard its reserves or "own capi-

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tal"[8] by claiming collateral—a property title—from the commercial bank and (ii) to burden its own capital, again a property title, to withdraw notes in case of any debtor's default and, thereby, guarantee the circulation of the notes forwarded to its sound debtors (see more detailed Heinsohn and Steiger 2006c).

The second of the above rules implies that the bank of issue incurs a loss of property premium by burdening its capital, which is compensated by the rate of interest charged to the commercial bank. The first rule implies that the latter bank incurs a loss of property premium by securing the loan through collateral, like the underlying asset in a repurchase agreement[9]—a loss which is compensated by the liquidity premium of the borrowed banknotes, money's capacity to finally settle contracts. This means that money is capable of finally selling or releasing property because it, itself, is a title to property of its creator.

In the following stages this process is repeated. The commercial banks lose property premium and are compensated by a (higher) rate of interest when they forward the money borrowed from the central bank in credit contracts to nonbanks, typically producers who, again, lose property premium and earn liquidity premium. With the money borrowed, producers start a monetary production which they have to sell on the market as commodities in sales contracts to earn the money they have to redeem with interest to the banks.

Why is this discussion of genuine money so important for economic development? Secured economic transactions, collateralized contracts, cannot be analyzed from the viewpoint of good securities alone. It goes without saying that the money claimed in sales and lease contracts and loaned in credit contracts has to be a genuine, or creditor's, money, a currency issued according to sound principles of banking, that is, not only against interest but also against good securities, and with sufficient capital of the issuing bank. Otherwise, contract partners would not exchange their valuable property titles against a domestic currency which, like the state, or debtor's, money[10] in most developing and transitional countries, is inferior, that is, nonconvertible to the currencies of developed economies and, instead, resort to them.

Furthermore, in addition to property titles to be used as collateral, titles suitable as the bank's capital also are needed to serve as a buffer for credit contracts that always involve the risk of becoming bad loans. Even in highly developed monetary economies, a lack of such titles often prevents entrepreneurs from getting access to the credit they need. It goes without saying that this presents a much greater obstacle in less developed countries.

Why is collateral so important for economic development? Could one not object that advanced economies do not just lend possession of already created goods but rather empower people to make new goods? Is collateral not only an indication of the bank evaluating a business plan, with the objective of reassuring itself that the applicant has been successful in the past? Such arguments were put forward by Joseph Schumpeter ([1911, 1926] 1934, 101; see more detailed Heinsohn and Steiger 2005, 68 f., 72, 78) in an analysis of the financing of the production of new goods by his famous "innovative"

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entrepreneur: "The frequent foundation of [the creation and lending of] money upon some kind of collateral only eliminates the insecurity which otherwise exists, but does not alter the fact that there is no new supply of products corresponding to the new demand for products proceeding from it."

Schumpeter fully understood that pledging of collateral has nothing to do with activating goods which otherwise would lie idle. Since, however, he did not distinguish a property title from a possession title, he did not comprehend what it is that is offered when collateral is pledged. Therefore, his denying the importance of collateral in the creation and lending of money nearly ends in a revival of the "real bills doctrine" of classical economics by which bills of exchange as "credit means of payment" are indeed based on already existing goods. As shown above, however, in a loan contract, the debtor only pledges the property side of his assets as collateral, whereas he continues undisturbed with the possession side of the very same assets, that is, with the possessory right to use the returns thereon. Schumpeter's innovative entrepreneurs may simply not want to pledge as collateral what they "may happen to own" (106) because they prefer the yield accruing of property unburdened and free, the property premium. But without collateralization, their bankers risk going into bankruptcy when their loans to the entrepreneurs turn bad. And in such case, even the most promising business plan would not help the bank.[11]

Backing by capital of the bank of issue and encumbrance by good securities of its counterparties, which are both property titles, are not only the fundamental requisite for the establishment of a genuine monetary system but also for any economic activity that triggers development, especially accumulation. However, the property theory of interest and money does not neglect the other side of the coin, the crisis, which it explains by the ever-prevailing tendency of both banks and producers in the property-based system to safeguard their assets by not providing loans and/or not running into debts. Therefore, the crisis cannot be solved just by the bank of issue reducing the rate of interest but at best by the state through loan-financed investments or through providing property titles to entrepreneurs in the form of "venture capital" financed by tax money. Furthermore, the institution of property does not develop a social security net out of itself. When introduced into possession-based systems, it rather destroys the existing, albeit low-level, schemes of social security, which can only be guaranteed by governmental institutions. Therefore, property economics does not neglect the state as a necessary institution both for the establishment and the survival of property rights.

My presentation of the core of property economics demonstrates that a theory of property rights, suitable for property reform programs, has to be based on the distinction between possession and property. Without this distinction, the essence of property law, the rights of burdening and encumbrance as the fundamental requisite for economic development, will not be understood. Even though one has to concede that new institutional economics makes a point of demonstrating the efficient use of resources by appropriate property institutions (see the following section), its emphasis on the physical use of resources, a possessional right, is at best a secondary element in the question of

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how to overcome underdevelopment. The school does not understand that, without a property law guaranteeing the rights to burden and collateralize assets, there will be no private but only individual use of resources. "Private," in the Latin sense of the word, means individuals' freedom from power relations, that is, the safeguarding, enforcement, and foreclosure of voluntarily established contracts on the basis of independent law. Without this law, property law, no efficient use of resources can be achieved, either. Rights of use cannot be implemented per se.

Further Approaches to Property Economics

Although de Soto, Bethell, and Pipes are not academic economists—de Soto is a former Peruvian entrepreneur and central banker, Bethell a former correspondent to *The Wall Street Journal,* and Pipes a renowned Harvard historian—their different explanations of the importance of property for economic development are very similar to Heinsohn and Steiger's theory. The difference between the authors from the Americas and the German authors is, first of all, a difference in emphasis.

While property economics analyzes the role of property with respect to the understanding of interest, money, and the economy, Pipes focuses on the relation among property, law, and freedom, with emphasis on independent law institutions that overrule power relations. His analysis, like that of Heinsohn and Steiger, draws on a clear-cut distinction between property and possession, especially exemplified by careful historical studies of England and Russia.

Bethell's approach, too, is based on historical studies—from the first property societies in ancient Greece and Rome to the more recent attempts to introduce property in developing and transitional countries, especially South Korea, Taiwan, and China. His emphasis is on the relation between property law and the economy. Although Bethell is influenced by the theory of property rights of new institutional economics, he does not follow North's approach (see the following section) of the importance of incremental economic change, the change of relative prices, as a necessary condition for the introduction of property law by civil authorities. Bethell rather demonstrates that, in analyzing the interaction between law and the economy, the former is far more important. Property rights, therefore, have always been introduced by discontinuous institutional change: through reform programs by governments from above or as a result of civil wars and revolutions from below.

De Soto emphasizes the relation between property and the economy, with emphasis on underdevelopment and, unlike property economics, not on the relation between property and the regulators of the economy, interest, and money.[12] His analysis, supported by references to successful property reform programs in history, especially the USA, Prussia, and Switzerland, is based on careful field studies by his Lima-based "Instituto Libertad y Democracia" (ILD) founded in 1980. The ILD has revealed that the poor in third world and transitional countries are not poor because they lack resources but because they are excluded from property rights. In his discussion, de Soto

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distinguishes not between possession and property but between informal and formal property. The widespread existence of informal property is seen as the basic cause of underdevelopment because it hinders the poor from collateralizing their resources to get credit for investments. However, de Soto's distinction between "informal" and "formal" property, albeit very similar to that of property economics, is misleading because it does not consider that informal "property," actually informal possession, still exists in the property-based system, where it is transformed, however, into formal possession and, thus, into a possessory right. De Soto's proposal for formalization preconceives the existence of formal property, property rights, without which possessory rights could not exist and to which they are necessarily related, for example, in a lease contract, where the rights of the tenant as the possessor of an asset is necessarily bound to those of his counterparty, the proprietor of the asset.

The contributions of Bethell, Pipes, and de Soto are not only important for our understanding of the institution of property but they also provide guidelines for the successful implementation of property law. After all, this is the most urgent problem involved in the fight against poverty in the underdeveloped territories of the world. Leaving history's discontinuous changes by forceful actions from above or below aside, Bethell and de Soto's discussions of property reform programs are especially enlightening because they focus not on property distribution but on the access to and acceptance of property rights by the poor.

The reforms of Eugen Huber in Switzerland in the early twentieth century deserve special attention, as emphasized by de Soto. Huber, a professor of law, had created the Swiss civil code (ZGB) of 1907, which at his time was regarded as the best and most modern property law. It decisively paved the way for the transformation of one of the most backward countries of Europe into today's most prosperous European economy. Why? As shown by de Soto (2000, 157, 171; see also Degiorgi 1988, 9–26, 94–111), Huber built a legal and political bridge from the more or less informal rights scattered in the different, possession-based rural areas of the country to one national property law. The law professor adjusted the Roman property doctrines of Swiss statutory law to the customs, rules, and behaviors of the mainly rural population by restraining the free disposal of property rights on agricultural land, especially with respect to inheritance law and the traditional social safety net.[13] Thereby, Huber contributed to overcoming the poor's fear of property as an institution threatening to destroy the social safety net which the possession-based systems guarantee after all, even though on a very low level.

The Theory of Property Rights, or New Institutional Economics

The Fundamentals of New Institutional Economics

The emphasis of the theory of property rights on institutional arrangements for the economic process is not new.[14] They had already formed the core of the approaches to

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economics by the German historical school and American institutional economics. However, while these approaches rejected the fundamental idea of neoclassical economics, namely, that of taking individuals and their preference functions as given, new institutional economics does not challenge this assumption. What it attempts is rather to extend the neoclassical model of barter exchanges by forcefully considering the neglected institution of property rights (Ménard and Shirley 2005b, 2). New institutional economics claims that only an appropriate analysis of these rights will allow transforming neoclassical economics into a mature theory of market economy, suitable for making the conditions for economic development understood.

New institutional economists regard property rights as an eternal and universal instrument of society to help its members deal with each other in economic exchanges. "This implies that it is *impossible not* to have a property rights system" (Demsetz 1998; emphasis added). *Property rights* are defined as an exclusive, transferable, and legal right to the physical use of scarce resources, the returns thereon, and alienation thereof. If this right is designated to a specific person, it is termed a *private*, or individual, property right, and a *common*, or state, property right if it is assigned to all members of "society."[15] The latter right is defined as a right without exclusivity of use. A resource to which a private property right applies is referred to as private property and, correspondingly, the application of common property right turns the resource into common property.

Unlike the neoclassical model, new institutional economics regards the way by which property rights are allocated and enforced as determined by transaction costs. There are inherent difficulties, frictions in economic exchanges, and, therefore, substantial costs in any attempt to allocate property rights. In the absence of an appropriate specification of rights, external effects result which need to be internalized by incentives. To economize transaction costs, wealth-maximizing individuals, therefore, substitute private property rights for common property rights as soon as they realize that the private rights leave room for unexploited gains of exchanges or benefits, that is, that the rights are not used efficiently because individuals cannot be excluded from an inefficient use. While Alchian and Demsetz consider this change in property arrangements as triggered by self-interest in the form of spontaneous order, North emphasizes that they are imposed on society by civil authority, the state, in the interest of individuals.[16]

The Explanation of the Emergence of Private Property Rights

In contradiction to Alchian and Demsetz, North's explanation of the emergence of private property rights is based on economic-historical studies identifying the causes of growth and stagnation of nations from the eighteenth century to our times. Only those countries were successful, he argues, whose governments had developed a structure of property rights that provided the incentives necessary for sustained economic growth, while those territories failed and remained in a state of "inefficient economic organization" in which the state, as can be verified by today's third world nations, did hinder the transformation of common into private property rights. Why? Because the govern-

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ments, looked at by North as wealth-maximizing agents, in these countries devised common rights in their own interests. However, even in the rare cases in history, for example, in late medieval England, where civil authorities supported the emergence of private property rights, the transformation has always been incremental, not discontinuous, that is, it cannot be implemented at will by the ruling class. North, therefore, emphasizes that without changes in relative prices that create incentives to construct the more efficient institution of private property, the state will never support this transformation by providing the necessary legal institutions. He verifies his thesis with the enclosure movement in feudal England in the thirteenth century, in which changes in the relative prices of land and labor induced both lord and peasant to seek a more exclusive use of land, which later was supported by the English crown.

Although new institutionalists correctly stress that the allocation of resources are more efficient with state-specified private property rights, they do not understand that the introduction of private property demands the implantation of laws which go beyond efficient organization. Furthermore, their analysis does injustice to both possession-based and property-based systems (see previous section). The connection between a lack of efficiency and a lack of specification of property rights is without foundation because there is always a possessor—as an individual or a collective—in systems which lack the institution of property. Efficiency, therefore, cannot be due to a superiority of private over common production activities.

For North, institutional change is always incremental. Although he concedes that a change in the property rights structure might also occur discontinuously, this possibility is forcefully ruled out without verification. On the contrary, discontinuous change by civil authorities is denied because this would endanger the interest of wealth-maximizing governments to preserve common property rights. But what about the Napoleonic laws that introduced private property in most of western Europe in the early nineteenth century, or the reforms of Heinrich von und zum Stein and Karl August von Hardenberg which induced the same change in Prussia in the same period? What about the similar reforms by Tsar Alexander II in Russia and the Tenno Meiji in Japan in the late nineteenth century and those of Huber at the turn to the twentieth century for Switzerland? And what about the land reforms by Syngman Ree in South Korea in 1949 and Chiang Kai-shek in Taiwan in 1953—not to mention the introduction of property reforms by the former *nomenklatura*, especially in China in the early 1990s after the fall of state socialism? And if a ruling class only purposed its own interest, one has to ask why it was not overturned by rebellions or wars, like the English feudal lords by the uprising of the Lollards under Wat Tyler in 1371, the starting point for the re-introduction of property in the form of private property in modern times? By the way, much the same rebellions and wars resulted, for the first time in history, in the introduction of private property in antiquity.

The new institutionalists' theory of property rights cannot explain the emergence of private property rights and, therefore, gives no hints to property reform programs in

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the third world and transitional countries. To explain the supposed blessings of private property, they should have distinguished between property and possession, which not to have done is their theory's fundamental flaw.

The Fundamental Flaw in New Institutional Economics: The Missing Distinction between Property and Possession

The inability of new institutional economics to distinguish between property and possession has been most clearly revealed by Demsetz (1998, 145), who has frankly admitted the difficulty of identifying the very core of property rights. Focusing on the use of the resource land, he wondered why "having" all property rights in the land is not necessarily the equivalent of being entitled to till a parcel of land. This can only be explained, he argued, by the fact that some persons "own"[17] the rights to land as a *common set* while others only "own" a *subset* of these rights. There exists, however, no common set of property rights to the land that can be divided into subsets, only a common set of possessory rights which as rights presuppose property. All and any assets have one characteristic in common: that of being "owned" by a proprietor *and* a possessor. And it is their rights that are different, not necessarily the persons to whom the rights are assigned. In the case of land, the right of property, the right to its encumbrance and alienation, and the right of possession, the right to till—to physically use the land—can be assigned to one and the same person. But both rights can also be assigned to different persons, for example, when the proprietor of the land rents it to a tenant. Then, the latter is the possessor of the land while the former remains its proprietor. The example also reveals that no possessory right can exist that is not related to a property right. Therefore, the right to change the form and substance of an asset, a possessory right, can always be restricted by the proprietor, for example, in the case of the lease of a house or flat.

What Demsetz should have looked for is the fundamental quality of property to constitute possessory rights and the right of the proprietor to burden assets—property titles —to create money and to encumber it for obtaining a money loan. To the best of our knowledge, neither this founding father of new institutional economics nor any other member of the school ever comes close to understanding property rights as a necessary precondition for possessory rights and to encumbrance and burdening as the all-important facets of property.

However, most recently Gary D. Libecap (2003, 153, 155), by referring to de Soto's approach (see previous section), has recognized the importance of collateral in an analysis of how to introduce property rights in a tribal community on the Amazon frontier. "Secure tenure, as represented by formal, enforceable title, will offer collateral for accessing capital markets for . . . investments and facilitate land sales."

Notwithstanding this most promising insight, Libecap did not make the potential of property to serve as collateral the fundamental characteristic of property rights. Instead, in his definition of property rights, he confused possession with property. Fur-

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thermore, he did not mention the right of encumbrance at all, and he only regarded the right of legal transfer as "the fundamental component" of property rights. "In general, the ownership of an asset consists of three elements: (1) the right to the use of the asset (*usus*), (2) the right to appropriate the returns from the asset (*usus fructus*), and (3) the right to change its form, substance, and location (*abusus*). This last element, which amounts to the right to bear the consequences from changes in the value of an asset, is perhaps *the most fundamental component of the right of ownership*. It implies that the owner has *the legal freedom to transfer* all or some rights in the asset to others at a mutually agreed-upon price" (2003, 145; emphases added).

It might be objected that "the right to change its form, substance and location" implies the right to collateralize an asset. However, collateralization is different from the right of change. Neither form, nor substance, nor location of an asset is changed when its proprietor uses it as collateral. Therefore, a further possible objection—the right of exchange includes the right to encumber—also misses the point. Both rights have in common that they do not change an asset, but, while the right of exchange implies a transfer of a commodity or an asset from one proprietor to another—from seller to buyer— the right to encumber leaves the asset in the hands of its proprietor, who can continue to exercise the right of use of such the asset inherent in its possession, for example, to appropriate the returns thereon.

One would expect that, by explicitly looking at the topic of possession, institutional economists would finally understand the difference between possession and property and would no longer lump possessional rights under the term *property*. In 1998, new institutionalist Richard A. Epstein devoted an entire dictionary entry to *possession*, to my knowledge the first time in an economic text. There he defined possession as "the source of all property rights" (62). This statement confirms that new institutional economics merely deals with the aspect of possession when it deals with the term *property*: "People own property so that they may possess it, just as they possess it, so they may use it" (68). The possibility of a separation between property and possession can only be seen in the author's analysis of the protection of possession in its transfer from one "owner" to another. However, the fundamental economic difference between a title to property that can be encumbered—this possibility was not even mentioned—and a right of possession to physical use never came to Epstein's mind.

In sum, new institutional economics never hints at the distinction between systems with informal, more or less arbitrarily set, rules of individual and common possession only and systems that are constituted by private and common property titles *in addition* to possession and transforming traditional rules of possession into private and common possessory titles.

Needless to say, new institutional economics gives no hint either to the core economic principles to be obeyed for protecting transactions in underdeveloped and transitional countries. The school's new look at the market as a system which can be organized most efficiently by a structure of hierarchical interwoven contracts leaves no room for

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turning the insights of this approach to property into recommendations for development and transformation policies. This holds true especially for the transaction costs approach to property rights as developed by Oliver Williamson (1975 and 1985), in which interventions by the state will always will result in inefficient outcomes and where, as emphasized by North (1994, 366), very little is known about how to create policies that significantly shape economic performance. In spite of its valuable insights into the necessity of expanding the neoclassical model of competitive equilibrium by the institution of property, demonstrating how the allocation of resources is influenced by transaction costs and incentives, new institutional economics cannot be taken seriously as long as it does not know that, unlike possession, property is not an eternal, universal institution but one which is man-made and which has to be introduced before the question of common versus private property rights can be discussed in a meaningful way.

Are Private Property Rights More Secure and, Therefore, Efficient than Common Property Rights?

The confusion of property with possession has also led to another weakness in new institutional economics: its sweeping assumption that private property creates security and leads to investment and, thereby, solves the problem of underdevelopment neglects the problem of insecurity when property rights are introduced. The supposedly causal connection between private property and investment has been questioned in a large number of field studies on land tenure in Africa, the most important ones being those by Gershon Federer and Raymond Noronha (1987), Richard Barrows and Michael Roth (1990), Susana Lastarria-Cornhiel (1997), Christian Lund (1998, 2000), and Alexandra von Bernstorff (2004).[18] Of these authors, Lund (2000, 10–19) provided a clear-cut critique of the basic assumptions made by the new institutional school, which is most suitable for the limited space of this paper.[19]

Lund (2000, 10) accused new institutional economics of "unwarranted simplification" of the tenure systems in the underdeveloped world. In Africa, for example, most "tenure systems are characterized by the existence of multiple tenure, that means, several users may have access to different resources on the land, one may farm, another gather fuel wood, a herder may be entitled to dry season grazing, and so on" (16). This tenure system implies a hierarchy between the rights of primary right holders (in the example: the farmers) and those of secondary right holders (the herders). However, when private property rights are introduced, the farmers' rights will be exclusive and the herders will be excluded from their rights. Therefore, privatization results in increasing tenure security for some persons only and, correspondingly, increasing tenure insecurity for other groups. As summarized by Lastarria-Cornhiel (1997, 1317) in a study on the impact of privatization in Africa: "With privatization, different rights to land have become concentrated in the hands of those persons . . . who are able to successfully claim their ownership right to land, while other persons lose the few rights they had and

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generally are not able to participate fully in the land market." Therefore, the assumption is questionable whether countries in sub-Saharan Africa will prosper by privatization. Lund (2000, 11–15) referred to Kenya, Burkina Faso, and Niger, where the supposedly causal connection between private land rights and plot yields could not be observed. With reference to field studies in Kenya, Uganda, and Zimbabwe, Barrows and Roth (1990, 289) also concluded that "the outcomes fail to measure up to expectations notably as regards higher investment and credit supply."

According to Lund (2000, 17), the meager success of privatization in Africa is due to a misunderstanding of property as a "thing": "either you have it alone . . . , or it is not yours at all." But "property is not a thing but a social relation . . . determining how rights to use and duties not to use a specific resource are distributed among people." However, Lund does not make clear what the social relation determining the rights to use land in Africa exactly is about. He only talks about the existence of "other types of tenure" on this continent that "are more certain for the rightholders." Therefore, "in Kenya it has often happened that buyers of land are not able to take possession of it. The local community simply does not accept that land is sold to a 'stranger'" (18). But why?

Like new institutional economists, Lund does not make a clear-cut distinction between possession and property. Therefore, he cannot understand that what we find in Africa is the typical conflict which arises when a reproduction system based on possession—in most cases common possession, where "land rights are typically defined for groups rather than individuals" (Feder and Noronha 1987, 143)—is "invaded" by a system based on property. As demonstrated in the previous section, even the most highly developed property-based society cannot establish out of itself a social safety net which, though on a very low material level and based on reciprocity, is the main characteristic of the possession-based community. What this means for property reform programs aimed at furthering economic development in the third world will be discussed in the following section.

Development Programs of Multilateral Institutions

Between 1970 and 2004 more than two trillion U.S. dollars have been poured into underdeveloped and transitional countries by the highly developed economies as development aid. This was mostly done by way of macroeconomic stabilization programs through governments and multilateral institutions like the International Monetary Fund or the World Bank. However, the programs did not touch the existing more or less possessional, microeconomic structures in the nations that received development aid. Here a little monetary restraint, there a minor fiscal stimulus, this was the slogan of an armada of development professionals. And do not forget liberalization of markets and, above all, privatization to make the programs workable, the experts advised. But to no avail: today, some 150 of the world's more than 190 nations still stay in a state of underdevelopment and poverty. Most recently, the United Nations in its Millennium

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Project has vowed to reduce poverty by 50 percent by the year 2015 (Sachs et al. 2005).[20] But by what means will this ambitious goal be achieved?

The analysis in this paper has revealed that poverty in the underdeveloped world is due to the missing institution of property. Only property triggers economic activity which, however, has not been understood, or insufficiently analyzed by economists of the past and the present—not to mention the development professionals in governments and established multilateral institutions. Therefore, in this section three different development programs will be analyzed which look for microeconomic alternatives to macroeconomic stabilization programs: (i) the property reform programs of the "Instituto Libertad y Democracia" (ILD); (ii) the social finance programs of the International Labor Office (ILO); and (iii) a development program proposed for the International Development Association (IDA) of the World Bank.

The Property Reform Programs of the "Instituto Libertad y Democracia" (ILD)

What are the guidelines for the property reform programs developed by de Soto's ILD as an alternative to the development programs of established multilateral institutions? First, the ILD (2003) claims to be committed to the poor, not to property. Therefore, it advocates the right of the poor to property, because the exclusion of the poor from a good property system is regarded as one of the most important causes of poverty.

According to the ILD, a good property system is defined as a system that triggers economic activity by property law, a law that provides and enforces rules and contracts: rules that organize the market as well as the titles and records to identify agents, and contracts that allow people to exchange goods and services as well as to apply for, and secure, credit. Furthermore, a good property system allows people to represent their resources in a standardized and universally accepted form and to store and transfer their value into capital assets. It is not enough to introduce property law; it has to be implemented as a law for each and every member of society. In most developing and transitional countries the law exists, but the majority of the people are excluded from it. They have no legal property rights to their resources and, therefore, remain poor. Any attempt to transform their informal possessions into legal property is connected with huge transaction costs, especially as shown by de Soto (2000).

The main challenge to property reform programs, according to the ILD, is the task of transforming the already existing extralegal, informal rights of the poor to their resources into legal, formal rights. Property reform programs of established multilateral institutions fail because they only document the already existing formal property, most of which belongs to the ruling class: the surveying, mapping, and modernization of property registries carried out by consultants and service companies financed by these programs.

According to the ILD, property reform programs, therefore, require that governments in developing and transitional nations obey the following seven rules, thereby always taking the existing extralegal structures as their starting point: (i) feasibility of the

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institutional change; (ii) technical ability to identify, locate, and classify rights over extralegal assets; (iii) reform of the legal system so as to make these assets legally acceptable; (iv) field operations of engaging the poor and bringing them to voluntarily accepting the rule of law; (v) removal of obstacles that hinder the legalization of the poor's informal possessions; (vi) specification of property documents in legal forms that make them usable for the generation of new wealth by transforming "dead" resources into "live" capital assets; and, last but not least, (vii) recognition of property documentation and records of the poor so that they can collateralize their assets and enter into credit contracts.

The ILD property programs, as the seven rules demonstrate, are first of all legal reform programs. They are based on the insight, emphasized by Bethell (1998), that law is superior to the economy and not the other way around as new institutional economics assumes. An appropriate implementation of property law—an institutional change that results in a changed microeconomic behavior of the poor by legalizing their informal, individual possessions into formal, private property—will suffice to trigger the economic activity lacking in developing and transitional countries. The activity cannot be induced by macroeconomic stabilization programs because they leave the property structure untouched. Furthermore, property law can only be installed by governmental-legal, that is, discontinuous changes.

However, while the property programs of the ILD are on the right track in grasping the core economic principles without which there will be no economic development, it has so far not succeeded in showing *how* to successfully implement these principles. It has only emphasized that this is not an easy task. Furthermore, the ILD has not paid enough attention to the huge transaction costs resulting from the implementation of property rights in systems based on possession, especially with regard to the risk of destroying the social safety net after all guaranteed by informal arrangements, which makes the poor hostile to property. On the other hand, the development programs of established multilateral institutions show that they are rightly criticized by the ILD, because they avoid the difficult task of turning extralegal possession into legal property.

The Social Finance Programs of the International Labour Office (ILO)

When discussing property reform programs in developing and transitional countries, one immediately recognizes a major constraint for economic development. The Geneva-based International Labour Office (ILO 2001 a and b, 2002) has identified this constraint as lack of collateral acceptable to banks for loans to, especially, small and medium-sized enterprises (SME). Like the ILD, the ILO is aware that many land and other possessors in the third world cannot borrow against their resources because these are not properly documented and that many others possess resources but are not their proprietors. However, the ILO forcefully rejects any proposal to overcome this problem by legalizing such informal "rights" and, thereby, transforming possessions into property. Instead, the ILO has developed so-called "social finance programs," more popu-

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larly known as "microfinance." The programs are aimed at circumventing the constraint the lack of collateral imposes on development by collateral substitutes in the form of peer pressure (joint liability), probation of credit scoring, interlinked contracts, and so-called "co-maker arrangement" without intended enforcement, where the sanction by the loan-giving bank is not foreclosure but rather the borrower's risk of no longer having access to credit.

However, what the ILO proposes with its programs amounts to nothing but the abandonment of the fundamental characteristic of property, its capability and right to encumber assets as the decisive precondition for economic activity. What the ILO does not understand is that the necessity of collateral is not due to asymmetric information between a bank and its borrower, the explanation by Stiglitz on which the ILO relies, but due to asymmetric distribution of risk between the counterparties in a credit contract (see the first section of this paper). Without collateral, the bank would risk its capital as soon as the borrower is unable to fulfill his or her obligations. And collateral substitutes cannot reduce this risk. Furthermore, as suggested by Graeme Buckley (1997, 1091), instead of relying on social finance programs whose "positive impacts for the supposed beneficiaries" show "little evidence . . . throughout Africa," attention should be "drawn to the availability and suitability of existing sources of finance, which may, paradoxically, be undermined by microfinance institutions" (see more detailed von Bernstorff 2004, 73–110).

The ILO's hope that collateral substitutes would enhance economic activity in developing countries is as naïve as the popular view that more wealth might be created by abolishing "unproductive" interest payments on loans. The social finance programs of the ILO have not hinted at the core principles of property at all; hence, they are not suitable for solving the problems of underdevelopment and transition. At best, collateral substitutes could be turned into customary rights, like possessory rights in tribal systems which, however, as has been demonstrated in the first section of this paper, are doomed to stay at a level of material reproduction that today would be called underdevelopment.

However, there exists an alternative to collateral substitutes which the ILO, unfortunately, does not discuss. Also in highly developed economies, SMEs, especially start-ups of young entrepreneurs, often face the problem that they lack collateral. How is the problem overcome? The state steps in as a substitute and guarantees the bank loan through a form of "venture capital." This means, of course, risking taxpayers' money (see first section). But this method is as social as collateral substitutes and, in addition, has the advantage of not violating the rule of property-based economy, which says that credit contracts cannot be established ex nihilo: they have to be based on property titles, that is, they have to be collateralized. However, there still exists another alternative to the lack of collateral which will be discussed in the following subsection.

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A Shift in the World Bank's Thinking on International Development Association (IDA) Programs?

Until most recently, the World Bank has devoted little attention to the importance of property rights for economic development. The last official pronouncement on property made by the bank was in its policy paper on land reform of 1975, which analyzed land rights more or less in terms of the physical use of land. Focusing on the question of who "owns" the land, the paper emphasized the scope for land distribution and not the access to property rights to land. It goes without saying that this approach was inappropriate, as agricultural use, a possession right, does not address the most important capacities of property rights to land for economic development: to be encumbered as collateral and to be burdened as capital.

Nearly three decades later, in a World Bank research report, Klaus Deininger (2003) dared a new look at property rights that might lead to a shift in the World Bank's thinking about how to further economic activity through its IDA development programs. The 2003 paper not only goes beyond the position in the 1975 paper but also reveals many of the insights of the theory of economics as formulated by property economics (see first section).

The focus of Deininger's analysis is on property rights to land or land rights, because land is the most important asset in developing and transitional countries. Because of its immobility and virtual indestructibility, land with secure, clearly defined, and easily transferable property rights is regarded as the ideal collateral. However, as pointed out in the first section, land in most parts of the underdeveloped world also serves as the only social safety net. Therefore, Deininger regards the collateralization of land as a remote option. Foreclosing on the land of the poor that have defaulted on credit would deprive them of their basic means of livelihood, with the result that only the rich would benefit from the possibility of collateralizing land.

As we have seen in the previous subsection, this is exactly the reason why the ILO favors social finance instead of property reform programs. Deininger does not follow the ILO's proposal of collateral substitutes. Instead, he suggests strengthening land rental contracts and markets. Because renting land requires only a limited capital outlay, the problem of lacking collateral is brought down to a minor scale without diminishing a tenant's incentive to invest in his or her rented land. While this proposal is sound—it can be supported, for example, by the successful introduction of private property in England in the sixteenth century, with the tenant as the first "capitalist" of modern times—Deininger's analysis of collateral is far from convincing. Drawing on Stiglitz' theory of credit rationing, with the explanation of collateral as a means against asymmetric information and moral hazard in credit markets, Deininger misses what is at stake: the asymmetric distribution of risk between the bank and its borrower (see the previous subsections "The Property Theory of Interest and Money, or the Core of Property Economics" and "The Social Finance Programs of the International Labour Office").

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Therefore, while Deininger's report may lead to a most promising shift in the World Bank's thinking on its IDA development programs in the direction outlined by property economics, its theoretical foundation needs to be developed more closely on the lines of that approach to make the programs a success.

Summary

On the basis of my discussion of the schools of property economics and new institutional economics and of the development programs of multilateral institutions, I emphasize the following three conclusions to be obeyed for property reform programs in the Third World and transitional countries:

(1) The core principles triggering economic activity are embodied in the institution of property that, both as common and private property, is created by men. At no time in history, and nowhere in the world, has property existed as common property that by incremental changes has been, or can be, transformed into private property; what has existed at all times and everywhere is possession, in both its forms of common and of individual extralegal possession. Therefore, recommendations for development programs based on new institutional economists' theory of property rights, favoring privatization, are misleading.

(2) The introduction of the institution of property into the merely possession-based systems of underdeveloped and transitional countries can occur only through discontinuous change of their governmental and legal structure into independent property law, with access to property rights and, thereby, possession rights also for the poor, as emphasized by property economics. Only such a reform would allow transformation of the poor's resources into assets, serving both as collateral for credit and as capital for securing loans and for creating a creditor's money.

(3) However, to successfully implement such a property reform is not a task which can be achieved by mere legislation or by programs of multilateral institutions. To overcome the hostility against property rights and their inherent possession rights in the underdeveloped parts of the world is a Herculean task which, even if not unsolvable, the latter institutions are the least appropriate to shoulder. Therefore, property reform programs can only support and strengthen governmental and legal structures in developing and transitional countries that are well-disposed toward property rights but which, at the same time, are able to respect the existing social relations of the extralegal possession-based systems. Furthermore, such programs will have to consider that the introduction of property rights does not constitute any social safety net but rather destroys the existing ones. And it is all these structures and relations which have to be carefully scrutinized before property reform programs can be discussed in a meaningful way.

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Notes

1. Armen Alchian and Harold Demsetz's ideas are influenced by Nobel laureate Ronald Coase's (1937 and 1960) transaction cost approach which, however, does not emphasize the incentive effects of private "ownership" as much as they do; see Demsetz 2003 (300). For the more recent development of the theory of property rights, which, however, does not change its fundamental ideas, see the collections by Terry L. Anderson and Fred S. Chesney (2003a) and Claude Ménard and Mary M. Shirley (2005a). While Anderson and Chesney regard the contributions in their volume by leading new institutional economists as the "basic text on property rights" (2003b, ix), Ménard and Shirley praise their collection as a book which "acquaints readers with the scope" and "recent trends" of new institutional economics "written by some of the foremost NIE [new institutional economics] specialists" (2005b, 3).
2. For a first, critical discussion of the different approaches of property economics, with contributions by all of its leading theorists, see the collection by Otto Steiger (2006a).
3. Therefore, when proprietor and possessor of a resource are not one and the same person, the right to change its substance and form can be restricted by the proprietor; see the more detailed section following.
4. The three systems are based on Karl Polanyi's (1944) seminal insight that *homo oeconomicus* is not a universal phenomenon. As distinct from Polyani, property economics terms only the socio-institutional structure of the property system a society and the other two a community and a seigniority, respectively, because, unlike the society, they are not based on free contracts entered into by its members; see Niemitz 2006. While Gunnar Heinsohn and Otto Steiger agree with Polanyi that the structures of the latter systems are determined by reciprocity or command, they are the first to reveal that the former system is based on the structure of property. Polanyi had only seen that reproduction in this "market society" can be characterized by exchange but could not find the socio-institutional structure he was looking for that makes exchange effective: the structure of property; see more detailed Heinsohn 2006.
5. While John Hicks emphasizes the neglect of good securities as the missing link between the financial and industrial sector in Keynesian macroeconomic theory, Joseph Stiglitz made collateral the fundamental of his theory of credit rationing. The necessity of offering collateral in a credit contract, in his approach, is explained by asymmetric information between the bank and its borrower. However, Stiglitz, failing to look at collateral as a property title, did not understand that without collateral there would be an asymmetric distribution of risk between the contract partners—a risk of loss that cannot be ruled out by symmetric information. Even with perfect information about the borrower, the bank cannot do without the pledging of its debtor's property titles. Otherwise, the bank would risk its own property titles, its reserves, as soon as the borrower were unable to fulfill his or her obligations.
6. The interesting question—where does the idea of a money of account come from?— has been answered by John Maynard Keynes in *A Treatise on Money* ([1930] 1971, 4, 10–12) with the help of Georg Friedrich Knapp's ([1905] 1924) state theory of money: to raise taxes, already the tribal community and the feudal seigniority needed a standard of measurement, the money of account. However, as shown by Heinsohn and Steiger (2003, 486), in such systems, preceding the property-based society, there existed no money standard by which values could be compared: items were just being counted, weighed, or measured as they stood. On the contrary, in the property-based societies of antiquity and modern times, it was private proprietors who, by establishing credit banks, first issued money proper as coins (antiquity) and as banknotes (modern times). And in *this* process of issuing money, they used the already existing standards of measurement—especially weights—of the preceding feudal systems as the name for their money of account, for example, the pound in early modern times.
7. Of course, money can also be created by buying property titles outright on the open market. But in such case, the problem arises that, to control the circulation of money, titles have to be sold outright on a regular basis.

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8. The term is borrowed from Ralph Hawtrey's analysis of the balance sheet of a central bank ([1932] 1970, 126), indicating that also a bank of issue needs a surplus of assets over liabilities, that is, a net worth as a buffer for bad loans. Nowadays, however, in the analysis of balance sheets of both banks and nonbanks, the term *capital* clearly stands for "net worth," and we will follow this practice.
9. A repurchase agreement is a form of secured loan. The bank of issue sells an asset to the commercial bank, with an agreement to buy it back later at the same price—while mortgage and charge leave possessory rights unaffected, pledge and lien deliver the possession of tangible property to the creditor. Collateral is not pledged as, for example, in a pawn shop, where the possessory right is blocked.
10. As demonstrated by Hans-Joachim Stadermann and Steiger (2001, 285–297; see also 2006), in a discussion of Keynes' state theory of money ([1930] 1971, 8–25; 1936, 200), not every medium called "money" is a genuine money. Genuine money means a creditor's money because it is a derivative of assets, that is, debt titles offered to the central bank by commercial banks, which are not the issuers but the creditors of these titles. On the other hand, state money is a debtor's money because the debt titles issued by the state are sold directly to the central bank, that is, without the laborious process of selling them to commercial banks on the capital market, which they can offer then to the central bank. Therefore, while in the case of a creditor's money the commercial bank is a debtor to the central bank, the bank is accepted by the central bank as counterparty only in its role as creditor to state-issued debt titles for which it, and not the state, is liable to the central bank.
11. It goes without saying that banks do not simply lend on collateral but always ask for a business plan. However, this does not mean that a most promising business plan can substitute for collateral. Therefore, even in the world's most advanced economy, collateralized loans "are commonplace, with about 70 percent of commercial and industrial lending in the US being made on a secured basis" (Kanatas 1992, I, 381). Most recently, the insight into the fundamental necessity of secured loans—and capital—in highly developed economies has been tremendously strengthened by the so-called *Basle II Accord* of the Bank for International Settlements (BIS), which will become effective in 2006; see more detailed Himino 2004.
12. In his most recent work, Hernando de Soto (2000, 56, 218) has recognized the striking similarity between his approach and that of Heinsohn and Steiger and accepted their property theory of interest and money.
13. In inheritance law, for example, in the case of several persons inheriting a farm, the farm was not divided into equal parts, but the first, and sole, heir had to compensate his brothers or sisters with a sum of money determined by the earning power, that is, the returns on the possession of the farm. No restraints were proposed by Huber that might endanger the fundamental property right of collateralization, as such is the case in many development and transitional countries where—for social reasons—real estate inhabited by people cannot be foreclosed on. Therefore, without collateral, rates of interest for money loans are sky high, as, for example, in most parts of sub-Saharan Africa: "The rates of interest charged . . . vary, ranging between 25% to 100%. The effective rate of interest on loans is estimated as much as 30% per month" (Nwanna 1998, 314).
14. This and the following two sections draws in part on Steiger 2006b.
15. Institutional economics applies the term "society" to all types of societal organizations, while property economics reserves the term to the property-based system only. Possession-based systems, which are not known to institutional economics, are characterized as reciprocity-based tribal communities or command-based feudal seigniorities; see "The Distinction between Possession and Property" above.
16. Because Alchian and Demsetz neglect the role of governmental institutions for the emergence of private property rights, their approach is characterized as a "naïve" theory. What they rely on is popular stories, such as Garret Hardin's famous "The Tragedy of the Commons" (1968), which show the overexploitation of resources under a regime of supposedly common property

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rights. However, Alchian and Demsetz do not know that Hardin's story is not about common property rights at all but analyzes what may happen in a feudal command system—a system that is based on possessory rules only, not even possessory rights: the tensions between extralegal common rules and likewise extralegal individual rules; see further "The Explanation of the Emergence of Private Property Rights" (later in this paper).

17. New institutional economics uses the term *ownership* as a synonym for property. In their property theory of interest and money, Heinsohn and Steiger speak only of *property*, not of *ownership*, because the latter term is ambiguous and means *both* property and possession. Their terminology has been followed in this paper.
18. For further references see Lund 2000 and von Bernstorff 2004.
19. For more detailed criticisms of new institutional economics, I refer to Barrows and Roth 1990, 266-269, and especially to von Bernstorff 2004, 111-156.
20. For a detailed discussion of the UN Millennium Project see Steiger 2006c; see also Heinsohn and Steiger 2006a, 196-197.

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