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## **Agricultural land market in Russia and large corporate farms**

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## Agricultural land market in Russia and large corporate farms

### 1. Privatization outcomes and incentives for land market development

In Russia in general, the share of land that is not publicly owned is as low as 7.6%. Privatization in Russia was mainly limited to farmland that was used for agricultural production prior to the reform. Here the share of privately owned land reaches 80% (Table 1). The second largest share of privately owned land accounts for land of populated localities where about 18% of land is privatized. Here, too, the land plots that were privatized were mainly those occupied by citizens' individual houses and those that were partly used for agricultural production. The rest of the land remained in public ownership.

**Table 1. Structure of ownership of farmland plots used for agricultural production**

operated by	total agricultural land		privately owned agricultural land	including land owned by operators	% of privately owned agricultural land	including % of land owned by operators
	mln ha	%				
citizens (not peasant farms)	34.2	18	16	15.6	47	46
peasant farms	19.5	10	11.9	6.5	61	33
large corporate farms	124.6	65	99.6	2.8	80	2
state-owned farms	13.3	7	0.9	0	6	0
total	191.6	100	128.36	24.9	67	13

Source: Federal state statistical monitoring. Form №22-3 (organizations). Data on rights enabling corporations, organizations, farms, societies involved in agricultural production to use land as of 1.01.06. Form №22-3 (citizens). Data on rights enabling citizens (groups of citizens) involved in agricultural production to use land as of 1.01.06. Form № 22-4 (organizations). Data on availability of land in use by corporations, organizations, farms, societies involved in agricultural production as of 1.01.06. Form № 22-4 (citizens). Data on availability of land in use by citizens (groups of citizens) involved in agricultural production as of 1.01.06.

This table shows that large corporate farms:

- Utilize about 65% of agricultural land;
- Use agricultural land that is in private property
- This means that this large corporate farms are strongly involved in transactions with agricultural land.

In addition, starting from 2001, the government has been attempting to include another 212.6 million of publicly owned land into land turnover. These are both agricultural and non-agricultural types of land that have been in a varying degree used by organizations

in their agricultural production process. These types of land had to be bought out or leased. Such supply volumes are usually considered detrimental for the market. However this land is dispersed among 56,400 organizations that have been exploiting this land exercising their right of use. And these organizations in particular have the right to buy out or lease this land. In other words, this land will not be available to the market in the true sense of the word.

## *2. Development of land market*

### 2.1. Law-permitted types of land transactions and constraints to the land market

At present, the legislation permits a wide variety of transactions in land shares<sup>1</sup> and land plots:

	Land share	Land plot
Sale	•	•
Transfer by way of gift	•	•
Lease		•
Transfer on terms of lifelong annuity	•	•
Investing in equity capital	•	•
Bequeathing	•	•
Using land as collateral		•
Trust management	•	•

The legislation is liberal – any citizen or organization (with the exception of those with the controlling interest owned by foreigners) can buy land.

Constraints to transactions:

- Transactions with land shares are only possible in favour of another member in jointly shared ownership, corporate or peasant farm that is using the land plot which is in jointly shared ownership of citizens. Otherwise the land share owner has to convert his/her land share into a physical land plot and only then make a transaction with it;
- If a land plot is to be sold, the priority right to purchase belongs to the respective municipal entity or oblast (a unit of administrative-territorial division in Russia). Only if the aforementioned entities refuse to purchase, the land plot can be sold to other individuals/entities;

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<sup>1</sup> shares in the right to joint shared ownership of a land plot, hereinafter referred to as land shares

- Foreigners and corporations where foreigners have controlling interest are banned from purchasing agricultural land plots;
- There are limitations on how much land a single individual (entity) can have in ownership.

However all these constraints are easily side-stepped and cannot be regarded as significant.

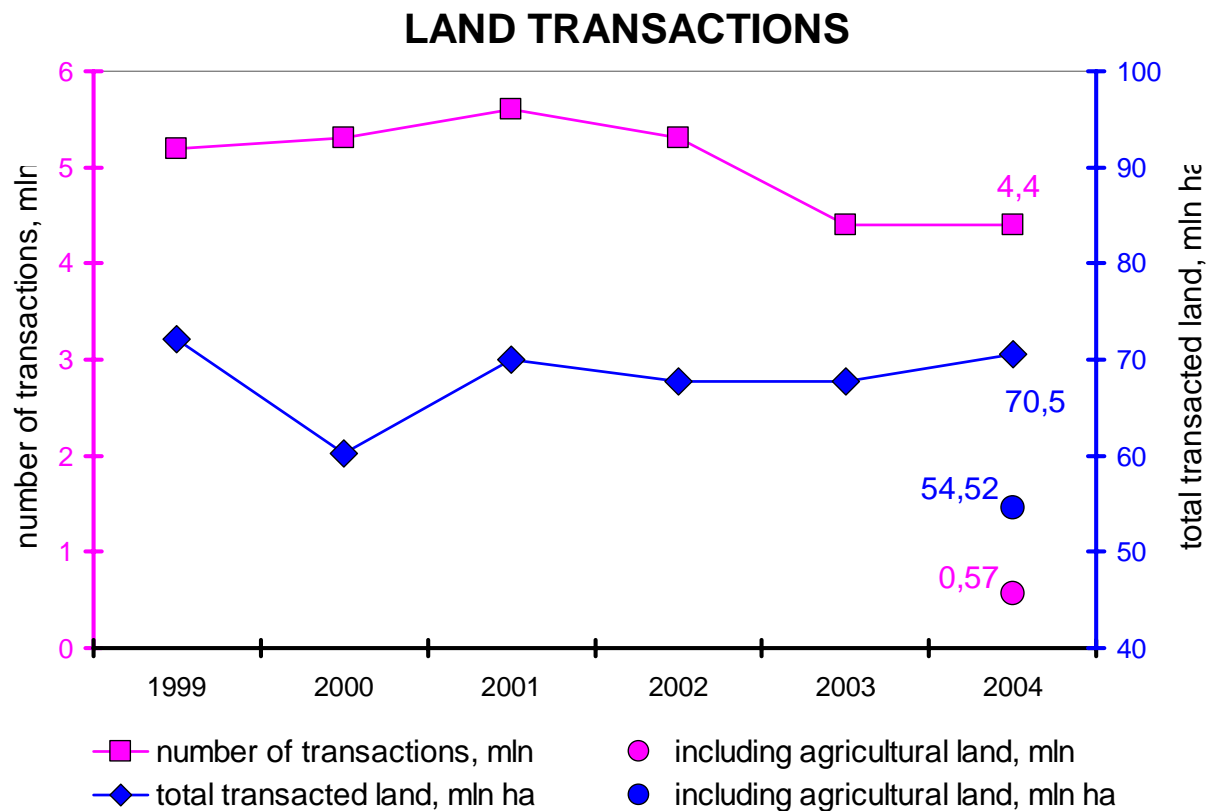
## 2.2. Amount of activity on land market

Official statistics keeps records of transactions in land plots only; transactions in land shares remain outside its scope. Since the majority of transactions are actually made in land shares (accounting for the territory of over 100 mln ha), one can conclude that no information on the bulk of the transactions is available at the national level.

### 2.2.1. Market of land plots

In 2004 (data for 2005 are not available), 1.2 million transactions in land plots were made involving altogether 12.3 mln ha or 0.7% of the Russian total land fund. The number of transactions in land plots was changing but the trend towards increasing size of transacted land plots remained unchanged:

Information on the transactions in all types of land is given in the following graph:



Transactions in agricultural land plots accounted for as little as approximately 4% of the total transactions. However these transactions involved 77% of the total transacted land. This is explained by the fact that the average size of a state agricultural land plot leased under one transaction was 585 ha, whereas one transaction in other types of land plots accounted for 4.4 ha. Transactions in farmland plots accounted for 28% of the total agricultural land. Information on types of transactions in agricultural land plots is given in Table 2.

**Table 2. Transactions in agricultural land plots**

Types of transactions	Number, mln (%)	Size, mln ha (%)	Average size of transacted land plot, ha
<i>in state-owned land plots</i>	0.19	54.31	292.9
% in total transactions in agricultural land	(32.6)	(99.6)	585.0
lease by peasant farmers and corporate farms	(16.3)	(99.6)	0.1
sale of land plots to citizens not registered as peasant farmers	(16.2)	(0)	25.3
sale of land plots to peasant farmers and corporate farms	(0.1)	(0.1)	
<i>in privately-owned land plots</i>	0.4	0.21	0.5
% in total transactions in agricultural land	(67.4)	(0.4)	

sale between peasant farmers and corporate farms	(0.3)	(0.1)	0.2
sale of land plots between citizens not registered as peasant farmers	(38.6)	(0.1)	28.3
transfer by way of gift	(4.7)	(0)	0.9
bequeathing	(23.8)	(0.2)	0.7
using as collateral	(0.0)	(0)	
<i>total transactions</i>	0.57	54.52	

Source: State (National) Report "On situation with and utilization of land in the Russian Federation in 2004". – M.: Federal Agency for Immovable Property Cadastre. – 2005 – 196 pages. P. 130-137

State and municipal farmland lease was the dominant form of transaction (92,800 contracts covering about 19% of land used by peasant and corporate farms were in effect in 2004).

The bulk of transactions made by private individuals involved buying and selling land plots between citizens, however, such transactions account for only 0.7% of the total land plots. This market can be considered the most developed as covert transactions in land plots through transactions in immovable property have been made in Russia at all times.

Transactions involving land plots used as collateral are practically non-existent.

At the same time, up to 2005, transactions in land shares involving their buying and selling and investing in equity capital of corporate farms were quite numerous in some Russian regions. Such transactions were most frequent around cities, particularly Moscow and Saint-Petersburg. There land is purchased for construction purposes. Despite repeatedly declared protection of agricultural land, farmland is being very easily removed from agricultural production.

Other regions where land shares are actively transacted are territories with conditions favourable for crops production and where intensive farming technologies can be used. New farm corporations and capital from other industries are moving to these territories. It is they, and not traditional agricultural producers, that are the entities which initiate land purchase in these regions.

The number of such transactions is not known. However, according to my experience, every time there was a buyer for land shares in Moscow Oblast (region) the number of refusals to sell did not exceed 15% of the total owners.

### 2.2.2. Prices

Statistics of selling prices is only available for state-owned land plots. This averaged as little as \$150/ha across Russia in 2004. For large farmland plots the average lease payment slightly exceeds the land tax and equals the land tax in most parts of Russia.

Information on prices for transactions between citizens, including peasant farmers and corporate farms is not available. Prices can be studied only on some pilot objects. For example, in Moscow region, taking into account the established practice of using farmland for non-agricultural purposes, the purchasing prices for land plots or rights to use land plots (land shares) for the period of 2003-2006 have become 20 times higher and reached on average of about \$3000 per land share, a standard land share size being 4-7 ha.

Market prices are not used to determine lease payments as, in fact, there is no somewhat developed market of leased land yet. Table 3 gives information on average lease payments.

**Table 3. Average lease payments for leasing state and municipally owned land plots in the Russian Federation, \$/ha**

Types of land plots	2004 (depending on location)	
	inside populated locality	outside populated locality
Land plots of citizens not registered as peasant farmers	61	29
Corporate and peasant farms	39	7
For reference: other companies	4286	582

\$1=RUR28. Source: State (National) Report "On situation with and utilization of land in the Russian Federation in 2004". – M.: Federal Agency for Immovable Property Cadastre. – 2005 – 196 pages. P. 132

The only prices that can be considered established are the prices for land plots of citizens not registered as peasant farmers. These land plots are, as a rule, occupied by houses. The prices are established because transactions in this sort of land plots have been made at all times – until 1990, it was the immovable property situated on the land plot that was sold and the right to the land plot passed to the new owner as a result of this transaction. The prices vary significantly depending on the location of the land plot.

Land plots of peasant and corporate farms are rarely sold. These land plots are quite different in quality. Therefore hardly anything can be said about their market prices at this stage.

### 2.2.3. Reasons for poor development of the land market



During the survey conducted in three Russian regions (with highly developed agriculture, medium agricultural development, and agriculturally depressed) covering 144 corporate farms, 206 peasant farms, and 187 household plots of citizens not registered as peasant farmers, the potential market players<sup>2</sup> named the following reasons – Table 4:

**Table 4. Reasons for poor development of land turnover**

Reason	Frequency of replies, %
no need	38
problems in connection with formalization of the transaction	31
too many land share owners	11
no information on what transactions are possible	10
ignorance of what selling prices and lease payments could amount to	10

Only in one of the three regions the respondents replied that they had been approached with an offer to buy, and only in one region (with highly developed agriculture) transactions involving purchase and sale of land took place. Citizens who most frequently pointed out that they might be willing to sell were household plot holders (citizens owning land plots and not registered as peasant farmers), i.e. owners of land plots with houses on them for permanent or summer residence.

Therefore the poor development of the land market is explained, firstly, by the fact that the demand for land to be used for farming by peasant or corporate farms exists only in certain Russian regions.

Secondly, the respondents noted that it was extremely difficult to make a transaction. If the whole land plot that is registered with the Cadastre were to be sold there would not be so many problems. However, as has already been mentioned above several times, all the land plots used by a peasant or corporate farm are entered into cadastral records as one unit. This unit of land (for example land used by a corporate farm) may consist of hundreds of land plots scattered all over a vast territory. In order to sell one field from this unit of land one has to prepare the documents necessary to register this field with the Cadastre (which is extremely expensive and takes a lot of time), collect a huge set of documents and spend a lot of time on formalization and registration of the transaction. Currently, problems are also arising in connection with the land plots that are already registered with the Cadastre. This is due to

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<sup>2</sup> BASIS Survey (2001-2005)

the fact that in 1998 the system of registration of rights changed and now the boundaries of all land plots have to be ascertained anew. Without this the right to land is not entered into the new Immovable Property Rights Register. In other words, the object of a transaction – a land plot – is not ready for the transaction. And this is a huge problem. This is the reason why de facto land is often used under a verbal arrangement.

The respondents also noted the lack of any market benchmarks to help them make a decision. They do not know where to get information on prices or demand. And this is an absolutely true observation. In Russia, accessible market information is not available. Consequently, similar land plots may be sold at significantly varying prices.

### 3. Opportunities for using land as collateral and specifics existing for farmland plots

The law allows a pledge (mortgage) of farmland. However the requirements enabling to use a farmland plot as collateral are quite severe: a pledge of share in the right to a farmland plot is not allowed (for other types of land this is possible), nor a pledge of a part of a farmland plot is allowed (first one has to get this part of land registered as a separate land plot to be pledged which takes up to 6 months and entails significant expenses).

Protection mechanisms designed to take control of or sell a pledged land plot do not make a pledge of land attractive for pledge holders unless he/she intends to retain the land plots if the loan is not repaid.

There is no limitation on loan types against collateral (for example loans to fund capital investments). Besides, the legislation requires the collateral to be insured otherwise the contract of pledge can be terminated at any point in time. The insurers, however, do not know what risks to insure in connection with a land plot. In fact, they have no practical experience in insuring farmland plots. Only few banks have a methodology for providing a loan to develop farmland.

As a result, lack of demand for land, absence of established prices for land plots, unavailability of finalized documents certifying the right to a land plot to be pledged often make a pledge of a land plot impossible. Corporate farms (controlling a larger part of the farmland) are unable to use land plots as collateral as these land plots are owned by citizens except for the 2% of the agricultural land that is in their ownership.

Recently, Russia has launched several national priority projects that will be funded from the budget. One of them is the project on Priority Development of the Russian Agro-Industrial Complex. This national project includes a pilot project on mortgage-based lending that is being actively implemented by *Rossel'khozbank* (the Russian Agricultural Bank). The bank developed lending methodology is filling in the existing legislation gaps. Moreover, the basis for successful mortgage development already exists which includes land plots of peasant farms and the 2% of the land used by corporate farms that is in their ownership. Two per cent may seem a low figure but in real terms it stands for 2.8 million ha which together with land owned by peasant farms amounts to as high as 9 million ha.

#### 4. Conclusion

In general, land in Russia is in private ownership of millions of private owners. Nevertheless, agricultural land market is not developed, the costs associated with transactions in land are extremely high and the demand for land exists only in some regions. The market is distorted because in some regions agricultural land is purchased for construction purposes. Corporate and peasant farms are incapable of competing with such buyers. And yet, the market is developing despite all the problems.