

# **Social Capital Formation and Restructuring in Post Socialist Agriculture – A Research Agenda**

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## **1 Introduction**

During recent years social capital has become a widely used concept among social scientists from different academic fields working with rather different paradigms. Therefore, social capital must not be treated as one single concept but rather as a bunch of ideas held together by the common observation that personal relations between actors (networks) in society have a systematic impact on economic performance by facilitating coordinated actions.

While the network aspect is accepted from a common ground of the academic discourse, regarding the elements and origins of social capital there is little common understanding. On one side it is argued that social capital is a resource for a single or a collective actor and even a whole society. On the other side all the attributes in social interaction that ease successful transaction within a group are interpreted as social capital factors and therefore formal institutions as well as informal ones are included (Herrmann Pillath and Lies 2001: 362). Further it proved to be difficult to single out social capital factors from other factors that influence societies performance like human capital or formal institutions. These unclear definitions opened the door for doubts and criticism. However, the idea of defining successful network relations as social capital is intriguing because no-one can deny the intuitive logic that successful networking and economic efficiency are somehow related.

In our paper we will in particular focus on the previously mentioned network aspect in this debate, because we gained the impression that it is precisely this aspect which plays an important role not only for the explanation of the outcomes of agricultural restructuring but also for the assessment of the future perspective of rural areas in Central and Eastern Europe.

The thoughts and empirical lessons we will present convey our way of thinking about and analyzing transition restructuring. The questions and theses we present at the end of our paper

are diverse and intend to prepare the grounds for fruitful discussion and research cooperation in the TransCoop project. Our results highlight important mechanisms and determinants that have contributed to the current status of rural development. They also show that the type of networks we observe has an impact on the emergence of new social structures and on the long-term economic perspectives of the communities. We observe several network strategies of rural actors to deal with structural changes. For reasons of analytical convenience, we analyze only two extreme but salient network strategies that evolved in the poorer rural areas of CEECs, like for example in Bulgaria, Romania, Russia and some parts of Hungary. We claim that these strategies mark up the borders of a social choice dilemma between "bridging" and "bonding" (Woolcock 1998) and do neither imply sustainable nor satisfactory outcomes.

The idea of the paper is to comparatively reflect the basic findings of our empirical research on rural restructuring in CEECs and Eastern Germany in the light of both, The New Institutional Economics and The Social Capital Thesis, both taken as heuristic concepts. We identify two pathways, we can observe as rather extreme outcomes of the restructuring process, as network strategies. From a network perspective both pathways describe unsatisfactory network structures. To understand the implications, we change the theoretical perspective and argue along a simple choice model. Along that model, we discuss the question of which elements in the structures we observe are responsible for our pessimistic assessment of the future perspectives of these strategies. This leads us to the some theoretical aspects of a research agenda on how to consider and normatively assess network structures. This research agenda is meant to be a contribution to further discussion about research objectives and methodology of workgroup three of the Transcoop project.

## **2 Overview**

Although post-socialist agricultural restructuring in the different Eastern and Central European Countries did start from rather heterogeneous conditions and has not been performed in a similar way in the different countries (Swinnen, Buckwell and Mathijs 1997). we still can observe some common features of these process in almost all of these countries. The primary focus of all the reforms has been on land reform, the restructuring of collective or state farms and the liberalization of formerly state controlled agricultural prizes. The first very immediate, very significant and also very persistent outcome of these policies has been a sharp decline of agricultural output and agricultural income and as a consequence rural unemployment. Due to the strong reliance of the rural economy on the agriculture sector these changes went along with dramatic social disruption in rural society. Twelve years after the

beginning of land reform and asset privatization policies the outcomes of the transition process in the agricultural sectors of poorer CEECs like Russia, Bulgaria, Romania but also those in the Czech Republic or Eastern Germany have little to do with the intentions of their designers. The dominant feature of farm structures in Central and Eastern Europe is the existence of a dualistic agriculture sector composed of comparatively large agricultural firms on the one side and a bulk of small, subsistence farms on the other. Land credit and service markets remained underdeveloped, agriculture is characterized by few large scale farms that often dominate communities and sometimes whole regions.

In most countries a huge proportion of agricultural products is produced by small scale subsistence oriented garden plots who do not participate in the market. Due to very low pensions, subsistence farming in the villages is the last resort for the elder part of the population while the younger generation has often left the countryside if not the country. After years of debates about reform policies and economic objectives and unfavorable economic conditions, new entrepreneurs are scarce. In some regions the term large scale farm describes a barely restructured model of the former socialist farm collective still working on the basis of machines and assets from the socialist era and organized as an Agricultural Producer Co-operative (APC). In others, large scale farm means a comparing to western standard giant leasing farm with the latest standards in farm equipment and management practices applied not only dominating the local labor market but also community politics. Especially in the poorer countries of the south like for example Bulgaria and Romania, Sharecropping arrangements between household plots that lease out access land to APCs or leasing farms are the state of the art in agricultural contracting.

### **3 The Frontiers of The New Institutional Economics - On Powerful Actors, Distributive Bargains and Bad Outcomes**

Research within the KATO project in which agricultural restructuring processes has given insight in some of the main determinants of agriculture restructuring in Poland, Czech Republic and Bulgaria. There are three empirical categories which already cross the borders of the usual objects of NIE-analysis and turned out to be of significant importance for our study design-:

- The structure of the action situation
- The characteristics of agricultural production
- The diversity of the actors.

### 3.1 The Structure of the Action Situation

The basic characteristics of the action situation have been uncertainty and lack of information. Local decision making processes have often turned out to be rather independent from the decision making process on the central political level. In other words, a discrepancy between formal laws and economic rights of action on a local level can be observed.

The vagaries of transitional market development together with weak property rights caused by political conflicts about land reform and privatization policies make it difficult to undertake investment. Frequent shifts on the central level (policy making) especially after elections produced high uncertainty about the path and the future of the restructuring and asset privatization processes.

Price fluctuations produced high uncertainties and risks for agricultural producers. Agricultural credit and service markets are still underdeveloped. Waves of extremely high inflation have caused high losses on the stock of private savings and destroyed many business relations. This has produced suspicion in post socialist societies against the capabilities of the market as a co-ordination mechanism. Weak jurisdiction, monopsonistic structures in the up- and downstream sector of agriculture and insecure land rights created high incentives to do what people have always done under the socialist regime: not to produce for the market.

### 3.2 Characteristics of Agricultural Production

A second fundamental feature that influenced the outcomes of land privatization and redistribution policies has been the connection of land use with land assets and the physical attribute of agricultural production. The availability (or rather the scarcity) and therefore the redistribution of machinery and other assets (livestock, stables, etc.) has been as much of importance for the set-up of new private farms as land.

The ear of the needle for the development of agricultural product as well as input markets has been the poor infrastructure. The dependence of agricultural producers of storage and transport facilities to market their production also has been an important determinant for the current outcome of the agricultural process in Central and Eastern Europe.

Finally, it have been the physical characteristics of land itself, which played a role, in particular in **the case** of redistribution of 'real' land. Fragmented ownership, missing land registers, the practice under socialism to built rural infrastructure and buildings without caring for **land** titles produced a lot of practical problems to split and redistribute land on the basis of historical land titles.

### **3.3 Diversity of Actors**

Considering the high uncertainties aligned with the policy reform and the given physical characteristics of the economic transactions involved our research highlighted the huge diversity among actors regarding their access to important information and resources. The occupational structure of the socialist agricultural firms turned out to be of crucial importance to explain this diversity. In the socialist era the village community was divided into a group of well specialized worker-members of the farm collective and a group of managers of the collective or state farm connected with the village mayor and familiar with the political and administrative apparatus of the Communist Party. Thus people in the village are by no means homogeneous actors but must be differentiated according to their access to information about politics and administrative issues. The implementation of reform policies was subject to debates and interpretation at the central level (government). Because of that it was mainly the former collective farm/state farm management together with mayors and party secretaries who elaborated models for the restructuring of the collective farm and its assets (Schluter 2001; Hanisch 2000; Milczarek 2001).

Because initially decisions like what to do with asset vouchers or whom to lease out land did not take place in a competitive market environment, they were hard to revoke. Power differences in terms of agenda setting capacities, information advantages and paternalistic reputation favored the former management of the socialist farm organizations against those actors wanting to start a new agricultural business (Hanisch 2000; Schluter 2001).

On the other hand, shared mental models (in North's terms: ideology) also influenced the decision making process in different ways. On the one hand was an individualistic ownership approach, in particular among the younger generation that never experienced anything else but socialism, generally not very widespread and popular. New farmers therefore in many cases faced collective opposition and resistance. Managers on the other hand could draw on shared mental models because of joint experiences during in higher education and the participation in collective professional activities during socialist time.

## **4 Post Socialist Network Strategies**

In this section we will present a quite simplistic picture of transitional strategies in the process of rural restructuring. Of course we are perfectly aware of the fact that the actual situation in the villages we observed do neither represent pure "Ghetto"- nor "Subsistence Village"-situations. However, we believe that there is a tendency in many of those villages to converge in one or the other direction.

#### 4.1 Village Dualism: Competitive Farms Next to the Village Ghetto

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**Village** dualism we labeled a situation we have often observed in the Vama region of Bulgaria but also in many regions of eastern Germany, the Czech Republic and elsewhere. This type of local context is characterized by the existence of a (or several) rather large farm enterprises who are well-integrated in formal agricultural markets. Either the village APC got bankrupted and was bought by its management or the incumbent collective farm management successfully convinced the village population to borrow or sell its shares of assets to them against the promise to give machine services and land rents. Investment are taken with the view to external markets and financed through bank loans. In practice, these firms benefit from dysfunctional land markets and a usually high unemployment rate because wages and land rents are low (Hanisch 2000). Because land ownership was fragmented by restitution and subsistence farming is widespread, it is often the case that only the larger of the few market oriented farms receive subsidized agricultural credits because they are the only ones in the village who know where and how to apply and how to follow complex administrative procedures.

Business ownership is concentrated on a small number of people from inside or outside the local community. Typically, the owners of the large farm were cadres of the former socialist agricultural firm and well connected to regional bureaucrats and member of parliaments. Today it is mostly because of their ability to pay taxes that they are well connected to the village mayor and community politics. Over time a 'competitive farm enterprise' emerged while a 'village ghetto' characterized by high unemployment, poverty and the emigration of the younger generation can be observed.

#### 4.2 The Subsistence Village

The subsistence village we labeled a situation we have for example observed in the Montana Region of Bulgaria but which is also common practice in parts of Hungary and Romania where conditions for agriculture are often less favorable, infrastructure was weak and the village economy is oriented towards subsistence. The farm collective restructured as an APC which supplies small subsistence oriented farms with machine services, processing and grain for household livestock and bread. Even the village bakery is often part of the APC. Members perform a type of sharecropping arrangement with the Coop. The percentage of the harvest which is extracted from the household differs from village to village. Members pay for machine services for one fraction of their pooled in land and get the amount of produce equal to the average yield in the APC. The rest of their land they give to the Coop for very low rents

in order to allow it to pay for overheads: At the end of the season the coop sells grain and sunflowers on the market via traders and receives money to pay the management, fuel and spare parts. In some villages we observed strong distrust against the management of the village collective among villagers in others villagers were satisfied with the situation and engaged in labor supervision and the control of the harvesting process in the coop.

Within the village community agricultural products like milk, cheese and meat are vitally exchanged among neighbors. Money usually does not play a larger role. Reinvestment in the machines and assets of the coop is regularly low. A minimum amount of non village products enter the village via relatives who live in the cities and eventually visit their grandfathers and grandmothers

From an institutionalist's perspective several reasons for the emergence of these two ways of coping with transition can be found. Both strategies rely on successful networking. The former strategy can be characterized as successful vertical networking between actors on different levels of action (government, producers, village politics, market). The farm firm has access to the formal credit market and state support, good connections to the agricultural policy arena and participates in the agenda setting for rural development projects. Because of its size, it enjoys appreciation from the level of agricultural administration and because of its tax paying capacity it has a formidable position in village politics. Farm managers and owners often show a paternalistic attitude towards villagers. Land rents tend to be low.

The latter strategy (the subsistence village) can be interpreted as a minimize market and natural risk strategy of members and managers. Average yield as a criterion for rental payments may be seen as an insurance against natural crop risk connected with single plots for the members. For the management physical payments in shares of the average harvest imply that no monetary liabilities against members emerge. The manager has to do business only for buying inputs and paying wages. Thus payment depend on his performance and the price risk for grain and sunflowers so long as buying and selling is controlled by the general assembly..

With grown up children who no longer live in the villages, relatively small life expectancy and a house, (most villagers are married), they are equal in terms of ownership, job opportunities, discount rate for future income and physical as well as human capital endowments. Expectations towards rents from land ownership are low and they expect to maintain the situation in the village stable as long as they live. Little investment in infrastructure or more productive technique is undertaken because it is not needed. People live on the stock of assets they produced during the socialist era in the lifestyle they are

accustomed to. For them, a type of subsistence farming represents the best return to the few physical inputs they can deliver. Because agricultural work is hard, they need the machine services from the coop and do not allow to much orientation towards the market. Because they cannot bare price or contract breach risks, they remain the member owners of the enterprise. Because everybody in the village does similar things, little specific knowledge is needed. Exchange happens but not on the basis of money. Those wanting withdraw machines and farm assets from the collective in order to start a private farm were excluded from having access to coop assets via informal sanctions (Hanisch 2000). For them, the village is only a good place to live in as long as they do not try to work against the coop and its management.

Obviously both outcomes which of course represent extreme positions in a continuum of possible developments among villages have little to do with the state of the art objectives in the debate about the future look and tasks of rural areas in Central and Eastern Europe, namely multi-functionality and sustainability.

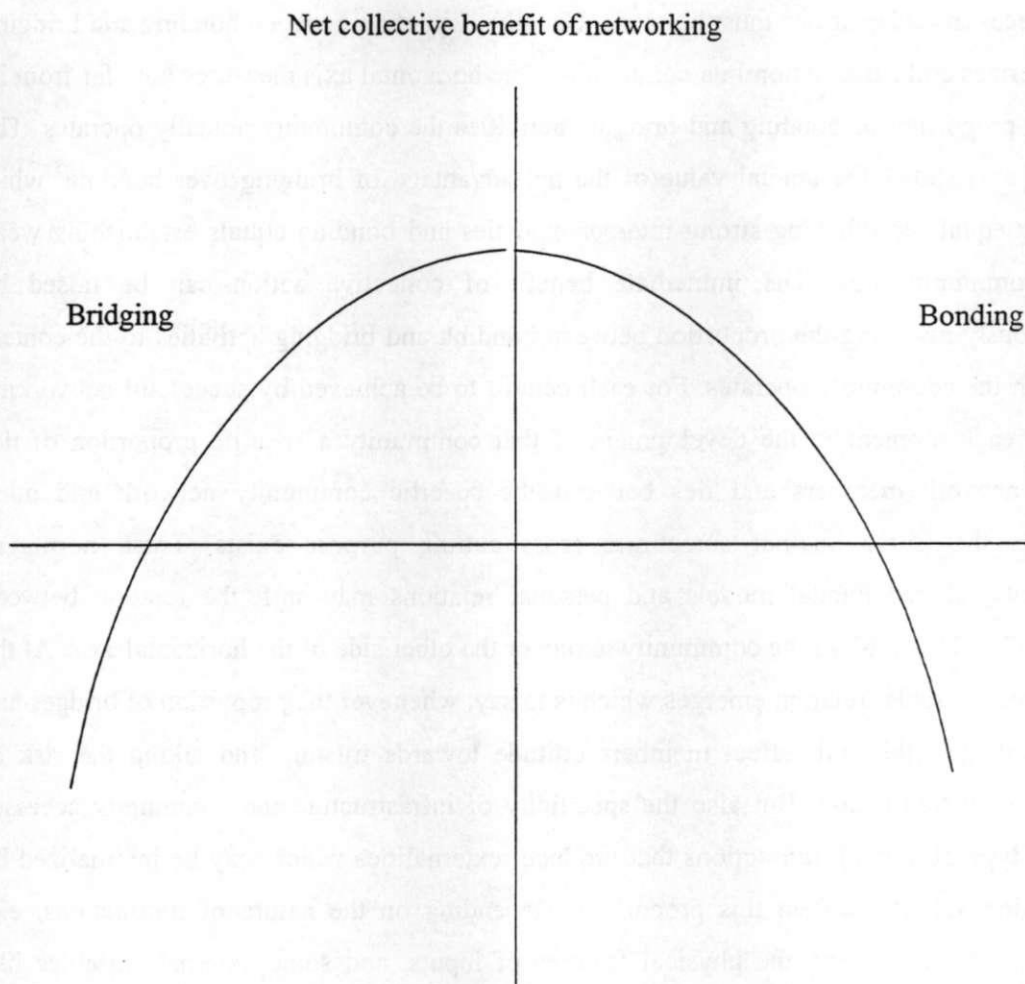
#### **4.3 Some Preliminary Conclusions**

Although our research started with an institutionalist's approach the results went far beyond the realm of textbook institutional economics. Because of that some of the findings are similar to those from research from different scientific disciplines which deal with similar issues (and therefore can also be interpreted differently). Here we in particular refer to the concepts of power, ideology and networks (see e.g. Alanen 2001; Laschewski 1998; Lampland 2002). NIE analysis allows to characterize the situation and some of the decisions made in the restructuring process but it has little to say about the impetus and competence of the involved actors to change the situation. As we have seen, networking plays a dominant role in coping with the transitional situation. But the role these networks actually play remains unclear and deserves further investigation. The concept of social capital may complement the analysis by introducing a network perspective. Network involvement has been important to understand the differences of individuals to improve their situation (Bourdieu 1986), but has also shaped individuals perceptions of the situation and has been seen as crucial for the development of shared mental models that again eased collective action. In the following we therefore explore a certain view on social capital deriving network analysis that allows us to re-interpret our observations and to address a future research agenda.



## 5 The Social Capital Thesis

The social capital thesis has many facets. The most familiar dimensions of social capital are those introduced by Granovetter (1973) as "strong" and "weak" ties. While the former refers to close friends and family relations the latter describe more distant associates and acquaintances. Recently, it has become popular to refer to these two dimensions as "bonding" and "bridging" (Woolcock 1998). Because we observe some similarities to the scientific discussion about credible commitment in policy making we will in the following argue along a simple political economy model (Dixit 1996: 69).



**Figure 5-2:** Bridging and Bonding in Networks

Source: Hanisch 2003: 97.

Social capital we define as a communities ability to reap the fruits of collective action by establishing and maintaining successful internal and external network activities. A desirable social outcome in this model is a community that captures maximum benefits from collective action over time and inter generations without constraining the objectives of other communities (sustainability) and without constraining the ability of community members to switch from one network to another (cheap exit).

The model illustrated below sees social capital as an equilibrium between two extremes of social behavior. The first is a community of anonymous actors only interested in outside community ties, which makes it hard to realize norms of reciprocity, trust and shared intra community beliefs. The other extreme is a community that has strong internal ties, but does not have any external linkages, which makes hard to learn from others or to change behavior when necessary adaptations must be made. Usually a situation between bonding and bridging characterizes collective action in a community. The horizontal axis measures how far from its optimal proportion of bonding and bridging activities the community actually operates. The vertical axis shows the annual value of the net advantage of bridging over bonding, while bridging equals establishing strong interpersonal ties and bonding equals establishing weak extra community ties. The immediate benefit of collective action can be raised by continuously matching the proportion between bonding and bridging activities to the context in which the community operates. For each benefit to be achieved by successful networking and for each moment in the development of that community a specific proportion of ties among network members and ties between the specific community network and other networks that serve another sometimes cross cutting purpose exists. Trust, norms of reciprocity, shared mental models and personal relations may shift the relation between "bridges" and "bonds" in the community to one or the other side of the horizontal axis. At the same time a circular relation emerges which is to say: whenever the proportion of bridges and bonds changes, this will effect members attitude towards trusting and taking the risk of interpersonal transaction. But also the specificity of infrastructure the community accesses and the type of mutual transactions that produce externalities which may be internalized by networking activities affect this proportion. Depending on the nature of transactions, e.g. measurability, frequency, the physical features of inputs, and some external variables like infrastructure and general economic development, there is a theoretical optimum of bonding and bridging activities in the community for each moment in time and each collective benefit to be achieved. The characteristics of the network relations and externalities (benefits or costs) change depending on a number of dynamic factors like the density of intra-network

relations, age of members (changing discount rate) but also external factors such as economic and political stability, the benefits offered by other networks, and the flow of information among all networks. In the following we want to use this simple model of thought in order to identify promising fields of further research on agricultural restructuring in CEECs.

## **6 A Research Agenda**

In the light of a network perspective our empirical observations about post socialist strategies in the villages may be reinterpreted: Both of our stylized strategies - Competitive Farms Next to the Village Ghetto and the Subsistence Village - can readily be classified into our simplistic concept: The former strategy focuses on successful "bonding across political, administrative and marketing networks". A modern type of entrepreneurship well embedded and vertically integrated into lobbying groups and markets emerged.

The latter strategy (the subsistence village) may be said to rely on strong personal ties, the cement of the subsistence economy (bridging). Both strategies have led to what we call "socially undesirable outcome." In the first case, we observed the erosion of the village society, the emergence of poverty and immense income inequality between the big farmers and the village population. The second case is characterized by the suppression of the few potential entrepreneurs by the many subsistence oriented (old) which has led to reduced incentives to do business, the emergence of a machine and asset monopoly in the cooperative increased dependence of the village land owners on the good will and abilities of the coop-management and the emigration of the younger population. Thus both situations are characterized by the consequent exclusion of some actors from the benefits of collective action.

From the standpoint of an 'optimal' network structure (that is the view of an external observer who wishes sustainable agricultural development and multifunctional rural areas) considerable change is needed to improve economic performance as well as social integration. However, it became clear that each community follows its own 'logic of collective action.' Collective historical experiences as well as demographic changes have a lasting grip on the expectations villagers have towards their future. Old paternalistic structures favor managers in their ability to gain support for their actions. To judge whether a situation is socially undesirable primarily implies to make a decision about whose desires shall be considered.

But even if we accept that substantial change is needed, there are some more problems to be considered. The fundamental question is, in how far and how fast networks can change strategies internally and in how far external intervention is needed. Therefore, we have to

understand- cognitive processes of learning of networks themselves, and to identify determinants that are supporting or inhibiting such processes. For example, in our cases we do not know the impact of increasing land rent or the emergence of new competitors on land and service on network attitudes and learning in the subsistence village.

These problems of learning networks and policy intervention raise further issues that can be related to the outcomes of the research that we outlined earlier. Part of them have not yet found substantial consideration in the social capital debate. In some cases we also find a problem of causal relationship involved. Is social capital the origin or the outcome of development?:

1. Social capital and the economic theory of agrarian institutions and organizations: Agricultural Producer Cooperatives, sharecropping arrangements, and subsistence cropping have little in common despite the fact that they are usually connected with inefficient agricultural institutions (Deininger 1995, Bardhan 1989, Ruttan 1988). While these structures have experienced much prejudicial assessment from economists (Briintrup and Heidhus 2002: 18) in many regions of CEECs they are about to pass what transaction cost economists have called "the test of time" and little is known about a situation in which the three elements constitute a community network and about the question how such a network learns to change. It is likely that the contracting behavior and organizational choices can only be understood as being closely embedded in these community networks. One can think of a whole research agenda which fruitfully amalgamates hypotheses from both theory strands.
2. Social capital formation and power: The observation that actors in the villages have different access to resources suggests to analyze how the internalization of benefits from collective action actually happens. In other words: where bargaining power is a determinant of social class structure it must be analyzed in a comparative fashion how networks deal with network goods and network bads in terms of excludability and rivalry and which consequences for the normative assessment of network activities must be drawn. A classification of the characters of different effects is needed.
3. Social capital and history: The starting point of post-socialist transition in (most) rural areas was a situation dominated by large hierarchical farm organizations. As we have seen, structures have a historical imprint on the positions as well in the thinking of people. There are many more important social changes that have been taken place in recent history to be considered (expropriation, resettlement, ethnical conflicts etc.) that play an

important role in the local memory, the mentalities and the visions of the people and have had lasting effects on the rural society.

4. Social/human capital formation, social security systems and demographic change: The observation that rural areas are a surrogate for missing social security systems suggests to investigate the long term effects and relations between pension payments and the emergence of self help networks to compensate for missing monetary income and risk insurance. Especially in East Germany where a very effective pension system exists the impact of this effect on the development of the community as a whole opens up an interesting research field for comparative analysis. Another question is how an aging community invests in network activities and what this means for the sustainability of rural infrastructure in CEECs. In all of the countries a growing proportion of the elder generation lives in rural areas. It can be assumed that the type of networks that results from this development differs from that of a community which is mixed in terms of age classes. A systematic analysis of the comparative effects is urgently needed because it can be assumed that elder people have different political, infrastructural, cultural and educational preferences and this in turn has consequences for the design of policies to make multi-functionality work. In this context the role of and incentives for migration must be explored.
5. Social capital and the role of cooperatives: Cooperatives as self help organizations have played an enormous role for both the development of the rural areas in Western Europe and the USA but also for the development of democratic thinking and civic organization in regions far away from parliaments and urban democratic life. In Central and Eastern Europe these structures are connected with communism because there the Communist Parties often coercively forced peasants and villagers to pool their land and assets into a "socialist agricultural producer cooperative" which of course had little to do with our understanding of a self help organization. However, today most large agricultural enterprises have re-registered as agricultural producer cooperatives. One reason for this at first glance astounding observation lies in the specificity of the agricultural assets and the enormous conflict settlement cost of physically distributing these assets to private hands. Another reason lies for sure in the reluctance of villagers to entrust "their machines and assets" to the undomesticated forces of market evolution. In other words, keeping things as they were was a collective strategy of relatively homogeneous subsistence oriented land owners which offered the opportunity to do little sequential changes without baring the risk of losing machine services when bankrupted. Our observations in the villages show

that the extend to which villagers participate in democratic decision making widely differs from village to village and over the regions in different countries. In some coops members in the general assembly vitally bargain with managers about rental shares labor supervision policies, investment and the cost of machine services. In other villages the manager dominates decision making in the coop and little democratic thinking among villagers can be observed. This raises the question of what factors stimulate the participation in village decision making and in how far and for which situations the cooperative with ist democratic constitution can be the locus of sequential learning about democratic structures civic engagement but also for successful strategies to deal with risks and to participate in the market.

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